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Effect of Market Penetration Strategy on Financial Performance of Tobacco Manufacturing Firms in Kenya

[1*] Michael Mbutu, [2] Benjamin Tarus, [3]Lucy Wanza
[1] MBA (Strategic Management) Student, [2, 3] Senior Lecturers
[1, 2, 3] *Department of Business Administration, the Catholic University of Eastern Africa, Kenya*

Abstract: The purpose of this study was to evaluate the effect of market penetration strategy on the financial performance of tobacco manufacturing firms in Kenya. The study was informed by resource-based theory and adopted an ex post facto research design. The target population was tobacco manufacturing firms with 350 company employees from British American Tobacco Kenya Ltd and Mastermind Tobacco Kenya Limited being the unit of analysis. The sample size was 187 and stratified random sampling technique was used. This study used closed ended questionnaires as a data collection technique. Cronbach's alpha coefficient was used to test the reliability of research tools with Cronbach alpha being above 0.7 for all variables. The results of this study were analyzed using descriptive and inferential statistics. Descriptive analysis involved frequencies distribution, percentages, means and standard deviations. The inferential analysis involved Pearson's correlation and the multiple regression analysis. The study revealed that market penetration strategy had a positive and significant effect on financial performance ($\beta 1= .481$, $t= 6.506$ and $p= .000<.05$). Research thus concluded that market penetration strategy had a significant effect on the financial performance of the tobacco companies in Kenya. The study recommends to management of tobacco manufacturing firms in Kenya to enhance their market penetration through penetration pricing where lower prices are charged for new improved products to attract more customers.

Keywords: Market penetration Strategy, strategy, financial performance

I. INTRODUCTION

The financial performance of an organization is measured by several factors and, consequently, different interpretations of the success of the financial performance are obtained. Each of these approaches to financial performance can be unique (Nyamweya & Obuya, 2020). In addition, all businesses are unique about the internal environment, so measuring economic performance is inherent. The results of the economic results are the result of the success or the market position achieved (Gitman, 2015). Financial performance encompasses the ways in which an entity attains market-based targets and financial goals. The financial performance of the organization means reaching the final targets of the entity as indicated in the strategic plan. Conceptually, the financial performance of an organization was taken as a comparison between the value generated by a company, measured by three general elements, namely the effectiveness, efficiency and importance of the financial performance of an organization with respect to the value that the owners will receive from the company (Fahey & King, 2015). Financial results can be determined in several ways. There are several specific models which are important factors for the profitability of the company. These are: characteristics of the company's competitive sector; company position in terms of quality or quantity of competitors and company resources (Collis, 2014). A company will have to continually review its growth strategy to be able to adapt to its commercial, reactive and commercial movements and maintain its competitiveness. The Ansoff matrix is a well-known categorization of growth strategies. Distinguishes between four strategies, namely: market penetration, product development, market development and diversification. Growth can be achieved with current products and current markets through market entry. Higher sales can be achieved from existing markets by attracting existing customers who are not offered or competitors. Alternatively, retail customers can improve loyalty and increase the value of their shopping cart (Pleshko, 2016).

1.1 The Tobacco Industry in Kenya

Two companies, which dominate the tobacco industry in Kenya, were determined as the most appropriate for this research. Jacqueline (2018) and Ngunjiri (2017) have successfully used case studies in previous studies. The tobacco industry is a significant player in the economy of the country. It plays job creation role and contribution to the exchequer. It provides 600,000 jobs directly (Li et al., 2019). In economic terms, the industry provides annual farm incomes over Ksh.717 million and export earnings to the government of about Kshs 420 million. Revenue to the government in form of taxation is estimated to be over Kshs 7 billion, with British American Tobacco (K) Ltd being the main contributor to this revenue. British American Tobacco (BAT) is a Kenyan company, BAT Plc., Which manufactures and sells cigarettes and tobacco. The company has sold over 10 brands in the Kenyan market. Its factory in Nairobi offers a variety of markets and produces various products. The company's factory is a production site in Eastern Europe, the Middle East and Africa. The brands of the company are Dunhill, Ambassador and Sportsman. BAT Kenya also offers Rothmans in the Kenyan market. Other products of the company include Dunhill Release, a menthol-converted cigarette; Offer of Embassy Fresh, a separate menthol cigarette and Dunhill Switch, capsules. The company has a green leafy plant in Thika. Mastermind Tobacco Kenya Ltd (MTK) is the only Kenyan tobacco company based in Nairobi. Mastermind Tobacco Kenya Ltd is engaged in the growth, production and marketing of tobacco. Since its inception in 2015, its brand portfolio has grown by twelve as one of the leading regional brands in the "Super match Kings".

1.2 Statement of the Problem

According to Derek and Betcher (2018), the advent of globalization and the introduction of more stiff regulations for the Tobacco industry has seen the increase of anti-tobacco forces and attitudes across the globe. There has been increased taxation and introduction of new trade barriers like exercise duty in Kenya, which has seen tobacco industries drop their profit margins. These punitive fiscal policies, which have been deliberately driven by governments to discourage consumption of tobacco products, have negatively affected the tobacco industry's financial performance. Hatchard (2014) notes that entities in the tobacco industry are facing many new risks, including that or losing their market share to the underground economy. Both MTK and BAT have not been spared by these changes in the market place, especially with the products they primarily deal with. The Tobacco control act of 2017 has greatly impacted financial performance, leading to high tax bills, diminishing revenues and shrinking markets. Companies in the tobacco sector have endured low profits and generally poor financial performance. Companies have mitigated on the financial and market share risks through underhand methods such as tax avoidance and advancement into the underground economy. Others have adopted to the declining market share by cutting their operations in Tobacco and diversifying their areas of interest. According to Derek and Betcher (2018), lobbying has increasingly become a key tool in the survival of companies in the tobacco industry. This approach is largely used in an effort to reverse the installation and effects of punitive fiscal policies against companies in the tobacco industry. The companies are trying to lobby policymakers into making favourable laws that will promote their sustainability and profitability. This study therefore sought to establish the effect of market penetration strategy on financial performance of the Tobacco firms in Kenya.

1.3 Objectives of the study

The study sought to establish the effect of market penetration strategy on financial performance of the Tobacco firms in Kenya.

1.4 Research Hypothesis

This study tested the following research hypothesis at the 95% level of significance:

> **Ha1**: There is a significant relationship between market penetration strategy and financial performance of Tobacco Manufacturing Firms in Kenya

II. LITERATURE REVIEW

2.1 Theoretical Review

The study adopted Transaction Cost Theory. Coase's transaction theory (2018) assumes that sometimes the market fails to effectively allocate factorial services and goods due to naturalistic and governmental externalities (Kogut, 2016). This entails higher costs for organizing the exchange on the market than for the internal organization of the exchange. These costs are generally referred to as natural exteriors, real estate external parts and technical exteriors. Strategic alliances are formed to place the transactions at these costs in a common collaborative structure, to reduce the costs incurred for the partners and thus prevent opportunism between the partners (Beamish & Bank, 2015). Apparently, the costs of external transactions are more than the internal costs of the company, as the company will grow as it is able to complete production efficiently. If internal costs were to be reduced, the company would be more likely to make home production cheaper. According to Coase (2018), a business will be expanded until the company's activities can be carried out at a lower price within the company. Therefore, if companies see a high risk of environmental uncertainty, they cannot outsource or exchange resources with the environment. According to Contractor and Lorange (2016), strategic alliances may depend on the degree of interdependence of the parties involved. Mergers and acquisitions represent the highest level of joint venture between the participating parent companies, while the lowest level of mutual dependence is in an informal cooperative enterprise. According to Hennart (2016), there is a better capital connection between strategic partners and their activities through coordination with consumers or contractual partners. This theory has been used to explain the possibility of strategic partnerships as an option for Tobacco manufacturing companies. Therefore, companies evaluate the cost of exchanging resources with the environment with the bureaucratic cost of carrying out the activities. This theory informs the relationship between market penetration strategy and financial performance given that a firms that penetrate markets through penetration pricing are those that are operating at a lower cost than competitors hence they can lower their prices below the competitors price so as to push their products into the market and attract more customers leading to improved financial performance.

2.2 Empirical Review

Gloria and Ding (2017) examined the impact of the media of a company's competitive strategy on market penetration and performance. The results of the analysis of the structural equations indicate that the mediation of competition is manifested mainly in the innovation strategy, the most important factor for creating greater value for the company in the new market. Kara (2014) analyzed the association of market penetration and consistent performance with the Kohli and Jaworski scale (2016) with nonprofit service providers. They found a statistically significant and positive relationship between market entry and the performance of non-profit service providers. Narver and Slater (2018) supported this approach, which used subjective performance measures to analyze internalization and performance reports using a sample of 53 products and services in a variety of industries and found solid industry relationships. Tse, Heung and Yin (2017) analyzed the market penetration and performance reports of 81 hotels in Hong Kong. The results showed a positive and significant relationship between entering the market and corporate performance. The study found a strong connection between market entry and corporate performance. Martin-Consuegra and Estebon (2017), who examined the relationship between market penetration and performance of 234 international airlines using the MARKOR tool, strengthened the study. The results of the study indicated a positive and significant relationship between market entry and performance. Similarly, the market insights of Mamat and Ismail (2015) assessed the effectiveness of the Bumiputera furniture companies in Malanta. Their results showed a positive and significant correlation between cross-functional coordination of market penetration, competition orientation and profitability, sales growth rate and customer inventory. In another study conducted by 220 Kenyan manufacturing companies, Lagat, Chepkwony and Kotut (2019) confirmed the positive and significant market orientation measured using the MAKTOR measurement scale and performance ratios. In the same way, Ogbonna and Ogwo (2014) analyzed the market penetration (customer orientation, competition orientation and cross-functional coordination) of the 52 Nigerian insurers and their performance (conditions of sales volume, profitability and market share). The survey results showed that insurers involved in entering the market made some progress, while those who did not establish market orientation underperformed.

III. METHODOLOGY.

3.1 Research Design, Population and Sampling

The research project formed a plan for data collection, measurement and analysis (Cooper & Schindler, 2016). The research adopted an ex post facto research project.. Ex post design studies show how variables connect, predict behaviour, but are unable to determine the causal relationships of variables. The target population for the study was 350 employees drawn from 2 firms from finance, marketing and strategic management department. The two firms are namely the British American Tobacco Kenya Ltd and Mastermind Tobacco Kenya Limited. Kothari (2019) defined the number of subjects selected from the universe (population) to form a sample as a sample. The sample size was determined by the using the formulae

$$n = N/ 1+ (N^* e2)$$

Where ‘n’ is the sample size to be calculated, ‘N’ is the target population, ‘e’ is the error term taken at 0.05. The sample size was thus calculated as:

$$n = 350/ 1+ (350^* 0.0025)$$

$$n = 186.666$$

$$n= 187$$

The sample size was thus 187 respondents. Stratified random sampling techniques was thus used to pick the sample size from the population. The study segregated the target population into three departments including marketing, finance and strategic management.

3.2 Research Instruments and Data Collection

This research used questionnaires, annual reports and audited accounts as an important data collection tool. The questionnaires of this research were designed by analyzing the research objectives, the hypotheses, the review of the literature and the conceptual structures. The questions were developed, reformulated and chosen to adapt to the research context to represent the variables in the research. In addition, the questionnaire was calibrated with the Likert five-point scale, which was anchored: "agree" (SA) and "disagree" (SD). The Likert scale / summed scale is made up of statements that indicate an attitude towards or against the object of interest. When the participant was asked to agree or disagree with each statement, each answer was assigned a numerical score to reflect its level of attitude and the scores were added up to show the general attitude of the participants. Structured questions were used in section B of the questionnaire to allow the researcher to gather information relevant to the questions in the study. The annual reports, on the other hand, provided important information, such as profitability and sales over the years, to show the economic status of these companies. In this study, the validity of the questionnaire began in the tool design phase. The researcher sought the contributions of the supervisors to evaluate the validity of the content and the predictability of the displayed content. The researcher also examined the questionnaire with an expert from the tobacco companies. To measure the reliability of the data collection tool, a pilot study was conducted with the tool prior to the research. The aim of the pilot study was to improve the questionnaire so that respondents had no problems answering the questions and therefore improve the quality of the data collected. He asked to fill in a questionnaire, the clarity of the instructions and the time needed to check the ambiguities in the questions. The survey replied to the questionnaires twice a week. Cronbach's alpha coefficient was applied to the results obtained to determine how the subjects were related to the same instrument. The Cronbach alpha coefficient above 0.7 was considered acceptable as a threshold value, which would improve the identification of the erased and erased variables (Hair et al., 2017). Before collecting the data, the researcher first received a letter from the Catholic University of East Africa. Subsequently, he received a research grant from the National Commission for Scientific Technology and Innovation (NACOSTI). Finally, the researcher requested permission from the directors of the selected companies to introduce themselves and explain the purpose of the study. When the permit was granted, he then replied to the respondents, who also explained the purpose of the visit. The questionnaires were based on "drop in and out" or the companies were chosen personally to ensure a high return based on the availability of the interviewees.

3.3 Data Analysis Techniques

When the completed questionnaire collected the researchers, it was included in a computer program called SPSS (statistical package for social sciences). The first data screening was performed using the sorting functions. Quantitative data were analyzed using descriptive and inferential statistical techniques. The descriptive statistics provided a profile of the target population, i.e. frequencies and percentages, on average, of standard deviations. The inferential statistics used were Pearson's correlation and Simple univariate regression model. The univariate regression and correlation have been used as a form of statistical inferential analysis to determine the relationship between dependent and independent variables. The model is demonstrated below.

$$Y = \alpha + \beta_1 X_1 + \varepsilon \qquad [1]$$

Where: Y = Financial Performance, α = Alpha (constant), $\beta 1$ = Beta (Coefficient of X_1) , X_1 = Market penetration strategy and ε is the error term.

IV. RESULTS AND DISCUSSION

4.1 Response Rate

A total of 187 questionnaires were issued of which 163 were adequately filled and returned on time. This represented 87.16 % of the targeted sample. This is a very high response rate, considering the limited amount of time that they were allowed to participate. The response rate was thus adequate for further analysis.

4.2 Demographic Information

The respondent group had 87(53.37%) males and 76(46.62%) females. The assumption made is that these percentages depicted the distribution of the workforce in the industry between genders. Regarding education level, out of the 163 participants selected for the study, the majority that were 97(59.5%) were university graduates, on the other hand, there were a total of 51 college graduates constituting 31.28 % of the total respondents. Only 15(9.2%) of the total number of study participants were secondary school dropouts of level of education of the respondents. The highest number of participants were university graduates while. Concerning the work experience of respondents, Table 4.3 indicates that majority of the employees selected from the two companies for the study had a work experience of 4-6 years constituting 34.96 % of the total participants, 25.15 %, 16.56%, and 14.72% of the respondents had a work experience of 1-3 years, less than a year, and 7-9 years respectively. Only 26 participants constituting 13% had a work experience of over 10 years.

4.3 Descriptive Statistics of the Study Variables

The study sought to establish the general distribution of study variables based on mean and standard deviation. The study variables included Market Penetration strategy and Financial Performance. The descriptive analysis has been organized in terms of study variables.

4.3.1. Market Penetration Strategy

The study used a 5-point Likert scale to measure the perception of the respondents regarding the state of market penetration in their respective firms. The study findings are presented in Table 1.

Table 1: Market Penetration Strategy

Statements on Market Penetration	Mean	Std. Dev
The firms efficient use of distribution channel facilitates the company's sales growth	4.36	.531
The firm effective use of distribution channels enhances your company's profitability	4.34	.688
The firm direct distribution channel enables company to satisfy its customers	4.33	.587
The frim efficient use of distribution channel increases the market share	4.23	.723
The firms efficient use of distribution channel increases the market share	3.98	.430
Overall Mean Score	**4.248**	**.5918**

The table 1 presents responses to statements regarding market penetration by the two firms studied. The responses on the statements regarding market penetration have been ordered from the most supported to the least supported based on the mean response. The most supported statement was that the firm's efficient use of distribution channel facilitates the company's sales growth as depicted by mean response (M=4.40) tending to strong to strong agreement with a standard deviation of .572 around the mean. The statement that was least supported by respondents was that the firms efficient use of distribution channel increases the market share of the companies as depicted by mean response (M= 3.98) tending to agreement and a standard deviation of .430 around the mean. Generally, the tobacco manufacturing firms studied had implemented market penetration strategies to enhance their financial performance as evidenced by overall mean score of 4.248 that is tending to agreement. The study thus concludes that market penetration strategy was highly in use among the firms studied.

4.3.2 Financial Performance

The research also examined the financial performance of tobacco manufacturing firms in Kenya. The statements regarding financial performance were evaluated based on a 5-point Likert scale where a score of 5 was very high; 4 was high; 3 was Moderate, 2 was low and was poor. The Finding have been presented in table 2.

Table 2: Financial Performance

Financial Performance	Mean	Std. Dev
Your sales growth in relation to your competitors has been better	4.33	.675
Profit growth in relation to your expectations has been satisfactory	4.25	.771
Your profit growth compare to that of competitors is better	4.24	.719
Your increased market size in new markets compare to your competitors is better	4.23	.811
There has been improvement in efficiency	4.21	.645
There has been capital growth realized from operations	4.02	.647
Overall mean score	**4.23**	**.742**

The table 2 shows the responses on financial performance as rated by the respondents. The statements have been arranged from the highest rated to the lowest rated question on financial performance. The most rated question about financial performance was that sales growth in relation to competitors has been better as evidenced by mean responses and stated deviation (M=4.33 and SD=.675) that tended to very high performance level. The least supported statement was that there been any capital growth realized from operations as shown by mean response (M= 4.02) of high performance and a standard deviation of .647 around the mean. The mean score was 4.23 implying that the firms enjoyed a relatively high level of performance in the current markets. Further, the study examined the financial statements and extracted details of sales growth and profitability growth to examine the financial performance of the two firms studied. The sales and profitability growth is presented in figure 1 and Figure 2.

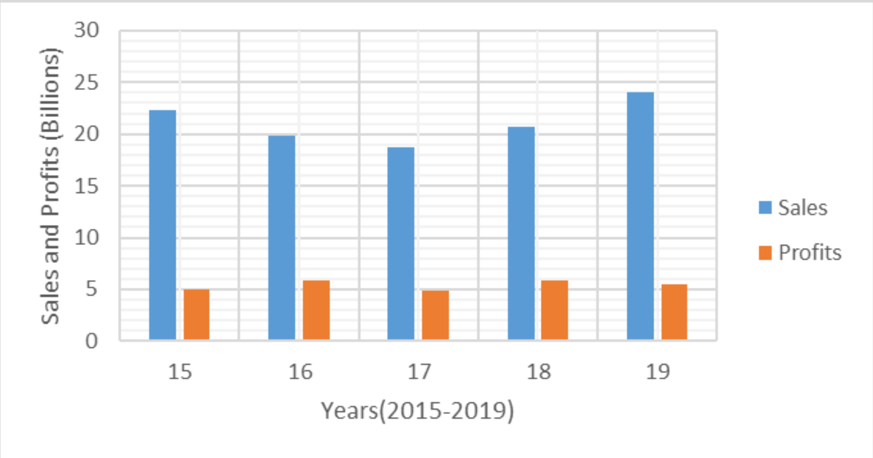

Figure 1: Sales and Profits of British American Tobacco

Figure 1 shows that the sales for BAT fell from Ksh. 24 billion in 2015 to Ksh.20 billion in 2016. The sales fell further in 2017 to Ksh.18 bilion. However, the sales rose from Ksh 22 billion in 2018 to Ksh.25 billion in 2019. On the other hand profits rose from Ksh. 5 billion to Ksh.5.2 billion in 2016. In 2017, the profits fell back to Ksh.5 billion. However, in 2018 profits rose to Ksh. 5.2 Billion and Ksh 5.1 Billion in 2019. The fall and rise in profits could have been caused by market penetration, diversification, product development and market development rates.

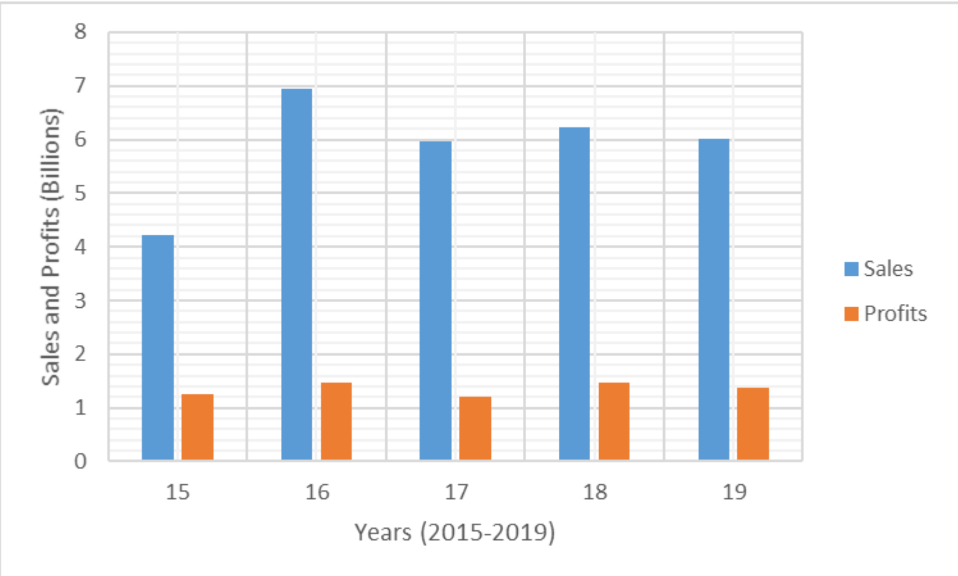

Figure 2: Sales and Profits of Mastermind Kenya

Figure 2 shows that the sales for MTK rose from Ksh. 4 billion in 2015 to Ksh.7 billion in 2016. The sales fell in 2017 to Ksh.6 bilion. However, the sales rose from to Ksh 6.1 billion in 2018 and Ksh. 6 billion in 2019. On the other hand profits rose from Ksh. 1.2 billion to Ksh.1.4 billion in 2016. In 2017, the profits fell back to Ksh.1.2 billion. However, in 2018 profits rose to Ksh. 1.4 Billion and Ksh 1.3 Billion in 2019. The fall and rise in profits could have been caused by market penetration, diversification, product development and market development rates.

4.4 Regression Analysis

The study examined the effect of market penetration strategy on financial performance of Tobacco manufacturing firms in Kenya. The study adopted simple OLS regression model with regression output included the model summary, analysis of variances (ANOVA) and regression coefficients. The findings are presented in table 3

Table 3: Effect of Market Penetration Strategy on Financial Performance

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.647[a]	.418	.415	.38668

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	17.309	1	17.309	115.765	.000[b]
	Residual	24.073	161	.150		
	Total	41.382	162			

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.502	.349		1.439	.152
	Market Penetration Strategy	.880	.082	.647	10.759	.000

a. Dependent Variable: Financial Performnce

b. Predictors: (Constant), Market Penetration Strategy

The model summary in table 3 presents the coefficient of determination (R^2) that implies that Market penetration strategy explains 41.8% of the variation in financial performance of the two tobacco manufacturing firms studied. The remaining variation of 58.2% is explained by other unobserved variables. Based on analysis of variances, the study established that market penetration strategy had a significant effect on financial performance of tobacco manufacturing firms in Kenya ($F= 115.765$, $p= .000< .05$) given that the p-value was less than 0.05 level of significance. Further, based on regression coefficients, the study established that market penetration had a significant and positive effect on financial performance ($\beta1=.880$, $t= 10.759$ and $p= .000<.05$). The study thus accepted the alternative hypothesis that there is a significant relationship between market penetration strategy and financial performance of Tobacco Manufacturing Firms in Kenya. The estimated model was thus shown in the equation [2].

$Y = .502 + .880X_1$ .... [2]

Where: Y = Financial Performance and X_1 = Market penetration strategy

4.5 Discussion of Results

The study examined the effect of market penetration on financial performance of two tobacco manufacturing firms in Kenya. The study established in table 4.12 that market penetration had a significant and positive effect on financial performance ($\beta1= .880$, $t= 10.759$ and $p= .000<.05$). The study thus accepted the alternative hypothesis that there is a significant relationship between market penetration strategy and financial performance of Tobacco Manufacturing Firms in Kenya. The study therefore concluded that market penetration had a major effect on financial performance of Tobacco Manufacturing Firms in Kenya and that increasing market penetration by the firm leads to increasing financial performance. The value ($\beta1= .880$) implies that increase in market penetration by one unit leads to increasing financial performance by .880 units. The findings of the study agrees with Kara (2014) on the association of market penetration and consistent performance with nonprofit service providers. They found a statistically significant and positive relationship between market entry and the performance of non-profit service providers. This finding was also supported by Narver and Slater (2018). Tse, Heung and Yin (2017) on the market penetration and performance showed a positive and significant relationship between entering the market and corporate performance. Martin-Consuegra and Estebon (2017) also indicated a positive and significant relationship between market entry and performance. Similarly, the market insights of Mamat and Ismail (2015) assessed the effectiveness of the Bumiputera furniture companies in Malanta. Their results showed a positive and significant correlation between cross-functional coordination of market penetration, competition orientation and profitability, sales growth rate and customer inventory.

V. CONCLUSION

Regarding the study objective, the study accepted the alternative hypothesis that there is a significant relationship between market penetration strategy and financial performance of Tobacco Manufacturing Firms in Kenya. The study therefore concluded that market penetration had a major effect on financial performance of Tobacco Manufacturing Firms in Kenya and that increasing market penetration by the firm leads to increasing financial performance. Given the positive effect of market penetration strategy on financial performance, the study recommends to management of tobacco manufacturing firms in Kenya to enhance their penetration into the society. The firms can enhance their market penetration through penetration pricing where lower prices are charged for new improved products to attract more customers. The study was on the effect of market penetration strategy on financial performance of tobacco manufacturing firms in Kenya. The study was thus limited to tobacco manufacturing firms with findings having limited application in the studied firms. The study thus recommends that future study should examined all manufacturing firms in Kenya for the purpose encouraging wide application of findings.

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