EFFECT OF RISK MANAGEMENT PRACTICES ON FINANCIAL PERFORMANCE OF COMMERCIAL STATE CORPORATIONS IN KENYA: A CASE OF JOMO KENYATTA FOUNDATION

Emmy Chelangat Rop and Dr. Gladys Rotich
EFFECT OF RISK MANAGEMENT PRACTICES ON FINANCIAL PERFORMANCE OF COMMERCIAL STATE CORPORATIONS IN KENYA: A CASE OF JOMO KENYATTA FOUNDATION

Emmy Chelangat Rop  
Post Graduate Student: Jomo Kenyatta University of Agriculture and Technology  
Corresponding Author’s Email: emmychelangat@yahoo.com

Dr. Gladys Rotich  
Lecturer: Jomo Kenyatta University of Agriculture and Technology  
Email: grotich@jkuat.ac.ke

Abstract

Purpose: Risk if not well managed could lead to dissatisfactory performance of most organizations. Risk management should be at the central part of an organization’s operations by integrating risk management practices into Systems, processes, and culture of the entire organization. This study sought to establish the effect of Risk management practices on financial performance of Commercial state corporations in Kenya, a case of JKF.

Methodology: The study adopted a descriptive study. The total population of the study was the employees of JKF. According to 2014/2015 Kenya National Audit office report, there are 119 employees of JKF. The study used secondary data which was collected from published reports and audited financial statements for five years for periods between 2011 and 2016. The collected data was analyzed using descriptive and inferential statistics. The study adopted regression analysis and statistical significance was measured at the 5% level of significance. R² was used to determine strength of the relationship of the variables under study.

Results: The study found significant relationships between financial performance of commercial state corporations and operational, financial and strategic risk management practices to an extent of 98.7%, 92.7% and 87.4% respectively. The findings indicate that there is a fairly strong positive relationship between reputational risk management practices and financial performance to an extent of 56.2%. Efficient management of operational risks leads to lower operating expense and increased profitability. Practices that lead to general reduction of liabilities would positively affect firm’s financial performance.

Unique contribution to Theory, Practice and Policy: The study recommended that state corporations should comprehensively implement risk management good practices as outlined in their “MWONGOZO” guidelines. Further it was recommended that future studies should be carried out to include all state corporations based on data from a longer duration.

Key Words: Risk Management Practices, Financial Performance, Commercial State Corporations and Jomo Kenyatta Foundation
1.0 INTRODUCTION

In the face of major indignities leading to downfall of big corporations, especially state owned ones, it is expected that the wider society has started questioning how organizations in Kenya and the world at large are run. Most state corporations have not performed to the expectation since inception and large amounts of money have been added by Government to meet operating and capital expenditures. An example is KMC which was re-opened on 2006 after 15 years of Closure. In 2013 the Commission risked being wound up because of its inability to pay suppliers. A loss of Ksh.316, 664,883 was reported thereby depleting retained earnings to a negative balance. The Commission was not living upto its mandate because of mismanagement and its survival depended on support from the government (Kenao, 2014). As reported in the SC Consolidated Financial Statements for the year ended 30th June 2016, most Commercial State corporations registered losses; Chemelil Sugar Company (Ksh.696,560,561), Kenya Broadcasting Corporation (Ksh.368,427,000), Kenya Civil aviation (Ksh.259,817,385), Kenya safari lodges and Hotel (Ksh.110,885,000), Kenyatta international Convention Centre (Ksh.63,450,000), Nzoia sugar company(Ksh.1,167,209,961), Numerical Machine Complex (Ksh.136,087,263) etc.(The National Treasury(TNT), 2016).

Krause and Tse (2016) identified that Firms that use sound risk management practices obtain higher valuations, achieve better financial performance and experience diminished costs of financial distress. Recent empirical evidence provides support for theoretical propositions in the literature that risk management practice increases value and returns. There is therefore need to pre-empt and prepare for them when and if they eventually occur. This is where risk management and financial performance comes in, changing perception about risks being threats to being opportunities to minimize cost. This study focused on Commercial state Corporations. Commercial state Corporations do not in general depend on exchequer funds to meet their operations except in cases where the Corporation is unable to sustain itself on account of persistent unexpected performance. However, this has not been the case as most Commercial state corporations have not performed to the expectation and large amounts of money have been added by the Government.

The public sector in many countries today faces a major challenge to adapt to the new global reality of doing more with less or doing less with less. At the same time risk management has developed into a dominant concept of vital importance for the survival of public organizations as a new methodology approach to decision making for public officials (Eleftheriadis & Vyattas, 2018). A study conducted by the Permanent Subcommittee on Homeland Security and Governmental Affairs of the United States Senate in 2007, identified a number of factors that affect financial Performance of firms in the United States. Such factors identified include; high risk lending, regulatory failure, inflated credit ratings and investment bank abuses were identified as the main cause of financial crisis in the United States (United States Senate, 2011).

A survey on global perspective on operational Risk management and practice by institute of operational Risk and the Centre for Financial professionals revealed that operational risk management practice is going through a process of continual change in range of aspects of the discipline. The significance of operational risk losses continues to grow in importance as continued large losses are experienced by institutions across the globe (Peters, Clark, Thirlwel & Kulwa, 2018).
Lyambiko (2015) on her study on the effect of operational Risk management practices on financial performance of commercial banks in Tanzania established that operational Risk management practices are positively correlated with financial performance of commercial banks in Tanzania. Oluwagbemiga, Idode and Ogunbade (2016) examined the relationship between risk management practices and financial performance of the Nigerian listed banks. The overall results reveals that risk management practices have a statistically significant impact on financial performance.

Muriungi, Waithaka and Muriuki (2017) found out that operational risk management, financial risk management, market risk management, strategic risk management contribute to financial stability of state corporations in Kenya. Kimotho(2015) found out that operational risk management, strategic risk management, financial risk management and governance risk management practices had positive significant effects on the Financial performance of commercial state Corporations in Kenya. A survey conducted by PWC indicated that despite the fact that Kenya has tried to address risks such as economic crime and fraud through various legislation, risk in Kenya was still high (52%) above the African average of 50% and substantially higher than the global average of 37% (Price Water House Coopers (PWC), 2014). The common types of risks reported in the survey were; asset misappropriation, accounting fraud, bribery and corruption, procurement fraud and cyber-crime. Asset misappropriation in form of theft, accounting fraud, bribery and corruption, procurement fraud and cybercrime increases the cost of doing business and therefore affects financial performance of the firms (PWC, 2014).

Jomo Kenyatta Foundation was the main Focus in this study. The Foundation has what is needed for the study. The Company’s turnover increased by about 13 million to Ksh. 591 million compared to the prior year’s turnover of Ksh. 577 million in 2014/2015 financial year. The improved position led to a gross profit of Ksh. 321 million while operating profits stood at Ksh.326 million after factoring in other income. Overall the Foundation recorded a profit of Ksh.86 million. This was mainly attributable to the increased sales as indicated earlier and cost containment which saw only marginal increase in cost of sales and operating expenses when compared to the previous year Performance Framework. The Jomo Kenyatta Foundation subscribes to the principle and practice of responsible corporate citizenship (Kenao, 2015).

In ensuring a well trained staff and in a bid to improve service delivery and the quality of the Foundation products, the Foundation has continued to implement its capacity development policy. The Foundation had a staff establishment of 119 employees as at 30 June, 2015 and has continued to support the training and development of staff through sponsorship to various colleges, courses and workshops. JKF projects to the future and its Strategic Plan is aligned to the country’s strategies as envisioned in the Constitution of Kenya 2010 and Vision 2030 together with the Millenium Development Goals (MDGs). The Plan has strategies expected to support the two core functions of publishing and scholarships in a sustainable manner. So far the Foundation has digitized some books to take advantage of the digital initiative being advocated by the Government. This is in addition to placing more books (Kenao, 2015).

Marketing department’s main objective is to ensure goods reach the market through the designated channels of distribution. Sales and marketing team visits the educational institutions to create demand then ensure the outlets have enough of stocks to service the created demand. Promotion of products is done through various activities and events like
displays and teacher workshops countrywide. JKF fully comply with the statutory requirements of timely submitting reports to the various regulatory bodies. The Foundation donates books as part of its Corporate Social Responsibility (Kenao, 2015).

Statement of the Problem

Commercial State Corporations do not in general depend on exchequer funds to meet their operations except in cases where the Corporation is unable to sustain itself on account of persistent unexpected performance. However, this has not been the case as most Commercial State Corporations have not performed to the expectation and large amounts of money have been added by the Government to meet operating and capital expenditures. For this reason, the wider society has started questioning how organizations in Kenya and the world at large are run.

A case in point is Kenya Meat Commission (KMC) which was re-opened on June 2006 after 15 years of Closure. In 2013 the Commission risked being wound up because of its inability to pay suppliers. A loss of Ksh.316, 664,883 was reported thereby depleting retained earnings to a negative balance. The Commission was not living up to its mandate because of mismanagement and its survival depended on support from the government (Kenao, 2014). As reported in the SC Consolidated Financial Statements for the year ended 30th June 2016, most Commercial State corporations registered losses; Chemelil Sugar Company (Ksh.696,560,561), Kenya Broadcasting Corporation (Ksh.368,427,000), Kenya Civil aviation (Ksh.259,817,385), Kenya safari lodges and Hotel (Ksh.110,885,000), Kenyatta international Convention Centre (Ksh.63,450,000), Nzoia sugar company (Ksh.1,167,209,961), Numerical Machine Complex (Ksh.136,087,263) etc. (TNT, 2016).

Taking into account that most of these corporations are big players in their respective segments, it is difficult to understand why they have continued to report deficits. Part of the reason for these deficits is the ineffective management of risks (Odoyo, Omwono, & Okinyi, 2014). Theoretically, risk management plays a key in improving firms’ financial performance (Kaplan & Mikes, 2012). A need therefore arises to investigate the effect of risk management practices on financial performance of commercial state Corporations.

2.0 LITERATURE REVIEW

Theoretical Review

Stakeholders Theory

This theory is believed to have been engrained in the management discipline in 1970 and was progressively advanced by Freeman (1984) and is said to encompass an extensive selection of stakeholders. The Stakeholder theory takes account of a wider group of constituents rather than focusing on shareholders (Mallin, 2007). Stakeholders include shareholders, employees, suppliers, customers, creditors, communities in the vicinity of the company’s operations and general public. Stakeholder theory represents that the company is a separate organizational entity and it is connected to different parties in achieving wide range of purposes (Donaldson & Preston, 1995).

The theory highlights interests of different groups and argues on the possibility of favoring one group’s interest over that of other (Jones & Wicks, 1999). Donaldson and Preston (1995) point out that manager are responsible to deploy their wise decisions and best efforts in
obtaining benefits for all stakeholders. This theory focuses strategic decision-making and suggests that the interests of all stakeholders have fundamental value, and no sets of interests are assumed to dominate others (Clarkson, 1995; Abdullah & Valentine, 2009). This theory is therefore relevant to the study as it showed how different stakeholders are important instate corporations as the Board and management ensures safeguarding of all the stakeholders interests through Risk Management Practices.

Over the years, critics have attacked the vagueness and ambiguity of stakeholder theory (Fassin, 2008). The best results come out from this theory when this theory is applied on continuous basis in organization and sometimes the assessment of the analysis of this theory may be subjective and it is also not possible that all stakeholder interests can be met at the same time and as usual company can give more importance to stakeholders like shareholders of the company instead of employees and consumers (Soni, 2016).

**Modern Portfolio theory**

In March 1952 Harry Markowitz introduced modern portfolio theory (MPT), a concept that has gained in popularity over the years and greatly influenced portfolio construction and management practice. Modern Portfolio theory (MPT) is a theory of investment which tries to maximize return and minimize risk by carefully choosing different assets (Markowitz, 1952). It is a mathematical formulation of the concept of diversification in investing so as to select a collection of investment assets that has collectively lower risk than any individual asset.

MPT is most widely used in asset allocation, which entails selecting the appropriate asset classes and weights for portfolios. Portfolio managers typically use historical data for the risk–return inputs. Applying both a historical performance as well as a risk premium approach, the authors provide several examples of the inputs that can be used in asset allocation. With either approach, the greater the volatility of an asset's returns, the harder it is to predict the future returns of that asset; portfolio managers may also wish to alter these inputs either subjectively or objectively (Fabozzi, Gupta, & Markowitz, 2003).

Mandelbrot and Hudson (2004) found that a collection of both types of assets can therefore have lower overall risk than either individually. For Risk Management, MPT has important implications in terms of risk minimization by investing in portfolios that have lower overall risks. Barton, Shenkir and Walker (2002) found that MPT enables firms’ Risk Management, using a holistic approach, to identify and manage its risk so as to create, protect and enhance shareholder’s value.

Olsson (2008) adds that MPT recognizes that risk management has evolved into a major industry and is still evolving with the evolution of the financial community and development of new complex financial instruments. This theory is important to our study as it outlines how firms in the new technological and economical dispensation try to maximize return and minimize risk by carefully choosing different assets that are risk averse.

MPT has been subjected to various criticisms. The assumptions made have been criticized due to research findings in other fields of study, particularly within behavioural economics. The behaviourial economists have proven that the assumption on “investors' acting rationally” is wrong. In the same way the studies carried out in the area of behavioural finance, have challenged the idea that all investors have exact idea of potential returns, as normally the expectations of investors are biased. Furthermore, the theory does mathematical calculations
on expected values, based on past performance to measure the correlations between risk and return. However, experienced investors consider past performance not to be a guarantee of future performance. Taking into account only past performances leads to over passing newer circumstances, maybe not having existed during the time when the historical data were compiled (IFCM, n.d).

**Conceptual Framework**

<table>
<thead>
<tr>
<th>Independent variables</th>
<th>Dependent Variable</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Operational risk management practices</strong></td>
<td>Operating expense Ratio</td>
</tr>
<tr>
<td><strong>Financial risk management practices</strong></td>
<td>Ability to pay long term and short term obligations (Solvency Ratio)</td>
</tr>
<tr>
<td><strong>Strategic Risk Management practices</strong></td>
<td>Budget to actual variance analysis (Profit budget Variance)</td>
</tr>
<tr>
<td><strong>Reputational risk management practices</strong></td>
<td>Change in Revenue (Sales volume)</td>
</tr>
</tbody>
</table>

**Figure: 1 Conceptual Framework**

**Empirical Review**

Syomiti (2016) conducted a study to investigate the effects of operational risk management practices on financial performance in insurance companies. Descriptive research design was adopted on this research. The research adopted a census survey of all the 47 registered insurance companies operating in Kenya. The study adopted descriptive statistics. Data was analyzed using qualitative while the returns were analyzed by use of regression and correlation analysis model. Based on the findings the study concluded most of the insurance companies have risk and compliance department. This is because it understood that financial sector is the most unpredictable sector in the current financial crisis and is exposed to a number of risks. By having a good operational risk management it is expected to significantly influence performance of company’s functioning and efficiency by 41%, 22%. Risk analysts, executive management and employees and board of directors influence the financial performance to a greater extent. The research also found out those companies insures different types of risks but not all risks and that the company does not insure catastrophic risks and the company sets aside sufficient technical reserves to pay for claims.

Muriungi et al., (2015) conducted a study to determine the effect of risk management on financial stability of state corporations in Kenya. This study was quantitative in nature and employed an explanatory research design. This was because the study intended to provide an understanding of the relationships among the research variables. The study concentrated on
only tourism sector state corporations because it was expected that the players had the relevant and accurate information needed in the study. This study use da purposive sampling design to select 2 state corporations in the tourism sector from a total of 187 state corporations. Descriptive and inferential statistics were used to analyse information generated from respondents. In order to ensure ethical considerations were maintained, the identities of respondents filling the questionnaires were kept anonymous by not requiring them to indicate their names on the Questionnaires. The study found out that in financial risk management, operational risk management practices, strategic risk management practices and governance risk management practices affects financial stability in the state corporation.

Kimotho (2015) conducted a study to establish the relationship between enterprise risk management practices and Financial Performance among Commercial State Corporations in Kenya. Specifically, the study aimed at establishing the influence of Operational risk management practices, Strategic risk management practices, Financial risk management practices and Governance risk management practices on the Financial Performance of Commercial State Corporations in Kenya. The target population comprised of all the 55 Commercial SC in Kenya. Quantitative and qualitative data was collected using a semi structured questionnaire. Quantitative data was collected for a period of 5 years from 2010-2014 and analysed using descriptive statistics and factor analysis while qualitative data was analysed using content analysis. The results of the study indicated that Operational, Strategic, Financial risk and Governance risk Management Practices had positive effects on the Financial Performance of Commercial State Corporations to an extent of 70%, 71%, 66% and 72% respectively.

Wanjohi et al., (2017) undertook a study on the effect of financial risk management on the financial performance of Commercial Banks in Kenya the study assessed the current risk management practices of the commercial banks and linked them with the banks’ financial performance. Return on Assets (ROA) was averaged for five years (2008-2012) to proxy the banks’ financial performance. To assess the financial risk management practices, a self-administered survey questionnaire was used across the banks. The study used regression analysis of data and the findings were presented in the form of tables and regression equations. The study found out that majority of the Kenyan banks were practicing good financial risk management and as a result the financial risk management practices have a positive correlation to the financial performance of commercial banks in Kenya.

Pendo et al., 2016 conducted a study on Influence of financial risk management practices on the performance of commercial banks operating in Migori County, Kenya. The research used a descriptive survey design. The population of interest consisted of the six banks under study which include the following: Equity bank Ltd, Cooperative Bank Ltd, National bank Ltd, Diamond trust bank Ltd, Kenya commercial bank Ltd and Barclays bank Ltd all operating in Migori County, Kenya. The results were that financial risk management practices had affected the financial Performance of the banks to a great extent as shown by 59.4%, 34.4% of the respondents said to a moderate extent, while a small proportion of the respondents as shown by 6.3% reported that financial risk management practices had affected the financial Performance of the bank to a less extent.

Omondi (2017) conducted a study to establish how corporate reputation strategies affected performance in Kenya’s oil marketing company. Study population was oil companies in Kenya and target population was 35 known oil marketing firms in Kenya. Primary data was
collected and analysed to derive conclusion. Outcome was that majority of companies had an already documented strategy to manage their reputation. The study also found out that most respondents agreed to the fact that corporate reputation management strategies contribute highly to success of the company. The study concludes that the variations in performance of oil marketing firms can be well explained by variations in response to the strategies including responding to negative cues, assertive strategies and auto communication.

Vig, Dumicic and Kloputan (2017) investigated the relationship between corporate reputation and financial performance. The survey of the paper was conducted in 2015 in Croatia. The questionnaire for assessing corporate reputation contained three reputational dimensions: products and services, corporate integrity, and organizational performance while the financial dimensions contained indicators of EVA, ROCE, ROA, ROE and the financial stability coefficient. Hierarchical regression methods were applied in the analysis. This research leads to the conclusion that some dimensions of corporate reputation can be important predictors of financial performance. Results of the research could be a valid motivation for business executives to consider reputation risk as a critical issue of corporate business strategy.

3.0 RESEARCH METHODOLOGY
The study adopted a descriptive study. The total population of the study was the employees of JKF. According to 2014/2015 Kenya National Audit office report, there are 119 employees of JKF. The study used secondary data which was collected from published reports and audited financial statements for five years for periods between 2011 and 2016. The collected data was analyzed using descriptive and inferential statistics. The study adopted regression analysis and statistical significance was measured at the 5% level of significance. R² was used to determine strength of the relationship of the variables under study.

4.0 FINDINGS
4.1 Background information
The study was based on published financial results for the Jomo Kenyatta Foundation from year 2012 to 2016. The following subsections present five year trends of the base indicators namely net income, total revenue, total liabilities, total assets and operating expenses.

4.1.1 Net Incomes trends
Net Income is a key factor in determination of ROA which is the dependent variable in this study. The figure below shows the trends of net income from the year 2012 to 2016 for JKF.
From figure 2 above, the annual net income steadily increased starting from a loss of Shillings sixteen million in 2012 to a profit of over eighty seven million in 2016. This indicates that JFK implemented workable strategies that saw to a steady increase in its income over the years.

4.1.2 Annual Total Revenue trends (year 2012-2016)

Total revenue was used as an indicator for reputational risk management strategies in this study. The figure below presents the annual revenues for the five years starting 2012 to 2016.

From the figure 3 above, there was remarkable rise in revenue from year 2012 to year 2013. The revenue stagnated for years 2014 and 2015. However, year 2016 saw a marked rise in revenues by over one hundred million shillings compared to year 2015. With the benefit of hindsight from the trend of net income discussed earlier, it appears that the gains in income was attributable more to increased efficiencies as opposed to corresponding rise in income.

4.1.3 Annual Operating Expenses trends (year 2012-2016)

The study used annual operating expenses expressed as a fraction of corresponding sales as an indicator for Operational Risk Management practices. The figure below presents the annual values of operating expenses for years 2012 to 2016.
From the figure 4 above, annual operating expenses rose by twenty million shillings between years 2012 and 2013. However, there was a sustained gradual downward trend for the next two years (2014 and 2015). Year 2016 however saw a marked rise of over one hundred million shillings in operating expenses. Annual operating expenses follow a trend similar to that of annual total revenues.

4.1.4 Total Assets and Total Liabilities trends (year 2012-2016)

The three key components in a balance sheet are Assets, liabilities and equity. The study adopted Return on Assets, which is the quotient of net income and total assets, as the dependent variable representing financial performance. The figure below shows comparative trends of assets and liabilities values for years 2012 to 2016.

Fig. 5 Assets and Liabilities trends for years 2012 to 2016

From figure 5 above, the trends of assets and liabilities have been similar throughout the period of study. However, as can be seen from the bars connecting the two line graphs, there has been steady albeit marginal increase in equity (which is the difference between assets and liabilities).

4.2 Financial Performance and Risk Management Practices

The study sought to establish the relationship between risk management practices and financial performance. The independent variables were solvency ratio, operating expenses ratio, total revenue and profit budget variance. The dependent variables were return on assets and return on equity. However, the results were presented for one dependent variable only, ROA, since the correlation analysis yielded a near perfect correlation between ROA and ROE as shown in the table below.

Table 1: ROA versus ROE Correlation

<table>
<thead>
<tr>
<th></th>
<th>ROA</th>
<th></th>
<th>ROE</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>ROA</td>
<td>Pearson Correlation</td>
<td>1</td>
<td>.992**</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.001</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>5</td>
<td></td>
<td>5</td>
</tr>
<tr>
<td>ROE</td>
<td>Pearson Correlation</td>
<td>.992**</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Sig. (2-tailed)</td>
<td>.001</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>5</td>
<td></td>
<td>5</td>
</tr>
</tbody>
</table>

**. Correlation is significant at the 0.01 level (2-tailed).
From table 1 above, the two indicators for dependent variable have a near perfect positive correlation of 99%. Thus only one indicator, namely ROA was adopted for further analysis.

### 4.2.1 Operational risk management practices and financial performance

The study sought to establish the relationship between operational risk management practices and financial performance. Linear regression analysis was used to establish the relationship. The tables below present the results.

**Table 2: Regression model for operational risk management and firm performance**

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.993(^a)</td>
<td>.987</td>
<td>.982</td>
<td>.00981</td>
</tr>
</tbody>
</table>

\(a\). Predictors: (Constant), Operating Expense Ratio

From table 2 above, the R square value is 0.987 indicating that operational risk management practices explains 98.7% of the variability in firm performance.

**Table 3: Table of Coefficients for operational risk management and firm performance**

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>1.162</td>
<td>.072</td>
<td>16.239</td>
</tr>
<tr>
<td></td>
<td>Operating Expense Ratio</td>
<td>-1.166</td>
<td>.078</td>
<td>-.993</td>
</tr>
</tbody>
</table>

\(a\). Dependent Variable: ROA

From table 3 above, the constant is 1.162 and the coefficient for operating expense ratio is -1.166 with a p-value of .001. The resulting linear regression equation is as follows.

\[
y = 1.162 - 1.166x
\]

\( (p<.05) \quad (p<.05) \)

From the foregoing results, operational risk management practices has a very strong (R2 =.98>.7) significant relationship (p=.001<.05) with financial firm performance.

The indicator for operational risk management practices was operating expense ratio which is a measure of what it costs to operate a piece of property compared to the income that property brings. This means that when expense ratio decrease, the firm’s financial performance increase. Decrease in operating expense ratio is due to efficiency in management of operational risk which leads to lower operating expenses and increased profitability.

These results conform to those of Syomiti (2016) who conducted a study to investigate the effects of operational risk management practices on financial performance in insurance companies and found that good operational risk management significantly influences performance of company’s functioning and efficiency.
4.2.2 Financial Risk management practices and financial performance

One of the main objectives of the study was to find out the effect of financial risk management practices on financial performance. The dependent variable was ROA and the indicator for financial risk management practices was solvency ratio. Linear regression analysis was used to establish the relationship. The following two tables summarize the regression analysis results.

**Table 4: Regression model for financial risk management and firm performance**

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.963(^a)</td>
<td>.927</td>
<td>.903</td>
<td>.02305</td>
</tr>
</tbody>
</table>

\(^a\) Predictors: (Constant), Solvency Ratio

From table 4 above, the R\(^2\) value is 0.927 indicating a very strong linear fit between the financial risk management practices and firm performance. This implies that financial risk management practices explain 92.7% of the variability in firm performance.

**Table 4: Table of Coefficients for financial risk management and firm performance**

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>.007</td>
<td>.017</td>
<td>.409</td>
</tr>
<tr>
<td></td>
<td>Solvency Ratio</td>
<td>.247</td>
<td>.040</td>
<td>.963</td>
</tr>
</tbody>
</table>

\(^a\) Dependent Variable: ROA

From table 4 above, the constant is 0.07 and the coefficient for solvency ratio is .247 with a p-value of .009. The resulting linear regression equation is as follows.

\[ y = 0.07 + 0.247x \]  
(p<.05)  
(p<.05)

From the foregoing results, financial risk management practices has a very strong (R\(^2\) =.98>.7) positive significant relationship (p=.001<.05) with financial firm performance. Practices that lead to a general reduction in liabilities would positively affect firm’s financial performance. Additionally, practices that lead to a general increase in income without proportionately increasing liabilities will improve firm financial performance. These findings support the findings of Muriungi et al., (2015) who conducted a study to determine the effect of risk management on financial stability of state corporations in Kenya. They found out that financial risk management practices affects financial stability in state corporations.

4.2.3 Strategic Risk management practices and financial performance

The study sought to determine the influence of strategic risk management practices and financial performance. The indicator for strategic risk management was profit budget variance while that of financial performance was ROA. The tables below show the findings.
From table 5 above, the regression model yielded a very good linear fit between strategic risk management and firm performance ($R^2 = .874 > .7$)

Table 5: Regression model for strategic risk management and firm performance

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.935a</td>
<td>.874</td>
<td>.831</td>
<td>.03034</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Profit budget Variance

The results displayed in table 6 above indicate that the constant is 0.108 and the coefficient for profit budget variance is -0.028 with a p-value of .020. The linear regression analysis thus yielded the following equation.

$$y = 0.108 - 0.028x$$

From the findings displayed in table 5 and 6 above, strategic risk management practices has a very strong ($R^2 = .874 > .7$) negative relationship (p=.020<.05) with financial firm performance.

The findings shows that strategic risk management practices have a strong relationship with firm performance. Thus, in order to increase firm financial performance, Commercial state corporations ought to implement better strategic risk management practices by specifically focusing on trends, future events and circumstances not only as threats but as untapped opportunities in strategic design, while considering the allocated resources needed to execute the adaptive strategy.

These findings are in agreement with those of Kimotho (2015) whose study sought to establish the relationship between enterprise risk management practices and Financial Performance among Commercial State Corporations in Kenya. He concluded that strategic risk management practices influence firm performance to a great extent.

4.3.4 Reputational Risk management practices and financial performance

The study sought to establish the effect of reputational risk management practices on financial performance. The indicator for reputational risk management practices was sales volume (presented in “million shillings”) while that of financial risk management was ROA. The tables below present the results.
Table 7: Regression model for reputational risk management and firm performance

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.750a</td>
<td>.562</td>
<td>.416</td>
<td>.05648</td>
</tr>
</tbody>
</table>

The results in Table 7 above show that the regression analysis yielded a fairly strong linear fit ($R^2 = .562 < .7$).

Table 8: Table of Coefficients for reputational risk management and firm performance

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>-.325</td>
<td>.215</td>
<td>-1.512</td>
</tr>
<tr>
<td></td>
<td>Total Revenue</td>
<td>.708</td>
<td>.361</td>
<td>.750</td>
</tr>
</tbody>
</table>

a. Dependent Variable: ROA

From table 8 above, the constant is -0.325 and the coefficient for operating expense ratio is -0.078 with a p-value of .145. The resulting linear regression equation is as follows.

$$y = -0.325 + 0.078x$$

(p>.05) (p>.05)

These results indicate that reputational risk management practices has a fairly strong ($R^2 = .562 < .7$) positive relationship with financial firm performance. However, this relationship was not found to be statistically significant (p=.145>.05).

The findings indicate that there is a fairly strong positive relationship between reputational risk management practices and financial performance. It suggest that reputational damaging events which impact on customer perception lead to the reduction in revenue and operating cash flow in a fairly strong positive impact. These findings contradict those of Omondi (2017) and Vig, Dumicic and Kloputan (2017) who found a strong relationship between reputational risk management practices and firm financial performance.

4.2.5 Joint relationship of Risk management practices and financial performance

The study sought to establish the combined effect of risk management practices on firm performance. Multiple stepwise regression analysis was used to establish this relationship. The tables below display the regression analysis results.

Table 9: Regression model for risk management practices and firm performance

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.993a</td>
<td>.987</td>
<td>.982</td>
<td>.00981</td>
</tr>
<tr>
<td>2</td>
<td>1.000b</td>
<td>.999</td>
<td>.998</td>
<td>.00329</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Operating Expense Ratio
b. Predictors: (Constant), Operating Expense Ratio, Solvency Ratio
From the table above, the regression analysis ended at the second step yielding two models. The first model yielded R square of .987 indicating that Operational risk management practices as represented by operating expense ratio explained 98.7% of the variability in performance. The second model yielded R Square of .999 implying that the predictors, namely Operational risk management practices and financial risk management practices accounted for 99.9% of the variability in Firm performance. The other two variables, namely strategic risk management practices and Reputational risk management practices were removed from the regression equation as they did not make any significant contribution to the goodness of fit.

Table 10: Table of Coefficients for risk management factors and firm performance

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>1.162</td>
</tr>
<tr>
<td></td>
<td>Operating Expense Ratio</td>
<td>-1.166</td>
</tr>
<tr>
<td>2</td>
<td>(Constant)</td>
<td>.840</td>
</tr>
<tr>
<td></td>
<td>Operating Expense Ratio</td>
<td>-.843</td>
</tr>
<tr>
<td></td>
<td>Solvency Ratio</td>
<td>.076</td>
</tr>
</tbody>
</table>

a. Dependent Variable: ROA

From table 10 above, the regression analysis yielded a best fitting model with two independent variables as indicated by the second model. The constant is 0.840 and the coefficient for operating expense ratio is -0.843 with a p-value of .007, while solvency ratio representing financial risk management practices has constant coefficient of 0.076 with a p-value of .038. The resulting linear regression equation is as follows.

\[ y = 0.840 - 0.843x_1 + 0.076x_2 \]

(p<.05) (p<.05) (p<.05)

From the table above, operational risk management practices (measured by operating expense ratio) has a negative significant (r<.05) relationship with firm financial performance. Financial risk management practices (solvency ratio) has a positive significant (r<.05) relationship with firm performance.

5.0 SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

Summary

The study found out that the Correlation analysis showed that there was a strong negative relationship between operational risk management practices and financial performance. This relationship was found to be statistically significant. The correlation analysis between financial risk management practices and firm performance yielded a very strong positive relationship and statistically significant. The correlation analysis showed that there was a strong negative relationship between strategic risk management practices and financial performance. This relationship was found to be statistically significant. The correlation analysis showed that there was a fairly strong positive relationship between reputational risk
management practices and financial performance. The relationship was not found to be statistically significant.

Conclusion

The study concluded that there exist a negative and significant relationship between operational risk management practices and financial performance. It can be concluded that there exist a strong positive relationship between financial risk management practices and financial performance. It was found that strategic risk management practices have a strong relationship with firm performance. It was concluded that while reputational risk management practices do have a positive relationship with firm financial performance, the relationship was not statistically significant.

Recommendations

The study recommended that parastatals should implement better risk management practices with a key focus being on operational, financial and strategic risk management practices. To this end, the ‘MWONGOZO’ code of governance for State Corporations issued by the PSC should be implemented to the letter. The code directs the Board of each SC to ensure that it set out its responsibility for risk management in the Board charter, approve the risk management policy and the risk management framework, delegate to management the responsibility to implement the risk management plan, monitor that risks taken are within the set tolerance and appetite levels, review the implementation of the risk management framework on a quarterly basis, appoint a Committee responsible for risk management in the organization, ensure that the Committee obtains relevant technical advice where necessary, evaluate the performance of the Committee once a year, establish a risk management function within the organization, ensure that risk assessment is carried out on a continuous basis and receive assurance from Management that the risk management framework is integrated in the daily activities of the organization.

References


Eleftheriadis, I. & Vyattas, V. (2018). Risk and performance in Public Sector. 10.1007/978-3-319-31816-5_3453-1


