

**THE RELATIONSHIP BETWEEN FINANCIAL MANAGEMENT
PRACTICES AND FINANCIAL PERFORMANCE IN THE DAIRY
INDUSTRY IN KENYA**

BY

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DECLARATION

This research project is my original work and has not been presented for award of a degree in any other University.

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DEDICATION

This work is dedicated to my dear wife, my mother and my siblings for their every support, encouragement, prayers and their presence in my life during the time I worked on this project. It is a collective family achievement

May God bless you all Abundantly

ABSTRACT

The objective of this study is to establish the relationship between financial management practices and financial performance of dairy industry in Kenya. For the purpose of the study, financial management practices are defined and demarcated as the practices performed by the accounting officer, chief financial officer and other managers in the areas of budgeting, supply chain management, movable asset management and control. No study that the researcher is aware of has been done to determine the extent to which the organizations in the dairy sector have embraced financial management practices and how these modern practices have improved their performance. This study therefore sought to determine the relationship between financial management practices and the financial performance of the organizations in the dairy sector in Kenya

The research design employed in the study was a cross-sectional research design where the researcher studied financial performance of dairy processors for the year 2014/2015 financial year and sought to determine the relationship between financial management practices and financial performance of these organizations in that period. In this study four aspects of financial management practices were studied namely; financial reporting analysis, fixed asset management, capital structure management and working capital management. Performance was measured by the return on assets (ROA) and regression analysis used to determine the resulting relationship.

The regression analysis found that without the four financial management practices, the dairy processors financial performance would be dismal. It was further established that quality of financial performance would rise by 0.304 with every unit positive increase in financial report analysis provided that other factors (noncurrent assets management, capital structure management and working capital management) are constant. This statistic is significant at 95% confidence level ($p = 0.000$). Noncurrent assets management would however lead to decrease in quality of financial performance by factor of 0.602 with P value of 0.000 should other factors be held constant, lastly from the findings, it is also evident that working capital management enables the dairy processors to be able to readily operationalize its activities and has the highest influence on quality of the firms' financial performance

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LIST OF ABBREVIATIONS

AIS	:	Accounting Information System
CBA	:	Cost Benefit Analysis
CSM	:	Capital Structure Management
FAM	:	Fixed Asset Management
FRA	:	Financial Reporting Analysis
KCC	:	Kenya Co-operative Creameries
KDB	:	Kenya Dairy Board
NKCC	:	New Kenya Cooperative Creameries
NPV	:	Net Present Value
ROA	:	Return On Assets
ROE	:	Return on Equity
SDP	:	Smallholder Dairy Project
WACC	:	Weighted Average Cost of Capital
WCM	:	Working Capital Management

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Many people who start to run a business do not engage themselves in financial matters. The reason may be because they do not have enough knowledge or interest in recording transactions, preparation and analysis of financial statements and secondary they are extremely involved in other aspects of business like managing people, sales purchasing and production. These entrepreneurs rely on their accountants to run the financial side of their business. While financial management is a critical element of the management of a business as a whole, within this function the management of its assets is perhaps the most important. In the long term, the purchase of assets directs the course that the business will take during the life of these assets, but the business will never see the long term if it cannot plan an appropriate policy to effectively manage its working capital. In effect the poor financial management of owner-managers or lack of financial management altogether is the main cause underlying the problems in SME financial management.

Financial management refers to the process of managing financial resources, including management decisions concerning accounting and financial reporting, forecasting, and budgeting, as well as capital budgeting decisions, which include decisions whether to lease or buy, and whether to issue debt or equity. Financial management is one of several functional areas of management but it is central to the success of any small business (Meredith, 1986). Financial management is the management of finances of a business in order to achieve the financial objectives of the business. The growing importance of this issue raises interesting questions

whether companies are improving their abilities to have effective financial management and implementing changes that will enable them to analyze results, to interpret, to forecast future performance and improve their business decisions (Barker 2003) McMahon et al. (1993) defines financial management based on mobilizing and using sources of funds: Financial management is concerned with raising the funds needed to finance the enterprise's assets and activities, the allocation of these scarce funds between competing uses, and with ensuring that the funds are used effectively and efficiently in achieving the enterprise's goal. Ross et al (1999) indicated three kinds of decisions the financial manager of a firm must make in business; these include the financing decision, and decisions involving short-term finance and concerned with the net working capital, investment and financial reporting

Shahwan and Al-Ain (2008) argued that users of financial report should be able to make decision about resource allocation and are capable to manage the resources. Business decision is relying on relevant information produced. Information should be of high quality. Besides, the information can be viewed in different dimensions, which are to monitor performance, to investigate relationship and to take advantage of trends. According to Xu, Nord, Nord and Lin (2003), information quality is information that is fit to be used and has four attributes which are accuracy, timeliness, completeness and consistency. Shahwan and Al-Ain (2008) noted that relevancy and reliability have been the qualitative characteristics to make accounting information useful. Recently, with the company's development and growth, it is important for company managers to understand and get involved in the accounting figures produced. Moreover, relevant accounting information could help users to make wise decisions (Shahwan and Al-Ain 2008). Accounting information is also viewed as relevant and very important to assist managers to

reduce uncertainty in decision-making. This information can be obtained from proper financial statements which come from effective financial management.

Damand (2003) argued that financial statements should be counted in, to enable managers to make decisions. From simple understanding on financial statements that show the value of the investments in balance sheets and the income received shown in the income statements will help the managers to make simple decision. Well managed resources will make the investors or bankers to consider committing some funds to the same management. Thus, it is very important for the management to keep the financial statement available. The must have qualities that should be given preferences by the managers are reliability and relevancy. Sometimes, the financial reports of the companies do not fulfilled this requirements thus making decision difficult. Again, Damand (2003) argued that if accounting information is more reflective on the economic reality and more transparent, the benefits are not only for the companies but for the society as a whole. However, most of the managers could not rely on financial statements because the aim of financial statements is not clearly stated. As a result, effective financial management is critically needed

1.1.1 Financial Management Practices

Gitman (2007) defines financial management as the area of business management, devoted to a judicious use of capital and a careful selection of sources of capital, in order to enable an organization to move in the direction of reaching its goals. This definition points to certain essential aspects of financial management namely prudent or rational use of capital resource and achieving the goal of the firm. According to Oduware (2011), financial management entails

planning for the future of a business enterprise to ensure a positive cash flow. According to (Moore and Reichert, 1989), financial management practices are defined as the practices performed by the accounting officer, the chief financial officer and other managers in the areas of budgeting, supply chain management, asset management and control. The most common financial management practices used are Accounting Information Systems (AIS), Financial Reporting and Analysis (FRA), Working Capital Management (WCM), Fixed Asset Management (FAM) and Capital Structure Management (CSM). All these practices are crucial for an efficient financial management in organizations.

Accounting Information System indicate an integrated framework within an entity (such as a business firm) that employs physical resources (i.e., materials, supplies, personnel, equipment, funds) to transform economic data into financial information for; conducting the firm's operations and activities, and providing information concerning the entity to a variety of interested users. Indeed, the combination or interaction between human, technology and techniques would permit an organization to administer its knowledge effectively (Bhatt, 2001; Thomas and Kleiner, 1995).

Working capital is a part of a firm's current assets. depending on the source, working capital can be defined in different ways. Working capital is defined as a company's total investment in current assets or assets that a company expects to be converted into cash within a year or less (Keown; Martin; Petty; and Scott, 2005). The investment in working capital involves carrying costs and shortage costs, so the firms have to find the tradeoff between them.

Capital structure is defined as the relative amount of debt and equity used to finance a firm. It's the relative amount of permanent short term debt, long term debt, preferred stock and common equity used to finance a firm. In contrast, financial structure refers to the amount of total current liabilities, long term debt, preferred stock and common equity used to finance the firm. Thus, capital structure is part of financial structure, representing the permanent sources of a firm's financing (Boateng, 2004).

Accounting information systems assist in the analysis of accounting information provided by the financial statements. Romney (2009) purport that the biggest advantage of computer-based accounting information systems is that they automate and streamline reporting. As pertains to Financial Reporting Analysis (FRA), recording and organizing the accounting information systems will not meet objectives unless reports from systems are analyzed and used for making managerial decisions (Gitman, 2011).

Working Capital Management (WCM) refers to decisions relating to working capital and short term financing (Garrison, 1999). These involve managing the relationship between a firm's short-term assets and short-term liabilities. Fixed (non-current) assets management (FAM) is an accounting process that seeks to track non-current assets for the purposes of financial accounting, preventive maintenance and theft deterrence (Garrison, 1999). Capital Structure Management (CSM) according to (Romney, 2009) means overseeing the capital structure of an organization. A company's capital structure refers to the combination of its various sources of funding. Most companies are funded by a mix of debt and equity.

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1.1.2 Financial Performance

Financial performance refers to the act of performing financial activity. In broader sense, financial performance refers to the degree to which financial objectives being or has been accomplished. It is the process of measuring the results of a firm's policies and operations in monetary terms. It is used to measure firm's overall financial health over a given period of time and can also be used to compare similar firms across the same industry or to compare industries or sectors in aggregation (Padachi, 2006). A well designed and implemented financial management in an organization is expected to contribute positively to the creation of a firm's value, Dilemma in financial management is to achieve desired trade-off between liquidity, solvency and profitability (Lazaridis, 2006).

The subject of financial performance has received significant attention from scholars in the various areas of business and strategic management. It has also been the primary concern of business practitioners in all types of organizations since financial performance has implications to organization's health and ultimately its survival. High performance reflects management effectiveness and efficiency in making use of company's resources and this in turn contributes to the country's economy at large. (Naser and Mokhtar, 2004). The financial performance of

organizations is usually measured using a combination of financial ratios analysis, benchmarking, measuring performance against budget or a mix of these methodologies (Barley, 2000). Performance measurement serves as a source of information about financial outcomes and the internal operations shown in an organization's financial statements. Effective performance measurement is key in ensuring that an organization's strategy is successfully implemented. Ofley (2003) argues that financial measure of performance is very crucial as it serves as a tool of financial management, a major objective of a business organization, and a mechanism for motivation and control within an organization.

The recommended measures for financial analysis that determine a firm's financial performance are grouped into five broad categories: liquidity, solvency, profitability, repayment capacity and financial efficiency. Liquidity measures the ability of the firm business to meet financial obligations as they come due, without disrupting the normal, ongoing operations of the business. Liquidity can be analyzed both structurally and operationally. Structural liquidity refers to balance sheet measures of the relationships between assets and liabilities and operational liquidity refers to cash flow measures. A frequent cause of liquidity problems occurs when debt maturities are not matched with the rate at which the business' assets are converted to cash, return on sales reveals how much a company earns in relation to its sales, return on assets determines an organization's ability to make use of its assets and return on equity reveals what return investors take for their investments. The advantages of financial measures are the easiness of calculation and that definitions are agreed worldwide. Traditionally, the success of a processing firm or any company has been evaluated by the use of financial measures (Tangen, 2003).

Solvency measures the amount of borrowed capital used by the business relative the amount of owner's equity capital invested in the business. In other words, solvency measures provide an indication of the business's ability to repay all indebtedness if all of the assets were sold. Solvency measures also provide an indication of the business's ability to withstand risks by providing information about the operation's ability to continue operating after a major financial adversity (Harrington and Wilson, 1989).

Profitability measures the extent to which a business generates a profit from the factors of production: labor, management and capital. Profitability analysis focuses on the relationship between revenues and expenses and on the level of profits relative to the size of investment in the business. Four useful measures of profitability are the rate of return on assets (ROA), the rate of return on equity (ROE), Operating profit margin and Net income (Hansen and Mowen, 2005).

Repayment capacity measures the ability to repay debt from both operation and non-operation income, It evaluates the capacity of the business to service additional debt or to invest in additional capital after meeting all other cash commitments. Measures of repayment capacity are developed around an accrual net income figure. The short-term ability to generate a positive cash flow margin does not guarantee long-term survivability (Jelic and Briston, 2001).

1.1.3 Relationship Between Financial Management Practices And Financial Performance.

Literature on financial management of many firms identifies the components of financial management practices crucial to the performance of every firm as financial planning and control, financial analysis, accounting information, management accounting, capital budgeting and working capital management (Osman 2007; Azhar et al. 2010).According to Maseko and Manyani (2011), accounting systems provide a source of information to owners and managers of businesses operating in any industry for use in the measurement of financial performance. It is crucial therefore that the accounting practices of businesses supply complete and relevant financial information needed to improve economic decisions made by entrepreneurs.

Ismail and Zin (2009) note that business strategy is one of the main components that contributes towards growth of any firm. Padachi (2010) points out that the main factors that contribute to success or failure of business are categorized as internal and external factors. The external factors include financing (such as the availability of attractive financing), economic conditions, competition, government regulations, technology and environmental factors. The internal factors are managerial skills, workforce and the accounting systems. This is consistent with the views of Ismail and Zin (2009) and Nandan (2010) that in the context of small and big businesses, accounting information is important as it can help the firms manage their short-term problems in critical areas like costing, expenditure and cash flow, by providing information to support monitoring and control. Ismail and King (2005), Son et al. (2006), and Shahwan and Al-Ain (2008) point out that accounting information is also useful for firms operating in a dynamic and competitive environment as it can help them integrate operational initiatives within long-term

strategic plans. Sarapaivanich (2003) find that SMEs lack of access to capital and high interest rates charges are partially the result of incomplete accounting records, and the inefficient use of accounting information. Poor record keeping and accounting information make it difficult for financial institutions to evaluate potential risks and returns making them unwilling to lend to SMEs.

1.1.4 Dairy Industry in Kenya

Kenya's dairy industry is dynamic and plays an important economic and nutrition role in the lives of many people ranging from farmers to milk hawkers, processors, and consumers. Kenya has one of the largest dairy industries in sub-Saharan Africa. Though the last livestock census was conducted in 1966, the current official cattle population statistics come from the Ministry of Livestock and Development, through its field reports compiled by extension officials. The official statistics place the number of milking cattle at 3.8 million (Government of Kenya, 2008). A survey conducted by Smallholder Dairy Project (SDP) asserts that there are approximately 6.7 million dairy cattle in Kenya (SDP, 2005). The Food Agricultural Organization (FAO 2012) on the other hand estimates a figure of 5.7 million milking animals.

Milk processing was adopted in Kenya in 1925 with the incorporation of Kenya Cooperative Creameries (KCC) Ltd as a public liability company, by way of shares. By then the industry was run through cooperative movements and a number of dairy cooperative societies came together to form Dairy Cooperative Unions. Kenya Dairy board was established through an act of Parliament Cap 336 of the laws of Kenya in 1958. The board was established to ensure the orderly and smooth development of the dairy sector in Kenya (GOK 2001).Up to 1992, dairy

industry in Kenya was under government control, which gave the policy guidelines, set prices, determined the players in the industry and set the market rules among other things. Kenya Cooperative Creameries (KCC) Ltd enjoyed a protected monopoly in the marketing of the milk and dairy products. Milk market liberalization policies were announced in 1992 and it opened up the processed milk market, which hitherto was monopolized by KCC. This liberalization in 1992 led to various challenges, key among them the emergence of a large informal sector and participation by private sector players in the milk business. This almost led to the collapse of the industry. (EPZ, 2005).

Over the last few years there has been a paradigm shift. The dairy sub sector is now one of the fastest growing sectors in the economy. This has led to increased stakeholder expectations. There is now increased demand for more efficient services among all the stakeholders from the Industry regulator which is Kenya Dairy Board (KDB 2007). Presently, the milk processing industry is regulated by the Kenya Dairy Board (KDB), established under Section 4 of the Dairy Industry Act Cap. 336 enacted by Parliament in 1958 and It is from this Act that the Board derives its mandate being to develop, promote and regulate the dairy industry, creating an enabling environment for increased private sector entrepreneurship in milk production, processing and marketing, enforcement of national standards for the industry and maintenance of a databank for the dairy industry and regulating of imports (EPZ, 2005).

According to KDB (2013), there were 54 (Fifty four) licensed milk processing firms in Kenya as at 31st January 2013. Out of these, 34 (Thirty four) are licensed as milk processors and 20 (Twenty) as Mini Dairies. The industry is however dominated by 5 processors namely: New

Kenya Cooperative Creameries (NKCC), Brookside Dairy Ltd, Githunguri Dairy Farmers Cooperative Society (Fresha), Sameer Agriculture and Livestock Ltd (Daima) and Buzeki Dairy Ltd (Molo milk). These milk processors currently produce a wide range of products namely fresh milk, yoghurt, mala, ice cream, cheese, UHT, powder milk, butter and ghee. Milk production in Kenya is currently dominated by small-scale producers located mainly in the Rift Valley, Central and Eastern provinces. Various production systems mainly rely on rain-fed agriculture and the current dairy cattle population is estimated at 3.8 million (Kenya Dairy Board, 2010).

Milk processors in Kenya export substantial quantities of milk and milk products to the region. Intra-regional trade of dairy products in the East African Community has continued to gain momentum and benefits in the dairy industry. The main products exported are long life milk and powder milk. It is important to note that dairy imports have gone down over time as Kenya becomes increasingly more self-sufficient in milk and milk products. However, specialized milk products are imported mainly from New Zealand and the European Union (Kenya Dairy Board, 2010).

1.2 Research Problem

Nowadays, competition is everywhere in the business environment. Because of that, companies are trying hard to create better interaction with customers and suppliers. Therefore, wise decision making is very crucial to the success of the companies. Shahwan and Al-Ain (2008) and Sian and Roberts (2009) suggested that managers need to have effective financial management as well as information technology (IT) as a tool to help them make effective decisions. Moreover, during the economic downturn, companies have to change their attitudes to be more competitive in the

environment. Those companies have to meet the customers' requirements and need to provide good products and services. As a result, the management has to make faster decision to improve the efficiency and effectiveness of the business activities. Mitchell et al. (2000) argued that accounting information is important because it can help companies solve short term problems and assist in decision making. Further, recent empirical evidence suggests that effective financial management may contribute to the success of companies in future (Barker 2003). Generally, the success of companies in managing its business financial should be evaluated by the owner of the companies in terms of their usefulness in decision making (Shahwan and Al-Ain 2008)

Studies on the relationship between financial management practices and financial performance have presented mixed results. Globally, a number of studies have been done in the area of financial management practices. Moore and Reichert (1989) in their multivariate study of firm performance and use of modern analytical tools and financial techniques study in 500 firms in US, they showed that firms adopting sophisticated capital budgeting techniques had better than average firm financial performance. More specifically, firms using modern inventory management techniques and Internal Rate of Return (IRR) reported superior financial performance, unlike those firms using methods such as Payback method and Accounting Rate of Return (ARR), (Raheman and Nasr, 2007).

Gloy, Hyde and LaDue (2002) reviewed the relationship between financial performance and several management factors in a study of 107 New York dairy farms over the period 1993 to 1999. A fixed-effects regression model was developed to examine the relationship between return on assets (ROA) and financial management practices. Financial management practices

included record-keeping practices, level of debt as measured by debt-to-asset ratio, asset structure as measured by the proportion of long-term assets to total assets, and rental practices. Indicator variables were constructed to distinguish whether farmers used either a hand ledger system, a computerized ledger system, hired an external accounting service to construct their accounts, or did not use any of the mentioned record-keeping methods. Only two of the financial management variables had a statistically significant and positive impact on ROA, namely level of debt and the use of financial record keeping. The highest ROA was achieved by farmers who hire an outside record-keeping service to construct their financial information. Shahwan and AlAin (2008) also mentioned that most small companies have improper financial management. In addition, the researchers pointed out that only a very small percentage of the companies prepare accounting information internally using accounting software.

Locally, a number of studies have been done on financial management practices. Wanyungu, (2001) who did a research financial management practices of micro and small enterprises in Kenya, A case of Kibera, while Mundu (1997) did a research on selected financial management practices by small enterprises in Kenya, Nyongesa (2011) looked at the relationship between financial performance and financial management practices of insurance companies in Kenya. The study revealed that there was a consistent, significant positive association between financial management practices and financial performance. However, the study did not establish reasons for this correlation

From the foregoing background information it's evident that, there exists scanty systematically documented information where the relationship between financial management practices and financial performance in the dairy industry is clearly outlined therefore a gap exists which needs to be addressed. The report aims to:

- i. To identify the financial management practices adopted by dairy companies in Kenya
- ii. To determine the relationship between financial management practices and financial performance of dairy companies in Kenya

1.3 Research Objective

The objectives of this study is

- i. To identify the financial management practices adopted by dairy companies in Kenya
- ii. To determine the relationship between financial management practices and financial performance of Dairy companies in Kenya

1.4 Value of Study

The significance of the study first of all will contribute to finance theory; this study draws on researchers' observation from the obviously ignored area on the relationship between financial management practices and financial performance of dairy processing firms in Kenya. It tries to fill the gap in previous literature about how financial practices affect performance of dairy processing firms. It will give a fresh insight into the possible correlation between financial management practices and performance in dairy processing firms by theoretical exploration and finally help expands the existing findings in the finance literature. Because quantitative research will be involved in the study, it will enhance the existing research with more empirical data

This study, as a whole, caters to a perceived need of dairy processing firms owners/managers for better budgeting practice to improve performance. The findings of this research will provide owners/managers of dairy processing firms with more useful understanding about financial management and performance. The results will simultaneously contribute to business consultants to better understand financial planning implementation and budgeting in dairy firms. This study also responds to the fast growth of milk processing firms and vendors, not only domestically but also globally.

The findings will also help the management of milk processors in solving the problems encountered in budgeting and how they can purpose to mitigate the challenges since this is one area which leads to success of any milk processor in Kenya and finally the research will form a reference point on future studies to the academicians and researchers for academic purposes in learning on the financial management practices adopted by the milk processors in Kenya

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

The chapter has been organized into Theoretical Literature Review, Financial Management Practices, Empirical literature review and Summary of Literature Review

2.2 Theoretical Literature review

2.2.1 Proprietary Theory

According to this theory, a company owned by some persons or groups is the center of interest, and is called the proprietor. Accounting is held to serve the proprietors ‘interests and the items in the financial statements are treated from the proprietors’, or stockholders’, point of view, since proprietors get the ultimate benefits of the business, as well as suffer from the failure the most (Rosenfield, 2005). The notion of proprietorship originally comes from the logic of the exposition of double-entry bookkeeping:

Assets – Liabilities = Stockholders’Equity

or Proprietorship From this basic accounting equation, it can be interpreted as all assets of the firm belong to the owners or proprietors, and any liabilities are also their obligations. Thus, revenues received by the firm are increases of the proprietorship of the firm and, likewise, the liabilities born by the firms are decreases of the net proprietary interest in the firm (Hendriksen & Breda, 2001). Interest, taxes, and other deductions are treated as expenses since they decrease the proprietorships; the only distribution is dividend paid to the stockholders. Husband (1954), an accounting theorist who favors the proprietary theory, finds that this treatment provides logic and consistency in accounting thinking as stockholders or owners are the ones who bear the ultimate risk. He insists that proprietary theory “appears to provide a more realistic basis for the

development of accounting principles, in spite of the fact that it encounters an obstacle in the situs of legal title”(Husband, 1934, p. 253). The proprietary theory is claimed to be best for sole proprietorship and thus when the businesses are bigger and more complex, the proprietary concept might be less acceptable. However, many of today’s accounting practices are still strongly affected by this concept and imply that retained earnings are the net wealth of the stockholders. The comprehensive income, which includes all items affecting the net wealth, is one of the accounting practices that reflect the influence of the proprietary theory (Hendriksen & Breda, 2001)

2.2.2 The Contingency Theory

According to Pike (1986) resource-allocation efficiency is not merely a matter of adopting sophisticated, theoretically superior investment techniques and procedures but consideration must also be given to the fit between the corporate context and the design and operation of the capital budgeting system. Pike (1986) focuses on three aspects of the corporate context which are assumed to be associated with the design and operation of a firm’s capital budgeting system

Contingency theory has become prominent in both organization theory and management accounting. It has also been suggested that the contingency approach is implicit in accounting policy making. The contingency framework is extended to corporate reporting and it is argued that this may provide a means of explaining and predicting such systems. The contingent variables are conceptualizes as falling into four classes which consist of: (1) societal variables; (2) the environment of the enterprise; (3) organizational attributes; and (4) user characteristics and others sources of information. These are shown to be associated with particular attributes of corporate reporting system.

Schweikart (1985) observes that there is significant concern evident in the international accounting literature relating to issues such as harmonization and differences in the accounting information presented across countries, as well as what he described as the “suggestion” that accounting information needs in different countries are subject to environmental influences. Schweikart’s (1985) observation that there had been little empirical work conducted to support the concept of environmental influences on accounting is no longer a valid one, as there are many researchers using a contingency theory as a vehicle to establish a theory of international accounting (e.g. see Cooke and Wallace, 1990; Adhikari and Tondkar, 1992; Douppnik and Salter, 1995; Salter, 1998)

2.2.3 Residual Equity Theory

In the residual equity theory, changes in asset valuation, changes in income and in retained earnings, and changes in interest of other equity holders are all reflected in the residual equity of the common stockholders. The specific equities include the claims of creditors and the equities of preferred stockholders. The balance sheet equations become as follows: Assets minus specific equities are equal to Residual equity’. The equity of the common stockholders in the balance sheet should be presented separately from the equities of preferred stockholders and other specific equity holders. According to Hendriksen (1982), the residual equity of view is a concept somewhere between the proprietary theory and the entity theory

The objective of the residual equity approach is to provide better information to common stockholders for making investment decisions. In a going-concern situation, the current value of common stock is dependent primarily upon the expectation of future dividends. Future dividends are dependent upon expectations of total receipts less specific contractual obligations, payments

to specific equity holders, and requirements for reinvestment. Since financial statement are not generally, prepared on the basis of possible liquidation, the information provided regarding the residual equity should be useful in predicting possible future dividends to common stockholders including liquidation dividends (Hendriksen, 1982).

2.3 Financial Management Practices

For the purpose of this section, financial management practices are defined and demarcated as the practices performed by the accounting officer in the areas of fixed asset management, accounting information systems, working capital management, financial reporting analysis and capital structure management. According to Rao (2005) financial management involves control and treasury. Control looks at financial accounting, cost accounting, taxes and data processing. Treasury is concerned with cash management, capital budgeting, financial planning, credit analysis, investor relations and pension fund management.

2.3.1 Fixed Asset Management (FAM)

For the purpose of this thesis the focus is on movable assets; the acquisition of capital assets can most certainly exert an effect on an organization's competitive advantage over the long term. Capital equipment is characterized by large expenditure and non-recurring expenditure. Purchasing capital equipment usually requires a relatively large capital outlay, which may sometimes amount to millions and which may have particular financial implications. Buying capital equipment can therefore be regarded as an investment which is financed from long-term, rather than from working, capital.

It is important to consider not only the purchase price of capital equipment, but also the total cost of ownership (Hugo *et al.*, 2006). Capital equipment is usually purchased at irregular intervals. It

is used up gradually in the production process, rather than as a part of the end product. Owing to the relatively long lifespan of equipment, it could take several years before it needs to be replaced and, at the time of replacement, old equipment could prove to be technologically obsolete. If the correct purchasing decision is made, capital equipment generates profits for the organization. Incorrect decisions may have disastrous consequences for the enterprise, since it will not be able to sell capital equipment over the short term. For the above reason, according to Burt, Dobler and Starling (Hugo *et al.*, 2006), top management should consider the acquisition of capital equipment, with care.

2.3.2 Accounting Information Systems (AIS)

Orwel (2009) states that the AIS is a system of records usually computer-based, which combines accounting principles and concepts with the benefits of an information system and which is used to analyze and record business transactions for the purpose of preparing financial statements and providing accounting data to its users. AIS assists in the analysis of accounting information provided by the financial statements. Romney et al (2009) purport that the biggest advantage of computer-based accounting information systems is that they automate and streamline reporting. Reporting is a major tool for organizations to accurately see summarized, timely information used for decision-making and financial reporting.

2.3.3 Financial Reporting Analysis (FRA)

Bookkeeping alone without preparing reports is likely not to be fundamental in aiding decision making unless proper reports are prepared and analyzed to attach a meaning so as to help decision makers. Financial statements usually provide the information required for planning and

decision making. Information from financial statements can also be used as part of the evaluation, planning and decision making by making historical comparisons (Gitman, 2011).

2.3.4 Capital Structure Management (CSM)

Capital Structure Management (CSM) according to Romney (2009) means overseeing the capital structure of an organization. A company's capital structure refers to the combination of its various sources of funding. Most companies are funded by a mix of debt and equity. When determining a company's cost of capital, the costs of each component of the capital structure are weighted in relation to the overall total amount. This calculates the company's weighted average cost of capital (WACC). The WACC is used to calculate the net present value (NPV) in capital budgeting for corporate projects. A lower WACC will yield a higher NPV hence achieving a lower WACC is always optimal.

2.3.5 Working Capital Management

According to (Garrison, 1999), Working Capital Management (WCM) refers to decisions relating to working capital and short term financing. These involve managing the relationship between a firm's short-term assets and short-term liabilities. The goal of WCM is to ensure that the firm is able to continue its operations and that it has sufficient cash flow to satisfy both maturing short-term debt and upcoming operational expenses. The context of working capital management includes cash management, receivables and payables management, and inventory management.

2.4 Empirical Literature Review

Several studies have been conducted on financial management practices of organizations. For instance, D'Amboise and Gasse (1980) studied the use of financial statement analysis by small manufacturers in Quebec, Canada and found that small manufacturers in shoe and plastic industries formally undertook the analyses based on financial statements and the findings revealed that manufacturing firms' managerial decisions were largely based on the financial reports prepared. The research conducted by DeThomas and Fredenberger (1985) found that 81 percent of the small enterprises regularly obtained summary financial information. Ninety-one percent of the summary information was in the form of traditional financial statements (balance sheets, profit and loss statements, fund statements), the remainder being bank reconciliation and operating summaries whereas no business was regularly receiving cash-flow information. The study further found that 61 percent of respondents felt the financial statements provided the information they required for planning and decision-making. Nevertheless, only 11 percent of respondents reported that they had used financial statement information formally as part of managerial evaluation, planning and decision-making, 2 percent of businesses utilized financial ratio analysis, and few made even simple historical comparisons.

Nguyen (2001), sought to assess the relationship between financial management practices and profitability of small and medium enterprises in Australia. He focused his attention at various financial management practices and financial characteristics and demonstrates the simultaneous impact of financial management practices and financial characteristics on SME profitability. He further examined fixed (non-current) asset management practices of a sample of 99 trading and 51 manufacturing SMEs. He found out the nearly 80 percent of SMEs always or often evaluate

capital projects before making decisions of investment and review the efficiency of utilizing fixed assets after acquisitions. Some 87 percent of SMEs stated that they used payback period techniques in capital budgeting; only 27 percent used the more sophisticated discounted cash flow techniques, the Net present value (NPV), internal rate of return (IRR) and modified internal rate of return (MIRR). These findings revealed that SMEs highly regarded fixed asset management although their knowledge of management techniques was not outstanding.

In Kenya Mundu (1997) sought to review selected financial management practices adopted by small enterprises in Kenya. The study found out that 66% of the respondents did not undertake cash budgeting, 70% of the business owners kept surplus cash with themselves and over 56% of the business owners were handling cash personally as the security to their money. Furthermore, more than 70% of the respondents sold on credit to those customers believed to be known by the business owner. Overdue accounts were followed up through reminders either by personal visits or telephone calls or both; 70% of the businesses charged prices on the basis of full cost plus margin which may be a mentally calculated price or selling at what the competitors are charging and only 16% of them kept cost control reports. Over 80% of the businesses had prepared a business plan with the most common reason being to get financing. These results led to the conclusion that the survival of SMEs heavily depended on the good practice of formal financial management

2.5 Summary of Literature Review

In the literature, it has been argued that the use of financial management practices may be related to improved financial performance. Some of the studies indicated that sophisticated capital budgeting techniques mostly NPV and IRR had a positive relationship with ROA while the

traditional methods showed an insignificant relationship. However, similar reported a negative relationship between the capital budgeting techniques and financial performance. This indicates that the mere adoption of various analytical tools is not sufficient to bring about superior performance and that, other factors such as marketing, product development, executive recruitment and training, labor relations etc., may have a greater impact on profitability.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter is a blueprint of the methodology that was used during the conduct of this study.. Research methodology, according to Kothari (2004), refers to the logical sequence of the research, the research methods and instruments used. As explained by Kinoti, (1998), the research methodology informs the choice of the research design, the study site, the research population, the sample size and sampling design to be used, the choice of data collection methods and the research tools to be used and finally the data analysis procedures and methods used.

3.2 Research Design

This study used cross sectional research design. This is because; the study took a cross section of firms in dairy industry. This approach is credited due to the fact that it allows analyzing the relations between variables under study using linear regression as long as the sampling units for the study are many. Secondly, cross-sectional survey provides a detailed and highly accurate picture. It is also useful in locating new data that contradicts past data. Finally, it is relevant because it involves specific predictions within narration of facts and characteristics concerning the research problem (Cooper and Schindler, 2008).

3.3 Target Population

Mugenda and Mugenda (1999) expounded that the target population is the population on which the researcher wants to generalize the results of the study. The target populations in this study were the licensed milk processors in Kenya. There were 54 (fifty four) licensed milk processing

firms in Kenya as at 31st January 2013 (KDB, 2013). Out of these, 34 (thirty four) were licensed as milk processors and 20 (twenty) as Mini Dairies. A random sample of 15 licensed processors was surveyed.

3.4 Sample Design

The study used simple random sampling to select a study sample. In random sampling, each item or element of the population has an equal chance of being chosen. Samples of 25% of the total number of licensed processors as at 31st January 2013 were selected to form studies sample. This resulted to a sample size of 15 milk processors. Kotler et al. (2001) argues that if well chosen, samples of about 10% of a population can often give good reliability. Therefore, a sample size of 15, which is 25% of the total population, was adequate for the study. The study will covered 2012-2015

3.5 Data collection

The researcher used both primary and secondary data, In this study, questionnaires functioned as a preliminary data collection technique providing primary data and empirical analysis in this study. The respondents' perceptions on the study variables were obtained from a self-administrated questionnaire conducted with staff (the managers, head of finance and accountants) involved in the formulating and implementing financial management practices. The self-administered questionnaires were either electronically or hand delivered.

The questionnaire included a combination of open-ended questions and closed-ended questions Dillman (2000). The Questionnaire was structured in two parts I and II. Part I contained questions on the general information about the milk processing and its performance. Part II contained

questions on the financial management practices adopted. A five-point Likert scale was used in the design of the financial management practice questions. According to Mugenda et al (1999) the Likert scale can be used to rate or rank the subjective and intangible components in research. The numerical scale helps to minimize the subjectivity and makes it possible to use quantitative analysis

Secondary data include information collected from journals reports and text books (Cooper and Schindler, 2008). Secondary data was done by desk research which leads to a wide literature review about previous research related to financial management practices and the financial performance of organizations. This is because these data is often guided by expertise and professionalism that may not be available to individual researchers or small research projects and also because of the breadth of data available. Financial statements and financial management practices records from the firms will also be used.

3.6 Data Analysis

Data analysis consists of data sorting, editing, cleaning and conducting final check on the data for accuracy, erroneous data completeness and consistencies to avoid going back to the original questionnaires and interviews (Katebire, 2007)

3.6.1 Measurement of Variables

The questions will be based on a scoring system on scale of 1-5 where a score of 1 means the respondent strongly disagrees on whether the organization followed a particular element of financial management practice. Score 2 meant the respondent disagreed, 3 meant he/she neither

agreed nor disagreed, 4 meant the respondent agreed while score 5 meant the respondent strongly agreed that that particular financial management practice was followed.

The study examines the relationship between financial management practices and financial performance of processing firms in the dairy sector. The following regression model will be used in the study

Regression equation used was:

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

Where:

Y = Financial performance as measured by Return on Assets (ROA)

X1 = Unit change in Return on Assets as a result of a unit increase in Financial Reporting Analysis

X2 = Unit change in Return on Assets as a result of a unit increase in Non-current Asset management

X3 = Unit change in Return on Assets as a result of a unit increase in Capital Structure Management

X4 = Unit change in Return on assets as a result of a unit increase in working capital management

ε = Error term

β_0 = Constant

$\beta_1, \beta_2, \beta_3$ and β_4 are parameters of estimates.

The error is the difference between the calculated dependent variable value and the actual value.

The Statistical Package for Social Sciences (SPSS) version 18 was used to analyze the data collected. The coefficient of determination, R squared, measure was used to test the significance of the regression model in explaining the relationship between financial management practices

and financial performance. R squared is a measure of goodness of fit and shows the percentage variance in the dependent variable that is explained by the independent variable(s). The higher the R squared the better the model. The ANOVA statistics was used to present the regression model significance. An F-significance value of $p = 0.000$ was established showing that there is a probability of 0.0% of the regression model presenting a false information. The P-Value and the t-test were used to test the individual significance of the predictor variables used in the study

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSIONS

4.1 Introduction

This chapter looks at data analysis, findings and summary of significant findings in the study.

This study examined the financial management practices and the financial performance of dairy firms in the industry. The population of study consisted of 54 milk processors. Data was collected from a sample of 14 firms. Questionnaires were filled in by top officers in the Finance and Accounting departments. All the 14 processors sampled responded. Data analysis and report of findings was done using descriptive statistics in the form of tables, frequencies and percentages. For analyses of the relationships between independent and dependent variables regression analysis was used

4.2 Financial Management Practices Adopted By Dairy Companies In Kenya

In this study, financial management practices were measured on the basis of four aspects namely: financial reporting analysis, fixed assets management, capital structure management and working capital management based on mean ranking. Elements of each aspect of financial management practice were then identified. On a scale of 1-5, (where 1-strongly disagree, 2-Disagree, 3 Neither Agree nor Disagree, 4 -Agree and 5-Strongly agree) where respondents were asked to tick appropriately the extent to which the company complied with the listed elements of Financial Management practice.

4.2.1 Financial Reporting Analysis

The study identified three key elements of financial reporting analysis namely: Whether the financial statements of the company are prepared in line with the financial accounting standards, whether the financial statements are prepared in accordance with GAAP and lastly whether the financial statements are published regularly

The findings were as indicated in Table 4.1 below.

Table 4.1 Results On The Respondent’s Perception Of Use Of Financial Reporting Analysis

Elements of FRA	N	Mean Score	SD
The financial statements of the company are prepared in line with the financial accounting standards	15	4.50	0.507
The financial statements are prepared in accordance with GAAP	15	4.00	0.586
The financial statements are published regularly	15	3.83	0.697
Grand Mean		4.11	0.597

Source .Author 2015

4.2.2 Fixed Assets Management

The study identified and used six elements of Fixed Assets Management. These included, the company maintains a non-current asset register, non-current assets have been tagged, movement of no-current assets have to be authorized by senior management, non-current assets count is carried out every year, capital expenditure on non-current assets must be authorized by senior management and repair and maintenance of non-current assets is carried out regularly.

The findings were as indicated in Table 4.2 below.

Table 4.2 Results Of Respondents' Perception Of Use Of Fixed Assets Management

Elements of FAM	N	Mean Score	SD
The company maintains a non-current assets register	15	4.17	0.378
The Non-current assets have been tagged	15	4.33	0.756
Movement of non-current assets have to be authorized by senior management	15	4.83	0.380
Non-current assets count is carried out every year	15	4.50	0.507
Capital expenditure on non-current assets must be authorized by senior management	15	4.50	0.507
The repair and maintenance of non-current assets is carried out regularly		4.33	0.478
Grand Mean		4.44	0.501

Source .Author 2015

4.2.3 Capital Structure Management

The study further sought to establish the use of capital structure management as a factor of financial management practice and used five elements of capital structure management namely, whether the capital structure of the processor is appropriate, whether the processor has fully utilized the debt facility according to its capabilities, whether the processor relies on equity capital only, whether the processor is quoted on the NSE and finally whether processor has foreign ownership

The findings were as indicated in Table 4.3 below.

Table 4.3 Respondents perception of use of Capital Structure Management

Elements of CSM	N	Mean Score	SD
The capital structure of the processor is appropriate	15	3.83	0.378
The processor has fully utilized the debt facility according to its capabilities	15	3.50	0.971
The processor relies on equity capital only	15	3.50	0.775
The processor is quoted on the NSE	15	2.17	0.910
The processor has foreign ownership	15	3.33	1.394
Grand mean		3.27	0.886

Source .Author 2015

4.2.4 Working Capital Management

Finally, indicators of working capital management were probed to determine their use within the dairy processors and used seven elements namely, whether the processor has a working capital management system, whether the processor maintains inventory record which are updated regularly, whether the receivable management system is fully automated, whether the optimal cash balances are maintained by the processor at all times ,whether the processor maintains proper record for all payables, whether they ensure there is sufficient cash flow to meet daily needs and finally whether they prepare cash flow forecasts to identify future surpluses and deficits

The findings were as indicated in Table 4.4 below.

Table 4.4 Respondents Perception On The Use Of Working Capital Management

Elements of WCM	N	Mean	SD
The company has a working capital management system	15	4.20	0.378
Maintains inventory records which are updated regularly	15	4.00	1.014
Receivables management system is fully automated	15	4.20	0.363
Optimal cash balances are maintained by the company at all times	15	4.50	0.507
Maintains proper records for all payables	15	5.00	0.000
Ensures there is sufficient cash flow to meet daily needs	15	4.67	0.478
Prepares cash flow forecasts to identify future surpluses and deficits	15	4.00	0.00
Grand Mean		4.36	0.394

Source. Author 2015

4.3 Findings of Financial Management Practices and Financial Performance

According to (Moore and Reichert, 1989), financial management practices are defined as the practices performed by the accounting officer, the chief financial officer and other managers in the areas of budgeting, supply chain management, asset management and control

4.3.1 Financial Management Practices of Specific Dairy Processors.

The study sought to determine the effects of financial management practices on the financial performance of dairy processors in Kenya. Four aspects of financial management practices were studied namely; financial reporting analysis, fixed assets management, capital structure management and working capital management. For each aspect, a practice index which measures the extent to which the company embraced that particular aspect of financial management

practice was derived from an average score of all the elements in the questionnaire. Which was based on a scale of 1-5 (whereby; 1-Strongly Disagree, 2-Disagree, 3-Neither Agree nor Disagree, 4 -Agree and 5-Strongly Agree).

4.3.2 Relationship Between Financial Management Practices and Financial Performance

A multivariate regression model was applied to determine the relationship between financial management practices and financial performance dairy processors in Kenya. Multiple linear regressions used in this model were

R shown in Table 5 is the correlation between the observed and predicted values of dependent variable implying that the association of 0.978 between financial management practices (financial reporting analysis, non – current asset management, capital structure management and working capital management) and financial performance was very good. R-Square is coefficient of determination and measures the proportion of the variance in the dependent variable – financial performance - that is explained by variations in the independent variables - financial reporting analysis, non – current asset management, capital structure management and working capital management. This implied that 95.1% of variance or correlation between dependent and independent variables. That is, 95.1% of variations or changes in financial performance are caused by the financial management practices adopted by dairy processors. However, it does not reflect the extent to which any particular independent variable is associated with financial performance.

Table 4.5 Model Summary

MODEL	R	R SQUARE	ADJUSTED R SQUARE	STANDARD ERROR OF THE ESTIMATE
1	.978a	.957	.951	.15392

Source. Author 2015

a. Predictors: (Constant), WCM, FAM, CSM, FRA

The ANOVA statistics shown in Table 6 was used to present the regression model significance. An F-significance value of $p = 0.000$ was established showing that there is a probability of 0.0% of the regression model presenting a false information. Therefore, the model is very significant.

Table 4.6: Analysis of Variance (ANOVA)

Model	Sum of Squares	Df	Mean Square	F	Sig
Regression	16.226	4	4.066	171.651	.000a
Residual .734	.734	31	0.024		
31 Total	17.000	35			

a. Predictors: (Constant), WCM, FAM, CSM, FRA

b. Dependent Variable: ROA

4.4 Results of Regression Analysis

In this study, the dependent variable is financial performance as measured by Return on Assets (ROA) while the independent variables are financial reporting analysis, fixed assets management, Capital structure management and Working capital management. β_1 , β_2 , β_3 and β_4 are parameter estimates that measure the effect of financial management practices on the financial performance of dairy processing companies. The regression compares the magnitude of the coefficients of the independent to determine which one had more effects on performance

Table 4.7 Regression Coefficients

Model	Unstandized coefficients	Std error	Standardized coefficients	T	sig
	B		Beta		
Constant	15.595	.585	-	26.641	.000
FRA	.340	.048	.904	7.034	.000
FAM	-.602	.051	-1.401	-11.733	.000
CSM	-.317	.024	-1.054	-13.199	.000
WCM	.858	.037	1.514	23.484	.000

Source . Author 2015

From Table 4.7, the following regression model is established:

$$\text{ROA} = 15.595 + 0.304X_1 - 0.602X_2 - 0.317X_3 + 0.858X_4 \quad P = 0.000$$

Where X_1 = financial report analysis, X_2 =noncurrent asset management, X_3 =capital structure management, X_4 =working capital management and $\beta_0 = 15.595$; $\beta_1 = 0.304$;

$\beta_2 = -0.602$; $\beta_3 = -0.317$ and $\beta_4 = 0.858$

The regression constant shows that when the independent variables (financial report analysis, noncurrent assets management, capital structure management and working capital management) are constant at zero, financial performance value would be 15.595. This shows that without the four financial management practices, the dairy processors financial performance would be dismal.

It was established that quality of financial performance would rise by 0.304 with every unit positive increase in financial report analysis provided that other factors (noncurrent assets management, capital structure management and working capital management) are constant. This statistic is significant at 95% confidence level ($p = 0.000$). Noncurrent assets management would however lead to decrease in quality of financial performance by factor of 0.602 with P value of 0.000 should other factors be held constant

Additionally, holding other factors (financial report analysis, non – current assets management and working capital management) constant, a unit increase in capital structure management would lead to a 0.317 decrease in financial performance ($p = 0.000$). Working capital management would lead to an increase in financial performance by a factor of 0.858 significant at $p = 0.000$ should financial report analysis, non – current assets management and capital structure management be kept constant. This indicates that working capital management would positively influence dairy processors financial performance. From the findings, it is also evident

that working capital management enables the dairy processors to be able to readily operationalize its activities and has the highest influence on quality of the firms' financial performance

4.5 Summary of Findings and Interpretations

Four aspects of financial management practices were studied. In the financial reporting analysis, the study found that on average, whether the financial statements of the company are prepared in line with the financial accounting standards scored 4.50, whether the financial statements are prepared in accordance with GAAP 4.00 and whether the financial statements are published regularly 3.83. The study thus found that on average, dairy processor's financial statements of the company are prepared in line with the financial accounting standards and they are also prepared in accordance with GAAP. Publishing statements regularly is still not embraced by most processors in this sector

In Fixed Asset Management the study found that on average, whether the company maintains a non-current asset register scored 4.17, whether non-current assets have been tagged 4.33, movement of no-current assets have to be authorized by senior management 4.83, non-current assets count is carried out every year 4.50, capital expenditure on non-current assets must be authorized by senior management 4.50 and repair and maintenance of non-current assets is carried out regularly 4.33. The study thus found that most processors in the dairy sector movement of no-current assets have to be authorized by senior management and non-current assets count is carried out every year, capital expenditure on non-current assets must be authorized by senior management while tagging of non-current assets and whether repair and maintenance of non-current assets must be authorized by senior management is still not embraced by most processors in this sector.

In capital structure management the study found out that the capital structure of the processor is appropriate with a score of 3.83, processor has fully utilized the debt facility according to its capabilities 3.50, the processor relies on equity capital only 3.50, whether the processor is quoted on the NSE 2.17 and processor has foreign ownership 3.33. The study thus found that on average the capital structure of the processors is appropriate and partially relies on equity capital the study also found that most processors have minimal foreign ownership

In this study in determination of whether the processor has a working capital management system scored 4.17, maintaining inventory record which are updated regularly scored 4.00, whether the receivable management system is fully automated 4.17, whether the optimal cash balances are maintained by the processor at all times 4.00, whether the processor maintains proper record for all payables 5.00, whether they ensure there is sufficient cash flow to meet daily needs 4.67 and finally whether they prepare cash flow forecasts to identify future surpluses and deficits 4.50. Thus on average the study found that processors maintain a proper record for all payable while system automation and having a working capital management is not fully embraced by processors.

In Financial Performance the analysis highlighted the respondent's financial management practices used by the companies and ultimately their effect on the firm's financial performance. To begin with, the study established that various financial management practices are commonly used across companies in the dairy industry. For instance, use of elements of financial reporting analysis was established in concurrence with the findings of previous studies who asserted that

information from financial statements can be used as part of the evaluation, planning and decision making by making historical comparisons. Other financial management practices pointed out as being significant for the dairy companies included capital structure management and working capital management. With regard to the effect of financial management practices on the company's performance that there was an overall positive effect on performance with working capital management due to its ability to enable the dairy companies to be able to readily operationalize its activities having the highest influence on quality of the firms' financial performance.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Introduction

This objective of the study was to determine the relationship between financial management practices and financial performance of companies in the dairy industry. This chapter is a recap of the discussions and findings drawn from the previous chapters. Significant findings are summarized, conclusions drawn, recommendations made to policy makers in addition to further recommendations on opportunities for further research.

5.2 Summary of Findings

Financial management is more than keeping accounting records. It is an essential part of organizational management and cannot be seen as a separate task to be left to finance staff or the honorary treasurer. A good financial management involves planning, organizing, controlling and monitoring resources so that your organization can achieve its objectives and fulfill its commitments to beneficiaries, donors and other stakeholders. Successfully managing financial resources is important in new as well as expanding businesses, so time should be taken to develop and implement financial plans that will ensure the success of any organization.

From the findings, the study found that without the financial management practices, the dairy industry company financial performance would be dismal if all other factors are held constant further the study also found that on average, companies in the dairy sector embrace various financial management practices that enables them attend to their financial management issues. . These according to a majority of the respondents were shown to include financial reporting

analysis as well as non – current assets management practices. Others include capital structure management and working capital management practices with each of these financial management practices scoring highly on elements of the respondents’ perception of their use by the dairy companies

Finally, results of regression analysis found that showed that the dairy companies’ overall financial performance was positively affected by the financial management practices. The findings specifically showed that financial reporting analysis and working capital management practices each had a significant positive effect on the company’s financial performance with working capital management practice being a higher contributor to the effect. Non – current assets management and capital structure management as financial management practices were found to each have a significant negative influence on the dairy companies’ financial performance

5.3 Conclusions for the Study

The study sought to determine the relationship between financial management practices and financial performance of dairy companies in Kenya. A sample of 14 companies was studied using across sectional research design. A research questionnaire was developed and distributed to the dairy processors to gather the data on the financial management practices. Based on data gathered from the respondents the following conclusions were realized on the financial management practices. Using regression analysis, the study concluded that financial reporting analysis and working capital management practices each had a significant positive effect on the company’s financial performance while . Non – current assets management and capital structure

management as financial management practices were found to each have a significant negative influence on the dairy companies' financial performance

The financial statements preparation of some companies were not as per the financial management standers for statement for financial position, Statement of Activities, Statement of Functional Expenses and Statement of Cash Flow to indicate the financial position as whole, It was further found that most dairy companies were found to have put in place robust financial management practices in the form of financial report analysis, non – current assets management, capital structure management and working capital management practices.

There are gaps on timely financial reports submission and availing of the monthly financial statement, the researcher observed that many companies maintain optimal cash balances at all times to enable them meet their daily needs .Finally it can be concluded that not all the financial management practices that are employed would give raise to the financial performance in all the industries regardless the nature of the business activity

5.4 Policy Recommendations

In the light of the above, the researcher would like to suggest to owner/managers that the careful management of working capital is vital for the survival of their firms. Poor management of working capital means that funds are unnecessarily tied up in idle assets hence reducing liquidity and also reducing the ability to invest in productive assets such as plant and machinery, so affecting financial performance.

The owner/managers of dairy processing companies should do the following if they want to make better use of good financial management practices, first to be competent and fulfill government requirements the organization must prepare financial statement and reports as per acceptable standards like preparation of statement of financial position, Statement of Activities, Statement of Functional Expenses and Statement of Cash Flow to indicate the financial position as whole, secondly Proper Cash forecast preparation is highly important for smooth implementation of activities as planned. Cash forecast document is required for availing the required cash for activities implementation. Thus it is required to avoid activities implementation delay due to shortage of cash at the right time.

Thirdly Financial and activities reports should be submitted to the concerned government body and timely also the financial information shall relate with the activities performed, that expenses report shall indicate the activities performed using those resources. Financial reports to be reconciled and linked with physical progress. Hence, establishment of financial management system linking the activities report with the activities performance and finally Dairy companies should enhance the process of preparation and publication of the company's financial statements, improve the company's capital structure and ensure that the companies fully utilize their debt facility according to their capabilities

5.5 Limitation of the study

Due to time and resource constraints the findings and conclusions of this study are limited on the Basis of the factors discussed below.

The population of the study consisted of 54 dairy processors providers that are spread across the Country. The researcher was however capable of collecting data from a sample of 15 dairy processors, which was 25 % of the population.

The second source of the study limitation is the data source. Primary data was collected with the help of structured questionnaires where respondents were asked the extent to which they agree with the financial management practice adopted by the dairy processors. Clearly the findings of this study are affected by the personal biases of the respondents.

The research design adopted was a cross-sectional design which covered the financial year 2012/2014. The results of this study therefore are limited to the period of study.

The study adopted a regression model to determine the relationship between financial management practices and financial performance of dairy processing firms. The researcher acknowledges that there could be other better models to be used in the study

5.6 Suggestion for Further Study

In this study, cross-sectional research design was used in which data on financial management practices was collecting only for the current year and compared with the financial performance of the financial year 2012/2014. The researcher suggests that further research be done using longitudinal research design so that the relationship is tested in a period of more than one year.

This study sampled a total of 15 dairy companies. The population of study is 54 dairy processors. The researcher recommends that the same study be repeated but this time all the dairy processors should be included in the study.

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ANNEXES

(I) List of Licensed Processors

Processor	location
1 KCC	Nationwide
1 Brookside	Thika
2 Premier Dairy	Kericho
3 Spin Knit Dairy Div	Nakuru/Nairobi
4 Meru Central Dairy	Meru
5 Limuru Milk Processors	Kiambu
6 Kilifi Plantation	Kilifi
7 Lelkina Dairy	Molo/Nakuru
8 Aberdare Creameries	North Kinangop
9 Donyo Lessos	Eldoret
10 Delamere	Naivasha
11 Nyota Dairy	Kitale/Trans-Nzoia
12 Kenya Milk Products	Nakuru
13 Ilara Dairy	Rongai/Nakuru
14 Sotik Dairy	Kericho
15 Guilford Institute	Njoro
16 Eldoville Farm	Nairobi
17 Chesumot	Kericho
18 Happy Cow	Nairobi
19 Palm House Dairy	Kiambu
20 Unigate Dairy	Nairobi
21 Echuka Farm	Kiambu
22 Eldairy Products Ltd	Eldoret
23 Teita Estate	Mwatate
24 Solai Mawa Factory	Solai/Nakuru
25 Aberdare Cheese	Naivasha
26 Sunpower Products	Kiambu

- | | | |
|----|--|----------|
| 27 | Bio – Foods | Nairobi |
| 28 | Stanley & Sons Ltd | Machakos |
| 29 | Kiambaa Dairy | Kiambu |
| 30 | Farmfresh Nairobi | |
| 31 | Danoma Ltd Mombasa | |
| 32 | Supa Duka Nakuru | |
| 33 | Crystal Dairy Kikuyu | |
| 34 | New Kenya Cremeries | |
| 35 | Buzeki Dairies | |
| 36 | Githunguri Dairy Farmers Cooperative Society (Fresha), | |
| 37 | Sameer Agriculture and Livestock Ltd | |
| 38 | Pamside dairies | |

Source: Kenya Dairy Board

(ii) Questionnaire

SECTION A: GENERAL INFORMATION

- 1. Name of the organization
- 2. Category of Organization.....
- 3. Designation of Officer.....
- 4. What percentage of your Budget is Funded by:
 - i. Donors.....
 - ii. Government.....
 - iii. Other(s).....
- 6. For how long have you been in Operation?

SECTION B: FINANCIAL MANAGEMENT PRACTICES

On likert scale of 1-5 where; **1-Strongly Disagree, 2-Disagree, 3-Neither Agree nor Disagree, 4-Agree and 5 Strongly Agree**, mark the extent to which you agree with the following:

**A. Financial Reporting Analysis
(FR (FRA))**

		1	2	3	4	5
1	The financial statements of the company are prepared in line with the financial accounting standards					
2	The financial statements are prepared in accordance with GAAP					
3	The financial statements are published regularly					

B. Fixed (Non-current) Assets Management (FAM)

		1	2	3	4	5
1	The company maintains a non-current assets register					
2	The non-current assets have been tagged					
3	Movement of non-current assets have to be authorized by senior management					
4	Non-current assets count is carried out every year					
5	Capital expenditure on non-current assets must be authorized by senior management					
6.	The repair and maintenance of non-current assets is carried out regularly					

C. Capital Structure Management (CSM)

		1	2	3	4	5
1	The capital structure of the company is appropriate					
2	The company has fully utilized the debt facility according to its capabilities					
3	The company relies on equity capital only					
4	The company is quoted on the NSE					

D. Working Capital Management (WCM)

		1	2	3	4	5
1	The company has a working capital management system					
2	Maintains inventory records which are updated regularly					
3	Optimal cash balances are maintained by the company at all times					
4	Maintains proper records for all payables					
5	Ensures there is sufficient cash flow to meet daily needs					
6	Prepares cash flow forecasts to identify future surpluses and deficits					

E. Return on Assets (ROA)

		1	2	3	4	5
1	The company returns are profitable relative to its assets.					
2	The use of assets by management are efficient					
3	There are adequate company assets					
4	The earnings generate by the company are adequate					
5	The process of acquisition of assets are tied to the companies long term plan					