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Full Length Research Paper

Managerial Competency and the Financial Performance of Savings, Credit and Cooperative Societies in Uganda

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Abstract

This study aimed at examining the relationship between managerial competency and financial performance of Savings, Credit and Cooperative Societies in Uganda. A quantitative research approach was used. Data were collected from Savings, Credit and Cooperative Societies operating in the eastern part of Uganda called Busoga using questionnaires. Data were analyzed using descriptive statistics, correlation and regression analysis methods. Results show that there is a positive relationship between managerial competency and financial performance (r =0 .610, p< .01). Results further reveal that corporate governance and managerial competence only explain 39% (R square= .392) of the variance in the financial performance of the Savings, Credit and Cooperative Societies in Uganda. This implies that 61% of the variance in financial performance is explained by other factors outside the model used. The results further indicate that the regression model was also well specified (F = 14.141, P <.01). This implies that the outcome from the model are reliable.

Keywords: Managerial Competency, Financial Performance, SACCOS, Uganda, Microfinance institutions

INTRODUCTION

From the study conducted by Murphy & Poist, (1994); managerial competency is one of the rare, valuable, and difficult to imitate resources to enable firms to attain superior performance. It involves knowledge, skills, personal traits and abilities (Gatewood &Field, 1994, Kerr & Werther, 2008, MacDuffie, 1995, Batt 2002; Levine &Toyson, 1990; Ahmad & Schroeder, 2003), which are predictors of success in the job that in turn affect the firms' performance. Morishima (2006) provides a relationship between corporate governance, Managerial competency and financial performance where corporate governance influences Managerial competency through corporate management strategies that in turn influence improvement of the financial performance. Although rich empirical literature exists focusing on corporate governance and financial performance, to my knowledge, Morishima (2006) is the only scholar who incorporated managerial competency.According to the Fin Scope Uganda Study Report of 2007, 62% of Uganda's population had no access to financial services.

The highest proportion of the un served population comes from the Eastern (Busoga inclusive) part of the country (Ministry of Finance, Planning and Economic Development -MOFPED, 2000).Savings, Credit and Corporative Societies (SACCOS) were adopted by Government of Uganda as a means through which the rural Communities could access financial services (www.ucscu.co.ug). This is so because SACCOs present one of the most appropriate ways and in some places the only alternative, to serve the non served population (SNV report, 2010). In order to implement the above, the Government of Uganda initiated a new Rural Financial Services Strategy through which the Rural Finance Services program (RFSP) was "born" in order to build a strong and vibrant SACCO movement. (http://www.ucscu.co.ug/data/smenu/21). The focus of RFSP is building a SACCO movement that is financially self sustainable. Good corporate governance and managerial competency have been the focal point for building profitable and self sustaining SACCOS (http://www.rfspug.org).Unfortunately, SACCOS have continued to register poor financial performance (Eriku, 2010). From the information available at Uganda Micro Finance Centre – Iganga zonal office, the average portfolio at risk for SACCOS in Busoga region increased from 87% to 90% in 2008/9 and 2009/10 financial years respectively. This is far below the benchmark of less than 10% .For the same period, the risk coverage ratio declined from 39% to 28%.Besides worsening; it is also below the benchmark of more than 50%. In a period of only 2 years, 20 SACCOS closed business after obtaining loans from MSC. (Uganda Microfinance support centre, Iganga zonal office, annual reports, 2008-2010)

Despite Government of Uganda and other stake holders effort to enhance the managerial competency and corporate Governance in SACCOS, their financial performance has generally remained poor (Watala, 2010; Eriku, 2010; Ocowun, 2010).The SACCOS in Busoga region in particular have shown a diminishing financial performance trend (MSC Iganga Zonal Office reports 2009-2011).

The average portfolio at risk, the risk coverage ratio and profitability showed a declining trend for the years 2008 to 2010.Besides worsening, they are far below the required benchmark.

The subject scope of this study was corporate governance, managerial competency and the financial performance of Savings, Credit and Cooperative Societies in Busoga region.

Literature review

Corporate governance and financial performance

Available research studies on Corporate Governance and Financial performance indicate that firms with better corporate governance tend to enjoy lower cost of capital (Black et al.2006), lower Cash Operating Expenses (COE) (Ashbaugh, Collins, & LaFond 2004). Lower COE improves the profitability of a firm. In Piprek (2007), the main constructs of financial performance are portfolio quality and profitability.

According to Miller (2011), firms that utilize governance tools more stringently to control agency costs will command greater contracting cost advantages, leading them to specialize in business with greater managerial discretion. Owing to the fact that Managers' pursue perquisite consumption instead of maximizing shareholder wealth when they are authorized to take discretionary actions, (Williamson, 1964, Jensen, 1986 and Stulz, 1990) argue that firms should reduce free cash flow under the discretionary control of managers so that they have fewer opportunities to undertake unprofitable investments. Myers & Smith (2010) find a stronger complementary relation between board independence and pay-for-performance among managers.

Other various studies show that corporate governance has a significant effect on the financial performance of an organization (Romano, Roberta, Bhagat, Sanjai & Brian, 2008, Chen & He, 2008, Chalhoub, 2009, Sueyoshi, et al., 2010, Mehdi, 2007, Brown & Caylor, 2009, Gürbüz', Aybars & Kutlu, 2010, Kumar, 2005, Black, et al. 2006, Ashbaugh, Collins, & LaFond 2004, Kaheeru, 2001, Edelman, 2010 and Maher & Andersson, 1999).

From the above, it is clear that the relationship between corporate governance and firm performance has received considerable attention with results showing significant relationship between the two.

However, (Dallas, 2011) notes that country-specific research on emerging markets has delivered mixed results, suggesting that empirical evidence on the relationship between corporate governance indicators and firm performance in emerging markets is inconclusive.

In addition, (Ponu, 2008) results from a study on Corporate Governance Structures and the Performance of Malaysian Public Listed Companies show that there is no significant relationship between corporate governance and company performance. Similar findings were obtained from Latona (2011), where it was found out that there is no difference in performance for companies having poor and excellent corporate governance. Hence no significant relationship was found between corporate governance and financial performance.

The above results indicate an inconclusive debate on the relationship between corporate governance and financial performance.

Board performance and financial performance

A 1997 survey commissioned by Russell Reynolds found out that the quality of corporate boards had become an important evaluation factor demanded by institutional investors. According to Heidrick and Struggles (2011), the continuing economic uncertainty and accompanying high profile governance failures mean that there is now greater attention on the boardroom than ever before. Increased accountability and scrutiny, multiple media and stakeholder pressures and shareholder activism are all contributing to making the job of a board member a lot more onerous and risky.

Despite rigorous efforts to raise corporate governance standards, insufficient attention has been paid to the behavioral as opposed to the technical challenges in boardrooms, such as the evolving role and required style of an effective chairman, team dynamics, optimizing delicate and complex relationships, enhancing diversity and the creation of a positive and thriving culture in the boardroom. For effective board performance, the board must benchmark with best in class boards and expediency in the approach to assessing corporate governance in furthering financial performance (BREFI Group, 2011; Heidrick & struggles 2011).

The key aspects for board performance include mix of board competencies, reviewing and engaging top talent for succession planning, effective board committees, right level of exposure to senior management, commitment, dedicating enough time to identifying opportunities, board evaluation, in depth experience, balance of independence and engagement with the right level of engagement with management and chairman's leadership style (Conger, Finegold & Lawle, 1998).The Board must develop, but not set a competitive strategy for the business that ensures a strategic planning process is in place, is sound and used to produce sound choices. The Board must monitor the implementation of current strategic initiatives to ensure they are on schedule and delivering effective results. In addition, ensure that the company has the highest caliber Chief Executive officer and executive team and that the company has adequate information. It must manage the risk by preventing and managing crises and ensure that controls and audit systems are in place for management to meet business objectives.

Whereas the debate of board performance concludes that board performance enhances good corporate governance, the findings were obtained from developed economies. In addition, it is a new debate that has no final conclusion. With All these gaps, it is imperative that this debate is extended to the financial performance of SACCOS.

Board composition and financial performance

Board composition refers to the number of independent non-executive directors on the board relative to the total number of directors (Tusiime et al., 2011). Independent non-executive directors are defined as independent directors who have no affiliation with the firm except for their directorship (Clifford & Evans, 1997, Tusiime et. al., 2011). There is an apparent presumption that boards with significant outside directors will make different and perhaps better decisions than boards dominated by insiders. The positions of the Board chairman and Chief Executive Officer (C.E.O) should be held by different and independent individuals following the agency theory (Eisenhardt, 1989, Jensen &Meckling, 1976, Hermalin & Weisbach, 2000).

The clear implication for corporate governance from an agency theory perspective is that adequate monitoring or control mechanisms need to be established to protect shareholders from management's conflict of interest – the so-called agency costs of modern capitalism (Fama & Jensen, 1983, Kiel & Nicholson, 2003).

To the contrary, the stewardship theory claims that managers are essentially trustworthy individuals and therefore good stewards of the resources entrusted to them (Donaldson & Davis, 1991, 1994, Donaldson, 1990). Proponents of the stewardship theory contend that superior corporate performance will be linked to a majority of inside directors as they work to maximize profit for shareholders. This is because inside directors understand the business they govern better than outside directors and so can make superior decisions. Underlying this rationale is the assertion that since managers are naturally trustworthy there will be no major agency costs (Donaldson & Preston, 1995). Stewardship theorists also argue that senior executives will not disadvantage shareholders for fear of jeopardizing their reputation .The stewardship theory argues that the board should have a significant proportion of inside directors to ensure more effective and efficient decision making. Similarly, CEO duality is seen as a positive force leading to better corporate performance, because there is clear leadership for the company.

On the other hand, sociologists have focused on the study of interlocking directorates and their implication for institutional and societal power (Pettigrew, 1992). By utilizing network analysis, investigators focus on the social networks in which enterprises are embedded and the importance of these networks for power within society (Scott, 1991). Such studies form the basis of resource dependence theory, which maintains that the board is an essential link between the firm and the external resources that a firm needs to maximize its performance (Pfeffer & Salancik, 1978; Pfeffer, 1972, 1973; Zald, 1969).

It is clear that the literature that addressed the relationship between board composition and financial performance (Hermalin & Weisbach, 1991, Mehran, 2005, Klein, 1998; Bhagat & Black, 2000, Topak, 2011); does not provide a clear cut on the right composition of the Board.

As such, there is no evidence to underpin a clear relationship between board composition and financial performance of a firm. As if that is not enough, it is not clear whether this has an impact on the SACCOS established in a developing country like Uganda. This is so because the studies were based on big Organizations in developing countries.

Board independence and financial performance

While executive directors are expected to provide first-hand information on the firms' operation to other board members (Boumosleh & Reeb, 2005; Tusiime et. al., 2011), they are usually aligned with the Chief Executive Officer. It is argued that board autonomy is critical to aligning the interests of owners and managers. An autonomous board can more effectively monitor and supervise management, enhancing shareholder value (Fama & Jensen, 1983, Baysinger & Butler, 1985). Board autonomy is generally measured by the proportion of independent directors on the board. In effect, a relatively autonomous board will help to minimize agency costs and thereby improve financial performance.

However, other studies suggest that excessive autonomy of the board can hinder financial performance. Excessive board autonomy may put management at career risk with higher management turnover (Heffes, 2007), create higher agency costs for creditors (Weber, 2006) and generate higher costs to protect the proprietary position of the firm. Therefore a high percentage of outside directors may result in lower financial performance (Agrawal & Kenoeber, 1996, Coles, McWilliams & Sen, 2001).

The above debate is clearly in support of the agency theory that focuses on mitigating agency costs through an independent board. This implies that it does not align well with other theories such as the stewardship theory and resource dependency theory. Besides, it does not provide the level of autonomy that boards should have in order to deliver superior financial performance of firms.

Transparency and financial performance

Transparency is integral to corporate governance. Transparency has become something of a synonym or proxy for good corporate governance (Casement, 2008, Rossouw, 2005, Augustine, 2012). Transparency is fundamentally about the availability of information to all the actors within the firm, principals, agents and stakeholders (Hebb, 2006).

Higher transparency reduces the information asymmetry between a firm's management and financial stakeholders (equity and bondholders), mitigating the agency problem in corporate governance (Sandeep & George, 2002). Ball (2001) argues that timely incorporation of economic losses in the published financial statements increases the effectiveness of corporate governance, compensation systems, and debt agreements in motivating and monitoring managers.

Corporate transparency comprises Financial accounting disclosures to major stakeholders, timeliness of disclosures, information dissemination and completeness of information. Robert & Abbie (2001) concur with this especially on institutional transparency, they outline the transparency dimensions as; completeness of financial information, release of information, timeliness and means of dissemination.

Greater information disclosure on the company's capital and control structures can be an important means to achieve a given goal. High quality and relevant information is crucial for exercise of governance powers. Full Disclosure seeks to avoid financial statements fraud (Beasley, 1996, Beasley, 2000; Matama, 2008).

There appears to be widespread agreement on the importance of trust in human conduct, but unfortunately there also appears to be an equally widespread lack of agreement on a suitable definition of the construct. Trust is a multifaceted construct, which may have different bases and phases depending on the context; it is also a dynamic construct that can change over the course of a relationship (Wayne & Megan, 2002).

There are at least five facets of trust that can be obtained from the literature on trust (Hoy & Tschannen-Moran, 1998; Tschannen-Moran & Hoy 2001; Matama, 2008; Wayne & Megan; 2002). These include benevolence, reliability, honesty and openness.

METHODOLOGY

Sampling design, sample size and procedure

The researcher used a simple random sampling technique. Using Krejcie and Morgan (1970) simplified table of sampling, 59 SACCOS were an appropriate sample size from a population of 69 SACCOS.

In order to choose the 59 SACCOS that formed the sample size, the researcher serialized all the 69 SACCOS from 1 to 69 following an alphabetic order of their names. The 69 serial numbers were each written on a piece of paper and folded. The 69 folded pieces of paper were put in a tin. The researcher randomly picked a piece of paper at a time until 59 pieces of paper were picked from the tin. The serial numbers that appeared on the 59 pieces of paper that were randomly picked; were matched to the SACCOS they represented thus forming the sample of the 59 SACCOS which were used for this research study.

The unit of analysis was a SACCO and the unit of inquiry was one respondent that was got from each SACCO. This respondent had to be a SACCO manager, a board member and/or SACCO accountant. These were the respondents who the researcher believed to be knowledgeable about the data that were required for this research study.

Data collection methods and instruments

The researcher used Primary data obtained from the respondents for this research study. This data was obtained from the respondents using a self administered questionnaire. Perceptions and beliefs were sought to a five-point Likert Scale of strongly agree (5), agree (4), not sure (3), disagree (2) and strongly disagree (1) with five being the highest (Tull and Hawkins, 1993).

Data analysis

The pre-coded data (Likert scale) was entered into Statistical Package for the Social Scientists (SPSS), cleaned to cater for inconsistencies and other data capturing problems like missing data. The data was later subjected to factor analysis, correlation analysis, regression analysis and variance analysis.

The Pearson correlation coefficient was carried out in order to establish the relationship between variables (that is, Corporate Governance, Managerial competency and financial performance. On the other hand, regression analysis was carried out in order to establish the effect of corporate governance and managerial competency on the financial performance of SACCOS in Busoga region.

Table 1. Sample Characteristics

Variable (N=51)	Description	Frequency	Percent
Designation	Accountant	3	5.9
	Manager	32	62.7
	Board member	16	31.4
Sex	Male	28	54.9
	Female	23	45.1
Education level	Certificate	1	2.0
	Diploma	34	66.7
	Degree	15	29.4
	Other	1	2.0
Years SACCO has been in operation	Over 5	1	2.0
	2-5	33	64.7
	Less than 2	17	33.3
Funds pool of the SACCO	More of shareholder capital	18	35.3
	More of debt	33	64.7
Number of Board members	Less than 5	10	19.6
	5-7	41	80.4
Number of employees	Less than 5	30	58.8
	5-10	21	41.2

Source: Primary data

In addition, variance analysis was done in order to establish the variance in the financial performance of SACCOS in Busoga region that is explained by corporate governance and managerial competency. Variance analysis was also carried out to establish how the variance in financial performance is explained by each of the independent variables within the model used. Furthermore, variance analysis helped to establish how the variance with in the independent variables is explained by its own constructs.

Factor analysis was carried out in order to ascertain the outstanding factors of each of the independent variables (Corporate Governance and Managerial competency).In addition, it helped to establish the order of importance of the elements to consider in each of the constructs within the independent variables.

Finally, the analysis was tabulated for easy comprehension by readers of the findings of the study.

FINDINGS

Background characteristics

The background information about SACCOS in Busoga region and the respondents was obtained. The results are shown in table 1. In reference to table 1 above, most of the SACCOS have been in operation between two and five years (64.7%), 2% have operated for more than five years and the rest have operated for less than two years (33.3%).Most of the SACCOS operate using more of debt than equity (64.7%) as compared to 35.3% of those operating with more equity than debt. The results also show that 19.6% of the SACCOS have less than five board members and 80.4% have five to ten board members. As regards to the number of employees, 58.8% have less than five employees and 41.2% have five to ten employees.

Concerning the individual characteristics of the respondents, majority were male (54.9%) as compared to the female (45.1%). More of the respondents were Managers (62.7%), followed by Board members (31.4%) and accountants (5.9%).This implies that the researcher obtained data from the target respondents. Regarding their education level, 66.7% had diploma, 29.4% had degree and 4% had certificate and other qualifications.

Relationships between the variables

In order to understand the relationship between corporate governance, managerial competency and financial performance, correlation analysis was done.

Correlation analysis

Correlation analysis helped to establish the relationship

Table 2. Correlation analysis

Variable	1	2
Managerial competency (1)	.676**	1
Financial performance (2)	.546**	.610**

***Correlation is significant at 1% (2 tailed)*
Source: Primary data

Table 3. Regression analysis

	Un standardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	T	Sig.
Managerial competency	.338	.143	.559	2.354	.023
Dependent Variable: Financial Performance					
R Square	.392		F Statistic	14.141	
Adjusted R Square	.355		Sig. (F Statistic)	.000	

Source: Primary data

between corporate governance, managerial competence and financial performance. The results that were obtained are presented in table 2.

Relationship between managerial competency and financial performance

The same results from table 2 show a positive relationship between managerial competency and financial performance (r =0 .610, p< .01). In essence, an improvement in the managerial competency of the SACCOS in Busoga region is associated with an improvement in their financial performance. Particularly, it implies that an improvement in the skills and knowledge of the Managers for these SACCOS is associated with an improvement in their profitability and portfolio quality. Similarly, a decline in the skills and knowledge of the managers is associated with a decline in the profitability and portfolio quality of these SACCOS.

Regression analysis

In order to establish the extent to which the variance in financial performance of SACCOS in Busoga region is explained by corporate governance and managerial competency, regression analysis was done. Regression analysis also helped to establish the significance of each of the independent variables (corporate governance and managerial competency) on the variance in the financial performance of SACCOS in Busoga region. The results that were obtained are presented in table 3. Results in table 3 indicate that corporate governance and managerial competence only explain 39% (R square= .392) of the variance in the financial performance of the SACCOS in Busoga region. This implies that 61% of the variance in financial performance is explained by other factors outside the model used.

These results further indicate that the regression model was also well specified (F = 14.141, P <.01) .This implies that the outcome from the model are reliable.

Discussion of findings

Relationship between managerial competency and financial performance

The findings indicate that managerial competency and financial performance of SACCOS in Busoga region are significantly positively associated. When the skills and knowledge of these SACCO managers improve, the profitability and portfolio quality significantly improve. As such, if the profitability and portfolio quality of these SACCOS are to improve, emphasis should be put on the skills and knowledge possessed by these managers.

These managers must have the required skills and knowledge to initiate programs that will improve financial performance. They should delegate tasks in a manner that aims at achieving financial targets. In addition, they should have measurement systems which they use to determine when the marginal benefits from a specific program are falling. Besides, they should have viable measurement metrics for making informed decisions about the systems to adopt in order to improve the financial performance of the SACCOS. The finding was in agreement with the study by Kerr & Werther (2008) who found out that the better the managerial competency of the firm, the better will be its financial performance. The findings from this study disagreed with those of Cetin (2010) who found a weak relationship between managerial competency and financial performance.

It is also important to note that where as prior studies by Veres, Locklear & Sims, (1990) and Keel (2006) identified skills, knowledge, abilities and personal traits as attributes that make up managerial competency, this research study finds only skills and knowledge as the significant factors to consider in the managerial competency of SACCOS in Busoga region.

CONCLUSION AND RECOMMENDATIONS

Managerial competency has proven to be significantly positively related to the financial performance of the SACCOS in Busoga region. It is imperative for all those charged with the policy direction of those SACCOS to give it the weight it deserves. The outstanding factors for managerial competency are skills and knowledge. Knowledge and skill gaps for existing managers within these SACCOS need be identified .Thereafter; necessary training and development must be done to bridge these gaps.

Similarly, while recruiting new managers for these SACCOS, it is important that their skills and knowledge about SACCO business take priority.

RECOMMENDATIONS

Since managerial competency of SACCOS in Busoga region is significantly positively associated with their financial performance, all effort should be made to strengthen. For example the Board performance, transparency and Board composition of these SACCOS should strengthen so that the skills and knowledge of the SACCO managers are enhanced.

The skill and knowledge gaps among managers of the SACCOS in Busoga region need be identified. This should be followed by the necessary training and development programs in order to bridge these gaps. This will help to improve the financial performance of these SACCOS. Skills and knowledge must take top priority in recruitment of new managers for the SACCOS in Busoga region. An assessment tool should be developed in line with the skills and knowledge elements as identified in table 4.2.This will help in getting the appropriate candidates to fill any future job opportunities among the SACCOS.

Further studies should be done to establish the factors that explain 63% of the variance in the financial performance of SACCOS in Busoga region. This is because it is important that all the factors affecting the financial performance of these SACCOS are addressed together in order to improve their financial performance.

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