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Research Article

Effect of Risk Management Practices on Financial Performance of Dairy Cooperative Societies in Meru County, Kenya

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Abstract: Risk management practices are one of the most important and challenging issues in performance of Dairy Societies in Kenya. Making sure Dairy Cooperative Societies develop, manage and implement a risk management system is essential in streamlining the societies operations and minimizing unnecessary financial leakages due to the effects of various risks. Lack of a homegrown and internally developed risk management system that suits the operations of the societies hampers the financial performance of Dairy Cooperative Societies. The study was restricted to investigating the effect of risk management practices on the performance of Dairy Cooperative Societies in Meru County, Kenya. The specific objective of the study was to establish the effect of risk management practices on the financial performance of Dairy Cooperative Societies. The study resorted to a census of all the 72 Secretary Managers of the Dairy Cooperative Societies in Meru County, whereas data was collected using a questionnaire. The descriptive research design was adopted for this study. The response rate was 88.88 per cent, while the coefficient of determination indicated that the independent variable contributed to 67.9 per cent of the variability in financial performance of Dairy Cooperative Societies as explained by R^2. After running the regression model it was established that the p-value and regression coefficients generated was as ($\beta = 0.521$ $p = 0.042$). This indicated that risk management practices had a positive and significant effect on financial performance of Dairy Cooperative Societies in Meru County, Kenya.

Keywords: Risk Management Practices, Contingency Plans, Policies and Regulations, Monitoring, Financial Performance.

BACKGROUND OF THE STUDY

Risk management is a key factor for consideration whenever decisions are being made on improving productivity and performance of the organization. The dynamic changes within the environment of operation has led organizations to develop proper mechanisms for risk control to mitigate against unplanned occurrences (Mwangi, 2014; Beckmann, 2007). The dynamic environment demands prior planning that includes mitigation of risks through implementation of risk management practices, such that organization takes the risks consciously and in a planned manner ensuring that there are no surprises from the environment and the competitors (Ebenezer and Omar, 2016).

Historically the financial sector in Kenya has always been subjected to various major risks, the careful management or rescue by the government has led to the survival of the financial sector. Many Kenyan Cooperative societies and commercial banks handle risks on a day to day basis with most of the commercial banks setting up a department to deal with risks emanating from their interactions in the finance industry. Therefore risks must be understood, prioritized for the role they play in the decision making of the financial and non-financial sectors in Kenya.

According to Ruparelia and Njuguna (2018) corporate governance principles like risk management contributes to an organization's confidence, image and reputation in the market. It contributes to an organizations ability to undertake various programs and activities due to contingency plans, monitoring and evaluation programs and policies ingrained in the organization process thus enhancing its compliance with the pertinent laws and regulations thus improving the organization's performance in the market. Despite these advantages the subject of risk management in relation to financial performance of Dairy Cooperative Societies is not well emphasized in most organizations (Kihumba, 2017).

The definition and measures for financial performance adopted by this study falls close to the one given by Bourguignon (1997) and Mohan and Chadramohan (2018) who looks at performance in three dimensions; performance as success, as a process and as an action. This implies the need of not only incorporating the target or goal setting but also of the process and the activities undertaken to accomplish the set goals. This is in cognizant to the environment in which a dairy cooperative operates in and its structure, where members come together with clear defined goals that need to be met, then there are processes that may be defined as the rules, regulations and procedures that need to be adhered to and which either fuels or inhibits the activities of the organization. And in keeping with the words of Drucker (1999) to assess performance, measurements like quality of service, customer's satisfaction, flexibility of processes, innovation and utilization of resources should be taken into consideration.

Statement of the Problem

The performance of financial and non-financial organizations has not been at optimum recently. This calls for reviewed approach on the management of risks in organizations (Mohammed & Onyiego, 2018). Losses related to member cooperative societies is not a new phenomenon in the industry and much is associated to the risk management systems implemented by the management of these societies. Dairy Cooperative Societies require adequate and reliable risk management systems and measures to manage any inherent risk that may arise in conducting their businesses. Therefore a mechanism for monitoring and planning is required to project future areas and processes that maybe affected by risks (Mwangi, 2014).

There a limited number of local studies on risk management and financial management of cooperative, with the most of the studies focusing on the commercial banks. Majority of the studies have focused on credit risk management, liquidity risk management and financial risk management (Mwangi, 2014; Mohammed & Onyiego, 2018; Harelimana, 2017). Simiyu (2008) and Ngare (2008) studied the effect of credit risk management in commercial banks. Muteti (2014) focused on the financial risk management practices in the finance industry while Mwangi (2014) focused on the relationship between risk management and financial performance of commercial banks in Kenya.

While the above studies provide insightful analysis on the effect of various forms of risk on performance of commercial banks in Kenya, there is no known study to the best of our knowledge that has been carried out on the effect of risk management on financial performance of Dairy Cooperative Societies in Meru County. This study therefore sought to fill this gap by answering the question, what is the effect of risk management practices on financial performance of Dairy Cooperative Societies in Meru County, Kenya?

Study's Objectives

The study was guided by the following objective;

i. To investigate the effect of risk management on the financial performance of dairy cooperative societies

This study is premised on the Stewardship theory. The major proponents of Stewardship theory were Davis, Schoorman and Donaldson in 1997. The theory is premised on the assumptions of trust, reputation, collective goals and involvement. There is an assumption that collectivism is preferred in place of individualism thus pro-organizational goals taking precedence to individual goals (Subramanian, 2018). According to Davis, Schoorman and Donaldson (2007) Stewardship theory ''defines situations in which managers are not motivated by individual goals, but rather are stewards whose motives are aligned with the objectives of their principals''.

Other proponents of stewardship theory posit that the organization is supposed to fulfill a greater calling of serving not only the shareholders, employees and customers but also the community (Karns, 2011). This means that the business main reason for existence is to serve and for it to fulfill this it has to remain economically sound. This implies that the management doesn't only drive the business towards profitability for the sake of shareholders but also for the community that is the existence of the business should be a win-win situation for all stakeholders. The Dairy Cooperative Societies are managed by agents on behalf of the shareholders. The management stewards the Societies towards the core goals of cooperatives which is prosperity through togetherness. The theory is further linked to the risk management practices of the societies as the management in conjunction with the board of directors are supposed to implement risk management system that safeguards the shareholders investments. Therefore this theory tends to shed light on the risk management practices within the organization and the risk management processes applied.

Mwangi (2014) in his study on the relationship between risk management and performance of commercial banks in Kenya established a positive and significant effect between risk management and financial performance. This study by Mwangi established that the risk management could be accounted for by the credit risk, in solvency risk, size of the bank and the operational efficiency. The study also states that the macro-economic factors also inhibit the risk management of an organization and should be taken into consideration when planning on risk mitigation activities within the organization. The study made use of descriptive research design and data was analyzed using both the descriptive and inferential statistics. The results by Mwangi (2014) are true to the extent that the organization has an established risk management system, risk management strategy and professionals who oversees the application of control mechanisms to mitigate against devastating organizational risk. Beside the risk management variable there were other independent variables like board size, capital adequacy and operating efficiency. The risk management variable was represented by the elements; credit risk, insolvency risk and interest risk and it was established that a unitary increase in either of these risks would lead to financial losses by the commercial banks under study (Mwangi, 2014).

The study by Wanjohi, Wanjohi and Ndambiri (2017) confirms the results of the study conducted by Mwangi (2014) where they established that risk management had a positive and significant effect on financial performance of banks in Kenya. The study by Wanjohi *et al,* (2017) made use of descriptive research design and data was collected from 43 commercial banks and one Mortgage Company in Kenya. The questionnaire were self-administered to the management of the banks to collect data pertaining to risk management while data on financial bank was accessed from the Central Bank of Kenya on performance of Banks as it was secondary data. This study established that majority of the banks were practicing good risk management practices and it also recommends the application of newer techniques for risk measurement like simulation techniques, risk adjusted techniques and value at risk.

RESEARCH DESIGN

The Conceptual Framework of the Study

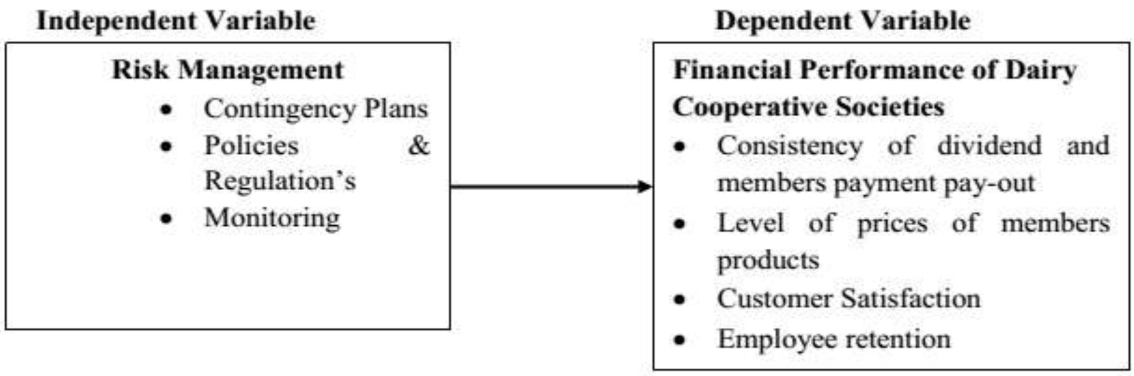

Figure 1: Conceptual Framework

RESEARCH METHODOLOGY

The purpose of this study was to investigate the effect of risk management practices on the financial performance of Dairy Cooperative Societies in Meru County. The study adopted the descriptive research design as its capable of describing the relationship between the independent and the dependent variable. It is also able to describe the phenomenon surrounding the interaction of the variables of the study. The target population of the study was the Secretary Managers in-charge of decision making in the Dairy Cooperative Societies. Due to the size of population the study resorted to a census where all the 72 Secretary Managers of the Dairy Cooperative Societies were administered with a questionnaire. Both the descriptive and inferential statistics were utilised to analyse the data collected through the structured questionnaire.

STUDY'S RESULTS

The study distributed 72 questionnaires to the ear marked respondents. After collecting and reviewing the filled questionnaires only 64 of them were found to meet the set standards for data analysis. The returned questionnaires represented an 88.8 per cent response rate which is within the recommendations of Mugenda and Mugenda (2008) who argued that a response rate of 60 per cent is adequate for inferential analysis. The gender were represented as follows; male 26.6 per cent and female 73.4 per cent. The work experience of the respondents was also tested and analyzed and established that 30 per cent of the respondents had more than 5 years of experience while 70 per cent of total respondents had less than 5 years of experience. Majority of the respondents were found to have had more than college diploma qualifications.

The reliability of the study instrument was established by the use of Cronbach Alpha Test. The analysis indicated that the Cronbach Alpha coefficient was 0.81 which was more than 0.5 as per Cooper and Schindler (2013) argument. The relationship between the constructs was measured by using Pearson's correlation analysis. The relationship between risk management practices and financial performance was at $r = 0.345$, $p < 0.01$.

The study sought to establish the contribution of the independent variable risk management practices on financial performance of Dairy Cooperative Societies in Meru County. The regression model is summarized as below;

Table 1.1 Regression Model Results

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.824[a]	.679	.576	.545	2.02

a. Predictors: (Constant), Risk Management Practices

b. Dependent Variable: Financial Performance

The Table 1.2 below indicates the effect of the independent variable (risk management) on the dependent variable (Financial Performance). The Table 1.2 indicates the results of the simple regression analysis. The results shows a positive and significant effect on the relationship between internal controls and financial performance of Dairy Cooperative Societies (β=0.042, $p< 0.05$). This means that an increase of 0.521 on risk management practices would lead to a unit increase on financial performance of Dairy Cooperative Societies.

Table 1.2 Regression Size of Effects

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
(Constant)	1.431	0.523		3.745	.000
Risk Management Practices	.521	.256	.622	2.142	.042

a. Dependent Variable: Financial Performance

Conclusion and Recommendations

The study determined the influence of risk management on the financial performance of Dairy Cooperative Societies in Meru County. It was established that risk management had a positive and significant effect on the financial performance of the societies. The regression coefficient of risk management stood at 0.521 which is statistically significant as the p-value is 0.042 which is less than 0.05.This therefore indicates that a unit increase in risk management results to a 0.521 increase in financial performance of Dairy Cooperative Societies in Meru County. When the questionnaire was administered to the Board members the majority of them were not aware of the implementation of a risk management system to their societies.

The study concludes that risk management practices are a major influence to the financial performance of dairy cooperative societies in Meru County. The multiple regression results show that risk management had a significant effect of 0.521 on financial performance of cooperative societies. It therefore indicates that risk management practices like; monitoring and evaluation, policies and regulations influenced the performance of the dairy societies. The development of workable policies and procedures contributes to mitigation of unforeseen risks thus improving the performance of the organization.

The study recommends that the board members should be made aware of the contents of the existing risk management plans. This would improve their ability to internalize the role that these plans and systems play and would help them in making decisions that improve the existence and the stability of the societies. The contribution of risk management towards financial performance of the societies should be well pronounced to the management and the board of the societies. This would clearly ensure that the right systems have been put into place.

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