

# Financial Distress among Manufacturing Companies in Uganda

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**Abstract:** *Analysis of the financial difficulties among industrial enterprises was the study's main objective. The study specifically looked at the connection between managerial ability and financial distress, the impact of cash flow management on financial hardship, and the relationship between managerial ability and cash flow management. Both qualitative and quantitative research methods were used in the study. In order to gather information from 200 industrial enterprises in the Kampala Metropolitan region, the study used interview guides. The results showed that managerial skills, cash flow management, and financial hardship among manufacturing enterprises had a substantial positive association. The findings also showed a favorable and significant correlation between managerial ability and cash flow management. The regression analysis's findings revealed that 34.7% of the total variance was significantly predicted by managerial ability and cash flow management.*

**Keywords:** Financial Distress, Managerial Competence, Cash Flow Management and Manufacturing Companies

## BACKGROUND

Financial distress in companies has long been an issue of concern to governments and the investing public. This is because a financially distressed company is unable to generate enough cash flow necessary for meeting contractually required payment and increasing the likelihood of bankruptcy, which has adverse consequences to not only the economy, but also the stakeholders who suffer considerable financial loss. More so, if a firm is in financial distress, employees are directly affected since their bonuses are likely to be cut, replacement and loss of reputation is inevitable as well (Ross, et al, 2012). Despite the risks associated with financial distress, some of the companies in Uganda are either distressed or are at the verge of financial distress (Kalyegira, 2016; Muhumuza & Adengo, 2016). From available statistics, the manufacturing value added (MVA) is relatively low. Between 2012 and 2014, MVA increased by only 0.21%. In addition, manufacturing firms in Uganda are characterized by high excess capacity, with capacity utilization of the installed capacity less than 50% of installed capacity for the majority of operations (African Development Bank (ADB), 2014). Besides, the contribution to GDP among manufacturing companies in Uganda is still low at 7% for over the last decade (ADB, 2014). Recently, manufacturing firms in Uganda applied for bail from government to be able to pay their debts. Some of these companies include Steel and Tube,

Uganda Clays Ltd, Steel Rolling Mills and Shumuk Aluminum, Roofing Steel Mills (Muhumuza & Adengo, 2016). This trend has raised concern by the manufactures, business community and the government in general. Evidence revealed that a total of over 65 companies had applied for a bail from government, to gain the capacity to repay their debt obligation (Muhumuza & Adengo, 2016). This high financial distress could be attributed to inadequate managerial competence and inadequate cash flow management among manufacturing firms (Muhumuza & Adengo, 2016)

Financial difficulty is widespread, according to prior research, and managerial proficiency and cash flow management have been the driving forces behind this research (Jahur & Quadir, 2012; Fatoki, 2014; Talik et al, 2012; Kroes & Manikas, 2014). According to Kroes & Manikas (2014), the main purposes of cash flow management are to examine a company's financial standing and compare the value relevance of operating, investment, and financing cash flows to that of earnings and accruals. If the company doesn't manage its cash flow, it will have to take on more debt and pay more in interest costs. Poor cash flow management compels businesses to abandon some of their capital projects that would solve their numerous obligations and would

### Statement of the Problem

Modern manufacturing, from raw materials to semi-finished goods and finished goods, is at the heart of global development. Even with a growing number of ground-breaking innovations and technologies, some fundamental challenges remain unresolved, including demand forecasting, inventory management, improving manufacturing plant efficiency, material waste, keeping track of sales leads, adapting to technological changes, and environmental consciousness. Manufacturing firms are critical to a country's economic growth. Uganda's contribution to GDP from manufacturing firms remains low, at 7 percent. This severe financial distress may be attributed to insufficient managerial competence and cash flow management. Kroes and Manikas (2014): Cash flow management is done primarily for two may ultimately lead to the firm financially restructuring its engagements with its creditors and equity investors. It is important to protect A manufacturing firm under financial distress ends up incurring non-core costs such as expensive financing, consultants fee, less productive employees, lawyer's fees, management compensation, and decline of stock prices. Managers of distressed manufacturing companies are tempted to misappropriate companies' assets and resources. Financial distress is just a stage that can lead to bankruptcy. However, the factors for financial distress among manufacturing companies in least developed countries such as Uganda is still missing. Therefore, the purpose of the study was to establish the extent to which managerial competence and cash flow management, as highlighted in prior studies are responsible for the financial distress among manufacturing firms in Uganda, a case of metropolitan region.

### Specific Objectives.

1. To examine the relationship between managerial competence and financial distress.
2. To examine the effect of cash flow management on financial distress.
3. To assess the relationship between managerial competence and cash flow management.

### Research questions

1. What is the relationship between managerial competence and financial distress?

### Sample size determination

To obtain the sample size, the researcher used the formula below;

$$k,m = 1974$$

reasons: to investigate a company's financial to evaluate operating, investing, and financing cash flows for their value and significance. Cash flow management is done largely for two reasons, according to Kroes and Manikas (2014): to assess the financial health of a company and to compare the value relevance of operating, investing, and financing cash flows to that of earnings and accruals. Both traditional start-up businesses and well-established public enterprises have relied heavily on the private equity markets in Europe and the United States as sources of funding. According to Ross et al. (1999), companies in financial difficulties make up a substantial part of the non-venture market. A company's contract default could be caused by financial difficulties, and this

manufacturing companies from financial distress due to the important role they play in the Ugandan economy.

2. What is the effect of cash flow management on financial distress?
3. What is the relationship between managerial competence and cash flow management?

## METHODOLOGY

### Research design

The study adopted qualitative and quantitative research design. Qualitative research approach is a systematic subjective approach used to describe life experiences and give them meaning, (Mubazi, 2008). More of qualitative approach will adopted in this study simply because it provided the researcher an opportunity of studying things in their natural settings and in terms of meanings, more so, it is descriptive in nature which enabled the researcher to get the depth of the phenomena under investigation.

### Population of study

The population of the study constituted of 200 industries or factories within Kampala Metropolitan region.

### Data sources

The study considered primary data to make though investigation about financial distress among manufacturing companies.

$$n = \frac{z^2 PQ}{e^2} = \frac{(1.96)^2(0.5)(0.5)}{(0.05)^2}, \alpha = 5\%$$

**Data collection methods**

The researcher employed interview guides to collect the data face-to-face from the respondents.

**Data analysis and presentation**

Statistical Package for Social Scientist (SPSS 22) was used for data entry and analysis. Frequency tables were used to describe the sample characteristics of the respondents. A correlation analysis tool (Person’s correlation coefficient) was used to establish the relationship between the variables. Logistic regression analysis was carried out to find the extent to which managerial competency and cash flow management predicted financial distress of manufacturing firms

**Results**

**Sample Characteristics**

**Table 1: Individual characteristics**

<b>A: Gender</b>		<b>Count</b>	<b>Percent</b>
Gender	Male	69	74.2
	Female	24	25.8
<b>Total</b>		93	100.0
<b>B: Positions held</b>		<b>Count</b>	<b>Percent</b>
Positions held	Finance manager	77	82.8
	Human resource manager	16	17.2
<b>Total</b>		93	<b>100.0</b>
<b>C: Age bracket</b>		<b>Count</b>	<b>Percent</b>
Age Bracket	25-34 years	18	19.4
	45-54years	64	68.8
	Above 55 years	11	11.8
	<b>Total</b>	93	100.0
<b>C: Education Background</b>		<b>Count</b>	<b>Percent</b>
Highest level of education attained	Diploma	4	4.3
	Bachelors	65	69.9
	Masters	24	25.8
<b>Total</b>		<b>93</b>	100

Source: primary data

Table 1's findings indicated that just 25.8% of respondents were women, whereas the bulk of respondents (74.2%) were men. According to the survey, this suggests that the majority of responders were male. According to the statistics on the roles held, finance managers made up the bulk of respondents (82.8%) while human resource managers made up 17.2%. According to the survey, this suggests that the majority of respondents were experts on the subject of financial difficulties. According to table 1's findings, 68.8% of respondents fell into the age category of 45 to 54 years, which is where the majority of respondents fell. This indicates that the majority of respondents from manufacturing companies are primarily mature and engaged. The highest qualification earned is,

**Table 2: Firm characteristics**

<b>A: Period of operations</b>		<b>Count</b>	<b>Percent</b>
Period of operations	Less than 5 years	17	18.3
	6-10 years	65	69.9
	10 years and above	11	11.8
<b>Total</b>		<b>93</b>	<b>100</b>
<b>B: Turn over annually</b>		<b>Count</b>	<b>Percent</b>
Turn over	less than 200 m	6	6.5
	201m to 400m	20	21.5
	401m to 600m	23	24.7
	601m to 800 m	33	35.5
	801m and above	11	11.8
<b>Total</b>		<b>93</b>	<b>100</b>

**Source: primary data**

The results in table 2 shows that majority (69.9%) of firms had been in operations for a period of 6-10 years. This means that overall in the industry, majority of respondents have acquired good experience and skills to execute their jobs professionally. This means that overall in the industry, majority of the firms have stayed long in terms of their number of years in operations to respond on financial distress issues. Lastly in terms of annual turnover, majority had between 601 million to 800 million annually.

**Correlation analysis**

The objectives of the study were based on the relationships between the different variables which were: managerial competency, cash flow management and financial distress. In order to achieve this, the Pearson (r) correlation coefficient was computed given the interval nature of the data and the need to test the direction and strength of associations that exist among the study variables.

**Table 3: Pearson correlations (Zero-order)**

<b>Variables</b>	<b>1</b>	<b>2</b>	<b>3</b>
Managerial competency 1	1.000		
Cash flow management 2	.295**	1.000	
Financial distress 3	.306**	.336**	1.000

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

**Source: Primary data**

The findings in Table 3 showed a positive and statistically significant relationship between managerial skill and financial distress (r = 0.306, p 0.01). This shows that improvements in managerial ability are related to improvements in manufacturing firms' financial distress. Therefore, an improvement in the financial positions and stress experienced

by manufacturing firms will result from improvements in the managerial capabilities of those organizations in terms of knowledge, skills, and abilities acquired.

Financial distress and cash flow management have a positive and significant link ( $r = 0.336$ ,  $p = 0.01$ ), according to the findings in table 3 above. This conclusion implies that a manufacturing company's financial difficulty would improve if cash flow management were improved. This controls are more likely to be in position to pay their obligations in time and hence improve financial distress.

The results in table 3 above indicated that there is a significant positive correlation between managerial competency and cash flow management ( $r = 0.295$ ,  $p \leq 0.01$ ). This indicates that positive change in managerial competency is associated with positive change in the cash flow management by manufacturing firms. This means that when manufacturing firms improve their managerial competency, then their cash flow management will be enhanced in these manufacturing firms.

### Regression Analysis

**Table 4: Regression of managerial competency and cash flow management on financial distress**

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	7.612	.974		7.813	.000
Cash flow management	.632	.126	.466	5.027	.000
Managerial competency	.682	.143	.444	4.783	.000
Dependent Variable: financial distress					
R Square	0.292			F Change	18.601
Adjusted R Square	0.3477			Sig.	0.000

Source: Primary data

The findings from table 4 above indicated that managerial competency and cash flow management together accounted for an average of up to 34.7% of the total variations in financial distress in manufacturing firms, suggesting that there are additional factors besides these two that influence financial distress of the manufacturing firms. However, financial strain was significantly predicted by managerial ability and cash flow management. According to the data in Table 4 above, a change in cash flow management would result in an average 46.6% reduction in financial distress. Additionally, an increase in managing ability results in 44.4 percent positive changes in financial distress. The model also indicated that cash flow management had the highest prediction potential compared to managerial competencies towards financial distress among manufacturing firms.

### Conclusions

The objective of this study was to investigate the relationship between financial distress, effective cash flow management, and managerial skill. According to the study's findings, manufacturing companies with highly skilled, educated, and information (with intelligent who understand financial obligations have stronger financial standings. Therefore, having managers with the necessary skills, knowledge, and competencies is crucial to enhancing the firm's capacity to meet its financial commitments. The study also revealed a favorable and significant link between poor cash flow management and financial trouble. Manufacturing companies must put in place suitable cash planning and monitoring procedures in order to achieve a better financial position. Thirdly, the study shows that better cash flow management is improved by managerial competency in manufacturing enterprises. improved abilities and knowledge,

### Recommendations

Following are the recommendations derived from the study's findings;

To ensure that their employees fully comprehend how financial concerns are handled, manufacturing companies must constantly enhance their managerial competencies. For instance, management in manufacturing companies should maintain a moderate level of liquidity, just enough to pay short-term commitments when they are due and prevent overinvestment in working capital.

To ensure that the assets pledged as security are productive enough to generate sufficient returns to meet the fixed financial charges, manufacturing companies should match their debt covenants with the assets pledged as security.

The management of enterprises should periodically assess their capital structure in order to adjust it in accordance with the financial forecasts, as cash flow management was a superior predictor.

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