A Free Cash Flow Theory Perspective on the Nexus Between Cash Management and Return on Equity: Evidence from Nigerian Food and Beverage Firms

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Abstract
Poor cash management can prevent companies from reinvesting surplus funds into high-return opportunities, which ultimately harms shareholder value and diminishes financial performance. To address this problem, this study examined the extent to which cash management affects return on equity of listed food and beverages firms in Nigeria based on the postulations of free cash flow theory. Ex-post facto research design was deployed in the study while the population comprised seventeen listed food and beverages firms listed on the Nigerian exchange group. Secondary data were extracted from the published financial statements of the thirteen sampled firms over a period of twelve years, spanning 2012 to 2023. Hypotheses were tested using Period Seemingly Unrelated Regression. It was found that increase in cash ratios significantly reduces the return on equity of listed food and beverage firms in Nigeria (b = -0.084507; p-value = 0.000000). In conclusion, while maintaining liquidity is essential for operational stability, an overly conservative approach to cash retention could limit firms' ability to seize profitable investment opportunities, and thereby impairing their financial performance. This conclusion implies that financial managers should adopt an optimal cash management strategy that balances liquidity and profitability by ensuring that excess cash is efficiently deployed into productive investments rather than being retained unnecessarily.

Keywords: *Cash Management, Return on Equity, Free Cash Flow Theory*

1.0 Introduction

Cash management is an integral part of corporate financial management that deals with the collection, allocation, and usage of funds to ensure smooth operational flow while maximizing the overall financial performance of a business. The importance of cash management is particularly emphasized in capital-intensive industries such as food and beverage firms, where liquidity and operational efficiency play significant roles in achieving long-term sustainability and profitability (Umar, Al-Faryan & Osemy, 2025). According to Moneke and Ezeagba

(2024) and Boloupremo and Umbe (2024), cash management practices are pivotal in making sure that a company has sufficient cash flow to meet its short-term obligations while also planning for future investments, ensuring it does not have excess idle cash that could otherwise be used for growth. As businesses operate in an environment of increasing uncertainty, companies must optimize their cash flow to achieve both profitability and solvency (Njore & Ndede, 2024). Poor cash management can lead to liquidity crises, forcing firms to resort to costly external financing or even bankruptcy. Effective cash management, on the other hand, provides firms with the ability to make strategic investments, optimize working capital, and ensure the efficient utilization of resources, which in turn enhances profitability and financial performance (Bari, Muturi & Samantar, 2019). This holds particular significance for food and beverage firms, which often face volatile demand, seasonality, and price fluctuations in raw materials, all of which can put pressure on their cash flow management strategies.

Cash management plays a crucial role in ensuring that a firm is financially stable, which in turn enables the firm maintain an optimal balance between liquidity and profitability. Financial stability is vital, as it provides these firms with the flexibility to weather economic downturns, invest in growth opportunities, and return profits to shareholders (Nworie & Ofoje, 2022). Cash management influences a firm's return on equity by shaping its operational liquidity and influencing decisions regarding reinvestment, debt management, and capital structure. Return on equity is a crucial financial metric that measures a company's profitability relative to shareholders' equity. Effective cash management ensures that a company has sufficient liquidity to capitalize on profitable investment opportunities (Njore & Ndede, 2024), which in turn boosts profitability and, ultimately, ROE. The Free Cash Flow (FCF) theory suggests that firms with excess free cash flow have more discretion in how they allocate their funds, which could be used to generate returns through strategic investments or used inefficiently, resulting in lower ROE.

The Free Cash Flow Theory posits that when firms generate more cash than they can profitably reinvest, managers may divert funds into suboptimal projects, often leading to reduced firm value (Umar, Al-Faryan & Osemy, 2025). However, by focusing on managing cash effectively, businesses can avoid such inefficiencies. The theory emphasizes the importance of managing excess cash and allocating it towards investments that yield high returns or repaying debt that would reduce the firm's cost of capital, improving its financial performance. Cash management practices aligned with this theory focus on minimizing the cash held idle (Misrah & Sari, 2025), increasing returns on assets, and improving shareholder value, all of which positively affect ROE.

Maintaining an optimal balance between cash inflows and outflows enables firms to meet their operational needs without over accumulating idle cash. Moreover, effective cash management would ensure that firms are able to reinvest surplus funds in high-return opportunities, thereby enhancing shareholder value and improving their financial performance (Njore & Ndede, 2024). However, many food and beverages firms face significant challenges in managing their cash flows due to a range of factors, such as economic instability, inflationary pressures, volatile exchange rates, and inconsistent consumer demand. As a result, these firms often struggle to maintain adequate liquidity, leading to cash shortfalls or inefficient use of available funds (Bari, Muturi & Samantar, 2019).

As a result, poor cash management practices can lead to increased reliance on costly external financing, which in turn reduces profitability and lowers ROE. Furthermore, firms may miss out on investment opportunities due to a lack of liquidity or might face difficulties in meeting their short-term obligations. This could harm the company's reputation, reduce investor confidence, and make it difficult for the firm to sustain its operations or expand in the future. In the worst case, ineffective cash management can lead to financial distress, increased debt levels, and ultimately, business failure (Umar, Al-Faryan & Osemy, 2025), hence the need for this study to proffer recommendations on how to address the problem.

1.1 Objective of the study

The main aim of the study is to examine the extent to which cash management affects return on equity of listed food and beverages firms in Nigeria based on postulations of free cash flow theory.

2.0 Literature Review

2.1 Conceptual Issues

2.1.1 Cash Management

Cash management refers to the process of managing a company's financial resources to ensure it has sufficient liquidity to meet its short-term obligations while optimizing the use of its available cash for operations and investments (Oroniran, Abdullahi & Olanisebe, 2023). This involves the effective planning, monitoring, and control of cash inflows and outflows to ensure that the company operates efficiently without facing liquidity crises. According to Bari, Muturi, and Samantar (2019), cash management is a critical component of corporate financial management because it directly impacts a firm's ability to maintain operations, fulfill financial commitments, and create shareholder value. Proper cash management ensures that a firm can pay its bills, meet payroll obligations, invest in profitable ventures, and maintain solvency, all while avoiding the costs associated with holding excessive amounts of idle cash or relying on expensive short-term borrowing (Boloupremo & Umbe, 2024).

The importance of cash management is underscored by the fact that cash is the lifeblood of a business (Kingma, 2024). Without effective management of cash, even profitable companies can run into financial difficulties if they do not have sufficient liquidity to cover day-to-day expenses. Cash management requires constant monitoring of cash flow, which refers to the movement of cash into and out of the business, often stemming from operations, investments, or financing activities (Dibie, 2022). It requires businesses to track cash receipts and disbursements carefully and plan for future cash requirements. The goal is to balance having enough cash on hand to run the business smoothly, while also minimizing the opportunity cost of holding excess cash that could be invested or used elsewhere. Effective cash management also involves making informed decisions regarding the timing and scale of investments in short-term or long-term assets (Nasimiyu, 2023), as well as determining how much cash should be held in reserve to meet unforeseen expenses or opportunities. This practice can help a company reduce its reliance on debt financing, lower its cost of capital, and improve its creditworthiness in the eyes of investors, creditors, and other stakeholders. Additionally, well-managed cash flow can be a source of competitive advantage for a firm, as it provides the flexibility to act quickly in response to changes in the market or opportunities for growth (Oroniran, Abdullahi & Olanisebe, 2023). Without an efficient cash management strategy,

businesses risk falling into financial distress, hampering their ability to generate returns and grow sustainably.

2.1.2 Return on Equity

Return on equity (ROE) is a key financial metric that measures the profitability of a company relative to the equity invested by its shareholders (Owolabi, 2022). It is an indicator of how effectively a company is using the capital invested by its shareholders to generate profits. ROE is calculated by dividing the company's net income by its shareholder equity, usually expressed as a percentage (Oroniran, Abdullahi & Olanisebe, 2023). The higher the ROE, the more efficient the company is at converting the investment capital into profits. As such, it is one of the most widely used metrics by investors, analysts, and financial managers to assess a company's financial performance and potential for future growth.

ROE is a comprehensive measure of a company's ability to generate profits from its equity base. It reflects the effectiveness of management in utilizing shareholder investments to produce earnings and provides hint on the firm's overall financial health. Investors often use ROE to evaluate how much return they are getting for every unit of equity they invest (Owolabi, 2022). A high ROE indicates that a company is effective in utilizing its equity base to generate income, which is typically seen as a sign of efficient management, strong profitability, and the potential for good returns. Conversely, a low ROE may signal inefficiencies in utilizing equity, indicating that the company is not using its resources effectively to produce profits. Return on equity is also important because it shows how well a company is managing its leverage. It is a reflection not just of the company's operating performance but also its capital structure. When a firm uses debt financing, it can increase its ROE by leveraging borrowed funds to boost earnings without increasing equity capital.

2.2 Theoretical Framework and Development of Research Hypothesis

The Free Cash Flow Theory, first propounded by Michael Jensen in 1986, emphasizes the relationship between free cash flow (FCF) and firm value (Misrah & Sari, 2025), focusing on the conflicts that arise between managers and shareholders when firms generate more cash than they can effectively reinvest. In his seminal work, "Agency Costs of Free Cash Flow, Corporate Finance, and Takeovers," Jensen proposed that firms with excess free cash flow face the risk of managers engaging in wasteful spending, as they may allocate funds to projects that do not maximize shareholder value (Jensen, 1986). The theory highlights the role of free cash flow in corporate decision-making, arguing that surplus cash should be either paid out to shareholders or used in profitable investments, rather than being retained by management for inefficient or self-serving purposes (Umar, Al-Faryan & Osemy, 2025). Jensen's work has been highly influential in corporate finance, providing a foundation for understanding agency costs and the implications of excess cash on firm performance.

The key postulations of the Free Cash Flow Theory are centered on the notion that the availability of free cash flow influences managerial behavior and ultimately impacts a company's value (Misrah & Sari, 2025). The theory suggests that when a firm generates excess cash—after meeting its operating expenses and necessary investments—it faces a critical decision: either return that cash to shareholders in the form of dividends or share repurchases, or reinvest it into the business. If management does not utilize the surplus effectively, it may invest in projects that do not add value, leading to agency problems, where the interests of managers diverge from those of shareholders (Jensen, 1986). The theory proposes that firms

with abundant free cash flow are at risk of managerial over-investment, which can lead to reduced returns on equity, as funds are allocated inefficiently. Therefore, controlling free cash flow through effective management practices is crucial to ensuring that the firm maximizes shareholder wealth and minimizes inefficiencies (Misrah & Sari, 2025).

The Free Cash Flow Theory is highly relevant to the topic of cash management and return on equity in Nigerian food and beverage firms. Cash management, as a practice, directly impacts the availability of free cash flow within a firm. By efficiently managing cash inflows and outflows, food and beverage firms can ensure that excess cash is not generated in the first place, or, if it is, that it is allocated optimally to maximize shareholder value. From the perspective of the Free Cash Flow Theory, firms with effective cash management practices will reduce the likelihood of agency problems, ensuring that surplus cash is either reinvested in high-return projects or returned to shareholders, rather than being wasted (Umar, Al-Faryan & Osemy, 2025). Based on the postulations of the theory, we hypothesise that:

Increase in cash ratio will significantly reduce the return on equity of listed food and beverages firms in Nigeria.

2.3 Synthetic Empirical Review

The empirical findings on the relationship between cash management and financial performance across various sectors and countries present a mix of positive and negative associations. Several studies, particularly those focused on the food and beverage sector in Nigeria, highlight a negative correlation between the cash conversion cycle and financial performance. For instance, Boloupremo and Umbe (2024) and Olorunfemi, Opusunju, and Jiya (2020) reported that a longer cash conversion cycle negatively impacts return on assets (ROA) in food and beverage firms. This contradicts the findings of Adekanmi, Odewole, and Adeoye (2022), who found a significant positive effect of the cash conversion cycle on financial performance, suggesting that efficient liquidity management can enhance profitability. Additionally, studies such as those by Owolabi (2022) and Odo and Ohazuluike (2021) provide evidence that current and cash flow ratios positively impact return on equity and profit, reinforcing the argument that effective cash flow management is critical for financial success.

In contrast, findings from studies in the industrial goods and consumer goods sectors indicate a negative impact of cash management measures on financial performance. Moneke and Ezeagba (2024) reported a negative effect of cash and cash equivalents on return on assets in industrial goods firms, implying that excessive liquidity may not always translate to profitability. Similarly, Oroniran, Abdullahi, and Olanisebe (2023) found that cash flow from operating and investing activities had a negative impact on profitability, whereas financing activities had a positive effect in consumer goods firms. Further reinforcing this trend, Nworie, Moedu, and Onyali (2023) demonstrated that the cash ratio negatively influenced earnings per share, while debtor and inventory turnover ratios had a positive impact. These findings suggest that while managing liquidity is crucial, an excessive cash buffer may limit potential investment opportunities, thereby reducing financial performance.

In the broader context, studies beyond Nigeria, such as Bari, Muturi, and Samantar (2019), emphasize the volatility of cash management in food and beverage retailing, where fluctuating market trends and inconsistent liquidity ratios hinder firms' ability to meet financial

obligations. Meanwhile, Duru, Okpe, and Okolo (2017) highlight the importance of operating cash flow, showing its positive and significant impact on profit after tax in food and beverage firms. However, investing and financing cash flows were found to have no significant effects, indicating that not all components of cash flow contribute equally to financial performance. These contrasting perspectives suggest that while effective cash management is critical, its impact varies depending on industry dynamics, firm-specific strategies, and economic conditions.

2.4 Gap in Literature

There is an extensive empirical research on cash management and financial performance, but they have not sufficiently addressed some significant gaps remaining in the literature. Prior studies, such as those by Boloupremo and Umbe (2024) and Olorunfemi, Opusunju, and Jiya (2020), have primarily focused on the cash conversion cycle's impact on profitability, with mixed results. Similarly, Moneke and Ezeagba (2024) and Oroniran, Abdullahi, and Olanisebe (2023) examined cash flow components but emphasized return on assets and overall profitability rather than return on equity (ROE). While studies like Owolabi (2022) explored the relationship between cash flow and ROE, the methodologies used, such as panel regression and Hausman and Kao tests, differ from the Period Seemingly Unrelated Regression (PSUR) employed in this study. Additionally, research by Adekanmi, Odewole, and Adeoye (2022) and Odo and Ohazuluike (2021) focused on liquidity and cash flow but did not comprehensively analyze the impact of cash management within the theoretical framework of free cash flow theory. Furthermore, studies like Bari, Muturi, and Samantar (2019) considered retail firms in Somalia, leaving a gap in country-specific findings relevant to Nigeria. Given these limitations, this study fills a crucial gap by specifically examining the extent to which cash management affects ROE in listed food and beverage firms in Nigeria using PSUR analysis over a twelve-year period, aligning with the principles of free cash flow theory.

3.0 Methodology

This study employed an ex-post facto research design, which was suitable for examining events that had already occurred (Nworie & Orji-Okafor, 2024; Okafor, Nworie & Muojekwu, 2024). Since the data on cash management and return on equity (ROE) were historical, the design was appropriate for analyzing the relationship between cash ratio and ROE without any need for manipulation or alteration of variables. The ex-post facto design was also cost-effective and time-efficient for the purpose of this study. The population of the study consisted of all food and beverage firms that were listed on the Nigerian Exchange Group (NGX) as of December 2023. A total of 17 listed food and beverage firms in the NGX were identified, as shown in Table 3.1.

Table 3.1: Population of the Study

1. Bua Foods Plc
2. Cadbury Nigeria Plc
3. Champion Brew. Plc.
4. Dangote Sugar Refinery Plc
5. Flour Mills Nig. Plc.
6. Golden Guinea Brew. Plc.
7. Guinness Nig Plc

8. Honeywell Flour Mill Plc
9. International Breweries Plc.
10. Mcnichols Plc
11. Multi-Trex Integrated Foods Plc
12. N Nig. Flour Mills Plc.
13. Nascon Allied Industries Plc
14. Nestle Nigeria Plc.
15. Nigerian Brew. Plc.
16. Unilever Nigeria Plc.
17. Union Dicon Salt Plc.

Source: Nigerian Exchange Group (2023)

Purposive sampling was used to select firms listed on the NGX as of 2012. This ensured that a balanced panel data set was available for analysis over the study period. Thirteen (13) firms were selected, as shown in Table 3.2.

Table 3.2: Sample Size

1. Cadbury Nigeria Plc.
2. Champion Brewery Nig. Plc.
3. Dangote Sugar Refinery Plc.
4. Flour Mills Nig. Plc.
5. Guinness Nig. Plc
6. Honeywell Flour Mill Plc.
7. International Breweries Plc.
8. Northern Nig. Flour Mills Plc.
9. Nascon Allied Industries Plc.
10. Nestle Nigeria Plc.
11. Nigerian Breweries Plc.
12. Unilever Nigeria Plc.
13. Union Dicon Salt

Source: Researcher's compilation (2025)

The study used secondary data from the published financial statements of the selected food and beverage firms listed on the Nigerian Exchange Limited (NGX) for the period from 2012 to 2023. These financial reports provided the necessary information on cash management (proxied by cash ratio) and return on equity (ROE) for analysis. The collected data were analyzed using descriptive statistics and period seemingly unrelated regression analysis. Descriptive statistics were used to summarize the data, including mean, maximum, minimum, and standard deviation. Pesaran CD was used to ascertain whether there was an issue of cross-sectional dependence test in the model. The null hypothesis is rejected if the p-value is less than 1% (0.01) and accepted if the p-value was greater than 1% (0.01).

This regression model tested is shown as follows:

$ROE_{it} = \beta_0 + \beta_1 CAR_{it} + \mu_0$ ……..…(1)

Where:

ROE = Return on Equity;

CAR = Cash Ratio;

B_1 = Beta coefficient that measures the sensitivity of cash ratio to changes in ROE;

β_0 = Constant;

μ_0 = Error term.

Table 3.3 shows the measurement of the variables.

Table 3.3: Measurement of Variables

Variable	Measurement
Return on Equity (ROE)	Net income / Shareholders' equity
Cash Ratio (CAR)	Cash and cash equivalents / Current liabilities

Source: Researcher's Compilation, 2025

4.0 Data Analysis

4.1 Descriptive Analysis and Model Diagnostics

Table 4.1 shows the descriptive analysis of the data.

Table 4.1 Descriptive Analysis

	ROE	CAR
Mean	0.096343	0.315069
Median	0.097128	0.179807
Maximum	1.872808	1.677621
Minimum	-3.723443	0.000138
Std. Dev.	0.536586	0.346812
Skewness	-3.309770	1.988167
Kurtosis	25.97429	6.621435
Jarque-Bera	3715.636	188.0192
Probability	0.000000	0.000000
Sum	15.02957	49.15072
Sum Sq. Dev.	44.62831	18.64316
Observations	156	156

Source: Analysis Output (2025)

Table 4.1 shows that the mean value of Return on Equity (ROE) is 0.096343, indicating that, on average, listed food and beverage firms in Nigeria achieved a return of approximately 9.63% on their shareholders' equity during the period under study. The maximum value of ROE is 1.872808, which suggests that the highest-performing firm experienced a return of approximately 187.28% on equity. On the other hand, the minimum value is -3.723443,

indicating that some firms experienced a loss of approximately 372.34% on their equity, which is a substantial negative return. The standard deviation of 0.536586 indicates considerable variability in ROE among the firms, with some firms performing significantly better or worse than the average. The negative skewness of -3.309770 indicates a highly left-skewed distribution, meaning that there are more firms with lower returns on equity than higher returns. The kurtosis value of 25.97429 suggests a very leptokurtic distribution, meaning that there are extreme outliers in the data. Finally, the Jarque-Bera test for normality has a probability of 0.000000, indicating that the ROE data does not follow a normal distribution, with a strong departure from normality.

The mean value of the Cash Ratio (CAR) is 0.315069, which indicates that, on average, the selected food and beverage firms in Nigeria hold cash and cash equivalents that are about 31.51% of their current liabilities. The maximum value is 1.677621, which indicates that the firm with the highest cash ratio has cash holdings approximately 167.76% of its current liabilities. The minimum value of 0.000138 is extremely low, almost zero, showing that some firms have very little cash or cash equivalents relative to their current liabilities. The standard deviation of 0.346812 indicates moderate variation in the cash ratio across firms. The skewness value of 1.988167 indicates that the distribution is positively skewed, meaning most firms have a relatively lower cash ratio, but there are a few with much higher cash holdings relative to their liabilities. The kurtosis value of 6.621435 suggests that the distribution is leptokurtic, with more firms clustered around the mean but with some firms displaying extreme values. The Jarque-Bera test for normality also has a probability of 0.000000, implying that the data for the cash ratio significantly deviates from a normal distribution.

Table 4.2 Residual Cross-Section Dependence Test

Null hypothesis: No cross-section dependence (correlation) in residuals
Equation: Untitled
Periods included: 12
Cross-sections included: 13
Total panel observations: 156

Test	Statistic	d.f.	Prob.
Pesaran CD	2.229309		0.0258

Source: Analysis Output (2025)

Table 4.2 presents the results of the Residual Cross-Section Dependence Test, with the null hypothesis stating that there is no cross-section dependence (or correlation) in the residuals. The Pesaran CD test statistic is 0.0258, with a p-value of 0.0258. Since the p-value is less than the conventional threshold of 0.05, we reject the null hypothesis, implying that there is significant cross-sectional dependence in the residuals. This means that the errors from the different firms in the sample are correlated, which is an important consideration in panel data models, as it could indicate that unobserved factors affect multiple firms simultaneously. This finding suggests that further steps should be taken to account for this cross-sectional dependence, such as using robust standard errors, hence the justification for the use of period seemingly unrelated regression analysis.

4.2 Test of Hypothesis

Ha: *Increase in cash ratio will significantly reduce the return on equity of listed food and beverages firms in Nigeria.*

Table 4.3 Test of Hypothesis
Dependent Variable: ROE
Method: Panel EGLS (Period SUR)
Date: 03/07/25 Time: 04:07
Sample: 2012 2023
Periods included: 12
Cross-sections included: 13
Total panel (balanced) observations: 156
Linear estimation after one-step weighting matrix

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CAR	-0.084507	0.006932	-12.19011	0.0000
C	0.071760	0.006172	11.62692	0.0000

Weighted Statistics

R-squared	0.490491	Mean dependent var	0.298923
Adjusted R-squared	0.487183	S.D. dependent var	1.622538
S.E. of regression	1.001170	Sum squared resid	154.3605
F-statistic	148.2518	Durbin-Watson stat	1.994148
Prob(F-statistic)	0.000000		

Source: Analysis Output (2025)

The regression results in Table 4.3 show the nexus between the Cash Ratio (CAR) and Return on Equity (ROE) for listed food and beverage firms in Nigeria. The model has an R-squared value of 0.490491, indicating that approximately 49.05% of the variation in ROE can be explained by the cash ratio, which is a moderate explanatory power. The Prob(F-statistic) of 0.000000 indicates that the overall model is statistically significant at the 1% level. The Durbin-Watson statistic of 1.994148 suggests that there is no significant autocorrelation in the residuals, which is a positive sign for the reliability of the model. The constant term (C) is 0.071760, meaning that when the cash ratio is zero, the expected value of ROE is 7.18%. This indicates the baseline return on equity for firms when no cash is held in excess of current liabilities.

The coefficient of the Cash Ratio (CAR) is -0.084507, meaning that for every 1-unit increase in the cash ratio, ROE is expected to decrease by 8.45%. This negative coefficient suggests that an increase in the proportion of cash holdings relative to current liabilities is associated with a decrease in return on equity. The p-value for this coefficient is 0.0000, which is less than the 1% significance level, indicating that this effect is statistically significant. This suggests that

increase in cash ratios significantly reduces the return on equity of listed food and beverage firms in Nigeria (b = -0.084507; p-value = 0.000000).

4.3 Discussion of Findings

The findings, which indicate that an increase in cash ratio significantly reduces the return on equity (b = -0.084507; p-value = 0.000000), align with the Free Cash Flow (FCF) Theory. The theory posits that excess cash holdings, when not effectively utilized for value-enhancing investments, may lead to inefficiencies, managerial opportunism, or suboptimal capital allocation. In the case of listed food and beverage firms in Nigeria, maintaining high cash reserves may suggest that firms are not deploying their liquid assets into productive ventures such as expansion, innovation, or dividend payouts, which could enhance shareholder value. Instead, excessive cash holdings may encourage managerial complacency, reduce financial discipline, and increase agency costs, ultimately leading to lower returns on equity. Additionally, firms with high liquidity might experience a trade-off between profitability and liquidity, as excessive cash retention can result in foregone investment opportunities and lower earnings potential. This explains why firms with higher cash ratios tend to experience reduced ROE, as they may not be leveraging their cash efficiently to generate higher returns for shareholders.

The findings indicating that an increase in cash ratio significantly reduces return on equity align with several studies that highlight the negative effects of excessive liquidity on firm performance. For instance, Nworie, Moedu, and Onyali (2023) found that the cash ratio negatively affected earnings per share in listed consumer goods firms, supporting the notion that excessive cash holdings may hinder profitability. Similarly, Moneke and Ezeagba (2024) reported a negative impact of cash and cash equivalents on return on assets among industrial goods firms, reinforcing the argument that excessive liquidity can diminish financial returns. Additionally, Oroniran, Abdullahi, and Olanisebe (2023) found that cash flow from operating and investing activities negatively impacted profitability, suggesting that inefficient cash utilization can reduce returns. Likewise, studies by Boloupremo and Umbe (2024) and Olorunfemi, Opusunju, and Jiya (2020) demonstrated a negative correlation between cash conversion cycles and return on assets in food and beverage firms, indicating that excessive liquidity management inefficiencies can lead to lower profitability. Conversely, Owolabi (2022) found that the current ratio and cash flow ratio had a positive and significant effect on return on assets and return on equity, suggesting that liquidity, when properly managed, can enhance financial performance. Similarly, Adekanmi, Odewole, and Adeoye (2022) reported a significant positive effect of the cash conversion cycle on financial performance, contradicting the notion that higher cash holdings necessarily reduce returns. Furthermore, Odo and Ohazuluike (2021) established that cash flow from operating, financing, and investment activities significantly influenced profits, implying that effective cash management strategies can improve financial outcomes. Bari, Muturi, and Samantar (2019) noted inconsistencies in liquidity ratios due to fluctuating market trends, highlighting the complexity of cash management's impact on financial performance. Meanwhile, Duru, Okpe, and Okolo (2017) found that operating cash flow had a positive and significant effect on profit after tax, although investing and financing cash flows had no significant effects, suggesting that the way firms allocate cash flows determines financial performance. Thus, while the findings align with

studies that emphasize the detrimental effects of excessive liquidity, some research suggests that strategic cash management can enhance firm profitability.

5.0 Conclusion and Recommendation

In conclusion, maintaining high levels of cash reserves may not always translate into improved financial performance. This emphasizes the delicate balance between liquidity and profitability, as excessive cash holdings might indicate inefficiencies in cash utilization. When firms accumulate large cash reserves without deploying them into productive activities, they may experience reduced shareholder value, lower profitability, and missed investment opportunities. This inefficiency can also increase agency problems, as managers may have less pressure to optimize resource allocation, potentially leading to suboptimal financial decisions. Thus, prioritizing liquidity at the expense of profitability may lead firms into struggling to maximize shareholder wealth, particularly in competitive industries such as food and beverages, where operational efficiency and strategic investments are key drivers of growth. This suggests that firms need to carefully evaluate their cash management practices to avoid the pitfalls of excessive liquidity, which could hinder long-term financial performance. Be that as it may, firms operating in volatile economic environments may still choose to hold more cash as a precautionary measure, yet the trade-off between security and profitability remains a crucial concern. Thus, while maintaining liquidity is essential for operational stability, an overly conservative approach to cash retention could limit firms' ability to seize profitable investment opportunities, and thereby impairing their financial performance. The conclusion above informed the following two recommendations:

1. Financial managers should adopt an optimal cash management strategy that balances liquidity and profitability by ensuring that excess cash is efficiently deployed into productive investments rather than being retained unnecessarily.

2. Shareholders should actively engage with management to ensure that cash reserves are utilized in ways that enhance firm value, such as reinvestments in expansion, innovation, or dividend payouts, rather than allowing excessive cash hoarding that may reduce returns.

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