ANALYSIS ON THE EFFECT OF INTERNAL FACTORS ON THE FINANCIAL PERFORMANCE OF FIRMS IN THE CEMENT MANUFACTURING INDUSTRY IN KENYA

BY

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UNITED STATES INTERNATIONAL UNIVERSITY-AFRICA

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STUDENTS 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: ________________________

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

Signed: ________________________        Date: ________________________

Dr: Amos Njuguna

Signed: ________________________        Date: ________________________

Dean, Chandaria School of Business
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ABSTRACT
The purpose of this study was to evaluate the effect of internal factors on the financial performance of firms in the cement manufacturing industry in Kenya. The study has answered the following questions: How does ownership structure influence the financial performance of cement manufacturing firms in Kenya? How does capital structure influence financial performances of cement manufacturing firms in Kenya? How does the size of the firm denoted by assets influence the financial performances of cement manufacturing firms in Kenya?

The correlation research design was used to describe the various variables of interest. The target population was the cement manufacturing companies that are listed on the Nairobi Security Exchange. A comparative study of two cement manufacturing companies that are listed on the Nairobi Security Exchange was conducted. Data was analyzed by use of a multivariate regression analysis of quantitative data in order to determine the effect of internal factor ratios on the financial performance.

The study has determined that internal factors and financial performance ratios were the driving force for cement manufacturing companies in relation to their financial health. Return on assets, return on equity and the return on sales were the key indicators of a firm’s financial performance while the debt to equity, debt ratio, long term debt to asset ratio, gearing ratio and the size of their fixed assets were effective indicators of their internal factors. The study also presented that ratios were effective representatives for the internal factors and financial performance of cement manufacturing companies. The predictive model comprising of ratios was found to be statistically significant to indicate the power of ratios on cement manufacturing companies’ financial performance using statistics to determine the level of significance. This study found that the Pearson correlation value was the strongest predictor of the how strong the correlation between the internal factors and financial performance was.

In relation to the size of fixed assets and its impact on financial performance Bamburi Cement Company had a significant negative relationship whereas EAPCC had a significant positive correlation between the size of their assets and their financial performance. In terms of the long term debt to asset ratio, EAPCC had a significant positive relationship with its financial performance whereas for Bamburi Cement Company was not significant.
EAPCC had a statistically significant negative relationship between its debt to equity, debt ratio and their gearing ratio and the size of their fixed assets and the firm’s financial performance, which implied that the organization should try and monitor the management of their capital structure. Bamburi Cement Company had a negligible relationship between its capital structure and the financial performance. This implied there was efficient management of its capital structure ratios.

The main recommendation from this study is that the cement manufacturing companies that are listed on the Nairobi Security Exchange should focus on the efficient management of their internal factors so as to produce consistent financial performance so as to keep the continuation of their business. Firms’ managers should wisely stick on their debt to equity ratio and the debt ratio so as to minimize their risk and to avoid bankruptcy. Firms’ managers should also monitor the relationship between internal factor ratios and the financial performance ratios. Especially the following ratios; gearing ratio, size of fixed assets, debt to equity ratio, debt ratio and the long term debt to asset ratio which have a significant impact on the financial performance.
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DEDICATION

Special thanks to my loving parents: Francis Zuriels Moturi and Zibiah Kemunto Moturi. My sisters Angela Moturi, Dr. Carolyne Moturi, Dr. Edna Moturi and Evelyne Moturi and my brothers William and Bryan Moturi whose encouraging words, and continued support ring in my ears throughout my studies. I dedicate this project and give special thanks to my brothers, sisters and nephews and nieces for being there for me throughout the entire masters’ programme. Special thanks to my mother and father for the tremendous support in all aspects, she’s been a blessing to me. This achievement would not have been happened without the support of The United States International University Lecturers, friends, and fellow students. I will forever stay remembering your contribution to this work.
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LIST OF ABREVIATIONS

DER or der: Debt to Equity Ratio

DR or dr: Debt Ratio

CMA: Capital Market Authority

NSE: Nairobi Security Exchange

ROA or roa: Return on Assets

ROE or roe: Return on Equity

ROS or ros: Return on Sales

SPSS: Statistical Package for Social Science
CHAPTER ONE

1.0. INTRODUCTION

1.1 Background of the Problem

The cement industry is usually referred to as the building block of a nation’s construction industry (Portland Cement Association, 2013). This is mainly due to the fact that there are very few construction projects that can occur without the use of cement in their design. Cement consumption is usually dependent on the time of year and the prevalent weather conditions (Portland Cement Association, 2013).

The construction industry which relies heavily on the use of cement in most of their activities, plays an important role in the economy since the actions of the industry play a vital role in the achievement of the country’s development goals in terms of providing shelter, infrastructure and employment (Ogunsemi, Aje, & Oladinrin, 2012). The services provided by the construction and engineering industry play a role in the economic growth and development of a country (Raza, 2008).

Globally, the cement and construction industry is considered to be the largest fragmented industry. It is estimated that the annual global cement production is around 4.6 billion tonnes which translated to a 6.3% increase when compared to the 4.3 billion tonnes that was recorded in 2014 (Association Européenne du Ciment The European Cement Association (CEMBUREAU), 2015). This is as a result of the increasing demand for cement in major emerging economies despite a global economic slowdown which occurred in the last quarter of 2015. The largest cement manufacturing country is China despite their economy experiencing a recession in the same year. Among the emerging economies the countries that experienced a growth in their cement production is Argentina and Saudi Arabia, while India suffered from a recession (Association Européenne du Ciment The European Cement Association (CEMBUREAU), 2015).

1.1.1 Financial Performance

Financial performance is usually referred to the analysis and interpretation of financial statements, it relates to the process of determining the financial strengths and weaknesses of a firm by establishing strategic relationships between line items in the balance sheet, profit and loss account and any other operative data. This allows the management of the company to be able to better understand the relationship between component parts of a
financial statement so as to better understand the position of the firm (Devi & Sabarinathan, February 2015). The main aim of financial analysis is to diagnose the information that is present in financial statements so as to accurately determine the profitability and financial soundness of the firm. In broader terms financial performance refers to the degree in which the financial objectives of a firm have been accomplished (Devi & Sabarinathan, February 2015).

The financial performance of companies is an issue that has garnered a lot of attention and interest from both financial enthusiasts, researchers and the general public as well as the management of corporate firms (Omondi 2013). The cement manufacturing industry acts as the driver of economic growth and especially in developing countries. The increasing phenomenon of globalization has made the concept of efficiency more important for manufacturing companies and cement firms are part of them. Cement manufacturing firms are usually dependent on their marketing and corporate strategies which determines their success and growth.

The financial performance of a company can be used a signaling tool to its shareholders, current and potential investors and creditors who want to provide capital to the firm. Carrying out performance analysis that is used for internal corporate purposes is different when compared to analysis that is done for the above mentioned group. This is a because analysis that is done for internal corporate purpose is to measure the managerial efficiency of the firm as well as to measure the utilization of various assets during the period among others (Walker, 2010). Factors affecting the financial performance of an organization are important since they can give a picture on which factors play a significant effect on whether a firm is able to make profits or loss.

Blach (2010) determined that the differences in financial ratio averages between industries can be used as corporate signals for past, current and future perspectives. Due to the fact that most firms are unwilling to voluntarily disclose the information to outsiders, the degree to which internal factors affect the financial performance of firms is unknown.

The cement manufacturing industry in Kenya started in the early 1930s which started with the incorporation of East African Portland Cement (EAPC). The company began as a trading company where they imported cement which was used in the construction work
done in East Africa, they later constructed their first factory in 1956 based in Athi River (Dyer & Blair Investment Bank, 2012). The initial capacity of the plant was 60,000 tonnes per annum and is currently producing over 700,000 tonnes a year. In 1951, Bamburi Cement Limited was founded and its major shareholder was a cement manufacturing company known as Lafarge which is based in France. Athi River mining (ARM) was then founded in 1974, whose main shareholder is the Paunarama family. The company initially began as a mineral extraction and processing company and later began a cement division.

The industry in Kenya has since then increased from three companies to six with the incorporation of National Cement Company Limited, Mombasa Cement Limited and Savannah Cement Company (Dyer & Blair Investment Bank, 2012). Due to the increase in positive gains over the years the sector continues to enjoy robust growth and remains a key component of the country’s immediate and longer term growth agenda. As a result the construction sector in 2014 contributed 4.8% to the country’s gross domestic product (GDP) which was an increase from 4.5% in 2013. The sector also grew to 11.1% in 2014 from 4.6% in 2013, this was evidenced by the increase in value of their output to Kshs. 687,537.3 million (Kenya National Bureau of Statistics, 2015). The growth was in mainly driven by the increase in infrastructure development in the East African region. This has led to an increase in demand for high quality and sustainably produced cement.

AIB Capital Limited (2016), state that cement consumption is growing faster than the rate of production on average in the region. The main driver of growth is said to be increase in housing projects as well as an increase in the demand for government infrastructure such as road and railway networks.

The industry mobilizes and effectively utilizes local human and material resources in the development of housing and infrastructure which then promotes local employment while improving economic efficiency (Anaman & Amponsah, 2007)

The increase in consumption of cement in the country has led to an increase in expansion efforts by the existing firms. Notably, Savannah cement announced its plans to build a second facility in the country so as to increase its annual production to 3m tonnes as compared to their previous capacity of 1.5m tonnes (Oxford Business Group, 2016).
1.1.2 Internal Factors

Cirikovic (2011) explains internal factors as factors that have an internal impact on the organization and which the organization can influence them. These group will include all the factors that are contained within an entity internally, such that any changes in the factors will lead to changes in the organizational structure.

Ownership structure relates to a mechanism in corporate governance which is used to facilitate the increase in efficiency of a firm and is believed to have an effect on the firm performance for many years (Chen L, 2012). Adam Smith (1776) observed that joint-stock companies were less efficient when compared to private copartner firms due to the fact that the directors would not watch over “other people’s money” with ‘the same vigilance “as their own.

Capital structure mainly refers to the mixture of variety of long term sources of funds and equity shares which would include the reserves and retained earnings of a firm. Since financial capital is an uncertain but critical resources for firms, suppliers of finance are therefore able to exert control over firms (Harris and Raviv, 1991). Debt and equity are the two main classes of liabilities with debt and equity holders forming the two types of investors in the firm. Each of this types of capital have an associated level of risk, benefit and control. An organization’s capital structure there represents a composition or structure of its liabilities.

According to the concept statement number 6 Financial Accounting Standards Board (FASB), it defines assets as probable future economic benefits which are obtained or controlled by a particular entity as a result of past transactions or events (Financial Accounting Standards Board [FASB], 1985). Assets are usually categorized into either tangible or intangible assets. In the context of this research study assets will refer to the group of tangible of assets that are held by the organization and are used to establish and grow the business. The study will refer to the asset structure which will include both the fixed and current assets held by cement manufacturing companies.

1.2 Statement of the Problem

According to the Kenya National Bureau of Statistics (2016), the construction industry is one of the sectors that is currently enjoying a continued state of growth. The consumption of cement in the country has as a result also increased in tandem with the growth in the
building and construction sector. There are currently no studies that have been conducted on the effect of internal factors on the financial performance of firms in this sector.

The effectiveness of internal control on financial overall performance of the firm has been considered to be vital, in every enterprise because the challenge of inner controls become to save you and locate fraud inside the firm. Internal controls are set to make sure secure custody of all property, to avoid misappropriation of the firm’s property and to come across and protect in opposition to probable frauds. Every firm whether production or non-production, ought to have control of the very best qualifications, quality and determination considering its inception. The management need to meet regularly to check the affairs of the firm and to direct the strategic course of the company and additionally make sure continued intention congruence (Reid & Smith, 2000).

Munene (2013) carried out a look at and determined out that some of the demanding situations skilled in regard to inner controls encompass; struggles with liquidity problems, economic reports aren't made well timed, accountability for economic assets is trying, frauds and misuse of institutional assets have been unearthed and a number of selections made have now not yielded the anticipated outcomes.

Wanjohi (2013) stated that size and evaluation of performance is valuable to managers, and addresses the questions what took place, why it passed off and what to do about it. Monetary overall performance gives quick time period comments to the manipulate structures as they reveal the implementation of strategic targets by using checking the organizations role, speaking the position, confirming priorities and compelling development

As it stands, I have not been able to find any study that has been carried out on the analysis of the effect of internal factors on the financial performance of firms operating in the cement manufacturing industry. This study therefore aims to bridge the gap by undertaking on the same. The corporate objective of firms is to maximize the profits and shareholders wealth. Thus this study has mainly focused on how different internal factors affect the various financial performance ratios and their effect on the corporate success of cement manufacturing firms in Kenya. This study will therefore be relevant and beneficial to the market.
1.3 Purpose of the Study

The purpose of this study was to analyze the effect of internal factors on the financial performance of cement manufacturing firms operating in Kenya.

1.4 Research Questions

1.4.1 How does ownership structure influence the financial performance of cement manufacturing firms in Kenya?
1.4.2 How does capital structure influence financial performances of cement manufacturing firms in Kenya?
1.4.3 How does the size of the firm influence the financial performances of cement manufacturing firms in Kenya?

1.5. Significance of the Study

The findings and recommendations of this research study will play a role in informing the various stakeholders in the market when it comes to better decision making.

1.5.1 Current and Prospective Investors

The findings of this study will be of importance to various stakeholders in the market among them being corporate and individual investors as well as owners of construction and cement firms. The main beneficiaries of the study will be corporate and individual stock market investors, since they will be able to use the findings of the study to determine their investment decisions and strategies.

1.5.2 Corporate Managers and Decision Makers

The research study will be of most important to these groups of people since they are the ones who are directly involved in the running of day to day operations of the firm. Due to the fact that they are considered to be the agents of the shareholders, they are expected to make decisions which take into consideration the expectations of the shareholders. As such their main duty is to create wealth and maximize the profits of their organizations. This research will therefore assist managers to understand how the various internal factors can affect their performance as well as how to improve it.
1.5.3 Academicians
Future researchers who want to study the same industry will be assisted with the new literature that will be introduced. Granting the fact that the existing literature may encompass most of the objectives I have in mind, this does not imply that it is exhaustive in terms of content. Therefore, there exists a gap to be filled with more research being done on the subject matter.

1.6 Scope of the Study

The cement manufacturing industry has six operating firms namely; ARM, EAPCC, Bamburi Cement Limited, Savannah Cement, National Cement and Mombasa Cement in the Kenyan market with an additional two firms expected to start operations in the coming years. Of the six firms in operation only are three listed firms in the NSE that is ARM, EAPC and Bamburi Cement Ltd.

This study focused on Bamburi and EAPCC, this was done so to evaluate why the two companies have varied performance. The data analyzed covered the years 2010-2015, and this was obtained from the financial statements of the specific firms. The main challenge experiences was gaining access to the financial statements, however, to curb this the researcher contacted the various auditors who availed the data. The study was done January to April 2017.

1.7 Definition of Terms

1.7.1 Internal Factors

Internal factors are defined as the factors within an organization that can strongly determine how well a company is able to meet its objectives, and they might be seen as strengths if they have a favorable effect on the business (Waititu, 2016).

1.7.2 Financial Performance

Financial performance is defined as the analysis of corporate performance which is usually expressed in terms of the profit and loss that is generated in a defined period of time.
1.7.3 Capital Structure

Harris and Raviv (1991) defined capital structure as a mixture of long term sources and equity shares which would include the reserves and retained earnings of a firm.

1.7.4 Ownership Structure

Thomsen and Conyon (2012), defined the ownership structure in the case of publicly listed firms to consists of two distinct features: First, ownership concentration meaning that a firm is owned by one or a few large owners (concentrated) or multiple smaller owners (dispersed) and ownership identity, referring to the type of owners such as individuals/families, institutions or other firms.

1.7.5 Size of Assets

As per the Financial Accounting Standards Board (FASB), (1985), these assets are referred to as property, plant and equipment and include land, building, equipment’s automobiles and furniture. These firms normally use their fixed assets so as to convert their raw materials into finished goods.

1.8 Chapter Summary

This chapter introduced the background of the study and the industry itself as well as the problem statement. At the same time, the chapter captures the objectives and importance of the study. In chapter two, we will be able to review the available literature which focuses on the internal factors and their effect on cement manufacturing companies.

Chapter two presents the literature review. It discusses the existing research literature on ownership structure, capital structure, and the asset structure and how they affect the financial performance of cement manufacturing companies. The discussion tackles all the research questions posed and provides a firm theoretical background for the study.

Chapter three presents the research methodology used in this study. It details the research design, population and sampling, data collection methods, research procedures and how data collected was analyzed. Chapter four presents the results and findings of the study. Chapter five presents the discussion, conclusion, and recommendations for action and further research.
CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction

In this chapter, literature review focuses on critical review of literature based on specific objectives. The review of specific objectives include: to determine the effect of ownership structure on financial performance of cement manufacturing companies; determine the effect of capital structure on financial performance in cement manufacturing companies, and the relationship between the size of the assets of a firm and the financial performance in cement manufacturing companies.

2.2 Ownership Structure and Financial Performance

The relationship between the ownership of a firm and its financial performance is a key issue in corporate governance. Some studies that focus on corporate governance support the presence of a linear or monotonic relationship between ownership and performance (Berle and Means, 1932; Jensen and Meckling, 1976; Lichtenberg and Pushner, 1994; Mehran, 1995), while the rest support a non-linear or non-monotonic relationship between the two (Morck et al., 1988; McConnell and Servaes, 1990 and 1995; Chen, Hexter, and Hu, 1993; Short and Keasey, 1999).

Both studies assumed a uni-directional relationship based on the assumption that the ownership was exogenous. This view was later questioned by Demsetz (1983) and Demsetz and Lehn (1985), where they both argued that the ownership structure was endogenously related to the firm performance with no direct relationship existing between the two. This debate has however been broadened by the more recent empirical studies. These studies have presented evidence that supports either a reverse-way or a bi-directional relationship between the ownership structure and financial performance by use of simultaneous equation approach to model endogeneity (Chung and Pruitt, 1996; Loderer and Martin, 1997; Cho, 1998; Bohren and Odegaard, 2001; Demsetz and Villalonga, 2001).
2.2.1 Institutional Investors and Financial Performance

Most of the research focusing on the relationship between ownership structure and financial performance has been based on the agency framework. It has been debated that the separation of ownership from control for a corporate firm creates an agency problem which results in conflicts between the managers and the shareholders (Jensen and Meckling, 1976; Shleifer and Vishny, 1997). Since ownership structure remains the foundation for exercising power and control over corporate entities under imperfect market conditions and or the nature of incomplete contracts, the issue of agency costs needs to be addressed as per the ownership structure of the firm so as to ensure efficient financial performance (Fama & French, 1998).

For a publicly listed firm which has a wide listing of shareholders, the challenge for the shareholders is to control the behavior of managers and or the board. On the other hand, the challenge for a closely held firm with a controlling shareholder and a small minority of external shareholders or a firm whose shares are held by a dominating shareholder is how to prevent the controlling shareholder from extracting excess benefits to the detriment of the minority shareholders (World Bank, 1999). As a result in order to ensure there is optimum performance and minimal agency costs, a firm must consider their ownership structure as one of their core governance mechanisms along with others.

In earlier and recent studies there has been a consensus that the presence of multinational enterprises (MNEs) has had a positive impact on the general performance of firms and the stock market as a whole. Therefore ownership of shares by foreign investors is believed to have a positive effect on the firm’s performance and in particular those in developed economies (Perrini, Rossi, & Rovetta, 2008).

Aitken and Harrison (1999) established using a sample of Venezuelan firms that the presence of foreign capital is closely linked to productivity improvements, but only for small firms. On the other hand, Perez-Gonzalez (2005) determined that controlled subsidiaries of multinational companies generally have improved overall productivity on their factors of production and in particular for firms that rely on technological innovations which are transfers by the parent companies.

Petkova (2008), established that Indian firms acquired by foreign investors recorded significant growth over a period of three years from the date of acquisition. A similar
study was carried out in Indonesia by Arnold and Javorcik (2005). They determined that Indonesian firms acquired by foreign investors’ recorded substantial improvements in productivity in both the year of acquisition and in the latter years.

Other studies were conducted in firms operating in developed economies. Doms and Jensen (1995), established that U.S firms with foreign capital are more productive when compared to firms with domestic capital, nonetheless they were less productive that U.S multinationals. Girma (2005, 2007) determined that immediately after their acquisition by a non-American investor, U.S firms immediately enjoyed substantial growth rates. However, in both cases the studies did not take into account the foreign investors home country and whether they came from and emerging or developed economy.

Konings (2001) conducted a study in three countries that is, Bulgaria, Romania and Poland, where he investigated whether the financial performance of companies with foreign capital was better than that of firms with domestic capital. The results obtained by Konings (2005) for Romania and Bulgaria suggests that the financial performance of firms was not affected by whether or not a firm had either foreign or domestic capital. This was in contrast for Poland, where the results showed that foreign capital had a positive and significant effect. The main reason for this variance was in the delays in carrying out reforms in both Romania and Bulgaria. He further stated that time is required in order to start enjoying the positive effects of foreign capital.

In a comparative study, Barbosa and Lourie (2005) conducted a study in Greece and Portugal and did not find any significant difference between multinationals and firms which were owned domestically. The established that the performance of firms in Portugal is not affected by the presence of foreign capital after discounting control for the firm and its industry characteristics.

2.2.2 Ownership Concentration and Financial Performance

It is widely recognized that the ownership concentration of a firm has the potential to limit the agency problem and then result in increased corporate performance. This positive effect as a result of ownership concentration can be explained by the efficient monitoring hypothesis, which states that higher concentration of ownership gives large shareholders stronger incentives and greater power at lower cost to monitor management. According to Grossman and Hart (1986), they believe that shareholders who have a larger
stake in the company will be more willing to play an active role in corporate decisions since to some extent they enjoy the benefits that arise from their monitoring efforts. The methods used to monitor and intervene range from informal conversations with management to formal alternative challenges (Shleifer and Vishny, 1986, 1997). In an instance where large shareholders cannot monitor management, they are still able to facilitate a third party takeover by dividing the gains from their own shares with the bidder.

Shleifer and Vishny (1986), determined that some degree of share ownership concentration enhances firm performance since a large number of shareholders, with a substantial portion of the gains from improving the firms performance will have a greater incentive in monitoring firm performance. Additionally Wruck (1988) found a strong and positive relationship between the change in ownership concentration and firm performance.

From as early as the late 1990s the potential conflict between the majority and minority investors has become a focus of interest for academics. Concentrated ownership structure may allow dominant shareholders to commandeer minority investors this is also known as the expropriation of minority shareholders hypothesis. Shareholders who own a large number of shares represent their own interests, which may not coincide with the interests of other stakeholders in the firm. Certain features of firm such as the pyramidal control structure, cross shareholding and super voting rights allow such shareholders to secure control rights which are not commensurate with the cash flow rights (La Porta et al., 1999; Claessens et al., 2000). The separation between control and cash flow rights induces the prevalent problems of controllers’ takeover (Denis and McConnell, 2003; John C. Coffee, 2005). The term “tunneling” is used by Johnson et al. (2000) to refer to the transfer of resources from the firm for the use and benefits of its controlling shareholders. The fear of small investors that their investment may be pilfered may induce high cost of capital to firms and as a result of this inefficient investment.

Bjuggren, Eklund and Wiberg (2007) evaluated the relationship between ownership structure and performance Swedish companies over a period from 1997 to 2002. The study found that the use of dual class shares, which give different voting rights and dividends to public shareholders and founders of the company resulted in a negative relationship on the company’s performance. Perrini, Rossi and Rovetta (2008) conducted
a similar study to determine the relationship between ownership structure and performance using a sample of firms based in Italy from 2000 to 2003. They concluded that the number of shares held by the five biggest shareholders of the company had a positive influence on firm valuation whereas management ownership only benefited firms that have less concentrated ownership companies. Sulong and Nor, (2008) carried out a study of listed Malaysian firms to investigate the effect of dividends, ownership structure and board governance on firm value. They established that concentrated and managerial ownership have insignificant effect on firm value which was unexpected.

Cho (1998), determined that firm performance affects the ownership structure which he defined as the percentage of shares held by directors and not vice versa. Jurgen (2000) established that the presence of large shareholders does not necessarily improve profitability and that the high degree of ownership concentration seems to be a sub-optimal choice for many of the tightly held German corporations. Their results both imply that ownership concentration negatively affects the profitability of the firms.

Hill and Snell (1988) observed that ownership concentration could be used to alleviate type 1 agency cost, although most of the studies were carried out in economic settings where the ownership was generally dispersed such as in the United States. In such settings it was established that ownership concentration had a positive effect on the research and development intensity as well as the corporate performance.

Demsetz and Lehn (1985) suggest that in countries where firm shares are widely held and where managers are forced to align their interests with those of their shareholders, the concentration of ownerships should be viewed as endogenous to firm performance in equilibrium. In support of this Demsetz and Len, Kole (1994) found a reverse causality between ownership concentration and firm value.

2.3 Capital Structure and Financial Performance

Decisions that relate to the financing are considered to be one of the most vital decisions for a firm. Financing is usually done using a mix of both debt and equity. The use of both debt and equity in financing is known as the capital structure. Booth, et al (2001) carried out a study on ten developing economies and determined that the determinant of capital structure are the same in both developing and developed countries. A similar study done
by (Singh, 2010) concluded that the decisions relating to capital structure depend on the firm’s own characteristics and the country’s macroeconomic factors.

Modigliani & Miller (1958) conducted research work that laid the foundation for the research on the topic of capital structure. In their view the firm’s value is not dependent on its capital structure but is dependent on the real assets of the firm which affects it. In the agency theory developed by Jensen and Meckling (1976), they asserted that managers do not always run the firm with the aim of maximising their shareholder wealth but may instead aim to pursue their own interests.

### 2.3.1 Debt and Financial Performance

One of the variables that determine the capital structure and choice of a firm is the debt maturity since this will affect its performance. Debt maturity has an effect on the company’s option in investing. Furthermore, the tax rate will also have an impact on company performance. Abor (2005) conducted a study to determine the influence of capital structure on the profitability of listed companies on the Ghana Stock Exchange over a period of five years. He observed that there was a significant positive correlation between the return on equity and SDA and that firms which earned a lot used more short term debt to finance their business. The findings of their study also showed that there was an adverse relationship between long term debt and return on equity. It also determined that there was a positive relationship between the total debt and the return on equity. This implies that firms which enjoy good profits are dependent on debt as their key financing option.

Modigliani & Miller (1963) were able to modify the earlier capital structure irrelevance theory where they argued that capital structure did not really matter when determining the value of a firm. This belief was based on the argument that the use of debt offered a tax shield to the firm. Based on this assertion, firms would then be able to decide on an all debt capital structure. This belief was however opposed by Brigham & Gapenski (1996) who argued that the Miller-Modigliani (MM) model was only applicable in theory since in practice, the cost associated with bankruptcy existed and would increase when equity is traded in for debt.
In an effort to prove the MM theory, Maina & Kondongo (2013) carried out a study to determine the effect of the debt-equity ratio on the performance of firms listed in the Nairobi Security Exchange (NSE) from the year 2002-2011. The study determined that there was a significant inverse relationship between the capital structure and all measures of performance. This result was in agreement with the MM theory which states that the capital structure of a firm is relevant in determining the performance of a firm. Their research also concluded that firms listed in the NSE were more prone to use short term debt as compared to long term debt.

A similar study was carried out by Abdul (2012) where he sought to evaluate the relationship between capital structure decisions and the performance of firms based in Pakistan. The study established that financial leverage had a significant inverse relationship with the performance which was measured using ROA, GM, and TOBIN’s Q. The relationship between financial leverage and firm performance was determined by the return on equity (ROE) which was negative but not significant. Javed & Akhtar (2012) in another study carried out a study to determine the relationship between capital structure and financial performance. The study established that there was a direct relationship between financial performance, financial leverage, size and growth of the company. The study focused on firms that were listed on the Karachi Stock Exchange in Pakistan and used correlation and regression analysis on the financial data. The outcomes of the study were consistent with the agency theory. It however, isolated all other financing decisions and focused mainly on financial leverage.

A study was carried out to establish the relationship between the capital structure and the return on equity for industrial and allied sectors in the NSE over the period between 2004 to 2008. Debt equity ratio was used to represent the capital structure while return on equity was used in place of performance. The study applied regression analysis and observed a negative relationship between the debt equity ratio and the ROE. Since the study focused only on one sector of the companies listed and to only one aspect of financing decisions, the findings can therefore not be extrapolated to include all the other sectors.

Hutchinson (1995), in his research argues that financial leverage has a positive effect on the firm’s return on equity provided that the earnings’ power of the firm’s assets exceeded the average interest cost of debt to the firm. Taub (1975) further confirmed that their was
a significant positive relationship between the debt ratios and the measures of profitability. Nerlove (1968), Baker (1973) and Petersen and Rajan (1994) also identified the positive association between debt and profitability and in particular for industries. In their study of leveraged buyouts, Roden and Lewellen (1995) determined that there was a significant positive relationship between profitability and the total debt as a percentage of the total buyout-financing package.

2.3.2 Company Size, Leverage and Financial Performance

The size of a firm refers to the amount and variety of its production capacity and ability or the amount and variety of services that it can concurrently provide its customers (Niresh and Velnampy, 2014). Niresh and Velnamy (2014), Prasanjaya and Ramantha (2013), Akbas and Karaduman (2012) concluded that a company is considered to be large or small when their total assets and total sales are taken to account. The size of a firm is the main determinant for its profitability due to the theory of economies of scale which can be found in the neo classical view of the firm.

A number of papers have proposed that the size of a firm is positively related to leverage ratio. The basis for the belief is evidence provided by Warner (1977) and Ang et al. (1982) that the relevance of direct bankruptcy cost is inversely proportional to the value of the firm. Thereby suggesting that the impact of these costs on the borrowing decisions of large firms might be negligible.

Woldemikael Shibru (2012) carried out a study whose main aim was to examine the relationship between leverage and the determinants of the capital structure decision and to explore which capital structure theory was applicable in commercial banks operating in Ethiopia. He used profitability, tangibility, growth, risk, size and liquidity as the factors that determine the mix of debt and equity in the capital structure. He used a sample of eight banks and the financial data over the period of 2000 to 2011. He established that profitability, tangibility, liquidity and growth all have a negative relationship with leverage whereas size and leverage have a positive relationship. There was no support that indicated that leverage was affected by risk. The conclusion by Shibru (2012), is that profitability, liquidity, tangibility and bank size are the major factors that determine the capital structure of commercial banks in Ethiopia.
Safarova (2010) studied the factors that determine the firm performance of companies in New Zealand. He established that size is the most important factor that determined the firm performance, followed by growth and leverage, while other factors such as tangibility, corporate governance, cash on hand and risk seemed to be marginally related to firm operating performance. Mirza and Javed (2013) performed a study on the determinants of financial performance of firms on Pakistan stock market and established that firms having a well governed ownership structure, capital structure and proper risk management tend to have a better financial performance.

The role that the size of a firm plays in profitability was studied by Lee (2009) who used fixed effect dynamic panel data model to analyze a sample of more than 7000 US publicly held firms. He concluded that absolute firm size played a significant role in profitability.

Ozgulbas et al. (2006) carried out study to determine the effects of firm size on performance over the firms operating in Istanbul Stock Exchange between the years of 2000 to 2005. Their study determined that big scale firms have higher performance when compared to small scale firms. In a similar manner Jonssonn (2007) studied the relationship between profitability and size of firms operating in Iceland. At The results of the study indicated that larger firms had higher profitability when compared to smaller firms.

In a study conducted by Velnampy (2006) on investment appraisal and profitability of Toddy bottling project in Sri Lanka. He found that the management of the project had failed to attain the budgetary results despite the net present value, internal rate of return and the benefit cost ratio indicating otherwise.

Velnampy (2006) analyzed the financial position of the companies and the relationship between the financial position and profitability using a sample of 25 publicly quoted companies in Sri Lanka using the Altman Original Bankruptcy Forecasting Model. According to the results, only 4 out of the 25 companies were in danger of going bankrupt in the near future. Additionaly he found that in deciding the financial performance of publicly listed firms, ratios such as earnings/total assets, market value or toatl equity/book value of debt ratio and sales/total assets in times were the most important ratios.
2.4 Relationship between Size of Assets and Financial Performance

2.4.1. Fixed Assets and Financial Performance

All cement manufacturing companies depend on the structure of their assets which consists of both fixed and current assets. These firms normally use their fixed assets so as to convert their raw materials into finished goods. As per the Financial Accounting Standards Board (FASB), (1985), these assets are referred to as property, plant and equipment and include land, building, equipment’s automobiles and furniture. Lzryadnova, (2013) determined that the investment in fixed assets for large and medium sized companies in Russia accounted for up to 96.4% of the total number of investments made in 2008.

Previous studies have indicated that the investment in fixed assets for a firm may have an effect on the firm’s profitability. Fixed assets play a major role in the profit ratio determination as well as in the evaluation of risk involved (Smith, 1980). Effective management of fixed assets is important in the creation of value to its shareholders. Manufacturing companies use their non-current assets to convert their raw materials into finished goods.

In a study conducted by Okwo, Ugwunta and Nweze (2012), they determined that a firm acquired fixed assets with the aim of generating sales. This means that the efficiency of fixed assets should be measured in relation to the sales. Generally, a high fixed assets turnover ratio implies that there is efficient utilization of non-current assets in the generation of sales, whereas a low ratio would imply that there is inefficient management and utilization of fixed assets. Therefore a firm whose assets are majorly depreciated may have a higher asset turnover ratio when compared to a firm which has just purchased their fixed assets. By comparing the two firms the asset turnover ratio of both the firms may be inconclusive in determining which of the two firms is more efficient in managing their fixed assets due to the effects of depreciation. The asset turnover ratio is used to measure how much sales are generated for every unit of capital that is employed.

A study carried out by Khalid (2012) examined the relationship between the asset quality, management proxies and profitability nexus. By using the return on assets and the profitability ratios as substitutes for bank profitability for the period between 2006-2007 and 2010-2011, the operating performance of the banks used in the sample was estimated.
with the help of financial ratios. Multiple regression was also used to examine whether a bank’s asset quality and operating performance were positively correlated. The results of the study determined that a bad asset ratio had an inverse relationship with the operating performance after adjusting for the effects of operating scale, traditional banking business concentration and the idle fund ratio.

Surroca, Tribo and Waddock (2010) evaluated the effects of intangible assets of a company on facilitating the relationship between corporate responsibility and financial performance in 28 countries. In the analysis of the study various variables were used some of which included financial performance and corporate responsibility. The results of the study indicated that there was no direct relationship between corporate responsibility and performance in only indirect financial relationship, which depends on the mediating effect of the company’s intangible assets (Surroca, 2010).

Barney (1991) believes that one of the characteristics contributing to a companies’ competitive advantage is their intangible assets which can be represented by innovation human resource among others. Becker et. al.(2010) studied the effects of firms size on profitability in the firms operating in the manufacturing sector in USA using the data of years 1987 to 2002. The results of the study indicated that there was a negative and statistically significant relationship between the total assets, total sales and the number of employees of the firms and their profitability.

Bacnhuenvijit (2012), studied the factors that affected performance of firms operating in Vietnam. A positive relation was found to exist between the total sales and the profitability of the firms while a negative relation was found between the profitability and the total assets.

2.4.2 Current Assets Management and Financial Performance

Current assets may represent a significant component of the total share of assets on the balance sheet of a firm. For a number of firms the management of current assets could therefore make or destroy the organizations financial performance. Flanagan, (2005) states that the current assets of a firm can be described as the life blood of every firm. He also emphasized that the primary task of every manager was to ensure that the current assets were kept flowing as well as ensure the use of cash flows to generate more profits.
The management of current assets is considered to be the primary goal of working capital management (Jain, Singh, & Yadav, 2013). Current assets management there refers to all the activities and decisions that managers undertake and which affects the size and effectiveness of current assets. It has been determined that the profitability of a firm is largely dependent on its current asset management. If a firm is inefficient in managing its current assets this will prove to be damaging to the firm. On the other hand if the firm has excess current assets this can result to there been idle funds which could be used to generate profit while having inadequate current assets will result in the interruption of operations which would also negatively affect profitability (Chowdhury & Amin, 2007).

A majority of empirical studies relating to the relationship between current asset management and financial performance support the traditional mindset of reducing the current asset proportion in total assets so as to reduce the current asset investment and in doing so this should result in a positive effect on the profitability of the firm. However, contrary to this traditional belief, an increase in the investment made to current assets may also result in an improvement in profitability. This can be observed in situations where high levels of inventory are maintained which results in a reduction in the cost of interruptions during the production process, a decrease in the cost of supply (Blinder & Maccini, 1991). A study carried out by Czyzewski & Hicks (1992), they both concluded that firms which had the highest return on total assets usually had higher cash balances and limited their liquidity management to static cash and asset ratio. Soenen (1993) used return on total assets as an index of financial profitability. This is due to the fact that although, return on equity is considered to be of more value to investors, return on total assets is normally not influenced by the total leverage of the firm.

Shin & Soenen (1998), carried out a study which highlighted the effect of efficient current asset management in value creation for shareholders. They determined that value creation resulted from the time lag between the purchase of raw materials and the collection of cash from the sale of finished goods. The manner in which current assets are managed has a significant effect on the profitability and liquidity of the firm. The study centered on determining whether a short net trading cycle is beneficial to a company’s profitability. They determined that there existed a strong negative relationship between the firms net trading cycle and its profitability. An additional study was carried out by Wang (2002), to evaluate the relationship between liquidity management and corporate
value for firms that were based in Taiwan and Japan. The study concluded that there was a negative correlation between the cash conversion cycle, return on assets and return on equity which was also affected by industry factors. The findings of the study highlighted that regardless of the differences in the financial systems and structural characteristics present in both countries, aggressive liquidity management led to an increase in the performance which as a result also increased the corporate value of both Japanese and Taiwanese firms.

Korankye & Adarquah (2013) analysed working capital management and its effect on firm profitability. Data was acquired from the financial statements of listed manufacturing firms in Ghana from 2004 to 2011 inclusive. From the seven listed manufacturing firms, six of the firms constituted the research sample. The paper uses working capital cycle, and gross operating profit margin as substitutes for working capital and profitability respectively. The control variables were leverage, interest cover and the ratio of current assets to total assets. The study found out that working capital cycle significantly affects firms profitability negatively.

In manufacturing and construction firms working capital management is considered to be very vital since it makes a large part of their assets (Horne & Wachowicz, 2000). Raheman & Nasr (2007), determined that working capital directly affects the profitability and liquidity of firms. Almazari (2013), carried out a study investigating the relationship between the working capital management and the profitability of Saudi cement manufacturing firms. The results indicated that the Saudi cement industry’s current ratio was the most important liquidity measure which effected profitability. They therefore concluded that cement firms must set a trade-off between these two objectives to as to ensure that neither the liquidity nor profitability suffers. It was also found that the size of a firm was positively correlated to its profitability.

2.5 Chapter Summary

This chapter focused on literature that has been on the macro economic factors that would affect the financial performance of a company. The literature mainly focused on factors such as inflation, interest and gross domestic product and how they positively or negatively affect the performance of the construction industry. The literature also allowed us to be able to identify the gaps that previous studies had not researched on as well as the
observations the previous researchers had made. In chapter three, we will be able to
discuss the research methodology to be used in the research and which tool will be used
to analyze the data that will be collected.
CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Introduction

In this chapter the research methodology that was used to guide the study will be discussed. Among the issues discussed include the research design to be adopted while conducting the study, the target population for the study, the sampling design, data collection methods, research procedures, data analysis methods as well as the analytical model that will be used to represent the relationship between the company’s ownership structure, capital structure and size of the firm denoted by the assets on the financial performance of cement manufacturing companies in Kenya and finally the chapter summary.

3.2 Research Design

The function of a research design is to ensure that the evidence obtained enables us to answer the research question as unambiguously as possible (Vaus, 2001). The study adopted a comparative research design to establish the relationship between the company’s ownership structure, capital structure and size of the firm denoted by the assets and the financial performance of cement manufacturing companies in Kenya. Sekaran and Bougie (2013), state that descriptive research is a design used to answer the question, what is happening? How is it happening? Why is it happening? This study adopted this design because it aims at collection financial information relating to the companies in relation to the internal factors affecting financial performance.

Furthermore, the correlational research approach was adopted as the study will seek to establish the relationship between the independent variable which is defined by ownership structure, size of assets and capital structure with the dependent variables which include the ROA, ROE and ROS. According to Cooper and Shindler (2011, p.149) one of the objectives of descriptive research is to discover the associations among different variables. This objectives can be referred to as a correlation study, which is a sub set of descriptive studies.

The study aimed at obtaining financial information relating to the performance and ownership structures of Bamburi Cement Company and EAPCC with the aim of
determining the effect of internal factors on financial performance of both companies. The study used quantitative research to gain a better knowledge and in-depth understanding of the results. The main objective of the study is to provide a clear understanding of how internal factors influence the financial performance and therefore conclude its impact on both companies.

3.3 Population and Sampling design

3.3.1 Target Population

The target population refers to all the elements that are included in the study. This is where the sample size is meant to be selected from. According to The Global Cement Report, (2016), Kenya currently has a total of 6 cement manufacturing companies based in Nairobi with most of the manufacturing plants based in Athi River. The target population for the study included two of the cement manufacturing companies that are in operation in Kenya, that is East African Portland Cement Company and Bamburi Cement

The aim of this research was to examine the effect of internal factors (ownership structure, capital structure and size of the firm denoted by the assets) on the financial performance (return on assets, return on equity and return on sales) of cement manufacturing companies listed on the Nairobi Security Exchange, with a focus on Bamburi Cement and East African Portland Cement Company. The objectives of the study was to study; the effect of ownership structure on the financial performance of cement manufacturing firms in Kenya (Bamburi Cement and EAPCC), the impact of firm capital structure on the financial performance of cement manufacturing firms in Kenya (Bamburi Cement and EAPCC), the effect of firm size denoted by assets on the financial performances of cement manufacturing firms in Kenya (Bamburi Cement and EAPCC).

The study covered a period of five years starting from 2011 to 2015 using their financial statements.

3.3.2 Sampling Design

3.3.2.1 Sampling Frame

A sampling frame is a list of population units/elements from which to select units/elements to be sampled (McDaniel & Gates, 2001). The method of sampling in the study was all the cement manufacturing companies in operation in Kenya. Each company then formed a sampling unit. The sample elements were their financial statements.
3.3.2.2 Sampling Technique

The study used a purposive sampling technique so as to generate the sample for companies to be used in the study. In this study, only two of the cement manufacturing companies in operation in Kenya as at the end of 2015 were included as study elements. Purposive sampling is a non-probability sampling method used when the elements of a sample size are identified using the judgment of the researcher. According to Allison (2012) purposive sampling usually allows the researcher to obtain a representative sample by using sound judgment which would result in the saving of time and money. It may also prove to be effective when there is a limited number of individuals who can serve as the primary source of data due to the nature of the research design, its aims and objectives.

They can also ensure that the selected groups of people have the appropriate characteristics. The purposive sample helps in gathering useful data and information that would not have been possible using probability sampling techniques, which require more formal access to lists of populations (Kombo, and Tromp, 2006). The purposive sample was representative and adequate for answering the questions in this study.

Due to the population size of cement manufacturing companies in Kenya, the study included one company that is profit making and another which is loss making, this will be a type of purposive sampling technique.

3.3.2.3 Sample Size

Kenya currently has 6 cement manufacturing companies that are in operation. Those are Athi River Mining, East African Portland Cement, Bamburi Cement these three are publicly listed companies while the rest are private companies which include Mombasa Cement, National Cement and Savannah Cement. The study aimed at using financial statements from only two of the 6 manufacturing companies.

3.4 Data Collection Methods

The study used secondary data. The secondary data was collected from visiting the webpages of each of the companies and personal visits so as to capture data in excel relating to their financial performance. The financial statements of the cement manufacturing companies will be collected from their relevant websites. The data that used in this study covered the period from 2011 to 2015.
The main advantage of using secondary data collected as compared to the use of primary data is that it is very economical in terms of saving the researchers’ effort as well as being very inexpensive. It also saves time since the researcher need not spend a lot of time in the field collecting data. The data to be collected will address the ownership structure, size of assets and the capital structure as well as the financial performance of the companies over the required period.

To facilitate the analysis of the secondary data there will be an analysis on the availability of the necessary data. The determination as to whether the data required is available or not will be done through analysis of the financial statements, if it is not available then contact with the necessary institutions will be requested so as to gather the information.

### 3.5 Research Procedures

The research procedure included the collection of data relating to the company’s ownership structure, capital structure and size of the firm denoted by the assets, while the financial statements relating to the companies will be downloaded from the various company websites.

In the instances that the financial statements were not be available on the webpage, company visits and communication was done so as to request that the necessary data be made available for the information to be inclusive of every company in the population.

The researcher obtained a written letter from the university stating that the required information was relevant in the completion of the students’ masters’ thesis.

### 3.6 Data Analysis Method

Data collected was quantitative in nature from secondary sources. The data collected was stored in an appropriate format that permitted statistical analysis. The analysis included computer-aided, statistical manipulation. The measures of the variables important to the research problem were collected and the information gathered from the financial statements was relevant to the study. All the data collected was inputted into the statistical package and data was cleaned for missing values and data entry errors. Data analysis was carried out using IBM SPSS 20.0. The quantitative data was analyzed for descriptive statistics. The descriptive statistics included frequency, percentages, mode, mean and standard deviation to profile sample characteristics and major patterns emerging from the
data. Interpretation of the statistical outputs was done and discussed in the presentation of results and findings in the next chapter.

Tables were used to summarize the responses for further analysis and comparison. This was by use of generated quantitative reports through tabulations, percentages, and measure of central tendency. According to Cooper and Schindler (2003), they observe that the use of percentages is important since they simplify the data by reducing all the numbers to range between 0 and 100 as well as translating data into a standard form with a base of 100 which is suitable for relative comparison. The model that will be used to present information will be graphs and tables.

The independent variable that was being measured in the study included company’s ownership structure, capital structure and size of the firm denoted by the assets. A multiple regression model will be used to test the relationship between among independent variables on the financial performance which will be measured using return on assets (ROA). For the independent variable of how ownership structure affects financial performance hypothesis testing was used to assume unequal variances.

**Table 3.1: Financial Ratios Used in the Study**

<table>
<thead>
<tr>
<th>Financial Performance Indicators</th>
<th>Ratios</th>
<th>Formulas</th>
<th>Definitions</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Return on Assets</td>
<td>Net Income/Total Assets</td>
<td>Indicates liquidity and short term solvency</td>
</tr>
<tr>
<td></td>
<td>Return on Equity</td>
<td>Net Income/Total Equity</td>
<td>Assesses the corporate operational efficiency</td>
</tr>
<tr>
<td></td>
<td>Return on Sales</td>
<td>Net Income/Sales</td>
<td>Evaluates the rate of return for ownership interest</td>
</tr>
<tr>
<td>Internal Factors Indicators</td>
<td>Total Asset Turnover Ratio</td>
<td>Net Sales/ Total Assets</td>
<td>Assesses a company’s ability to manage all of its assets to generate sales</td>
</tr>
<tr>
<td></td>
<td>Fixed Assets Turnover</td>
<td>Sales/Net Fixed Assets</td>
<td>Evaluates the effectiveness of a firm in managing its fixed assets to generate sales.</td>
</tr>
<tr>
<td></td>
<td>Debt to Equity</td>
<td>Total Debt/ Total Equity</td>
<td>Determines the extent to which a company uses debt to finance its assets as compared to those financed by its shareholder equity</td>
</tr>
<tr>
<td></td>
<td>Debt to Assets Ratio</td>
<td>Total Debt/ Total Assets</td>
<td>Determines the proportion of a company’s assets that are financed by debt</td>
</tr>
<tr>
<td></td>
<td>Fixed Assets to Long Term Debt Ratio</td>
<td>Fixed Assets/ Long Term Debt</td>
<td>Evaluates the solvency of a company, in regards to whether the number of fixed assets may be able to meet its long term debt.</td>
</tr>
</tbody>
</table>
The hypothesis used in the research was as follows:

$H_0$: There is no relationship between ownership structure and financial performance.

$H_1$: There is a relationship between ownership structure and financial performance.

### 3.7 Chapter Summary

This chapter presented the research methodology that was used in this study. The chapter covers research design, population and sampling design, data collection methods, research procedures, data analysis methods. The next chapter presents the results and findings of the study.
CHAPTER FOUR

4.0 RESULTS AND FINDINGS

4.1 Introduction

This chapter highlights the results and findings as a result of collected data which is based on objectives of the research. The data was analyzed using both descriptive and inferential statistics and in particular Pearson correlation, regression analysis and ANOVA have been used to establish the fitness of the model as well as to determine the link between specific internal factors and the financial performance of cement manufacturing companies listed at the Nairobi Securities Exchange. This chapter is divided into different sections including; the section of this chapter gives general information on both EAPCC and Bamburi Cement which are both listed in the NSE, the third section presents the findings on the internal factors that affect financial performance (ownership structure, capital structure and size of the firm denoted by the assets), and the fourth represents the components of financial performance (ROA, ROE and ROS).

The fifth section of this chapter presents the trend of internal factors affecting financial performance, the sixth presents the trend of financial performance (return on assets, return on equity and return on sales), the seventh part will present the multivariate regression analysis of the data where the internal factors represents the independent variable whereas financial performance (return on assets, return on equity and return on sales) is considered to be the dependent variable. Finally the eighth section presents the relationship between the internal factors (ownership structure, capital structure and size of the firm denoted by the assets) and financial performance (return on assets, return on equity and return on sales). Lastly the ninth section gives a summary of this research.

4.2 General Information

The aim of this research was to examine the effect of internal factors (ownership structure, capital structure and size of the firm denoted by the assets) on the financial performance (return on assets, return on equity and return on sales) of cement manufacturing companies listed on the Nairobi Security Exchange, with a focus on Bamburi Cement and East African Portland Cement Company. The objectives of the study were; the effect of ownership structure on the financial performance of cement manufacturing firms in Kenya (Bamburi Cement and EAPCC), the impact of firm capital
The effect of firm size denoted by assets on the financial performances of cement manufacturing firms in Kenya (Bamburi Cement and EAPCC) The cement manufacturing companies under consideration were EAPCC and Bamburi Cement Company. The independent variable was taken to be the internal factors of the company (capital structure, ownership structure and the size of the firm) whereas the dependent variable was considered to be the financial performance of the firm (return on assets, return on equity, and return on sales).

4.2.1 Nature of Business

Table 4.2 represents the companies that were included in the study that is EAPCC and Bamburi Cement Company and their operations relating to the products they offer for sale.

Table 4.1: Nature and Operations of Cement Companies under Study

<table>
<thead>
<tr>
<th>COMPANY</th>
<th>NATURE AND OPERATIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td>East African Portland Cement Company</td>
<td>The flagship cement brand for the company is Blue Triangle Cement. Other cement related products that are manufactured by the company include precast concrete product</td>
</tr>
<tr>
<td>Bamburi Cement Company</td>
<td>They are considered to be the largest cement manufacturing company in the region and its Mombasa plant is the second largest cement plant in Sub Saharan Africa. Their flagship cement brands include; NGUVU, Power Plus, Powercrete 52.5 and Power Max these four cement products target various market segments in the industry. The company also manufactures and sells BamburiBlox which is a concrete paving solution and Bamburi Ready Mix Concrete which provides a convenient solution to the construction process.</td>
</tr>
</tbody>
</table>

4.3 Financial Performance of the Firms under Study

Financial performance refers to the analysis of corporate performance usually expressed in terms of profits and losses that are generated for a period of time. The evaluation of the
financial performance of a firm aids decision makers in judging the results of corporate strategies and the activities of the firm in terms of money. The following ratios are normally used when evaluating corporate financial performance: return on assets (ROA), return on equity (ROE), and return on sales (ROS).

4.3.1 Return on Assets

The cement manufacturing companies under study have an annual return on assets (ROA) of not more than 32%. Figure 4.1 below presents that Bamburi Cement Company has the highest annual average return on assets of 14.2% this means that Bamburi is more efficient in generating returns from its invested assets. On the other hand, EAPCC has an annual average return on assets of 6.05% earning of its overall resources. Based on the historical return on assets for both companies, it is evident that Bamburi Cement Company is more efficient in managing its assets when compared to EAPCC.

![Figure 4.1: Cement Manufacturing Companies Annual Average ROA (2010-2015)](image)

4.3.2 Return on Equity

The cement manufacturing companies that are included in the research have an annual return on equity (ROE) less than 60%. Generally, ROEs 15-40% are considered to be good. In the company’s under study Bamburi Cement Company has an average annual return of 18.73% and has been able to maintain it above 10%, On the other hand, EAPCC has managed to raise its ROE from a negative of -5% to 52% over a period of six years.
The cement companies under study have an annual return on sales (ROS) of less than 26%. The figure 4.3 below presents that Bamburi Cement Company has the highest annual average return on sales of 19.15%. This means that Bamburi Cement Company is more efficient at generating profits from its revenue. EAPCC on the other hand has an average annual return on sales of 15.93%. This has mainly been due to a fair gain on an investment property in 2015.
4.4 Components of Internal Factors
Internal factors are company specific variables which influence the performance of company’s internally and they can be controlled by management. Every company has its own internal factors that affect the financial performance differently. Company specific factors include, assets quality, ownership structure, capital structure (Shipho, 2011).

4.4.1 Debt Ratio
The debt ratio of a company is used to determine the proportion of its corporate debt relative to its total assets. It is mainly used to evaluate the reliance of a firm in using debt to finance its business. As per Choi (2010), the debt ratio which can be referred to as the solvency ratio expresses the total liabilities of a company as the total assets percentage. Thus it is used to highlight the number of assets that the firm may be forced to sell in order to pay off its liabilities.

![Debt Ratio Trend for EAPCC and Bamburi Cement (2010-2015)](image)

**Figure 4.4: Debt Ratio Trend for EAPCC and Bamburi Cement (2010-2015)**

4.4.1.2 Debt to Equity Ratio
Debt to equity ratio measures the cement manufacturing companies’ financial leverage and indicates how much debt the cement companies under study are using to finance their assets relative to the amount of indicated in shareholder’s equity. According to the figure 4.5 below, EAPCC has a higher debt to equity ratio compared to Bamburi Cement Company. This means that Bamburi has a stronger equity position when compared to EAPCC. As per the debt to equity ratio EAPCC has in the past financed a number of its assets through debt due to the high ratios as compared to Bamburi Cement Company.
4.4.1.3 Fixed Assets to Long Term Debt Ratio

The fixed assets to long term debt ratio is used to determine the solvency of an organization. A firm’s long term debts are normally often secured using fixed assets, which is why creditors are normally interested in this ratio. The higher the fixed assets to long term ratio, the better the firm is in meeting any of its long term debts. Whereas a low ratio indicates that the firm may struggle to pay off its long term financial obligations.

Figure 4.5: Debt to Equity Ratio Trend for EAPCC and Bamburi Cement (2010-2015)

Figure 4.6: Long Term Debt to Total Assets Ratio Trend for EAPCC and Bamburi Cement Company (2010-2015)
4.4.2 Size of the Firm

The size of the firms is measured by the total assets of a company since the cement manufacturing industry is a capital intensive industry. Therefore the number of assets is used to highlight the capacity and the size of the firms. Total assets of a company can be found in the balance sheet. Figure 4.6 shows the total assets for Bamburi have been increasing at an almost steady rate over the past six years, whereas those for EAPCC has maintained a steady increase in assets up until 2015, where the total number of assets increased significantly.

![Figure 4.6: Trend on Size of Assets for EAPCC and Bamburi Cement Company (2010-2015)](image)

4.4.3 Ownership Structure

The study uses the ownership and financial data on EAPCC and Bamburi Cement Company which were both listed on the Nairobi Securities Exchange. Most data could be found on each of the companies websites based on their annual, quarterly and audit reports except for the data on ownership concentration. The data on ownership concentration were hand-collected from each firm’s annual reports. Three ownership structures were used in the study. In place for ownership concentration, the percentage shares held by a controlling shareholder (labeled as CR1) is used.

The controlling shareholder refers to a group of shareholders who control the company such as shareholders owning substantial equity stake in a company, their family members and affiliated entities. Foreign ownership is measured by the percentage of shares held by
foreign investors (FOR) and institutional ownership is measured by the percentage of shares held by institutional investors such as pension funds, government bodies (INS). Table 4.2 and 4.3 represents the ownership structure of the cement manufacturing companies under the study.

**Table 4.2: Ownership structure of EAPCC as per domicile as at 2015**

<table>
<thead>
<tr>
<th>Domicile</th>
<th>No. of Shares</th>
<th>Percentage</th>
<th>No. Of Holders</th>
</tr>
</thead>
<tbody>
<tr>
<td>Foreign Institutions</td>
<td>26,622,276</td>
<td>29.58%</td>
<td>29</td>
</tr>
<tr>
<td>East African Community</td>
<td>25,325</td>
<td>0.03%</td>
<td>9</td>
</tr>
<tr>
<td>Local Institutions</td>
<td>61,801,366</td>
<td>68.67%</td>
<td>133</td>
</tr>
<tr>
<td>Local Individuals</td>
<td>1,551,033</td>
<td>1.72%</td>
<td>982</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>90,000,000</strong></td>
<td><strong>100.0%</strong></td>
<td><strong>1,153</strong></td>
</tr>
</tbody>
</table>

**Table 4.3: Ownership Structure of EAPCC as per Shareholder as at 2015**

<table>
<thead>
<tr>
<th>Name of Shareholder</th>
<th>Shares</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Board of Trustees National Social Security Fund</td>
<td>24,300,000</td>
<td>27.00%</td>
</tr>
<tr>
<td>(NSSF)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>The Permanent Secretary to the National Treasury</td>
<td>22,799,505</td>
<td>25.30%</td>
</tr>
<tr>
<td>Cementia Holdings AG</td>
<td>13,180,442</td>
<td>14.60%</td>
</tr>
<tr>
<td>Associated International Cement Limited</td>
<td>13,144,442</td>
<td>14.60%</td>
</tr>
<tr>
<td>Nairobi Nominees Ltd A/C BCL</td>
<td>11,265,068</td>
<td>12.50%</td>
</tr>
<tr>
<td>Kestrel Capital Nominees Ltd A/C 006</td>
<td>725,627</td>
<td>0.80%</td>
</tr>
<tr>
<td>Gidjoy Investments Limited</td>
<td>700,000</td>
<td>0.80%</td>
</tr>
<tr>
<td>Kestrel Capital Nominees Ltd A/C 007</td>
<td>496,380</td>
<td>0.60%</td>
</tr>
<tr>
<td>Kenya Commercial Bank Nominees Limited A/C 885</td>
<td>450,000</td>
<td>0.50%</td>
</tr>
<tr>
<td>Nairobi Nominated Ltd A/C MSV</td>
<td>218,500</td>
<td>0.20%</td>
</tr>
<tr>
<td>Other Shareholders</td>
<td>2,720,036</td>
<td>3.00%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>90,000,000</strong></td>
<td>100%</td>
</tr>
</tbody>
</table>
Table 4.4: Ownership Structure of EAPCC as per Domicile as at 2015

<table>
<thead>
<tr>
<th>Domicile</th>
<th>No. of Shares</th>
<th>Percentage</th>
<th>No. Of Holders</th>
</tr>
</thead>
<tbody>
<tr>
<td>Foreign Institutions</td>
<td>242,688,358</td>
<td>66.9%</td>
<td>51</td>
</tr>
<tr>
<td>Foreign Individuals</td>
<td>615,020</td>
<td>0.2%</td>
<td>63</td>
</tr>
<tr>
<td>Local Institutions</td>
<td>105,223,714</td>
<td>29.0%</td>
<td>662</td>
</tr>
<tr>
<td>Local Individuals</td>
<td>14,432,183</td>
<td>4.0%</td>
<td>2,514</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>362,959,275</strong></td>
<td><strong>100.0%</strong></td>
<td><strong>3,290</strong></td>
</tr>
</tbody>
</table>

Table 4.5: Top Shareholders of Bamburi Cement Company as at 2015

<table>
<thead>
<tr>
<th>Name of Shareholder</th>
<th>Shares</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fincem Holdings Limited</td>
<td>106,360,798.00</td>
<td>29.30%</td>
</tr>
<tr>
<td>Kencem Holdings Limited</td>
<td>106,360,797.00</td>
<td>29.30%</td>
</tr>
<tr>
<td>Standard Nominees RES A/C KE 11396</td>
<td>55,150,278.00</td>
<td>15.19%</td>
</tr>
<tr>
<td>Paramount Company Limited</td>
<td>7,200,000.00</td>
<td>1.98%</td>
</tr>
<tr>
<td>Amarjeet Baloobhai Chhotabhai Patel</td>
<td>5,000,990.00</td>
<td>1.38%</td>
</tr>
<tr>
<td>Standard Chartered Kenya Nominees A/C KE 11916</td>
<td>3,411,560.00</td>
<td>0.94%</td>
</tr>
<tr>
<td>Standard Chartered Kenya Nominees Ltd A/C KE 002258</td>
<td>2,500,000.00</td>
<td>0.69%</td>
</tr>
<tr>
<td>Standard Chartered Nominees Ltd A/C KE 22446</td>
<td>2,191,600.00</td>
<td>0.60%</td>
</tr>
<tr>
<td>Standard Chartered Non Res A/C KE 9273</td>
<td>2,173,700.00</td>
<td>0.60%</td>
</tr>
<tr>
<td>Standard Chartered Nominees A/C 9098 AC</td>
<td>2,158,355.00</td>
<td>0.59%</td>
</tr>
</tbody>
</table>

4.4.4 Hypothesis Testing for Ownership Structure

The study sort to establish whether ownership structure influenced the financial performance of the companies. Therefore a hypothesis was developed so as to establish the relationship between the two variables. As per the below tables we can observe that the relationship between the top 3 shareholders and the financial performance was significant whereas for EAPCC it was not.
Table 4.6: T-test for Ownership Structure and Financial Performance

<table>
<thead>
<tr>
<th></th>
<th>Coefficients</th>
<th>Standard Error</th>
<th>t Stat</th>
<th>P-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bamburi Top 3</td>
<td>0.288</td>
<td>0.046</td>
<td>6.230</td>
<td>0.025</td>
</tr>
<tr>
<td>Shareholders</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>EAPCC Top 3</td>
<td>0.175</td>
<td>0.061</td>
<td>2.863</td>
<td>0.103</td>
</tr>
<tr>
<td>Shareholders</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

4.5 Profit Margin Trend for EAPCC and Bamburi Cement Company

The figure 4.8 below presents the financial performance trend of both EAPCC and Bamburi Cement Company which are under study. The higher the trend the higher the corporate financial performance of the organization.

![Figure 4.8: Trend on Financial Performance for EAPCC and Bamburi Cement Company (2010-2015)](image)

4.6 Capital Structure Trend for EAPCC and Bamburi Cement Company

Taking into account that internal factors are critical to the management of cement companies for financial performance. The aim of cement companies is to therefore maximize the potential of its internal factors so as to improve their financial performance. As per figure 4.6 and 4.7 Bamburi has the highest fixed assets to long term debt ratio as well as the number of fixed assets whereas EAPCC has the highest debt to equity ratio, debt to asset ratio and gearing ratio over the period under study.
4.7 Relationship between Internal Factors and Financial Performance

Regression analysis was performed for both companies, with the independent variables being debt to equity ratio (der), debt ratio (dr), gearing ratio (gr), long term debt to assets ratio (ltar), and total assets (ta). Return on assets (ROA), Return on sales (ROS) and Return on Equity (ROE) which are ratios that determine financial performance represented the dependent variables.

From the table 4.7 to 4.8, the Pearson correlation indicated the relationship between the independent variable to dependent variables. A Pearson’s correlation value that is close to 1 indicates that the relationship is either strongly positively or negatively correlated. To
further improve the importance of the Pearson’s correlation figure a sig (2-tailed) value that is less than or equal to 0.05 implies that there is a significant relationship between the independent and dependent variables.

4.7.1 Effect of Ownership Structure on Financial Performance

In the study the analysis established that the diversity in the top 3 shareholders of both companies affected the financial performance differently. In the case of Bamburi Cement Company the top 3 shareholder had a significant relationship with the financial performance of the company since its P-values were lower than 0.05. EAPCC on the other hand had an insignificant relationship with its financial performance.

4.7.2 Effect of Capital Structure on Financial Performance

In the study the analysis determined that despite the debt to equity ratio (der), the debt ratio (dr), and the gearing ratio all being negatively correlated to the return on equity, return on assets and the return on sales for Bamburi Cement company and the long term debt to assets ratio being negatively correlated to the Return on assets, return on sales while it is positively correlated to the return on equity, their relationship is not statistically significant. On the other hand in the case of EAPCC, both the debt to equity ratio (der), long term debt to asset ratio, the gearing ratio and debt ratio (dr) have a statistically significant relationship with return on equity (roe), return on assets and the return on sales because their Pearson correlation sig. (2-tailed) values are lower than 0.05.

4.7.3 Effect of Assets on Financial Performance

In the case of Bamburi Cement Company, the size of the fixed assets of the company has a significant relationship with the return on assets, return on sales and the return on equity because their Pearson’s correlation sig (2-tailed) values are below 0.05. On the other hand the study determined that EAPCC had a less than significant relationship between the size of their fixed assets and the variables of financial performance. This was regardless of the fact that the Pearson correlation figures.
Table 4.7: Relationship between Internal Factors and Financial Performance of EAPCC (2010-2015)

<table>
<thead>
<tr>
<th></th>
<th>Return on Assets</th>
<th>Return on Equity</th>
<th>Return on Sales</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Return on Assets</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pearson Correlation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Return on Equity</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pearson Correlation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Return on Sales</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pearson Correlation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Debt to Equity Ratio</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pearson Correlation</td>
<td>-.762</td>
<td>-.806</td>
<td>-.736</td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td>.078</td>
<td>.053</td>
<td>.096</td>
</tr>
<tr>
<td><strong>Debt Ratio</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pearson Correlation</td>
<td>-.878*</td>
<td>-.870*</td>
<td>-.891*</td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td>.022</td>
<td>.024</td>
<td>.017</td>
</tr>
<tr>
<td><strong>Long Term Debt to Assets Ratio</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pearson Correlation</td>
<td>.932**</td>
<td>.889*</td>
<td>.967**</td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td>.007</td>
<td>.018</td>
<td>.002</td>
</tr>
<tr>
<td><strong>Gearing Ratio</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pearson Correlation</td>
<td>-.850*</td>
<td>-.864*</td>
<td>-.846*</td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td>.032</td>
<td>.026</td>
<td>.034</td>
</tr>
<tr>
<td><strong>Size of Fixed Assets</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pearson Correlation</td>
<td>.906*</td>
<td>.853*</td>
<td>.932**</td>
</tr>
<tr>
<td>Sig. (2-tailed)</td>
<td>.013</td>
<td>.031</td>
<td>.007</td>
</tr>
</tbody>
</table>

* Correlation is significant at the 0.05 level (2-tailed).

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

This chapter has underlined the findings of the study based on the research objectives. The first section has introduced the chapter and was followed by general information on both Bamburi Cement Company and EAPCC. The next sections have emphasized the findings on components of financial performance, components of internal factors, the financial performance trend, the internal factors trend then the multivariate regression of corporate data under study and finally the relationship between the internal factors and financial risk. The next chapter gives the chapter summary, discussions, conclusions and recommendations.
CHAPTER FIVE

5.0 DISCUSSIONS, CONCLUSION AND RECOMMENDATION

5.1 Introduction

This chapter combines four sections including: summary of findings, discussions, conclusions and recommendations of this research. The purpose of this study was to analyze the effect of internal factors on the financial performance of cement manufacturing companies in Kenya. This chapter focuses on the discussions and conclusions of the findings in line with the research questions; it ends with the recommended practice, improvement and clear suggestions for future researchers.

5.2 Summary

This study was driven by the following questions: How does ownership structure influence the financial performance of cement manufacturing firms in Kenya? How does capital structure influence financial performances of cement manufacturing firms in Kenya? How does the size of the firm denoted by assets influence the financial performances of cement manufacturing firms in Kenya? The study used a predictive research design and secondary data from financial statements which had been published on their company websites.

The stratified and random sampling was used where two companies from the three listed cement manufacturing firms listed on the Nairobi Securities Exchange (NSE). The data was drawn from the annual financial statements ranging from 2010 to 2015. The study used tables, figures for financial performance trend, and internal factors trend, and the multivariate regression from STATA software for the effect of internal factors (debt to equity ratio (der), debt ratio (dr), gearing ratio (gr), long term debt to assets ratio (ltar), and size of total assets (ta)) on financial performance (ROA, ROE and ROS), and for the correlation SPSS software was used to show the relationship between financial performance (ROA, ROE and ROS) and the internal factors (DER, DR, GR, LTAR and TA) to answer the research questions.

The ratios were selected to compute the financial performance and internal factors. In this study the financial performance was determined by the three following ratios; return on
Internal factors and financial performance ratios were the determining force to achieve the findings in line with the objectives of the study. Return on assets (ROA), return on equity (ROE), and the return on sales (ROS) are the key indicators of firms’ financial performance while debt to equity (DER), debt ratio (DR), gearing ratio (GR), long term debt to assets (LTAR) and the size of fixed assets (TA) were found to be an efficient representative for a firm’s internal factors of the cement manufacturing companies under study. The predictive model comprising of ratios was found to be statistically significant for some ratios and not as significant in others the model was also affected by the type of company that was been assessed. This study found that in Bamburi Cement Company the there was a significant negative correlation between the size of its fixed assets their financial performance. On the other hand in the case of EAPCC, the debt to equity ratio, the debt ratio, long term debt to assets ratio and the gearing ratio all had a significant negative correlation to the financial performance of the company. The size of fixed assets of the organization had a statistically significant positive correlation with the financial performance. However, it is crucial to take into account that the combination of ratios offered a better predictive model than a single ratio.

5.3 Discussion

5.3.1 Financial Performance of the Organizations

The study has presented that financial performance is comprised of three components namely return on assets (ROA), return on equity (ROE) and return on sales (ROS). From the two cement manufacturing companies under the study both of them had various return on assets (ROA), return on equity (ROE) and return on sales (ROS) which were the main assets (ROA), return on equity (ROE), and return on sales (ROS). Microsoft excel was used for the tables and figure construction which aided the deeper understanding for this study. Presenting the trend of financial performance and internal factors of the two cement manufacturing companies that are listed on the Nairobi Securities Exchange under study was done in order to understand the financial state of these companies. STATA software was used in this study to compute the correlation between the effect of the internal factors (DER, DR, GR, LTAR and TA) as the independent factor and the degree of its relationship with the financial performance (ROA, ROS, and ROE). This software was since it was more efficient for multivariate regression of data whereby there is more than two dependent variables (financial performance ratios).
indicators of financial performance. The manner in which management of a company balances the three components is the bone of contention in financial performance. The study has shown that the two companies that are been evaluated are using these three components which include return on assets (ROA), return on equity (ROE) and return on sales (ROS) as their main sources of financial performance.

This is viable and consistent with a large number of investors and analysts tend to focus on place a large emphasis on financial performance indicators such as return on assets (ROA), return on equity (ROE) and return on sales (ROS), and the retained earnings ratio related to equity when measuring the sustainable growth (Johnson and Soenen, 2013). Findings of this study indicated that a company should not use a single component to determine their financial performance. As per Tafri et al. (2009), Qin and Pastory (2012) and Rusiqa (2013), they state that the financial performance is determined by three component which are return on assets (ROA), return on equity (ROE) and return on sales (ROS).

The two companies under the study are both listed on the Nairobi Securities Exchange, this implies that these companies are able to easily access funds and in particular debt financing. As such it is easier to use these two companies in the study than the companies that are unlisted. This research is in agreement with Zuhura (2014) where he carried out a study to evaluate the inverse relationship of financial risk and financial performance in commercial banks in Tanzania and Entrepreneurial Risk and Performance: Empirical Evidence of Romanian Agricultural Holdings (Burja, 2013). Both Zuhura (2014) and Burja (2013) used these three components of financial performance which are mentioned above in their study.

The two companies under study had various return on assets (ROA), return on equity (ROE), and return on sales (ROS) during 2010-2015. All these components of financial performance have indicated the level of cement manufacturing companies performance used in this study. The return on assets (ROA), highlights the organizations efficient management in generating the net income from the institutional resources (Khrawish, 2011). Of the two companies Bamburi Cement Company had the highest annual average return on assets (ROA) of 14.77% whereas EAPCC had an average annual return on assets of 5.96%.
The return on equity (ROE) ratio is used to indicate the corporate’s efficiency in using the shareholders’ funds (Khrawish, 2011). Bamburi Cement Company had the highest average annual return on equity (ROE) of 18.73%, this means that the company was efficient in generating profit of 18.73% for every unit of shareholders equity while EAPCC generated 9.73% profit from each unit of shareholders equity that was used. The consistent decrease in return of sales for both the companies indicated the financial troubles (Daly, 2011) that the companies are both facing. Bamburi had the highest average annual return on sales of 19.15% whereas EAPCC had an average annual return on sales of 15.93% which is mainly as a result of a fair gain on an investment property which was realized in 2015.

As per (Khrawish, 2011), the company which enjoys higher returns gives positive signals since it generates more cash internally and a higher return translates to a higher profit (Daly, 2011). From the results of this study the average annual return on assets, average annual return on equity and the average annual return on sales for Bamburi Cement Company are higher than those of EAPCC, this means that Bamburi Cement Company performed well from 2010 to 2015 when compared to EAPCC.

5.3.2 Size of the Firm

The study presented that the size of the firm can be represented using ratios such as long term debt to assets ratio and the size of a company’s fixed assets. The fixed assets to long term debt ratio is used to indicate the solvency of an organization in relation to the extent to which the debts are secured using fixed assets. A high ratio implies that the firm will be able to meet any of its long term debts as when they fall due. Bamburi Cement Company has a consistently higher ratio as compared to EAPCC figure 4.3. The size of assets of a company are considered to be important for companies that are in a capital intensive industry. EAPCC has a higher number of assets when compared to Bamburi Cement Company Figure 4.4.

5.3.3. Effect of Ownership Structure on Financial Performance

The ownership structure of a company is a critical internal factor as they will have an opinion on the investment and capital decisions of a company. In this study it was determined, that EAPCC had a higher concentration of local institutions as their
shareholders whereas Bamburi Cement Company has a higher concentration of foreign intuitions as their shareholders Table 4.6 and 4.7.

The study established that Bamburi Cement Company had a significant relationship between its top 3 shareholders when compared to EAPCC. This may be due to the fact that Bamburi Cement Company has a higher concentration of foreign investors relative to EAPCC whose major shareholders are government institutions.

5.3.4 Capital Structure and Financial Performance

The capital structure of a firm can be represented by use of debt ratio, the debt to equity ratio, and the gearing ratio. The manner in which the company is able to manage these ratio can result in an implication on the financial performance of a company.

The debt ratio, the debt to equity ratio and the gearing ratio were used in different studies for financial performance. Maina & Kondongo (2013) determined that there was a significant inverse relationship between the capital structure and all the measures of performance. The debt ratio (DR) is used to indicate the solvency ratio that expresses the total liabilities of a company as the total assets percentage (Choi, 2010). EAPCC has the highest debt ratio from 2010 to 2015 this implies that EAPCC uses more of its debt to finance its assets when compared to Bamburi Cement Company in Figure 4.1. if the debt to equity ratio (DER), the company is considered to be not solvent and its activity is on high risk (Miles, 2010). If the ratio increases, then the company will experiences difficult situation because it is financed by their creditors rather than its internal resources which may result in a dangerous trend (Sangmi and Nazir, 2010). EAPCC had a consistently higher ratio from 2010 to 2015 as compared to Bamburi Cement Company Figure 4.2.

5.3.5 Financial Ratios that are Most Accurate to Predict the Effect of Internal Factors on Financial Performance

In this study the debt ratio was the first accurate indicator of internal factors, secondly debt to equity and thirdly the gearing ratio. These three play the highest impact on financial performance for the cement manufacturing companies under study from 2010 to 2015. These internal factor ratios are statistically significant and correlate with the financial performance ratios (return on assets, return on equity and return on sales).
5.4 Conclusions

5.4.1 Relationship between ROA, ROE and ROS

Financial performance has three main components namely return on assets (ROA), return on equity (ROE), and return on sales (ROS). The study has established that there is a strong positive relationship between the financial performance ratios. Companies should be able to balance these three ratios for profit maximization and risk minimization. As per Samad and Glenn (2012), the financial performance is used to forecast the success or failure of a firm. Cement manufacturing companies that are listed in the Nairobi Securities Exchange have easy access to funds as compared to those that are not listed. These companies should therefore increase their performance so as to be able to generate more funds and attract investors so as to generate more revenues.

5.4.2 Relationship between Capital Structure and Financial Performance

This study has highlighted two ratios that are related to the capital structure namely, the debt to equity ratio and the debt ratio (DR). The efficient management of these ratios has a positive implication on the financial performance of the company. From this study it has been highlighted that listed firms which have good management of their capital structure ratios have an easier access to funds when compared to firms that having poor capital structure ratios.

5.4.3 Relationship between Ownership Structure and Financial Performance

The study determined that firms which have a higher percentage of owners who are from foreign institutions usually have a buffer when it comes to the financing options that are available to them. In the case of Bamburi Cement Company and EAPCC, Bamburi was able to avoid buffer themselves from accessing financing due to the fact that it was a subsidiary of a large foreign cement manufacturing company. EAPCC on the other hand had high financing cost as a result of seeking financing from local financial institutions.

5.4.4 Relationship between Size of the Firm and Financial Performance

This study determined that while cement manufacturing companies rely heavily on its assets to increase performance care must be taken to ensure that the relationship between the size of assets and financial performance is monitored. Bamburi Cement Company was seen to have a negative correlation between its assets and the financial performance and
this would indicate that they either need to increase their operations or reduce the size of their fixed assets. EAPCC on the other hand had a strong positive relationship between their fixed assets and the resulting financial performance.

5.4.5 Financial Performance Trend for Cement Companies

From this study, cement manufacturing companies that are listed should boost their financial performance since it signifies their good performance. These companies should focus on their return on assets (ROA), return on equity (ROE), and return on sales (ROS) since these three ratios are used to signal that their ability to access more funds so as to generate more revenue.

5.4.6 Internal Factors Trend for Cement Companies

The companies under study should maximize the efficiency of their internal factors by ensuring that they monitor the relationship between the factors and the financial performance. Bamburi Cement Company should take time to monitor the size of their fixed assets and its effect on their performance. This is because currently the company has a strong negative correlation between its assets and their performance. EAPCC on the other hand should focus on their debt to equity ratio, their long term debt to asset ratio as well as their gearing ratio.

5.5 Recommendations

5.5.1 Recommendations for Improvement

5.5.1.1 Components of Financial Performance

Cement manufacturing companies that are listed on the Nairobi Securities Exchange should be managed effectively and efficiently in relation to their financial performance ratios namely return on assets (ROA), return on equity (ROE), and return on sales (ROS). Cement manufacturing companies should focus on ensuring sustained financial performance trade off to keep the continuation of their business. Firm managers should be sure that they grow their financial performance in an efficient and effective manner so as to generate their assets in order to maximize the revenue that is generated from their business ventures.
5.5.1.2 Components of Internal Factors

This study considered three main internal factors that is the capital structure of the firm, the size of the company in terms of fixed assets and the ownership structure. These three were represented using these ratios: debt to equity ratio, the debt ratio (DR), fixed assets to long term debt ratio, size of fixed assets. Firm managers should monitor the relationship between the internal factors and its financial performance so as to ensure that they maintain optimal performance. They should wisely monitor their debt to equity ratio and the debt ratio so as to minimize their risk and ensure that they avoid bankruptcy. Cement manufacturing companies should focus on maintaining consistent financial performance through the efficient management of their internal factors.

5.5.1.3 Financial Performance Trend of Cement Companies

The cement companies listed should place emphasis on analyzing their financial performance trend. In other words good financial performance comes from positively concentrating on their return on assets (ROA), return on equity (ROE), and the return on sales (ROS). Firm managers should monitor firm’s signals so as to maintain diligent financial performance which is necessary for the generation of more revenue due to an increase in the access to funds.

5.5.1.4 Internal Factors Trend on Cement Companies

The cement companies should take time to analyze the effect of their internal factors on financial performance. Firm mangers should wisely work on their debt ratio minimization and be aware of their debt to equity ratio management and the optimal size of assets that are required in order to avoid company bankruptcy and improve efficiency and performance.

5.5.1.5 Effect of Internal Factors on Financial Performance

The cement manufacturing companies should balance the relationship between the internal factors ratios and their financial performance ratios. Especially, the following internal factors ratio: debt to equity ratios, debt to assets ratio, size of fixed assets, fixed assets to long term debt ratio and gearing ratio which have a significant effect in the financial performance. The empirical evidence form the firm’s income statements will help cement manufacturing companies to hold on to their success by maximizing their financial performance and avoid bankruptcy. The cement companies that are listed on the
Nairobi Securities Exchange should be able to balance their financial performance ratios as well as maximizing the efficiency of their internal ratios so as to maximize their profits in order to access more funds and attract investors with the target of increased revenue generation.

### 5.5.2 Recommendations for Further Research

This study has only focused on the comparative analysis on internal factors on the financial performance of cement manufacturing companies that are listed on the Nairobi Security Exchange. Further research should be done on how these factors combine with external factors affect the financial performance of all the cement manufacturing companies that are listed on the Nairobi Securities Exchange.
REFERENCES


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## APPENDICES

### APPENDIX 1: Financial Performance and Internal Factor ratios

<table>
<thead>
<tr>
<th>Financial Ratios</th>
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APPENDIX 2: Data for the Cement Manufacturing Companies Listed in the Nairobi Securities Exchange under Study

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<td>2011</td>
<td>2012</td>
<td>2013</td>
<td>2014</td>
<td>2015</td>
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<td>-</td>
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