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# Effect of Budgetary Control on Financial Management in Stima Savings and Credit Cooperative Society, Kenya

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**Abstract:** ***There were hitherto hardly any documented empirical evidence on how budgetary control influences financial performance of Saccos. In this regard, this study was necessitated to address this knowledge gap. The study evaluated the effect of budgetary control on financial management in Stima Sacco Society, Kenya. It examined how cost control influenced financial management in the Sacco. This study adopted descriptive survey research design. The employees working with the Stima Sacco Society in Kenya constituted the target population. Stratified random sampling method was adopted to draw the 59 sampled respondents from the study population. A structured questionnaire was employed to collect data. A pilot study was carried out prior to conducting the main study in order to determine both the validity and reliability of the research questionnaire. The Statistical Package for Social Sciences Version 24 software facilitated data analysis. Data analysis was in form of both descriptive and inferential statistics. Descriptive statistics took the form of frequencies, percentages, means and standard deviations. Inferential statistics were in the form of correlation and regression analyses. The results of the analyses were presented in form of tables. The study revealed that the relationship between cost control and financial management was statistically significant. It was concluded that unlike cost control was very important in management of finances at the Sacco. It is recommended that the Stima Sacco Society should ensure that effective measures are taken so that as the Stima Sacco Society purposes to increase its revenue, all forms of costs are minimized.***

**Keywords:** Budgetary control, cost control, financial management, Saccos Stima Sacco

## 1. Introduction

In finance, there exists two types of control. These are budgetary and financial control. This study, however, focuses on the budgetary control and is relevance to financial performance of Savings and Credit Cooperative Societies (SACCOs). Budgetary control describes the establishment of budgets whereby responsibilities of executives are related to the requirements of a certain policy, and also the continuous comparison of actual with the budgeted results with the aim of either securing the policy objective through individual action or to provide a basis for budget revision. It is noted that presently, a budget plays a crucial role in the planning and control process of virtually all firms whether in private or public sector [1].

Budgeting plays crucial roles in organizations. Some of the principle roles of budgeting include planning, control, coordinating, evaluating, directing, performance improvement, communicating and decision making [2]. In respect to this study, the focus will be on the control role played by budgeting. The importance of budgetary control is underscored by the assertion that it has significant influence on motivating employees. This leads to savings in service charge. It is advised that budgetary control ought to be intensified with the aim of motivating employees to embark on reducing service cost and as such result in savings.

An analysis of the situation in China indicated that it is accepted wisdom that the implementation of an appropriate budgeting system has a capacity to influence the financial efficiency and effectiveness of government [3]. In the same, it is asserted that governments at all levels in the United States have successively been changing their budgeting systems. The transition has been from line-item budgeting to programme budgeting to incremental and zero-based budgeting. The ultimate budgeting phase is performance-based budgeting. The latter (PBB) could be traced from the accounting reforms propositions made in the era of President Harry Truman of the US [4].

According to a report on financial management training for Saccos in Uganda, these financial institutions have been facing problems with their budget control and expenditure management [5]. The report observed that these challenges could be overcome through mentorship and setting up proper accounting system. In the same light, it was stated that most Saccos in the country have failed to appreciate the importance of prudent financial management which has resulted in poor financial performance.

In reference to development of Saccos in both Tanzania and Kenya, board members in most of these financial entities are drawn from volunteers who are non-professional. However, these board members assume very technical issues which include budgeting and financial expenditure control. The cooperative movement in Kenya has been facing pressure from various quarters in the recent past. These pressures have been emanating from both within and outside Saccos and have been occasioned by deteriorating trend in financial performance. The poor financial performance in local Saccos has been attributed to mismanagement of these societies. In the wake of the foregoing challenges, the relevant government organs formulated policies aimed to streamline budgets and budgetary control systems among other issues [6].

The management of Saccos is mandated with ensuring that there are adequate funds which must be appropriately employed. This calls for effective budgeting policies and procedures to be put in place with the objective of effectively managing the available funds. A budget is

described as a critical management and control tool that facilitate making of decisions on income and expenditure plans of Saccos [6]. This assertion is in line with the argument that budgetary control systems are universal and are as such essential tools for financial planning. Therefore, budgetary is purposed to enable forecasting of revenue and expenditures. This explains why most firms including Saccos employ budget control as the main means of corporate internal controls [7].

It is quite evident that Saccos in Kenya have been facing a myriad of challenges due to a number of factors including their management structure that makes it possible to have non-professionals on board. This has indeed compromised the financial performance of these financial entities given the fact that non-professionals are not suitable in developing and overseeing budgets and budgetary controls. The current study has put into perspective the relevance of budgetary controls on financial performance of Stima Sacco Society where it has suggested viable recommendations which if and when implemented are bound to enable Saccos to improve their financial performance.

## 2. Statement of the Problem

Savings and credit cooperative societies are financial institutions that operate in a very dynamic and competitive financial sector. They face competition from other Saccos, commercial banks, microfinance banks, microfinance institutions and other unregulated financial entities such as shylocks. Saccos in Kenya have been exposed to turbulent times their inability to withstand the competitive storm in the sector has led to their collapse [8]. The financial problems facing Saccos are compounded by the fact that unlike, say commercial banks which are able to access credit facilities from the Central Bank at reduced interest rates, Saccos rely almost exclusively on the contributions of their members and to some extent, the FOSA and BOSA services offered by selected few entities. A local study reinforces this assertion where it revealed that Saccos witnessed challenges in meeting loan requests by members, and that their members preferred bank loans since the latter do not peg amount of credit advanced on savings [9]. Saccos are also more prone to non-performing loans (NPLs) since ordinarily they do not demand for collateral when advancing credit facilities, rather they rely on member guarantee. The financial conditions spelt out by Saccos before they advance credit to borrowers make them unappealing, a situation they strive to mitigate by advancing loans on relatively lower interest rates compared to other lenders. However, the recently interest rate cap of 14.5% enacted in Kenya in line with the Banking (Amendment) Act 2016 has or is bound to throw Saccos into financial dilemma. This is due to the fact that these entities have to take cue and reduce their rates to points that will definitely negate their financial performance while holding other factors constant. Against this backdrop, these entities are supposed to look into factors that may enable them to address the prevailing financial situation occasioned by financial factors such as reduced interest rates on loans. Given that there are hardly any documented empirical evidence on how budgetary control influences financial management of Saccos, then the present study was necessitated to address this knowledge gap.

## 3. Objectives of the Study

### 3.1 General Objective

To evaluate the effect of budgetary control on financial management in Stima Sacco Society, Kenya.

### 3.2 Specific Objective

To evaluate the effect of cost control on financial management in Stima Sacco Society

## 4. Research Hypothesis

**$H_0$:** There is no significant effect of cost control on financial management in Stima Sacco Society.

## 5. Conceptual Framework

A conceptual framework diagrammatically represents variables of a study and how they were hypothesized to interact. Figure 1 outlines the conceptual framework for this study.

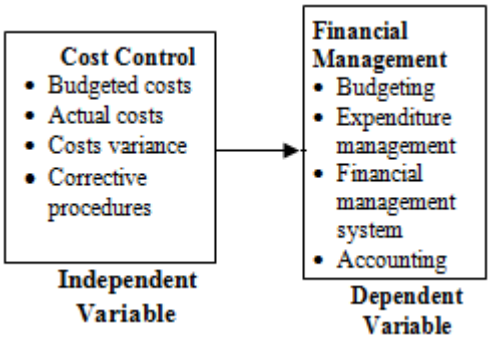


**Figure 1:** Conceptual Framework

A shown in Figure 1, the study will be guided by a set of two major variables. These are independent and dependent variables. Independent variable also referred to as predictor variable was the cost control. Financial management was the dependent variable. Each of the foregoing variables is characterized by a set of measurable parameters. The framework holds that the mentioned independent variable was a component of budgetary control and was hypothesized to influence financial management in savings and credit cooperative societies.

## 6. Literature Review

The study delved into pertinent concepts, theories and empirical studies.

### 6.1 Theoretical Framework

The study reviewed and discussed the theory of budgeting and agency costs of free cash flow theory.

#### 6.1.1 Theory of Budgeting

The theory of budgeting was advanced by Hirst [10]. The theory states that an effective budgetary control solves a firm's need to plan and also considers how to confront future potential risks and opportunities by putting in place an

efficient system of control. According to the theory budgets are the principal components of an efficient control process. Therefore, as pointed out [11] budgets are of paramount importance to an effective budgetary control [12].

Budgets are a collection of future of plans and forecasts. They project future financial performance of an organization. This enables evaluation of the financial viability of a chosen strategy [13]. The establishment of both short-term and medium-term objectives by budgets is important in providing estimates of future sales revenues and expenditure. This also enables setting of short-term and long-term objectives for a coordinated management policy.
The theory of budgeting further rationalizes consideration of optional courses of action. Budgeting allows setting of standards for performance by establishing comparison of actual results with the created standards. In the contest of the present study, the theory of budgeting facilitates an understanding of the importance of not only budgeting but also budgetary control in savings and credit cooperative societies. The budgets enable forecasting of future revenues and expenditure which enables Saccos to plan rationally and appropriately for the future.

**6.1.2 Agency Costs of Free Cash Flow Theory**
The theory of agency costs of free cash flow was proposed by Jensen in 1986. This theory is an advancement of the agency theory by Jensen and Meckling of 1976. The theory states that free cash flow (FCF) is the cash flow that is in excess of the required cash to fund all projects that have positive net present values (NPV) when discounted at the relevant cost of capital. Moreover, it is stated that FCF is the sum of the cash flow to equity and cash flow to debt holders after interest-tax-shield [14].

The agency costs of free cash flow theory further holds that dividends are replaced with debt, managers are bound to transfer excessive cash flows to investors and as such limit the allocation of resources to low-return projects or activities. The theory advocates for adoption of leveraged buyouts (LBOs). LBOs are asserted to enable reduction of the agency costs of a firm through reallocation of resources, squeezing out capital for growth [15].

The theory of agency costs of free cash flow can be employed in the context of the present study to explain the importance of budgetary control and financial management. Similarly to budgeting, this theory rationalizes prioritization of projects and/or activities whose NPVs are high. This is an important element of budgetary control. The theory further underscores the adoption of LBOs which serve to reduce agency costs and as such, this is certainly an important factor in management of finances of savings and credit cooperative societies.

**6.2 Empirical Review**

This section covers a review of past empirical studies in relation to cost control as part of budgetary control and also financial management.

**6.2.1 Cost Control and Financial Management**
A study carried out in the US empirically analyzed the effect of performance-based budgeting on State government expenditure [3]. The study concurred that state official employ performance information to identify the potential impact of proposed policy changes. Premised on these analyses, the officials make policy decisions that seek to minimize costs while simultaneously maintaining programme effectiveness. However, it is admitted that the scope of performance-related initiatives including performance-based budgeting go beyond simply cutting costs.

An empirical investigation into efficiency and profitability of Tanzanian Saccos observed that these financial institutions operate at small scale and also in risky operating environment in terms of composition of their clients and business type [16]. The foregoing circumstances may result in increased transaction costs. Increased transaction costs were observed to occasion reduced profits, efficiency and sustainability of Saccos. In the study, it is noted that cost minimization leads to cost efficiency. To this end, the study recommends that managers and members of Saccos are supposed to focus on increasing efficiency through cost-cutting.

Empirical studies reviewed underscore the importance of cost element in Saccos. In a study done amongst Saccos in Kenya, it is posited that cost of mobilizing funds is one common budgets in Saccos [8]. More so, the aspect of investing demands these entities to embark on a cost-benefit analysis in order to opt for investment option whose benefits outweigh cost outlays. The authors observed that the cost of capital for every different funding is supposed to be evaluated since various types of capital have different rates of return. When Saccos are advancing credit facilities, administrative efficiency is supposed to be factored in. This implies the total cost of administration to loan amount advanced. Reduced administrative costs translate into increased growth of Saccos. To this end, administrative costs are supposed to be retained at their minimum possible levels [8].

A study on the effect of budgetary control on effectiveness of NGOs in Kenya puts the aspect of cost as part of budgetary control into perspective [12]. Budgetary control according to the study and quoting an earlier study [17] is asserted to be the system of controlling costs through budgets. When budgetary controls are implemented effectively, an entity is able to minimize costs and subsequently enhance quality of its services based on the budgetary allocations. The study further indicated that cost reduction is an important budgetary control aspect that influences performance of a firm [12].

**6.2.2 Financial Management**
Financial management is supposed to be aligned with the decisions of establishing the most suitable mix that is bound to maximize the wealth of shareholders in a firm including savings and credit cooperative societies. An empirical study on the effect of government regulations on financial performance of Saccos in Kenya it is revealed that there is a lot that is supposed to be done in order to address challenges

of financial management decisions that generally affect the financial performance of Saccos [6].

A local study examined the effect of financial sustainability on the performance of deposit-taking Saccos in Nairobi County, Kenya [19]. The study used descriptive research design and focused on all the 34 deposit-taking Saccos (DTS) which had complied with Sacco Society Regulations Authority (SASRA) regulations. The study findings led to the recommendation that all DTS are supposed to adopt prudential financial management standards spelt out by both SASRA and World Council of Credit Unions (WOCCU).

## 7. Research Methodology

A research design is a blueprint of conducting a study [20]. This study adopted descriptive survey research design. This design was chosen based on the fact that the study had clear objectives and involved participants from various branches of Stima Sacco Society in Kenya. Target population refers to an aggregate of subjects sharing common or similar characteristics [21]. The employees working with the Stima Sacco in Kenya constituted the target population.The mentioned staff working with the Stima Sacco Society in Kenya comprised the study population. This implies the target and study population were similar. Stima Sacco Society had 156 members of staff attached across all 6 branches in Kenya and the head office when this study was conducted.

A sample is a subset of the study population and is necessitated when the study population is relatively large [22]. Stratified random sampling method was adopted to draw a sample of 59 respondents from the study population. This method was chosen because it enabled fair and equitable distribution of respondents across all strata (branches) of Stima Sacco Society. A research instrument refers to a tool that facilitates data collection. In the context of the present study, a structured questionnaire was employed to collect data from the sampled respondents. It is posited that questionnaires are the most appropriate tools for data collection in survey studies [23].A pilot study was carried out prior to conducting the main study. The rationale of this study was to determine both the validity and reliability of the research questionnaire.

The questionnaires were pilot tested on employees of Stima Sacco Society, Mombasa Branch. These respondents were excluded from the main study in order to avoid compromising the final study findings. Validity testing seeks to determine whether or not the research instrument measures what it is intended to measure [24]. In this study, content validity was determined through consultation with the assigned university supervisors whose opinions were considered sufficient in assessing the validity of the research questionnaire.

The results of the reliability test showed that all the variables, that is, cost control ($\alpha$ = 0.79) and financial management ($\alpha$ = 0.80) returned Cronbach coefficients greater than the reliability threshold of 0.7. Therefore, all the study constructs were found to be reliable.

### 7.1 Data Processing and Analysis

After collecting the questionnaires, the researcher ensured that only the ones that had been filled completely and according to instructions were considered for analysis. The Statistical Package for Social Sciences (SPSS) Version 24 facilitated data analysis. Data analysis was in form of both descriptive and inferential statistics. The results of the analyses were presented in form of tables. The following regression model was adopted.

$$\mathbf{Y= \beta_0 + \beta_1 X_1 \varepsilon}$$

Where Y, $X_1$, $\varepsilon$, $\beta_0$, and $\beta_1$ represented financial management, cost control, error term, constant, and regression coefficient of the predictor variable respectively.

### 7.2 Results and Discussions

Response rate refers to the number of questionnaires that are duly filled and returned to the researcher. Therefore, it is also referred to as questionnaire return rate [25]. The sample size constituted 59 employees of Stima Sacco in Kenya. As such, the number of questionnaires filled totalled 59. Forty-eight questionnaires were appropriately filled and collected from the respondents. This reflected 81.36% response rate. The foregoing response rate was deemed sufficient in that it surpassed the 75% threshold in survey studies [25].

#### 7.2.1 Cost Control

The study examined the views of Stima Sacco Society employees regarding various parameters of cost control. A summary of their opinions is as shown in Table 1.

**Table 1:** Descriptive Statistics for Cost Control

| | *n* | *Mean* | *Std. Dev.* |
|---|---|---|---|
| Stima Sacco Society budgets various costs of including administrative, marketing and operational costs | 48 | 4.63 | .489 |
| Stima Sacco Society factors in the actual costs after carrying our various activities in a financial year | 48 | 4.50 | .505 |
| The Sacco evaluates variance between budgeted costs and actual costs incurred | 48 | 4.56 | .616 |
| Corrective procedure is undertaken in case there in negative variance | 48 | 4.13 | .606 |
| The Sacco purposes to reduce its costs across the board | 48 | 4.81 | .394 |

It was revealed that the sampled employees strongly agreed that the Stima Sacco Society purposed to reduce its costs across the board (mean = 4.81; std dev = 0.394), and that the Sacco budgeted various costs including administrative, marketing and operational costs (mean = 4.63; std dev = 0.489). It was also strongly concurred that the Stima Sacco Society evaluated variance between budgeted costs and actual costs incurred (mean = 4.56; std dev = 0.616), and also that the Sacco factored in the actual costs after carrying our various activities in a given financial year (mean = 4.50; std dev = 0.505). The study further revealed that respondents were in agreement that corrective procedure was undertaken in case there was negative variance (mean = 4.13; std dev = 0.606).

### 7.2.2 Financial Management

The study sought the views of the employees working with the Stima Sacco Society on financial management in their Sacco. Their views are as shown in Table 2.

**Table 2:** Descriptive Statistics for Financial Management

| | n | Mean | Std. Dev. |
|---|---|---|---|
| Stima Sacco has sound budgets for various departments | 48 | 4.44 | .616 |
| The Sacco effectively manages all expenditures | 48 | 4.00 | .875 |
| There is an effective financial management system | 48 | 4.25 | .438 |
| As part of financial management, all books of accounts and financial statements are effectively compiled | 48 | 4.44 | .501 |
| The Sacco evaluates the financial performance of every department at the end of financial year | 48 | 4.56 | .501 |

The study found that, the employees were in strong agreement that the Sacco evaluated the financial performance of every department at the end of financial year (mean = 4.56; std dev = 0.501). In addition, it was observed that employees agreed that the Sacco had sound budgets for various departments (mean = 4.44; std dev = 6.16), as part of financial management, all books of accounts and financial statements were effectively compiled (mean 4.44; std dev = 0.501), there was an effective financial management system (mean = 4.25; std dev 0.438), and that the Sacco effectively managed all expenditures (mean = 4.00; std dev = 0.875).

### 7.2.3Relationship between Cost Control and Financial Management

The study examined the relationship between cost control as part of budgetary control, and financial management. Spearman rank correlation as shown in Table 3 was used to determine the aforesaid relationship. The relationship between cost control and financial management was found to be positive, weak and statistically not significant ($r_s$ = 0.126; $p > 0.05$). This meant that even though enhancing control of costs was likely to enhance financial management at the Stima Sacco Society, the foregoing relationship was not strong enough to invoke in-depth examination of cost control in the Sacco.

**Table 3:** Spearman Rank Correlation Matrix

| | | | 1 | 2 |
|---|---|---|---|---|
| Spearman's rho | Cost control | Correlation Coefficient | 1.000 | |
| | | Sig. (2-tailed) | . | |
| | Financial management | Correlation Coefficient | .126 | 1.000 |
| | | Sig. (2-tailed) | .395 | . |
| | | n | 48 | 48 |

### 7.2.4 Effect of Budgetary Control on Financial Management

The data collected was regressed in order to determine the extent of the effect of the cost control on financial management at the Stima Sacco Society. The results of the regression analysis were presented in form of inferential statistics that included general correlation coefficient (R), coefficient of determination ($R^2$), F-statistic, p-value, regression coefficients (β), and T-statistic.

**Table 4:** Model Summary

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
|---|---|---|---|---|
| 1 | .484[a] | .234 | .217 | .24254 |
| a. Predictors: (Constant), Cost Control | | | | |

The study as shown in Table 4 established that there existed a positive and moderately strong general relationship between budgetary control as represented bycost control and financial management at the Stima Sacco Society (R = 0.484). The foregoing relationship according to the results indicated in Table 5, was found to be statistically significant (F = 14.051; $p < 0.05$). These findings implied that as budgetary control, through cost control, was enhanced, so did the financial management in the Sacco. Moreover, Table 4 indicated the results of the coefficient of determination ($R^2$= 0.234). The results indicated that the cost controlas part of budgetary control explained 23.4% of financial management at the Stima Sacco Society. The results reflected the importance of cost control as an indicator of budgetary control in Saccos in Kenya.

**Table 5:** Analysis of Variance

| Model | | Sum of Squares | df | Mean Square | F | Sig. |
|---|---|---|---|---|---|---|
| 1 | Regression | .827 | 1 | .827 | 14.051 | .000[a] |
| | Residual | 2.706 | 46 | .059 | | |
| | Total | 3.532 | 47 | | | |
| a. Predictors: (Constant), Cost Control | | | | | | |
| b. Dependent Variable: Financial Management | | | | | | |

The findings indicated in Table 6 are the results of regression coefficients.

**Table 6:** Regression Coefficients

| Model | | Unstandardized Coefficients | | Standardized Coefficients | t | Sig. |
|---|---|---|---|---|---|---|
| | | B | Std. Error | Beta | | |
| 1 | (Constant) | 2.405 | .517 | | 4.653 | .000 |
| | Cost Control | .427 | .114 | .484 | 3.748 | .000 |
| a. Dependent Variable: Financial Management | | | | | | |

The results shown in Table 6 followed the model illustrated below.

$$\mathbf{Y = \beta_0 + \beta_1 X_1 + \varepsilon}$$

The interpretation of the model meant that for every unit change in financial management at the Stima Sacco Society, there had to be (0.427) unit change in cost control while holding other factors (2.405) constant.

### 7.2.5 Hypotheses Testing

The null hypotheses ($H_0$) was tested using the t-test statistics at 5% (0.05) significance level otherwise referred to as probability value (p-value). This meant that confidence level was at 95%. The results of the t-test statistics are as shown in Table 6.

**$H_0$:** There is no significant effect of cost control on financial management in Stima Sacco Society.

**$H_A$:** There is significant effect of cost control on financial management in Stima Sacco Society.
Results of t-test statistics returned ($t = 3.748$; $p < 0.05$)
The results meant that there was statistically significant effect of cost control on financial management in Stima Sacco Society.

Therefore, the null hypothesis (**$H_0$**) was rejected.

## 8. Summary, Conclusions and Recommendations

This section covers the summary of major study findings, conclusions drawn and then suggests recommendation in line with the study objectives.

### 8.1 Summary

It was revealed that the Stima Sacco Society purposed to reduce its costs across the board and that the Sacco budgeted various costs including those for administrative, marketing and operations. It was also indicated that the Stima Sacco Society evaluated variance between budgeted costs and actual costs it incurred, and also that the Sacco factored in the actual costs after carrying our various activities in a given financial year. The study further revealed that corrective procedure was undertaken in case there was negative variance. Moreover, it was revealed that albeit the observation that enhancing control of costs was likely to enhance financial management at the Stima Sacco Society, the foregoing relationship was not strong enough to invoke in-depth examination of cost control in the Sacco.
The study found that the Stima Sacco Society evaluated the financial performance of every department at the end of financial year. In addition, it was observed that the Sacco had sound budgets for various departments, and as part of financial management, all books of accounts and financial statements were effectively compiled. It was further revealed that the Sacco had an effective financial management system. More so, the Sacco was found to effectively manage all its expenditures. The study findings indicated that as budgetary control was enhanced, so did the financial management in the Stima Sacco Society. It was further observed that the budgetary control variables of resource allocation, accountability, zero-based budgeting and cost control contributed greatly and significantly towards management of finances at the Sacco. Cost control followed closely by zero-based budgeting were found to be the most important tenets of budgetary control since their effect on financial management at the Stima Sacco Society was established to be the greatest.

### 8.2 Conclusions

The study concluded that the Stima Sacco Society strived to reduce administrative, marketing and operational costs among other costs across all departments. The study also deduced that the Sacco evaluated the difference or variance between budgeted costs and costs that were actually incurred. It was concluded that, in tandem, the Sacco executed corrective procedure particularly in the event that the cost variance was negative. Cost control was proven and as such concluded to be important in managing finances at the Stima Sacco Society.

### 8.3 Recommendations

It is recommendable for effective measures to be taken to ensure that as the Stima Sacco Society purposes to increase its revenue, all forms of costs are minimized. The foregoing strategy is likely to boost the profitability of the firm. Moreover, it is advisable for the Sacco to examine closely and critically cost variances. In tandem, the Sacco should promptly address any negative cost variances in order to mitigate on any potential losses and instead enhance the firm's profitability.

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