EFFECT OF CORPORATE DISCLOSURE ON FINANCIAL PERFORMANCE OF FIRMS LISTED ON NAIROBI SECURITIES EXCHANGE, KENYA

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Abstract: Investors today are more cautious when making decisions on matters investment. They request to be equipped with information for them to be able to make informed decisions on where to put their money. This trait has been attributed to a decline in financial performance and the rising trend of corporate failures both locally and globally. The main objective of the study was to determine the effect of corporate disclosure on financial performance of companies listed on Nairobi Securities Exchange, Kenya. The specific objective that guided the study was to determine the effect of financial disclosure on financial performance of firms listed on Nairobi Securities Exchange. The research adopted a longitudinal research design. The population of the study comprised of all firms listed on the Nairobi Securities Exchange. Purposive sampling was used in the research to select the 42 listed companies that had a complete set of data over a six year period (2013-2018). Secondary data was collected using a disclosure check index retrieved from annual financial statements of the listed firms. Data was analysed using descriptive and inferential statistics with the aid of STATA software. Results of the study revealed that financial disclosure had a positive significant effect on financial performance at 5% significance level hence the study recommends that companies should adhere to provisions stipulated by International financial reporting standards in ensuring full disclosure of financial information.

Keywords: Corporate disclosure, financial disclosure, listed firms, financial performance.

I. INTRODUCTION

Corporate disclosure is a cardinal pillar of corporate governance that facilitates informed decision making at different levels of the organization (Nyamongo, 2017). The gravity of corporate disclosure has been appreciated in different aspects of modern day business and academia. This has led to the introduction of numerous standards such as the International financial reporting standards (IFRS) which companies must adhere to with the aim of achieving reliable financial information (Boshnak, 2017).

Considering increased interest on Nairobi securities exchange as an important avenue to foreign and domestic investments, it is important that investor confidence is enhanced. Corporate disclosure must therefore be done with the interest of investors at heart rather than immediate profits which is normally the primary aim of most managers within the institutions (Atandi, 2017). The information released by managers to primary users can only be relevant if it is capable of making a difference in the decisions they make. If too much irrelevant information is produced, users may overlook the relevant information.

Previous studies on corporate disclosure have revealed numerous scandals and collapse of major corporations like Tyco, Enron, WorldCom and bank of credit international in the United Kingdom and the United States of America. This has created worldwide interest in issues of corporate governance and particularly the area of corporate disclosure within the organizations (Lakhal, 2015). In Africa; questions have been raised of several organizations such as Stanbic bank in

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Uganda and Tanzania which have been in the media for all wrong reasons. Kenya is not an exemption to these cases as several companies like Kenya airways, Mumias sugar, Pan paper and Uchumi have all been characterized with increased cases of mismanagement that has been widely attributed to lack of proper corporate disclosure of the company results (Muturi, 2018).

Over the years, several researchers have paid attention on the of corporate disclosure however, few studies have been done to determine its effect on financial performance of firms listed at the Nairobi Securities Exchange, Kenya.Contradicting results have also been arrived at by the researchers and therefore there is need to carry out further research on the same

1.1 Specific objectives

i. To determine the effect of financial disclosure on financial performance of firms listed on Nairobi Securities exchange, Kenya.

1.2 Research hypothesis

i. \( H_0 \): Financial disclosure has no significant effect on financial performance of firms listed on Nairobi Securities Exchange.

II. LITERATURE REVIEW

The value of most companies in Kenya is depicted through their financial statements. Financial disclosures provide internal and external stakeholders of the business with additional information regarding business operations. It is important that a good corporate governance system should consider financial disclosure as fundamental. This would ensure effective and efficient business operations with high levels of disclosure where managers are accountable for their actions (Nyamongo, 2017).

In most cases, small businesses have very minimal disclosures to make in their financial statements as compared to larger firms which are compelled to provide additional information to lenders and investors. These disclosures should done in accordance with the generally acceptable accounting principles or voluntary to assist the management and other interested stakeholders in decision making. (Hood, 2015).

Listed companies on the other hand ought to try to increase the level of financial information disclosure and minimize chances of information asymmetry which will trigger positive financial performance. This would help current and potential investors’ to gather the required information which can influence their decision making (Muriithi, 2018).

Jahanshad (2014) investigated the relationship between financial information transparency and financial performance of listed companies in Tehran stock exchange for a six year period (2006-2011). 94 companies in the Tehran stock exchange were studied and after measurement of information transparency and financial performance of the companies the results suggested that there was a significant positive relationship between financial information transparency and financial performance at 95% confidence level.

Edogbanya (2016) examined company financial disclosure and firm performance in Nigeria. He used the disclosure scoring index to measure financial disclosure. The research used secondary data from listed firms. Financial performance was measured using Tobin’s q and ROA. The study found out that transparency of relevant information can lead to firm performance as shown with significant positive relationship with Tobin’s q and significant negative relationship with return on assets.

Awolowo (2012) studied the effect of financial policy and firm specific characteristics on corporate performance. Data from 70 firms was collected over a period of 16 years (1990-2006). Data was analysed using pooled OLS, fixed effect model and generalized model. The results showed a negative effect on the relationship between growth, size and foreign direct investment and firm performance even though the other variables showed a positive relationship with firm performance.

Standard setters and policy makers should consider financial disclosure not only in the context of recent financial crisis but also in the light of other matters that are perceived by investors to be influencing the financial reporting environment. They should consider factors such as political uncertainty and risks, increasing globalization, increased complexity of businesses among others.
Conceptual framework

<table>
<thead>
<tr>
<th>Independent variable</th>
<th>Dependent variable</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial disclosure</td>
<td>Financial Performance</td>
</tr>
<tr>
<td>- Financial policy</td>
<td>- R.O.A</td>
</tr>
<tr>
<td>- Investment policy</td>
<td></td>
</tr>
</tbody>
</table>

Fig.1

3. RESEARCH DESIGN

Research design refers to the general strategy that adopted by a researcher to integrate the different components of the study in a logical and coherent way in order to effectively address the research problem. The study adopted a longitudinal research design to collect and analyse data. Longitudinal research design was adopted because it involves studying variables over an extended period of time (Gimblett, 2006).

3.1 Target population

Target population implies the entire group of individuals, objects or items from which the researcher wants information from (Ranjit, 2015). Mugenda&Mugenda (2003) refer to population as an entire group of individuals having a common observable characteristic. The researcher targeted all 65 firms listed on Nairobi securities exchange. This was to enable the researcher to come up with conclusive results on all firms listed on NSE.

3.2 Sampling and sample size

A sample can be defined as a finite part of a population under study which can be used to gain generalized information representing the entire population (Kombo & Tromp, 2009). This study adopted purposive sampling technique. This was because firms that had a complete set of data over the six year period were used as a representation of the entire population. 42 firms listed on Nairobi securities exchange that had a complete set of data for the six year period (2013-2018) were considered for the study.

3.3 Data collection procedures.

Secondary data drawn from audited financial reports of firms listed on Nairobi securities exchange was utilized in this research. Data was collected from individual companies audited financial statements retrieved from the company’s annual reports. The main data collection instrument was the disclosure check Index for the specific study variables which is attached as appendix II. Scoring approach was used for items disclosed with score of (1) given if a company has provided information and (0) if information is not provided (Muriithi, 2018).

Level of disclosure = Actual items disclosed / Total possible items in the index.

3.4 Data analysis and presentation

Descriptive and inferential statistics were used in data analysis. Descriptive statistics comprised of measures such as skweness and kurtosis for the variables under study. Correlation analysis was carried out to show the strength of the relationship between the variables under study. Regression analysis was also carried out to show the nature of relationship between dependent and independent variables (Kothari, Andrew and Leone, 2005).

IV. RESULTS

4.1 Response rate

The researcher targeted all companies listed onNSE and had complete financial statements over the six year period (2013-2018). Data was collected from annual reports of the companies. Out of the 65 companies listed on NSE over the period, 42 had a complete set of data. This translates to 64.6% response rate. 23 firms listed on Nairobi securities exchange did not have financial statements for all the six years under study and did not therefore form part of the sample.
4.2 Descriptive statistics for secondary data

Table 1: Descriptive statistics

<table>
<thead>
<tr>
<th>Variable</th>
<th>Obs</th>
<th>Pr(Skewness)</th>
<th>Pr(Kurtosis)</th>
<th>Chi (2)</th>
<th>Prob&gt;chi2</th>
</tr>
</thead>
<tbody>
<tr>
<td>FD</td>
<td>252</td>
<td>0.0301</td>
<td>0.0018</td>
<td>8.544</td>
<td>0.1040</td>
</tr>
</tbody>
</table>

Descriptive statistics are important because they enable presentation of data in a way that allows for simpler interpretation (Maingi, 2016). From the results in table 1, financial disclosure was positively skewed with the probability of skewness being 0.0301. The researcher used two statistical methods to test for normality. Byrne (2010) argued that data is considered to be normal if skewness is between -2 to +2 and kurtosis is between -7 to and +7. From the table above, skewness and kurtosis values are within this range and therefore we can conclude that the variable (financial disclosure) is normal. This was supported by the Jarque-bera test which is used to test whether a given series is normal or not. The probability for FD was 0.1040. The null hypothesis shows that the series are normally distributed whereas the alternative hypothesis shows that the series are not normally distributed. Applying the Jarque bera test, normality was accepted at 5% significance level. This implied that the null hypothesis (H₀: normality) cannot be rejected. Therefore the residuals were normally distributed.

4.3 Inferential statistics

Table 2: Correlation analysis.

<table>
<thead>
<tr>
<th>VARIABLES</th>
<th>FD</th>
<th>ROA</th>
</tr>
</thead>
<tbody>
<tr>
<td>FD</td>
<td>1.0000</td>
<td></td>
</tr>
<tr>
<td>ROA</td>
<td>0.0823</td>
<td>1.0000</td>
</tr>
<tr>
<td></td>
<td>0.1926</td>
<td></td>
</tr>
</tbody>
</table>

Financial disclosure had a correlation coefficient of 0.0823. This was interpreted to mean that financial disclosure was weakly but positively correlated to return on assets. The results are in agreement with Musyoka (2017) through her study effect of voluntary disclosure on financial performance of companies listed on NSE. She found financial disclosure to have a weak but positive correlation to return on assets.

4.4 Regression results for secondary data

Results for regression analysis are presented in this section. Hausman test as discussed below was carried out to determine whether to use random or fixed effect model.

4.4.1 Test for fixed and random effects.

The study carried out the Hausman test to determine whether to use the fixed or random effect model. When we fail to accept the null hypothesis, it means that fixed effect is favourable (Rothstein, 2010). The fixed effect model is used to find out whether variables under study have similar characteristics whereas the random effect model finds out whether they have different characteristics. The results were as shown in table 4.6 below:

Table 3: Hausman Test

<table>
<thead>
<tr>
<th>Hausman Test</th>
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<tbody>
<tr>
<td>Ho:difference in coefficients not systematic</td>
</tr>
<tr>
<td>F=3.35</td>
</tr>
<tr>
<td>P=0.0201</td>
</tr>
</tbody>
</table>

The results in table 3 indicated a probability of 0.0201 which is less than the critical p value of (0.05) or 5% significance level. The researcher therefore failed to accept the null hypothesis that the difference in coefficients was not systematic. This study therefore adopted the fixed effect (within) regression model as the p value was less than 0.05.
Table 4: Fixed effect regression on financial disclosure versus financial performance

<table>
<thead>
<tr>
<th></th>
<th>R-sq:</th>
<th>F(1,209)</th>
<th>Prob&gt; F</th>
</tr>
</thead>
<tbody>
<tr>
<td>within</td>
<td>0.0361</td>
<td>7.82</td>
<td>0.0057</td>
</tr>
<tr>
<td>between</td>
<td>0.0001</td>
<td></td>
<td></td>
</tr>
<tr>
<td>overall</td>
<td>0.0068</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

| ROA      | Coef.       | Std. Err.  | T       | P>|t|   | [95% Conf. Interval] |
|----------|-------------|------------|---------|-------|---------------------|
| FD       | 0.0985671   | 0.0352536  | 2.80    | 0.006 | 0.0290689 - 0.1680652 |
| _cons    | -0.0042643  | 0.0239665  | -0.18   | 0.859 | -0.0515113 - 0.0429827 |

From table 4 above, an R squared of 0.0361 reveals that 3.61% of the variance in financial performance can be accounted for by financial disclosure. However, financial disclosure had a significant effect on financial performance of companies listed on NSE with a p value of 0.006 at 5% significance level.

The results revealed that financial disclosure had a regression coefficient of 0.985671. This implied that a unit change in financial disclosure would result to 0.0985671 unit change in financial performance in the same direction. Financial disclosure was then said to have a positive and significant effect on financial performance of companies listed on NSE, Kenya.

These results are consistent with Tarus (2013) who researched on corporate disclosure: Evidence from Kenya. He found out that financial disclosure had a positive and significant effect on firm performance. However the results are inconsistent with Sahore (2017) who researched on corporate disclosures and financial performance of selected Indian Manufacturing and non-manufacturing companies and found financial disclosure to have an insignificant effect on firm performance.

The regression model is as shown below:

ROA = -0.042643 + 0.0985671FD

From the regression model if financial disclosure is held constant financial performance will be at 0.042643.

V. CONCLUSION

From the study, we can conclude that financial disclosure had a positive significant effect on financial performance of firms listed on NSE, Kenya with a p value of 0.006. The fixed effect multiple regression model revealed that when other variables are controlled, a unit change in financial disclosure would result to a significant change in financial performance in the same direction.

VI. RECOMMENDATION

The study recommends that companies should adhere to provisions stipulated by International financial reporting standards and ensure that all relevant information is appropriately disclosed to stakeholders. This will boost investor confidence and attract both local and international investors.

REFERENCES


