

EFFECT OF ACCOUNTS PAYABLES MANAGEMENT ON FINANCIAL PERFORMANCE OF MICRO FINANCE INSTITUTIONS IN KENYA

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Abstract: Since the first institution was granted a license by the Central Bank of Kenya in 2009, the majority of microfinance institutions in Kenya have experienced losses. For example, the total loss before tax for the microfinance institutions indicated a general drop in performance. Reduction in financial income was a major factor in the profitability sector's collapse. The industry recorded a lower return on equity ratio and return on assets due to a fall in performance. Therefore, this study sought to investigate the effect of accounts payables on financial performance of Micro Finance Institutions in Kenya. A descriptive research design was adopted in the study. The 13 microfinance institutions in Kenya as of December 31, 2019, as listed on the Central Bank of Kenya website, comprised the study's population. We conducted a census with thirteen MFIs. Using secondary data collection sheets, the study examined data from published financial statements and annual reports covering the previous five years, from 2018 to 2022. The financial performance of Micro Institution was assessed using Return on Assets (ROA). A descriptive statistical analysis, utilizing the mean and standard deviation, was performed on the quantitative data received from the study. In order to determine how much each variable influences the others, the study also used inferential statistics, specifically correlation and multiple regression analysis. Tables were used to display the data. The study discovered a relationship between Kenyan Microfinance Institutions' financial success and their management of accounts payable. According to the study's findings, MFIs prioritized highlighting the benefits that a product or service can offer the consumer, which resulted in a more consultative sales approach. According to the study, MFIs should process map their accounts payable to enable prompt identification of any inefficiencies or bottlenecks.

Keywords: Accounts Payables Management, Financial Performance.

1. INTRODUCTION

A number of operational changes have been made to Kenya's financial institutions, including privatization, market expansion to attract additional investors, and financial sector liberalization aimed at increasing investment and savings rates and enhancing the institutions' financial performance (Holland, 2019). Tarashev, Borio, and Tsatsaronis (2020) state that because the financial market is characterized by stringent regulation, the focus of the stakeholders in the financial sector has been on the need to open up the financial system in order to increase the profitability and operational effectiveness of the financial institution. Therefore, the government, regulatory agencies, financial intermediaries, and financial market systems must take the lead in financial institution deepening in order to increase the provision of financial services.

According to Machiuka (2018), the examination of financial performance takes into account the firm's financial situation, the degree of sector rivalry, and a thorough grasp of its cost and profit centers. According to Harker and Zenios (2021), a

company's working capital performance provides valuable insight into its financial status. The availability of a company's working capital is one of the first things a lender or investor will look at on a balance sheet because it is a crucial sign of financial health. Thus, the goals of working capital management are to keep things running smoothly, improve productivity, and raise sales and profits for the company.

The effective handling of a business's working capital has an impact on its bottom line. In this case, efficient working capital management seeks to optimize shareholder wealth, so these businesses maintain an appropriate level of working capital on hand to increase their value (Gill, Biger & Mathur, 2018). Working capital management must be efficient, according to Farris and Hutchison (2021), to satisfy the financial needs of businesses that are expanding quickly. For example, an efficient administration of working capital reduces the operational cycle of any organization that depends on it. Thus, one could argue that it requires more work for a company with a long operational cycle to manage working capital effectively.

In 1987, the Malaysian government introduced a microfinance program as one of the ways to combat poverty in the country. Since then, several organizations have been founded with the intention of helping low-income people start their own small companies with small loans in order to boost their income streams and maintain household consumption (Adejoke, 2020). Malaysian MFIs are struggling, even though a 2021 World Bank study claimed that MFIs in Asian nations are developing faster than those in Eastern Europe. Malaysian MFIs are useless in this sense, according to Mokhtar and Ashhari (2021), because they are totally dependent on government subsidies, local financiers, and donations, which makes them inefficient in terms of self-reliance.

Microfinance institutions (MFIs) in Nigeria are recognized as significant participants in the country's microfinance industry. Funding from microfinance organizations (MFIs) is increasingly acknowledged as an important source of financing for persons with low incomes and those without access to banking or other traditional financial services (Tadele & Rao, 2017). More importantly, Shukran and Rahman (2019) point out that financial services offered by MFIs are viewed as helpful for both helping the impoverished in these countries and eliminating poverty in growing nations like Bangladesh and Nigeria. Due to widespread delinquency, high transaction costs, poor credit quality, loan payback defaults, and managerial errors, the bulk of microfinance institutions in Nigeria have collapsed. Therefore, efficient working capital management is essential to a company's overall financial stability and operational effectiveness.

The intense competition in Kenya's microfinance sector is seen in the fluctuating market share and profitability of this sector. The MFI sector, traditional commercial banks, and telecommunication money transfer platforms are in competition with each other (Okombo, 2018). Ongore and Gemechu (2021) claim that a number of interconnected barriers to the growth of a banking and finance industry in Kenya have been the primary cause of the country's demand for microfinance. Kenyan microfinance banks have also observed intense pricing competition because their financial structure gives them less flexibility to change their rates. Thus, a company's earnings and profitability can be increased by using efficient working capital management, which can also help to keep everything running smoothly.

The primary goal of an organization's working capital management plan is to keep its current assets and liabilities in the right proportion. Apart from assisting businesses in fulfilling their financial commitments, an effective working capital management system boosts their earnings (Filbeck & Krueger, 2018). According to Deloof (2020), working capital needs vary by industry and even within closely similar companies. Contributing factors include the timing of asset purchases, the possibility that a business will write off a portion of its past-due accounts receivable, variations in collection and payment practices, and, in certain situations, capital-raising initiatives a business is pursuing.

The process of efficiently and effectively managing a company's accounts payable in order to maximize cash flow and minimize expenses while guaranteeing that the company's short-term debts are paid on time and in full is known as accounts payable management (Enow & Kamala, 2016). Sedevich-Fons (2020) states that receiving and processing invoices, confirming their accuracy, making sure payments are made within the vendor's specified terms, balancing the accounts payable balance, and keeping accurate records are all common steps in the accounts payable management process. Consequently, by taking advantage of early payment discounts and avoiding late payment costs, efficient accounts payable administration can assist a business in optimizing its cash flow.

Organizations need to have good accounts payable management to make sure that their payables improve cash flow and maintain positive working relationships with their suppliers (Ikechukwu & Nwakaego, 2019). According to Jung, You, Chi, Yu, and Hwang (2021), efficient accounts payable practices help companies manage their cash flow by reducing the

expenses related to late payments, such as penalties, interest charges, lost discounts for on-time payments, and payments made to creditors before debtors' payments are received. Thus, a company with efficient, streamlined accounts payable operations eventually saves money by getting rid of these fees and lowering the processing costs for supplier bills, all of which enhance cash flows.

A company's financial performance can be used to measure the financial outcomes of its activities and decisions. The business's return on investment, return on assets, and shareholder value all reflect these outcomes, accounting profitability, and its constituent parts (Sidra & Attiya, 2017). According to Adams, Thornton, and Sepehri (2019), decision-makers can evaluate the results of business strategies and efforts just in terms of money by evaluating a company's financial success. Therefore, measuring financial performance serves as an indicator of how successfully a corporation uses resources from its primary operation to turn a profit.

A few NGOs established pilot programs offering donor-funded lending services in the late 1960s, marking the beginning of the Kenyan microfinance industry. Over time, a few of these groups have transformed into highly profitable, self-sustaining, and commercialized establishments. As of December 2015, there were 49 MFIs registered in Nairobi County. These included development institutions, wholesale and retail MFIs, commercial banks offering microfinance services, microfinance institutions, and SACCOs. The majority of these microfinance organizations are based in Nairobi, with more than 750 locations, a US\$ 63.64 billion loan portfolio, 1.1 million institution savers, and 350,000 borrowers (Microfinance Bulletin, 2019).

Kenya's microfinance sector is made up of a variety of rival institutions that differ in size, formality, professionalism, visibility, and commercial orientation in addition to their geographical reach. Commercial banks, development finance organizations like the Agricultural Finance Corporation (AFC) and the Kenya Post Office Savings Bank (KPOSB), deposit-taking microfinance institutions, and a number of non-deposit-taking microfinance institutions are among the organizations that are registered, regulated, and/or supervised under various laws. Microfinance organizations offer a broad array of financial services to low-income people and small businesses in both rural and urban areas. These services include money transfer, microinsurance, savings and credit facilities, and money transfer.

2. STATEMENT OF THE PROBLEM

The goal of efficient working capital management is to make sure that the company's current assets and current liabilities are utilized as efficiently as possible in order to maximize profits (Deloof, 2017). According to Harris (2019), working capital components are interconnected, and a firm's level of profitability is largely determined by how well they are managed. Since the first institution was granted a license by the Central Bank of Kenya in 2009, the majority of microfinance institutions in Kenya have experienced losses. For example, for the year ending December 31, 2017, the microfinance institutions recorded a combined loss before tax of Ksh. 622 million due to an overall deterioration in performance. ROE dropped to -5.5 percent and ROA to -0.9 percent in 2017. When they made a tiny recovery to ROA of -0.4 percent and ROE of -3 percent in 2019 before sharply declining to ROA of -3 percent and ROE of -28 percent in 2020, it got worse in 2018, when ROA was -2 percent and ROE was -13.8 percent (CBK, 2021). The industry reported a poorer return on assets and equity ratio—negative 0.9 percent and negative 5.5 percent, respectively—than it did three and a half years ago due to a deterioration in performance.

3. LITERATURE REVIEW

Theoretical Literature Review

The father of modern macroeconomics, John Maynard Keynes, developed the liquidity preference theory of interest, which he published in his 1936 book *The General Theory of Employment, Interest, and Money*. In order to explain why longer-term investments are associated with higher interest rates, the theory focuses on three key factors: the interest rate, liquidity preferences, and the quantity or supply of money. Keynes (1936) demonstrated that, in monetary production economies, money or liquidity is more essential for economic activity than saving, and that the need for liquidity influences the interest rate. Furthermore, Keynes (1936) described three motives in relation to the liquidity preference model.

According to Modigliani (2016), investors who favor cash or other highly liquid assets over securities with long-term maturities and higher risk should anticipate a higher interest rate or premium. The liquidity preference theory is the name given to this. Everyone agrees that the most liquid asset is cash. Interest rates on short-term securities are lower because, in

accordance with the liquidity preference theory, investors do not forfeit liquidity for longer periods of time when buying short-term assets as opposed to medium- or long-term securities. The theory clarifies the rationale behind the various ways used in cash management, allowing the study to determine how these approaches have been applied by the various organizations and how this has affected their financial performance.

Empirical Literature Review

The study conducted by Nwakaego and Ikechukwu (2016) investigated the impact of accounts payable management on the financial outcomes of Nigerian domestic and industrial manufacturing enterprises. The companies' annual reports, which served as the source of the data, were examined. The multiple regression technique was employed to test the hypotheses. The profitability ratio was positively and significantly impacted by accounts receivable at the 1% significance level, according to the results. Therefore, the profitability ratios of Nigerian paint and building/chemical companies will rise proportionately with a unit increase in the variables. Both the debt ratio and the sales growth rate had negative but negligible effects on these organizations.

The study conducted by Likalama and Kirwa (2017) examined the management of accounts payable as a factor influencing the profitability of agro-firms located in the Eldoret Business Center. A descriptive survey design was used in the study, and 510 respondents were the target population. A questionnaire was utilized to gather data, while 214 other employees were sampled at random and 51 managers were selected using the purposeful sampling technique. For the data analysis, both descriptive and inferential statistics were used. The study found that an agricultural firm's profitability can be predicted by its accounts payable management.

The impact of accounts payable administration procedures on the liquidity of public technical training institutes in the Rift Valley Region of Kenya was investigated by Mutai and Kimani's (2019) study. In this study, a descriptive research design was adopted. According to the Technical and Vocational Education and Training (TVETA) list from August 2017, the target population consisted of principals and accountants of public technical training institutes in Kenya. Census survey method was employed in this investigation. In this study, primary and secondary data were also employed. The study used both descriptive and inferential statistics, including product moment correlation analysis and multiple regression. The results of the study showed that the Rift Valley Region's public technical training institutions' liquidity was significantly impacted by their accounts payable management techniques.

4. RESEARCH METHODOLOGY

A descriptive research design was adopted in the study. The 13 microfinance institutions in Kenya as of December 31, 2019, as listed on the Central Bank of Kenya website, comprised the study's population. We conducted a census with thirteen MFIs. The research employed a secondary data collection sheet that comprised document assessments of data from publicly available financial statements and annual reports covering the previous five years, from 2018 to 2022. Return on Assets (ROA) was used to gauge the financial performance of Micro Institutions. The quantitative data from the study were analyzed using mean and standard deviation as well as descriptive statistical analysis. To determine how much each variable influences the others, the study also used inferential statistics, such as multiple regression analysis and correlation analysis. Tables were used to present the results.

5. FINDINGS

The descriptive statistics results of accounts payables management are presented in Table 1.

Table 1: Accounts Payables Management

	Minimum	Maximum	Mean	Standard deviation
Accounts Payable days	0.0128	0.5315	4.592	0.2674
Value of item sale	0.1571	0.6450	6.934	0.4186

The accounts payable days had a mean of 4.592 and a standard deviation of 0.2674, according to the results shown in Table 1. Additionally, the results show that the accounts payable days had a minimum value of 0.0128 and a maximum value of 0.5315. This suggests that MFIs had a low number of accounts payable days. According to Enow and Kamala (2020), a decrease in accounts payable indicates that the company is quickly clearing its outstanding debts with suppliers. As a result, it can be seen from Table 1's statistics that the number of days for accounts payable was high. This suggests that MFIs are

quickly clearing their outstanding debts to suppliers. Maintaining liquidity within a company's daily operations is the most important issue in accounts payable management, according to Enow and Kamala (2020). This is because it helps prevent suppliers and creditors whose claims are due soon from putting undue pressure on management. The results also corroborate the findings of a 2017 study by Likalama and Kirwa that examined the management of accounts payable as a factor in agro-firm profitability at Eldoret Business Center. The study found that an agricultural firm's profitability can be predicted by its accounts payable management.

The value of item sale had a mean score of 6.934 and a standard deviation of 0.4186, according to the data as shown in Table 1. The results also show that the item sale's minimum and maximum values were, respectively, 0.1571, and 0.6450. This suggests that the MFIs prioritized highlighting the benefits that a product or service can offer the consumer, which resulted in a more consultative sales procedure. As a result, the MFIs' sales staff were better equipped to comprehend their clients' demands and make more precise offers. The results are consistent with Sinha and Verma's (2020) observation that a sales team can attain remarkable outcomes by implementing a negotiation method that centers around the advantages of the offer to the prospective client. The results are consistent with a study conducted in 2016 by Nwakaego and Ikechukwu, which looked at how accounts payable administration affected the financial performance of Nigerian domestic and industrial manufacturing firms. The profitability ratio was positively and significantly impacted by accounts receivable at the 1% significance level, according to the data.

6. RESULTS OF INFERENTIAL STATISTICS

Correlation analysis

Table 2: Correlation Analysis

		Operational cost	Financial performance
Accounts payables management	Pearson Correlation	1	
	Sig. (2-tailed)		
Financial performance	Pearson Correlation	.774**	1
	Sig. (2-tailed)	.000	
	N	13	13

The management of accounts payables had a 0.774 Pearson r value and a significance value of 0.000, or less than 0.05, in relation to financial performance. This is a substantial correlation between the financial performance of Kenyan microfinance institutions and the management of accounts payable.

Results of Regression Analysis

Table 3: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.669	.785	.776	1.254

According to Table 3's findings, the adjusted R square value was 0.776, or 76.6%, indicating how much the administration of accounts payable influenced the financial performance of Micro Finance Institutions in Kenya. Thus, other variables not examined are accounted for by the remaining percentage (23.4%).

Table 4: Analysis of Variance

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	112.017	1	112.017	132.17	.000
	Residual	9.321	11	.847		
	Total	121.107	12			

Table 4 presents the findings, which indicate that at 0.000, the significance value is less than 0.05. Furthermore, the statistical F value is higher—132.17—than the statistical mean—112.017. Consequently, this indicates that the model was significant.

Table 5: Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	.704	.218		3.229	.000
Accounts payables management	.812	.336	4.130	2.417	.001

The findings in Table 5 revealed that a constant value at 0.704 represents the amount by which the financial performance of Micro Finance Institutions in Kenya would be when accounts payables management is kept constant.

The established regression equation was as follows;

$$\text{Financial performance} = 0.704 + 0.812 (\text{accounts payables management})$$

Table 5's findings further demonstrate that the management of accounts payable had a positive t-value of 2.417 and a significant value of 0.001. Thus, the financial performance of Kenya's Micro Finance Institutions was significantly improved by the management of accounts payable. The study concluded that accounts payables management had a significant impact on the financial performance of Micro Finance Institutions in Kenya, thereby rejecting the hypothesis.

7. CONCLUSIONS

The study concludes that by emphasizing the benefits that a product or service can provide to the consumer, MFIs were able to encourage a more consultative sales approach. Because of this, the MFIs' sales teams were more equipped to comprehend their clients' demands and tailor their offerings accordingly. One of the crucial business procedures that aids in efficiently managing the entity's financial responsibilities is accounts payable management. Maintaining the so-called solid credit and enduring relationships with the vendors are made possible by the accounts payable management. The administration of accounts payable is in charge of making sure that payments are made on time in order to prevent late fees, penalties, and other costs.

8. RECOMMENDATIONS

The study recommends that in order to promptly detect any inefficiencies or bottlenecks, the MFIs should draw out your accounts payable procedure. Improve their accounts payable process by breaking down overly complicated workflows to identify areas that are overly complex. Lower the likelihood of data entry errors since even tiny mistakes can mount up, resulting in time and money lost for the organization in correcting the inaccuracies or handling the aftermath. Automate the process of verifying invoices in accordance with the policies and procedures of the institution to resolve purchase-related concerns.

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