THE EFFECT OF WORKING CAPITAL MANAGEMENT ON PROFITABILITY OF SMALL AND MEDIUM-SIZED ENTERPRISES IN NAIROBI, KENYA

BY

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UNITED STATES INTERNATIONAL UNIVERSITY-AFRICA

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STUDENT’S DECLARATION

I, the undersigned, declare that this is my original work and has not been submitted to any other college, institution or university other than the United States International University in Nairobi for academic credit.

Signed: ______________________________ Date: ______________________________

Ayub Hussein Nunow (ID 635115)

This project report has been presented for examination with my approval as the appointed supervisor.

Signed: ______________________________ Date: ______________________________

Mr., Kepha Oyaro

Signed: ______________________________ Date: ______________________________

Dean, Chandaria School of Business
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ABSTRACT

The main purpose of this study was to examine the effects of working capital management on profitability in small and medium sized enterprises in Nairobi. In order to realize this, four research questions guided the process. These were i) how does accounts receivables put an effect on the profitability of small and medium-sized enterprises in Nairobi? ii) how does inventory holding period put an effect on the profitability of small and medium-sized enterprises in Nairobi? iii) what is the effect of accounts payable on small and medium-enterprises profitability in Nairobi? Iv) what is the effect of cash conversion cycle on small and medium-enterprises profitability in Nairobi? To realize this, a descriptive research design was adopted.

The total population of this study comprised of all registered small and medium sized enterprises in Nairobi with the Federation of Small and micro enterprises estimated at one thousand six hundred from which using a stratified random sampling a sample size of one hundred and sixty. Data was collected using structured questionnaire with the assistance of trained research assistants. Using SPSS a regression analysis was carried out between the dependent variable and all other variables. ANOVA analysis was also carried out to determine the differences in means between the variables.

To analyze the effects of accounts receivables on the profitability SMES the study confirmed that the business screens customers or clients reference before giving credit and it was also revealed that the business enterprise monitors accounts receivables and analyses reports on debtors. A Pearson correlation done between profitability (dependent variable) against other factors of account receivable revealed a positive and significant relationship. To analyze the impacts of inventory holding on the profitability, it was revealed that the business keeps accurate inventory records and also ensures funds are set aside for reorder. From the regression analysis, all the account inventory days of holding variables had a significant positive effect on organizational profitability except if the business keeps accurate inventory records.

To analyze the effects of accounts payable on profitability, the study revealed uncertainty on business sometimes being unable to pay its suppliers on time and if it receives cash discounts from its suppliers upon payment within a stipulated period. The research established that the firms’ regularly budget for the future expenditure, however some issues were not clear and this involved the business having operations related challenges.
due to lack of funds, and whether the availability of cash affects the firm’s profitability. From the regression analysis all variables had a positive relation except if the business has a cash management system and the firm maintains sufficient cash balances for operation.

The study concluded that for effective performance, the firms need to have a well-maintained record of account receivable. The findings of the study reveal that most of SMEs in Nairobi have a well-established credit policy. Inventory holding period is a very important aspect in the cash conversion cycle and most of the SMEs in the Nairobi perform a regular review of its inventory levels, this was also accompanied by the businesses keeping accurate inventory records. The SMEs need to maintain a good relationship with the creditors and from the study it was apparent uncertain on whether the business are able to negotiate for cash discounts from its suppliers upon payment within a stipulated period, or if the business is sometimes charged an interest by its suppliers for late payment. Most of the firms have also apparently taken measures such as maintaining sufficient cash balances for operations and regularly budgeting for the future expenditure.

The study recommend that the firms need to have an up to date credit collection policy in place and undertake a thorough credit checks on all customers and create a clear outlined payment guideline such as indicating when payment is due and the specific contact persons. It was necessary to ensure that the SMEs are educated on such effects on the performances. Additionally another issue that arise is the levels of the Economic Order Quantity (EOQ) as such there is also a need for education and awareness. The firms need to encourage credit transactions with suppliers over the use of cash; this will enable the firms use the cash available for other purposes. The business should also seek to maintain sufficient inventory as failure lead to lost sales and customer loyalty. For further studies it is Recommendation that other studies be done to determine how working capital management affect overall financial health of any company. This study only focused on firms in Nairobi and therefore this result are skewed towards the perceptions and data in Nairobi. It is suggested therefore that such a study be done in other towns to make the results more reliable.
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CHAPTER ONE

1.0 INTRODUCTION

1.1 Background of the Study

Working capital has more technical of the two explains working capital as the difference between all short-term assets and short-term liabilities. Assets in business refer to anything of value a company owns. Liabilities are outstanding debts, such as loans and credit. The simpler definition describes working capital as the cash available for the day-to-day operations as a business (Sagner, 2010).

Working capital management involves the management of both current assets and current liabilities to minimise the risk of going bankrupt and at the same time increasing returns on assets (ROA). It involves planning and controlling the gross current assets as against the net working capital which deals with the cash of the company (Mathur, 2002). Aspects of working capital management include short-term loans, merchandise purchased on credit, goods and services provided on credit and merchandise, goods and services paid for upon delivery. Managing working capital essentially entails managing the cash flow of a business on a daily, weekly and monthly basis in such a way that satisfies all debts while reserving enough capital to continue operations and the generation of profits.

The objective of working capital management is to make sure that a firm can continue operating and to ensure that it has made enough money from operations to take care of short-term debt and upcoming expenses (Bose, 2012). This means that the company must maintain the right ratio of assets, liabilities and working capital otherwise it would have become very difficult for them to stay in the market. With most pasted literatures carried out in the business world it had traditionally been concentrating on the study of financial decisions, which were long-term and had also focused on the firm’s performance. This had allowed scholars to concentrate on looking deep into analysing the capital structure, dividend, investments and company valuations. But, as of late there has been recent surveys that had been carried out and shown indications that managers spent a good amount of time in coming up with a solution to their everyday problems which involves working capital decisions for their firm (Raheman & Nasr, 2007).

Small and medium enterprises would face bankruptcy when insufficient capital resources prevents them from paying their debts. Successful working capital management allows
small and medium enterprises to pay all debts as they mature, or come due, while continuing profitable business operations, which concludes a positive impact to their standing and relationship with their competitors. At the very least, successful working capital management allows small and medium enterprises to break even when calculating their profits either at the end of the day or month depending on how the firm looks at it (Teruel and Solano 2007). Therefore, working capital management is directly responsible for the avoidance of bankruptcy of small and medium enterprises. Unsuccessful working capital management can lead directly to bankruptcy by preventing a business from paying off liabilities or by preventing the generation of new capital with which to pay future debts, therefore keeping working capital at a good stand allows small and medium enterprises to prosper and prevent themselves from bankruptcy.

Working capital is important to small and medium enterprises as it is key in the financial health of a company whereby, it deals with the efficiency of the small and medium enterprise and their turnovers of their inventory, accounts receivables and payables. The efficiency pillar is amongst the 4 pillar of the financial health of a company, other being the profitability pillar, leverage pillar and liquidity pillar. These pillars are important for a company since it helps keep companies from falling and allows the analysis of the ratios used in the financial health to see which areas of the firm should be focused on (Santosuosso, 2014). According to Eljelly, working capital management of corporate entities is one of the most crucial aspects in attaining optimal liquidity position and in ensuring that corporate going concern. It is important in making decisions for companies when making a trade-off between liquidity and profitability, in a way that optimizes the amount and composition of their current assets and how they are financed, allowing better management of their assets (Eljelly, 2004).

In this study, we will be looking at the small and medium-sized enterprises in the Kenyan context. Small and medium-sized enterprises have played a huge role in the Kenyan economy as it has led to many positive impacts to the people of Kenya. According to the Kenya National Bureau of Statistics in 2015 the council had taken part in training small and medium-sized to developing new products which were test-market to the regional markets of East African Community (EAC), Common Market for Eastern and Southern Africa (COMESA) and which was later marketed to the rest of Africa (Statistics, Economic Survey, 2015).
According to the economic survey of Kenya 2011, it was stated that the 503,000 jobs created last year, 440,400, or 80.6 per cent were in the SMEs (Statistics, Economic survey, 2011). The survey had shown that small and medium-sized enterprises play a huge role in the growth of Kenyans Gross Domestic Product (GDP) as well as increasing employment rate of those mostly residing in Nairobi. Due to new businesses being opened up in Kenya it paves way for heavy employment in agricultural and construction work force sector allowing many Kenyans lacking qualifications to enter agricultural and constructional labour (Bowen, Morara, & Mureithi, 2009).

According to the Laws of Kenya, small and medium-sized enterprises have been defined according to the amount of person’s employee within the establishment of the business. Small-sized businesses were described as micro-enterprise whilst medium-sized businesses were described as small-enterprise according to the micro and small enterprise act of 2012 (Kenya, 2012). Micro-sized enterprises being known as small-sized enterprises had to employ less than ten people with a turnover that doesn’t exceed five hundred thousand Kenyan shilling. With small-sized enterprises it would only be considered medium-sized if the employees employed between ten to fifty people as well as having an annual turnover between half a million to five million Kenyan shillings.

1.2 Statement of Problem

Kenya hope to achieve their goal of reaching vision 2030 as it is the destination Kenya is believed to at it greatest. With this small and medium-sized enterprises are key in reaching that destination since it contributes to the economy as well as allows a path to the decline of unemployment (Statistics, 2015). With majority of the country working it allows the Gross Domestic Product (GDP) of Kenya to increase which leads to more investment from the Government to aid the entrance of new small and medium-sized enterprises without saturating the market too much.

It is hard for the SMEs to access finances from the financial institutions since they lack proper working capital management skills Atrill (2006). The major problem that arises is on how working capital management practices affect the profitability of SMEs. Most of the Small and Medium Enterprises face challenges in balancing between surplus and shortage of working capital. As a result, these firms have been experiencing slow growth because of inability to pay daily expenses of their operations and difficulty to exploit new markets and undertake profitable projects due to shortage of working capital mainly
because of poor working capital management. There is, therefore, a need for firms to have efficient working capital management practices. This study sought to find out the effect of working capital management practices on profitability of SMEs in Nairobi County.

In Westerfield, Ross, Jordon and Jaffe (2010), it was accounted for that there exist a crisscross between money inflow and money outflow during operating activities in small enterprises. To control the flow of cash and in this way lessen the potential negative impacts on profitability and risk, it is imperative that working capital management instruments and strategies are embraced. This in the process will enhance their quality settling on choices on working capital suggests making a trade-off among profitability and risk (Ross, Westerfield, Jaffe, & Jordan, 2010).

1.3 Purpose of the Study

The purpose of this study was to determine the effect of working capital management on the profitability of Small and Medium-sized enterprises within Nairobi, Kenya.

1.4 Research Questions

The study was guided by the following research questions:

1.4.1 How does accounts receivables put an effect on the profitability of small and medium-sized enterprises in Nairobi?

1.4.2 How does inventory holding period put an effect on the profitability of small and medium-sized enterprises in Nairobi?

1.4.3 What is the effect of accounts payable on small and medium-enterprises profitability in Nairobi?

1.4.4 What is the effect of cash conversion cycle has on working capital management on profitability of small and medium sized enterprises?

1.5 Significance of the Study

The object of the research presented in this study is to look at the effects of working capital management on the profitability of small and medium-sized enterprises in Nairobi, Kenya which would help firms understand the importance of managing their working capital to gain good profit standing in their operations.
1.5.1 Small and Medium sized enterprises

This research study would further allow firms to understand how to allocate their funds to maximize their profits.

It would serve as a guideline for small and medium-sized enterprises within Nairobi to understand the importance of managing working capital and ways to prevent from the business from bankruptcy.

1.5.2 Suppliers

It would provide tools of measuring their working capital as well as their inventory days holding, account receivables, and account payables. This would help suppliers understand the importance of working capital with the aid of this study they will be able to efficiently private their services to consumers much easier than they would have.

1.5.3 Scholars and Researchers

This study would further help scholars and university students to understand the procedures of working capital management as well as providing research guidelines for obtaining data to support a claim to their research.

1.6 Scope of Study

The scope of this study would cover small and medium-sized enterprises dispersed around Nairobi since it would give better results due to the different enterprises within Nairobi County. Nairobi is known to host most businesses in Kenya as it is the hub for all business transaction making it ideal for potential business minded individuals to open up their establishments in the city.

The study would cover a selected sample size of most small and medium-sized enterprises in the Nairobi County which falls into their respected industries which they belong to. This research has then limited the study to the effect of working capital management on profitability of small and medium-sized enterprises within Nairobi, Kenya.
1.7 Definition of Terms

1.7.1 Account Receivable

Accounts receivable is short-term amounts due from buyers to a seller who have bought goods or services from the seller on credit and have to pay it back (Sagner, 2010).

1.7.2 Account Payable

The aggregate amount of an entity's short-term obligations to pay suppliers which provided products and services which the firm purchased on credit (Brigham & Ehrhardt, 2005).

1.7.3 Inventory Holding

Measures the rate at which inventory is used over a measurement period (Reilly & Brown, 2006).

1.7.4 Working Capital

Business’s net investment in current assets which includes debtors, stock material, working-in-progress, finished goods, cash and short-term deposit and investments (Ryan, 2004).

1.7.5 Cash Conversion Cycle

The length of time between a firm's purchase of inventory and the receipt of cash from accounts receivable (Ehrhardt & Brigham, 2008).

1.7.6 Small medium enterprise

Businesses whose personnel numbers fall below the limit of fifty employees (Kenya, 2012).

1.7.7 Working capital management

Working capital management is a tactical focus on maintaining a sufficient amount of working capital to support a business, while minimizing the investment in this area (Preve & Sarria-Allende, 2010).

1.7.8 Profitability

The ability of a business to earn a profit (Pirasteh & Fox, 2010).
1.8 Chapter Summary

This chapter covers the statement of the problem along with the purpose of the study in which this report had introduced as well as the background of the study. The research questions have indicated the direction as well as the focus of this study which will later outline the importance of this report and how it could benefit those that use this report. In the next chapter, the literature review which shall be looked at will give an understanding of the literature that has been written by many scholars and other researchers. Chapter Three will look at the methodologies which shall be used to gain data from the targeted sample. Further this study would show Chapters four and five of the research showing the results of data collected from participants and further analyzed to provide conclusion and recommendations.
CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction

This section will center on the research questions that were put forward in Chapter One. The main objective of this research study that brought forth the research questions is to determine the effect of working capital management on the profitability of SMEs within Nairobi, Kenya. The main thematic base for this literature review will revolve around the research questions, and previous scholarly work will enable this research paper to wipe out any replication of literature. The research questions will be divided into sub headings whereby each and every one of them will delve into what different scholars have documented their research concerning this particular topic.

2.2 Effects of Receivable Accounts on Profitability

2.2.1 Accounts Receivable Period

On the supply side, the profitability from SMEs in Nairobi is considered as an interest as far as accounts receivables are concerned. The advantages of accounts receivables are based on four complementary angles. First is the reductions of operational costs. Second is the expansion of the sales. Third is the raising of the rate on return. The fourth one is the setting up of stable business associations with the purchasers (Pandey, 2004).

First and foremost, Dellannay and Weill (2004) notes that accounts receivables decrease the operational costs. In fact, accounts receivable increments lead to working adaptability. While undoing the credit terms, suppliers can decrease the stockpiling costs for unverifiable demands of stocks and the expenses of changing their produce levels when demands shift (García-Teruel & Martínez-Solano, 2010). This is correlated with the exact information, which uncovers that SMEs in Nairobi with variable demands may want to offer a more drawn out accounts receivables period to diminish the operational instability, and along these lines diminish the operational costs (Dellannay & Weill, 2004).

Furthermore, SMEs in Nairobi use accounts receivable to support deals all the while. Lazaridis and Tryfonidis (2006) prescribes that SMEs use accounts receivables rather than direct cost deterioration to build deals particularly amid times of low finances.
Essentially, Dellannay and Weill (2004) suggest that when SMEs deals are sensitive to
the interest changes, accounts receivables is a particularly imperative technique to
invigorate clients to secure stocks in a time of low demands. Moreover, as per
Welner(2000), accounts receivables can be utilized as value separation between the
money and the clients. This will be beneficial at whatever point the flexibility of the
demands of money clients surpasses that of credit clients or at whatever point money
clients’ reservation costs are efficiently greater than those of credit clients (Berglof and
Bolton, 2002).

In actual sense, Dellannay and Weill (2004) indicates that SMEs change the credit term
and rebate for brief payment as indicated by the demand flexibility of clients and they
may pay diverse costs for the same stock as per whether purchasers postpone the
payments or not. SMEs whose overall revenues are moderately high are more tolerant to
delays on the payment or more credit period. This is because of the way that these SMEs
can utilize higher peripheral income to bring about extra costs which are utilized to
produce new sales and build profitability. Albeit some SMEs lack high net revenues,
despite everything they view accounts receivable as an effective approach to support sales
and build profitability (García-Teruel and Martínez-Solano, 2014). As expressed in non-
price rivalry theory, SMEs in overall have less market power when contrasting with the
huge businesses. Baños-Caballero, García-Teruel, and Martínez-Solano, 2012) notes that
SMEs lack some points of demand rates to penetrate market through price war because
expansive ventures pick up advantages from economies of scale and tremendous capital
backings . Accordingly, SMEs, so as to build their market shares of the overall industry
and productivity, like to give accounts receivable.

2.2.2 Suppliers and Account Receivables

Thirdly, notwithstanding quickening demands, Harris (2005) brings out the point that
interest revenue is another reason that suppliers gain income from accounts receivables.
When the inherent rate of profit grossed for accounts receivable exceeds that of the
marginal share, suppliers would have premiums to offer accounts receivable to their
clients (Dellannay and Weill, 2004). Suppliers regularly offer credit terms and the implied
loan fee scopes to over 40% in a net period finishing after one month when clients do
without the rebate (Atrill, 2006). Here the markdown for the initial payment is considered
as a verifiable loan fee for the late instalments. It demonstrates that the particular rate of
profit for accounts receivable is greater than 40%, which implies that accounts receivables is for the most part a lucrative venture for supplier, particularly when client default risk is minimal.

Lastly, accounts receivables assist SMEs to build up a steady business relationship in due course (Wilner, 2000). Wilner (2000), states that accounts receivables may expand clients’ reliance on their suppliers, which may bring about a greater interest rate. This contention is likewise bolstered by the asset reliance theory, asserting that SMEs may have inconveniences to get to every basic asset, and they depend on suppliers to offer fractional basic assets (Kwame, 2007). Correspondingly, accounts receivables here can be considered as an exchanging boundary. Purchasers may lose access to transient finances if they need to change suppliers because suppliers just offer accounts receivables opportunities to whom that they have built up experienced comprehension with (Gitman, 2005). Consequently, suppliers are tied with clients in a vibrant business affiliations by means of accounts receivables.

Be that as it may, Baños-Caballero, et al. (2012) the development of accounts receivables is associated with a few negative impacts for the suppliers. Suppliers would have to pay more regulatory costs for example default debts and check-up costs. Every time suppliers ought to monitor the monetary capacity of the purchasers. This requires both direct cash expenses and human asset costs. At the point when these expenses surpass the advantage from income development, suppliers fail to offer accounts receivables to their clients. Likewise, accounts receivables in this case suggests high direct financing expenses and opportunity costs (Mian and Smith, 1992). The cash on the accounts receivable may contribute on great profitability extends as opposed to negligible amounts. Protracted payments suggests the diminished present value of incomes, particularly in a time of severe inflation rates.

Therefore, there is a compromise between the advantages and expenses on accounts receivables. Emery (1984) recommends a thought of ideal accounts receivables arrangement. It states that when the marginal expenses are equivalent to marginal income regarding accounts receivables, the finances due achieves the optimal level. Accordingly, Wilson and Summers (2002) claim a non-monotonic (inward) correlation between accounts receivables and SMEs value. They explain that specific levels of accounts receivables can actually boost the SME value. Nonetheless, there is no observational
consummation to bolster this theory. By complexity, Hill and Lockhart (2012) examine more than 10,000 SMEs amid the timeframe of 1973-2006, and they discover that there is a direct positive correlation between shareholders worth and accounts receivables. Moreover, Moyer, McGuigan, and Kretlow (2005) expound on how accounts receivables impact SMEs execution. They analyse the non-monetary Belgian SMEs amid the timeframe of 2006-2009 and they inferred that SMEs which expanded accounts receivables within the 2008 budgetary crisis that were contrasted with pre-crisis times have a generally greater productivity within the crisis years. Also, García-Teruel and Martínez-Solano (2014) study the correlation amongst profitability and accounts receivables with over 71,000 SMEs in Spain within the timeframe of 2000-2007. They discover a positive direct correlation between investment in accounts receivables and SME productivity. Similarly, because of the intense market rivalry, SMEs are compelled to offer accounts receivables. Accounts receivables is instrumental to help trades and their vital objective is to enter market for those SMEs in development process. Therefore, it is more probable that accounts receivables has a direct positive association with profitability in the SMEs. As indicated by this literature review, the hypothesis that can be drawn out is that the profitability in small and medium-sized enterprises in Nairobi is positively correlated with the accounts receivables offered by the SMEs.

2.2.3 Trade Credit

The supply of trade credit is usually utilized by SMEs as a marketing instrument to increase or uphold sales (Pandey, 2004). Proficient receivables management boosted by a reduced creditor’s collection timeframe, minimal levels of bad debts and a vibrant credit program regularly enhances the organizations’ capacity to draw in new clients and likewise increase the fiscal performance thus the necessity for a vibrant credit program that will guarantee that the SMEs’ worth is heightened (Ross, Westerfield, and Jordan, 2003). The expenses incurred due to financial discounts, the damages caused by bad debts and expenses of overseeing credit and credit accumulations constitute the conveying costs associated with providing credit which rises when the amount of receivables provided is also raised. Lost sales coming about because of not providing credit to clients constitute the opportunity cost which diminishes when the measure of receivables is raised. Companies that are effective in receivables administration for the most part decide their
ideal credit levels which minimizes the aggregate expenses of providing credit (Ross et al., 2008).

Meltzer (1960) states that an essential capacity trade credit may be to relieve customers’ financial frictions, along these lines encouraging expanded offers which facilitates growth (Nadiri, 1969). What's more on determining financing frictions, trade credit might support deals toward alleviating informational asymmetry the middle of suppliers and purchasers with product quality (Smith, 1987). In this sense, the seller’s speculation done in trade credit facilitates in return decreasing questionable uncertainty of the products quality. Also, trade credit empowers value separation (Brennan et al., 1998); eventually the period of credit or discount for prompt payments, firms would sell their goods at various prices regarding the demand elasticity of their customers. On a long expression perspective, trade credit could provide for future benefits by Creating and keeping up changeless business connections (Wilner, 2000). Also expanded sales, trade credit might build incomes through investment returns (Emery, 1984) or diminishment over transaction costs (Emery, 1987). However, those procurement about trade credit entails a negative impacts for example, default danger alternately late payment, which might harm firm productivity. Moreover, extending supplier financing includes managerial costs connected with the providing and monitoring process, and additionally transaction expenses to converting receivables under trade (Emery 1984). Further, carrying receivables on the accounting report intimates regulate financing with the goal decreasing stores accessible for extension undertakings.

As noted by Lazaridis, and Tryfonidis (2006) in their research, an expansion in the level of accounts receivables in a company boosts both the net working capital and the expenses of holding and overseeing accounts receivables and both may prompt a decline in the value of the firm. A research conducted by Lazaridis and Dimitrios (2005) discovered that organizations which seek after increased levels of accounts receivables to an ideal level build their profitability due to a growth in market share and sales. A research conducted by Raheman, and Nasr (2007) highlight that companies can establish their value by shortening the timeframe of accounts receivables, as likewise affirmed by the discoveries of Deloof (2003) who noted that the length of receivables accumulation period negatively affects a company’s performance. A research conducted by Padachi (2006) likewise avowed that setting up a vibrant credit program guarantees legitimate
debt collecting techniques and is imperative in enhancing productivity in receivables administration thus the performance of the companies. Teruel and Solano (2005) proposed that managers can establish value by decreasing their company’s periods of accounts receivable and stock.

Baveld (2012) conducted a research on the association between accounts receivables and profitability during the world’s crisis period. The research was intended for examining how public listed companies in the Netherlands handle their working capital. The research contrasted two periods; the non-crisis timeframe of 2004-2006 and the fiscal crisis timeframe of 2008-2009. Baveld's study indicated a noteworthy negative relationship between gross operating profit and accounts receivables during amid non-crisis timeframe. Then again, during the crisis times, no critical connection between these two variables was noted. The outcome of this research may propose that the correlation between a company’s profitability and accounts receivables changes during crisis in a way that several companies ought not to keep their accounts receivables at minimal levels so as to boost profitability during the crisis.

Mathuva (2009) researched on the impact of working capital management upon business profitability by utilizing an example of 30 organizations registered on the Nairobi Security Exchange (NSE) for 15 years until 2008. The findings of his research showed that there is a very critical negative correlation between profitability and accounts accumulation timeframe. As to the correlation between profitability and the stock conversion timeframe or the average payment timeframe, the outcomes were positive and noteworthy.

2.3 Effects of Inventory Holding Period on Profitability

2.3.1 Stock Level

As indicated by the scholarly work made by Edwin Sitienei and Florence Memba (2015), the expansion of stock holding prompts a reduction in the gross profit of the SMEs. This infers with a shorter time stock is being held and prompt a significant increment in the arrival on venture which would mean an increase in profitability (Sitienei and Memba, 2015). SMEs with littler gross overall revenues need to make progress toward higher stock turnover for them to stay in the business sector without making a lot of a losses. The study additionally reasoned that the span of the SME is imperative as with an expansion
in deals that would come about as development of profit for the SMEs and likewise enable the SME to concentrate intensely on stock turnover. The findings made by Muturi and Wachira (2015) additionally upheld that with less holding of stock a SME where the shorter stock transformation period the higher is the profitability of the SME and the other way around.

Keeping up ideal stock levels decreases the expense of conceivable intrusions and keeps loss of business emerging from lack of items. It additionally lessens supply costs also, secures against value vacillations. Setting the right stock holding time frame is the primary objective of stock administration. A study to research the ideal stock levels was completed by Swaminathan (2001), in which the study discovered that modifying crude materials and completed merchandise as a segment of stock is speedier than the stock as a whole to achieve the sensible levels. Autu, Kaite and Molay (2011) discovered that there are some different techniques that can ease stock administration, for example, request amount technique and without a moment to spare inventories.

Observational studies have demonstrated that stock transformation period negatively affects a business’ performance. For example, shortening the stock change time frame could expand stock out expenses of stock which results in losing deals opportunities and leads to poor performance (Deloof, 2003). Administrators of SMEs ought to in this manner keep their stock to an ideal level since an error of stock will prompt tying up overabundance capital to the detriment of beneficial operations (Dimitrios and Koumanakos 2008).

Dimitrios and Koumanakos (2008) brings up that an excess of stock could request more physical space, could prompt a monetary loss, and expansions the likelihood of inventories harms, crumbling and losses. Also, holding vast measure of stock regularly demonstrates wasteful and imprudent administration practices and systems. On the other hand, too little inventories may prompt the intrusion of operation in assembling, expand the likelihood of losing deals and therefore bring down the profitability of the SMEs.

Singh (2008) concentrated on the relationship between stock administration and working capital administration concentrating on the significance of stock administration. He discovered that organizations with a poor stock administration can bring about difficult issues which demolish the long haul profitability and SMEs survival shots. Likewise
SMEs with well-thought stock administration can lessen the stock to an ideal level which has no negative impact on generation and deals. The concentrate likewise demonstrates that the extent of stock specifically influences the working capital and its administration.

2.3.2 Valuation of Stock

As per Singh (2008) it is critical to keep record and administration of stock as it speaks to the venture of assets for a SME and that its speculation shouldn't be unnecessary or insufficient but instead ought to be kept ideal permitting no wastage of products. The article further clarified that SMEs which neglect to deal with their stock would prompt long haul benefit and in addition they will neglect to make due in the business sector (Singh, 2008). Firms have an inborn value, and that inherent worth depends on the measure of free income they can give within their useful lifetime. Cash later is worth under cash now, be that as it may, so future free money streams must be marked down at a proper rate. The hypothesis behind most stock valuation strategies is that the worth of a firm is equivalent to the whole estimation of all future free money streams. All future money streams are reduced because of the time estimation of cash. If one knows all future money streams of a firm, and one has an objective rate of profit for the cash, then one can know the careful measure of cash he ought to pay for that firm.

However, stock valuation is not that simple by and by, in light of the fact that managers can only gauge future free money streams. This valuation approach, in this way, is a mix of skill and science. Given the inputs, the yields are genuine. When managers know precisely the amount of income is to be created, and they have an objective rate of return, they can know precisely what to pay for a profit stock or any organization with positive free money streams paying little mind to whether it pays a profit or not. However, the inputs themselves are just gauges, and require a level of expertise and experience to be exact with. Therefore, stock valuation is skill and science (Singh, 2008).

2.3.3 Stock Systems and Procedures

Stock control is fundamentally checking and dealing with the measure of stock either on the offering floor, or away at any given time. It is critical this is done proficiently on the grounds that stock is the single biggest resource of the store. The fundamental reason for stock administration is to build the store’s benefit by guaranteeing that appropriate levels of stock are in the store at all times. The approaches and techniques used to fulfill this
will fluctuate contingent upon the kind of store. For stock administration to be powerful, somebody must be in charge of setting suitable arrangements, setting up suggested stock levels, and guaranteeing that control frameworks are working legitimately. With stock control, despite the fact that managers actualize the techniques and guarantee that staff are doing them, they should comprehend the explanations for the arrangements and methodology. For instance, an arrangement to screen stock levels is set up in light of the fact that inadequate stock cutoff points deals and over the top inventories tie up cash that might be required elsewhere in the store. It is imperative that the managers mentor their team about inventory control (Bonin and Wachtel, 2003).

Notwithstanding knowing the purposes behind the techniques, it is the managers’ responsibility to guarantee that their staff to likewise comprehend the significance of precise stock control. They have to comprehend the effect of their errors and work towards disposing of them quite far. Stock developments in stock movements are a consistent action in retailing. Stock must be moved in the most proficient route conceivable by taking after the store’s arrangement and continually considering the costs included.

Costs identified with stock development include transportation or cargo charges, lost deals if your store is missing stock, capacity costs and interruption to the general exercises of staff in store. To minimize these expenses guarantee that stock is moved proficiently. To accomplish this it is important to delegate the undertakings, know who is responsible for every undertaking and be sure that staff are doing their undertakings productively. Agrawal and Smith, (1996) as cited by Korobow (2012) notes that, stock administration is imperative since it helps in keeping up an exchange off between conveying expenses and requesting costs which would imply that it will minimize the aggregate expense of stock. Stock administration would promote encourage in the keeping up satisfactory stock of the SME for smooth creation and deals operations which would likewise stay away from the stock-out issue that a SME generally would confront in the absence of legitimate stock administration. Appropriate stock control framework could be connected by a SME to stay away from losses, harms and abuses.

Eneje et al (2012) investigated those effects for raw materials economy on the profitability from claiming brewery organizations to Nigeria utilizing n cross sectional information from 1989 with 2008 which might have been assembled to the dissection
from those yearly reports of the sampled brewery organizations. Measures of profitability were analysed and identified with proxies for raw materials management by brewers. The Ordinary Least Squares (OLS) expressed in the structure of a numerous relapse model might have been connected in the dissection. The contemplate uncovered that those neighbourhood variable raw materials stock administration planned will catch those effects of productive oversaw economy about raw material stock toward an organization on its profitability is altogether solid and certain and effect the profitability of the brewery organizations previously, Nigeria. They reasoned that productive management about raw material stock will be a main consideration will be held with eventually perusing Nigerian brewers over upgrading alternately boosting their productivity.

2.4 Effects of Accounts Payables on Profitability

2.4.1 Supply Credit

From the demand angle, the profitability from SMEs in Nairobi can be considered as transient debts as far as accounts payables is concerned and the advantages of accounts payables are discussed by different scholars. Firstly, accounts payables is a proficient way to deal with the SMEs money related gratings in short term (Autukaite and Molay, 2011). Considering the restricted informational openness, financial institutions are hesitant to provide debts to SMEs or they require high loan costs to repay high risks (Bonin and Wachtel, 2003). Accounts payables can be more available, particularly over the time of a tight money related strategy. Within the time of a tight financial approach, clients will probably change to accounts payables because around that time the compelling loan interests exceed the prevailing expenses of accounts payables. This is because of the way that the accounts payables terms are generally steady, which implies that certain financing costs are predictable. In the meantime, the interest costs of bank loans are expanding during a tight fiscal period, which prompts more costly expenses of bank loans than that of accounts payables (Bonin, and Wachtel, 2003). SMEs, lessening the expenses from the raising capital, will gain more profitability.

Secondly, as indicated by the credit proportioning theory, SMEs can’t access to the customary financial framework. The genuine data asymmetry amongst SMEs and prospective creditors makes it troublesome for SMEs to raise capital. Be that as it may, suppliers as traders can get to clients’ private data for example item quality and
operational conditions that are less expensive than banks. Suppliers precisely investigate
the present and future fiscal state of purchaser SMEs and after that choose whether to
give credit. Data advantage over the financial institutions may enable suppliers to prolong
credit with minimal risk. In addition, accounts payables in truth assumes a flagging part
for financial institutions. Numerous researchers contend that there is a positive correlation
between bank loans and accounts payables (Delannay and Weill, 2004). Agostino,
Giuntam, Nugent, Scalera, & Trivieri 2011) explore more than 4,500 SMEs in Italy and
they agree to this positive correlation.

Delannay and Weill (2004) contend that if suppliers will offer accounts payables and
afterward bear default risks, for financial institutions, this would imply that suppliers have
gained data avowing that purchaser SMEs can pay back the debts. Subsequently, financial
institutions have a positive outlook towards purchasers, and hence grant debts to the
purchasers. At the end of the day, accounts payables empower the private information of
the seller to be utilized as a part of the loaning relationship, and this extra information can
reduce credit proportioning caused by unfavorable choices (Delannay & Weill 2004).
SMEs get more capital from business sector, increasing more venture and development
opportunities.

Finally, Martinez-Sola, Gracia-Teruel, and Martinez-Solana (2013)as expressed in the
transaction theory, clients gain advantage from the lessened expenses by going around the
need to deliver the twofold coincidence of needs required in barter trade. Accounts
payables is utilized as a mechanism that stands as a payment or predetermined substitute
to quick financial use. It lessens uncertainty by means of business pooling. With the
uncertain supply for instance, volume and timing of cash streams are uncertain in the
stream of the merchandise. Cash should be carried and arranged in a complete transaction
procedure. This stochastic cash shows high holding expenses and opportunity costs
(Martinez-Sola et al, 2013). By disposing of these expenses by means of accounts
payables, the operational revenue is more possible and adaptable in the transaction and
clients can contribute cash on other high rate of return initiatives to maintain profitability.
Furthermore, accounts payables are utilized as an assessment instrument too for clients to
evaluate the nature of the product.
Martinez-Sola, et al (2013) states that, the purpose of extending the payment to purchasers is to check the nature of the product. Purchasers can decline the payment process if products have quality issues, which causes lesser transaction costs. Consequently, purchasers settle on obtaining choices as indicated by credit terms and different states of accounts payables. Korobow (2012), states that SMEs in this item quality guarantee a correlation hypothesis. Along these lines in the functional transaction procedure, purchasers would spare time which spend on assessing product quality and it would diminish costs on deficient products too by means of accounts payables.

In a synopsis, SMEs are to a great degree sensitive to the suppliers funding because of requirements on bringing up capital in the customary business sector. As stated, accounts payables helps SMEs to outshine fiscal erosions and cause cutbacks to the operational expenses. In order for the SMEs to be in substantial surviving, they appreciate the advantages from accounts payables. Equally, accounts payables do not demonstrate clear impeding consequences for the SME’s profitability as per the scholars. As indicated by this literature review, the hypothesis that can be drawn out is that the profitability of the small and medium-sized enterprises in Nairobi is positively related with accounts payables offered by the SMEs (Wilner, 2000).

2.4.2 Accounts Payable Credit

Wilson and Summer (2002) in an observational investigation of the demand for trade credit by small UK companies, additionally discovered solid proof of a bankrolling demand for trade credit. They discovered those small companies that reimburse their trade credit liabilities late seem to do as such when they achieve their threshold on short-lived bank loans. These credit proportioned companies were regularly developing and export prescribed. As a result, if the inconvenience of statutory interest essentially decreases the trade credit offered to littler companies, this may prompt extreme liquidity issues and more disappointment rates unless backup cash is promptly accessible. Various different answers for this issue of late payment have been advanced. For instance, it has been contended that credit administration is an ignored capacity in numerous issues and greater disappointment rates unless the backup money is promptly accessible. Wilson et al (1995) distinguished poor credit administration as one of the basic reasons for late payment.
Deloof (2003) analyzed 1009 huge Belgian non-monetary related companies from 1992-1996 and found that managers can expand the profitability of companies by diminishing the days in accounts receivable and stock. As indicated by his examination, less productive firms extend their accounts payable.

Nobanee and AlHajjar (2009) examined more than 2,000 Japanese non-monetary firms registered in the Tokyo Stock Exchange from 1990-2004 and reasoned that organization managers can build profitability by curbing the money conversion cycle, the receivables accumulation period and the stock conversion time frame. The outcomes likewise proposed that augmenting the payables deferral period could expand profitability. Be that as it may, managers ought to be watchful on the grounds that prolonging the payables deferral period could harm the organization’s credit reputation and damage its profitability over the long haul.

Moreover, trade credit permits clients to confirm that those stock accepted complies with those suitably terms (quantity, quality, and so on.), furthermore guarantee that at whatever services which are to be done as long as they were agreed. In the items don't reach the expectations, the client can decide to not pay and give back the merchandise (Smith, 1987). Also, Danielson and Scott, (2004) pointed out that, trade credit offers a greater amount budgetary adaptability over bank loans. Levels trade credit expand or diminishing for business action that a firm takes part in. The point when organizations face liquidity issues it may be on delay instalment should suppliers over renegotiate credit states for banks. What may be more, suppliers tend with take after a more tolerant liquidation approach over banks the point when a firm confronts fiscal trouble (Huyghebaert et al., 2007). However, utilizing suppliers as a hotspot of financing might turn out to make precise unreasonable to the firms, because of those reality that the understood investment rate done in trade credit, which will be often connected with a rebate to early payment, will be normally high. Specifically, there would two fundamental types of trade credit: A) full instalment around a certain date after conveyance for merchandise, Furthermore b) instalment with a rebate to promptly instalments in the markdown period, alternately instalment of the net sum during the end of the downright credit time. Consequently, financing through credit starting with suppliers might result in a chance to be an modest sourball of financing to those discount period, Be that expanding financing in this route might bring about losing the markdown to early payment, with a secondary good fortune
cost, Now and again surpassing 20 percent, relying upon the discount rate and the
discount time (Wilner, 2000).

Anichebe and Agu (2013) inspected those effects of stock management ahead
authoritative chose associations on Enugu Nigeria. Utilizing a descriptive research and
furthermore a test size about two hundred and forty eight (248) respondents, they made
that there will be huge association between handy stock administration and organizational
effectiveness. Inventory management oversaw economy might have been discovered
should bring a critical effect on organizational productivity. There was a great
correspondence between inventory management and organizational profitability. They
reasoned that stock management will be quiet important, as the prosperity growth of the
organization. Those whole productivity from claiming an association will be attached of
the volume about results sold which need a regulate relationship with those nature of the
result.

Postponing payments to suppliers enables organizations to survey the nature of the items
that were purchased and this can be an economical and adaptable wellspring of financing.
In any case, managers ought to know that late payment can have certain high expenses at
whatever point early payment discounts are accessible. Since cash is additionally secured
up working capital, the more the investment in current assets, the lesser the risk and the
lower the profitability achieved (Falope & Ajilore, 2009).

2.5 Effects of Cash Conversion Cycle on Profitability

2.5.1 Liquidity

A firms liquidity is its ability to meet its short term obligations (usually a year) and this is
only possible by the firm having the ability to convert its assets into cash. Short term,
generally, signifies obligations which mature within one accounting year (Lamberg &
Vålming, 2009). Through the ordinary course of a business, firms are able to acquire
inventory on credit, which they utilize to generate products, these are then sold in cash or
credit. These actions give rise to accounts payable and receivable, until the firm collects
cash from accounts receivable and settles the payable accounts (Muscettola, 2014). The
cash conversion cycle (CCC) is therefore a measure (in days) and replicates the length of
time taken to sell stock, collect receivables, and pay dues by a firm. A short cash
conversion cycle is often recommended as it allows ready available funds for a firm to
invest in assets or other activities that increase investment return, increase efficiency, and comparing the firm performance to close competitors.

CCC = days inventory outstanding (DIO) + days sales outstanding (DSO) – days payable outstanding (DPO)

Where: Days inventory outstanding = (average inventory/cost of goods sold) x 365: Days receivable outstanding = (average accounts receivable/sales) x 365: Days payable outstanding = (average accounts payable/cost of goods sold) x 365 and the shorter the CCC is, the healthier a company will be (Boyce, 2014). An institution that fail to settle its credits and short term liabilities on time may suffer from operations related challenges and this may certainly ruin its reputation. When a firm lack cash or liquid assets at its disposal this may result into it missing out on some of the benefits that would have been offered to them by the suppliers. The loss incurred from missing out on this incentives may lead to high cost of goods thus affecting the firms’ profitability. This therefore calls for the institution to regularly maintain some level of liquidity (Singha, Gupta, & Sharma, 2015).

There is currently no set up standard for liquidity and this varies from a firm to another depending on among others; the nature of the business, size and location of the enterprise. A firms’ liquidity is a crucial element that is observed by various stakeholder like: supplier, employees, and shareholders. Suppliers are interested in finding out if the company is capable of paying them before they can issue goods on credit. Employees on the other hand, have interest as to whether the firm can meet their financial obligation. Additionally, shareholder are interested in understanding the liquidity of the firm as this impacts greatly on the profitability (Lamberg & Vålming, 2009). Among the studies done on the impact of CCC on a firm’s performance, Lazaridis and Tryfonidis (2006), research in Greece observed that there exist a connection between working capital management and profitability and this was attributed to the efficient management of the cash conversion cycle. With an effort to expound on Lazaridi’s and Tryfonidis’s (2006) findings, Gill, Biger and Mathur (2010) study on 88 American firms listed on New York Stock Exchange for the period 2005 to 2007 established a significant statistical association between the cash conversion cycle and profitability. They further concluded that managers had the capability to create profits by efficiently handling the cash conversion cycle and maintaining accounts receivables at an optimal level. According to
Costa (2014) study on cash conversion cycle across industries the findings reveal that CCC differs between firms due to the size, and accounting process.

2.5.2 Cash Management

According to Van Horne (2000), a firm with excess amount of current assets may face low return on investment because of the cash being held up. On the other hand, those with low current assets may incur shortages and experience challenges in operations. It is on this paradigm that it is recommended for firms to maintain optimum level of liquidity and profitability. Hamza, Mutala and Antwi (2015) highlight that an institution should be in a position to generate sufficient cash to be sustain its immediate obligations to be able to trade. Cash management is considered among the main aspects that determine the efficiency of working capital this involves planning and controlling of all cash flows from and into the business. (Weston & Copeland, 2008).

According to Costa (2014), cash management is geared towards optimization of the available cash to maximize the level of earnings and amount of cash held by the firm incurs an opportunity cost as such funds would have been invested in more productive projects. On the contrary, a firm needs to strike a balance between having too much or too little cash. Operating with very little cash balances increases the firm’s financial risk for being unable to meet their obligation as they fall due. Efficient cash management practices involves not only the determination optimal cash to hold but also planning and monitoring of available cash flows.

Many small enterprises lack data on the estimated future cash inflows and they also never budget or plan for the expected funds. This directly impacts on the future survival and sustainability of the enterprises. According to Nick (2009) findings it was revealed that enterprises which regularly budget for the future once a month increase their chance of survival by up to 80%. He also points out that small businesses assume that cash flow problems are automatically solved by increased growth in the future. Mong (2011) established that few small businesses create a cash budgets despite the importance of cash forecasting as a tool for efficient cash management.

2.5.3 Firm Characteristics

When the size of a firm increases in size this is bound to impact on, the working capital required. Large firms possess more control over suppliers and are better placed to
negotiate for conducive payment terms and conditions. Kwasi (2010), research in 11 Ghanaian Oil market firm to analyse the trends in working capital management and impact on their performance in a seven year period from 2001, he established the existence of a high variability of working capital and a negative relation between profitability and other factors of the CCC. Ching, Novazzi, and Gerab (2011) study of Brazilian listed companies to establish variability between corporate groups that undertake working capital intensive and fixed capital intensive policies for the period 2005 to 2009, the finding revealed similar results for the two groups of companies.

According to Uyar (2009) research in Taiwanese firms to examine how profitability and size of companies impacted on working capital, the results suggested an existence of a negative relationship between a firms size and profitability and cash conversion cycle. Wilson (2009) on the other hand investigated how firms with a well-established financial management system impacted on Working capital management and the results showed that a firm’s size, debt ratio, and growth affected the management of Working capital. Similarly, Nilsson, et al. (2010) under took a research of Working capital management in Swedish firms, he made a comparison of the effects firm’s characteristics on cash conversion cycle. The elements used for comparison included profitability, company size, operating cash flow, and sale growth. The results suggest a relationship between the variables and Working capital management.

Mathuva (2010) found contradicting confirmation with those management for inventories done Kenya. He contended that organizations expand their stock levels to decrease those cost about could reasonably be expected handling stoppages and the likelihood for no entry on raw materials and other results. He further stated the discoveries about blinder and Maccini (1991), which demonstrate that higher stock levels diminishes those expense of supplying items also Additionally protects against value variances created toward evolving macroeconomic elements. Also contradicting proof may be found by Mathuva (2010) for those administration from claiming account payables. He found a sure effect of the amount times accounts payables ahead a firm’s productivity in Kenya. He demonstrated this sure connection with two reasons, primary he contended that additional gainful organizations sit tight more which are profitable to pay their bills. These organizations utilization these accounts payables as a short-term sourball about subsidizes. Those second contention the reason organizations build their accounts payables is that these organizations have the capacity on expand their working capital.
levels and in this manner expanding their productivity. This is in line with hypothesis of a
negative effects of the Cash Conversion Cycle (CCC) on the profitability of a firm. This
is brought about by the way that those amount of day’s accounts payables necessities will
make include in the estimation of the CCC.

2.6 Chapter Summary

This literature review relied on what various scholars have discovered with respect to the
research questions. The three research questions have been tended to and there was a
definite necessity of more research to be conducted. The literature review conducted in
this case is simply what scholars have documented based on their research surrounding
the premise of SMEs in broad terms while Nairobi as Kenya’s capital has been
interrelated with their scholarly work. More inquiries concerning the profitability of
SMEs in regards to the accounts receivables, accounts payables and inventory holding
period calls for further investigations on this matter in regards to working capital
management as general objective of the study in this case.
CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Introduction

This chapter will provide the research design and methodology in which the research shall be undertaken by. It will further be looking at the target population with the sampling frame utilizing the sampling design and sample size of the pool. It will further include data collection instrument to measure as well as the research procedures that will take place allowing us to reach our analysis.

3.2 Research Design

Research design, according to Creswell (2003), is the scheme, outline or plan that is used to generate answers to the research problems. This study had taken the descriptive research design, in which it is a study of relatively short duration and it involves a systematic collection of data which will be presented to give a much better understanding of the research topic. Descriptive research has three main objectives which have made it the most appropriate research design for this research study. Descriptive research helps discover whether a relationship exists between variables, helps determining the frequency of occurrence and finally it describes the state of the variables (Copper and Schindler 2013). It was aimed at getting relative information related to the effect of working capital management on profitability of small and medium sized enterprises in Nairobi. The independent variable of this study is working capital management whilst the dependant variable would be profitability of small and medium sized enterprises. The independent variable includes account payable, account receivables and inventory management.

3.3 Population and Sampling Design

3.3.1 Population

According to Saunders, Lewis and Thornhill (2009), population is the complete set of cases or group members. The population which had been undertaken in this study would be focused on small and medium sized enterprises in Nairobi which are registered under the Kenya Private Sectors alliance under the micro and mall enterprise federation (MSEF). The estimated total population was four hundred (400) small and medium sized enterprises.
3.3.2 Sampling Design

3.3.2.1 Sampling Frame

According to Saunders, Lewis and Thornhill (2009), sampling frame is the complete list of all the cases in the population, from which a probability sample is drawn. The sampling frame of the population of 400 small and medium sized enterprises. The population was gathered from Nairobi City Council which had shown the population of small and medium sized enterprises in Nairobi.

3.3.2.2 Sampling Technique

The sampling techniques refers to the method used in obtaining samples from a population in a way that the sample selected will help determined a stated hypothesis in regards to the population as stated by Copper and Schnilder (2013). The descriptions of the small and medium sized enterprises by their nature of their business constituted strata.

The sampling technique used in the study was stratified random sampling whereby differentiating them into their respected strata’s from management level to owners of the small and medium sized enterprises.

3.3.2.3 Sample Size

According to Copper and Schnilder (2013), a sample is what would be considered as a small portion obtained from an accessible population. It is made into subgroups which then are carefully selected to be the representation of a population. Due to some limitations which are associated with time and cost the whole population cannot be analysed. Using random sampling, two hundred small and medium enterprises were selected for the study.

Out of the 200 participants in the study fifty percent were owners of the enterprise whilst both top managers ad senior employees were both contributing to twenty five percent each respectively.

The major benefits of sampling techniques are that it makes research easier and efficient in terms of time and costs. Whilst the benefits of the sample size obtained is that it would be easier to conduct interviews over time but can still be managed by an individual.
Table 3.1: Sample Size

<table>
<thead>
<tr>
<th>Respondents</th>
<th>Target population</th>
<th>Percentage of population</th>
<th>Sample Response expected</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owners</td>
<td>100</td>
<td>50%</td>
<td>80</td>
</tr>
<tr>
<td>Top Managers</td>
<td>50</td>
<td>25%</td>
<td>40</td>
</tr>
<tr>
<td>Senior Employees</td>
<td>50</td>
<td>25%</td>
<td>40</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>200</strong></td>
<td><strong>100%</strong></td>
<td><strong>160</strong></td>
</tr>
</tbody>
</table>

3.4 Data Collection Methods

This study used primary data collection which entailed structured questionnaires. This was because a questionnaire is considered the most suitable tool for survey research (Oso & Onen, 2009). The questionnaires were administered to the respondents who are employees and owners of the enterprises at a proportion of 6:4 respectively. The data collected was believed to be authentic given annual reports are audited giving the financial information presented in them credible. Questionnaires also reduce researcher bias, they are cost effective, easy to analyse and less intrusive.

The data collected from the questionnaires were free from bias and researchers influence making sure that the data is valid and accurate. The questions addressed by the questionnaires sought to gather descriptive data on the basis of the research questions. The first part of the questionnaire sought to obtain information regarding background information on the respondents. Whilst the second part of the questionnaires sought to gather information regarding to the research questions.

3.5 Research Procedures

The researcher was given a research clearance permit by the City County Secretary office. The researcher proceeded to the field to collect data from the 40 SMEs in Nairobi City after having carried out pilot study in the same area using a sample size of 4 respondents hence excluded from the actual survey. The questionnaires were given out to small and medium sized enterprises each individually in their respected establishments where they were filling out the forms and thus collected from them personally allowing no fraud to take place.
3.6 Data Analysis Method

Data collected was collated and triangulated into recurring themes which formed the basis of the findings. The data was handled using both SPSS and Microsoft Excel simultaneously providing accurate calculation from the data collected from the study. SPSS and Excel has both been efficient in analysing data from the respondents.

In some instances certain qualitative themes were clustered together and given quantitative dimensions through excel applications. The study also did a regression analysis where the dependent variable was correlated against the various independent variables to determine the relationship between them. Regression analysis was used to determine the regression between dependent variable and the independent variables of the study. The final analysis was then distilled after which the key findings were mapped out and developed into a draft report.

Data analysis was done using tables provided by SPSS and Excel which further helps the study be more understanding and shows the correlation.

3.7 Chapter Summary

This chapter summarized the methodologies needed to be carried out when undertaking research. It had mentioned the research design this report will be using to gain information and discuss the population and sampling design of the recipients of the environment the research will be conducted in. The sampling design is divided into three categories which include the frame, technique, and the size of the sampling design. Thus lead to the data collection methods which will be used and the procedures the research will use which will help with the data analysis method once the information is gathered at once. In chapter four of the study, it presents the discussion of the finding from chapter three in the form of tables. The followed by the conclusion and recommendation of the study.
CHAPTER FOUR

4.0 DATA ANALYSIS AND INTERPRETATION

4.1 Introduction

This chapter presents the findings established from the study as well as their interpretations. The chapter has the results on demographics of the respondents such as gender, level of education, age range, ownership of the business, years of operation, and number of employees in the enterprise and Nature of the Business/Operations. The chapter will further outline the effect of working capital management on profitability of small and medium-sized enterprises in Nairobi, Kenya

4.1.1 Response Rate

The response rate of a test measures the statistical power of a research and the higher the rate the better. In this study, the researcher distributed 160 questionnaires and all were filled and returned. This represents a response rate of 100% as shown in Table 4.1.

Table 4.1: Response Rate

<table>
<thead>
<tr>
<th>Questionnaires</th>
<th>Number</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Filled and collected</td>
<td>160</td>
<td>100</td>
</tr>
<tr>
<td>Non Responded</td>
<td>0</td>
<td>0.0</td>
</tr>
<tr>
<td>Total</td>
<td>160</td>
<td>100</td>
</tr>
</tbody>
</table>

4.2 Demographic Information

This section of the analysis offers the results on the various demographic factors of the respondents who participated in this research study.
4.2.1 Gender of Respondents

From the study the variable gender was evenly distributed with a mean of 1.67 and a standard deviation of 0.471. Majority of the respondents were female accounting for 67.5% of the population while the male accounted for 32.5% as shown in table 4.2

Table 4.2: Gender of Respondents

<table>
<thead>
<tr>
<th>Variable</th>
<th>Distribution</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Frequency</td>
</tr>
<tr>
<td>Male</td>
<td>52</td>
</tr>
<tr>
<td>Female</td>
<td>108</td>
</tr>
<tr>
<td>Total</td>
<td>160</td>
</tr>
</tbody>
</table>

4.2.2 Level Of Education

To investigate the education level of the respondents the variable had a mean of 2.97 and a standard deviation of 1.467. Degree holders were the majority with 48 respondents accounting for 30% of the population, this was followed by diploma holders with 38 respondents accounting for 23.8% of the total. Postgraduate holders were 35 and this was 21.9% of the total as shown in table 4.3.

Table 4.3: Education

<table>
<thead>
<tr>
<th>Variable</th>
<th>Distribution</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Frequency</td>
</tr>
<tr>
<td>Certificate</td>
<td>28</td>
</tr>
<tr>
<td>Diploma</td>
<td>38</td>
</tr>
<tr>
<td>Degree</td>
<td>48</td>
</tr>
<tr>
<td>Masters</td>
<td>5</td>
</tr>
<tr>
<td>Post Graduate</td>
<td>35</td>
</tr>
<tr>
<td>Others</td>
<td>5</td>
</tr>
<tr>
<td>Missing</td>
<td>1</td>
</tr>
<tr>
<td>Total</td>
<td>160</td>
</tr>
</tbody>
</table>

4.2.3 Age range

To investigate the age of the respondents the variable had a mean of 1.8 and a standard deviation of 0.87. The age group 26-35 were the majority with 74 respondents accounting for 46.3% of the population, this was followed by those below 25 with 48 respondents
accounting for 30% of the total. Those of between 36-45 were 32 and this was 20% of the total as shown in table 4.4.

**Table 4.4: Age range**

<table>
<thead>
<tr>
<th>Variable</th>
<th>Distribution</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>26-35 years</td>
<td></td>
<td>74</td>
<td>46.3</td>
</tr>
<tr>
<td>Less than 25</td>
<td></td>
<td>48</td>
<td>30.0</td>
</tr>
<tr>
<td>36-45 years</td>
<td></td>
<td>32</td>
<td>20.0</td>
</tr>
<tr>
<td>46 years and over</td>
<td></td>
<td>5</td>
<td>3.1</td>
</tr>
<tr>
<td>Missing</td>
<td></td>
<td>1</td>
<td>.6</td>
</tr>
<tr>
<td><strong>Totals</strong></td>
<td></td>
<td><strong>160</strong></td>
<td><strong>100.0</strong></td>
</tr>
</tbody>
</table>

**4.2.4 Owner of the Business**

To analyze the ownership the variable was found to have a mean of 1.50 and a standard deviation of 0.502. From the finding 80 of the respondents were owners accounting for 50% of the total as shown in Table 4.5

**Table 4.5: Owner of the Business**

<table>
<thead>
<tr>
<th>Variable</th>
<th>Distribution</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td></td>
<td>80</td>
<td>50.0</td>
</tr>
<tr>
<td>No</td>
<td></td>
<td>80</td>
<td>50</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td><strong>160</strong></td>
<td><strong>100.0</strong></td>
</tr>
</tbody>
</table>

**4.2.5. Years of Business Operation**

To investigate how long the SMEs have been in operation the variable had a mean of 1.32 and a standard deviation of 0.723. The findings revealed that most of the SMEs are less than 3 years old this represented 78.1% of the total respondents. This was followed by those of between 3-6 years and the results are shown in table 4.6.
Table 4.6: Years of Business Operation

<table>
<thead>
<tr>
<th>Variable</th>
<th>Distribution</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Frequency</td>
<td>Percent</td>
<td></td>
</tr>
<tr>
<td>less than 3</td>
<td>125</td>
<td>78.1</td>
<td></td>
</tr>
<tr>
<td>3-6years</td>
<td>23</td>
<td>14.4</td>
<td></td>
</tr>
<tr>
<td>7-10 years</td>
<td>6</td>
<td>3.8</td>
<td></td>
</tr>
<tr>
<td>11-14years</td>
<td>4</td>
<td>2.5</td>
<td></td>
</tr>
<tr>
<td>15 and above</td>
<td>2</td>
<td>1.2</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>160</strong></td>
<td>100</td>
<td></td>
</tr>
</tbody>
</table>

4.2.6. Nature of the Business/Operations

The study sought to establish the nature of the SMEs under study whether they were commercial and trade or service based. The findings revealed that the majority were commercial and trade and this were 125 representing 78% while only 22% were service based as shown in table 4.7.

Table 4.7: Nature of the Business/Operations

<table>
<thead>
<tr>
<th>Variable</th>
<th>Distribution</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Frequency</td>
<td>Percent</td>
<td></td>
</tr>
<tr>
<td>Commercial and Trade</td>
<td>125</td>
<td>78.</td>
<td></td>
</tr>
<tr>
<td>service</td>
<td>35</td>
<td>22</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>160</strong></td>
<td>100</td>
<td></td>
</tr>
</tbody>
</table>

4.2.7. Number of Employees in the Enterprise

The study sought to establish the number of employees in the SMEs under study. The findings revealed that the majority of the firms had between 11 and 30 employees 33% while only 10% had less than 5 employees as shown in table 4.8.

Table 4.8: Number of Employees in the Enterprise

<table>
<thead>
<tr>
<th>Variable</th>
<th>Distribution</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Frequency</td>
<td>Percent</td>
<td></td>
</tr>
<tr>
<td>less than 5</td>
<td>16</td>
<td>10</td>
<td></td>
</tr>
<tr>
<td>6-10</td>
<td>29</td>
<td>18</td>
<td></td>
</tr>
<tr>
<td>11-30</td>
<td>53</td>
<td>33</td>
<td></td>
</tr>
<tr>
<td>31-50</td>
<td>35</td>
<td>22</td>
<td></td>
</tr>
<tr>
<td>Above 50</td>
<td>27</td>
<td>17</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>160</strong></td>
<td>100</td>
<td></td>
</tr>
</tbody>
</table>
4.3 Effects of Accounts Receivables on the Profitability SMEs

The study sought to establish the effects of accounts receivables on the profitability SMES and the respondents were asked a number of questions that they were rating with the least being Strongly Disagree (1) and the highest being Strongly Agree (5).

4.3.1 Descriptive on Effects Of Accounts Receivables on the Profitability SMEs

Most respondents agreed that the business screens customers or client’s reference before giving credit and this had the highest mean of (4.23), this was followed by whether the business enterprise monitors accounts receivables and analyses reports on debtors aging with a mean off (3.91). The least means were for the variables whether there is a credit collection policy in place (3.21) and if the business offers some sales on credit (3.19). The results are shown in table 4.9.

Table 4.9: Effects of Accounts Receivables on the Profitability SMEs

<table>
<thead>
<tr>
<th>VARIABLE</th>
<th>MEAN</th>
<th>STD</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Business offers some sales on credit</td>
<td>3.19</td>
<td>1.250</td>
</tr>
<tr>
<td>The business has in place a credit policy</td>
<td>3.67</td>
<td>1.010</td>
</tr>
<tr>
<td>The business most debtors stick to the credit period</td>
<td>3.41</td>
<td>1.369</td>
</tr>
<tr>
<td>The business screens customers or clients reference before giving credit</td>
<td>4.23</td>
<td>1.222</td>
</tr>
<tr>
<td>The Business enterprise monitors accounts receivables and analyses reports on debtors aging</td>
<td>3.91</td>
<td>1.009</td>
</tr>
<tr>
<td>There is a credit collection policy in place</td>
<td>3.21</td>
<td>1.234</td>
</tr>
</tbody>
</table>

4.3.2 Regression between Effects of Accounts Receivables and Profitability SMEs

A regression analysis was done between variables of accounts receivables and profitability of SMEs. On analysis, the adjusted R square value was 0.99 and a p-value of (0.000) was significant. This means that 99% of the variation in profitability was caused by the variation in the account receivable.
Table 4.2: Model Summary on Accounts Receivables and Profitability

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>Change Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>R Square Change</td>
</tr>
<tr>
<td>1</td>
<td>.995a</td>
<td>.990</td>
<td>.990</td>
<td>.11400</td>
<td>.990</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>F Change</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>df1</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>df2</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Sig. F Change</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Credit collection policy, clients reference, credit period, credit policy, monitors accounts sales on credit

An ANOVA analysis was done between effects of accounts receivables and profitability at 95% confidence level, the F critical was 2480.120 and the P value was(0.000) therefore significant the results are shown in table 4.11 below.

Table 4.3: ANOVA on Accounts Receivables and Profitability

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Regression</td>
<td>193.381</td>
<td>6</td>
<td>32.230</td>
<td>2480.120</td>
</tr>
<tr>
<td></td>
<td>Residual</td>
<td>1.962</td>
<td>151</td>
<td>.013</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>195.344</td>
<td>157</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Dependent Variable: performance
b. Predictors: (Constant), Credit collection policy, clients reference, credit period, credit policy, monitors accounts, sales on credit

4.3.3 Coefficient of Account receivable on Organizational Profitability

A Pearson correlation was done between profitability (dependent variable) against other factors of account receivable. The results of the regression coefficients, t-statistics, standard errors of the estimates and p values are shown in table 4.12.

When organizational profitability was predicted on account receivable(Constant (pvalue=0.402) sales on credit (Beta=.232, pvalue=.000) business has in place a credit policy (Beta=.113, p value =.000), debtors stick to the credit period (Beta=.212, p value=.000), screen customers before giving credit (Beta=.173, p value=.000), The business monitors accounts receivables (Beta=.195, p value =.000), there is a credit collection policy in place (Beta=.125, p value=.000). All the variables were positive and significant (pvalue<0.05).
From the analysis above, all the account receivable variables had a significant positive effect on organizational profitability.

### 4.4 Effect of Inventory Holding On the Profitability of SMES

The study sought to establish the effects of inventory holding on the profitability SMES and the respondents were asked a number of questions that they were rating with the least being Strongly Disagree (1) and the highest being Strongly Agree (5).

#### 4.4.1 Descriptive on Inventory Holding On the Profitability

Most respondents agreed the business keeps accurate inventory records and this had the highest mean of (4.38), this was followed by whether the Business ensures funds are set aside for reorder with a mean of (4.19). The least means were for the variables the length of inventory holding period has a material impact on the profitability of SMES mean of (3.57), and the business should set Economic Order Quantity (EOQ) to ensure adequate stocks are maintained mean of (3.49) as shown in table 4.13.

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>.039</td>
<td>.047</td>
<td>.841</td>
</tr>
<tr>
<td></td>
<td>sales on credit</td>
<td>.207</td>
<td>.029</td>
<td>.232</td>
</tr>
<tr>
<td></td>
<td>business has a credit policy</td>
<td>.124</td>
<td>.028</td>
<td>.113</td>
</tr>
<tr>
<td></td>
<td>debtors stick to the credit period</td>
<td>.173</td>
<td>.019</td>
<td>.212</td>
</tr>
<tr>
<td></td>
<td>screens customers before giving credit</td>
<td>.158</td>
<td>.018</td>
<td>.173</td>
</tr>
<tr>
<td></td>
<td>monitors accounts receivables</td>
<td>.214</td>
<td>.030</td>
<td>.195</td>
</tr>
<tr>
<td></td>
<td>There is a credit collection policy in place</td>
<td>.112</td>
<td>.031</td>
<td>.125</td>
</tr>
</tbody>
</table>
Table 4.5: Descriptive on Inventory Holding On the Profitability

<table>
<thead>
<tr>
<th>Variable</th>
<th>Mean</th>
<th>STD DEV</th>
</tr>
</thead>
<tbody>
<tr>
<td>The business reviews inventory levels periodically</td>
<td>4.12</td>
<td>.881</td>
</tr>
<tr>
<td>The business keeps accurate inventory records</td>
<td>4.38</td>
<td>.760</td>
</tr>
<tr>
<td>The business has installed an inventory control system</td>
<td>3.79</td>
<td>1.397</td>
</tr>
<tr>
<td>A longer inventory holding period negatively effect profitability</td>
<td>4.09</td>
<td>.937</td>
</tr>
<tr>
<td>The length of inventory holding period has a material impact on the profitability of SMEs</td>
<td>3.57</td>
<td>1.161</td>
</tr>
<tr>
<td>The Business should set Economic Order Quantity (EOQ) to ensure adequate stocks are maintained</td>
<td>3.49</td>
<td>1.107</td>
</tr>
<tr>
<td>The Business ensures funds are set aside for reorder</td>
<td>4.19</td>
<td>.997</td>
</tr>
</tbody>
</table>

4.4.2 Regression between Effects of Inventory Holding and Profitability SMEs

A regression analysis was done between variables of inventory day of holding and profitability of SMEs as shown in table 4.14. On analysis the adjusted R square value was 0.978 and a p-value of (0.000) was significant. This means that 97.8% of the variation in profitability was caused by the variation in the account inventory days of holding.

Table 4.6: Regression between Effects of Inventory Holding and Profitability SMEs

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>Change Statistics</th>
<th>Change Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>R Square Change</td>
<td>F Change</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>df1</td>
<td>df2</td>
</tr>
<tr>
<td>1</td>
<td>.989a</td>
<td>.979</td>
<td>.978</td>
<td>.16587</td>
<td>.979</td>
<td>992.723</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Funds are set aside for reorder, Reviews inventory, Economic Order Quantity, length of inventory, inventory control, accurate inventory, longer inventory
An ANOVA analysis was done between effects of inventory days of holding and profitability at 95% confidence level, the F critical was 992.723 and the P value was (0.000) therefore significant the results are shown in table 4.15 below.

**Table 4.15: ANOVA of Inventory Holding and Profitability SMEs**

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>191.189</td>
<td>7</td>
<td>27.313</td>
<td>992.723</td>
<td>.000b</td>
</tr>
<tr>
<td>Residual</td>
<td>4.154</td>
<td>151</td>
<td>.028</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>195.344</td>
<td>158</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Dependent Variable: performance  
b. Predictors: (Constant), Funds are set aside for reorder, Reviews inventory, Economic Order Quantity, length of inventory, inventory control, accurate inventory, longer inventory

**4.4.3 Coefficient of Inventory Day of Holding on Organizational Profitability**

A Pearson correlation was done between profitability (dependent variable) against other factors of inventory day of holding. The results of the regression coefficients, t-statistics, standard errors of the estimates and p values are shown in table 4.16.

When organizational profitability was predicted on inventory days of holding(Constat p value=0.049), business reviews inventory levels periodically (Beta=0.040,p value=0.273),the business keeps accurate inventory records (Beta= -.219, p value=0.000), the business has installed an inventory control system (Beta = 0.187, p value=.000), longer inventory holding period has a negative effect on profitability of SMEs (Beta=0.211,p value=0.000), The length of inventory holding period (Beta=0.485,p value = 0.000), business should set Economic Order Quantity (EOQ) to ensure adequate (Beta=0.205, p value=0.000), business reviews inventory levels periodically (Beta=0.118,p value = 0.022).
<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
</tr>
<tr>
<td>1</td>
<td>.289</td>
<td>.145</td>
</tr>
<tr>
<td></td>
<td>.051</td>
<td>.046</td>
</tr>
<tr>
<td></td>
<td>-.320</td>
<td>.066</td>
</tr>
<tr>
<td></td>
<td>.149</td>
<td>.034</td>
</tr>
<tr>
<td></td>
<td>.251</td>
<td>.054</td>
</tr>
<tr>
<td></td>
<td>.465</td>
<td>.038</td>
</tr>
<tr>
<td></td>
<td>.206</td>
<td>.034</td>
</tr>
<tr>
<td></td>
<td>.132</td>
<td>.057</td>
</tr>
</tbody>
</table>

From the analysis above, all the account inventory days of holding variables had a significant positive effect on organizational profitability except the variable business keeps accurate inventory records (Beta=-.219).
4.5 Effect of Accounts Payable on SME Profitability

The study sought to establish the accounts payable on the profitability SMES and the respondents were asked a number of questions that they were rating with the least being Strongly Disagree (1) and the highest being Strongly Agree (5).

4.5.1 Descriptive on Accounts Payable on SME Profitability

To analyze the descriptive statistic most respondents agree that the business is sometimes unable to pay its suppliers on time with a mean of (3.57), this was followed by the business receives cash discounts from its suppliers upon payment within a stipulated period of time with a mean of (3.46). The variable with the least mean was the variable payment period allowed by suppliers to the firm was reasonable (3.05) as shown in table 4.17

**Table 4.8: Descriptive on Accounts Payable on SME Profitability**

<table>
<thead>
<tr>
<th>Variable</th>
<th>Mean</th>
<th>Standard deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>The business receives credit facilities from its suppliers</td>
<td>3.34</td>
<td>1.252</td>
</tr>
<tr>
<td>The business receives cash discounts from its suppliers upon payment within a stipulated period of time</td>
<td>3.46</td>
<td>1.578</td>
</tr>
<tr>
<td>The business is sometimes charged an interest by its suppliers for late payment</td>
<td>3.89</td>
<td>1.153</td>
</tr>
<tr>
<td>The business past debts have ever been waived by its suppliers</td>
<td>3.45</td>
<td>1.367</td>
</tr>
<tr>
<td>The business is sometimes unable to pay its suppliers on time</td>
<td>3.57</td>
<td>1.332</td>
</tr>
<tr>
<td>The payment period allowed by your suppliers to your firm is reasonable</td>
<td>3.05</td>
<td>1.431</td>
</tr>
</tbody>
</table>

4.5.2 Regression analysis between variables of Accounts Payable and Profitability

A regression analysis was done between variables of account payable on profitability of SMEs as shown in table 4.18. On analysis, the adjusted R square value was 0.979 and a p-
value of (0.000) was significant. This means that 97.9% of the variation in profitability was caused by the variation in the account payable.

Table 4.9: Model Summary on Accounts Payable and Profitability

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>Change Statistics</th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>.990\textsuperscript{a}</td>
<td>.979</td>
<td>.979</td>
<td>.16326</td>
<td>R Square Change</td>
<td>.979</td>
<td>1193.956</td>
<td>6</td>
</tr>
</tbody>
</table>

Dependent Variable (profitability).

4.5.3 Coefficients of variables of Accounts Payable and Profitability

A Pearson correlation was done between profitability (dependent variable) against other factors of accounts payable. The results of the regression coefficients, t-statistics, standard errors of the estimates and p values are shown in table 4.19.

When organizational profitability was predicted on accounts payable (Constant p value=0.000), the variables business receives credit facilities from its suppliers (Beta=.437, p value=0.000), the business receives cash discounts from its suppliers upon payment within a stipulated period of time (Beta=-0.043, p value= 0.336), the business is sometimes charged an interest by its suppliers for late payment (Beta=0.164, p value = 0.000), the business past debts have ever been waived by its suppliers (Beta=0.110, p value = 0.055), the business is sometimes unable to pay its suppliers on time (Beta=0.412, p value=0.000), the payment period allowed by your suppliers to your firm is reasonable (Beta= -0.070, p value=0.141).
## Table 4.19: Coefficients of Accounts Payable and Profitability

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>.434</td>
</tr>
<tr>
<td></td>
<td>The business receives credit facilities from its suppliers</td>
<td>.387</td>
</tr>
<tr>
<td></td>
<td>The business receives cash discounts from its suppliers upon payment within a stipulated period of time</td>
<td>-.030</td>
</tr>
<tr>
<td></td>
<td>The business is sometimes charged an interest by its suppliers for late payment</td>
<td>.158</td>
</tr>
<tr>
<td></td>
<td>The business past debts have ever been waived by its suppliers</td>
<td>.090</td>
</tr>
<tr>
<td></td>
<td>The business is sometimes unable to pay its suppliers on time</td>
<td>.345</td>
</tr>
<tr>
<td></td>
<td>The payment period allowed by your suppliers to your firm is reasonable</td>
<td>-.055</td>
</tr>
</tbody>
</table>

From the analysis all the variables had a significant positive effect on organizational profitability except the variable the payment period allowed by your suppliers to your firm is reasonable (Beta =-0.070). The business receives cash discounts from its suppliers upon payment within a stipulated period of time (-0.043), The business past debts have ever been waived by its suppliers (Beta=0.110).

### 4.6 Effect of Cash Conversion Cycle on Profitability

The study sought to establish cash conversion cycle on the profitability of SMES and the respondents were asked a number of questions that they were rating with the least being Strongly Disagree (1) and the highest being Strongly Agree (5).
4.6.1 Descriptive Statistics Cash Conversion Cycle on Profitability

To analyze the descriptive statistic on the variables of cash conversion cycle the variable the firm regularly budget for the future expenditure had the highest mean of 4.03. The business has had operations related challenges due to lack of funds (3.99), availability of cash affects the firms profitability (3.85). The variable with the lowest mean was business has witnessed a lack of sufficient inventory (3.24).

Table 420: Descriptive Statistics on Cash Conversion Cycle

<table>
<thead>
<tr>
<th>variable</th>
<th>Mean</th>
<th>Standard deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>The business generates sufficient cash</td>
<td>3.43</td>
<td>1.230</td>
</tr>
<tr>
<td>The business receives timely payments from debtors</td>
<td>3.46</td>
<td>1.207</td>
</tr>
<tr>
<td>The business has had operations related challenges due to lack of funds</td>
<td>3.99</td>
<td>.994</td>
</tr>
<tr>
<td>Availability of cash affects the firms profitability</td>
<td>3.85</td>
<td>1.089</td>
</tr>
<tr>
<td>The business has witnessed a lack of sufficient inventory</td>
<td>3.24</td>
<td>1.287</td>
</tr>
<tr>
<td>The firm is able to meet its short term obligations</td>
<td>3.28</td>
<td>1.202</td>
</tr>
<tr>
<td>The business has a cash management system</td>
<td>2.99</td>
<td>1.458</td>
</tr>
<tr>
<td>The firm maintains sufficient cash balances for operations</td>
<td>3.79</td>
<td>1.155</td>
</tr>
<tr>
<td>The firm regularly budget for the future expenditure</td>
<td>4.03</td>
<td>1.087</td>
</tr>
</tbody>
</table>

4.6.2 Regression analysis between variables of Cash Conversion Cycle and Profitability

A regression analysis was done between variables of cash conversion cycle on profitability of SMEs as shown in table 4.21. On analysis the adjusted R square value was 0.996 and a p-value of (0.000) was significant. This means that 99.6% of the variation in profitability was caused by the variation in the cash conversion cycle.
Table 4.101: Model Summary on Cash Conversion Cycle and Profitability

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>R Square Change</th>
<th>F Change</th>
<th>df1</th>
<th>df2</th>
<th>Sig. F Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.998</td>
<td>.996</td>
<td>.996</td>
<td>.06971</td>
<td>.996</td>
<td>4004.489</td>
<td>10</td>
<td>148</td>
<td>.000</td>
</tr>
</tbody>
</table>

4.6.3 Coefficients of Cash conversion Cycle and Profitability

A Pearson correlation was done between profitability (dependent variable) against other factors of cash conversion cycle. The results of the regression coefficients, t-statistics, standard errors of the estimates and p values are shown in table 4.22.

When organizational profitability was predicted on cash conversion cycle (Constant p value=0.286), the business generates sufficient cash (Beta=0.122, pvalue 0.000), the business receives timely payments from debtors (Beta=0.281, pvalue 0.000), the business has had operations related challenges due to lack of funds ( Beta=0.174, pvalue 0.000), availability of cash affects the firms profitability ( Beta=0.237, pvalue 0.000), the business has witnessed a lack of sufficient inventory ( Beta=0.249, pvalue 0.000), the firm is able to meet its short term obligations ( Beta=0.005, pvalue 0.828), the business has a cash management system (Beta=0.058, pvalue 0.017), the firm maintains sufficient cash balances for operations (Beta=-0.0361, pvalue 0.063), the firm regularly budget for the future expenditure (Beta=0.014, pvalue 0.419), the firm has total control over suppliers ( Beta=0.038, pvalue 0.147).
### Table 4.11: Coefficients of Cash conversion Cycle and Profitability

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>.030</td>
<td>.028</td>
<td>1.065</td>
</tr>
<tr>
<td></td>
<td>The business generates sufficient cash</td>
<td>.110</td>
<td>.018</td>
<td>.122</td>
</tr>
<tr>
<td></td>
<td>The business receives timely payments from debtors</td>
<td>.260</td>
<td>.022</td>
<td>.281</td>
</tr>
<tr>
<td></td>
<td>The business has had operations related challenges due to lack of funds</td>
<td>.195</td>
<td>.026</td>
<td>.174</td>
</tr>
<tr>
<td></td>
<td>Availability of cash affects the firms profitability</td>
<td>.242</td>
<td>.018</td>
<td>.237</td>
</tr>
<tr>
<td></td>
<td>The business has witnessed a lack of sufficient inventory</td>
<td>.216</td>
<td>.027</td>
<td>.249</td>
</tr>
<tr>
<td></td>
<td>The firm is able to meet its short term obligations</td>
<td>.005</td>
<td>.023</td>
<td>.005</td>
</tr>
<tr>
<td></td>
<td>The business has a cash management system</td>
<td>-.044</td>
<td>.018</td>
<td>-.058</td>
</tr>
<tr>
<td></td>
<td>The firm maintains sufficient cash balances for operations</td>
<td>-.034</td>
<td>.018</td>
<td>-.036</td>
</tr>
<tr>
<td></td>
<td>The firm regularly budget for the future expenditure</td>
<td>.015</td>
<td>.018</td>
<td>.014</td>
</tr>
<tr>
<td></td>
<td>The firm has total control over suppliers</td>
<td>.029</td>
<td>.020</td>
<td>.038</td>
</tr>
</tbody>
</table>

From the findings all variables had a positive beta except the variables the business has a cash management system (Beta= -0.058, p value 0.017) and the firm maintains sufficient cash balances for operation (Beta = -0.036, pvalue 0.063).
4.7 Chapter Summary

This chapter has presented the interpreted results and findings. The first section provided an analysis of the various demographic data on the respondents. The second section analyzed the findings how accounts receivables put an effect on the profitability. The third section provided findings on how inventory holding period affect profitability. The fourth section presented effect of accounts payable on profitability while the fifth effect analyzed effect of cash conversion cycle on profitability. Inferential analyses are also presented. The next chapter will discuss the findings, conclusions and recommendations.
CHAPTER FIVE

5.0 DISCUSSION, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter offers the summary and deliberations on the results of this study as well as descriptions and significance to related literature. This chapter dissects the effect of working capital management on profitability of small and medium-sized enterprises, the conclusion, and the recommendation are presented according to the specific research questions.

5.2 Summary

The main purpose of this study was to examine the effects of working capital management on profitability in small and medium sized enterprises in Nairobi. In order to realize this, four research questions guided the process. These were how does accounts receivables put an effect on the profitability of small and medium-sized enterprises in Nairobi? How does inventory-holding period put an effect on the profitability of small and medium-sized enterprises in Nairobi? What is the effect of accounts payable on small and medium-enterprises profitability in Nairobi? What is the effect of cash conversion cycle on small and medium-enterprises profitability in Nairobi? To realize this, a descriptive research design was adopted.

The total population of this study comprised of all registered small and medium sized enterprises in Nairobi with the Federation of Small and micro enterprises estimated at one thousand six hundred from which using a stratified random sampling a sample size of one hundred and sixty. Data was collected using structured questionnaire with the assistance of trained research assistants. Using SPSS a regression analysis was carried out between the dependent variable and all other variables and an ANOVA analysis was undertaken to determine the differences in means between the variables.

To analyze the effects of accounts receivables on the profitability SMES the study confirmed that the business screens customers or clients reference before giving credit and it was also revealed that the business enterprise monitors accounts receivables and analyses reports on debtors. A Pearson correlation done between profitability (dependent variable) against other factors of account receivable revealed a positive and significant
relationship. To analyze the impacts of inventory holding on the profitability, it was revealed that the business keeps accurate inventory records and also ensures funds are set aside for reorder, there was uncertainty on whether the length of inventory holding period has a material impact on the profitability and if business should set Economic Order Quantity (EOQ) to ensure adequate stocks are maintained. From the regression analysis, all the account inventory days of holding variables had a significant positive effect on organizational profitability except if the business keeps accurate inventory records.

To analyze the effects of accounts payable on profitability the study revealed uncertainty on business sometimes being unable to pay its suppliers on time and if it receives cash discounts from its suppliers upon payment within a stipulated period of time, a regression analysis showed that all the factors of accounts receivable had a significant positive effect on organizational profitability except the issues of payment period allowed by suppliers to the firm, and cash discounts from suppliers upon payment within a stipulated period of time, there was also a negative relation on business past debts being waived by suppliers.

To analyze the effects of cash conversion cycle on profitability the research established that the firms’ regularly budget for the future expenditure, however some issues were not clear and this involved the business having operations related challenges due to lack of funds, and whether the availability of cash affects the firm’s profitability. From the regression analysis, all variables had a positive relation except if the business has a cash management system and the firm maintains sufficient cash balances for operation.

5.3 Discussions

5.3.1 Effects of Accounts Receivables on Profitability of Small and Medium Enterprises

From the analysis sales on credit, business credit policy, customers screening, monitors accounts receivables all had a significant positive effect on organizational profitability. Most of the respondents were uncertain that the business offers some sales on credit and this contradicts the findings by Dellannay and Weill (2004) who noted that accounts receivables decrease the operational costs. In fact, accounts receivable increments lead to working adaptability. While undoing the credit terms, suppliers can decrease the stockpiling costs for unverifiable demands of stocks and the expenses of changing their produce levels when demands shift (García & Martínez, 2010).
Seemingly, most of the respondents agree that the business has in place a credit policy and according previous reviewed literature study, SMEs in Nairobi use accounts receivable to support deals all the while. Lazaridis and Tryfonidis (2006) prescribes that SMEs use accounts receivables rather than direct cost deterioration to build deals particularly amid times of low finances. Essentially, Dellannay and Weill (2004) suggests that when SMEs deals are sensitive to the interest changes, accounts receivables is a particularly imperative technique to invigorate clients to secure stocks in a time of low demands. Moreover, as per Welner (2000), accounts receivables can be utilized as value separation between the money and the clients. This will be beneficial at whatever point the flexibility of the demands of money clients surpasses that of credit clients or at whatever point money clients’ reservation costs are efficiently greater than those of credit clients (Berglof & Bolton, 2002).

The findings however revealed that the business screens customers or clients reference before giving credit. This is a precaution taken and Harris (2005) brings out the point that interest revenue is another reason that suppliers gain income from accounts receivables. When the inherent rate of profit grossed for accounts receivable exceeds that of the marginal share, suppliers would have premiums to offer accounts receivable to their clients (Dellannay and Weill, 2004). According to Welner (2000), this is important as the account receivables assist SMEs to build up a steady business relationship in due course. He further states that accounts receivables may expand clients’ reliance on their suppliers, which may bring about a greater interest rate. This contention is likewise bolstered by the asset reliance theory, asserting that SMEs may have inconveniences to get to every basic asset, and they depend on suppliers to offer fractional basic assets (Kwame, 2007).

Accordingly, Wilson and summers (2002) claim a non-monotonic (inward) correlation between accounts receivables and SMEs value. They explain that specific levels of accounts receivables can actually boost the SME value. Nonetheless, there is no observational consummation to bolster this theory. By complexity, Hill and Lockhart (2012) examine more than 10,000 SMEs amid the timeframe of 1973-2006, and they discover that there is a direct positive correlation between shareholders worth and accounts receivables. Moreover, Moyer, McGuigan, and Kretlow (2005) expound on how accounts receivables affects SMEs execution. They analyze the non-monetary Belgian SMEs amid the timeframe of 2006-2009 and they inferred that SMEs, which expanded
accounts receivables within the 2008 budgetary crisis that were contrasted with pre-crisis times, have a generally greater productivity within the crisis years.

The study also revealed that the business enterprise monitors accounts receivables and analyses reports on debtors aging. The supply of trade credit is usually utilized by SMEs as a marketing instrument to increase or uphold sales (Pandey, 2004). Proficient receivables management boosted by a reduced creditor’s collection timeframe, minimal levels of bad debts and a vibrant credit program regularly enhances the organizations’ capacity to draw in new clients and likewise increase the fiscal performance thus the necessity for a vibrant credit program that will guarantee that the SMEs’ worth is heightened (Ross, Westerfield, and Jordan, 2003). As noted by Lazaridis, and Tryfonidis (2006) in their research, an expansion in the level of accounts receivables in a company boosts both the net working capital and the expenses of holding and overseeing accounts receivables and both may prompt a decline in the value of the firm. A research conducted by Lazaridis and Dimitrios (2005) discovered that organizations which seek after increased levels of accounts receivables to an ideal level build their profitability due to a growth in market share and sales.

The research revealed inconsistency on the availability a credit collection policy in the SMEs, this differed with the findings from Martínez-Solano (2014) study which established the correlation amongst profitability and accounts receivables with over 71,000 SMEs in Spain within the timeframe of 2000-2007. They discover a positive direct correlation between investment in accounts receivables and SME productivity. Similarly, because of the intense market rivalry, SMEs are compelled to offer accounts receivables.

5.3.2 Effects of Inventory Holding Period on the Profitability of Small Enterprises

From the study majority agree that the business reviews inventory levels periodically. Studied indicate that keeping up ideal stock levels decreases the expense of conceivable intrusions and keeps loss of business emerging from lack of items. It additionally lessens supply costs also, secures against value vacillations. Setting the right stock holding period is the primary objective of stock administration. A study to research the ideal stock levels was completed by Swaminathan (2001), in which the study discovered that modifying crude materials and completed merchandise as a segment of stock is speedier than the stock as a whole to achieve the sensible levels. Autu, Kaite and Molay (2011) discovered
that there are some different techniques that can ease stock administration, for example, request amount technique and without a moment to spare inventories. Observational studies have demonstrated that stock transformation period negatively affects a business’ performance. For example, shortening the stock change period could expand stock out expenses of stock, which results in losing deals opportunities and leads to poor performance (Deloof, 2003). Administrators of SMEs ought to in this manner keep their stock to an ideal level since an error of stock will prompt tying up overabundance capital to the detriment of beneficial operations (Dimitrios & Koumanakos 2008).

It was also discovered that the business keeps accurate inventory records and similar findings by Dimitrios and Koumanakos (2008) indicated that keeping an excess of stock could request more physical space, could prompt a monetary loss, and expansions the likelihood of inventories harms, crumbling and losses. In addition, holding vast measure of stock regularly demonstrates wasteful and imprudent administration practices and systems. On the other hand, too little inventories may prompt the intrusion of operation in assembling, expand the likelihood of losing deals and therefore bring down the profitability of the SMEs. Singh (2008) concentrated on the relationship between stock administration and working capital administration concentrating on the significance of stock administration.

The findings show that most of business has installed an inventory control system in place and this is important, as studies have shown that for stock administration to be powerful, somebody must be in charge of setting suitable arrangements, setting up suggested stock levels, and guaranteeing that control frameworks are working legitimately. Bonin and Wachtel (2003) indicate that with stock control, despite the fact that managers actualize the techniques and guarantee that staff are doing them; they should comprehend the explanations for the arrangements and methodology. For instance, an arrangement to screen stock levels is set up in light of the fact that inadequate stock cut off point’s deals and over the top inventories tie up cash that might be required elsewhere in the store. It is imperative that the managers mentor their team about inventory control. They further indicated that notwithstanding knowing the purposes behind the techniques, it is the managers’ responsibility to guarantee that their staff to likewise comprehend the significance of precise stock control. They have to comprehend the effect of their errors and work towards disposing of them quite far. Stock developments in stock movements are a consistent action in retailing. Stock must be moved in the most proficient route
conceivable by taking after the store’s arrangement and continually considering the costs included. Agrawal and Smith, (1996) as cited by Korobow (2012) notes that, stock administration is imperative since it helps in keeping up an exchange off between conveying expenses and requesting costs which would imply that it will minimize the aggregate expense of stock.

A regression analysis was done between variables of inventory day of holding and profitability of SMEs and a p-value of was significant, this means that 97.8% of the variation in profitability was caused by the variation in the account inventory days of holding. Singh (2008) discovered that organizations with a poor stock administration could bring about difficult issues, which demolish the long haul profitability and SMEs survival shots. Likewise, SMEs with well-thought stock administration can lessen the stock to an ideal level, which has no negative impact on generation and deals. The concentrate likewise demonstrates that the extent of stock specifically influences the working capital and its administration.

5.3.3 Effect of Accounts Payable on Small and Medium-Enterprises

From the findings, there was uncertainty on business receiving credit facilities and cash discounts from its suppliers. This was not in line with the findings by Autukaite & Molay (2011) who discovered in their research that accounts payables is a proficient way to deal with the SMEs money related gratings in short term. Considering the restricted informational openness, financial institutions are hesitant to provide debts to SMEs or they require high loan costs to repay high risks (Bonin and Wachtel, 2003). Accounts payables can be more available, particularly over the time of a tight money related strategy. Within the time of a tight financial approach, clients will probably change to accounts payables because around that time the compelling loan interests exceed the prevailing expenses of accounts payables. This is because of the way that the accounts payables terms are generally steady, which implies that certain financing costs are predictable. In the meantime, the interest costs of bank loans are expanding during a tight fiscal period, which prompts more costly expenses of bank loans than that of accounts payables SMEs, lessening the expenses from the raising capital, will gain more profitability (Bonin & Wachtel, 2003).

Most of the respondents agreed the business is sometimes charged an interest by its suppliers for late payment. Falope and Ajilore (2009) discovered that postponing
payments to suppliers enables organizations to survey the nature of the items that were purchased and this can be an economical and adaptable wellspring of financing. In any case, managers ought to know that late payment can have certain high expenses at whatever point early payment discounts are accessible. Since cash is additionally secured up working capital, the more the investment in current assets, the lesser the risk and the lower the profitability achieved.

The study revealed that the payment period allowed by suppliers to the firm was a reasonable one. Accounts payables is utilized as a mechanism that stands as a payment or predetermined substitute to quick financial use. It lessens uncertainty by means of business pooling. With the uncertain supply for instance, volume and timing of cash streams are uncertain in the stream of the merchandise. Cash should be carried and arranged in a complete transaction procedure. This stochastic cash shows high holding expenses and opportunity costs (Martinez-Sola et al, 2013). By disposing of these expenses by means of accounts payables, the operational revenue is more possible and adaptable in the transaction and clients can contribute cash on other high rate of return initiatives to maintain profitability.

Furthermore, accounts payables are utilized as an assessment instrument too for clients to evaluate the nature of the product. Martinez-Sola, et al (2013) states that, the purpose of extending the payment to purchasers is to check the nature of the product. Purchasers can decline the payment process if products have quality issues, which causes lesser transaction costs. Consequently, purchasers settle on obtaining choices as indicated by credit terms and different states of accounts payables.

5.3.4 Effect of Cash Conversion Cycle on Profitability of Small and Medium Enterprises

There was uncertainty on how whether the business generates sufficient cash and if business receives timely payments from debtors. This is a serious problem when it comes to a firm’s liquidity position. Through the ordinary course of a business, firms are able to acquire inventory on credit, which they utilize to generate products, these are then sold in cash or credit. These actions give rise to accounts payable and receivable, until the firm collects cash from accounts receivable and settles the payable accounts(Muscettola, 2014). According to research an institution that fail to settle its credits and short term liabilities on time may suffer from operations related challenges and this may certainly
ruin its reputation. When a firm lack cash or liquid assets at its disposal this may result into it missing some of the benefits that would have been offered to them by the suppliers. The loss incurred from missing these incentives may lead to high cost of goods thus affecting the firms’ profitability. This therefore calls for the institution to regularly maintain some level of liquidity (Singha, Gupta, & Sharma, 2015).

Most of the respondents admitted that the business has had operations related challenges due to lack of funds and that availability of cash affects the firms’ profitability. Empirically among the studies done on the impact of CCC on a firm’s performance, Lazaridis and Tryfonidis (2006), research in Greece observed that there exist a connection between working capital management and profitability and this was attributed to the efficient management of the cash conversion cycle. With an effort to expound on Lazaridi’s and Tryfonidis’s (2006) findings, Gill, Biger and Mathur (2010) study on 88 American firms listed on New York Stock Exchange for the period 2005 to 2007 established a significant statistical association between the cash conversion cycle and profitability. They further concluded that managers had the capability to create profits by efficiently handling the cash conversion cycle and maintaining accounts receivables at an optimal level. According to Costa (2014) study on cash conversion, cycle across industries the findings reveal that CCC differs between firms due to the size, and accounting process.

There was uncertainty on whether the business has witnessed a lack of sufficient inventory and being able to meet its short-term obligations. According to Van Horne (2000), a firm with excess amount of current assets may face low return on investment because of the cash being held up. On the other hand, those with low current assets may incur shortages and experience challenges in operations. It is on this paradigm that it is recommended for firms to maintain optimum level of liquidity and profitability. Hamza, Mutala and Antwi (2015) highlight that an institution should be in a position to generate sufficient cash to be sustain its immediate obligations to be able to trade. Cash management is considered among the main aspects that determine the efficiency of working capital this involves planning and controlling of all cash flows from and into the business. (Weston & Copeland, 2008).

Additionally most business were also uncertain of the existence of a cash management system. A study by Costa (2014) highlighted that cash management is geared towards
optimization of the available cash to maximize the level of earnings, and amount of cash held by the firm incurs an opportunity cost as such funds would have been invested in more productive projects. On the contrary, a firm needs to strike a balance between having too much or too little cash. Operating with very little cash balances increases the firm’s financial risk for being unable to meet their obligation as they fall due. Efficient cash management practices involves not only the determination optimal cash to hold but also planning and monitoring of available cash flows.

While analysing if the firm maintains sufficient cash balances for operations and regular budget expenditure, most of the respondents agreed. According to Many small enterprises lack data on the estimated future cash inflows and they never budget or plan for the expected funds. This directly affects the future survival and sustainability of the enterprises. According to Nick (2009) findings, it was revealed that enterprises, which regularly budget for the future once a month, increase their chance of survival by up to 80%. He also points out that small businesses assume that cash flow problems are automatically solved by increased growth in the future. Mong (2011) established that few small businesses create a cash budgets despite the importance of cash forecasting as a tool for efficient cash management.

Similarly Kwasi (2010), research in 11 Ghanaian Oil market firm to analyse the trends in working capital management and impact on their performance in a seven year period from 2001, he established the existence of a high variability of working capital and a negative relation between profitability and other factors of the CCC. Ching, Novazzi, and Gerab (2011) study of Brazilian listed companies to establish variability between corporate groups that undertake working capital intensive and fixed capital intensive policies for the period 2005 to 2009, the finding revealed similar results for the two groups of companies. According to Uyar (2009) research in Taiwanese firms to examine how profitability and size of companies impacted on working capital, the results suggested an existence of a negative relationship between a firms size and profitability and cash conversion cycle. Wilson (2009) on the other hand investigated how firms with a well-established financial management system impacted on Working capital management and the results showed that a firms size, debt ratio, and growth affected the management of Working capital.
5.4 Conclusion

5.4.1 Accounts Receivables put an Effect on the Profitability of SMEs

For effective performance, the firms need to have a well-maintained record of account receivable. The findings of the study reveal that most of SMEs in Nairobi have a well-established has credit policy. Additionally it was also revealed that most of these firms are able to do a thorough screens customers or client’s reference before giving credit. This is as a way of mitigating credit risks associated with credit sales. Most of the business enterprises also monitor accounts receivables and analyze reports on debtors.

5.4.2 Inventory Holding Period put an Effect on the Profitability of SMEs

Inventory holding period is a very important aspect in the cash conversion cycle and most of the SMEs in the Nairobi perform a regular review of its inventory levels, this was also accompanied by the businesses keeping accurate inventory records. The firms are also aware of the negative implications of a longer inventory-holding period on the profit margins. It was also established that most of them ensure funds are set aside for reorder.

5.4.3 Accounts Payable Affect Profitability of SMEs

The SMEs need to maintain a good relationship with the creditors and from the study it was apparent uncertain on whether the business are able to negotiate for cash discounts from its suppliers upon payment within a stipulated period, or if the business is sometimes charged an interest by its suppliers for late payment. Other issues that arise are also that most of the SMEs have no evidence concerning their past debts being waived by its suppliers nor being unable to pay its suppliers on time.

5.4.4 Cash Conversion Cycle Affect Working Capital Management of SMEs

Maintaining the cash conversion cycle seem to be an issue and this is apparent from the fact that the businesses have had operations related challenges due to lack of funds. Such issues have also influenced the profitability. Most of the firms have also apparently taken measures such as maintaining sufficient cash balances for operations and regularly budgeting for the future expenditure.
5.5 Recommendation

5.5.1 Recommendation for Improvement

5.5.1.1 Accounts Receivables put an Effect on the Profitability of SMEs

The business offers some sales on credit and by doing so; the firms are able to give the debtors option to get the products. However, there is a need for the firms to have an up to date credit collection policy in place. The firms also need to have some form of measures to determine the individual. It is also essential to undertake a thorough credit checks on all customers and create a clear outlined payment guideline such as indicating when payment is due and the specific contact persons.

5.5.1.2 Inventory Holding Period put an Effect on the Profitability of SMEs

From the study, most of the respondents are indifference when questioned on the negative effect of a longer inventory-holding period on profitability. It is therefore necessary to ensure that the SMEs are educated on such effects on the performances. Additionally another issue that arise is the levels of the Economic Order Quantity (EOQ) as such there is also a need for education and awareness.

5.5.1.3 Accounts Payable Affect Profitability of SMEs

The firms need to encourage credit transactions with suppliers over the use of cash; this will enable the firms use the cash available for other purposes. In addition, there is a need to create cash discounts agreements with suppliers upon payment of dues within a stipulated period of time and this should be a reasonable one for the firms benefit.

5.5.1.4 Cash Conversion Cycle Affect Working Capital Management of SMEs

The business have to find a means of generating sufficient cash for their sustainability and this could involve acquiring goods on credit or even seeking funding. The business should also seek to maintain sufficient inventory as failure lead to lost sales and customer loyalty. The firm also need to be able to meet short-term obligations when they fall due and this can only be possible through maintaining a cash management system that works.

5.5.2 Recommendation for Further Studies

The study focused only on working capital management on profitability of small and medium-sized enterprises in Nairobi, it is recommended that other studies be done to
determine how working capital management affect overall financial health of any company.

The study only focused firms in Nairobi and therefore this result are skewed towards the perceptions and data from SMEs in Nairobi. It is suggested therefore that such a study be done in other towns to make the results more reliable.
REFERENCES


Anichebe, N. A. & Agu, O. A. (2013). Effect of Inventory Management on Organizational Effectiveness. Information and Knowledge Management, 3 (8), 92 – 100


APPENDIX A: QUESTIONNAIRE

SECTION A: GENERAL INFORMATION

1. **What is your Gender?**  Male □  Female □

2. **What is your highest level of education?**

   Certificate □  Diploma □  Degree □
   Post graduate Diploma □  Masters □  Others □

3. **What is your age range?**

   Less than 25 years □  26-35 years □  36-45 Years □  46 years and over □

4. **Are you the owner of the business?**  Yes □  No □

5. **Number of years the business has been in operation**

<table>
<thead>
<tr>
<th>Years</th>
<th>Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 3 years</td>
<td>1</td>
</tr>
<tr>
<td>3 – 6 years</td>
<td>2</td>
</tr>
<tr>
<td>7-10 years</td>
<td>3</td>
</tr>
<tr>
<td>11- 14 years</td>
<td>4</td>
</tr>
<tr>
<td>15 years and over</td>
<td>5</td>
</tr>
</tbody>
</table>

6. **Nature of the Business/Operations**

<table>
<thead>
<tr>
<th>Category</th>
<th>Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>Commercial and Trade</td>
<td>1</td>
</tr>
<tr>
<td>Service</td>
<td>2</td>
</tr>
</tbody>
</table>

7. **Please indicate the number of employees in your enterprise**

<table>
<thead>
<tr>
<th>Range</th>
<th>Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 5</td>
<td></td>
</tr>
<tr>
<td>5-10</td>
<td></td>
</tr>
<tr>
<td>11- 30</td>
<td></td>
</tr>
<tr>
<td>31- 50</td>
<td></td>
</tr>
<tr>
<td>Over 50 employees</td>
<td></td>
</tr>
</tbody>
</table>

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SECTION B: ACCOUNTS RECEIVABLES PUT AN EFFECT ON THE PROFITABILITY OF SMALL AND MEDIUM-SIZED ENTERPRISES

What is your level of agreement to the following statements on the effects of accounts receivables on the profitability of small and medium-sized enterprises? (5- Strongly agree, 4- Agree, 3-Neutral, 2-Disagree, 1- Strongly Disagree)

<table>
<thead>
<tr>
<th>Statement</th>
<th>Strongly Disagree</th>
<th>Disagree</th>
<th>Neutral</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>1  The Business offers some sales on credit</td>
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<tr>
<td>2  The business has in place a credit policy</td>
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<tr>
<td>3  The business most debtors stick to the credit period</td>
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<tr>
<td>4  The business screens customers or clients reference before giving credit</td>
<td></td>
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<tr>
<td>5  The Business enterprise monitors accounts receivables and analyses and reports on debtors aging</td>
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<tr>
<td>6  There is a credit collection policy in place</td>
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</tbody>
</table>
SECTION C: THE EFFECT OF INVENTORY HOLDING ON THE PROFITABILITY OF SMALL AND MEDIUM-SIZED ENTERPRISES

On a scale of 1-5 where; 1-Strongly Disagree; 2-Disagree; 3-Neutral; 4-Agree; and 5-Strongly Agree, indicate the extent that you believe relating to the effect of inventory holding period on the profitability of small and medium-sized enterprises.

<table>
<thead>
<tr>
<th>Statement</th>
<th>Strongly Disagree</th>
<th>Disagree</th>
<th>Neutral</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>1  The business reviews inventory levels periodically</td>
<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>2  The business keeps accurate inventory records</td>
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<tr>
<td>3  The business has installed an inventory control system</td>
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<tr>
<td>4  A longer inventory holding period has a negative effect on profitability of SMEs</td>
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<tr>
<td>5  The length of inventory holding period has a material impact on the profitability of SMEs</td>
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<tr>
<td>6  The Business should set Economic Order Quantity (EOQ) to ensure adequate stocks are maintained.</td>
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<tr>
<td>7  The Business ensures funds are set aside for reorder</td>
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</tbody>
</table>
SECTION D: THE EFFECT OF ACCOUNTS PAYABLE ON SMALL AND MEDIUM-ENTERPRISES PROFITABILITY IN NAIROBI

What is your level of agreement to the following statements in relation to the effect of accounts payable on small and medium-enterprises profitability in Nairobi? (5- Strongly agree, 4- Agree, 3-Neutral, 2-Disagree, 1- Strongly Disagree)

<table>
<thead>
<tr>
<th>Statement</th>
<th>Strongly Disagree</th>
<th>Disagree</th>
<th>Neutral</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>1  The business receives credit facilities from its suppliers</td>
<td></td>
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<tr>
<td>2  The business receives cash discounts from its suppliers upon payment within a stipulated period of time</td>
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<tr>
<td>3  The business is sometimes charged an interest by its suppliers for late payment</td>
<td></td>
<td></td>
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<td></td>
<td></td>
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<tr>
<td>4  The business past debts have ever been waived by its suppliers</td>
<td></td>
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<tr>
<td>5  The business is sometimes unable to pay its suppliers on time</td>
<td></td>
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<tr>
<td>6  The payment period allowed by your suppliers to your firm is reasonable</td>
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</tbody>
</table>
SECTION E: THE EFFECT OF CASH CONVERSION CYCLE ON SMALL AND MEDIUM-ENTERPRISES PROFITABILITY IN NAIROBI

What is your level of agreement to the following statements in relation to the effect of Cash conversion cycle on small and medium-enterprises profitability in Nairobi? (5-Strongly agree, 4- Agree, 3-Neutral, 2-Disagree, 1- Strongly Disagree)

<table>
<thead>
<tr>
<th>Statement</th>
<th>Strongly Disagree</th>
<th>Disagree</th>
<th>Neutral</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>1  The business generates sufficient cash</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2  The business receives timely payments from debtors</td>
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<tr>
<td>3  The business has had operations related challenges due to lack of funds</td>
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<tr>
<td>4  Availability of cash affects the firms profitability</td>
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</tr>
<tr>
<td>5  The business has witnessed a lack of sufficient inventory</td>
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<tr>
<td>6  The firm is able to meet its short term obligations</td>
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<tr>
<td>7  The business has a cash management system</td>
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<tr>
<td>8  The firm maintains sufficient cash balances for operations</td>
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<tr>
<td>9  The firm regularly budget for the future expenditure</td>
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<tr>
<td>10 The firm has total control over suppliers</td>
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</tbody>
</table>
**SECTION F: SMALL AND MEDIUM-ENTERPRISES PROFITABILITY IN NAIROBI**

What is your level of agreement to the following statements in relation to small and medium-enterprises profitability in Nairobi? (5- Strongly agree, 4- Agree, 3-Neutral, 2- Disagree, 1- Strongly Disagree)

<table>
<thead>
<tr>
<th>Statement</th>
<th>Strongly Disagree</th>
<th>Disagree</th>
<th>Neutral</th>
<th>Agree</th>
<th>Strongly Agree</th>
</tr>
</thead>
<tbody>
<tr>
<td>1  Cash cycle has an impact on the firms ROE</td>
<td></td>
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<tr>
<td>2  Accounts payable has an impact on the firms leverage</td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>3  Accounts receivable has an impact on the firms profitability</td>
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</tr>
<tr>
<td>4  Long inventory holding days has an impact on the firms net profit</td>
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</tr>
<tr>
<td>5  Too much account receivable has an effect on the firms ROA</td>
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</tr>
</tbody>
</table>