

# Financial Capability and Competitiveness of Local Pharmaceutical Manufacturing Firms in Kenya

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## Abstract

This study was carried out to establish the influence of financial capability on competitiveness of local pharmaceutical manufacturing firms in Kenya. The study used both descriptive and explanatory research designs. The population for this census study was all the 31 local manufacturing pharmaceutical firms in Kenya. The CEOs or managing directors, finance, human resource, marketing, operations and quality compliance managers were the target respondents. Primary data was collected using questionnaires. Descriptive and inferential statistics were conducted. Results showed that respondents agreed that financial capability had an influence on competitiveness of local pharmaceutical manufacturing firms in Kenya. The study concluded that financial capability influenced competitiveness of pharmaceutical manufacturing firms in Kenya. the study recommends management of pharmaceutical manufacturing firms to forecast the firms' income and expenditure, monitor emerging financial patterns and capital expenditure.

**Keywords:** Financial Capability, Manufacturing Pharmaceutical Firms, Kenya

## Introduction

### Background of the Study

A financially capable organization is better positioned to invest in research and development, technological advancements, and employee training—all of which contribute to enhanced competitiveness (Alimin et al., 2012). Adequate financial resources enable a company to fund innovation, improve operational efficiency, and seize strategic opportunities in the market. This financial strength allows organizations to weather economic downturns, adapt to changing market conditions, and make necessary long-term investments (Yildirim et al., 2019). The nexus between competitiveness and financial capability underscores the

importance of a balanced and strategic approach to financial management. Organizations that effectively manage their finances are better equipped to innovate, adapt, and compete in dynamic business landscapes, ultimately fostering long-term success and resilience (Roman et al., 2012).

Financial capability encompasses an organization's financial health, resources, and strategic financial management and plays a critical role in the success and sustainability of pharmaceutical manufacturing firms (Abubakar, 2015). In the pharmaceutical manufacturing sector, significant investments are required for the discovery, development, and manufacturing of drugs. These processes demand state-of-the-art facilities, advanced technologies, and skilled personnel, all of which incur substantial costs and thus, financial capability enables firms to make these investments, ensuring the quality, safety, and efficacy of their products (Imbambi et al., 2020).

### **Statement of the Problem**

When Covid 19 pandemic hit the country, reliance on global supply chain for some medical supplies prevented timely and effective response (Raj et al., 2022). This created the need to strengthen and expand local production of medical and pharmaceutical products in Kenya. There are serious challenges that manufacturing in Africa comes with like significant cost involved in the appropriate development of new products (JICA, 2013). Pharmaceutical manufacturing firms need to have a clear structure of their competitive resources and strategic capabilities that are not imitable or transferable easily to other competitors. Development of the strategic capabilities is useful to the organizations in sustaining their business and achieving better performance which is a challenge to most local pharmaceutical manufacturing firms. According to Wanjiku (2017), possessing strategic capabilities enables an organization to directly improve the value it is offering to the market or customers through their products or services resulting from possession of core competencies. Chepkole and Deya (2019) established that financial capability had a positive and significant influence on competitive advantage of IT Firms in Nairobi City County. This shows the interest in the influence of financial capability on competitiveness of pharmaceutical manufacturing firms in Kenya.

Empirical studies have shown mixed results on the influence of financial capability and competitiveness of organizations. In their study, Fonseka et al (2014) on the effect of financial capability on competitiveness and sustainability of organizations in Chinese markets found a positive relationship with organizational competitiveness. Chepkole and Deya (2019) established the impact of financial capability on competitiveness of IT firms in Nairobi City County and found out that financial capability had a positive and significant influence on competitiveness of IT firms. These studies have been carried out in different contexts and may not be generalized to a Kenyan context. The current study therefore sought to fill these gaps by establishing influence of financial capability on competitiveness of local pharmaceutical manufacturing firms in Kenya

### **Objective of the Study**

To establish the influence of financial capability on competitiveness of local pharmaceutical manufacturing firms in Kenya

### Research Hypothesis

The study sought to test the following null hypothesis:

**H<sub>01</sub>:** There is no significant influence of financial capability on competitiveness of local pharmaceutical manufacturing firms in Kenya

### Literature Review

#### Theoretical Review

The Pecking Order Theory (POT) was proposed by Myers (1997) and it opines that a firm initially tries to use its internally generated financing sources before issuing debt and later issuing equity as the last resort (Lemmon & Zender, 2009). The theory explains the financial decision making in an organization and further explicates that the lopsided particulars (data) on the notion that benefits accrued from outside financing with respect to trade-off theory and the costs linked with it are much less compared to financing from within. Organizations that are profitable are most likely to have more retained earnings (Kayo et al., 2010).

In reference to using various financing instruments, this theory gives a preferential order. Transaction costs are a key component regarding making of decisions concerning capital structure in organizations (Mazur, 2007). In most organizations, internal financing transaction costs are lower compared to external financing transaction costs. Equity according to this theory is a less preferred method of raising capital since the assumption is that managers have better understanding of the organization and the market than the investors' issue of new equity. The perfect order should therefore be to exhaust retained earnings before issuing debt and later issuing equity as the last resort. Applying debt raises the variance of earnings which translates to investors asking for greater returns after making their investments. Organizations thus should seek capital structure that capitalizes on tax benefits from using more debt while lessening the likelihood and prospects of bankruptcy costs. Organizations have an advantage of using debt rather than internal capital for them to enjoy shields benefits from debt tax. Less tax is paid by organizations in stances where debt capital is used instead of retained earnings since the tax shield allows it. Based on the theory, the value of an organization is created when they have more debts.

Lemmon and Zender (2009) argued that one aspect of this theory is that organizations that are profitable always opt for internal financing rather than taking new debts or issuing equity. Further, Sen, Bhattacharya and Korschun (2006) acknowledged that sustainable or stable debt financing is not there and thus a soberer financing method in the financial system is required. There are particular costs linked with both debt and equity. When referring to this theory, local pharmaceutical manufacturing firms in Kenya can opt for a particular financing order of retaining earnings, debt or equity in their financial structure that can enhance their performance financially. When the local pharmaceutical manufacturing firms opt for external financing, payment of interest that is linked with the use of debt capital is accrued which depends on the interest rate settled.

### Conceptual Framework

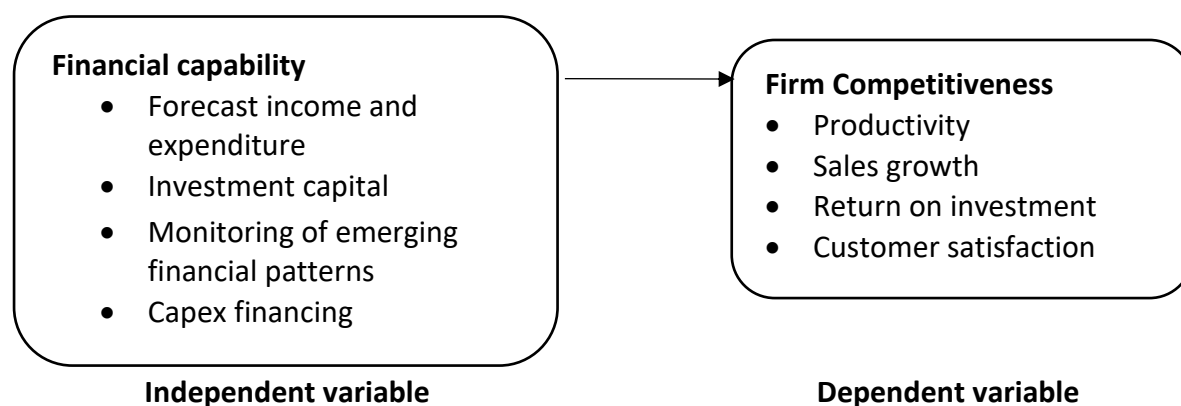


Figure 1: Conceptual Framework

### Empirical literature

Fonseka et al (2014) studied the effect of financial capability on competitiveness and sustainability of organizations in Chinese markets. Data was obtained from 4,530 observations in a firm and hierarchical regressions conducted. Results showed that comparing internal financial and external financial capabilities, internal financial capabilities did not provide a significant benefit. Further, financial capabilities in raising capital from the available shareholders, the public and easy access to financing from banks had a positive relationship with organizational competitiveness.

A research aimed at assessing correlation between financial capability and competitiveness of medium and large manufacturing enterprises in Rwanda was carried out by Claude (2018). The research used both correlation and regression analysis technique. The research design employed was survey. One hundred and twenty-five (125) middle managers from the medium and large manufacturing enterprises were targeted. The data collected were analyzed using SPSS. The findings showed a significant positive influence of financial capability towards organizational competitiveness.

Chepkole and Deya (2019) established the impact of financial capability on competitiveness of IT firms in Nairobi City County. One hundred and forty-three (143) owners of IT firms in Nairobi City County were targeted and census survey design adopted. Primary data collection was done using questionnaires. Financial capability was found to have a positive and significant influence on competitiveness of IT firms.

A study seeking to examine the impact of financial capability for competitiveness in the banking industry in Kenya was carried out by Wamburu (2017). Data was drawn from 129 respondents from the senior management of the 43 commercial banks in Kenya. Primary data was obtained from top, middle and lower level managers of the commercial banks using semi-structured questionnaires. The collected data was analyzed descriptively. Results showed that a strong correlation between competitive advantage and financial capability in commercial banks in Kenya.

### Methodology

The study used was census survey design. This design was significant as it helped in getting data that shaped the basis for more research in the subject of competitiveness of firms. It was a census study targeted all the 31 local manufacturing pharmaceutical firms in Kenya. The CEOs or managing directors, finance, human resource, marketing, operations and quality

compliance managers were the target respondents. Questionnaires were used in data collection. Data analysis was done using Statistical Software for Social Sciences (SPSS) where both descriptive and inferential statistics were conducted.

## Research Findings and Discussions

### Response Rate

Out of the 31 pharmaceutical manufacturing firms in Kenya, 22 of them participated in the study. In majority of the pharmaceutical manufacturing firms, results show that the 6 respondents that were targeted responded and filled the questionnaires. Out of a total of 186 questionnaires that were expected, 127 returned fully filled implying a response rate of 68.2%. Nine pharmaceutical manufacturing firms in Kenya did not participate in the study

### Descriptive Statistics on Financial Capability

The study sought to determine the impact of financial capability on the competitiveness of manufacturing firms in Kenya. Results in Table 1 indicates that 75.6% of the respondents strongly agreed with the position that forecasting on the income and expenditure is done to identify trends that have an effect on the firm's competitiveness (24.4% agreed) and had the highest mean of 4.76 and a standard deviation (SD) of 0.43. Results also show that 97.6% agreed that their firm monitors emerging financial patterns to maintain its competitiveness, had a mean of 4.52 and a standard deviation of 0.55. 85.8% of respondents agreed that high capital expenditure financing positively impacts competitiveness of their firm. The mean was 4.32 and had a standard deviation of 0.84.

Table 1

*Level of agreement with statements on financial capability*

Financial capability	Frequency and Percentages					Mean	SD
	SD	D	N	A	SA		
Forecasting on the income and expenditure is done to identify trends that have an effect on the firm competitiveness				31 24.4%	96 75.6%	4.76	0.43
The firm monitors emerging financial patterns to maintain its competitiveness			3 2.4%	55 43.3%	69 54.3%	4.52	0.55
High capital expenditure financing positively impacts competitiveness of the firm	1 0.8%	4 3.1%	13 10.2%	44 34.6%	65 51.2%	4.32	0.84
<b>Aggregate Mean</b>						<b>4.53</b>	<b>0.61</b>

SD= strongly disagree; D= disagree; N= neither agree nor disagree; A= agree; SA= strongly agree

### Financial capability and competitiveness of pharmaceutical manufacturing firms

**H<sub>01</sub>:** There is no significant influence of financial capability on competitiveness of local pharmaceutical manufacturing firms in Kenya

Regression analysis was carried out to determine the influence of financial capability on the competitiveness of manufacturing firms in Kenya. The linear regression model analysis results

are shown in form of model summary, ANOVA test and regression coefficients. The model summary showed that the coefficient of determination (R square) of 0.323 indicated that the model explained only 32.3% of the variation or change in the dependent variable, with the remainder of 67.7% being explained by other factors other than financial capability as shown in Table 2. The results on the Analysis of Variance (ANOVA) are presented in Table 3. The results with a p-value of 0.005 being less than 0.05, indicates that the model is statistically significant in explaining the relationship between financial capability and competitiveness of pharmaceutical manufacturing firms in Kenya.

The regression coefficients shown in Table 4 indicates that a constant (p-value = 0.000) of 1.721 and a gradient coefficient of 0.058 which indicated the extent to which a unit change in financial capability causes a change in competitiveness of the pharmaceutical manufacturing firms. Financial capability was significant (p-value = 0.018) in positively influencing the competitiveness of pharmaceutical manufacturing firms in Kenya.

Therefore, the financial capability and competitiveness model can now be presented as:

$$Y = 1.721 + 0.058 X_1 + \varepsilon$$

Table 2

*Model Summary*

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.453 <sup>a</sup>	.323	.316	.37248

a. Predictors: (Constant), financial capability

Table 3

*ANOVA*

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	0.417	1	0.417	3.006	.005 <sup>b</sup>
	Residual	17.343	125	0.139		
	Total	17.760	126			

Dependent Variable: Competitiveness

Predictors: (Constant), Financial capability

Table 4

*Regression Model Coefficients*

	Unstandardized Coefficients		Standardized Coefficients		Sig.
	B	Std. Error	Beta	t	
(Constant)	1.721	.324		5.315	.000
Financial capability	.058	.058	.453	1.002	.018

a. Dependent Variable: Competitiveness

### Discussion of Findings

From the results of the descriptive analysis, most of the respondents strongly agreed that forecasting on the income and expenditure is done to identify trends that have an effect on

the firm's competitiveness (75.6%). Forecasting helps organizations develop comprehensive financial plans by estimating future income and expenditure. It provides insights into the financial resources available, allowing organizations to allocate funds appropriately and set realistic goals. Further, forecasts assist in making informed decisions related to investments, expansion, and resource allocation. By projecting future income and expenditure, organizations can evaluate the potential influence of these decisions on their financial position and assess their feasibility. Understanding emerging financial patterns gives organizations a competitive edge. It enables them to differentiate themselves from competitors by being early adopters of innovative financial practices or by capitalizing on emerging market segments. By identifying new revenue streams, cost-saving opportunities, or efficiency improvements, firms can position themselves ahead of the competition and enhance their overall market position. Monitoring emerging financial patterns helps organizations identify and mitigate risks. It allows them to recognize potential financial threats, such as market downturns, currency fluctuations, or changing consumer preferences, and develop strategies to mitigate their impact. Capital expenditure financing allows organizations to invest in critical infrastructure, such as production facilities, distribution networks, and information technology systems. The inferential analysis of the study model revealed that financial capability had significant and positive influence on the competitiveness of pharmaceutical manufacturing firms in Kenya

## **Conclusion and Recommendations**

### **Conclusions of the Study**

The study concluded that financial capability influenced competitiveness of pharmaceutical manufacturing firms in Kenya. Pharmaceutical firms need financial resources to launch new products, conduct market research, establish distribution networks, and promote their products. Expansion into new geographical markets or therapeutic areas often requires significant upfront investments. Strong financial capability enables firms to pursue growth opportunities and gain a competitive edge. The study also showed that financial capability is significantly related to competitiveness of pharmaceutical manufacturing firms.

This study makes theoretical contributions by bridging gaps in existing literature since it examined the effect of forecast income and expenditure, investment capital, monitoring of emerging financial patterns and capex financing on competitiveness of pharmaceutical manufacturing firms. The contextual significance lies in its direct relevance to Kenya's pharmaceutical industry, providing insights that informs policy interventions and strategic business decisions. By exploring the interplay between financial capability and competitiveness, the study offers a nuanced understanding of the industry's dynamics, potentially aiding the development of targeted measures to enhance the resilience and growth of local pharmaceutical manufacturers in the Kenyan context.

### **Recommendations of the Study**

The study recommends management of pharmaceutical manufacturing firms to forecast the firm's income and expenditure, monitor emerging financial patterns and capital expenditure. Forecasting allows pharmaceutical manufacturers to identify potential risks and uncertainties in their income and expenditure. By considering various scenarios and market conditions, the firms can assess the potential influence of external factors such as changes in regulations, market competition and pricing pressures. Cost of equipment, machinery, critical infrastructure such as production facilities, distribution networks, and information



technology systems can be properly reviewed before purchase. This helps them develop risk mitigation strategies, such as diversifying their product portfolio, exploring new markets, or adjusting pricing and cost structures.

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