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CREDIT POLICY IMPLEMENTATION AND FINANCIAL PERFORMANCE OF MANUFACTURING COMPANIES IN LAGUNA

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ABSTRACT

The main focus of this study was to determine the credit policy implementation and its impact on the overall financial performance of manufacturing companies in Laguna. The findings of this study can be used as a reference in the formulation of good controls with sensible credit policies toward efficient working capital management and in achieving a value-enhancing balance between profitability and risk minimization. This study utilized the descriptive correlational research method design that enabled the study to determine the relationship between the level of credit policy implementation and the financial performance level of selected manufacturing companies in Laguna. This study used a stratified random sampling method, the respondents of the study were 163 employees in charge of credit and collection of manufacturing companies in SEPZ – PEZA Laguna. The study used a Researcher-made instruments in a form of questionnaire via google form to identify the credit policy implementation and financial performance level of selected manufacturing companies in Laguna.

Using the four-point Likert Scale, the simple mean, and Pearson product-moment correlation, findings revealed that the levels of credit policy implementation and the levels of financial performance were extremely high among the manufacturing companies in Laguna. It implies that there is a strong positive relationship between the two variables since the p-value is all less than .05. These are all indicators of good controls which fosters the ability to pay and it reduces the risk of receiving late payment or missed payments.

Keywords: credit policy, financial performance, sales volume, accounts receivable, collection

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INTRODUCTION

Manufacturing companies use trade credit in dealing with their customer to stay at a competitive advantage. The increased globalization and advancing technology offer a new opportunity to grow and expand market share The company needs to be clear about its stand on giving customer terms and collecting past-due payments. Without a strategy, there would be a liquidity problem that might lead negative effect on the company's growth and survival.

The credit policy is one of the most critical financial decisions and consists of establishing the terms and conditions for sales on credit. It includes standards for the customer qualification, collections procedure, and steps to be taken in case of a non-payment by the customers.

Many companies are extending credit to customers, a prominent marketing and financial management strategy. Trade credit creates accounts receivable that the company needs to collect in the future. Customer satisfaction will be the company's profit; this requires management to combine good controls and a sensible credit policy.

The Corporate Financial Officer (CFO) Selection team, a financial consulting services in the USA in the article dated September 20, 2020, entitled "Accounts Receivables: Getting Paid," Accounts Receivables are an on-demand topic for business owners because it is the primary driver of cash flowing into the company. 39% of invoices are paid late in the US, and clients have asked 52% of businesses to extend their payment terms. The longer the invoice is open, the less likely it is that company will receive payment. Bad debt disrupted the comp

any's cash flow and long-term profitability. Each year, an average of 4% of accounts receivable amortized as bad debt reduces a $10 million annual revenue by $ 400,000.

CRIF D&B Philippines, an expert in digital solutions, analytics, and credit information systems, arranged a seminar on "Managing Credit and Collection during a Pandemic" last February 16, 2021, emphasized the importance of reviewing and reexamining current credit and collection policies in light of the current difficult times. It was noted that as of June 2020, 38.3% of Philippine companies made their payments on time, which is a 5% decrease from the 43.30% statistics from December 2019.

CRIF D&B Philippines also provides "Credit and Collection Strategies and Tactics during Pandemic" which are applying customer segmentation, use of data analytics, streamlining operations and processes, and applying an Omni channel communication strategy. 44% of the working capital management was the main issue for MSMEs during the ongoing pandemic.

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More than half (59%) of micro, small and medium-sized enterprises (MSMEs) in Philippines consider working capital management an urgent concern, according to a survey by Divinagracia. The survey also revealed that 31% of large businesses and 43% of MSMEs expect liquidity issues if enhanced community isolation system is lifted.

ABC Philippines' cash management functions need to ensure faster collection of all receivables to avoid a working capital issue and payment defaults. The credit period for receiving cash ranges from a minimum of 30 days to a maximum of 90 days, depending on the company's size.

Finally, the main aim of this study was to examine the level of credit policy and its impact on the financial performance of ABC Philippines and how it was in comparison with the other manufacturing companies in Laguna. It showed how companies describe accounts receivable management as one of the implications of efficient working capital management to achieve a value-enhancing balance between profitability and risk minimization.

METHODS

The study utilized the descriptive correlational research method, which enabled the study to determine the relationship between the level of credit policy implementation and the financial performance level of selected manufacturing companies in Laguna located in Special Economic Processing Zone (SEPZ) registered under Philippine Economic Zone Enterprise (PEZA). The study was conducted during the academic Year 2021 – 2022.

The reliability of the data collection instrument for this study was determined by Cronbach's alpha between.791 and.859 > .05, which confirmed the "good" and "acceptable" internal consistency and reliability.

Data used in the investigation came from 65 employees assigned to credit and collection of manufacturing companies in SEPZ – PEZA Laguna. Only 54 respondents were able to accomplish and return the completed survey questionnaires. The study addressed specific ethical concerns before, during, and after the data gathering. The respondents were assured that all their personal data will be treated with the utmost confidentiality and for academic purposes only.

Participation of the respondents is voluntary and with their consent. Data collection took almost a month.

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The study used researcher-made instruments to obtain relevant information. The first part identified the level of implementation of the credit policy in terms of credit application and screening, credit terms, and

monitoring and collection which was measured using the Likert -Type Scale (Always/Fully Implemented-4, Often/Implemented -3, Rarely/Partially Implemented -2, Never/Not Implemented –1). The second part determined the level of financial performance in the implementation of credit policy. It was encoded as (Strongly Agree/Excellent-4, Agree/Good -3, Disagree/Average -2, Strongly Disagree/Poor–1).

The study used the mean and four-point Likert Scale to describe the level of credit policy implementation and level of financial performance in selected manufacturing companies. The Pearson product-moment correlation was used to determine the relationship between credit policy and the financial performance of the selected manufacturing firms. Regression analysis was used to determine the impact of credit policy implementation on the financial performance of companies.

RESULTS AND DISCUSSION

Discussion of the credit policy implementation and its impact on the financial performance of manufacturing companies in Laguna is presented in the succeeding tables and textual presentations:

Table 1.1 *Level of Credit Policy Implementation in terms of Credit Application and Screening*

Indicators	Mean	Interpretation
1. Updates credit policy periodically or as the need arises	3.41	FI
2. Uses the current credit policy in dealing with all customers on account	3.74	FI
3. Informs customer beforehand of the requirements (past cash transactions, the volume of the order, financial documents, etc.) to qualify in the application for a credit line	3.76	FI

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4. Processes credit applications from customers only upon submission of required documents.	3.70	FI
5. Conducts credit investigation protocols using in-house or outside services for the purpose.	3.56	FI
6. Reviews the applicant's transaction history and the result of credit investigation before approval/disapproval.	3.63	FI
7. Discusses with the applicant the result of their application for the credit line.	3.57	FI
General Assessment	**3.62**	**FI**

Legend: 3.25-4.00 Always - Fully Implemented (FI) 2.50-3.24 Often - Implemented(I)1.75-2.49 Rarely - Partially Implemented (PI) 1.00-1.74 Never - Not Implemented (NI)

It is shown in table 1.1 that that manufacturing companies in Laguna are able to implement good credit control practices as evidenced by the obtained general assessment of 3.62. This is in lieu of utilizing credit application and screening of data obtained from the customer. This is very important in making informed judgement prior granting credit limits to the customer which will affect the company's profitability.

In support of these findings, Omar, Muturi, and Samantar (2018) noted that the client appraisal has a positive relationship with the profitability of the Telecommunication Companies in Garowe Puntland, Somalia. It is also worth mentioning that it gives postpaid credit services (Internet, electricity, and Telephone Airtime) to the customers, so the study focused on postpaid services and how credit is managed, as well as the implications for company profitability.

Table 1.2 *Level of Credit Policy Implementation in terms of Credit terms*

Indicators	**Mean**	**Interpretation**
1. Offers trade discount for bulk orders received from the customer (Example: 10 or 10/5)	2.89	I

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2. Offers cash discount for early payment made by the customer (example): 2/10, n/30)	2.48	PI
3. Uses credit scoring to determine the credit limit	3.17	I
4. Monitors customers exceeding the credit limit	3.52	FI
5. Requires early payment for a customer that exceeds the credit limit	3.09	I
6. Increases credit limit to customers with good credit standing.	3.22	I
7. Provides penalty provisions in case of payment default	2.70	I
General Assessment	**3.01**	**I**

Legend: 3.25-4.00 Always - Fully Implemented (FI) 2.50-3.24 Often - Implemented (I) 1.75-2.49 Rarely - Partially Implemented (PI) 1.00-1.74 Never -Not Implemented (NI)

It is shown in table 1.2 , that the level of credit policy implementation in terms of the credit terms obtained a general assessment of 3.01**.**The results imply that most companies in Laguna have established credit limits as part of the credit control process to manage risk exposure.

In support of these findings, Kyambi and Muturi (2018) stated that manufacturers in Nairobi County, Kenya, are offering discounts as an incentive for early payments as part of their credit terms. As a result, credit policies generally affect the accounts receivable of Nairobi County manufacturing companies, and such policies should be carefully formulated to take advantage of the policy's implementation and thus improve performance.

Table 1.3 *Level of Credit Policy Implementation in terms of Monitoring and collection*

Indicators	Mean	Interpretation
1. Sets limit on the amount of credit provided to customers	3.46	FI
2. Analyzes Accounts Receivable Aging schedule at least once a month	3.76	FI

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3. Sends monthly Statement of Account to the customer	3.70	FI
4. Endorses the delinquent customer to Sales Team for collection assistance	3.43	FI
5. Provides online payment options	3.74	FI
6. Reminds customers of their past due accounts	3.81	FI
7. Charges interest on overdue accounts	2.69	I
8. Sends at least two notices per month for accounts that are 60 days past due	3.26	FI
9. Sends demand notice for accounts more than 90 days past due	2.91	I
10. Seeks legal action if payment is not received within 30 working days after the date of demand notice	2.59	I
General Assessment	**3.34**	**FI**

Legend: 3.25-4.00 Always - Fully Implemented (FI) 2.50-3.24 Often - Implemented (I) 1.75-2.49 Rarely Partially Implemented (PI) 1.00-1.74 Never -Not Implemented (NI)

It is shown in table 1.3 that the level of credit policy implementation in terms of the credit application and screening obtained a general assessment of 3.34.

It implies that most companies in Laguna have established procedures for monitoring and collecting particular reminders when the customer has past due accounts. This is a proactive way to avoid customer default in payment that may lead to the risk of non-payment.

According to Desiderio (2020) a survey by PwC Philippines, manufacturing companies are facing challenges in their working capital due to past due accounts which may result in a risk of non-payment of customers.

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Table 2.1 *Financial Performance Level in terms of Volume of Accounts receivable*

Indicators	Mean	Interpretation
1. Increased sales on credit	3.37	VS
2. Reduced uncollectible accounts, collection cost, and investigation cost	3.33	VS
3. Increased Accounts Receivable collection	3.52	VS
4. Maintained a lower ratio of accounts receivable to sales.	3.30	VS
5. Increased number of customers who availed of early payment discounts	3.26	VS
General Assessment	**3.36**	**VS**

Legend: 3.25 - 4.00 Strongly Agree – Very Satisfactory (VS) 2.50 - 3.24 Agree -Satisfactory (S) 1.75 - 2.49 Disagree – Fairly Satisfactory (FS) 1.00 - 1.74 Strongly Disagree - Unsatisfactory U)

It is shown in table 2.1 that the financial performance level in terms of volume of accounts receivable obtained a general assessment of 3.36

It implies an increase in cash inflow and indicates the company's liquidity, enabling the company to pay its obligation as it falls due which is very significant to the financial performance of the company as a whole. In addition, it means a good indication of credit and collection practices as it lowers the average collection period and a high chance of debt recovery.

In support of these findings, Cheptum (2019) indicates that credit collection practices have a significant positive impact on the financial performance of manufacturing firms in Kenya ($p<0.05$). This could be because manufacturers can control and manage credit through knowledgeable and experienced credit managers. To summarize, debt collection activities have had a significant and positive impact on company financial performance.

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Table 2.2 *Financial Performance Level in terms of Average Collection Period*

Indicators	Mean	Interpretation
1. Maintains an average collection of 30 days	3.35	VS
2. Increases collection effort	3.61	VS
3. Customers pay on or before the due date.	3.44	VS
4. Reduces grace period of collection to a minimum	3.24	S
5. Real-time posting of collection	3.69	VS
General Assessment	**3.47**	**VS**

Legend: 3.25 - 4.00 Strongly Agree – Very Satisfactory (VS) 2.50 - 3.24 Agree - Satisfactory (S) 1.75 - 2.49 Disagree – Fairly Satisfactory (FS) 1.00 - 1.74 Strongly Disagree - Unsatisfactory (U)

It is shown in table 2.2 that the financial performance level in terms of volume of accounts receivable obtained a general assessment of 3.47 It implies that the company has an efficient collection process and the lower the average collection period the shorter the cash cycle of the business is, which has a positive impact on its profitability. Real-time posting and reduction in grace period collection is an indication of good credit and collection practices that will mitigate lower credit risk.

In support of this, Munene (2018) found in the study that there is a strong positive and statistically significant correlation between EWASCO's average collection period and financial performance in Embu County, Kenya, in terms of the average collection period. The relationship between the number of days, net credit sales, and accounts receivable was also important, EWASCO improves financial performance by minimizing average collection time

Table 2.3 *Financial Performance Level in terms of sales volume*

Indicators	Mean	Interpretation
1. Keeps customers informed of improvements to existing products	3.72	VS

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2. Develops new line of products for new/existing customers	3.67	VS
3. Provides value-added services to clients	3.65	VS
4. Encourages customers to avail of trade and cash discounts	3.39	VS
5. Delivers good on time	3.65	VS
6. Expands market share by lowering its prices	3.39	VS
7. Meets customer's demand for an increase in credit limit	3.46	VS
General Assessment	**3.56**	**VS**

Legend: 3.25 - 4.00 Strongly Agree – Very Satisfactory (VS) 2.50 - 3.24 Agree - Satisfactory (S) 1.75 -2.49 Disagree – Fairly Satisfactory (FS) 1.00 - 1.74 Strongly Disagree - Unsatisfactory (U)

It is shown in table 2.3 that the financial performance level in terms of volume of accounts receivable obtained a general assessment of 3.56

It implies that there is effectiveness in the selling effort of the company thru improvement, and expansion of market share by offering a discount percentage to attract customers. This is a favorable impact on the profitability of the company as it increases sales volume.

In support of the findings, Kyambi and Muturi (2018) mentioned that many companies use all forms of programs, offering trade credit being one such program, to attract new customers to their products and/or maintain existing market share. In this type of competition, manufacturing executives have a real incentive to use product promotion strategies to reduce their inventory to market in the hope of converting it into a successful sales transaction and building customer loyalty.

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Table 3 *Test of a significant relationship between credit policy implementation and the financial performance*

Credit Policy Implementation	The Financial Performance	r value	P- value	Remarks	Decision
Credit application and screening	Volume of Accounts receivable	.440**	0.001	Significant	Reject H_o
	Average Collection Period	.578**	0.000	Significant	Reject H_o
	Sales volume	.430**	0.001	Significant	Reject H_o
Credit terms	Volume of Accounts receivable	.395**	0.003	Significant	Reject H_o
	Average Collection Period	.391**	0.003	Significant	Reject H_o
	Sales volume	.412**	0.002	Significant	Reject H_o
Monitoring and collection	Volume of Accounts receivable	.462**	0.000	Significant	Reject H_o
	Average Collection Period	.389**	0.004	Significant	Reject H_o
	Sales volume	.424**	0.001	Significant	Reject H_o

**. Correlation is significant at the 0.01 level *. Correlation is significant at the 0.05 level (2-tailed).

It is shown in table 3 that that there is a significant relationship between the credit policy implementation and the financial performance. The probability values are all less than the level of significance at .05 thus rejecting the null hypothesis.

It implies that there is a strong positive relationship between the two variables since the p-value are all less than .05. Informing customers beforehand of the requirements (past cash transactions, the volume of the order, financial documents, etc.) influences the average collection period by 57.80%. Also reminding the customer of their past due accounts and monitoring customers exceeding credit limits increases the accounts receivable collection by 46.20% and 39.50% respectively. These are all indicators of good controls which fosters the ability to pay and it reduces the risk of receiving late payment or missed payments.

In support of the findings, Munene (2018) found in the study that there is a strong positive and statistically significant correlation between EWASCO's average payment period and financial performance in Embu County, Kenya, in terms of the accounts receivable, net credit sales and number of sales. The average collection period was found to have a significant positive relationship with EWASCO's financial performance in Embu County, indicating that increasing the period of debtor's payment improves the overall financial performance of Embu Water and Sanitation Company Limited in Embu County, Kenya.

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Table 4.1 *Regression Analysis on the impact of the level of credit policy implementation on the financial performance in terms of Volume of Accounts Receivables*

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Remarks	Decision
	B	Std. Error	Beta				
(Constant)	1.937	0.39		4.967	0.000		
Credit application	0.182	0.145	0.222	1.259	0.214	Not Significant	Accept H_o
Credit terms	0.022	0.111	0.040	0.198	0.844	Not Significant	Accept H_o
Monitoring	0.208	0.163	0.275	1.273	0.209	Not Significant	Accept H_o

Dependent Variable: Volume of accounts receivables
R – Square = .668
Adjusted R Square = .655
F-value = 51.524
Significance =.000

It is shown in table 4.1 that the impact on the level of credit policy implementation in terms of Volume of accounts receivables has no variable significantly impacts financial performance. Since the probabilities are all higher than the level of significance at.05, the null hypothesis is accepted.

It implies that granting credit terms will increase accounts receivable. Increasing payment terms will increase sales and accounts receivable, which means that the company needs a credit line or other financing to record these amounts in accounts receivable and pay invoices in some cases. Shortening the loan period has the opposite effect.

In support of this, Azman and Ramakrishnan (2021) confirmed in their study that receivable management does not significant impact on firm performance (B=0.142, t-value is. 0.684, P>0.05) which concluded that most firms in Malaysia do not focus on receivable efficiency but rather to payable management.

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Table 4.2 *Regression Analysis on the impact of the level of credit policy implementation on the financial performance in terms of Average Collection Period*

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Remarks	Decision
	B	Std. Error	Beta				
(Constant)	1.595	0.412		3.876	0.000		
Credit application	0.541	0.153	0.584	3.544	0.001	Significant	Reject H_o
Credit terms	0.056	0.117	0.09	0.482	0.632	Not Significant	Accept H_o
Monitoring	-0.077	0.172	-0.09	-0.447	0.657	Not Significant	Accept H_o

Dependent Variable: Average Collection
R – Square = .338
Adjusted R Square = .298
F-value = 8.498
Significance =.000

Table 4.2 based on the table, Credit applications significantly impact the financial performance. The probability value of **.001** is less than the level of significance at .05, thus rejecting the null hypothesis. The Credit application and screening significantly impact the financial performance by 33.8 %.

The relationships ($p < 0.05$) are significant with average collection period ($\beta=0.584$, $p < 0.05$. It shows that the average collection period reflects the effectiveness of accounts receivable management practices, particularly in the processing of credit applications and screening. This is the first step in the screening process so the company should be vigilant in extending credit to customers.

In support of these findings, Fidelis, A., & Umoffong's (2020), study shows that the average collection period (ACP) has a positive and significant financial performance for listed consumer goods companies in Nigeria. The variable's average collection period (ACP) coefficient is found to be positive and significant (2ACPit = 0.00561, t-Statistic=0.267). This indicates that the average collection period has a significant impact on a firm's profitability.

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Table 4.3 *Regression Analysis on the impact of the level of credit policy implementation on the financial performance of the selected manufacturing companies in Laguna in terms of* ***sales volume***

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Remarks	Decision
	B	Std. Error	Beta				
(Constant)	2.158	0.424		5.087	0.000		
Credit application	0.206	0.157	0.234	1.312	0.196	Not Significant	Accept H_o
Credit terms	0.092	0.12	0.154	0.762	0.450	Not Significant	Accept H_o
Monitoring	0.114	0.178	0.14	0.640	0.525	Not Significant	Accept H_o

Dependent Variable: Sales volume
R – Square = .223
Adjusted R Square = .177
F-value = 4.791

Table 4.3 shows the Regression Analysis of the impact of the level of credit policy implementation on the financial performance of the selected manufacturing companies in Laguna in terms of sales volume. Based on the table, no variable significantly impacts financial performance. The probability values are all greater than the level of significance at .05, thus accepting the null hypothesis.

It implies that there are companies that lower their credit standing to boost sales but they also increase bad debts. When standards are set too low, bad debt losses are too high; on the other hand, when standards are set too high, the firm loses sales and thus profits. As a result, a balance must be maintained between the costs and benefits of strict credit standards.

In support of these findings, Musa, Kyari, Abba, and Babagana (2017) investigated the relationship between credit management and the profitability of manufacturers using listed companies on the Nigerian Stock Exchange. The study shows a negative relationship between credit policy and manufacturing profitability, based on statistics of 0.36 and a p-value of 0.72. The results show that credit policy and liquidity management have no significant relationship to manufacturing profitability.

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Conclusions

The manufacturing companies in Laguna can implement good credit control practices utilizing credit application and screening of data, established credit limits, monitoring and collection.

On the other hand, some companies do not offer a cash discount for early payment maybe because of the effect on revenues brought by the reduction in price. When establishing a credit policy, the benefits and costs of discounts must be balance.

While the financial performance of manufacturing companies in Laguna in particular the volume of accounts receivable collection, average collection period, and sales volume are all indications of good credit and collection practices that will mitigate lower credit risk.

Congruently credit policy has a relationship with the financial performance of the selected manufacturing companies in Laguna, specifically the average collection period, measures the effectiveness of accounts receivable management strategies, particularly in the handling of credit applications and screening. Whereas the other variable does not significantly impact the financial performance of manufacturing companies in Laguna.

Recommendations

The present investigation has some limitations particularly on the sample size which was used in the study since it was only limited to the manufacturing companies located in SEPZ-PEZA Laguna

A larger population study may be conducted to consider across industries to make more comprehensive inferences on the effect of credit policies on the financial performance of manufacturing companies. Companies may adapt the output of this study to improve financial performance in the new normal.

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