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RESEARCH ARTICLE

THE ROLE OF BUDGET CONTROL PRACTICES ON PERFORMANCE OF COMPANIES: EVIDENCE FROM KISUMU COUNTY, KENYA

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Abstract

The study sought to assess the role of budgetary control practices on performance of manufacturing firms in Kisumu County, Kenya. The study was anchored on finance distress theory. The study adopted correlational research design. The target population was the thirteen (13) manufacturing firms in Kisumu County and a census survey was employed in this study. The primary data was collected by use of questionnaires administered to 36 respondents drawn from produvtion/operations, finance and accounting sections of the manufacturing firms. Pilot study involving three respondents was conducted and analyzed using Cronbach's alpha whose values were all 0.7 and above indicating that the research instrument used is reliable. The data was analyzed using Descriptive and inferential statistics such as frequencies, percentages, mean, standard deviation and multiple regression analysis. The findings of the study were budget control practice had a positive significant effect on performance (B = .466, p= 0.005) indicating that practice of budgetary control leads to increase in performance among manufacturing firms in Kisumu County. The findings from this study may be helpful to policy makers in manufacturing firms and Government in setting policies to govern the operations of manufacturing firms in Kenya; shareholders in making investment decisions that maximise wealth and academicians may find results from this study useful in forming a basis for future theory development in the fields of financial control practices and performance.

Introduction:-

Globally, the performance of manufacturing firms has been improving steadily with time as shown by the increase in Gross Domestic Product which is approximated $2.1 trillion in GDP (12.5 percent of total U.S. gross domestic product) and the sector supports approximately 17.1 million indirect jobs in the United States, in addition to the 12.0 million persons directly employed in manufacturing, for a total of 29.1 million jobs directly and indirectly supported, more than one-fifth (21.3 percent) of total U.S. employment in 2019 (Bureau of Economic Analysis, 2019). This increase is attributed to the ever-increasing need for consumer goods churned out of these manufacturing firms (Bureau of Economic Analysis, 2019).

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Locally, industry's contribution to the national gross domestic product (GDP) has stagnated at approximately 5.5 percent in the period from 2003 to 2017. In 2019 this figure fell to 3.8 percent. The decline was attributed to the general slowdown in the world economy, post-election violence in the country, the devaluation of the Kenyan shilling, and low productivity and high production costs. The profits realized from manufacturing and allied sector has been declining for several years from 1980 to 2019. Profits in the Kenyan manufacturing sector have been declining over time and this has been due to less capital available for investment (Orege, 2019).

Budgeting control is becoming indispensable in both private and public sectors in modern world because of evolving complex methods of doing business involving technology, and increased size of business units. Budgeting control forms a very vital part of any financial system. They require that resources of any organization are used effectively and properly in order to have accurate reports of activities (Laudon & Laudon, 2016). However, poor or ineffective budgeting control put resources at risk where there are inefficiencies or theft, abuse or fraud. It is therefore the responsibility of the management to ensure proper and effective financial controls are in existence. The responsibility also lays on management to ensure that these controls are effectively operated (Prempeh, Twumasi & Kyeremeh, 2015). Many organizations consider budgetary control as the base for financial control gives a wide management platform and lead to effective resource allocation. It contributes in management of assets and better allocation of resources which generates more income. The main objectives of budgetary control include combining ideas from the various levels of management in the budget control process, coordinating various activities in the firm, revealing areas of weakness and planning and controlling a firm’s income and expenditure to achieve organizational goals. In many profitable companies, budget is actually a key to their success (Horngren et. al., 2012).

Theoretically, the finance distress theory has been used to explain the importance of budgetary control practice and performance. This theory proposes that firms enter into financial distress as a result of poor management of risks and economic distress and this affects their performance (Whitaker, 1999), When performance deteriorates to the point where a firm cannot meet its financial obligation, the firm is said to have entered the state of financial distress. The first signals of financial distress are violations of debt payments and failure or reduction of dividends payouts and this affects performance (Wruck, 1990). Firms experience financial distress due to poor managerial policies, inefficient and ineffective internal control systems, non-disclosure of financial information and inability to recognize stakeholder rights (Boritz, 1991). This theory seeks to identify the choices of practices that may help a firm improve its performance in respect to financial control and specifically budgetary control. It helps to analyze the relationship between budgetary control and performance of manufacturing firms in Kisumu County, Kenya.

Globally, there have been a number of studies that have documented the importance of financial control and the general inadequacy of financial controls in organizations in United Stated of America. The collapse of Enron in United States of America has been as a consequence of breakdown of financial control (Balakrishnan, Danninger, Elekdag & Tytell, 2011). The company's collapse resulted from the disclosure that it had reported false profits; using accounting methods that failed to follow generally accepted accounting principles (GAAP). The American International Group’s (AIG) auditors, PricewaterhouseCoopers, concluded that the company's financial controls over financial reporting were deficient. AIG lnc. had been under investigation over alleged suspicious transactions that regulators said were used by the insurer to massage its finances (Mulford & Comiskey, 2011).

In Africa, countries have also suffered from the wrath of financial control which has affected performance of public and private organizations. In African economies, listed companies have also witnessed several cases of collapses, some of which include the Intercontinental Bank Plc, Oceanic Bank Plc, Platimum Habib Bank Plc, Anglo-African textile industry, Steel rolling Nigeria limited, Nigeria wire and cable (all in Nigeria). In Nigeria, financial controls aspect that is been advocated by the investors and academic scholars is the audit controls and budgetary controls (Omar & Simon, 2011).

Despite the importance of budgetary control on performance of manufacturing firms, it has received little attention for scholarly and practical implications. Studies focusing on budgetary controls have not targeted manufacturing firms. Chelagat and Akama (2016) examined financial control practices in community based organizations. Chebet, Nyangua and Nyabonga (2018) assess the effect of financial control on Profitability of SACCOs in Kericho County. On the other hand, studies on manufacturing companies have concentrated on internal control system. Mwakimasinde, Odhiambo and Byaruhanga (2014) analyzed the effect of internal control systems on the profitability of sugarcane out grower companies in Kenya. Ngetich (2017) examined effect of internal control on profitability of firms listed at NSE .These studies did not cover budgetary control therefore; the current study sought to assess budgetary control practices and performance of manufacturing firms in Kisumu County, Kenya.

Kisumu County has several light industries; these include beverages, textiles, molasses, fish processing plants and agricultural produce processors. Kisumu County has 13 manufacturing firms that include; United Millers, Equator Bottlers, Ndugu Transport Company, Muhoroni Sugar, Chemilil Sugar, Jubilee Jumbo Hardware, Kibos Allied Sugar, Spectre International, Agrochemical, Mayfair Holdings, Mayfair Holdings, Kisumu Concrete Products and Tuff Foam among others. These firms all are multi-billion shilling companies and they are also Kisumu largest employers.

Theoretical Review
Finance Distress Theory
This theory was proposed by Baldwin and Scott (1983). This theory postulates that firms enter into financial distress as a result of poor financial control mechanisms, management of risks and economic distress which affects their performance. When performance deteriorates to the point where a firm cannot meet its financial obligation, the firm is said to have entered the state of financial distress. The first signals of financial distress are violations of debt payments and failure or reduction of dividends payouts hence affecting performance. According to the theory therefore, if firms institute internal control mechanisms, their performance is likely to improve. This theory seeks to identify the choices of practices that may help a firm improve its performance in respect to financial control and specifically asset control, audit control and budgetary control. From the theory of finance distress, budgetary control and performance were linked as shown in the figure below. In the Figure, the independent variable is budgetary control practices which has four constructs namely budgetary estimates, budgetary planning process, budgetary allocations and expenditures and timely budget approvals whereas the dependent variable is performance with three constructs: revenue turnover, sales volume and net profit growth. In this study, it was hypothesized that budgetary control affects performance of manufacturing firms. In addition, asset and audit control practices are incorporated as control variables.

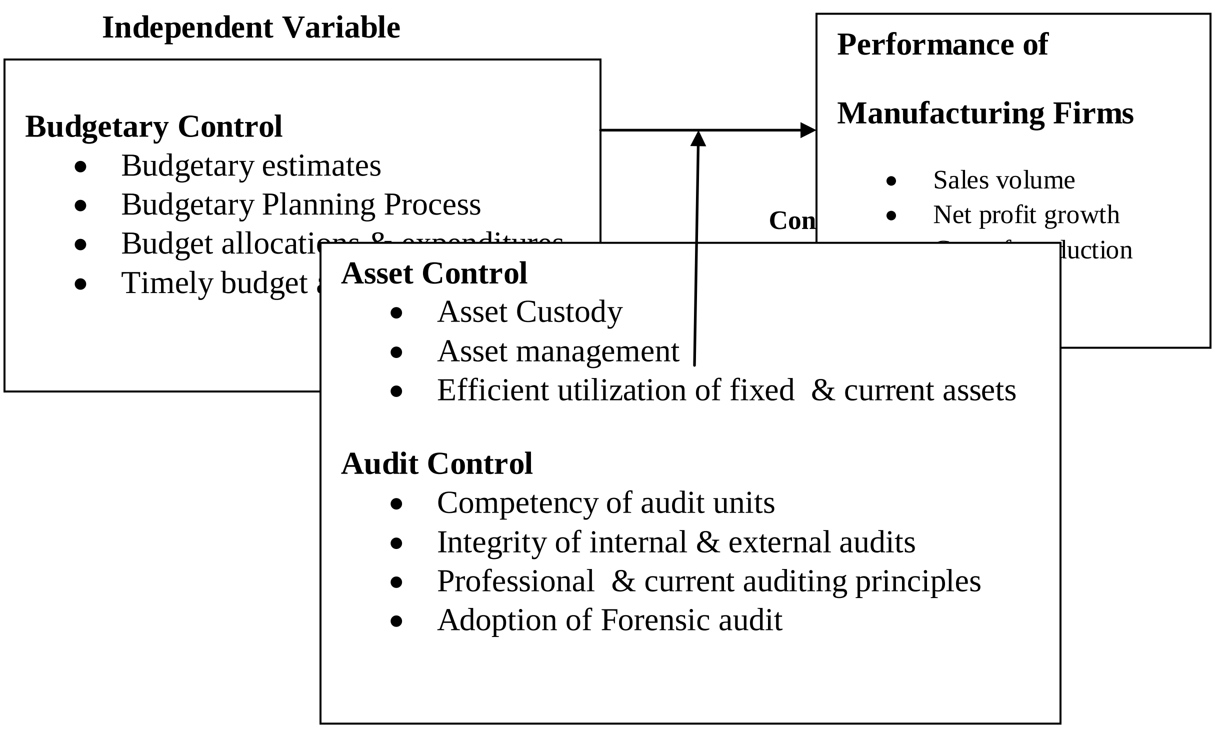

Figure 1.1:- Budgetary Control practices and performance relationship.
Source: Adapted from Wanyama et al (2019)

Empirical Literature Review:-

Prior studies have mainly concentrated on effect of internal checks and systems on performance notably Abdi (2015); Munene (2013), Origa (2016), Mawanda (2008); Njonde and Kimanzi (2014) focused on and Rono (2016). Whereas Rono (2016) investigated the effectiveness of the internal control system in the management of finances in public universities; Njonde and Kimanzi (2014) focused on integrated financial management information system (IFMIS) on performance of Kenya's public sector using explanatory research design. On the other hand, Abdi (2015) and Origa (2016) using descriptive research design found that embracing effective internal control practices had enhanced performance as compared to non-application of effective internal control practices. Ismailjee (2013) evaluated the financial controls namely control activities, the cash receipts and disbursements of the transport services in Nairobi using a descriptive survey design. On the contrary, only a few studies focused on budgetary control as practice in relation to performance among cement and beverage manufacturing firms (Chircir and Simiyu, 2017 and Nafisatu, 2018) using a case study design. However, none of these studies assessed the role of budgetary ontrol practices on performance of manufacturing companies in Kisumu County, Kenya.

Research Methodology:-

This study used a correlation research design to investigate relationships between variables without the researcher controlling or manipulating any of them. A correlation reflects the strength and or direction of the relationship between two (or more) variables. The study conducted an analysis of the 13 manufacturing companies that are in Kisumu County, registered under Kenya Association Manufacturers (KAM). This scientific research method involved the collection and analysis of data to describe a phenomenal in its current conditions or to the state. The target respondents for this study were finance, accounts, operations and production managers of 13 manufacturing companies in Kisumu County and census survey was employed in this study.

In order to test the reliability of the instruments, internal consistency techniques was involving three (3) respondents drawn from one manufacturing company. The respondents involved in the pre-test study were not included in the main study. Cronbach's Alpha was used to analyze the pre-test study output. Nunnally (1978) argued that a Cronbach's alpha value of 0.7 and above proves that the research instrument used is reliable. This study adopted a coefficient of 0.7 as the benchmark for reliability.

Table 3.1:- Cronbach's Alpha Reliability test results.

Construct	Number of items	Reliability coefficient
Asset control practice	4	0.847
Audit control practice	4	0.870
Budget control practice	4	0.808
Performance	4	0.741

Source: Survey Data (2022) n = 3

Model Specification

The regression model is derived from the linear equation, and the following equation was used;

$Y_i = \beta_0 + \beta_1 X_{1i} + \beta_2 X_{2i} + \beta_3 X_{3i} + \varepsilon$

Where;

Y= Performance,

i= Respondents

β_0= Constant Term,

$\beta_1, \beta_2, \beta_3$= Beta coefficients,

X_1 = Asset control Practice ,

X_2 = Audit control Practice,

X_3 = Budgetary control practice,

ε = Error term.

Results` And Discussions:-

Table 4.1:- Descriptive Statistics on Budgeting Control Practice elements.

Audit Control Practice	**S.A**		**A**		**N**		**D**		**S.D**			
											M	**Std. D**
Collaborative budget making processing	3	(8.3%)	2(5.6%)	6	(16.7%)		11	(30.6%)	14	(38.9%)	2.14	1.24
Budgetary estimates are in line with the company's needs	12	(33.3%)	15(41.7%)	3	(8.3%)		3	(8.3%)	3	(8.3%)	3.833	1.23
Timely approval of all budget estimates The budget allocations match company expenditures	1 9	(2.8%) (25.0%)	3(8.3%) 6(16.7%)	7	(19.4%) 9(25.0%)		5 9	(13.9%) (25.0%)	20 3	(55.6%) (8.3%)	1.89 3.25	1.166 1.317
Overall Mean score = 3.000, n= 36												

Source: Survey Data (2022)

1-Strongly disagree, 2-Disagree, 3- Neutral, 4-Agree, 5-Strongly Agree

Table 4.1 shows the overall mean is 3.00 indicating that respondents did not either agree or disagree on the manufacturing firms embracing collaborative budget making process, preparing budgetary estimates that are in line with company's financial needs, timely approval of all budget estimates and matching budget allocations with the company expenditures.

Table 4.2:- Descriptive Statistics on Performance elements.

Performance elements	**S.A**		**A**		**N**		**D**		**S.D**			
											M	**Std. D**
Sales volume improved over the last five years	13	(36.1%)	15(41.7%)	2	(5.6%)		2	(5.6%)	4	(11.1%)	3.86	1.29
Net profit has been declining over the last five years	3	(8.3%)	4(11.1%)	4	(11.1%)		8	(22.2%)	17	(47.2%)	2.11	1.348
Revenue	1	(33.3%	8(22.2%)		(22.2%		5	(13.9%		(8.3%)	3.58	1.31

turnover` has been increasing over the last five years The cost of production has been declining in the last five years	2 1	) (2.8%)	2(5.6%)	8	) 4(11.1%)		1 0	) (27.8%)	3 19	(52.8%)	1.77 8	7 1.04 5
Overall Mean score = 3.000, n= 36												

Source: Survey Data (2022)

1-Strongly disagree, 2-Disagree, 3- Neutral, 4-Agree, 5-Strongly Agree

Table 4.2 shows the overall mean is 3.00 indicating that respondents did not either agree or disagree on the manufacturing firms' sales volume, revenue turnover increasing over the last five years. In addition, they did not agree or disagree that net profit and cost of production have been declining in the last five years.

Budgetary Control Practice and Performance of manufacturing firms

To achieve the study objective, multiple regression analysis whose results are summarized in Tables 4.9, 4.10 and 4.11.

Table 4.3:- Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.546[a]	.298	.232	1.13126	.298	4.520	3	32	.009	.461
a. Predictors: (Constant), Asset Control, Audit Control, Budgetary control										
b. Dependent Variable: Mean Performance										

Table 4.4:- ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	17.354	3	5.785	4.520	.009[b]
	Residual	40.952	32	1.280		
	Total	58.306	35			
a. Dependent Variable: Mean Performance						
b. Predictors: (Constant), Asset Control, Audit Control, Budgetary control						

Table 4.5:- Multiple Regression Analysis Coefficients[a]

Model		**Unstandardized Coefficients**		**Standardized Coefficients**	**t**	**Sig.**
		B	**Std. Error**	**Beta**		
1	(Constant)	5.253	.959		5.478	.000
	Asset Control Practice	-.228	.138	-.247	-1.648	.109

`	Audit Control Practice	-.393	.198	-.295	-1.981	.056
	Budgetary Control Practice	.466	.156	.450	2.990	.005
a. Dependent Variable: Mean Performance						

The fitted model is as follows:

$$\mathbf{Y = 5.253 - .228X_1 - .393X_2 + .466X_3}$$

The results in Table 4.5 indicate that budgetary control practice significantly positively affects performance of manufacturing firms in Kisumu County (B = .466, p= 0.005) implying that practice of budgetary control leads to increase in performance among manufacturing firms in Kisumu County. The results of the study are congruent with those of Chirchir and Simiyu (2017) and Nafisatu (2018) who found a positive relationship between budgetary control and performance among cement and beverage manufacturing firms. However, the finding are at variance with those of Abdi (2015); Munene (2013), Origa (2016), Mawanda (2008); Njonde and Kimanzi (2014) who reported that budgetary control had a negative effect on performance. In the same vein, Ismailjee (2013) evaluated the financial controls namely control activities, the cash receipts and disbursements of the transport services in Nairobi and reported a positive relationship between the variables.

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