Relationship between cost of credit and financial performance of manufacturing firms listed in the Nairobi stock exchange

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Abstract: The study analyzed empirically the relationship between the cost of credit and the financial performance of Kenya manufacturing firms quoted in the Nairobi Stock Exchange and the consequent level of impact to their overall financial position. The study used a survey of the firms as well as the firms final accounts and balance sheets of the five years period. The result of the study showed a correlation between the cost of credit and the financial performance of the firms as regards firms borrowing. In the overall, however, the study revealed that there are no relationship between the cost of credit and financial performance of manufacturing firms under normal circumstances. It also revealed that interest rate contributes the highest percentage of the cost of credit. On individual firm basis, the study indicated that the impact of the cost of credit varies from one firm to another. It further showed that the level of borrowing significantly affected the percentage cost of credit. However, the type of credit undertaken by the firms determined the cost of credit with bank borrowing taking the greatest share. Basically, all firms used trade credit to substitute their level of borrowings. The study was limited in getting responses from all the targeted respondents. Access to financial information for the entire period of study in all the firms and measurement of the cost of credit acted as additional limitations. The study recommended reduction of interest rates across the board relaxation of lending requirements by the financial institutions as well as strengthening of regulatory and legal systems in relation to lending and borrowing. The study, therefore, underscore the need to formulate a prudent credit policy for individual firms as well as the need for a conducive macro and micro economic environment in an attempt to synchronize the benefits of using credit facilities and also facilitate the financial mobilization of firms, so that their optimum contribution to economic development can be achieved.