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Corporate Disclosures and Financial Performance of Manufacturing and Allied Firms Listed at the Nairobi Securities Exchange, Kenya

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Abstract: This study sought to establish how corporate disclosures affect the financial performance of manufacturing firms listed on the Nairobi Securities Exchange. The study was hinged on the Agency the Stakeholder theories whilst deploying both descriptive and correlational research designs. The study used self-administered close-ended questionnaires to collect data. Data analysis was undertaken using the STATA software. The analysis involved diagnostic tests of normality and multi collinearity to ensure that the variables conform to the assumptions of multiple regression. Correlation analysis showed how strongly the variables under investigation are related and regression analysis tested the study hypotheses. The study findings revealed a positive and significant relationship between all four disclosure variables and financial performance. Research findings further indicated that at 5 percent significance level, Risk disclosure (Sig. = 0.006), Financial disclosure (Sig. = 0.030), Corporate Governance disclosure (Sig. = 0.015) and Corporate Social Responsibility disclosure (Sig. = 0.005) have a significant effect on Financial Performance. These findings suggest that increasing the quality and quantity of these disclosures can lead to improved financial performance. The study recommends that manufacturing firms listed on the NSE should enhance their financial and risk disclosures, strengthen corporate governance and invest in CSR initiatives to improve transparency, investor confidence, and in the long run, financial performance.

Keywords: Corporate Governance Disclosure; Corporate Social Responsibility Disclosure; Financial Disclosure; Financial Performance.

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Introduction

Financial performance has been a topic of concern for both academicians and practitioners. In the recent past, the continuous collapse of firms like Mumias Sugar and Nakumatt Holdings, has shifted the attention to the contribution of disclosures of pertinent information to the various stakeholders towards the collapse of these firms. According to Boniface (2019), corporate disclosures refer to release of financial and non-financial information by a company to its stakeholders, including investors, regulators, customers and the public. Etienne et al (2012) asserted that increase in disclosures levels creates value for shareholders by way of a firm attracting additional investments due to the ability to draw external financing. According to the United States Securities Exchange Commission (2002), investors have lost billions in the form of share value erosion due to non-disclosure or in-adequate disclosure practices. This is evident in the corporate world both globally and locally, where non-disclosure or inadequacy of disclosures has led to massive financial losses by corporations, leading to huge losses to the investors. In attempt to shield investors from disclosure related losses, the International Organization of Securities Commissions formed a technical committee to draft guidelines for listed firms' ongoing disclosures and major development reporting for its member Security market regulators (Technical committee of the IOSC, 2002).

To protect investors from suffering huge losses, a number of Securities Exchange regulators have taken stern action against corporates who have failed to disclose pertinent information to its stakeholders. In 2013, the Cypriot financial regulators fined the bank of Cyprus 160,000 Euros for failure to disclose to its shareholders the lender's interest in the Greek government bond, a matter that almost brought the bank to its knees (Cyprus Exchange Commission, 2013).

The Capital Markets Authority's decision to fine the former Uchumi Limited Executive Director Jonathan Ciano, several board members and their transaction advisor, Faida Investment Bank 21.7 million Kenya shillings highlights the critical importance of corporate disclosures in the securities market. The fines stem from their 2014 rights issue, which raised 895.8 million shillings, where they failed to disclose material information regarding conflicts of interest by the CEO and the misuse of proceeds from the rights issue. (Mike, 2019).

The Nairobi Securities Exchange (NSE) history began in the 1920s, when share trading began in Kenya while the country was still a British colony. The NSE was then registered as a private company in 1991. It subsequently turned to a public company in 2011. The Capital Markets Authority (CMA) regulates activities of the NSE. It is in charge of approving offers and public listings of securities traded at NSE. CMA ensures that trading laws, regulations and requirements are followed to the latter and sustainability of the securities market integrity, which furthers investor trust, aiming at guaranteeing an orderly, fair and efficient securities market in Kenya (Capital Markets Authority, 2022). Currently, the NSE has listed 62 companies categorized based on their principal activities.

According to Mpiana (2017), a forensic audit report by KPMG East Africa revealed that the senior management of the Mumias Sugar Limited failed to disclose material facts to its board of directors in a botched importation deal, leading to losses to the tune of 1.1 billion Kenya shillings. The massive losses worsened the already bad financial situation of the sugar miller, eventually leading it to receivership and subsequent suspension of Mumias Sugar Company's stock from trading at the Nairobi Securities Exchange. Different scholars have arrived at different results while attempting to study the effect of corporate disclosures on financial performance of listed companies. Boniface (2019), in his study to assess the influence of corporate disclosures on financial performance of corporates quoted on the securities Exchange across East Africa noted that there exists a significant positive relationship between corporate disclosures and financial performance of the firms under study. King'wara (2020) carried out a study aimed at establishing if there exist any associations between corporate social responsibility disclosures and financial performance of firms domiciled in Kenya. The study revealed no relationship between financial performance of the companies under study and corporate social responsibility disclosures (Boniface, 2019). Additionally, no research has explicitly sought to investigate the impact of corporate disclosures on manufacturing firms quoted on the NSE. It is on these premises that this study sought to determine the effect of corporate disclosures on financial performance of manufacturing companies trading on the Nairobi Securities Exchange.

Theoretical Underpinnings

Several scholars have fronted several theories attempting to relate corporate disclosures and financial performance of various entities. The researcher settled on agency and stakeholder theories to serve as a guide for this study.

Agency Theory

Jensen and Meckling (1976) propounded the Agency Theory. According to the Agency theory, an agency relationship exists when one or more principals designate an agent and grant that agent power to act on their behalf. Managers (agents) of a company frequently receive authorization by the shareholders (principals) to make operational and financial decisions on their behalf, leading to a possible agency conflict. Compared to the principal, who is the shareholder, the agent, who is the manager, unquestionably has the informational upper hand. This leads to a conflict of interest, which eventually raises the cost of the agency. This theory was appropriate to this study since it clearly elucidated the need for disclosure of corporate governance, risk and financial activities to assure the principals that their interests have been given priority in the corporate activities.

Stakeholder Theory

Edward Freeman advanced the Stakeholder Theory. This theory posits that an organization's success depends on its ability to create value for all its stakeholders, not just its shareholders (Freeman, 1984). This theory was critical to the study since it deals with the requirement that corporations engage in actions that advance not only the interests of their shareholders but also those of other stakeholders. Corporate social responsibility disclosures, financial disclosures and corporate risk disclosures in company annual reports will promote the interests of a variety of stakeholders, enabling them to make informed decisions regarding the company's activities.

Empirical Literature Review

Risk Disclosures and Financial Performance

A study by Fathyah and Lim (2018) sought to establish the relationship between corporate risk disclosures and business performance with board gender and board diversity as the moderator variables. Risk disclosures were measured in terms of financial, operational, strategic and integrity risks. In the study, the researchers used the Structural Equation Model. The research findings showed that the level of risk disclosures in corporate annual reports had a significant and positive relationship with the financial performance of the firms under study. However, the moderating effect appeared insignificant while validating the hypothesis that the presence of a female board member enhanced the relationship between corporate risk disclosures and financial performance. These authors were in line with those of a study by Omaliko et al. (2020), addressing the impact of non-financial disclosures on company performance. While non-financial disclosure consisted of corporate governance, risk management and intellectual capital disclosures, the measure of financial performance used by the study was Return On Equity (ROE). Based on the research questions, the study tested hypotheses using the Panel Regression Model and STATA 15. Findings were that risk and risk management disclosures appeared to have an impact on the profitability of the firms under consideration.

Financial Disclosures and Financial Performance

Ijami and Miroga (2020) conducted a study and concluded that the disclosure of accounting and financial reporting systems had a positive but a moderate effect on the financial performances of investigated companies. The study recommended that sugar companies should enhance their financial performance by ensuring that they disclose accurate and timely financial and accounting information to its stakeholders. Similarly, Gidali et al. (2021) revealed a positive and significant relationship between financial disclosure and financial performance.

Corporate Governance Disclosures and Financial Performance

Hasnah and Adejoh (2016) assessed the transparency of non-financial enterprises listed in Nigeria and its relationship with performance. The study recommended that corporations should disclose more corporate governance-related information than what the law mandates.

In a bid to establish the relationship between corporate governance disclosures and financial performance, Anjalla and Shikha (2016) conducted a study among 38 non-financial firms listed on the Indian Securities Exchange. The study yielded a positive correlation between corporate governance disclosures and performance of firms. In another study, Muhammad et al (2017) examined the role of transparency and disclosure index in 30 banks for five consecutive years (2007-2011). The study revealed that ownership structure disclosures have an inverse relationship with ROE and ROA; on the other hand, board and management structure disclosures positively correlated with financial performance of the companies.

Corporate Social Responsibility Disclosures and Financial Performance

In Kenya, Mugambi and Fatoki (2019) conducted a study to establish the effect that CSR disclosures have on the financial performance of manufactured firms. The study revealed that both environmental and community participation disclosures are positively related to financial performance while the employee disclosures were found to have an insignificant positive impact on the financial performance of the companies under study. Cloudy and Oday (2022) examined the influence of voluntary non-Disclosure on profitability of listed companies. The study revealed that CSR disclosures had a positive albeit insignificant effect on the financial performance of manufacturing firms notwithstanding their engagement in either voluntary or mandatory disclosures.

The existing literature underscores the importance of corporate disclosures in enhancing financial performance. However, the literature primarily focused on accounting-based performance measures like ROA and ROE, neglecting other metrics such as Tobin's Q and dividend per share. Additionally, most research has examined listed companies across various stock exchanges, overlooking industry-specific analyses. This study sought to assess the impact of corporate disclosures on the financial performance of manufacturing and allied companies listed on the NSE.

Methodology

This section outlines the research methodology, including the design, sampling technique, data collection methods and data analysis procedures.

Design

The study deployed the correlation research design. The correlational design reported the causal relationship between the dependent and independent variables under study.

Population and Sampling

The study targeted finance and accounting staff of 8 out of the 9 manufacturing firms listed in the NSE as at the end of 2022, thus giving a total population of 320. The study used the "Wald formula" which is described as the ample size formula for estimating a single proportion, yielding a sample of 180.

Instruments

Data collection involved a questionnaire that consisted of properly constructed close-ended items, designed to cover all the variables.

Data Analysis

The data was analyzed using STATA software. Correlation analysis was used to show how strongly the variables under investigation were related. Lastly, regression analysis was used to test the hypotheses. The regression model was critical as the regression co-efficients were key in establishing the strength and direction of the relationship between dependent and independent variables. The resultant regression model was as below:

$$Y = C + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \beta_4X_4 + \varepsilon$$

Where;

Y= Financial performance (FP)

X_1= Risk disclosures (RD)

X_2= Financial disclosure (FD)

X_3= Corporate Governance Disclosure

X_4=CSRD (Corporate Social Responsibility disclosures)

$\acute{\varepsilon}$ = Error term

Results and Discussion

This section presents the study's findings. The study discusses the results in relation to research objectives and methodologies in previous sections.

Normality Tests

The researcher assessed the normality test by both Shapiro-Wilk and Kolmogorov-Smirnov tests at 95% confidence interval. The summary of the findings appear in Table 1.

Table 1: Normality test

	Kolmogorov-Smirnov[a]			Shapiro-Wilk		
	Statistic	df	Sig.	Statistic	df	Sig.
Financial Performance	0.142	180	0.079	0.911	180	0.009
CSR Disclosure	0.206	180	0.001	0.819	180	0.000
Corporate Gov Disclosure	0.136	180	0.116	0.931	180	0.033
Financial Disclosure	0.148	180	0.058	0.900	180	0.004
Risk Disclosure	0.135	180	0.122	0.919	180	0.015

From table 1, results from Shapiro-Wilk (SW) indicate that the residuals were not normally distributed (sig. <.05) meaning that the tests of normality failed. However, results from Kolmogorov-Smirnov (KS) indicated that the residuals were normally distributed (sig. >0.05) meaning that tests of normality passed for all the variables except for Corporate disclosure. Oztuna et al (2006) postulate that the violation of the normalcy assumption should not have significant implications when working with big samples, typically defined as those with a size greater than 30 or 40.

Multi Collinearity Tests

In Table 2, Variance inflation factors (VIF) or tolerance values assessed the presence of multi collinearity. If the Variance Inflation Factor (VIF) values are less than 10, there is no issue with multi collinearity. When the tolerance values are equal to or less than one, it indicates the absence of multi collinearity.

Table 2: Multi collinearity test results

Variable	Collinearity Statistics	
	Tolerance	VIF
(Constant)		
Risk Disclosure	0.859	1.165
Financial Disclosure	0.829	1.207
Corporate Gov Disclosure	0.794	1.259
CSR Disclosure	0.772	1.295

Table 3: Primary data multiple regression

Coefficients						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	0.066	0.522		0.126	0.901
	Risk Disclosure	0.268	0.091	0.345	2.950	0.006
	Financial Disclosure	0.225	0.098	0.272	2.286	0.030
	Corporate Gov Disclosure	0.271	0.104	0.316	2.598	0.015
	Corporate Social Responsibility Disclosure	0.252	0.083	0.373	3.025	0.005

a. Dependent Variable: Financial Performance

All the tolerance and Variable Inflation Factors fell below the thresholds of 1 and 10 respectively, clearly indicating clearance.

Multiple Regression

The results of the multiple regression appear in Table 3.

From the table 3, the study established that an increase in risk disclosures by one-unit leads to an increase in the financial performance by 0.268 units. Additionally, a unit increase in financial disclosure would enhance the financial performance by 0.225. Moreover, with an increase of one unit in corporate governance disclosure, the financial performance would also increase by 0.271. Finally, an increase of one unit in CSR disclosure would improve financial performance by 0.252 units. The study further established that at 5 percent level of significance, Risk Disclosure (Sig. = 0.006), Financial Disclosure (Sig. = 0.030), Corporate Governance Disclosure (Sig. = 0.015) and Corporate Social Responsibility Disclosure (Sig. = 0.005) were all found to have statistical significant effect on the Financial Performance. As a result, the following regression equation was extracted; Y = 0.066 + 0.268 risk disclosure + 0.225 financial disclosure + 0.271 corporate governance disclosure + 0.252 CSR disclosure.

The findings of the study are in line with those by Mwenda et al. (2021) that risk disclosures positively affected performance. The findings on the impact of financial disclosures on the financial performance of manufacturing companies were in line with the findings of Gidali et al. (2021) on corporate disclosures and financial performance of firms listed on the NSE. As established in both the studies, there is a positive direct relationship between financial disclosures and firm performance. The findings were further in agreement with Anjalla and Shikha's (2016).

Conclusions and recommendations

Conclusions

Given the positive and significant correlations, higher levels of financial disclosures enhances the financial performance. Therefore, in order to lessen the degree of information asymmetry and subsequently improve the financial performance, listed corporations should disclose as much financial information as possible. Whereas risk disclosure's positive correlation with financial performance was consistent with existing findings, to boost investor confidence, management must disclose risk exposure information as much as possible. A higher degree of disclosures contributes to increased investor confidence, which in turn improves financial performance.

Recommendations

Manufacturing firms listed on the Nairobi Securities Exchange should strive to improve the quality and quantity of their financial disclosures, which will enhance transparency and investor confidence. To mitigate information asymmetry and boost investor confidence, the manufacturing companies should disclose comprehensive information about their risk exposures. The firms should consider investing in CSR initiatives that can enhance stakeholder relationships, improve brand reputation and ultimately improve the financial performance.

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