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Effect of Working Capital Management on Financial Performance: Evidence from Listed Firms at Dare S Salaam Stock of Exchange

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Abstract: *This study focused on examining how management of working capital can affect the financial performance of non-financial companies listed at Dar-es-salaam stock exchange. Financial performance in this study was represented by return on equity and market ratio namely Tobin's q while working capital management was represented by liquidity ratio (current ratio), debtor collection period and inventory turnover ratio. The study used both a descriptive and quantitative research design. Firms listed on-financial at Dar-es-salaam stock of exchange covering the period of 10 years from 2008 to 2017. This study concluded a significant negative relation between debtor collection period and financial performance. While creditor payment period, inventory days and liquidity ratio are positively related with performance. But the relation with creditor payment period and liquidity ratio is significant. The firm must focus on reducing receivable period and increasing inventory days and payable period for them to improve financial performance.*

Keywords*: Working capital , DSE, Dar-es-salaam Stock Exchange, Financial performance*

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I. Introduction

The working capital decision is extremely important and strategic as it affects profitability and the firm's value. Working capital deals with current assets and liabilities has gained significant attention in the challenging economic environment of today. Working capital is an important part of financial management decisions in all firms (Sharma & Kumar, 2011), since it provides enough liquidity to meet day to day cash requirements. It is difficult for the company to reduce working capital to a minimum level without disturbing its normal operation. This means that every company must ensure that their working capital is at an optimal level in a way that doesn't affect their future sales and profit.Every company focuses on the main objective of maximizing the shareholder's wealth. This can be achieved by balances between the aforementioned indicators. Working capital is the sum of the amounts invested in the current assets and working capital management is concerned with determining the volume and compound of the resources so that the shareholder's wealth maximized (Ahmadabadi*et al,* 2013). The amount of working capital a company should carry depends on its sales volume, its need for gross circulating capital relative to its sales volume and the stability of its operation.

1.1 Dar-es-salaam stock exchange

Dar-es-salaam stock exchange (DSE) was incorporated as a private company limited by guarantee (a non- profit-making body) in 1996. It began its operation in 1998. Up to now, DSE listed 28 companies at DSE, 14 licensed brokers and 6 custodian banks. In 2013 the DSE launched a second-tier market, the Enterprise Growth Market (EGM) with lower listing requirement. The EGM is designed to attract small and medium companies with high growth potential. DSE is the third stock exchange in Africa to demutualize after the Johannesburg stock exchange and Nairobi securities exchange.

Many studies have been conducted globally (Abdulrazeez, 2018; Ha, 2016; Kuddumi& Ramadan; 2012, and Makau, 2017). For the case of Tanzania there are few studies conducted (Mtani & Masanja, 2018) conducted study on the impact of working capital on financial performance a case of supermarkets in Arusha city. Also (Ponsian*et al,* 2014) conducted the study on the effect of working capital management of profitability a case of Manufacturing companies listed at Dar-es-salaam stock of exchange. But in my knowledge, there is no study has been made in Tanzania concerning the effect of working capital management on firm performance for non-financial firms listed at Dar-es-salaam stock of exchange. This study seeks to fill this existing gap and answer the question; what effect does the working capital management have on the firm's financial performance for non-financial companies listed at Dar-es-salaam stock exchange.

This study will examine the impact of working capital management on financial performance of companies listed at Dar-es-salaam stock exchangea). to find out whether debtor collection periods improve financial performance of listed firms. b). To find out whether inventory days improve financial performance of listed firms. c). To identify how creditor payment period, improve firm performance of listed firms. d). To identify how liquidity ratio, improve financial performance of listed firms.

II. Literature Review

Many studies have been done to analyze the relationship between a company's management working capital and the company's financial performance in different countries like(Niresh,2012; Yahaya, 2016; Kumaraswamy, 2016 and Almazari, 2014). The result from many studies showed mixed results, but the majority of them showed that there is a negative correlation between financial performance and management of working capital. These researches have used different variables to investigate the correlation between the management of working capital and financial performance by using various methodologies such as time series or linear regression and panel data regression. Some of those researches related to this research are summarized below to examine and establish the research gap.

Abdulazeez, Baba, Fatimac, & Abdulrahaman, (2018)in their study of the impact of working capital management and financial performance for listed conglomerate companies in Nigeria covering the period of ten years from 2005 to 2014. Debtor collections period, creditor payment period and cash convention cycle were used to measure working capital management. Descriptive statistics, ordinary least square (OLS) and regression analysis were used to analyze the data. The study found a negative relationship between debtor collection periods, creditors payment periods and size of the firm with financial performance, while a positive insignificant relationship between cash convention cycle and financial performance. The study suggested that conglomerate companies listed in Nigeria should reduce the debt period in order to improve financial performance.

Mwangi, Makau, & Kosimbei, (2014) the effect of working capital management on the performance of non-financial companies listed in the Nairobi securities. The research design used in this study was explanatory and non-experimental. A sample of 42 non-financial companies covering the period from 2006 to 2012. The study applied to the panel data model, Feasible Generalized Least Square (FGLS) regression result revealed that an aggressive financing policy had a significant positive effect on return on equity while a conservative investing policy was found to affect performance positively. The study recommended that for any non-financial companies listed at Nairobi securities exchange that needs to improve its performance must adopt aggressive financing policy and conservative investing policy.

Hellen Mberia & Willy Muturi (2017)analyze working capital management on the water processing firm's financial performance in Puntland, Somalia. The study covered the period from 2011 to 2015. The period is divided into quarters and the variable of working capital was determined in each quarter. A variable such as cash conversion ratio, stock turnover ratio, payable turnover ratio, and the receivable turnover ratio was used to measure working capital. Multiple linear regressions were used to analyze the data. The analysis indicated that the cash conversion ratio and stock turnover ratio positively affect the return on asset of water companies. Receivable turnover had a negative effect on return on asset while payable turnover had no effect on the return on asset.

From the empirical review above we can see that there are the contradiction results relating to relationship between elements of working capital management and firm performance. Most of the elements of working capital management used were debtor collection period, creditor payment period, inventory days and cash conversion cycle. Return on equity is mostly used as measure of firm's performance.

Some of researchers (Abdulrazeez, 2018andKumarswamy, 2016) evidenced debtor collection period, inventory days are negatively related with firm performance and creditor payment period impact firm's performance. These findings are related to the theoretical evidence. But cash conversional cycle is positively rerated to profitability. On other hand (Yahaya, 2016) evidenced that debtor collection period and inventory days are positively related to financial performance while creditor payment period are negatively related to the firm performance. But (Nour & Soltan, 2015) concluded that payable period and inventory days have positive impact on financial performance. Receivable period has no impact of performance. Many studies conducted on the effect of working capital management on financial performance and revealed contradicting results regarding the relationship between elements working capital management and elements for financial performance. (Nouri & Soltani,2015; Yahaya, 2016; Hasan, 2014 and Ha *et al.* 2016) concluded a positive relationship between elements of working capital management with financial performance. While (Almazari, 2014; Makau, 2018; Usman *et al*, 2017and Angahar & Alematu, 2014) revealed a negative relationship. For the purpose of this study the following hypothesis has been formulated.

H_0 There is no relationship between the debtor collection period and financial performance of listed firms.

H_0 There is no relationship between Inventory days and financial performance of listed firms.

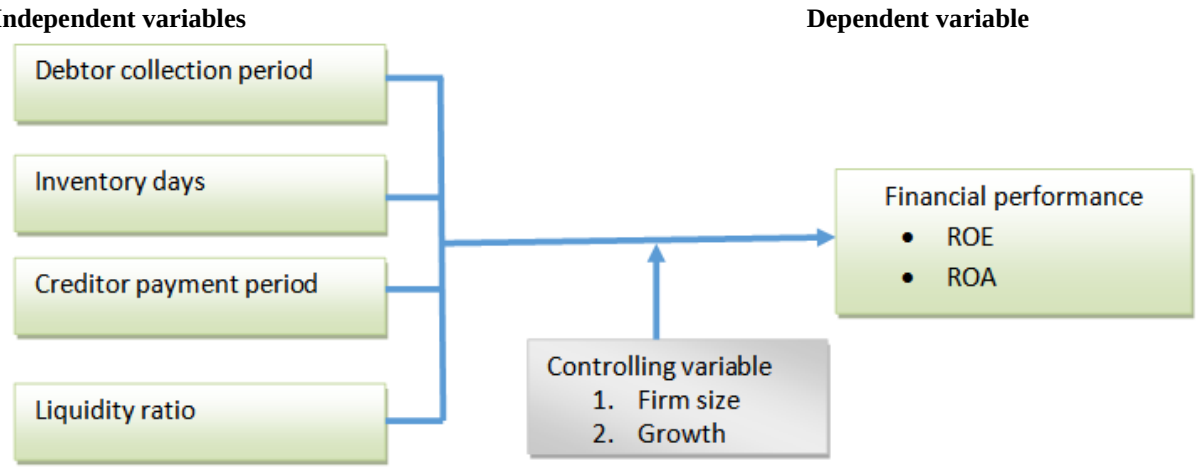
H_0 There is no relationship between creditor payment periods with financial performance of listed firms.

H_0 There is no relationship between liquidity ratio and financial performance of listed firms.

III. Methodology

3.1 Research approach and design

This study used the ex-post facto research design using regression analysis to test for the influence of working capital components on the financial performance of listed companies at Dar-es-salaam stock exchange. The study methodology was descriptive research methodology as it helps to explain each phenomenon characteristic in the study. The dependent variables of the study are Financial performance which were measured by return on equity and Tobin's Q,while independent variables are working capital management was measured by the following variables; creditors payment period, inventory days, debtor's collection period and cash conversion cycle.



This study estimates the equations in the first difference form.
The model that will be used in this study was shown below.

$$\Delta Y_{i1}=\alpha\Delta Y_{i0}+\sum\beta\Delta X_i$$

Where the Y_{i1} representdependent variables, Y_{i0}represent the historical value of dependent variable and X_1, X_2, …….X_n represent independent variable that serve as valid instruments. Instruments for other cross-sectionalequations are constructed in the same way.

3.2 Data collection

The study used secondary data collected from companies registered at Dar-es-salaam stock of exchange.The period covered in this study was from 2008 to 2017. Since the study will use only listed firms in Tanzania and it is statutory requirement for every listed firm to submit audited financial report to Dar-es-salaam stock of exchange. Then those annual reports are published to make them available to the public.Published annual reports from those companies are used as the mains source of the information to describe the variables used in the study and their relationship. These data are obtained from Dar-es-salaam stock exchange and respective company's website.

Table 3.2 Sample size

S/No	Name of the company	Period covered	Number of years
1	Tanzania Breweries Limited (TBL)	2008 - 2017	10
2	Tanzania Cigarette Company (TCC)	2008 - 2017	10
3	Tanga Cement Company Plc (TCCP)	2008 - 2017	10
4	Tanzania Portland Cement Company Limited (TPCC)	2008 - 2017	10
5	TAPETA Limited (TTP)	2008 - 2017	10
6	TOL Gases Limited (TOL)	2008 - 2017	10
7	Swiss port Tanzania Plc (SWIS)	2008 - 2017	10
	Total observation will be;		**70**

IV. Data Analysis And Presentation

4.1 Descriptive Statistics

The descriptive statistics of return on equity (ROE), return on assets (ROA), Tobin's q, debtor collection period (DCP), inventory days (ID), creditor payment period (CPP), liquidity ratio (LR) and the controlling variables that is firm size and growth. This analysis shows mean, medium, standard deviation, skewness and kurtosis. Also, it presents the maximum and minimum value of each variable used which help in getting a picture about the maximum and minimum value a variable has achieved.

Table 4.1: summary descriptive statistics

	N	Minimum	Maximum	Mean	Std. Deviation	Median	Skewness	Kurtosis
	Statistic	Statistic	Statistic	Statistic	Statistic	Statistic	Statistic	Statistic
ROE (%)	70	-2115.75	104.08	-1.81	258.24	31.71	-8.180	67.861
ROA (%)	70	-26.28	48.37	17.02	17.15	20.55	-.560	-.095
TOBINS_Q	70	-2.57	64.45	3.27	7.93	1.88	6.851	52.834
DCP(Days)	70	5.16	118.34	40.44	27.63	35.00	1.059	.700
ID (Days)	70	2.52	371.07	112.55	86.76	103.21	1.203	1.285
CPP(Days)	70	41.94	318.75	117.13	60.86	100.34	1.257	1.232
LR (Times)	70	.30	4.28	1.80	1.00	1.58	.468	-.698
FS (Bil)	70	5.79	1112.61	220.01	274.97	166.68	1.940	3.399
Growth (Bil)	70	-8.57	717.97	132.56	162.16	106.43	1.916	3.917

The table above is the summary statistics of 70 observation of all variable used in this study. The mean value of return on equity is -1.81%this show the poor performance of the firm listed at DSE and standard deviation is 258.24% while the minimum value of return on equity is -2115.75% and the maximum value is 104.08%. Return on assets has a mean value of 17.02% shows with the standard deviation of 17.15% while the minimum value -26.28% and maximum value of 48.37%. Tobin's q has a mean of 3.27, standard deviation of 7.93, minimum value of -2.57 and maximum value of 64.45. On other hand independent variables like average debtor collection period, inventory days and creditor payment period have a mean value of 40.44, 112.55 and117.13 days with the standard deviation 27.63, 86.76 and 60.86days respectively. The minimum debtor collection period, inventory days and creditor payment period are 5.16, 2.52 and 41.94 days respectively, while maximum value was 118.34, 371.07 and 318.75days respectively. Liquidity ratio has a mean value of 1.8 times which is near to the bench mark value of 2 times, standard deviation of 1times, minimum value of 0.3 times and maximum value of 4.28 times. Controlling variable such as firm size and growth has a mean value of 220.11 and 132.56 and standard deviation of 274.97 and 162.16 respectively.

Table 4. 2: Correlation matrix

	ROE	ROA	TOBINS_Q	DCP	ID	CPP	LR	FS	GROWTH
ROE	1								
ROA	.355**	1							
TOBINS_Q	-.918**	-.071	1						
DCP	.028	-.276*	-.126	1					
ID	-.009	.121	.076	-.326**	1				
CPP	.056	-.070	-.091	.257*	.437**	1			
LR	.173	.604**	.028	-.388**	.246*	-.331**	1		
FIRM_SIZE	.105	.254*	.019	-.303*	.137	-.081	.084	1	
GROWTH	.106	.215	.016	-.318**	.147	-.103	.162	.968**	1
**. Correlation is significant at the 0.01 level (2-tailed).									
*. Correlation is significant at the 0.05 level (2-tailed).									

From the table above, we can see that ROE is insignificantly positively related to debtor collection period (DCP), creditor payment period (CPP) and liquidity ratio (LR). This mean that as debtor collection period, creditor payment period and liquidity ratio increase the return on equity also increase. On other hand return on equity (ROE) is negatively correlated with inventory days (ID), meaning that when the inventory days decrease the return on equity increase.

Return on assets (ROA) is positively related to inventory days (ID) and liquidity ratio (LR). But the correlation with liquidity ratio is significant at 5% level. Then when inventory days and liquidity ratio increase the return on assets also increase. Furthermore, the return on assets has a significant correlation at 5% with

debtor collection period (DCP). Also return on assets and creditor payment period (CPP) are insignificantly negatively related. It means that when debtor collection period and creditor payment period decreased then the return on asset increase.

Tobin's q is both negatively related to debtor collection period (DCP) and creditor payment period (CPP), meaning the decrease in both DCP and CPP lead to increase in tobin's q. moreover tobin's q with both inventory day (ID) and liquidity ratio (LR) are positively correlated. Then any increase in ID and LR lead to increase in tobin's q.

Then all ROE, ROA and tobin's q are positively related to firm size (FS) and growth. On other hand ROE is positively related to ROA and negatively related to tobon'sq .Also, the correlation between firm size and growth is approximately to one, this mean that these variables explain the same. For the purpose of this study the growth was dropped and firm size will remain as the only controlling variable.

4. 3 Regression analysis

To evaluate whether there is significant relationship between efficiency measures of working capital management and measure of financial performance. The model used to run these regressions analysis was panel Generalized Method of Movements with orthogonal deviation. The tables below show the results for regression analysis.

4.3. Regression result for ROA

Table 4.3: GMM regression results between Working capital on ROA

	Coefficient	t-Statistic	Probability
DROA(-1)	-0.141380	-12.73569	***0.0000
DDCP	-0.021748	-11.47942	***0.0000
DCPP	0.675195	7.286723	***0.0000
DID	0.290988	2.053713	**0.0463
DLR	-0.393213	-3.349526	***0.0017
DFS	2.243108	13.78075	***0.0000
Year dummy2008	20.59186	2.97210	***0.0040
Year dummy2009	6.341076	0.93154	0.3552
Year dummy2010	1.253462	0.19542	0.8536
Year dummy2011	1.586736	0.24034	0.8131
Year dummy2013	-1.092166	-0.16513	0.8714
Year dummy2014	2.378603	0.35576	0.7278
Year dummy2015	3.651802	0.53245	0.5960
Year dummy2016	4.844964	0.70543	0.4853
Year dummy2017	0.772426	0.11175	0.9134

Significant level * p<0.10, ** p<0.05, *** p<0.01

From the table above, the regression result shows that debtor collection period, liquidity ratio and growth have a negative significant influence on return on assets. However, creditor payment period, inventory days and firm size have significant positive influence on return on assets. Also, historical information of return on assets has negative significant influence on current return on assets. Except the dummy variable for 2008 the remaining dummy are insignificant on financial performance.

V. Regression result for TOBIN'Q

Table 4.4: GMM regression results between Working capital on TOBIN'S Q

	Coefficient	t-Statistic	Probability
DTOBIN(-1)	1.985545	5.378079	***0.0000
DDCP	-0.068646	-3.978723	***0.0004
DCPP	-0.578985	-1.221194	0.2312
DID	0.726497	1.010150	0.3202
DLR	-1.393931	-2.253147	**0.0251
DFS	-1.149156	-0.694737	0.4924
Year dummy2008	-0.512007	-0.125042	0.9071
Year dummy2009	-0.886543	-0.214381	0.8364
Year dummy2010	-0.936603	0.224975	0.8262
Year dummy2011	-0.480827	-0.115420	0.9095
Year dummy2013	1.043738	0.224371	0.8051
Year dummy2014	11.10819	2.621341	0.0112
Year dummy2015	1.923754	0.450217	0.6553
Year dummy2016	0.966597	0.223540	0.8254

Year dummy2017	1.044623	0.242354	0.8133

Significant level * p<0.10, ** p<0.05, *** p<0.01

From the table 4.8 above, it shows that there is a positive significant relationship between historical information of tobin's q with the current tobin's q. The results also show that liquidity ratio and debtor collection period have significant negative influence on tobin's q. Growth has positive influence on tobin's q. But inventory days, creditor payment period and firm size has no significant influence on tobin's q. All dummy variables are insignificant related with tobin's q.

VI. Discussion Of Findings

1 **Debtor collection period (DCP) on financial performance**

Table 4.3 show that debtor collection period has significant negative influence on return on asset. The result portrays that decrease by one unit in debtor collection period lead to increase in return on asset by 0.02 units. This result is supported by Kumaraswamy (2016)who found a negative relation between return on asset and debtor collection period. According to operating cycle theory, firm must ensure that their liquidly enough to meet their operating cost. Then this theory encourage firm to reduce debtor collection period for them to improve performance which agree with the finding of this study.

In table 4.4 depicted that debtor collection period and tobin'q are significantly negatively related. This mean that the increase in debtor collection period by one-unit leads to 0.0686 units decrease in tobin's q. this finding is relevant with working capital theories which infuses firms to reduce their receivable collection periods for them to improve financial performance

2 Creditor payment period (CPP) on financial performance

Table 4.3 show significant positive relation is existing between return on assets with creditor payment period. Then the increase in creditor payment period leads to the increase in the return on assets. Then firms listed at Dar stock of exchange must delay the payment to suppliers for them to ensure the availability of money to meet daily operation that improve financial performance. This results also are supported by existing theories of working capital management that suggest that firm must maintain optimal working capital to smooth their operation. Kumaraswamy (2016) supports the finding of this study by establishing a significant positive influence of creditor payment period on return on asset.The result shown in table 4.4 was insignificant negative relation is existing between creditor payment period with tobin'q. This result contradicts with the existing theories of working capital managements. Hassan, Imran, Amjad & Hussain (2014) concluded the same results on the relationship between creditor payment periods with return on equity. But this result is contrarily with Bagha*et all* (2016) for which they found a negative significant relation between creditor payment periods with return on equity.

3 Inventory days (ID) on financial performance

Table 4.3 shows that inventory days and return on asset are significantly positively related. Then one unit increase in inventory days leads to 0.291 units increase in return on asset. For listed non-financial firm in Tanzania must focus on increasing inventory days for them to increase profitability. This finding was supported by Kumaraswamy (2016) who concluded that significant positive relation existing between inventory days and return on asset. On other hand Angahar & Alematu (2014) contradict with the result of this finding by concluded the negative significant influence of inventory days and return on asset. Also, theories of working capital management suggest that inventory days and financial performance are negatively related. This is contrarily to the finding of this study.Table 4.4 portray that inventory days is insignificantly positively related with tobin's q. This means that the increase in inventory days lead to insignificant increase in tobin's q. This result is contradicting the existing theories of working capital management. Then for listed non-financial firm in Tanzania when they need to improve financial performance, they should nod not focus on inventory days since is not significant for improving financial performance.

4 Liquidity ratio (LR) on financial performance

A negative significant relation is existing between liquidity ratio and return on assets as shown in table 4.3 above. It was shown that the increase in liquidity by one-unit lead to 0.393 decrease in return on assets. This was supported by Angahar & Alematu (2014) for which they established a negative significant relationship between debt ratio and return on asset in Nigeria. But this result contradicts with by Kumaraswamy (2016) who established a positive influence of working capital on return on equity. Working capital management theories also contradict with the finding of this study. Tables 4.4 suggest that the negative relation existing between liquidity ratio and tobin's q. this finding was the same as shown by ROA above. The firm must reduce their

liquidity ration to enhance financial performance. The study also this finding advice the firm to reduce liquidity ratio but reducing this ratio too much it may cause the firm to fail to pay some obligation that fall due that lead to poor performance.

5 Firm size (FS) on financial performance

Table 4.3 the result shows that positive and significant relation between firm size and return on asset. Meaning that as the sizes of the firm expand it helps non-financial firm listed in Tanzania. The result contradicts the finding of Sharma & Kumar (2018) who concluded the negative significant relationship between firm size and return on asset. Tobin's q and firm size have insignificant influence on each other. But the existing relationship between then is negative. Different theories have explained that if the firm expands it enjoys economies of scale that help them to be more profitable. Then the relation shown between tobin's q and firm size is contrarily to theories point of view.

From the discussion above it shows that most of the independent variables has significant relationship with financial performance. Therefore, the null hypothesis (H_0) is rejected and alternative hypothesis (H_1) is accepted. Except for inventory days which show that has no relation with financial performance. Hence basing on the result of this study the following are drown conclusion on developed null hypothesis.

H_0 There is no relationship between the debtor collection period and financial performance oflisted firms. **The null hypothesis is rejected.**

H_0 There is no relationship between Inventory days and financial performance of listed firms. **The null hypothesis is accepted.**

H_0 There is no relationship between creditor payment periods with financial performance of listed firms. **The null hypothesis is rejected.**

H_0 There is no relationship between liquidity ratio and financial performance of listed firms. **The null hypothesis is rejected.**

VII. Conclusion And Recommendation

The influence of debtor collection period (DCP) on financial performance measures that is return on equity, return on asset and tobin's q is significant negative. Then non-financial firms listed in Tanzania should focus on management of receivables for them to perform.

The influence of creditor payment period (CPP) on financial performance was positive. Return on equity (ROE) shows a positive but insignificant relation with CPP. Also return on asset (ROA) portrays a significant positive relation with CPP. For the case of tobin's q the negative insignificant relation is shown with CPP. Then we conclude that CPP is positively related with financial performance.

Inventory day (ID) is negatively insignificant related with return on equity. But both return on asset and tobin's q are positively related with ID. The study concluded that inventory days is positively related to financial performance.

The influence of liquidity ratio (LR) of financial performance is negative. Since two financial performance measures that is ROA and TOBIN'S Q suggest significant negative relation except ROE for which it shows a significant positive relationship. It is concluded that LR has a positive relation with financial performance.

Firm size and financial performance are negatively related, this was shown by ROE and TOBIIN'S Q for which they concluded the negative relationship with firm size for non-financial firm listed firms in Tanzania.

Effective working capital management will ensure that firms are focusing on reducing the trade receivable period to improve performance. Trade policies that may involve stringent receivables collections mechanisms may irritate loyal customers exposing the firm to probable risk of losing. Then firm must adapt good receivable policy that minimize days and maintain customer.

Non-financial firms are also recommended to delay payment to the supplies. By doing that firm will have enough money to invest on other activities that will increase profitability in short run like bond and treasure bill. But too much delay will distort firm reputation and credibility to supplier that will affect performance in long run.

Also holding excessive inventory may prove costly in the short term due to cost of capital investment and firm's inability to meet its short-term financial objectives due resulting illiquidity.

It is important for non-financial firms to make a preliminary cost-benefit analysis of the various working capital management decisions before committing the firms' resources towards a specific decision. Effective capital management policies will therefore enable firms to carefully evaluate their financing needs whether long term or short term.

The further studies to be made by future researchers could to take a look at the following aspects; The influence of external factors that affect working capital like interest rate risk, business risk, competitors' risk, political risk, foreign exchange risk and their relative impact to the profitability of the firms. The scope of

further studies should be extended when conducting research on the similar topic with different companies from different industries by increasing the years of the sample of the study.

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