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EFFECT OF BUDGETARY CONTROL PROCESS ON FINANCIAL PERFORMANCE OF TEA FACTORIES:A STUDY OF SELECTED TEA FACTORIES IN KISII COUNTY,KENYA

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Abstract

The aspects of budgeting and budget control have a great significance amongst the procedures applied in organization's planning and control functions. Currently, tea processing has been recording poor performance which has resulted from ineffective and inefficient budgets and budget control systems leading inadequate allocation of resources. The main objective of this study was to assess the effects of budgetary control on the financial performance of tea factories in Kisii County. Specifically, it sought to establish the effect of budget planning, budget execution and budget monitoring on the financial performance of tea factories in Kisii County. A correlational research design was used in this study. The study selected the entire population of 70 top management of the tea factories. Both primary and secondary data were used through questionnaires and document analysis and analyzed using descriptive statistics, regression and correlation. The results show that: budget planning, budget execution and budget monitoring have a positive significant effect on financial performance of the tea factories. The study thus recommends that: the tea factories should ensure that budget controllers are well trained through in-service training to ensure that they are able to competently deal with budget planning at the private service. Their terms of reference should go beyond surface risk assessment to effectively identifying financial threats to which will later be dealt with effectively with a robust system of budget planning as an important financial management objective. They should continue using the already workable budgeting strategies that have enabled an effective budget monitoring. The tea factories should ensure that budgeting goes beyond financial transactions to financial control by expanding the scope of budgeting at their organizations. The budget controllers should be motivated to delve deeper into financial matters of the private service.

Keywords: Budgetary control, budget planning, budget execution and budget monitoring

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I. INTRODUCTION

1.1 Background of the Study

Many business firms have identified the need to develop comprehensive budgetary control systems for the purposes of minimizing variances, costs and maximize efficiency in the budget (Alesina&Perotti, 2014). Budgetary control is a key aspect because any waste, stock out or even theft can lead to poor business performance. Organization resources needs to be managed in the most effective and efficient manner for purposes of achieving the intended objectives and goals. This indicates that organization should be able to achieve the desired objective cost effectively through minimization of cost. Thus managing implies proper co-ordination and control of the organization efforts towards achieving the organization objectives.

Several theoretical and empirical studies conducted in the world show that the effect of budgetary control system is not direct. For example, several studies conducted in the United States of America show that budgetary control practices have a positive and significant effect on organizational financial performance. Other studies conducted in Asia show that budgetary controls can stifle the performance of employees. For example, Lesina andPerotti(2014) who conducted a study in they argued that management charts facilitates the managing process in the future course of some objectives and even decision making process in the most professional manner through proper utilization of individual and group efforts in a coordinated way. Budgeting is the best way to achieve effective organization performance. Budgets are regarded as monetary expressions with certain targets to be accomplished in a particular year by given individuals, organization, group or even nation. It tries to realize superior outcomes over time with the obtainable and expected resources. These particular targets are often influenced by the previous experiences and future expectations (Atkinson, Banker Kaplan and Young 2011).

Budget system facilitates more effective management plan with co - ordinate, controlled and well evaluated activities. It is a tool which is intended to give greater effectives as regards to organizational efficiency achievement (Chenhall & Langfield, 2014). For this to be achieved, the functional aspects need to outweigh the dysfunctional aspects. Due to the existence of a budget plan, decisions cannot be merely done through spontaneous reactions to stimuli in unclassified environment goals. It is essential to highlight that management actions are the driver element in every entity and of course essentially unavoidable (Hansen, David & Van der Stede, 2003). Some of the management activities include planning, organizing, directing, controlling and directing economic resources. However, it is important to systematically and objectively assess the efficiency and effectiveness effect of the activities in the light of the budget. Therefore, there is a lot of concern on the adoption of budgetary procedures to evaluate management activities and organizational financial performance (Lazaridis & Try Fonidis, 2006).

Tea processing is supposed to take into consideration both financial and non-financial processes together (Hokal & Shaw, 2014). A key aspect is that before reviewing is done on the financial variances, any firm is supposed to question about its expected position in the business environment based on the understanding of what has taken place, what will happen and any unexpected and planned events to take place. It is important to conduct appropriate structuring of the planned actions against time frames and operational actions (Drury, 2006); Hokal & Shaw (2014).

The main challenges facing the tea processing sector includes the ever increasing cost of production due to increasing factors such as the high cost of power, tax administration, regulations and poor infrastructure. There is a lot of decreased demands for the locally processed tea due to the rising poverty among the citizens and reduced exports. Other challenges include; security issues with recent cases of terror attacks, arbitrary charges levied by regulatory and local authorities, inadequate government support for local produce, weak linkages with local suppliers. However, opportunity for growth exists with the roll out of common tariff under the integrated EAC customs union since Kenya's manufacturing sector is the largest in the region (Kenya's Economic Outlook, 2013).

1.2 Statement of the Problem

In the most recent times, tea factories have recorded dismal performance due to inadequate budgets and budget control systems to facilitate adequate allocation of resources thus achievement of organizations objectives and goals as well as performance maximization. A study conducted by Bocquist (2011) in Netherlands found that companies performance has kept on decreasing due to the flawed budgetary planning and control systems, which most of this companies management have not yet recognized. Some firms have weak budgetary analysis but they tend to take it as an individual problem rather a budgetary system control challenge. This rather misdirect effort had led to increased frustration. As a result, the alignment of capital allocation has been the biggest challenge in disapproving financial performance. Some firms so far are not able to understand the link between budgetary control and performance and this has highly affected their performance negatively. Most of the organizations from small scale business to large scale business have not yet identified the power of budgets and budgetary control when it comes to performance outcomes. Most organizations concentrate on production without keeping an eye on improving their budgets performance.

Kipkemboi (2013) conducted a study on the effect of budgetary control on performance on non-governmental organizations (NGOs) in Kenya. His findings collaborate with those of Munene. In his study it was found out that budgets are often adopted for purposes of planning, monitoring and also control. He also noted that there is a slight positive relationship between the budgetary controls and organization performance. He recommended that budgetary control may not be the only reason for not achieving high performance; rather there is many other factors which affected the performance of the NGOs. It is clear from the review that there are no studies that have been conducted to assess the effect of budgetary control process on financial performance of tea factories in Kenya. This study therefore sought to fill this gap of knowledge by assessing the effect of budgetary control processes on financial performance of tea factories in Kenya.

1.3 Objective of the Study

1.3.1 General Objective

The main objective of this study was to assess the effect of budgetary control process on financial performance of selected tea factories in Kisii County.

1.3.2 Specific Objectives

- To establish the effect of budget planning on the financial performance of factories in Kisii County.
- To determine the effect of budget execution on the financial performance of tea factories in Kisii County.
- To assess the effect of budget monitoring on the financial performance of tea factories in Kisii County.

II. LITERATURE REVIEW

2.1 Theoretical Review

2.1.1 Agency Theory

An agency relationship refers to an agreement which involves two or more persons that is (principal(s)) and the other party usually the agent. This agent conducts certain activities or functions as directed from the principal. This principal in this case delegates some functions which involve decision making to a given agent (Jensen and Meckling 1976). The agency theory is based on the assumption that both the principles and the agents interests should diverge. However, it is noted that the principal can limit this particular divergence from his or her interest through establishment of certain incentive to the agent developed to limit opportunistic conduct from the agent. In corporate structure, a given organization management its board of directors act as agents on behalf of the firms owners or shareholders (Hill and Jones, 1992). Since the managers who run the tea factories are agents of the farmers and may act in their own best interests, this theory is relevant in underpinning the study variables of budgetary control and firm financial performance.

2.1.2 Control and Responsibility Accounting Theory

Control refers to a comparison process between the standard and the real performance, with comparisons served on the grounds of determining the appropriate responses to actual expected results. At the point when the stand point of direct relationship is planning then most appropriately it turns to be a complementary to planning (Simiyu, 2009). According to Hopwood (1976) argued that that are three forms of work control in organizations which include; social controls, administrative controls and self-controls. The administrative controls comprises of performance system approaches and budgeting monitoring techniques. The social controls refers to those controls that operate via employee sharing common objectives such as quality circles and team work. Self-controls emanate from individual character and they tend to be influenced by suitable system of rewards. It is noted that this forms of control take an interrelated pattern.

2.3 Conceptual Framework

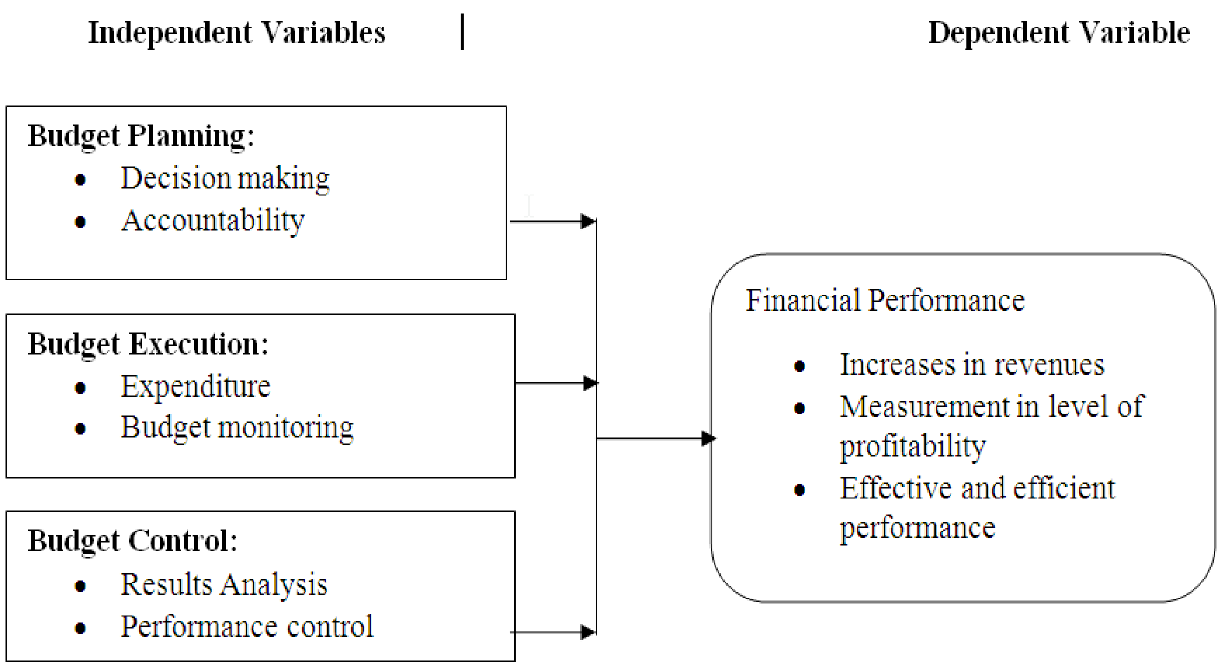

Figure 2.1: Conceptual Framework

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2.3 Empirical Literature

Sizer (2009) noted that planning form part of the budgeting system. Budgeting system comprises of activities such as long range planning, strategic planning and short term planning. The author emphasized on short term planning with more focus on human and financial resources in a particular organization. Arora (2015) established that budget planning involves selecting objectives and various actions to achieve those particular objectives. Planning acts as a tool for forecasting.

The importance of budget has resulted to conflicting results among authors. Sterdy (1960) and Cherrington and Herrington (1973) indicated that there was a negative relationship between participation and organizational performance. Additionally, Cress and Pettijohn (2015) conducted a surveyed on 219 publicly traded US Companies and established that 79 percent of the companies involved in the study revealed that low level managers had a significant role in both the initial and other stages of budget preparation.

Carr (2011) highlighted that managers control budget activities for which they are given authority. Analysis of variances helps managers to identify costs which don't conform to the long term plan thus requiring alteration through studying the various reasons for establishing budget inefficiencies. The budget forms the basis of controlling various resources in an organization. However, these studies did not assess the effect of budget control processes and financial performance of tea manufacturing firms in Kenya.

Drury (2006) argued that budgetary monitoring and control approaches is a continuous and systematic process which is associated with the following stages;formulating targeted performance for each department in a given organization. Communicating of budgetary policy particulars to all stakeholders for easy support of the set targets and objectives and hence facilitate ownership of the outcome. This is a continuous process whereby actual results is compared against the budgeted performance and regular reporting of variance to the relevant authorities. This enables the responsible officers to get the facts between actual and budgeted performance.

Briston (2001) argued that financial control and monitoring facilitates efficient and cost effective approaches adoption within the accountability system. He however stated that, the available financial control arrangements are subjected to improvements for effective monitoring in better budget implementation with regards to the required work programs.

Ambetsa (2014) carried out a survey study of budgeting practices by commercial airlines operating at Wilson Airport, Nairobi whereby it was noted that some challenges were faced during budget evaluation leading to deficiencies, some individuals refused to participate in the budget preparation and inadequate management support was also stated. The study concluded that airlines employed the budget, implement it and evaluate its organization performance. Most business enterprise have adopted system or informal way of making use of the budget however, the big question lies on the effectiveness on the implementation of the budget.

Muleri (2011) did a survey on budgeting practices among the British non-governmental development organizations in Kenya and established that quite a number of organizations have adopted budgeting modern measures and philosophies that facilitate control of financial mismanagement. Budgets have been used to enhance cost effectiveness especially in planning for productions, co-ordination of activities as well as auditing (Muleri, 2011).

III. RESEARCH METHODOLOGY

3.1 Research Design

This study employed a co relational research study. A correlational research study attempts to provide results on particular characteristics of a given population or phenomenon (Mugenda & Mugenda, 2003).Correlation research design acts as a pre-cursor to quantitative research design which gives a general overview in certain valuable pointers as to regards to variables worthiness testing quantitatively.

3.2 Target Population

This particular study target population was the top management of the tea factories in Kisii County. The Tea factories are managed by KTDA and comprised of the following; - Kiamokama, Nyamache, Itumbe, Rianyamwamu, Eberege and Ogembo. Each tea factory has averagely 12 top management comprising of six directors, the factory unit manager, the factory accountant, the procurement manager, the plant engineer, the factory sales manager and the factory assistant manager. This implies that the target population was 72.

3.3Sample Size and Sampling Procedures

Since the target population was small and manageable, the study selected the entire population of 72 top management and directors. Cooper and Schindler (2003) argued that the most fundamental thing in sampling is to select some of the elements in a given study populationbut only in the event the population is large and thus not manageable. In the event the population is small, they argue that the entire population should be selected to enhance reliability.

3.4 Data Collection Instruments

This particular study used both primary and secondary data. Questionnaires were used for primary data collection from the field. Questionnaires were distributed to various financial managers in the selected firms. This facilitated adequate and accurate information. The researcher had formulated closed ended questionnaires for purposes of getting unique information. The researcher chose questionnaires because they are less costly, convenient and less biased. The secondary data comprised of budgetary records and financial records for various years in data relating to budget verse actual variance in various tea factories. These records were used to complement the raw data.

3.5 Data Analysis Procedure

The study findings comprised of quantitative data. Descriptive statistics was adopted in data analysis. Data was edited for accuracy, uniformity and completeness and later arranged for coding. The Analysis of variation (ANOVA) was used for purposes of analyzing the descriptive statistics. Regression and correlation analysis formed part of the major statistical techniques used in this study.The regression models presented the dependent variable (financial performance) and independent variable (planning, monitoring and control) as expressed in the equation below.

$$\mathbf{Y = \beta o + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \mathcal{E}}$$

Where:-

Y - Financial Performance as measured bylevel of profitability,
β1 - Budget Planning (Revenue allocation to activities/operations)
β2 - Budget Execution
β3 - Budget Monitoring
Ɛ **-** Error term

IV. RESULTS AND DISCUSSION

4.1 Correlation Analysis

As part of the analysis, Pearson's Correlation Analysis was done on the Independent Variables and the dependent variables. The results is as seen on Table 1

Table 1 Correlations

	FM	BP	BE	BM
FM	1			
BP	.655**	1		
BE	.635**	433**	1	
BM	.710**	.205**	.038	1

**** p< .05**

Pearson correlation analysis was conducted to examine the relationship between the variables. Cooper and Schindler (2000) highlighted correlation coefficient matrix(*r*) range from 0.10 to 0.29 is looked at as weak, from 0.30 to 0.49 is looked at as medium and from 0.50 to 1.0 is looked at as strong. However, according to Field (2005), correlation coefficient should not go beyond 0.8, to avoid multi-co linearity, which is not a problem in the present study.

All the independent variables had a positive correlation with the dependent variable with Budget Monitoring having the highest correlation of ($r=0.710$, $p< 0.01$) followed by Budget planning with a correlation of ($r=0.655$ $p< 0.00$) and then Budget execution with a correlation of ($r=0.635$ $p< 0.00$). This indicates that all the variables are statistically significant at the 99% confidence interval level 2-tailed. This shows that all the variables under consideration have a positive relationship with the dependent variable.

4.2 Regression Analysis

Since the measures that are used to assess the primary constructs in the model are quantitative scales, regression analysis can be used to achieve this end. Regression analyses are a set of techniques that can enable us to assess the ability of an independent variable(s) to predict the dependent variable(s). As part of the analysis, Regression Analysis was done. The results is as seen on Table 2, 3 and 4

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Table 2 Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.882[a]	.779	.841	.176

a. Predictors: (Constant), Budget Monitoring, budget planning and budget control

b. Dependent Variable: Financial Performance

From table 4.9 it is clear that the R-value was .882 showing a positive direction of the results. R is the correlation between the observed and predicted values of the dependent variable. The values of R range from -1 to 1 (Wong and Hiew, 2005). The sign of R indicates the direction of the relationship (positive or negative). The absolute value of R indicates the strength, with larger absolute values indicating stronger relationships. Thus the R value at .882 shows a stronger relationship between observed and predicted values in a positive direction. The coefficient of determination R^2 value was 0.779. This shows that 77.9 per cent of the variance in dependent variable (Financial Performance) was explained and predicted by independent variables (Budget Monitoring, budget planning and budget execution).

The F-statistics produced (F = 64.904) (Table 3) was significant at 5 per cent level (Sig. F< 0.05), thus confirming the fitness of the model and therefore, there is statistically significant relationship between Budget Monitoring, budget planning and budget execution, and financial management.

Table 3: Model ANOVA

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	232.743	4	43.096	64.904	.000[a]
	Residual	12.878	64	.664		
	Total	244.511	68			

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b. Dependent Variable: Financial Performance

Table 4. Coefficients

Model		**Unstandardized Coefficients**		**Standardized Coefficients**		
		B	**Std. Error**	**Beta**	**t**	**Sig.**
1	(Constant)	2.767	.361	.287	7.668	.000
	Budget Planning	.385	.078	.393	4.968	.000
	Budget Execution	.168	.065	.193	2.584	.004
	Budget Monitoring planning	.329	.064	.352	5.140	.000

a. Dependent Variable: Financial Management

Results in Table 4 above indicate that all the three variables of budgetary process positively and significantly predict financial performance of the tea factories. This is confirmed by the beta values of (β = 0.385, p = 0.00), (β = 0.168, p = 0.04) and (β = 0.328, p = 0.00) for budget planning, budget execution and budget monitoring respectively. The implication is that when budget planning is improved by a unit, financial performance in the tea factories significantly improves by 38.5% when all other factors are held constant. Similarly, when all other factors are held constant, a unit increase in budget execution leads to a 16.8% significant increase in financial performance in the tea factories. Additionally, it can be concluded that a unit increase in budget execution leads to a 32.8% increase in financial performance holding all other factors constant.

V. CONCLUSIONS AND RECOMMENDATIONS

Based on the objectives and findings of the study, the following are the conclusions:The private service institutions incurred a lot in budget planning. However, budgeting had so far not been effective in managing the risks and risk assessment was not a constitutive element of budget planning that helped in efficient adoption of budgeting. Further, budgeting had so far not been able to effectively identify financial threats to which were later dealt with effectively because the system of Budget planning at the institution was not an important financial management objective. Finally, budgeting overall, had not had a beneficial role to play in risk assessment. It can therefore be concluded that budget planning had a significantly negative influence on prudent financial management in the tea factories.

Budgeting had been helpful in budget monitoring for the offices. Further, through budgeting the management had been able to create proper and workable contingency plans. However, budget monitors had not assisted greatly in ensuring that money did not run out to negatively affect future expenses and costs. Finally, budgeting had made it clear that something will definitely go wrong with finances in the future and something therefore needed to be done. It can therefore be concluded that budget monitoring had a significantly positive influence on prudent financial management in the tea factories.

The private service institutions needed a lot of financial control; however, budgeting was restricted to financial transaction only and did not extend to budget control. Moreover, budgeting had not made financial system errors to be significantly identified in the early stages and had been used mainly to discover fraud but not promote efficiency in financial controls. Finally, therefore budgeting overall had not had a positive influence on financial control in the private service. It can therefore be concluded that budget control had a significantly negative influence on prudent financial management in the tea factories.

Based on the objectives and conclusions this study recommends;The tea factories should ensure that budget controllers are well trained through in-service training to ensure that they are able to competently deal with budget planning at the private service. Their terms of reference should go beyond surface risk assessment to effectively identifying financial threats to which will later be dealt with effectively with a robust system of budget planning as an important financial management objective.

The factories should continue using the already workable budgeting strategies that have enabled an effective budget monitoring. Further, the Ministry of Finance should enact a policy that expands budgeting to offer full scope budgeting commensurate to that of external budgeting. The tea factories should ensure that budgeting goes beyond financial transactions to financial control by expanding the scope of budgeting at their organizations. The budget controllers should be motivated to delve deeper into financial matters of the private service.

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