INVESTMENT PLANNING PRACTICES AND FINANCIAL PERFORMANCE OF MICRO RETAIL ENTERPRISES IN BUNGOMA TOWN, KENYA

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ABSTRACT

Investment planning enables the investor to hold an optimum portfolio based on costs, benefits and risks which are fundamental in maximization of return on investment. The retail business environment in Kenya is risky and uncertain, characterized by an ever changing competitive environment and fluctuation of factors which influence retail demand such as taxation and inflation rates. This adversely affects financial performance of micro retail enterprises. This study was conducted in order to determine the relationship between investment planning practices and financial performance of micro retail enterprises in Bungoma town, Kenya. The influence of portfolio diversification on financial performance of micro retail enterprises was assessed. This study was founded on modern portfolio theory. Descriptive survey research design was used. A total of 1912 registered micro retail enterprises in Bungoma town comprised the study population. A sample of 331 micro retail enterprises was involved in the study. Simple random sampling was used to select micro retail enterprises for the actual study. A pilot study was conducted in order to test the reliability of the research questionnaire. Content validity of the research instrument was ensured by consulting the university supervisor while reliability was tested using Cronbach's alpha coefficient. Self-administered questionnaires and secondary data sheets were used to collect data. Both descriptive and inferential statistics were used for data analysis. Descriptive statistical tools included frequencies, percentages, means, variances and standard deviations. Inferential statistics included Pearson's Product Moment Correlation and multiple regression analysis. Findings were presented in tables, charts and graphs. This study found out that portfolio diversification positively and significantly influences financial performance of micro retail enterprises ($b1 = 0.217$; $p < 0.05$). It was concluded that if managers/owners increase the variety of asset classes in their portfolios financial performance of micro retail enterprises could be enhanced. The study recommended that investors and organizational policy makers in micro retail enterprises should diversify their portfolios in order to enhance financial performance. It was also recommended that the principles of modern portfolio should be applied in investment planning process. Also, financial advisors and consultants should prioritize strategic asset allocation and systematic portfolio construction for micro retail enterprises. The government should also organize seminars on basic investment planning skills for managers/owners of micro retail enterprises. Suggestions for further research were also made. It is expected that such initiatives will promote economic development.

Key Words: *financial performance, micro retail enterprises, portfolio diversification, strategic asset allocation, mean-variance optimization*

INTRODUCTION

Investment planning involves identification of financial goals, determination of investment time horizon, understanding of risk appetite, determination of investment strategy, identification of investment avenues, determination of investment portfolio, portfolio evaluation and portfolio revision (Mangalam & Kapoor, 2014). Investment planning is a process that involves six steps namely; setting of investment goals, understanding of

investment personality, designing an investment portfolio, selecting specific investments, managing and monitoring the portfolio and rebalancing or redesigning the portfolio (Broadridge Investor Communication Solutions Incorporation, 2013).

Portfolio diversification refers to investment of funds in a variety of asset classes. Diversification within asset classes aims at reducing exposure to risks associated with a particular company, sector or market segment (Donaldson, Bruno, Walker, Schlanger, & Kinniry, 2013). Retailers can diversify by adopting related or unrelated retail formats (Cossin, 2008). The time horizon and the need, ability and willingness to take risk are vital in choosing the appropriate asset allocation (Economywatch, 2010). Strategic asset allocation involves the determination of long-term target allocations to investable asset classes. Harry Markowitz's mean-variance optimization (MVO) is the most widely used quantitative strategic asset allocation framework (Idzorek, 2006). Allocation of funds to real assets in a portfolio is a great tool of diversification as they have lower correlation with equity-like asset classes and preserve value during inflation (Mercer Limited Liability Company [LLC], 2014). Risk budgeting arrives at risk exposures expressed in terms of value-at-risk or percentage contributions to risk rather than asset weights in portfolio construction (Meketa Investment Group, 2010).

Financial measures are generally accepted in assessment of retail business success because they are objective (Panigyrakis & Theodoridis, 2009). In financial analysis, the measures that determine a firm's financial performance are grouped into four categories namely; profitability, efficiency, leverage and liquidity. Profitability ratios measure the firm's return on its investments. Efficiency ratios measure how intensively the firm is using its assets. Leverage ratios measure the indebtedness of the firm. Liquidity ratios measure how easily the firm can obtain cash (Brealey, Myers & Allen, 2011). The retail sector in Kenya is ailing despite its significant role in the economy of Kenya. Inflation rates have hit hard on both buyers and sellers. Micro retail enterprises have always ended up not reporting any profits at all unless they raise their prices (Juma, 2016). Changing tax rates and currency depreciation poses challenges as retailers have to adjust prices, ensuring retail demand is not negatively affected. For example, the introduction of the Excise Bill in June 2015 increased taxes on products such as beer, cigarettes, juices and bottled water (Oxford Business Group, 2015).

In Germany, micro retail enterprises diversify into both grocery and non-grocery retailing in order to ensure stable growth and financial performance. Drugstores are increasingly offering grocery products. Pure play internet retailers also diversify geographically by opening physical outlets to increase sales in the midst of strong competition (Euromonitor International, 2016b). In Malaysia, retailers diversify and rebalance their product portfolios amidst changing consumer needs, with preference for international brands growing. This assists them to avoid decline in financial performance in the competitive retail business environment (Euromonitor International, 2017a). In Thailand, retailers diversify their portfolios in order to enhance performance. They increase their outlets and include service offerings, although the concept of online retailing tends to limit geographical expansion (Euromonitor International, 2017b).

Portfolio diversification among micro retail enterprises in South Africa is a key determinant of financial performance. Retailers diversify the range of products offered and increase retailing channels in order to remain competitive and accommodate consumers with low purchasing power. Grocery retailers offer a wide range of non-grocery products in order to enhance value sales. This led to positive overall sales in 2015 when there was rising inflation and currency depreciation in South Africa (Euromonitor International, 2016f). In Morocco, retailers diversify their product portfolios and expand by establishing additional retail channels. This enhances financial performance amidst strong competition and reduced consumer purchasing power due to rising inflation and currency depreciation (Euromonitor International, 2016d). In Algeria, micro retail enterprises diversify by increasing the range of products offered. This enables them to sustain and improve financial performance in the midst of competition from modern retail chains that are highly expanding (Euromonitor International, 2016a). In Nigeria, micro retail enterprises diversify their product portfolio amidst competition from international players. Grocery retailers increase the stock and range of non-grocery items in order to enhance value sales (Euromonitor International, 2016e).

Diversification is the main strategy employed to enhance financial performance of micro retail enterprises in the Kenyan retailing market which has seen massive penetration by international retailers. Portfolio diversification through offering related and unrelated products is employed by micro retail enterprises in order to curb increased competition. Grocery retailers widen their portfolios by opening non-grocery retail shops, hence increasing sales revenues in non-core business segments (Euromonitor International, 2016c). Micro retail enterprises in Nairobi diversify their product portfolio and increase service offerings in order to counter intense competition and improve financial performance. Product portfolio diversification aims to satisfy customer needs and offer competitive advantage. Geographic diversification by strategically locating businesses close to customers also enhances success of micro retail enterprises (Bowen, Morara & Mureithi, 2009).

STATEMENT OF THE PROBLEM

Investment planning enables investors to achieve an optimum portfolio based on costs, benefits and risks which are fundamental in maximization of return on investment (Powerplan, 2016). Despite Kenyan retail sector growing strongly as evidenced by expansion of modern retail chains and shopping malls, financial performance of a number of micro retail enterprises is poor. 2.2 million micro, small and medium establishments (MSMEs) were shut down in Kenya between 2012 and 2016, majority being in retail sector. 92.2% of 50,000 sampled licensed MSMEs were micro establishments, indicating high closure of micro retail enterprises (Kenya National Bureau of Statistics [KNBS], 2016). The retail business environment in Kenya is risky and uncertain, characterized by an ever changing competitive environment and fluctuation of factors which influence retail demand such as taxation and inflation rates. This adversely affects financial performance of micro retail enterprises (The Economist Group, 2013). The short-term effects of this problem are loss of market share, slow growth, financial distress and exit of retailers from the market. In the long run, economic growth and development will be negatively affected as the retail sector is a key pillar to the economy of Kenya (Juma, 2016). A number of studies conducted show that the

investment planning practices adopted by retailers determines their performance. Oh, Sohl and Rugman (2014) from Germany analysed regional and product diversification of European retail multinationals. Sohl, Rudolah and Muller-Stewens (2012) from Germany investigated dimensions and performance implications of diversification strategies in the global retailing industry. Indeed, there was need to find out what can be done to enhance financial performance of micro retail enterprises in Kenya. The studies reviewed did not assess the relationship between portfolio diversification and financial performance of micro retail enterprises. Most studies on portfolio diversification were not done in African countries. Furthermore, studies on portfolio diversification showed mixed findings. Therefore, this study determined the relationship between portfolio diversification and financial performance of micro retail enterprises in Bungoma town, Kenya.

GENERAL OBJECTIVE

The general objective of the study was to determine the relationship between investment planning practices and financial performance of micro retail enterprises in Bungoma town, Kenya.

RESEARCH HYPOTHESIS

H_{01}:There is no significant relationship between portfolio diversification and financial performance of micro retail enterprises in Bungoma town, Kenya.

LITERATURE REVIEW

Theoretical Review

This section presents a discussion of modern portfolio theory which formed the basis for the conceptualized relationship between portfolio diversification and performance. Modern portfolio theory was developed by Harry Markowitz in 1952. The principal proposition of this theory is that diversification through portfolio formulation can reduce risk and enhance returns. The theory states that the risk of an individual asset doesn't matter, but its contribution to overall risk does. Selecting the right portfolio from a set of different assets is done through mean variance analysis (The Institute of Chartered Accountants of India, 2014). There are several assumptions of modern portfolio theory. Firstly, the investor seeks to maximize his expected utility of terminal wealth. Secondly, the investor has a single-period investment horizon. Thirdly the investor is risk-averse. Fourthly, the investor will choose his optimal portfolios on the basis of means and standard deviations of returns. Lastly, markets are perfect implying that transaction costs and taxes do not exist and securities are indefinitely divisible (Nielsen & Jorgensen, 2008).

Modern portfolio theory identifies the efficient frontier which is the set of portfolios that have highest expected return for a given level of risk and, by duality, minimum variance for a given expected return. MVO leads to maximization of expected return for a given level of risk or minimization of risk for a given return. According to the theory, investors perceive the same efficient set and their decisions are influenced by risk preference. The theory asserts that diversification is significant for combination of securities in the portfolio because low

correlation between securities can decrease the overall portfolio risk (Nielsen & Jorgensen, 2008). The modern portfolio theory has been highly criticized especially due to its simplistic assumptions being a predominant bias. Translation of the theoretical foundation of the theory into a viable portfolio construction algorithm faces technical difficulties stemming from the instability of the original optimization problem with respect to available data. The first criticism is that the theory does not really model the market. Secondly, modern portfolio theory does not consider personal, environmental, strategic, or social dimensions of investment decisions. Thirdly, modern portfolio theory does not take cognizance of its own effect on asset prices (Omisore, Yusuf & Nwufo, 2012).

Modern portfolio theory was very relevant to the study as it was the basis for the conceptualized relationship between portfolio diversification and financial performance of micro retail enterprises. This theory explains that retailers can choose a set of assets to invest in for optimization of portfolio risk and return. According to this theory, retailers can choose a combination of assets whose returns are negatively correlated hence decreasing the overall portfolio risk and enhance returns. This is very important in the risky and uncertain retail business environment in Kenya (Waweru & Ngugi, 2014).

Empirical Review

This section presents important empirical research findings from relevant literature on the influence of portfolio diversification on performance. A number of studies have been done locally and globally in regard to portfolio diversification and performance. Sohl, Rudolph & Muller-Stewens (2012) from Germany examined dimensions and performance implications of diversification strategies in the global retailing industry. The study found out that corporate-level assortment diversification into food and non-food retailing leads to decrease in profits over time. A U-shaped relationship between related within-industry diversification and firm performance and negative effect of unrelated within-industry diversification on firm performance was noted. It was found out that international diversification and firm performance have an inverted U-shaped relationship. It was also established that intra-regional diversification has a positive effect on firm performance while inter-regional diversification has an inverted U-shaped relationship with firm performance.

Iqbal, Hameed and Qadeer (2012) studied the impact of diversification on performance of manufacturing companies listed at Karachi, Lahore and Islamabad Stock Exchanges in Pakistan. The findings of the study indicate no positive relationship between diversification and firms' performance. Multiple comparisons showed that on average performance of companies at different levels of diversification is not same in terms of return on assets. Highly diversified and less diversified firms perform somehow equally as compared to moderately diversified firms based on return on assets. However, all three classes did not show much difference in performance according to their classes based on return on equity and market return as the results were insignificant.

Shen, Wang and Su (2011) studied diversification and performance of pharmaceutical and electronics firms whose stock is traded on the Shanghai and Shenzhen stock exchanges in China. The study found out that product diversification has an inverse U-shaped relationship

with firm performance. It was noted that geographic diversification has a U-shaped relationship with firm performance. This shows that both low and high levels of geographic diversification contribute more to firm performance. Furthermore, the interaction of product and geographic diversification has a negative impact on firm performance, implying that both strategies should not be implemented at the same time.

Raei, Tehrani and Farhangzadeh (2015) studied the relationship between diversification strategy, performance and risk of firms listed in Tehran Stock Exchange in Iran. Diversification was measured by Herfindahl index while return on equity was the only performance measure used. The study adopted the appropriate significant model with random effects after carrying out Hausman test. It was noted that a positive relationship exists between diversification strategy and return on equity. However, it was established that the relationship between diversification strategy and performance of firms is insignificant at 95% confidence level.

Giannotti, Mattarocci and Spinelli (2011) studied the role of portfolio diversification in the hotel industry in Italian market. The study specifically evaluated the benefits related to Markowitz portfolio diversification approach for portfolio construction in the hotel real estate market. It was established that standard geographic and sector diversification is associated with improved performance. The study found out that portfolio concentration leads to increased efficiency. It was further noted that portfolio efficiency declines in case there are concentration constraints for hotels in the same category and area.

Adamu, Zubairu, Ibrahim and Ibrahim (2011) conducted a study to evaluate the impact of product diversification on financial performance of construction firms in Nigeria. The study established that there is a nonlinear relationship between the extent of diversification and performance. It was noted that there is no significant difference between performance of undiversified and moderately diversified firms based on average profit margin, average return on equity and average return on total asset. Undiversified and moderately diversified firms also perform better than highly diversified firms based on profit margin and return on total assets (ROTA). But for return on equity, it is only moderately diversified firms that outperform highly diversified firms.

Oyewobi, Windapo and Cattell (2013) studied the impact of business diversification on construction companies' corporate performance in South Africa. It was established that low positive relationships exist between geographic diversification, product diversification and profit margin. The study also found out that weak negative correlations exist between product and geographic diversification and performance measured by ROTA and return on capital employed (ROCE). It was noted that product diversification exhibits a negative non-linear relationship with ROTA, while geographic diversification and ROTA are positively related. However, differences between performance of diversified and undiversified firms are not significant.

RESEARCH METHODOLOGY

Research Design

Research design refers to the outline for collection, measurement and analysis of data. It guides the entire research process (Sreevidya & Sunitha, 2011). The study used descriptive survey research design. It is suitable for description and measurement of phenomena at a point without manipulation. Descriptive research is undertaken to provide answers to questions of who, what, where, when and how (Sreevidya & Sunitha, 2011). According to Mugenda (2008), descriptive studies are easy and simple to conduct.

Population of the Study

Population refers to the entire group of individuals, objects or things that share common attributes, from which the researcher seeks to find information. The target population is the entire group of individuals, objects or things that share common attributes and to which results will be generalized. The target population of the study was all the micro retail enterprises in Kenya. The accessible population is a subset of the target population that reflects specific characteristics and can be practically reached in order to select a representative sample (Mugenda, 2008). All the 1912 micro retail enterprises, registered by County Government of Bungoma Revenue Directorate as at 2nd June 2017, comprised the accessible population.

Sample Size and Sampling Technique

Yamane's (1967) formula was used to determine the sample size. For a 95% confidence level and e = 0.05, the size of the sample should be is determined by the formula shown in Equation 3.1.

$$\mathbf{n = \frac{N}{1+N(e^2)}}\text{...}\textbf{Equation 1}$$

In the above formula, n is the sample size, N is the population size and e is the level of precision. Accordingly, the sample size is shown in Equation 3.2.

$$\mathbf{n = \frac{1912}{1+1912(0.05^{2)}} = 330.7958 = 331}\text{...........................}\textbf{Equation 2}$$

The sample size was 331 micro retail enterprises operating in Bungoma town, Kenya. Simple random sampling was used to select the micro retail enterprises whose managers/owners participated in the study as it is unbiased (Ogula, 2010).

Data Collection Instruments

The study used self-administered semi-structured questionnaires in order to gather primary data on investment planning practices and financial performance. Questionnaires give respondent adequate time to give well thought out answers. Bias of interviewer is also eliminated (Kothari, 2004). Secondary data sheets were used to collect data on financial performance of micro retail enterprises, which was obtained from financial records.

Pilot study refers to a small-scale rehearsal of the larger research design. It enables testing of the feasibility, equipment and methods (Sreevidya & Sunitha, 2011). A pilot study was conducted to test the reliability of the research questionnaire. It involved about 10% of the size of the sample population (Kothari, 2004). Hence, 34 managers/owners drawn from 34 micro retail enterprises in Kitale town took part in the study. Participants in pilot testing were not involved in the final study. According to Mugenda (2008), ensuring validity of the research questionnaire also ensures that it is reliable as valid measures are always reliable.

Validity is the degree to which an instrument measures what it purports to measure. It is the accuracy, truthfulness and meaningfulness of inferences that are based on the data obtained from a tool or a scale for each construct in the study (Mugenda, 2008). Content validity of research questionnaire was ensured by consulting the university supervisor. This assisted in evaluation of the concepts the questionnaire was trying to measure and to determine whether the set of items accurately represented the concepts. Reliability is the consistency with which a research instrument measures the construct or content area it is intended to measure. It is reported as a coefficient ranging from 0.00 (low) to +1.00 (high). A coefficient above or equal to 0.70 is considered sufficient for most cases (Sreevidya & Sunitha, 2011). Therefore, reliability of the questionnaire was tested using Cronbach's alpha coefficient where a threshold value of ≥ 0.7 was used.

Data Collection Procedures

After testing the validity and reliability of the research questionnaire and making amendments accordingly during pilot study, the researcher sought the consent of Jomo Kenyatta University of Agriculture and Technology and the management of micro retail enterprises in Bungoma town. The research questionnaires were then administered on the sampled respondents by the researcher in person or research assistant.

Data Processing and Analysis

The data collected was cleaned, edited, coded and stored before being analyzed. Both descriptive and inferential statistics were used for data analysis. Descriptive statistical tools included frequencies, percentages, means, variances and standard deviations. Inferential statistics included multiple regression analysis and Pearson Product Moment Correlation. Data was presented in tables, charts and graphs. The study adopted the following multiple regression model:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon \ldots\ldots\ldots\ldots\ldots\ldots\ldots\text{Equation 3}$$

Where: **Y** represents financial performance of micro retail enterprises in Bungoma town, Kenya; β_0 represents the y-intercept; β_1, β_2, β_3 **and** β_4 represent coefficients of portfolio diversification, risk-based capital budgeting, strategic investment goal setting and portfolio rebalancing respectively; X_1, X_2, X_3, **and** X_4 represent the independent variables; ε represent error term

The financial performance measures used in this study were net profit margin, total asset turnover, return on net assets and return on total assets. These measures were measured subjectively on a Likert scale of 1 to 5, for strongly disagree to strongly agree respectively. Secondary data on these financial metrics were used to corroborate the findings. This approach has been used by various researchers as secondary quantitative data is more objective. Onduso (2013) obtained secondary data from financial records in order to complement raw data so as to provide an in-depth analysis of financial performance in the descriptive study. Madrara (2012) obtained data from financial reports such as income statements and balance sheets in order to support empirical findings.

According to Suklev and Debarliev (2012), financial performance can be measured on a Likert scale. There is no consensus among researchers on how to measure financial performance, with both subjective and objective measures being used (Khan, Khalique & Nor, 2014). There is wide use of subjective approach for measuring organizational performance in empirical research. Perceptions of managers about performance are consistent with objective measures (Glaister, Dincer, Tatoglu, Demirbag, & Zaim, 2008). Organizational performance can be measured using return on sales, return on investment and return on assets (Jusoh & Parnell, 2008). This study used four metrics to measures financial performance which is an approach used in literature, for example in a study by Zehira and Yavuz (2014) on organizational learning, crisis management capability and firm performance in Turkey where financial performance was measured on a Likert scale.

RESEARCH RESULTS

Portfolio Diversification

The researcher sought the opinions of the respondents on portfolio diversification. It was agreed there is an approach adopted for diversification within asset classes to reduce risks and enhance returns (mean = 3.93; std dev = 0.951; var = 0.905). The managers/owners also agreed that the enterprises broadly invest such that as other assets' returns increase, other assets' returns decrease (mean = 3.93; std dev = 1.027; var = 1.055). The respondents agreed that the enterprises invest funds in assets with highest expected return for a given level of risk or least risk for a given level of expected return (mean = 3.66; std dev = 1.218; var = 1.484). Respondents were in agreement that in choosing the asset mix to invest in, the enterprises allocate funds to assets based on each asset's contribution to risk (mean = 3.53; std dev = 1.168; var = 1.365). The relevant results are presented in Table 1.

Table 1: Descriptive Statistics for Portfolio Diversification

	N	Min	Max	Mean	Std Dev	Variance
The enterprise invests funds in assets with highest expected return for a given level of risk or least risk for a given level of expected return	331	1	5	3.66	1.218	1.484
In choosing the asset mix to invest in, the enterprise allocates funds to assets	331	1	5	3.53	1.168	1.365

based on each asset's contribution to risk						
There is an approach adopted for investing within asset classes to reduce risks and enhance returns	331	1	5	3.93	.951	.905
The enterprise broadly invests such that as other assets' returns increase, other assets' returns decrease	331	1	5	3.93	1.027	1.055

Financial Performance of Micro Retail Enterprises

This study further sought opinions of managers/owners on financial performance of their enterprises. The study noted that respondents were in agreement that the ability of the enterprises to derive returns from investment of Ksh. 1 in net assets was improving (mean =3.6767; std dev = 0.83559; var = 0.698). The respondents were undecided on whether the ability of the enterprise to derive returns from investment of Ksh. 1 in total assets was improving or not (mean =3.3474; std dev = 0.78440; var = 0.615). Respondents were also unsure of whether the ability of the enterprises to control the cost of sales, operating and financing expenses was improving or not (mean =3.3172; std dev = 0.57654; var = 0.332). The managers/owners were also unsure of whether the efficiency of the enterprises in generating sales revenue from utilization of Ksh. 1 of total asset was improving or not (mean =2.5196; std dev = 0.64813; var = 0.420). These findings based on multiple measures of financial performance imply that the micro retail enterprises perform differently with some respondents agreeing and others disagreeing that financial performance was improving. The pertinent results are presented in Table 2.

Table 2: Descriptive Statistics for Financial Performance

|	N	Min	Max	Mean	Std. Dev	Variance
The ability of the enterprise to control the cost of sales, operating and financing expenses is improving	331	2	4	3.3172	.57654	.332
The efficiency of the enterprise in generating sales revenue from utilization of Ksh. 1 of total asset is improving	331	1	5	2.5196	.64813	.420
The ability of the enterprise to derive returns from investment of Ksh. 1 in net assets is improving	331	2	5	3.6767	.83559	.698
The ability of the enterprise to derive returns from investment of Ksh. 1 in total assets is improving	331	2	5	3.3474	.78440	.615

The study also sought information from the managers/owners of the micro retail enterprises on actual financial performance from their financial records. The findings indicate that net

profit margin was 58.52% in 2013. In 2014, the net profit margin was 58.41%. In 2012, the net profit margin was 57.09%. Net profit margin was 54.22% in 2015. In 2016, net profit margin was 50.97%. It was established that total asset turnover was 1.06 in 2014. In 2013, total asset turnover was 1.05. Total asset turnover was 1.04 in 2012. In 2015, total asset turnover was 1.01. In 2016, total asset turnover was 0.99. It was also noted that return on net assets was 68.89% in 2014. In 2013, return on net assets was 68.61%. In 2012, return on net assets was 64.75%. Return on net assets in 2015 was 62.31%. In 2016, return on net assets was 57.60%. This study established that return on total assets was 60.78% in 2014. Return on total assets was 60.12% in 2013. In 2012, return on total assets was 57.86%. Return on total assets was 54.06% in 2015. In 2016, return on total assets was 50.43%. On average the enterprises reported net profit margin of 55.84%, total asset turnover of 1.03, return on net assets of 64.43% and return on total assets of 56.65%. The findings imply that financial performance was generally declining. The detailed results of analysis are depicted in Table 3.

Table 3: Financial Performance of the Retail Enterprises from 2012 to 2016

| Financial measure/Year	2012	2013	2014	2015	2016	5-year average
Net profit margin	57.09	58.52	58.41	54.22	50.97	55.84
Total asset turnover	1.04	1.05	1.06	1.01	0.99	1.03
Return on net assets	64.75	68.61	68.89	62.31	57.60	64.43
Return on total assets	57.86	60.12	60.78	54.06	50.43	56.65

The study further analyzed the actual financial measures graphically to depict the trend over the five years. The results indicate that net profit margin rose between 2012 and slightly decreased between 2013 and 2014. However, it decreased steadily between 2014 and 2016. This implies that financial performance based on net profit margin was generally declining. The trend of net profit margin from 2012 to 2016 is depicted in Figure 1.
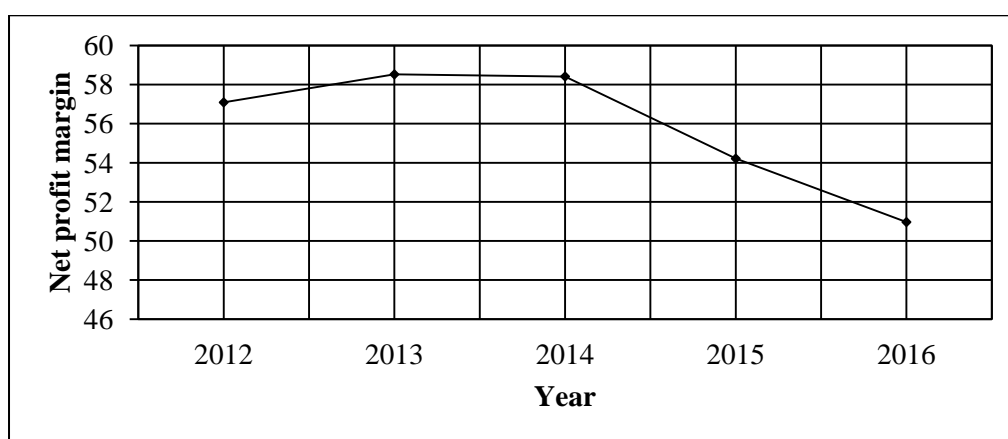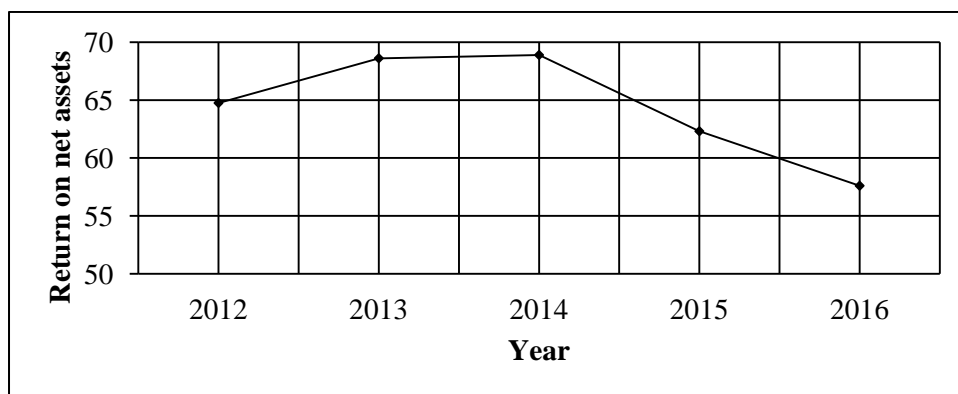

Figure 1: Net Profit Margin Trend

The study also examined the trend of asset total asset turnover in the micro retail enterprises. The findings indicate that total asset turnover rose between 2012 and 2014. However, it

decreased steadily between 2014 and 2015. Between 2015 and 2016, total asset turnover decreased but at a lower rate compared to 2014 and 2015. This implies that financial performance based on total assets turnover was generally declining. The results of graphical analysis are presented in Figure 2.
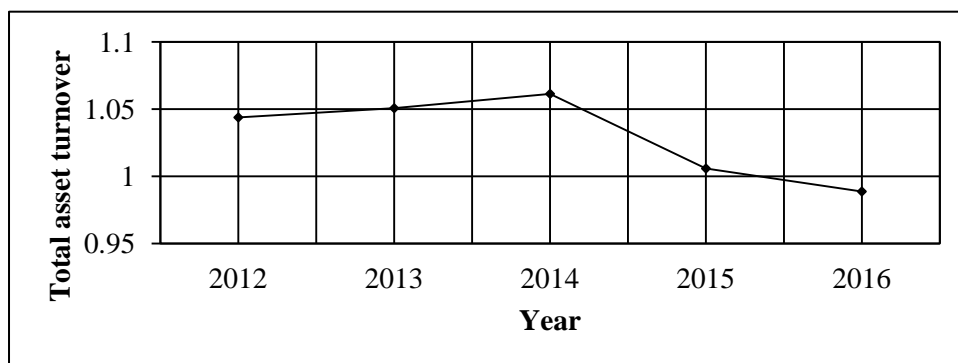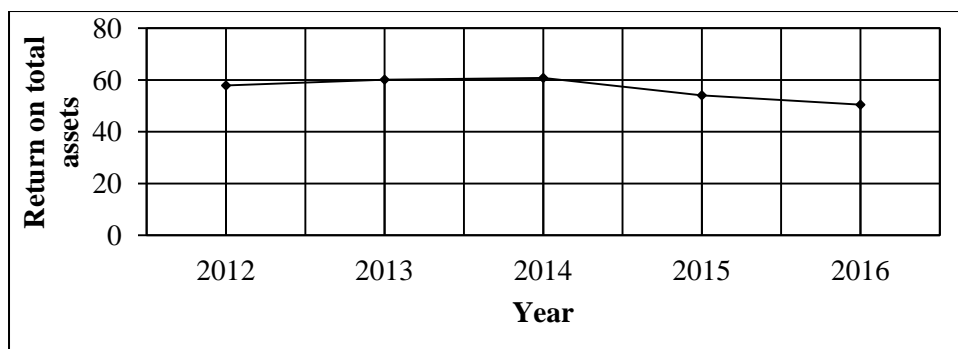

Figure 2: Total Asset Turnover Trend

The study also examined the trend of return on net assets in the micro retail enterprises. The findings indicate that return on net assets rose between 2012 and 2014. However, it decreased steadily between 2014 and 2016. This implies that financial performance based on return on net assets was generally in a downward trend. The results of graphical analysis are presented in Figure 3.

Figure 3: Return on Net Assets Trend

The study also analyzed the trend of return on total assets in the micro retail enterprises. The findings indicate that return on total assets rose between 2012 and 2014. However, it decreased steadily between 2014 and 2016. This implies that financial performance based on return on total assets was generally declining. The results of graphical analysis are presented in Figure 4.

Figure 4: Trend of Return on Total Assets

Generally, the findings indicate that financial performance based on net profit margin, total asset turnover, return on net assets and return on total assets was higher in 2013 compared to 2012 but declined steadily from 2014 to 2016. These findings corroborate results from the survey on financial performance of the micro retail enterprises. It implies that the subjective measures of financial performance used in this study correlate with the objective measures of financial performance. The findings of the study supports the findings by KNBS (2016) that a high number of micro retail enterprises were facing closure owing to poor financial performance in the midst of strong competition.

Portfolio Diversification and Financial Performance

The study established that respondents were in agreement that investment of funds in business projects or assets was aimed at optimizing risk and return in the portfolio. It was also agreed that the amount of finances allocated to particular assets in the enterprise portfolio was determined by the associated level of risk. Respondents also consented that there was a strategy adopted for diversifying within asset classes in order to optimize portfolio returns. There was also general agreement among the respondents that investments are geared towards achieving a portfolio with uncorrelated returns from various assets. It was established that there is a positive and significant correlation between portfolio diversification and financial performance ($r = 0.322$; $p < 0.01$). It was noted that improving portfolio diversification leads to significant enhancement of financial performance and vice-versa ($b1 = 0.217$; $p < 0.05$). These findings support the argument of modern portfolio theory that risk and return optimization through portfolio diversification leads to improved performance.

Financial Performance of Micro Retail Enterprises

The study found out that the respondents were in agreement that the ability of the enterprises to generate for each shilling of net asset was improving. It was noted that respondents could not decide whether the ability of the enterprises to derive returns from investment a shilling in total assets was improving or not. It was also unclear if the ability of the enterprises to control the cost of sales, operating and financing expenses was improving or not. The managers/owners were also unsure of whether the efficiency of the enterprises in generating sales revenue from utilization of a shilling invested in total asset was improving or not. The respondents were also unsure on whether the overall financial performance of the enterprises

was improving or not. Findings based indicated that the financial performance of micro retail enterprises measured by net profit margin, total asset turnover, return on net assets and return on total assets was generally declining.

Relationship between Portfolio Diversification and Financial Performance

The study examined the relationship between portfolio diversification and financial performance of micro retail enterprises in Bungoma town. Pearson correlation coefficient (R) was used to show the direction and strength of the relationship between the independent variable and the dependent variable. The study findings indicate that the relationship between portfolio diversification and financial performance was positive and significant (r = 0.322; p < 0.01). This implies that the more the portfolios of micro retail enterprises are diversified the more their financial performance improves and vice versa. The correlation analysis results are presented in Table 4.

Table 4: Correlation Analysis for Portfolio Diversification

		Financial performance
Portfolio diversification	Pearson Correlation	.322**
	Sig. (2-tailed)	.000

**. Correlation is significant at the 0.01 level (2-tailed).

REGRESSION ANALYSIS

The study examined the influence of portfolio diversification on financial performance. The study conducted the t-test of statistical significance of the regression coefficient of portfolio diversification. The null hypothesis is that portfolio diversification has zero regression coefficient (B) in the population. The findings indicate that portfolio diversification is a significant predictor of financial performance (t = 8.632; p < 0.05). Therefore, the study rejected the null hypothesis that there is no significant relationship between portfolio diversification and financial performance of micro retail enterprises in Bungoma town, Kenya at a significance level of 5%. It was concluded that there is a significant relationship between portfolio diversification and financial performance of micro retail enterprises in Bungoma town, Kenya. The results of analysis are presented in Table 5.

Table 5: Evaluating Individual Regression Coefficients

	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	.374	.189		1.984	.048
Portfolio diversification	.217	.025	.363	8.632	.000

a. Dependent Variable: Financial performance

From the results of the t-test of individual regression coefficients, it was clear that portfolio diversification and the constant would be included in the regression equation as they were significant ($p < 0.05$). The results indicate that improving portfolio diversification by 1 unit enhances financial performance by 0.217 unit. The finding partially supports the finding by Raei et al. (2015) that there is a positive relationship and insignificant relationship ($p > 0.05$) between diversification strategy and firm performance. This study finding also concurs with results of a study by Giannoti et al. (2011) which established that portfolio diversification as advocated for by Harry Markowitz leads to improved performance. This finding contradicts with findings of studies on diversification and performance conducted by Sohl et al. (2012), Iqbal et al. (2012), Shen et al. (2011), Adamu et al. (2011) and Oyewobi et al. (2013). One of the possible reasons for these contradicting results is that the firms concerned could have diversified within asset classes without due consideration of correlation of asset returns.

The findings from the regression analysis support the propositions of the theory that this study was anchored on. The basic tenet of modern portfolio theory of risk and return optimization through portfolio diversification is supported by the study results. The regression function shown in Equation 4.1 was used to explain the results of regression analysis.

$$Y = 0.374 + 0.217X_1 \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\text{Equation 4}$$

CONCLUSIONS

There are several conclusions that were made in respect of the study findings. These are in line with the objective of this study. This study concluded that there is a positive and significant relationship between portfolio diversification and financial performance; which is in line with the argument of modern portfolio theory. It was concluded that risk and return optimization guided investment decisions hence determining fund allocation for projects. It was also concluded that sub-asset class fund allocation strategies had been set in order to benefit from uncorrelated returns from the enterprise portfolio. However, majority of respondents did not have a variety of financial assets or securities such as equities or stocks, bonds and money market instruments such as treasury bills which could explain why financial performance of micro retail enterprises was declining.

RECOMMENDATIONS

The researcher put forth a number of recommendations based on the outcomes of the study. They are also in line with the study objective. There are several recommendations for investors and organizational policy makers in micro retail enterprises. First, the study recommends that they should increase the variety of asset classes in their portfolios such that they have both financial assets such as stocks, bonds and money market instruments as well as real assets such as cash, property and commodities. This will enable them to benefit from uncorrelated returns of assets in their portfolios as long as the asset classes have different risk-return profiles.

There are also has a number of recommendations with regard to practical application of modern portfolio theory which this study was anchored on in micro retail enterprises. As regards modern portfolio theory, this study recommends that its principles be applied in portfolio construction. It is also recommended that financial advisors and consultants should focus on strategic asset allocation and portfolio construction process as advocated for by modern portfolio theory, as opposed to naive portfolio diversification strategy. To the government, this study recommends that seminars on basic investment planning skills should be organized periodically both at the national and county level for owners/managers of micro retail enterprises.

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