EFFECT OF WORKING CAPITAL FINANCING POLICY ON FINANCIAL PERFORMANCE OF FIRMS LISTED AT THE NAIROBI SECURITIES EXCHANGE

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DECLARATION

I, the undersigned hereby affirm that this work is my original research project report and it has never been presented in part or in totality to any other institution of learning for the award of any degree or examination.

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D61/5307/2017

This research has been submitted with my approval as the University Supervisor

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DEDICATION

This project is dedicated to my parents Philip Makau and Esther Mwende the great promoters of education, who are my number one cheer leaders and have motivated me to reach this far. I also dedicate it to my daughter Shantelle Mwende who was at one time my companion in the journey and motivated me to push further till the end and to my husband Benard Kyalo for his support, patience and understanding

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ABBREVIATIONS

APP - Average Payables Period

CCC - Cash Conversion Cycle

CEOs - Chief Executive Officers

DW - Durbin Watson

FGLS - Feasible Generalised Least Square

GMM - Generalized Method of Moments

ITO - Inventory Turnover Period

NSE - Nairobi Securities Exchange

ROA - Return on Assets

ROE - Return on Equity

SPSS - Statistical Package of Social Sciences

VIF - Variance Inflation Factors

WCM - Working Capital Management

ABSTRACT

Working capital management is a significant constituent in business finance as it directly affects the company's profitability and liquidity. However, majority of financial managers attach great premium to other financial commitments, notably capital budgeting and financing decisions. In addition, most CEOs pay less attention to WC financing in carrying out the company's day-to-day business and delegate most decisions on working capital to low-ranking staff whose decisions are rarely implemented by the senior management. Thus, this study explored the effect of working capital financing policy on financial performance of firms listed at the Nairobi Securities Exchange. The research was grounded on working capital cycle theory, the transaction costs theory and the trade of theory of working capital. The study employed a descriptive study design and the population was made up of 45 non-financial corporations quoted at NSE as at 31st December 2018. The research entirely used secondary data, which was retrieved by use of data collection sheet for a time-period of five years from 2014 to 2018. The collected data was sorted and keyed into the SPSS then analyzed using descriptive statistical tools like the mean, standard deviation, maximum and minimum values and the regression technique to establish the link between the dependent and explanatory variables. The results revealed a negative and significant relationship between aggressive financing policy (AFP) and ROA while the relationship between leverage and ROA was also negative and statically significant respectively. The results further established that the relationship between company size and ROA was positive but statistically insignificant but the association between liquidity (CR) and ROA was negative and significant respectively. The study concluded that the aggressive financing policy (AFP), leverage and liquidity significantly affects the financial performance of firms listed a NSE. The study thus recommended that the management of listed firm should minimize the use of short term financing sources since they reduce the firms' profitability levels and that the management of firms listed at NSE should hold optimal liquidity since too much liquidity adversely affects the firms' profit levels.

CHAPTER ONE: INTRODUCTION

1.1 Background of the Study

Working capital management is considered as a key element in determining organizations financial performance (Niresh, 2012, Taani, 2012). Working capital financing is a significant facet in retaining the corporation's liquidness, survival, profitability and solvency (Raheman et al., 2010; Yahaya & Bala, 2015). Performance of working capital thus provides a vital view of the firm's financial position. As a significant indicator of financial soundness, the availability of working capital is one of the first points that the creditor or investor will consider in the financial position statement (Konak & Güner, 2016). Companies reduce risk and enhance profitability through the assessment of the working capital determinants (Nazir & Afza, 2009, Thakur & Muktadir, 2017). Therefore, investing in working capital is fundamental to make the right financing decisions, as short and long-term financing modes have benefits and drawbacks that significantly affect the firm’s profitability (Mahmood et al., 2019).

This study is pegged on the working capital policy theory, the transaction cost theory and the tradeoff theory of working capital. The working capital policy theory states that managing of working capital influences business performance and that the company needs to change working capital over time, depending on the level of money generation and holding high level of stock and receivables result to a decrease in firms’ profit levels (Aminu & Zainudin, 2015). Transaction cost theory supports the fact that most companies in each area of working capital have a lower return on capital than other likely uses and that these companies have very little to invest in working capital (Bei & Wijewardana, 2012). The tradeoff theory of working capital supports that firms management have to

assess the trade-off between anticipated profitability and risk, where each tradeoff represents the opportunity cost of the other before establishing the optimal working capital investment (Niresh, 2012).

In Kenya, the Nairobi securities exchange is imperative that it offers an appropriate market for investors who intend to purchase and the investors who intent to sell of their securities hence creating liquid financial instruments (Kamuti & Omwenga, 2017). The exchange distributes valuable statistical data in aggregated form to different institutions for beneficial usage (Nyabuti & Alala, 2014). NSE is a choice market for local and international investors seeking to enter East African markets (Omondi & Muturi, 2013). Although most NSE companies have improved their performance, a number of companies in the last decade have recorded a decline in profitability and while others being delisted from the exchange. Significant determinations to turn around or even liquidate such companies have focused mainly on financial restructuring (Lalah, 2018).

1.1.1 Working Capital Financing Policy

Working capital financing policy entails the determination of optimal funding strategy of investments in short term assets like cash, inventories, receivables, marketable assets and the firm current liabilities (Muhammad, Jan & Ullah, 2012). Effective working capital financing comprises of managing and forecasting short-range obligations and assets in a manner that reduces the possibility of being unable to settle outstanding obligations and avoids too much holding of short term assets (Taani, 2012). In specific, the two key approaches for financing working capital are the aggressive and the conservative working capital financing policies (Thakur & Muktadir, 2017).

An aggressive working capital financing plan utilizes greater quantity of current liabilities and a smaller amount of non-current liabilities (Nazir & Afza, 2009). An aggressive funding strategy uses higher short term finances and less long-term finances. Although an aggressive strategy reduces the cost of capital, it enhances the likelihood of short-range liquidity difficulties (Temtime, 2016). An aggressive plan is mainly aimed at reducing high levels of liquidity to meet current needs (Panigrahi, 2014). Aggressive financing strategy arises when there is large percentage of short-term funds in WCF. The proportion of short-term liabilities in relation to aggregate assets is usually used to proxy the extent of aggressiveness, where a lower ratio represents a moderately aggressive policy (Thakur & Muktadir, 2017).

A conservative working capital financing strategy uses leverage and capital that is more non-current and a smaller amount of current funds (Nazir & Afza, 2009). The conservative strategy of financing working capital is a low-risk policy that ensures investments in assets is covered by long-term financing. Most managers are satisfied with this strategy, due to the lower possibility of inability to meet liabilities when they due (Bei & Wijewardana, 2012). According to the conservative approach, long-term funding should cover the estimated total funding needs and the use of short-range finances ought to be limited to emergencies or unexpected outflows (Panigrahi, 2014). In a more conservative strategy, a larger share of capital is invested in cash, but a degree of profitability is sacrificed (Thakur & Muktadir, 2017).

1.1.2 Financial Performance

Financial performance is generally an indicator of a company's comprehensive financial strength over time and is used to compare related companies in a similar industrial sector

or to equate segments or industries as a whole (Nazir & Afza, 2009). Financial performance largely reveals the outcomes and results of the commercial sector, which as a whole, illustrates the financial health of the sector and illustrates how effective a firm employs its assets to capitalize on stockholders wealth (Naz, Ijaz & Naqvi, 2016). Corporation's financial performance is a key measure, which defines competitiveness, the capabilities of an entity and economic interests of firm's management and the reliability of existing or future suppliers (Sichigea, Ganea & Tupangiu, 2011).

Financial performance provide shareholders and stakeholders with comprehensive information that helps in decision-making (Aliona, 2016). The reason behind financial performance measurement is to get useful information in terms of cash flow, resource utilization, efficiency and effectiveness (Batchimeg, 2017). A company's higher financial performance shows how it utilizes its assets efficiently and efficiently and contributes to macro economies (Matar & Eneizan, 2018). Investors always take into account the financial performance of companies to identify the required investment opportunities. Good company performance is a factor that stimulates shareholders to invest their money in a particular firm, which would ultimately increases shareholder wealth and value of the firm (Ahmadabadi, Mehrabi & Yazdi, 2013).

Financial performance is analysed using nonfinancial and financial indicators. Non-financial indicators encompass information provided by marketing, production and human resource departments and usually assesses the company's activities without taking into consideration account accounting principles (Aliona, 2016). Financial indicators include the accounting ratios among them the return on shareholders' equity, return on assets and the Tobin q. ROA is the ratio of annual after tax earnings to aggregate assets while ROE is

an internal profitability proxy for stockholder's value (Sichigea, Ganea & Tupangiu, 2011). Tobin's q equates the firm's worth as provided by the securities exchange with the par value of the firm's assets (Nazir & Afza, 2009).

1.1.3 Working Capital Financing Policy and Financial Performance

Working capital financing policy entails the instituting of an optimal way to finance an entities inventory and receivables requirement, cash and payable in manner than minimizes costs (Temtime, 2016). The tradeoff theory states that efficient working capital has to strike an equilibrium between taking too high or little liquidity to achieve an optimal profitability level thus an entity's firm liquidity should be neither excessive nor inadequate (Niresh, 2012). According to the working capital cycle theory, companies are expected to invest working capital in appropriate manner, finance WC and monitor the elements influencing working capital effectively to enhance profitability (Temtime, 2016).

Yogendrarajah and Sangeetha (2014) studied how managing working capital affects profitability and revealed that huge investment receivables and inventories was associated with minimal financial performance. Miloş and Miloş (2014) study on working capital and corporate productivity in Romania concluded that working capital financing had weak and an inverse association with performance. Konak and Güner (2016) examined funding of working capital and SMEs profitability and revealed an indirect association between ROA and short-term WC financing.

Further, Onsongo and Onyiego (2018) examined WCM practices and profitability of cooking oil-producing firms in Kenya revealed that debtor's days, payables period, stock turnover significantly affects firm performance. Bagh, et al (2016) study on WCM on

manufacturing firms' performance in Pakistan established that CCC, ITO and APP had an inverse but significant impact on ROA. In the Puntland State of Somalia, Hassan, Maturi and Mberia (2017) investigated WC requirements and profitability and revealed that creditor's period (APP) had an insignificant impact on firm performance.

1.1.4 Firms listed at the Nairobi Securities Exchange

Nairobi Securities Exchange (NSE) is a main securities exchange in Kenya and provides a computerized platform for trading and quoting of stocks. NSE is among the robust securities markets in Africa, which has attracted investors from all over the world (Omondi & Muturi, 2013). The NSE is publicly-traded and is the second listed securities exchange in Africa (Orayo & Ombaba, 2017). NSE is an associate of African Stock Exchanges Association and also the East African Stock Markets Association and a full affiliate of the futures markets association, World Federation of Securities Markets and the exchange of partners of the UN Sustainable Stock Exchange initiative (Kamuti & Omwenga, 2017).

The NSE is a standout amongst the most significant securities trades in Africa to a great extent because of its comparative size in the landmass and its remarkable introduction toward the East-African locale (Shimenga & Miroga, 2019). The NSE has 64 quoted companies classified into 11 areas which include agriculture, automobile, banking, energy and petroleum, commercials and service, construction and associated, insurance, manufacturing, telecommunications and technology and the growing enterprise market sector (Onsongo & Onyiego, 2018). NSE has undergone a number of changes in the past to improve its efficiency and adjust to the economic environment variations, investor interest and technological changes (Nyabuti & Alala, 2014).

The NSE supports, develops, promotes and operates the securities exchange and carries out all the functions of the Kenya securities market (Omondi & Muturi, 2013). However, performance of companies quoted at NSE have been dwindling over the years. Poor profitability of the quoted firms at the NSE has affected shareholders negatively through the loss in market value of shares and non-declaration of dividends (Lalah, 2018). In addition, short-term assets represent more than 50% of the aggregate assets of most firms listed at the NSEs. Lalah (2018) posits that most manufacturing firmed listed at NSE use the less aggressive investment policy, which adversely affected the firms' profitability.

1.2 Research Problem

Working capital management is a significant constituent in business finance as it directly affects the company's profitability and liquidity (Yogendrarajah & Sangeetha, 2014). The tradeoff theory supports that the tradeoff between liquidity and profitability is important since companies are likely to fail and go bankrupt if financing of working capital is not properly considered (Raheman et al., 2010). Majority of financial managers however attach great premium to other financial commitments, notably capital budgeting and financing decisions (Thakur & Muktadir, 2017). Yahaya and Bala (2015) posits that most CEOs pay less attention to WC financing in carrying out the company's day-to-day business and delegate most decisions on working capital to low-ranking staff whose decisions are rarely implemented by the senior management.

The NSE in Kenya has always provided a well-regulated, robust and world-class platform for equity securities and bond trading (Nyamweno & Olweny, 2014). However, several listed firms have failed to meet their financial targets and have ended up giving profit warnings. Examples include, the Standard Group, Bamburi cement, Sanlam, Housing

finance, Express Kenya, Sameer Africa and Kenya power in 2019 (NSE, 2019). A number of listed companies are experiencing declining performance and currently Kenya Airways, Express Kenya and Longhorn publishers are topping the list of other firms that have turned to selling assets to shore up their medium term performance (Orayo & Ombaba, 2017). In addition, several companies, including Uchumi supermarkets and Mumius Sugar listed at the NSE have had liquidity problems in the last few years and have failed to settle their short-term financial liabilities upon maturity (Mwangi, Makau & Kosimbei, 2014).

Numerous studies have assessed the association between companies' performance and WCM. In Bangladesh, Thakur and Muktadir (2017) examined working capital financing and manufacturing firms' profitability found an adverse influence of WC financing on performance though the study dwelled on manufacturing entities. Nazir and Afza (2009) assessed WCM policies and corporations' profitability and concluded that executives enhance value through the adoption of a conservative working capital financing strategy but the study focused on conservative financing policy. Further, Raheman et al. (2010) explored WCM and Pakistan firms' profitability and revealed that CCC, operating cycle and inventory period significantly affected profitability but the study focused on WCM practices.

Several studies have also been carried out in Kenya among them Wanguu and Kipkirui (2015) on WCM on profitability of cement manufacturing companies which revealed that inventory days, receivables and payables period significantly influence performance though the study focused on cement manufacturing firms. Nyabuti and Alala (2014) assessed WCM policy and performance listed firm and found a significant association between WCM policy and performance though the study focused on traditional WCM

practices. In addition, Kiptoo, Kariuki and Kimani (2017) assessed WCM practices and performance of Kenyan tea firms revealing that inventory and payables management significantly affected performance but the context was tea processing firms and the study dwelled on WCM practices and not working capital financing.

Empirically, WCM and companies performance literature has received significant devotion in finance and accounting literature globally and in Kenya. However, much attention is given to the traditional WCM practices comprising inventory, debtors and payables management. In addition, the studies have been carried out in different sectors with most of them focusing on the manufacturing sector. Most of the WCM studies in Kenya also focus on the various sectors at the NSE and concentrate more on the WCM practices as opposed to working capital financing. This investigation thus endeavors to provide answers to the question, what is the impact of working capital financing policy on financial performance of companies quoted at the NSE?

1.3 Research Objective

To explore the effect of working capital financing policy on financial performance of firms listed at the Nairobi Securities Exchange.

1.4 Value of the Study

The results will provide practical insights that will help the management of quoted companies to adopt effective working capital financing and management policies to enhance greater productivity and business performance. The management of the quoted firms can use the study recommendations and conclusions to formulate appropriate policies on enhancing their firms' profitability.

The research findings shall be significant to different policy making and regulatory entities may use the study conclusions and recommendations to develop strategic policies to enhance working capital financing and listed firms' performance. The findings of this research would be of help to prospective researchers and will complement the current empirical literature on fiscal performance, and theoretical literature on WC cycle theory, the transaction costs hypothesis and the tradeoff theory of working capital.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

The part reviews a number of theories guiding the study under the theoretical review, the various factors that affect listed firms financial performance and the review of related studies under empirical review. The chapter also presents the study's conceptual diagram and finally a summary of the reviewed studies.

2.2 Theoretical Review

The research was grounded on working capital cycle theory, the transaction costs theory and the trade of theory of working capital.

2.2.1 Working Capital Cycle Theory

The working capital cycle theory originated from Sagan (1955) and was further advanced by Walker (1964) and emanated from the conventional model of the cash conversion cycle (CCC). The working capital cycle principle expounds the manner in which working capital ought to be managed and highlights the paybacks in relation to liquidness, productivity, solvency, cost-effectiveness, and maximizing the value of shareholders resulting from the appropriate management of WC (Temtime, 2016). The theory assumes that the primary role of a WC executive is to make available funding when needed and to temporarily spend extra resources in relation to the specific security and liquidity requirements by observing returns and corresponding risks of the available investments (Atseye, Ugwu & Takon, 2015).

The working capital cycle theory emphasizes that at the very minimum, working capital influences and supports other finance function like financing, dividend and capital

budgeting decisions since working capital cash flows are incorporated into the overall cash flows of the business (Altaf & Ahmad, 2019). The theory indicates that managing WC follows a cycle that depends on the type of entity being analysed (Bei & Wijewardana, 2012). With such a cycle, a company can always determine the WC needs. The theory thus defines the WC cycle as the time that a company has to transfer cash to commodities or finished products until it receives money from its debtors (Aminu & Zainudin, 2015).

The theory presupposes that working capital policy is dependent on the risks and rewards associated with alternative strategies (Temtime, 2016). Higher investment returns and risk as well as financing approaches are deemed aggressive whereas low risk and lower returns approaches are considered relative or moderate. The lowermost risk and the lowest return is deemed a conservative strategy (Bei & Wijewardana, 2012). The theory postulates that working capital management seeks to ensure that efficiency requirements are met so that investments in working capital components are not too low or too high (Aminu & Zainudin, 2015). The working capital cycle theory in this study highlights the need to manage WC accounts and informs that this might significantly influence the company's financial strength.

2.2.2 Transactions Cost Theory

The transaction cost theory was authored by Coase (1937) and explains that there exists various overheads for undertaking transactions at the market. Therefore, the company would prefer to organize intra-company transactions if charges were lower than the cost of making the market transactions. Given that the additional cost of in-house transactions exceeds the cost of executing market transactions, companies seek to reduce costs associated with transaction through vertical integration (Mroczek, 2014). The proponents

of the theory claim that overall costs of a business are basically divided into twofold parts entailing (1) production and (2) transaction costs (Li et al., 2014). The central claim of the theory is that transactions are designed to minimize the costs associated with their implementation (Williamson, 2009).

This theory expounds why companies exist, grow or outsource activities to an exterior environ while trying to reduce resource-sharing costs with the environment and minimize routine exchange costs within the enterprise. If internal routine costs are lower than external transaction expenses, the company will develop (Bei & Wijewardana, 2012). The dominant preposition of the model is that transactions are handled to minimize the costs associated with their implementation. In this case, the goods are related to working capital management (Williamson, 2009). In managing working capital, the four main elements of cash, debtors, stocks and creditors, whose management requires consistent resource planning (Foss, 2008).

The transaction cost theory in relation to working capital management states that debt management can reduce transaction costs for paying bills (Foss, 2008). Instead of paying for every product delivery, the company can collect and pay liabilities monthly or quarterly. The client can therefore distinguish the compensation process from the planning agreement (Williamson, 2009). According to the theory, an enterprise could need to build large stocks of loans, but this could be combined with additional stocking and funding costs, to ensure a continuous product cycle. Managers should therefore establish a cost-minimized and competitive strategy.

2.2.3 The Tradeoff Theory

Hirigoyen (1985) and Eljelly (2004) advanced the tradeoff theory of working capital, which suggests that business seek to maintain optimum liquidity levels to ensure equilibrium between the costs and benefit of cash holdings. The theory argues that the value of cash is neither destroyed nor created under ideal capital market assumptions (Niresh, 2012). The theory states that day-to-day liquidity maintenance is fundamental in managing working capital and guarantees a sound functioning of the organization and its responsibilities. Therefore, it's vital to monitor the company's liquidity status since without it the firm cannot survive (Panigrah, Namita & Chaitrali, 2018).

The theory also states that the WC investment levels and investment funding at a given production level is accompanied by a compromise between risk and returns. In general, the greater the risk, the greater the return that management and shareholders require to finance WC investments (Raheman et al., 2010). According to the theory, WC requirements have an impact on the corporation's liquidness and profit levels, hence influencing funding and capital budgeting decisions. Smaller WC needs translate into lower funding requirements and lower capital costs, leading to more cash for shareholders (Nishanthini & Meerajancy, 2015).

The tradeoff theory suggests that the major concern of corporates is the effective managing of the everyday actions in a smooth manner while increasing the shareholder's profitability (Nishanthini & Meerajancy, 2015). From the viewpoint of this study, the model emphasizes that the manager in charge of finance should manage their current assets and liabilities prudently. Minimization of funds tied in the current assets implies that the freed up funds can be invested hence improving the entities financial performance. In the same way, cash,

stocks (inventory) and receivables must be adequate to prevent business having challenges with their daily operations.

2.3 Determinants of Financial Performance

This section will discuss financial leverage, company size and liquidity as the main determinants of listed firms' financial performance.

2.3.1 Financial Leverage

Leverage denotes to the share of borrowed fund to equity in the company's structure of financing. Financing or leverage decisions are important management decisions because they affect the return and risk of shareholders and the market value of an entity (Omondi & Muturi, 2013). Financial leverage is a key parameter in terms of financial economics as it relates to the company's proficiency to address different stakeholders needs (Li et al., 2014). Both the long-term and the short-term lender are interested in the corporate debt level as it reduces the company's risk of paying for debt services that is interest and repayment of principal. A heavily indebted company offers creditors less protection in the event of bankruptcy (Batchimeg, 2017).

Financial leverage is seen as a positive signal for corporate value, and management companies have committed to creditors to generate interest and principal cash flows (Atseye, Ugwu & Takon, 2015). Companies with higher debt are likely to report negative results due to default risk. If a company fails to pay off its liabilities, it would be difficult for the entity to borrow additional funds from financiers (Batchimeg, 2017). The debt ratio shows what percentage of corporate fund which comes from financiers or creditors. A

greater level of debt share shows that more credit (borrowings) are being used compared to equity financing (Atseye, Ugwu & Takon, 2015).

2.3.2 Company Size

The size of the business plays an imperative function in the nature of the corporate affiliations it maintains within and outside its operating environment, and hence in profitability (Li et al., 2014). The size of an entity is associated with the firm's profitability such that as the size of the business expands so does ROA and vice versa (Wanguu & Kipkirui, 2015). Particularly, small companies are at a disadvantage because they try to cover the high operating costs of industry and diversify their products to compete with larger firms (King'ori, Kioko & Shikumo, 2017).

Large companies tend to increase their negotiating power by using size as an advantage, and have different preferred supply strategies to attain economies of scale (Li et al., 2014). Larger companies are more competitive than smaller companies in using economies of scale and generating higher profits (Omondi & Muturi, 2013). Larger enterprises have enhanced access to debt capital and thus have the flexibility to plan their investments, leading to a positive relationship with company performance (Atseye, Ugwu & Takon, 2015). Different indicators including assets, value, market capitalization, asset value, turnover and market capitalization are employed to measure size of the firm (King'ori, Kioko & Shikumo, 2017). Company size is calculated as a log of the company's overall assets.

2.3.3 Liquidity

Liquidity refers to available cash for the anticipated future taking into account the financial commitments corresponding to that period (Omondi & Muturi, 2013). Liquidity denotes the ability of firms to address their pending obligations in the short term with the cash and cash equivalents at their disposal (Sichigea, Ganea & Tupangiu, 2011). Effective liquidity management is also expected to include the forecasting and managing of WC, reducing the possibility not paying current debt and preventing unnecessary investment in short-term assets. A company's success is usually based on earnings and liquidity prospects (Li et al., 2014).

Liquidity is a prerequisite for companies to settle their current commitments, and their continued survival can be secured through a gainful business (Yogendra Rajah & Sangeetha, 2014). Companies use liquid funds to fund their undertakings and investments when borrowings are inaccessible. Increased liquidity can enable the company to cope with unexpected unforeseen events and meet low-income commitments (Omondi & Muturi, 2013). Effective management of liquidity beyond survival aids firms to increase their profitability by reducing their input needs. It also offers strategic advantages in economically challenging times (Batchimeg, 2017). Current ratio is the ultimate indicator of a company’s liquidness.

2.4 Empirical Review

Tingbani et al. (2018) explored how WCM affects profitability of quoted companies at London Securities Market. The study collected unbalanced panel data from 802 firms between 2004 and 2014 and a dynamic panel method for analysis. The outcomes showed

that a number of contingency factors including environmental management, assets, and competences significantly affected the link between profit levels and WCM. The investigation additionally found that WCM significantly affected company's profitability.

Mweta and Kipronoh (2018) in Kenya studied how WC requirements affects performance of quoted construction and allied corporations. The authors adopted an explanatory study design and collected archival data from 2012 to 2016 with the regression method being used for analysis. The outcomes documented a non-significant relation amongst inventory days, debtors days, period of payables, CCC and ROE and ROA. However, the results showed a significant association between inventory days, payables period, debtors' days, CCC and gross profit margin.

Muia, Banafa and Mwanzia (2016) surveyed the influence of WCM on profitability of enterprises quoted at the NSE. The research employed a descriptive survey and retrieved data from the nine quoted industrial companies between 2011 and 2015 with multiple regression method being used for analysis. The fallouts documented a significant and indirect relation between receivables period, leverage and firm profit levels.

Mwangi, Makau and Kosimbei (2014) explored how WCM affects performance of NSE quoted non-financial corporations. The researchers' used an explanatory research design and collected secondary data from 42 non-financial firms from 2006 to 2012 where the FGLS technique (Feasible Generalized Least Square) being used for data analysis. The authors documented that aggressive financing strategies significantly and positively influenced the entities ROA and ROE, while a conservative funding policy had a direct influence on ROE.

Olweny and Nyamweno (2014) explored how WCM influenced ROA of companies quoted at the NSE. The authors selected 27 firms and collected secondary data from 2003 to 2012, which was analysed using the GMM estimation technique. The findings showed that debtors' days and the CCC had adversely affected the quoted corporations' profitability, while the payables and inventory days positively and significantly influenced the entities profitability.

Ahmadabadi, Mehrabi and Yazdi (2013) examined how WCM affects performance of quoted corporations in Iran. The research collected secondary data between 2006 and 2010 and used the regression method for data analysis. The findings revealed an insignificant link between managing of WC and firm performance though individual measures of WC including ACP, APP and CCC significantly affect performance of listed firms.

Jagongo and Makori (2013) assessed WCM influence on Kenyan listed companies' financial performance from 2003 - 2012 through a balanced panel data collected from quoted construction and manufacturing companies. Using the regression method, the research revealed an inverse relation between ROA and debtors' period and the CCC, but a direct relation between ROA and inventory and payables period. The study also found that the leverage, liquidity and the entity size significantly affects the entities profitability.

Taani (2012) assessed WCM influence on financial leverage on performance of Jordanian corporations. The research collected panel data from 45 industrial firms and used the multiple regression method for data analysis. The findings revealed that a company's WCM strategy and size significantly affected the net profit margin. The study also revealed that WC practices had an insignificant influence on firm performance.

Muhammad, Jan and Ullah (2012) explored the relation between ROA and WCM of quoted textile corporations in Pakistan. The authors collected archival data from 2001 to 2006 and panel data methodology for data analysis. The results showed a robust and direct association between ROA and cash, receivables and stock period, but an inverse association between payables period and profitability.

Niresh (2012) investigated how performance of Sri Lankan quoted manufacturing corporations was affected by WCM policies and practices. The study selected thirty companies, collected secondary data from 2008 to 2011, and used the regression method to analyze data. The results showed an insignificant relation between CCC and financial performance. The research also found that conservative financing policy was the most preferred by Sri Lankan manufacturing firms.

2.5 Conceptual Framework

The conceptual framework for the study includes working capital financing policy as the explanatory variable and its indicators will include aggressive and conservative financing policies. The dependent variable will be firms' financial performance proxied by ROE and control variables will include leverage, company size and liquidity as indicated by figure 2.1

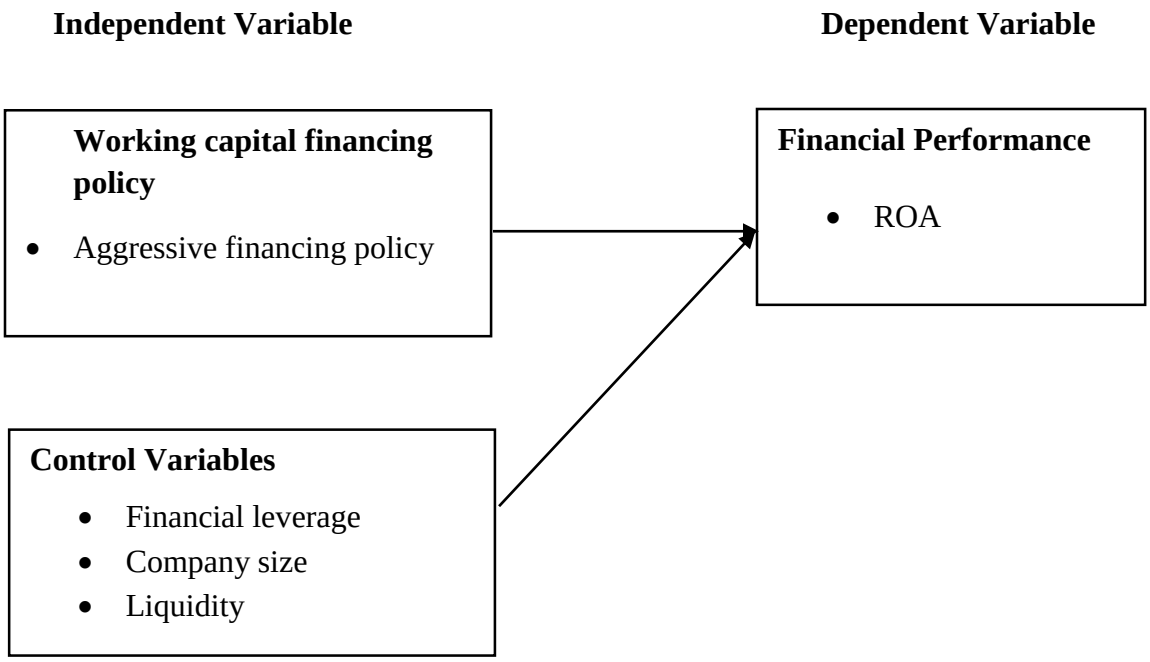

Figure 2.1: Conceptual Framework

2.6 Summary of Literature Review

The study reviewed a various surveys among them Tingbani et al (2018) who assessed WCM on profitability of entities quoted at London Stock Exchange and Ahmadabadi, Mehrabi and Yazdi (2013) on listed firm in Iran. Other studies include Taani (2012 on industrial firms in Jordan, Muhammad, Jan and Ullah (2012) on listed textile firms in Pakistan and Niresh (2012) manufacturing firms in Sri Lanka. In Kenya, the reviewed studies include Mweta and Kipronoh (2018) on listed construction and allied firms, Mwangi, Makau and Kosimbei (2014) listed nonfinancial firms, Jagongo and Makori (2013) on quoted construction companies. The reviewed studies however focus on different business industries hence the finding may not be replicated to all companies quoted in a securities exchange. Additionally, diverse methodologies were used to carry out the studies. Hence, the necessity to explore the impact of WC financing policy on financial performance of corporations quoted at NSE.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

The methodology part discussed the study design, targeted population and the tools and process of collecting data. The section further discussed the test of assumption under diagnostic tests, techniques and tools of data analysis and the adopted analytical model.

3.2 Research Design

A study design is denotes the strategy according to which research participants are chosen, data is collected and analyzed (Coopers & Schindler, 2009). A study design refer to the arrangement by which the researcher answers the research problem and entails the tools of collecting data and the techniques of data analysis a researcher intends to use (Kothari, 2009). This study employed a descriptive study design. The descriptive design tries to define or outline a topic and often creates a group of issues, people or events, collects data, and catalogs frequencies in search variables or their interactions (Kombo & Tromp, 2006). A descriptive research design is useful in a study in which a researcher is interested in a state that already exists in the industry and no variables manipulation.

3.3 Population

Population as defined by Kombo and Tromp (2006) is an entire collection of persons, events or items that possess common features. Population represents the entire set of units of analysis or the total assortment of components on which conclusion is to be made. The population of this study was made up of 45 non-financial corporations quoted at NSE as at 31st December 2018. The study excluded financial firms since the nature of their business

is different and WCM plays a minimal role in their operations. Hence, the study therefore undertook a census of the 45 non-financial listed firms.

3.4 Data Collection

Data collection entails the strategies adopted in a study to ensure that reliable, valid and reliable data is obtained to inform research results (Coopers & Schindler, 2009). This research entirely used secondary data, which was retrieved by use of data collection sheet for a time-period of five years from 2014 to 2018. The secondary data was retrieved from the firms' financial reports and annual reports, which was obtained from the CMA and the individual firms' websites.

3.5 Diagnostic Test

This research conducted a number of diagnostic test among them multicollinearity test, homoscedasticity test, autocorrelation test, normality and linearity test. Multicollinearity will be assessed using the Variance Inflation Factors (VIF) and the correlation matrix and to assess for homoscedasticity the Breusch-Pagan/Cook-Weisberg test was used. The Durbin Watson (DW) was employed to assess for serial correlation where a DW statistic, which lies between 1.5 and 2.5, was an indication of absence of autocorrelation while Normality in this study was assessed using the Shapiro Wilk test whereas the linearity test was assessed through the plotting of normal p-p plot.

3.6 Data Analysis

The data gathered was sorted and keyed into the SPSS then analyzed using descriptive statistical tools like the mean, standard deviation, maximum and minimum values and the

regression technique to establish the link between the dependent and explanatory variables.

3.6.1 Analytical Method

The study adopted the multiple linear regression method as the main analytical tool. The regression equation was formulated as follows

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon$$

Where,

Y - Financial performance measured using return on equity

X_1 - Aggressive financing policy measured using short-term finances to aggregate assets

X_2 - Financial leverage proxied using ratio of debt to assets

X_3 – Company size proxied using the natural log of total assets

X_4 – Liquidity proxied using the current ratio

β_1 - β_4 – Beta coefficients of the regression equation

β_0 & ε = Constant and the error term

3.6.2 Test of Significance

Assessment of the analytical model significance was done through the F test statistics where a significant F value showed that the overall model was significant. The t test statistics on the other hand was used to assess explanatory and control variables significance where a significance t value indicated the individual variable was significant.

CHAPTER FOUR: DATA ANALYSIS, RESULTS AND INTERPRETATIONS

4.1 Introduction

This chapter presents the results of the analyzed study data which entails the descriptive and inferential statistics. The chapter also present an interpretation of results.

4.2 Descriptive Statistics

The population of this study was made up of 45 non-financial corporations quoted at NSE as at 31st December 2018. The study however managed to collect data from 40 firms thus a response rate of 88.9%. The collected data was summarized under table 4.1

Table 4.1: Descriptive Statistics

Variable	N	Minimum	Maximum	Mean	Std. Dev	Skewness	Kurtosis
ROA	200	-.562	.367	.01938	.152098	-1.087	1.352
AFP	200	.012	1.553	.29903	.239790	1.756	1.611
Leverage	200	.000	.617	.15319	.168290	1.172	1.205
Size	200	12.48	22.23	16.2527	1.96940	.538	.508
CR	200	.076	12.087	1.05190	1.403908	1.458	1.190

Source: Study Data

Table 4.1 shows that the average ROA was 0.01938 with minimum and maximum values of -0.562 and 0.367 while the average value of the aggressive financing policy (AFP) was 0.29903 with minimum value of 0.012 and maximum value of 1.553. The results show that leverage had an average value of 0.15319 with minimum and maximum values being 0.000 and 0.617 respectively. The average value for firm size was 16.2527 with minimum and maximum values being 12.48 and 22.23 while liquidity (CR) had an average value of

1.05190 with minimum and maximum values being 0.076 and 12.087 respectively. The kurtosis and skewness value range within -2 and +2 which indicates that the data is normally distributed.

4.3 Diagnostic Tests

The study conducted the multicollinearity test, homoscedasticity test, autocorrelation test, normality and linearity test.

4.3.1 Multicollinearity Test

The Variance inflation factors were used to assess for multicollinearity

Table 4.2: Multicollinearity Test

Variable	Tolerance	VIF
AFP	.514	1.944
Leverage	.739	1.352
Size	.893	1.120
CR	.565	1.769

Source: Study Data

Table 4.2 shows the VIF values are 1.944, 1.352, 1.120 and 1.769 and lie within the range of 1 and 10. This indicates nonexistence of multicollinearity among the study variables.

4.3.2 Homoscedasticity Test

The test was conducted using the Breusch-Pagan test for heteroscedasticity

Table 4.3: Homoscedasticity Test

Breusch-Pagan test for heteroscedasticity	
Test statistic: LM =	3.940018,
with p-value =	P(Chi-square(4) > 3.940018) = 0.91494

Source: Study Data

The findings on table 4.3 indicates that the Test statistic is 3.940018 with a p value of 0.91494>0.05. This indicates nonexistence of heteroscedasticity in the study data

4.3.3 Autocorrelation Test

Table 4.4 shows the results

Table 4.4: Autocorrelation Test

Model	**Durbin-Watson**
1	1.515

Source: Study Data

Table 4.4 indicates that the Durbin Watson statistics value is 1.515, which lies between 1.5 and 2.5 respectively. This indicate that there is no autocorrelation in the study data.

4.4.4 Linearity Test

Figure 4.1 show the linearity test results

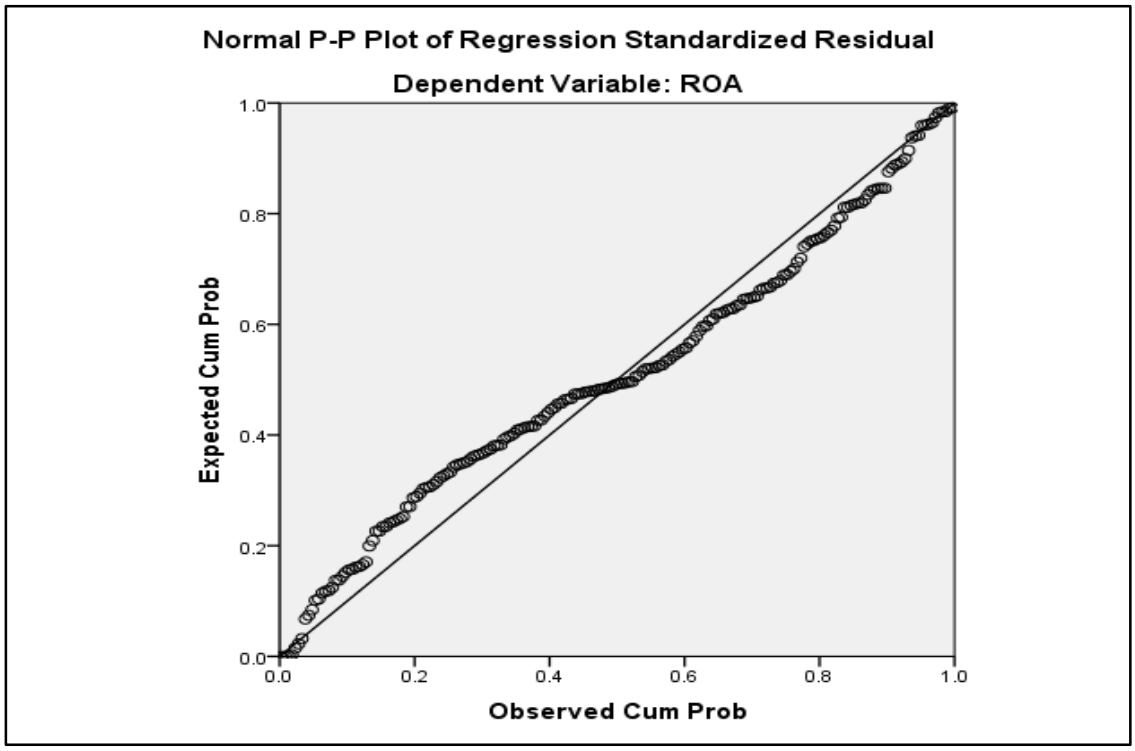

Figure 4.1: P-P Plot

Source: Study Data

Figure 4.1 shows that the data points exhibit a linear relationship based on the plotted graph. This indicates that the assumption of linearity has not been violated

4.4.5 Normality Test

Table 4.5: Normality Test

	Kolmogorov-Smirnova			Shapiro-Wilk		
	Statistic	**df**	**Sig.**	**Statistic**	**df**	**Sig.**
Standardized Residual	.059	200	.091	.975	200	.940

a. Lilliefors Significance Correction

Source: Study Data

Table 4.5 shows that p values under the Kolmogorov-Smirnov and Shapiro-Wilk test were 0.091 & 0.940>0.05 respectively. This indicate that the data is normally distributed.

4.4 Correlation Analysis

This test assessed the existing association among the variables of the study as illustrated under table 4.7

Table 4.6: Correlation Matrix

	ROA	**AFP**	**Leverage**	**Size**	**CR**
ROA	1				
AFP	-.461**	1			
Leverage	-.329**	.443**	1		
Size	.074	-.094	.192**	1	
CR	-.422**	.633**	.390**	.105	1

**. Correlation is significant at the 0.01 level (2-tailed).

Source: Study Data

Table 4.6 shows that the correlation for the aggressive financing policy (AFP) and ROA is -0.461 which indicates a weak and negative while the correlation between leverage and ROA was -0.329 which also indicate a weak and negative correlation respectively. The

correlations between size and ROA was 0.074 hence an indication of a positive and weak correlation while the correlation between liquidity (CR) and ROA was -0.422 hence an indication of a negative and weak correlations respectively.

4.5 Regression Analysis

Regression assessed the link between share returns the study's independent variables. Regression results were as follows

4.5.1 Model Summary

Table 4.7: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.513[a]	.263	.248	.131874

a. Predictors: (Constant), CR , Size, Leverage, AFP

b. Dependent Variable: ROA

Source: Study Data

Table 4.7 shows that the R square value was 0.263 thus an indication that the explanatory variables comprising of liquidity (CR), size, leverage and aggressive financing policy (AFP) accounts for 26.3% of the variation in ROA. Thus, 73.7% of the variation is accounted for by other determinants which the study did not incorporate.

4.5.2 Analysis of Variance

Table 4.8: Analysis of Variance

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.212	4	.303	17.429	.000[b]
	Residual	3.391	195	.017		
	Total	4.604	199			

a. Dependent Variable: ROA

b. Predictors: (Constant), CR , Size, Leverage , AFP

Source: Study Data

Table 4.9 shows that the calculated F statistics value of 17.429 is statistically significant at 95% confidence level. This is indicated by a P value of 0.000<0.05 thus indicating that the regression model is fit and a good predictor of the study relationships.

4.5.3 Regression Coefficients

Table 4.9: Regression Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.019	.083		-.229	.819
	AFP	-.155	.054	-.244	-2.848	.005
	Leverage	-.141	.065	-.156	-2.187	.030
	Size	.008	.005	.104	1.606	.110
	CR	-.024	.009	-.217	-2.658	.009

a. Dependent Variable: ROA

Source: Study Data

The results on table 4.9 shows a negative and significant relationship between aggressive financing policy (AFP) and ROA while the relationship between leverage and ROA was also negative and statically significant respectively. The results further indicates that the

relationship between company size and ROA was positive but statistically insignificant but the association between liquidity (CR) and ROA was negative and significant respectively.

4.6 Interpretation of the Findings

The study established a negative and significant relationship between aggressive financing policy (AFP) and ROA. The finding thus means that a unit increase in aggressive financing policy significantly but adversely affect financial performance of the firms listed at the NSE. A study by Thakur and Muktadir (2017) found an adverse influence of WC financing on performance. Tingbani et al. (2018) found that WCM significantly affected company's profitability. Mwangi, Makau and Kosimbei documented that aggressive financing strategies significantly and positively influenced the entities ROA and ROE, while a conservative funding policy had a direct influence on ROE.

According to the study, the relationship between leverage and ROA was negative and statically significant. The finding thus indicates that a unit increase leverage significantly but negatively affect the NSE listed firms financial performance. Batchimeg (2017) supports that effective management of liquidity beyond survival aids firms to increase their profitability by reducing their input needs. It also offers strategic advantages in economically challenging times.

The findings further established that the relationship between company size and ROA was positive but statistically insignificant. The finding thus indicates a unit increase in the size of the company does not significantly affect the performance of the entities listed at the NSE. However, Wanguu and Kipkirui (2015) posit that as the size of an entity is associated with the firms profitability such that as the size of the business expands so does ROA and

vice versa. Omondi and Muturi (2013) states that larger companies are more competitive than smaller companies in using economies of scale and generating higher profits.

Lastly, the study found that the association between liquidity (CR) and ROA was negative and significant. The finding thus indicate that a unit increase in liquidity significantly but adversely affects the listed firms' financial performance. This is consistent with the risk return trade of which stipulates a negative relationship exists between liquidity and firm profitability. Batchimeg (2017) reports that companies with higher debt are likely to report negative results due to default risk. If a company fails to pay off its liabilities, it would be difficult for the entity to borrow additional funds from financiers.

CHAPTER FIVE: SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This chapter entails a summary of the study findings, conclusions as well as the study recommendations. The chapter further highlights the study limitations and areas that require additional research.

5.2 Summary

The aim of this study is to explore the effect of working capital financing policy on financial performance of firms listed at NSE. The research was grounded on working capital cycle theory, the transaction costs theory and the trade of theory of working capital. The study employed a descriptive study design and the population was made up of 45 non-financial corporations quoted at NSE as at 31st December 2018. The research entirely used secondary data, which was retrieved by use of data collection sheet for a time-period of five years from 2014 to 2018. The collected data was sorted and keyed into the SPSS then analyzed using descriptive statistical tools like the mean, standard deviation, maximum and minimum values and the regression technique to establish the link between the dependent and explanatory variables. The study however managed to collect data from 40 firms thus a response rate of 88.9%.

The descriptive analysis results established that the average ROA was 0.01938 while the average value of the aggressive financing policy (AFP) was 0.29903 respectively. The results revealed that leverage had an average value of 0.15319 whereas the average value

for firm size was 16.2527 while liquidity (CR) had an average value of 1.05190respectively.

The correlation results revealed that the correlation for the aggressive financing policy (AFP) and ROA was weak and negative while the correlation between leverage and ROA was also weak and negative correlation respectively. The study found that the correlation between size and ROA was positive and weak correlation while the correlation between liquidity (CR) and ROA was negative and weak correlations respectively.

The regression results revealed a negative and significant relationship between aggressive financing policy (AFP) and ROA while the relationship between leverage and ROA was also negative and statically significant respectively. The results further established that the relationship between company size and ROA was positive but statistically insignificant but the association between liquidity (CR) and ROA was negative and significant respectively.

5.3 Conclusion

The research indicated there exist a link between aggressive finance policy (AFP) and ROA was negative and significant. The research results show that aggressive financing policy significantly affects financial performance of the firms listed at the NSE. The study found that the relationship between leverage and ROA was negative and statically significant. From this observation, the research further concludes that leverage affects significantly the NSE listed firms financial performance.

Additionally, results show a link between company size and ROA was positive but statistically insignificant. The study thus concludes that the size of the company does not significantly affect the performance of the entities listed at the NSE. The study further

found that the link between liquidity and ROA was negative and significant. The study thus concluded that liquidity significantly affects the listed firms' financial performance.

5.4 Recommendations

The findings led to the conclusion that the aggressive financing policy significantly and negatively affects financial performance of the firms listed at the NSE. The study thus recommends that the management of listed firm should minimize the use of short term financing sources since they reduce the firms' profitability levels.

The results also led to the conclusion that leverage significantly and negatively affects the NSE listed firms financial performance. The study thus recommends that the management of NSE listed firms should use less debt-financing sources since they adversely reduce the firms' returns on investment.

The study further establishes that the size of the company does not significantly affect the performance of the entities listed at the NSE. The study whoever recommends that the management of the listed firms should invest more in fixed assets to growth their firms and increase profitability levels.

The study further concluded that liquidity significantly and negatively affects the listed firms' financial performance. The study based on the finding recommends that the management of firms listed at NSE should hold optimal liquidity since too much liquidity adversely affects the firms' profit levels.

5.5 Limitations of the Study

This study focused on the listed non-financial firms only hence the study did not focus on other segments at the NSE. Thus, the findings may not be generalized to the other financial firms listed firms at the Kenyan securities exchange. Further, the study's context was Kenya thus the findings may not be generalized to other countries other than Kenya.

Secondly, the study used secondary data which is historical in nature and does not reflect the firm current and future prospects. In addition, secondary data does not capture qualitative factors and other managerial decisions by the firms' management. In addition, different firms use different accounting standards which may lead to different interpretation of the calculated financial ratios.

Lastly, the study further focused only on aggressive financing policy, leverage, company size and liquidity thus the findings are based on the considered study variables. The study also used the regression model and the descriptive research methods hence the findings are based on the considered methodology. The study further covered only 5 years between 2014 and 2018 thus the findings may not be generalized to the previously used periods.

5.6 Suggestion for Further Research

The model summary of the study revealed that only 26.3% of the various in the listed manufacturing and allied firms performance (ROA) was accounted for by aggressive financing policy, leverage, company size and liquidity. This indicates that there are other internal factors which affects the financial performance of the listed manufacturing and allied entities. The study thus recommends an additional research on the other internal factors, which might affect firms' profitability levels.

The study also did not assess the various factor that might affect working capital financing on different organization. The study thus recommends an additional research on the determinants of working capital financing. The study only focused on aggressive financing policy but there is also aggressive investment policy. The study thus gives suggestion on how aggressive investment policy affects firms financial performance.

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APPENDICES

Appendix I: Listed Non-Financial Firms

1.	Williamson Tea	30.	Eveready East Africa
2.	Unga Group	31.	East African Breweries
3.	Umeme	32.	Eaagads Ltd
4.	Uchumi Supermarket	33.	E.A.Portland Cement
5.	Trans-Century	34.	E.A.Cables Ltd
6.	TPS Eastern Africa (Serena)	35.	Deacons (East Africa) Plc
7.	Total Kenya	36.	Crown Paints Kenya.
8.	Standard Group	37.	Centum Investment
9.	Scangroup	38.	Carbacid Investments
10.	Sasini Ltd	39.	Car and General
11.	Sameer Africa PLC	40.	British American Tobacco
12.	Safaricom PLC	41.	Bamburi Cement
13.	Rea Vipingo	42.	B.O.C Kenya
14.	Olympia Capital Holdings	43.	Athi River Mining
15.	Nation Media Group	44.	Flame Tree Group Holdings
16.	Nairobi Securities Exchange	45.	Express
17.	Nairobi Business Ventures Ltd		
18.	Mumias Sugar		
19.	Longhorn Publishers		
20.	Limuru Tea		
21.	Kurwitu Ventures		
22.	Kenya Power & Lighting		
23.	Kenya Orchards		
24.	Kenya Airways		
25.	KenolKobil		
26.	KenGen		
27.	Kapchorua Tea.		
28.	Kakuzi		
29.	Home Afrika		

Appendix II: Data Collection Sheet

	2014	2015	2016	2017	2018
Net income					
Total assets					
Short-term finances					
Total debt					
Current assets					