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EFFECT OF AVERAGE ACCOUNT PAYABLES ON PROFITABILITY OF PRIVATE SECURITY FIRMS IN KISUMU COUNTY, KENYA

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Abstract:
In today's dynamic business environment, efficient account payable management is a critical factor in sustaining and enhancing profitability while mitigating risk and maximizing firm value. Although firms strive to align their strategies with growth objectives and annual profitability targets, inadequate liquidity can hinder their ability to generate returns for shareholders. Therefore, effective account payable management practices are essential. Despite the significance of this topic, there remains a gap in understanding the impact of account payable management on the profitability of private security firms, particularly in emerging economies like Kenya. This study examines the effect of account payable management on profitability of private security firms in Kisumu County, Kenya, from 2019 to 2023. Specifically, the study assesses the impact of average accounts payable on the profitability of these firms. A correlational research design was adopted, targeting private security firms registered with the Private Security Regulatory Authority in Kisumu County. The study relied on secondary data obtained from financial statements, with Return on Assets (ROA) serving as the profitability measure. Findings indicate that average accounts payable significantly influence the profitability of private security firms in Kisumu County (β =9.301, p=0.006). Results imply that account payable for private security firms in Kenya should be well managed for the firms to improve their profitability. These results provide valuable insights for private security firm managers, scholars, and policymakers, including government and stakeholders, in shaping financial management strategies.

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Keywords: working capital management practices, average accounts payable, private security firms, profitability

1. Introduction

Management of short-term finances involves strategic handling of a firm's short-term assets and liabilities, with the primary objective of ensuring liquidity, enhancing profitability, and maximizing shareholder value (Smith, 2019). Effective working capital management (WCM) entails regulating short-term resources and obligations to optimize asset returns while minimizing liability costs (Johnson, 2021). A well-managed working capital position strengthens a firm's financial health, ensuring liquidity and supporting business expansion, ultimately contributing to shareholder value.

Working capital refers to the financial resources required for a firm's daily operations, primarily short-term financing. It is typically non-interest-bearing, such as capital tied up in inventory (Smith, 2022). The primary objective of WCM is to maintain seamless operations by ensuring adequate liquidity to meet both immediate short-term obligations and future operational expenses (Naseer & Bibi, 2018). Efficient management of short-term finances is particularly crucial for private security firms, as the effective handling of short-term assets and liabilities significantly impacts their financial performance. While profitability remains a key objective, ensuring sufficient liquidity is equally critical.

Accounts payable represent a firm's short-term obligations to suppliers for goods or services obtained on credit. According to Deloof (2014), accounts payable can significantly affect profitability, either enhancing or diminishing a firm's financial performance. The effect of accounts payable on a security firm's earnings primarily depends on supplier relationships and cash flow management (Lazaridis & Tryfonidis, 2016). Failure to meet accounts payable obligations may result in penalties, interest charges, or even the revocation of supplier credit (Filbeck & Krueger, 2005). Padachi (2006) notes that firms facing financial constraints must balance extended payment delays from customers with delays in settling supplier payments. Security firms may extend payable days due to excessive inventory investments or delays in receivables (Deloof, 2014). By delaying payments, firms can retain cash for longer periods, allowing for alternative investments or operational expenditures, thereby enhancing profitability (Lazaridis & Tryfonidis, 2016).

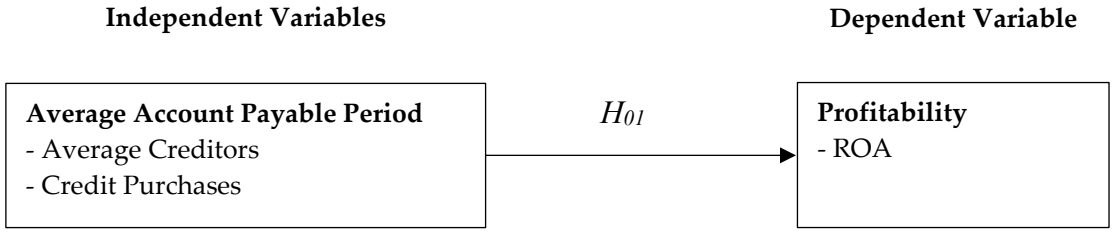
Focusing solely on profitability without adequate liquidity management can lead to significant financial distress (Naseer & Bibi, 2018). Striking a balance between these two objectives is essential, as prioritizing one at the expense of the other can have adverse effects, including insolvency or bankruptcy (Naseer & Bibi, 2018). Consequently, working capital must be carefully managed to safeguard a firm's financial stability and enhance profitability. Optimizing a firm's working capital position ultimately contributes to overall firm value (Achchuthan & Kajamanthan, 2013).

Financial performance is an objective measure of a firm's effectiveness in utilizing its assets to generate revenue (Margaretha & Oktaviani, 2016). Researchers employ both accounting-based and market-based measures to assess business performance. Accounting-based measures provide insights into managerial effectiveness and are particularly relevant in studies involving corporate governance and firm performance (Hutchinson & Gul, 2004; Mashayekhi & Bazazb, 2008).

Gerrit and Mohammad (2010) identify various financial performance indicators, including return on assets (ROA), return on sales, return on equity, return on investment, return on capital employed, and sales growth. This study adopts Return on Asset as the primary measure of financial performance, as it is widely regarded as a critical profitability metric, reflecting the percentage earned on each unit of money invested in assets (Rushdi & Tennant, 2003). Profitability, defined as a firm's ability to generate income (Johnson & Brown, 2021), is largely dependent on operational efficiency and the optimal utilization of available resources (Smith, 2022).

Effective working capital management plays a crucial role in this process, as the management of cash, receivables, and inventory directly influences profitability (Smith, 2022). Excessive inventory can lead to increased storage costs, obsolescence, and potential losses due to theft, thereby diminishing profitability (Knauer & Wöhrmann, 2013). Conversely, inadequate inventory levels may result in stockouts, customer dissatisfaction, and lost sales, ultimately affecting profitability.

Figure 1: Conceptual Framework



Source: Adopted and modified from Lazaridis, I., & Tryfonidis, 2016.

2. Literature Review

Accounts payable, also known as trade payable, are the aggregate amount of an entity's short-term obligations to pay suppliers for products or services which the entity bought on credit. (Deloof *et al.*, 2003), accounts payable can have a serious impact on profitability and can either improve a firm's profitability or cause it to decline. The two primary ways that account payables impact security firms' profitability are the company's relationship with its suppliers and the company's cash flow (Lazaridis & Tryfonidis, 2006). Defaulting on paying the accounts payable may trigger a penalty or interest payment, or the revocation or curtailment of additional credit from the supplier (Filbeck, 2005).

According to (Padachi, *et al.* 2008), if a firm is forced through financial stringency to keep its working capital constant, then, increased payment delays from customers

must be balanced by delaying payments to suppliers. The implication of those assertions is that security firms make significant investments in payables while adopting a working capital management policy (Ross, 2017). Security firms extend payable days if they over-invest in inventory or are not being paid on time from receivables (Deloof, 2003). Delaying payments allows the company to retain more cash for a longer period, which can be used for other investments or operational expenses, ultimately enhancing profitability (Lazaridis & Tryfonidis, 2006).

However, excessive delays in accounts payable management may negatively affect supplier relationships. Prolonged payment periods can lead to strained relationships, loss of discounts, or even potential disruptions in the supply chain. These adverse effects could result in higher costs for the company and ultimately impact profitability (Filbeck & Krueger, 2005). Striking the right balance between delaying payments for optimal cash flow management and maintaining strong supplier relationships is crucial for sustaining profitability in the long run (Shin & Soenen, 1998). This study thus seeks to understand the effects of account payable and profitability of private security firms in Kisumu County.

Extensive research on Working Capital Management has predominantly focused on industries other than private security firms. For instance, studies by Anser and Malik (2013) and Madugba and Ogbonnaya (2016) focused on the manufacturing sector, while Yahaya (2016) examined the pharmaceutical industry. Similarly, Iyewumi *et al.* (2015) investigated the oil and gas sector. Consequently, Yazdanfar and Ohman (2014) conducted a study using a large panel dataset of 15,897 Swedish small and medium-sized enterprises (SMEs) across five industrial sectors from 2009 to 2012. Their findings highlighted a preference for internal financing over external sources, with trade credit exerting a negative effect on profitability. Their study identified accounts payable, short-term borrowing, and long-term borrowing as key determinants of firm profitability. However, given the Swedish context, the applicability of these findings to private security firms in Kisumu County, Kenya, remains uncertain.

Madugba and Ogbonnaya (2016) investigated the effect of the average payment period on the financial performance of Nigerian manufacturing firms. Their regression analysis revealed a significant relationship between the average payment period and earnings per share, as well as return on capital employed. The study recommended employing professional inventory management strategies to optimize financial stability. Given the existing research gaps, this study focuses on private security firms in Kisumu County, Kenya, to provide insights into the effect of WCM on their profitability.

3. Methodology

This study examines the influence of average accounts payable on the profitability of private security firms in Kisumu County using a correlational research design. Correlational research assesses statistical relationships between variables without implying causation (Fraenkel & Wallen, 2000). This approach is appropriate for

determining whether the management of working capital practices, specifically average accounts payable, is associated with firm profitability (Creswell & Plano-Clark, 2011).

3.1. Sample Size and Study Population

The study population comprises 30 private security firms listed under the Private Security Regulatory Authority (PSRA) in Kisumu County. Data spanning 2019-2023 was collected from all listed firms, ensuring comprehensive analysis.

3.3 Data Analysis

Secondary data was sourced from financial statements, including key metrics such as total assets, liabilities, capital, and net income. The data were analyzed using SPSS statistical software, employing both descriptive and inferential statistical analysis.

3.4 Model Specification

A regression model was developed to examine the relationship between average accounts payable (X) and profitability (Y):

$Yi = \beta 0 + \beta 1X1\ (AAP) + \varepsilon i$

Where:
Yi = Profitability metric (ROA),
$\beta 0$ = Constant,
$\beta 1$ = Regression coefficient,
X1 = Average accounts payable period,
εi = Error term.

4. Results

The objective of this study was to examine the effects of the average accounts payable (AAP) period on the profitability of private security firms in Kisumu County. Specifically, the study sought to assess the impact of the Average Account Payable period on return on assets (ROA) as a measure of profitability.

4.1 Average Accounts Payable and Profitability

Table 1 presents the model summary of the effect of Average Account Payable on Return on Asset.

Table 1: Model Summary of the effect of Average Accounts Payable on ROA

Model Summary[b]					
Model	**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**	**Durbin-Watson**
1	.493[a]	.243	.216	2.34418	1.947
a. Predictors: (Constant), Average Accounts Payable					
b. Dependent Variable: Return on Assets					

Source: Financial statements (2019 – 2023).

As indicated in Table 1, the correlation coefficient (R) of 0.493 suggests a moderate positive relationship between AAP and ROA. Additionally, the coefficient of determination ($R^2 = 0.243$) indicates that AAP accounts for 24.3% of the variation in ROA, while the remaining 75.7% is explained by other factors not included in the model. Furthermore, the Durbin-Watson statistics of 1.947 suggest the absence of autocorrelation.

Table 2 presents the results of the ANOVA analysis assessing the relationship between Average Account Payable and Return on Asset.

Table 2: ANOVA analysis of the effect of Average accounts payable on ROA

ANOVA[a]						
Model		**Sum of Squares**	**Df**	**Mean Square**	**F**	**Sig.**
1	Regression	49.478	1	49.478	9.004	.006[b]
	Residual	153.865	28	5.495		
	Total	**203.343**	**29**			
a. Dependent Variable: Return on Assets						
b. Predictors: (Constant), Average Accounts Payable						

Source: Financial statements (2019 – 2023).

The ANOVA results indicate a statistically significant relationship between Average Account Payable and Return on Asset at the 5% level of significance [F (1, 28) = 9.004, p = 0.006].

Table 3 presents the regression coefficients, which indicate the predicted mean change in Return on Asset associated with a one-unit change in Average Account Payable.

Table 3: Regression Coefficients for the effect of Average accounts payable on ROA

Coefficients[a]								
		Unstandardized Coefficients		**Standardized Coefficients**	**T**	**Sig.**	**Collinearity Statistics**	
Model		**B**	**Std. Error**	**Beta**			**Tolerance**	**VIF**
1	(Constant)	7.301	.923		7.908	.000		
	AAP	-3.017	1.005	-.493	-3.001	.006	1.000	1.000
a. Dependent Variable: Return on Assets								

Source: Financial statements (2019 – 2023).

The results indicate that Average Account Payable has a statistically significant negative effect on profitability (ROA), as evidenced by the regression coefficient ($\beta = -3.017$), t-statistics (-3.001), and p-value ($0.006 < 0.05$). These findings suggest that for every one-unit increase in Average Account Payable, profitability decreases by 3.017 units. The results contradict previous studies by Kumaraswamy (2016) and Yahaya (2016), which found that Average Account Payable had a significant positive effect on profitability.

5. Conclusions and Recommendations

The study findings indicate that Average Account Payable has a significant relationship with Return on Asset among private security firms in Kisumu County. It is concluded that key elements of Average Account Payable, namely average creditors and credit purchases, significantly influence profitability. This suggests that private security firms in the region should effectively manage their average creditors and credit purchases.

Based on these findings, the study recommends that private security firms should consider extending their Average Account Payable period by negotiating more favorable payment terms with suppliers. This could alleviate cash flow pressures and enhance financial stability. Additionally, private security firms should formulate clear policies on working capital management to guide financial decision-making. Enhancing the financial literacy of management teams through targeted training programs on working capital management is also recommended. Finally, regular appraisals of working capital strategies should be conducted to identify weaknesses and implement necessary improvements, ensuring sustainable financial performance.

Conflict of Interest Statement
The authors declare no conflicts of interest.

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