THE EFFECT OF VOLUNTARY DISCLOSURE ON STOCK RETURNS OF COMPANIES LISTED AT THE NAIROBI SECURITIES EXCHANGE

By:

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DECLARATION

I, the undersigned, declare that this is my original work and has not been submitted to any other college, institution or university other than the University of Nairobi for academic credit.

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DEDICATION

I dedicate this work to the Almighty God and to my family; my dearest dad Albert Asava and mum Rachael Tunen Asava, for their encouragement and support throughout my studies.

ABSTRACT

Managers execute their steward role of managing the affairs of the organizations on behalf of the shareholders. They are therefore required to report their conduct and practices to them periodically. To protect the shareholders, financial and accounting standards board regulators, auditors and governmentsconduct an oversight role and act as watchdogs to guard against any misconduct by the managers. As such, there is specific financial information that is statutorily required to be reported.

However, business organizations have over the years reported financial and non-information to the shareholders and the general public. Included in their reporting are voluntarydisclosures,some of which are not statutorily required to be reported. Notably, every release of information by an organization has got some cost implication to the firm and therefore the value addition of such voluntary disclosure ought to be evaluated.

This study sought to establish the effect of voluntary disclosures on stock returns of companies listed in the Nairobi Securities Exchange. Using a content analysis of annual reports of companies composing the NSE 20 Share Index, the study sought to establish the effect ofvoluntary disclosures such as; business data,analysis of business data, forward-looking information and information about management and shareholders,individually and jointlyon stock returns.

The findings revealed that there is no relationship between voluntary disclosures and stock returns.Through SPSS analysis, the studyobtained a coefficient of determination of 0.171 and a Pearson Product Moment coefficient of correlation of 0.029 (near to 0.00) for the multiple linear regression model representing the relationship between voluntary disclosures and stock returns of the companies. Hence, only 17.1% of the data points would be mapped ona linear plot. The Pearson Product Moment (correlation coefficient) obtained was 0.03 depicting no relationship between voluntary disclosures and stock returns.The results of the studyconfirmed the findings established elsewhere by Zareian and Hail in other markets.

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ABBREVIATIONS AND ACRONYMS

CMA	Capital Market Authority
CPA	Certified Public Accountant
CSR	Corporate Social Responsibility
EMH	Efficient Market Hypothesis
EPS	Earnings per Share
FASB	Financial Accounting Standard Board
FTSE	Financial Times Securities Exchange
NSE	Nairobi Securities Exchange
SPSS	Statistical Package for Social Science

CHAPTER ONE: INTRODUCTION

1.1 Background of the Study

Investors require financial information for purposes of their financial decision making. All decision makers have a framework of what information they need to accomplish some purpose depending on their mental abilities and experience (Zareian, 2012). One of the key aims of accounting information reporting is to help the users of the information to predict the returns on their investment.The stock returns of an investor's investments in the stock market are affected by the financial information provided by the management (Guillaume, 2007). Furthermore, the investors use the financial information to estimate the rate of return.

Zareian (2012) posits that the extent of the effect of accounting information is somehow complicated. But since investors invest on any economic unit when they have enough information, managements' development of plans and policies to achieve succinct levels of information disclosureto the capital markets can effectively communicate to the investors and leverage their knowledge about the stocks hence leverage their decision (Francis et al, 2003). Zareian (2012) linked voluntary accounting disclosure with stock returns in the capital markets.

1.1.1 Voluntary Disclosure

Voluntary disclosure refers to disclosure of information regarding the organization up-and-beyond the statutory requirements. The practice of voluntary disclosure has attracted a lot of attention from researchers. Meek, Roberts & Gray (1995),classify voluntary

disclosures as strategic, non-financial and financial information. They classify the disclosures depending on what they are intended for and the contents of such disclosed information. Since the management know more about the company than the shareholders, customers, suppliers, creditors, and government regulators including capital market authorities (Feng & Li, 2007), the management finds it useful to inform the outsiders what they know about the company.

Financial Accounting Standards Board (FASB) classifies voluntary disclosures into 5 categories as shown in the table below.

Table 1.1: FASB: Classes of Voluntary Disclosures

Voluntary Disclosure	**Example**
Business data	Breakdown of market share growth and information on new products
Analysis of business data	Trend analysis and comparisons with competitors
Forward-looking information	Sales forecast breakdown and plans for expansion
Information about management and shareholders	Information on stockholders and creditors and shareholding breakdown
Company background	Product description and long-term objectives
Information about intangible assets	Research and development and customer relations.

Source: (FASB Annual Report, 2013)

The key aim of voluntary disclosures is to inform the public more about the company. In turn, the management hopes that the stakeholders of the company will respond favorably to the company. Whether strategic, non-financial or financial voluntary disclosures, Meek, Roberts, & Gray (1995), posits that most organizations gain some benefits by virtue of disclosing more than is expected if the issued information is strategically availed

to the important parties who are likely to act in favor of the company. The disclosures are sometimes not periodic while others are periodically released including voluntary disclosures released together with annual reports of an organization.

According to Foster (1986), regulations on mandatory supply of financial information through statements are not the only reason why organizations provide financial information. Firstly, he argues that financial information was provided before installation of the regulatory bodies. Secondly, firms not under regulatory brackets still provide statements. Thirdly, firms provide financial statements more frequently than is required by the regulations. Fourthly, many organizations provide substantially more information than is required by the regulators.

1.1.2 Stock Market Returns

Stock market returns is sometimes synonymous to stock prices (Foster, 1986). A strong market is one that impounds new information to stock prices and hence making the stock prices for the firms stableand accurately valued. Due to misvaluations of firms by public capital markets, managers provide the information known by them alone to the capital markets to correct the misvaluations, since stocks value is dependent on information (Velashani & Mehdi, 2008). Walter (2006), noted that since organizations in the same industry tend to mimic one another, voluntary disclosure by one organization is mimicked by other firms, hence more information released to the market tending the capital markets towards efficiency.

The information asymmetry and agency conflict can adversely impede the allocation of resources in capital markets of an economy (Velashani & Mehdi, 2008). The disclosure

requirements themselves and the bodies such as regulators, standards setters, auditors, and capital market intermediaries seek to facilitate and enhance the credibility of management disclosures hence playing an important role in mitigating the problem of information asymmetry and agency conflict (Healy & Palepu, 2001). Deegan (2010), posits that corporate disclosure is critical for the well functioning of an efficient capital market. Furthermore, companies exercise voluntary disclosures for capital market reasons.

The market forces exerts pressure on the companies' such that they can only give relevant and perceived information so thattheir securities will fetch reasonable prices hence leverage their ability to get capital from the markets (Healy & Palepu, 2001). In support, of Foster (1986), Leuz&Verrecchia (2000), posited that there is a relationship between economic theory and contemporary accounting implying that more disclosure means lower information asymmetry costs. Hence, the more a company discloses its state of affairs, the more it mitigates chances of obligations to shareholders or potential buyers and sellers of the entity's stocks and hence better performance of the market.

1.1.3 Effect of Voluntary Disclosure on Stock Returns

Many studies reveal that organizations operating in industries highly dependent on external financing have a considerably higher level of voluntary accounting disclosures (Velashani & Mehdi, 2008). They further realized that the results were still up-held after controlling for differences in legal and financial systems amongst countries, and firm-specific controls for firm size and performance. The findings revealed that organizations with relatively higher levels of disclosure usually have lower costs of capital (Walter

2006). Therefore, voluntary disclosures lower information asymmetry costs and hence the cost of external financing for the firm.

Notably, transaction costs reflected in the bid-ask spread should reduce as information asymmetry reduces. Marilyn &Heibatollah (1994)stated that accounting disclosure reduces the bid-ask spread as a proxy of transaction costs. Further, Christine (1997) also revealed that cost of equity capital is reduced in firms with relatively higher levels of disclosures. In her studies, companies with relatively more analyst reports had lower costs of equity capital. Partha (1998) noted that companies which were ranked highly by financial analysts had lower interest costs of issuing debts.

It is the economic benefits that encourage the managers to provide more information to the public through voluntary exposure. Also, since regulatory disclosures do not succinctly reflect the management performance, the management engages in voluntary disclosure to say more about the company. In turn, the stakeholders get to know more about the company, while reducing the costs of capital. There is an overall economic benefit for companies and the capital market since the cost of raising capital is reduced. Further, the market participants are informed by dealing with the demerits of information asymmetry and its related costs. These factors attract more investors to a market hence an increased success of the market.

1.1.4 Nairobi Securities Exchange

The Nairobi Securities Exchange, formally Nairobi Stock Exchange was constituted in 1954 as a voluntary association of stock brokers in the European community. It was registered under theSocieties Act.Since then the market has undergone tremendous

transformations. At the heart of the Exchange ismarket liquidity enhancement by fostering transformational and utmost ethical practices amongst the participants so that more investors are assured of free and fair information for their trade related decision making (Ngugi, 2003).

Therefore, the Kenyan Government has initiated reforms at the NSE aiming to transform the exchange to be the vehicle to mobilize domestic savings and to attract foreign capital investments (Barako, 2007). Consequently, corporate financial reporting and especially enhanced voluntary disclosures is an important ingredient of enhancing confidence and trust of the market by both local and foreign investors (Ngugi, 2003).Since the year 2008, the exchange has greatly emphasized on corporate governance with some participants punished for faulting the acceptable market regulations.

Amongst other changes are enhanced communications by and within the NSE itself. In November 2011, the exchange launced the FTSE NSE Kenya 15 and FTSE NSE Kenya 25 Indices, as a result of an extensive market consultations with local asset owners and fund managers. The launch of the indices reveals the interest of growth into the domestic investment and diversification opportunities in the East African region.This was followed by the NSE becoming a member of Financial Times Services Division (FISD) of the Software and Information Industry Association (SIIA) in March 2012. By providing the indices in its website, the initiative provides the investors with current information of reliable indication of the Kenyan equity market's performance during trading hours.

With itsemphasis on attracting more investors, NSE has to encourage all the participants in the market to provide as much information as is practically possible.Barako (2007)

Posits that the level of disclosures including voluntary disclosures amongst the participants in the NSE has increased over the years. Definitely, with the CMA emphasizing on tightening corporate governance amongst the market participants, the extent of disclosure including voluntary disclosure is bound to be enhanced in the NSE.

1.2 Research Problem

Financial reporting is anchored on the agency relationship between the management on one hand and the shareholders and stakeholders on the other hand. The managers who manage the organizations on behalf of the shareholders have to report to the shareholders. The stakeholders all make decisions which either impact the organization or they themselves are affected by the organizations, since the value of their decision is pegged on the position of the organization presently and its decisions thereafter (Karamanou & Vafeas, 2005).

Investors get information regarding the organizations trading in NSE through their annual reports and other announcements.It is the dire need of information so that stock prices in the NSE reflect the most current information, that the NSE, like any other exchange market encourages the firms to disclose as much information as is possible. This is advantageous since literatures reveal that organizations with good corporate governance, more so in corporate reporting are able to raise capital from the markets relatively cheap (Zareian, 2012). Furthermore, the greater the disclosures, the greater the extent to which the stock prices reflect the whole truth hence obeying the market fundamentals. This helps the investors to rightfully choose the securities to invest in.

Ponnu & Maurice (2009) in their corporate social responsibility disclosure in Kenyapublished in African Journal of Business Management, only investigated the relationship between CSR voluntary disclosure and returns on stocks for the NSE trading companies during the period 2008 to 2012. They focused on CSR reporting and not all voluntary disclosures. They realized that CSR disclosure received only modest attention and the theme most commonly disclosed was community involvement, which had little relationship to stock returns. Also, they noted that there were significant differences among various industry groupings with respect to company background and themes of CSR disclosure.

Oyenje (2012) investigated whether there is a relatioship between corporate social responsibility practices and financialperformance of firms in the manufacturing, construcion and allied sectors of the NSE. Their findings revealed a relationship between CSR, manufacturing intensity and returnon assets with a correlation of 0.87. Further, there was a significant postive relationship between CSR practices and financial performance.

Munyao (2012) studied the effects of corporate governance practices on the financial performance offorex bureaus in Kenya. Established board of diretors, independent board members and strong internal controls which emphasise inclusive financialreporting were cited as important corporate governance practises. He cited benefits such as improved profitability, return on investment and reduced business risk as accruing to Forex Bureaues with good financial controls and reporting.

Lopokoiyit (2012) investigated the effect of corporate governance practices on the share prices of companies listed in theNSE. He noted that there is a direct relationship between corporate governance practices and share prices. He also observed that corporate governance practices led to improvement of EPS, debt/equity ratio and return on assets.

Literatures from past studies reveal that most researchers have been skewed to the factors that influence the extent of voluntary disclosure. Those studyingthe relationship between voluntary disclosure and stock returns, like Ponnu & Maurice (2009),Oyenje (2012), Munyao (2012) and Lopokoiyit (2012) focused on the CSR and corporate governance and related issues. Other researchers elsewhere have linked causality between quality voluntary disclosures and stock returns and in turn the stock market performance.Yet again, some have had conflicting results.

Since voluntary information disclosures have a cost implication, there is a need to establish whether voluntary information disclosures impacts the stock market returns expected by the investors. The question that really begs is whether voluntary information disclosures by the companies listed in Nairobi Securities Exchange, impacts the stock returns of the particular organization.

1.3 Research Objective

The objective of this study is to establish the relationship between voluntary disclosures and stock returns of companies listed at the Nairobi Securities Exchange.

1.4 Value of the Study

The findings can help stock market participants understand the implications of voluntary disclosures on the company's stock returns. Company executives can therefore make an informed decision in engaging on voluntary disclosures. To the stock traders, the research can help them determine how to action after voluntary disclosures, so as to earn better returns for their investments. Also,this study cancontribute to the body of literatures on the implications of voluntary accounting disclosures and stock market returns and related fields.As such, future researchers can draw literatures from the study.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

This chapter provides literatures from past researchers and scholars on the implications of voluntary accounting disclosures on stock market performance. The chapter examines the concepts of voluntary accounting disclosures on stock market prices in relation to the extent to which organizations have exercised voluntary accounting disclosures and its effect to the stock market performance. By considering the work from diverse authors, the chapter builds on the theoretical and the conceptual framework on the effects of voluntary accounting disclosures on stock returns.

2.2 Theoretical Framework

One of the accounting information goals is helping users in predicting the returns on their investment. Some variables affecting firms' stock returns in themarket result from financial information provided by management. Extent of effect of this information is complicated and somehow unknown. Investors, invest on an economic unit when they have enough information, including financial information (Botosan, 1997). Thus using policies and plans of information disclosure may deliver top information and knowledge of managers to the capital market and be effective in communication between managers and investors.

Decision making requires information; and managers are always confronted with a problem on which information to release to investors to aid in their decision making.One of the major difficulties in accounting standards development is thelack of knowledge of

decision making nature and logical process which decision makers attempt to access. The firm's rate of return on investment is one of the main decision making criteria for investors and its calculation as a criterion for firm performance evaluation is obtained from information disclosed by the firm management (Barako, 2007).

2.2.1 Efficient Market Hypothesis

In finance, a stock price reflects or contains financial information. The efficient-market hypothesis (EMH), also called Joint Hypothesis Problem, asserts that financial markets are informationally efficient (Barako, 2007). Consequently, one cannot consistently achieve returns in excess of the average market returns on a risk-adjusted basis, given the information available at the time the investment is made, since before any investor acts on the information, the market will have adjusted the stock prices to reflect new information (Fama & French, 1992).

The three major versions of the hypothesis include: weak form, semi-strong form, and strong form. The weak-form EMH claims that prices on traded assets including stocks, bonds, or property already reflect all past publicly available information. The semi-strong-form EMH claims thatprices reflect all publicly available information. The strong-form EMH asserts that prices instantly reflect even hidden or insider information. Its proponents argue itis pointless to search for undervalued stocks or to try to predict trends in the market through either fundamental or technical analysis (Zareian, 2012).

While academics point to a large body of evidence in support of EMH, many dissensions have been raised. Critics have blamed the belief in rational markets for many of the late 2000s financial crisis. For example, investors, such as Warren Buffett have consistently

beaten the market over long periods of time, which by definition is impossible according to the EMH (Feng & Li, 2007). Detractors of the EMH also point to events, such as the 1987 stock market crash when the Dow Jones Industrial Average (DJIA) fell by over 20% in a single day, as evidence that stock prices can seriously deviate from their fair values.

In response, proponents of the hypothesis have stated that market efficiency does not mean having no uncertainty about the future.Market efficiency is a simplification of the world which may not always hold true, and that the market is practically efficient for investment purposes for most individuals.

2.2.2 Random Walk Theory

Consistent with the efficient-market hypothesis is the random walk hypothesis which is a financial theory stating that stock market prices evolve in a random fashion hence cannot be predicted (Hubert, 2001).The theory precisely states that stock price changes have the same distribution and are independent of each other, so the past movement or trend of a stock price or market cannot be used to predict its future movement. It is the notion that stocks take a random and unpredictable path. Proponents of the random walk theory believethat it is impossible to outperform the market without assuming additional risk.

Critics of the theory, however, contend that stocks do maintain price trends over time. They argue that it is possible to outperform the market by carefully selecting entry and exit points for equity investments. Martin Weber, a leading researcher in behavioral finance, found trends in stock markets after performing many studies. In one of his ten years stock market analysis, he looked at the market prices for noticeable trends and

found that stocks with high price increases in the first five years tended to become under-performers in the following five years contradicting the random walk hypothesis (Hubert, 2001). Another contradiction was his findings of stocks that had an upward revision for earnings outperforming other stocks in the following six months.

Hubert (2001) posits that an investor with this knowledge has an edge in predicting which stocks to pull out of the market and which stocks — the stocks with the upward revision — to leave in. Martin Weber's studies detract from the random walk hypothesis, because there are trends and other tips to predicting the stock market. Furthermore, the contradictions of the efficient market hypothesis allows for some investors to earn an abnormal earnings by capitalizing on the weaknesses in the market.

2.2.3 Symmetry Effect

Information asymmetry models that assume that one party to a transaction has relevant information whereas the other(s) do not, reveals that more information by a witty investors presents a potentially harmful situation because one party can take advantage of the other party's lack of knowledge. This would lead to adverse selection - the ignorant party lacks information while negotiating, and moral hazard - the ignorant party lacks information about performance of the agreed-upon transaction or lacks the ability to retaliate for a breach of the agreement (Leuz & Verrecchia, 2000).

2.3 Empirical Literature

Cases of works on information disclosure are summarized in the following paragraphs so that it is concluded with ease which information should be reflected in financial reports

and how people process information for achieving their prediction and decision making regarding future uncertain events as per available literatures.

Sing-Vey &Desay (1971) performed a research titled anexperimental quality analysis of financial disclosure by firms in USA. They argue that information disclosure by the firms may be in various forms and an annual report to stockholders is an important form of periodical disclosure. They found that: Disclosure quality is better in large firms compared to smaller ones. Also, disclosure quality is better in the firms with more number of stockholders. Further, disclosure quality is better in the firms audited by CPA institutes compared to the firms audited by small institutes.

Botosan (1997) performed a work titled as the disclosure level and cost of equity capital. He used annual reports of the firms and rating by Association for Investment Management and Research (AIMR) for measurement of voluntary disclosure level and found that the cost of equity capital was decreased by more voluntary disclosure.

Lwangu (2009) performed a study on the link between corporate governance, company size and company announcements on disclosure compliance for companies quoted at the NSE and noted that all 23 companies sampled had been complying with the corporate governance disclosures, but with the introduction of the other variables, he noted that most of the firms (84%), didn't comply when it came to corporate governance and board size but only 17.2% (4.3%) of the sample population did comply with the CMA regulations. There was also a positive correlation between company size and compliance but a negative correlation with company announcements which is attributable to the fact

that company announcements are a prerogative of the company's board and the law is not clear on what is or is not to be announced.

Wesonga (2008) performed a study on the use of financial disclosures for decision making by investors in Kenya with a case study of institutional investors at Nairobi Stock Exchange. The findings of the study led to the conclusion that majority of the institutional investors use financial disclosures as asource of vital information for investment decisions. Investors have exerted little pressure to managers and preparers of information for adequate disclosures. Further, Kenya lacked comprehensive legal framework to ensure relevant information flow for investment decision making and investor protection. Also, investors do not have confidence in financial analysts and stockbrokers in the use of relevant and reliable financial information. Investment decisions are complex and require both financial and non-financial information, insight and experience.

Mwirichia (2008) carried out a survey of corporate governance disclosures among Kenyan firms quoted at Nairobi stock exchange and found that financial sectors make more intensive corporate governance disclosure than the non-financial sector and that in general; companies have been found to be more active in making financial disclosures rather than non-financial disclosures. Local ownership, the size of the company, whether or not the company is a multinational, and size of the company were found notto have any significant impact on corporate governance disclosure.

Hail (2001) had earlier investigated the impact of voluntary corporate disclosure on the expected cost of equity capital and stated that quality of disclosure is inherently

subjective like cost of equity capital and its evaluation is very difficult. He scaled sample firms for fiscal year 1997 based on disclosure index in three categories for calculation of disclosure quality of financial accounts such as; Context and non-financial information including 10 items and totally 20 scores, procedural analysis and managerial analysis including 11 items and 20 scores, and information on value based risk and project related information including 9 items and 14 scores. Hail concluded that there is a negative and very important relationship between disclosure quality and the expected cost of equity capital.

Zareian (2012)conducted a post event correlation analysis seeking to establish whetherthere is a significant relationship between information disclosure quality and stock returns change in investment firms. With disclosure quality and stock returns as the variables, he conducted Kolmogorov - Smirnov test analysis on all firms listed in the Tehran stock exchange in the period 2004-2008. The findings were inconsistent. He noted thatin some years there was absolutely no correlation between disclosure quality and stock returns, yet there were some correlation in other years.

Barako (2007) while studying determinants of voluntary disclosures in Kenyan Companies Annual Reports observed that most voluntary disclosures are aimed at informing the public more about the positive attributes of the company than it is for negative attributes. He noted that rarely do companies report negative informations voluntarily. He further postulates that organizations cannot link their disclosures and financial performance.

Many literatures reveal that there are various reasons for reluctance of the firms to increased financial information disclosure level. Firstly, information disclosure informs everybody including competitors who become aware of the firm's unfavorable situation. This is harmful for stockholders. Secondly, they argued that labor unions may bargain better when they gain information on wages. Thirdly, they argued that investors are not able to understand accounting procedures and policies and information disclosure leads to their aberrance rather than their guidance. They also observed that other available information sources may provide financial information needed by investors with a lower cost than information provided by financial statements. Lastly, they advanced that the lack of awareness of investors' needs is a reason for limiting information and in fact less information disclosed.

2.4 Summary of Literature Review

Many theorists have underpinned the importance of financial information in advising the users of the financial information in their decision making. Since the users of the financial information are many and have diverse needs, theorists suggest that organizations can either offer a common financial information or a tailor-made annual report for the financial users' needs to be met. They all agree that the level of disclosure is not possible to be met notwithstanding the diverse needs of the financial information users.Furthermore, the cost of disclosure is most of the times uncompensated for. It is the general costs of information disclosures that calls for organizations to decide the extent to which to disclose. Executives' key question is for what value are the voluntary disclosures.

Literatures reveal that there is no relationship between voluntary disclosures and stock returns. Lack of relationship between disclosure quality and stock returns changes in investment firms is consistent with findings of different authors. On the other hand, lack of such relationship can be attributed to: limitation due to subjectivity of the disclosure quality measurement. That is, a change in disclosure quality measurement index will affect its value which may influence the research results. Also, it can be attributed to ineffectiveness of the markets. Again, investors in capital markets may not rely on financial accounts for decision making. The presence of other variables,of which authors may not be able to control, ormay be unknown by the author couldhave an influence on the research results. Finally, it may be due to limited voluntary information items provided by the firms resulting from disclosure culture in the different markets (Zareian, 2012).

Although no significant relationship was obtained between disclosure quality and stock returns, it is observed that the relationship direction is mostly positive. In other words, stock returns increase by increase in disclosure quality. Therefore, the firms can increase stock returns by increasing disclosure quality, though it is low.

Considering the necessity of increased knowledge in stockholders on investment in stock exchange, different markets ought to be studied in order to advise investors and corporate leaders accordingly. Furthermore, Kenya's capital marketis becoming a key target by the government to raise necessary capital to meet the national development needs. This predicts that more investors will invest in the stock markets and that many unlisted organizations are likely to be listed. The need to link the necessity of voluntary disclosure amongst the firms listed in the NSE is therefore paramount. Scanty literatures on the

effect of voluntary disclosures on stock returns in the context of the NSE listed firms exist and hence the necessity of this study.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter provides the methods and procedures employed to conduct the study. The chapter discusses the research design of the study, data collection methods and techniques employed to analyze the collected data.

3.2 Research Design

A research design refers to a systematic arrangement of the measures, factors and the tools to be applied in the collection and analysis of the obtained data in order to achieve the objectives of the study in the most efficient and effective way. Kothari (2004) posits that a research design directs the researcher by offering him or her with guidelines on how to collect, analyse and interpret the data in an coherent manner.

This study assumedadescriptive research design aiming to determine a causal relationship between voluntary disclosures and stock returns of the NSE listed firms. A descriptive study design canbe used to find out the present state of affairs in relation to what extent organizations voluntarily disclose non-statutory required data to the public and the implications the voluntary disclosure on the stock returns for a firm trading in the NSE.

Furthermore, the descriptive study design was preferred since it is suitable in its applicability within littletime and cost constraints (Mugenda & Mugenda, 2003). Further, it is dependable, valid and generalizablein this kind of a research in that it is good for the purposeof data collection and analysis, regardless of whether the data isqualitative or quantitative.

3.3 Population

Mugenda&Mugenda (2003) defines a population as a sum of all the items considered under a study. According to Bryman& Bell (2007), a population is the totality of the individuals and objects from which a scientifically generalizable inference can be achieved. The population for this study included the 62 companies in the Nairobi Securities Exchange as at August 1, 2013.

3.4 Sample and Sampling Method

Donald &McBurney (2009) define a sampling frame as the set of all the available sample units from which a researcher can choose. He further advances that the elements should be available in the frame at any given stage in the sampling process. According to Mugenda&Mugenda (2003), the sample frame should contain only the elements of the population which are eligible for selection.

This research studied the organizations composing the NSE 20 share index. The companies composed in computing the NSE 20share index were considered appropriate since their reporting was deemed conclusive and thorough as their financial reporting is vigilantly checked by the regulators for compliance, before their stock performance effect can be included in the 20 share index.

3.5 Data Collection Methods

This study used secondary data sources. Secondary data is the data that is already available having been collected in the past by other parties other than the researcher for the purpose of the current study (Mugenda & Mugenda, 2003). It is advantageous for its

availability, hencefast and easy to collect.Also, it is efficient in both monitory and time constraints. However, it is criticized for its likelihood for obsolescence.For the purpose of this study, secondary data collection was the only method that could be used and was utilized. Importantly, the impact of out-datedness would not arise, since the data considered spannedwithin the last 5 years between 2007 and 2012. This was important since this study sought to describe the effects of voluntary disclosure on stock returns for the firms listed in Nairobi Securities Exchange.

For the purpose of this study, asuccinct content analysis on financial reports of the sampled companies during the period 2008-2012was analyzed. Specifically, the studylooked for non-statutory disclosures related to inclusion of number of directors, board meeting attendance, breakdown of market data and informations on new products, trend analysis and comparisons with competitors and forward looking information like sales forecasts and expansion plans.

For the stock returns, the data on annual dividends and share prices of the sampled firms for the period 2008-2012 was obtained from NSE. The data was used to compute the stocks return for each period.

Through content analysis, the studyidentified voluntary disclosures that would improve the parameters which are generally included in balance score cards. These parameters include: Financial, "How do we look to shareholders?", Customer, "How do customers see us?" Internal business processes, "What must we excel at?", and Learning and growth factor "How can we continue to improve, create value and innovate?”

Voluntary disclosure aspects were rated in aspect to the above factors. In each reporting period, the extent of voluntary disclosure was rated on a scale between 1 and 5, where 1 meant very low and 5 very high voluntary disclosure. The ratings on each parameter was recorded accordingly alongside the variables X1, X2, X3 and X4.Similarly, the stock return computed using the dividends for each year plus the share price capitalization during the period was recorded accordingly.

3.6 Data Analysis Methods

The collected secondary data was analyzed using Statistical Package for Social Science (SPSS) version 20. A regression analysis was conducted on the data set. The Pearson ProductMoment was used to analyze the data in which correlation coefficient (R^2) and the coefficient of determination (R) of the data set (each form of voluntary disclosure, and stock returns) wasestablished. The findings from the analysis was organized, summarized and presented using tables, and used to answer the study question.

The relationship between voluntary disclosures and stock market performance for the purpose of this study was deemed to take the expression;

$R_i = a + b_1x_1 + b_2x_2 + b_3x_3 + b_4x_4 + \mu_e.$

Where;R_i(Computed as $\frac{d_1+P_1-P_0}{P_0}$) = Actual Stock Return, a = is the part of the stock return explained by other variables, x_1 = Voluntary business data disclosures, x_2 = Voluntary analysis of business data, x_3 = Voluntary forward-looking informations, x_4 = Information about management and shareholders and μ_e= refers to an error term.

Table 3.1: Categories of Voluntary Disclosures

Voluntary Disclosure	**Example**

Business data	Breakdown of market share growth and information on new products
Analysis of business data	Trend analysis and comparisons with competitors
Forward-looking information	Sales forecast breakdown and plans for expansion
Information about management and shareholders	Information on stockholders and creditors and shareholding breakdown

Source: (FASB, Annual report,2013)

CHAPTER FOUR: DATA ANALYSIS, RESULTS AND DISCUSSIONS

4.1 Introduction

This chapter presents the results of the analysis, findings and discussions onthe effect of voluntary disclosure on stock returns of companies listed at the Nairobi Securities Exchange.The data of the study was obtained through content analysis of the annual reports of the companies composing the NSE 20 share index as atAugust 1, 2013.

4.2 Descriptive Statistics

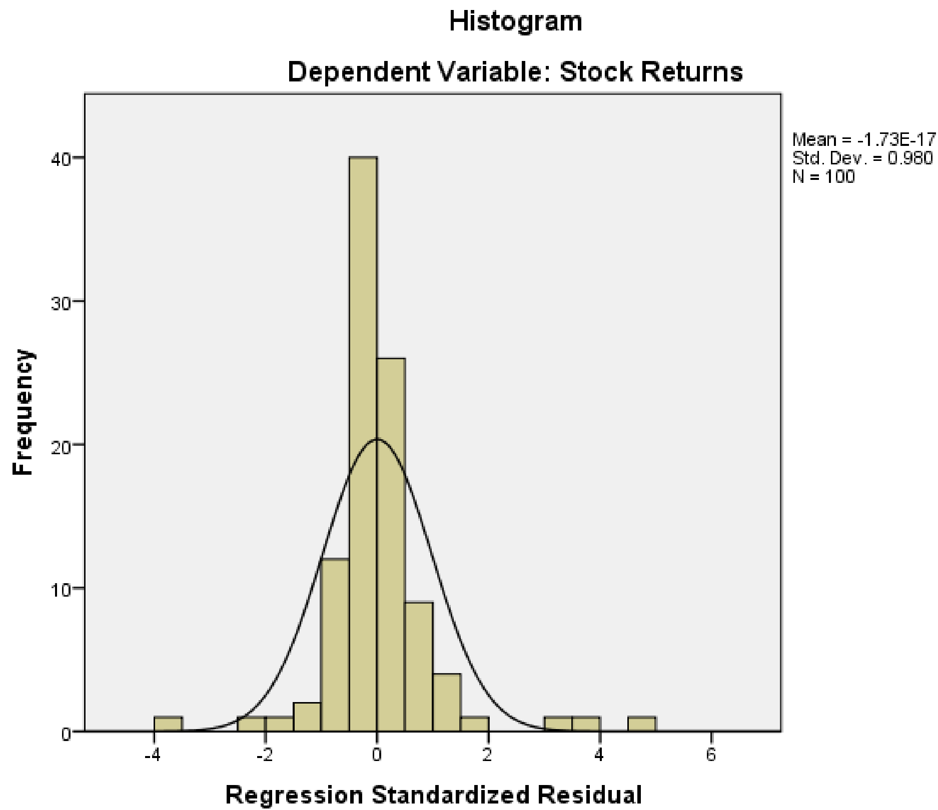
The study sought to establish the variability of the data used for the analysis.The findings revealed that the dataused had little variations as shown in the table 4.1 below. In particular, the mean and standard deviation for the stock returns during the period was 0.057 and 0.13 as shown below depicting that the stock returns obtained by the companies in NSE 20 Share averaged at 5.7% and varied thinly over the period2008 to 2012.

Table 4.1: Descriptive Statistics

Voluntary Disclosure Category	Mean	Std. Deviation	N
Stock Returns	.0572	.13069	100
Breakdown of market share growth and information on new products	3.8800	.74237	100
Trend analysis and comparisons with competitors	3.4600	1.21788	100
Sales forecast breakdown and plans for expansion	3.6800	1.17103	100
Information about management and shareholders	3.7400	1.12474	100

Source: Researcher, 2013

Figure 4.1: Test for Normality



Source: Researcher,2013

In testing for normality, the findingsrevealed that the stock returns for the NSE 20 Share companies followed a fairly normal distributionshape as shown in the histogram figure 4.1 above.

4.3 Ordinary Least Squares Analysis

4.3.1 Voluntary Business Data Release and Stock Returns

The analysis involved aregression of the indexes on voluntary disclosures of business data and stock returns. Business data sought included a breakdown of market share growth and information on new products. The analysis established a very weak linear

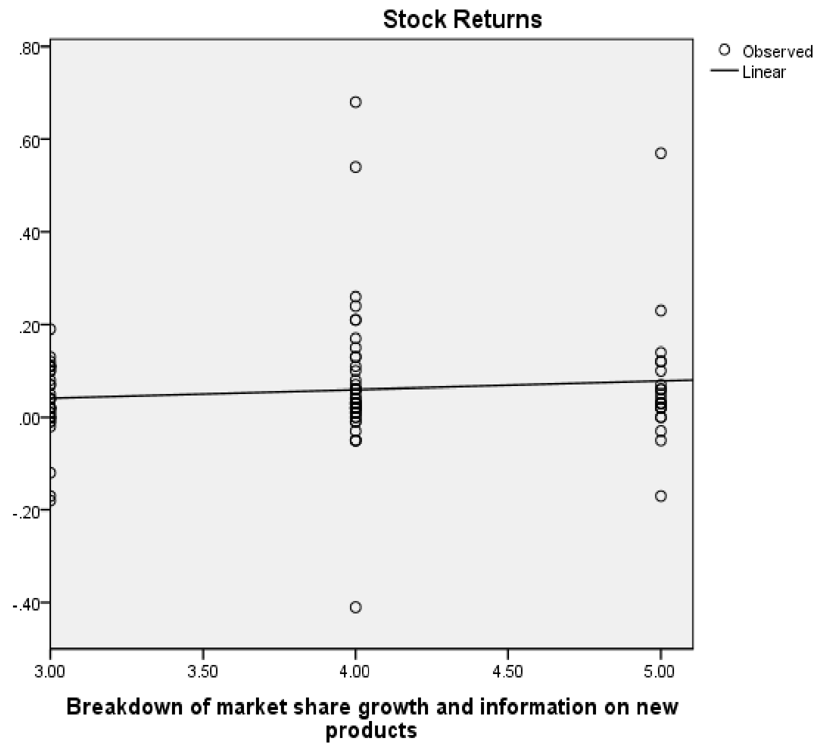
relationship of the form RI=0.019X1-0.016, with a coefficient of determination R of 0.107 and Pearson Product moments(correlation coefficient) R Square of 0.011 (almost 0) signifying a very weak or totally no relationship between release of voluntary market share growth analysis and information on new productson the stock returns of a company as shown in table 4.2and scatter diagram in figure 4.2below.

Table 4.2: Voluntary Business Data Releases and Stock Returns

Equation	Model Summary			Parameter Estimates	
	R Square	R	Sig.	Constant	b1
Linear	.011	0.107	.290	-.016	.019

Source: Researcher, 2013

Figure 4.2: Voluntary Business Data Releases and Stock Returns



Source: Researcher, 2013

4.3.2 Voluntary Analysis of Business Data and Stock Returns

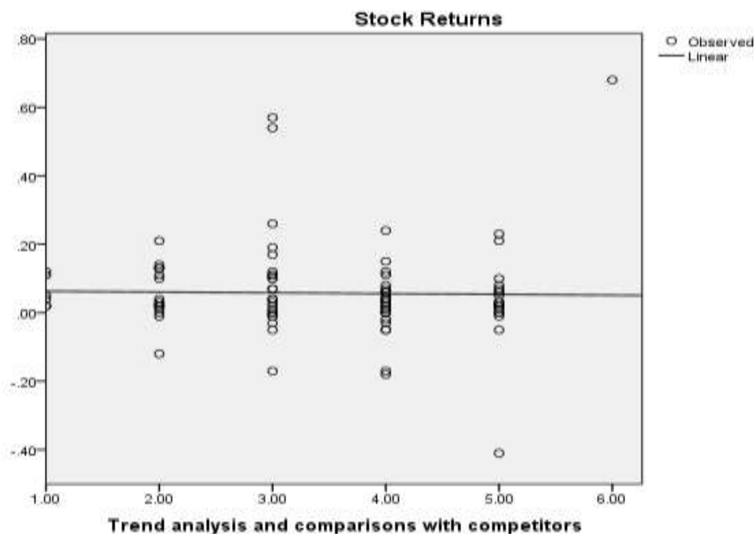
The research sought to establish the effect of voluntary disclosure of analyzed business data. The data sought through content analysis for this purpose included trend analysis and comparisons with competitors. It was established that there is no relationship between voluntary releases of trend analysis and comparisons with competitors as depicted by Pearson Product moment (correlation coefficient) R Square of 0.00 as shown in table 4.3and scatter diagram in figure 4.3 below.

Table 4.3: Trend Analysis and Comparisons with Competitors and Stock Return

Equation	Model Summary					Parameter Estimates	
	R Square	R	df1	df2	Sig.	Constant	b1
Linear	.000	0.022	1	98	.831	.065	-.002

Source: Researcher, 2013

Figure 4.3: Trend analysis and comparison with competitors Stock Return



Source: Researcher, 2013

4.3.3 Release of Forward-Looking Information and Stock Prices

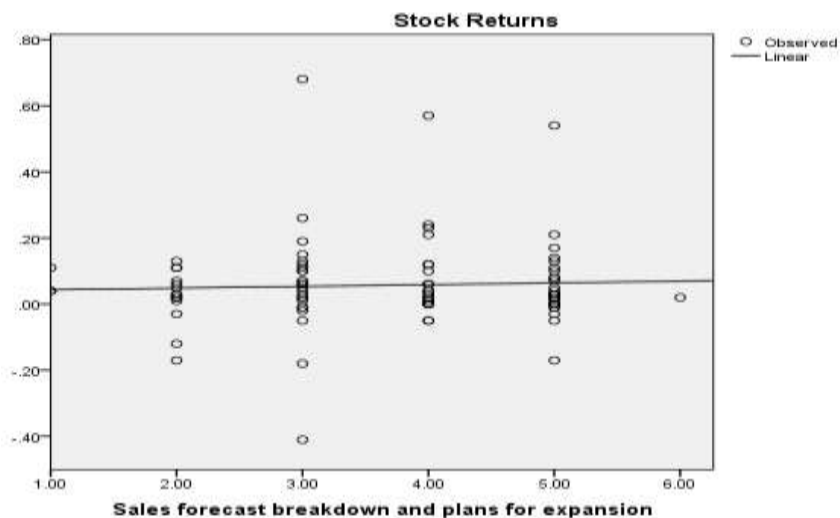
The analysis sought to establish the relationship between release of forward-looking information such as sales forecast and expansion plans and stock returns of an organization. As shown by Pearson Product Moments (correlation coefficient) of 0.002, the regression analysis revealed that there is no relationship between the release of forward-looking data such as sales forecast breakdown and plans for expansion as shown in table 4.4and figure 4.4below.

Table 4.4:Effect Sales Forecast Breakdown and Expansion Plans on Stock

Equation	Model Summary					Parameter Estimates	
	R Square	R	df1	df2	Sig.	Constant	b1
Linear	.002	.044	1	98	.643	.038	.005

Source: Researcher, 2013

Figure 4.4: Effect of Sales-forecast Breakdown and Expansion Plans on Stock Return



Source: Researcher, 2013

4.3.4Release of Information about Management and Shareholders on Stock Return

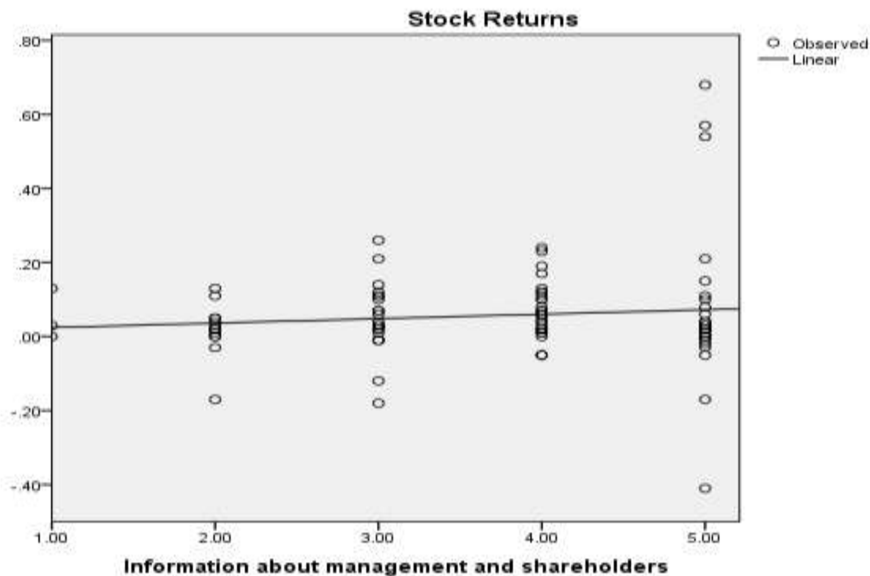
On regressing the indexes obtained through content analysis regarding the release of information on stockholders and creditors and shareholding breakdown with the stock returns, it was established that there is a very weak relationship between release of such information and stock returns of a company as depicted by a Pearson Product Moment (correlation coefficient) of 0.01 and coefficient of determination equal to 0.11 shown in table 4.5 and the scatter diagram in figure 4.5 below.

Table 4.5: Management and Shareholders information Release and Stock Return

Equation	Model Summary					Parameter Estimates	
	R Square	R	df1	df2	Sig.	Constant	b1
Linear	.011	0.105	1	98	.305	.012	.012

Source: Researcher, 2013

Figure 4.5: Management and Shareholders information Releases and Stock Return



Source: Researcher, 2013

4.4The Multiple Regression Model

The analysis also involvedconducting a regression on the stock return against the following four variables;

1) Breakdown of market share growth and information on new products,
2) Trend analysis and comparisons with competitors,
3) Sales forecast breakdown and plans for expansion, and
4) Information on stockholders and creditors and shareholding breakdown.

The analysis established a multiple linear regression model of the form with the coefficients shown on table 4.6;

$$R_i = -0.054 - 0.011x_1 + 0.022x_2 + 0.04x_3 + 0.013x_4$$

Table 4.6: Multiple Linear Coefficients

Model, Dependent Variable: Stock Returns	Unstandardized Coefficients	
		B
(Constant)	(b)	-.054
Trend analysis and comparisons with competitors	(x1)	-.011
Breakdown of market share growth and information on new products	(x2)	.022
Sales forecast breakdown and plans for expansion	(x3)	.004
Information about management and shareholders	(x4)	.013

Source: Researcher, 2013

Findings further established thatthe linear relationship between the stock return and the four predictor variables; Information about management and shareholders, Breakdown of market share growth and information on new products, Sales forecast breakdown and plans for expansion, Trend analysis and comparisons with competitors, isfaintly linear, or there is nolinear relationship with stock returns as is depicted bycoefficient of

determination of 0.171 and a Pearson Product moment (correlation coefficient)of 0.029(near to 0.00) as shown in table 4.6 below.

Table 4.7: The Strength of Linear Relationshipof the Multiple Linear Model

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
					Sig. F Change
1	.171[a]	.029	-.012	.13145	.586

Source: Researcher 2013

4.5 Discussions

Hail (2001) had studied the impact of voluntary corporate disclosure on the expected cost of equity capital and stated that quality of disclosure is inherently subjective like cost of equity capital and its evaluation is very difficult.

In this research, it was noted that voluntary disclosures such as; Information about management and shareholders, Breakdown of market share growth and information on new products, Sales forecast breakdown and plans for expansion, Trend analysis and comparisons with competitors, individually have no relationship with stock returns as depicted by Pearson Product Moment of equal or near 0.00.Even in the combined model, it was established that there is no relationship between voluntary disclosures and stock returns as depicted by a Pearson Product Moment 0.029.

Studies by Hail (2001)resolved that there is a negative and very important relationship between disclosure quality and the expected cost of equity capital.By conducting a post event analysis,Zareian (2012) sought to establish theeffect of information disclosure

quality on stock returns using data of all firms listed in the Tehran stock exchange for the period 2004-2008. He found many inconsistencies and noted that in some years there was absolutely no correlation between disclosure quality and stock returns, yet there were some correlation in other years.

This study conducted a longitudinal analysis of the voluntary disclosures and stock return of companies composed in the NSE 20 Share Index. The results of the analysis were consistent with past researchers such as Zareian and Hill.The results revealed that all the four forms of voluntary disclosure have very little or no relationship on stock returns.

CHAPTER FIVE: SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

The study sought to establish the effect of voluntary disclosure on stock returns of companies listed at the Nairobi Securities Exchange. This chapter provides a summary of findings as well as the conclusions and recommendations according to the objectives of the study.

5.2 Summary of Findings

Using a content analysis of the annual reports of companies composing the NSE 20 Share index, this study sought to unravel the effect of voluntary disclosure on stock returns of companies listed at the nairobi securities exchange. The research entailed conducting a content analysis of annual reports for the period 2008-2012.

Four categories of common voluntary disclosures such as release of;Breakdown of market share growth and information on new products,Trend analysis and comparisons with competitors,Sales forecast breakdown and plans for expansion, and the Information on stockholders, creditors and shareholding breakdown were identified.An index (1-5) for each year was assigned for each voluntary disclosure depending on the extent to which the company disclosed in its annual reports.

The four voluntary disclosure categories formed the predictor variables in a function with stock returns as the dependent variable hence the pre-formulated model;

$$R_i = a + b_1x_1 + b_2x_2 + b_3x_3 + b_4x_4 + \mu_e$$

Where;R_i(Computed as $\frac{d_1+P_1-P_0}{P_0}$) = Actual Stock Return, a = the part of the stock return

explained by other variables, x_1 = Voluntary business data disclosures, x_2 = Voluntary analysis of business data, x_3 = Voluntary forward-looking informations, x_4 =Information about management and shareholders

Firstly, a regression analysis (using SPSS) was conducted on each voluntary disclosure category with stock returns. The results revealed that stock returns of companies composing NSE 20 Share index are not affected by voluntary release of information such as;

1. Business data (market share growth and information on new products),
2. Analysis of business data (Trend analysis and comparisons with competitors),
3. Forward-looking information (Sales forecast breakdown and plans for expansion),
4. Information about management and shareholders,

On conducting a multiple linear regressionincluding the four variables, a weak linear model was established of the form;

$$R_i = -0.054 - 0.011x_1 + 0.022x_2 + 0.04x_3 + 0.013x_4$$

The analysis obtained coefficient of determination of 0.171 and a Pearson Product moment (correlation coefficient) of 0.029 (near to 0.00) for the multiple linear regression model. As such only 17.1% of the data points would be on a linear plot. With a Pearson Product Moment (correlation coefficient) 0.03, the findings revealed that there was no relationship betweenvoluntary disclosures and stock returns.

5.3 Conclusions

The findings of this study reveal that there exists no relationship between voluntary accounting disclosures and stock returns of companies listed in Nairobi Securities

Exchange. The findings of this research fairlyconfirmed the results of the research done elsewhere by Hail (2001) and Zareian (2012).

Hail (2001) established that there is no relationship between voluntary disclosures and stock returns. He however established that there is negative linear relationship between the voluntary disclosures and the cost of equity.As such,an increase in voluntary disclosures would reduce the cost of acquiring equity capital from capital markets. Hail (2001) held that increasing voluntary disclosuresreducethe cost of capital since such disclosuresincrease thedemand and liquidity of the company's stock. He posits that this reduces the cost of publicity and issuance of the stocks since investors know the firm better.

If voluntary disclosure enhances demand and liquidityof a stock, then it in turn would increase stock prices since increased demand causes an increasein price change. If this be the case, then voluntary disclosures would enhance stock return since stock price increase, results to a higher stock capitalization which would in turn enhance stock return.

Zareian (2012)studied the relationship between quality of voluntary disclosure and stock returns and sought to establish stock correlations between voluntary disclosure quality and stock returns each year. Zareian (2012) noted thatwhile there was absolutely no correlation between disclosure quality and stock returns in some years, there were some correlations in otheryears.

In this research, the four disclosures such as; business data (market share growth and information on new products), analysis of business data (Trend analysis and comparisons

with competitors), forward-looking information (Sales forecast breakdown and plans for expansion), and information about management and shareholders, individually did not reveal any correlation with stock returns.Even when combined, voluntary disclosuresdo not influence stock returns. Therefore,an increase (decrease) of voluntary disclosuresdoes notenhance (decrease) stock return.Their relationship is neither linear, nor does there exist any causation. As such, other factors and not voluntary disclosures are responsible to changes in stock returns of listed companies.

5.4 Recommendations

This paper recommends that, since there is no relationship between voluntary disclosures and stock returnsof the NSE listed companies, and since the theory links voluntary disclosure with reduction of cost of equity,the management of organizations should disclose voluntarily both for the purposes of reducing the cost of equity when they require it and also because it is synonymous to rendering of good corporate governance practice.

Even though the cost of reporting does not improve stock returns, it informs the public more about the organization hence a good corporate governance practice. Furthermore, a study byLopokoiyit (2012) obtained a direct relationship between corporate governance practices and share prices of the NSE listed companies. He also observed that corporate governance practices led to improvement of ratios such as; EPS, debt/equity ratio and return on assets.

Although no significant relationship was obtained between voluntary disclosure and stock returns, it is observed that the relationship direction is mostly positive though very small.

In other words, stock returns increase by increase in voluntary disclosure. Therefore, the firms can increase stock returns by increasing voluntary disclosure, though the relationship is weak.

5.5 Limitations of the Study

This study focused on the effect of voluntary disclosures and stock returns of NSE listed companies. The study sampled 20 companies composing the NSE 20 Share index. The research was constrained by time hence could not study voluntary disclosures of more companies or over a relatively long period, like 20 to 50 years.

Further, measurement of voluntary disclosures has always been a subjective exercise. Voluntary disclosures ratings established in other developed markets do not exist in the Kenyan context. The subjective measuremet of voluntary disclosures through assigning an index by the researcher would have affected the findings since different researchers will no doubt give different ratings.

5.6 Suggestion for Further Studies

The studyrecommends that further research focusing on the specific industriescould perhaps reveal more focused results as different industries may respond differently to certain information releases.

Also, an analysis of the effect of voluntary information release on stock returns as soon as it is releasedcan help depict the short term effect of such informationdisclosures on stock return.

Further, the researcher suggests that a study should be carried out on the relationship between voluntary disclosures and cost of capital in the context of Kenyan capital market.

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APPENDICES

Appendix I: Content Analysis: NSE 20 share index

This index primarily focuses on price changes amongst these 20 companies.The NSE 20-Share Index has been in use since 1964 and measures the performance of 20 blue-chip companies with strong fundamentals and which have consistently returned positive financial results. The Nairobi Securities Exchange Ltd 20 Share Index (^N20I) is a price weight index. The members are selected based on a weighted market performance for a 12 month period as follows: Market Capitalization 40%, Shares Traded 30%, Number of deals 20%, and Turnover 10%. Index is updated end of day only. Included in the Index are Mumias Sugar, Express Kenya, Rea Vipingo, Sasini Tea, CMC Holdings, Kenya Airways, Safaricom, Nation Media Group, Barclays Bank Kenya, Equity Bank, Kenya Commercial Bank, Standard Chartered Bank, Bamburi Cement, British American Tobacco, Kengen, Centum Investment Company, East African Breweries, EA Cables, Kenya Power & Lighting Company Ltd. and Athi River Mining.

Appendix II: Voluntary Disclosure Score Card

		DISCLOSURE SCORE				
Voluntary Disclosure	**Example**	**Very High 5**	**High 4**	**Moderate 3**	**Low 2**	**Very Low 1**
Business data	Breakdown of market share growth and information on new products					
Analysis of business data	Trend analysis and comparisons with competitors					
Forward-looking information	Sales forecast breakdown and plans for expansion					
Information about management and shareholders	Information on stockholders and creditors and shareholding breakdown					

Appendix III: Voluntary Disclosure Index (X_n), and Stock Returns(Y)

Company Name	Year	X1	X2	X3	X4	Y
Mumias Sugar	2008					
	2009					
	2010					
	2011					
	2012					
Express Kenya	2008					
	2009					
	2010					
	2011					
	2012					
Rea Vipingo	2008					
	2009					
	2010					
	2011					
	2012					
Sasini Tea	2008					
	2009					
	2010					
	2011					
	2012					
CMC Holdings	2008					
	2009					
	2010					
	2011					
	2012					
Kenya Airways	2008					
	2009					
	2010					
	2011					
	2012					
Safaricom	2008					
	2009					
	2010					
	2011					
	2012					
Nation Media Group	2008					
	2009					
	2010					
	2011					
	2012					
Barclays Bank Kenya	2008					

	2009					
	2010					
	2011					
	2012					
Equity Bank	2008					
	2009					
	2010					
	2011					
	2012					
Kenya Commercial Bank	2008					
	2009					
	2010					
	2011					
	2012					
Standard Chartered Bank	2008					
	2009					
	2010					
	2011					
	2012					
	2012					
Bamburi Cement	2008					
	2009					
	2010					
	2011					
	2012					
British American Tobacco	2008					
	2009					
	2010					
	2011					
	2012					
Kengen	2008					
	2009					
	2010					
	2011					
	2012					
Centum Investment Company	2008					
	2009					
	2010					
	2011					
	2012					

East African Breweries	2008					
	2009					
	2010					
	2011					
	2012					
EA Cables	2008					
	2009					
	2010					
	2011					
	2012					
KPLC Ltd	2008					
	2009					
	2010					
	2011					
	2012					
Athi River Mining	2008					
	2009					
	2010					
	2011					
	2012					
Total						

Appendix IV: List of companies on the Nairobi Securities Exchange

AGRICULTURAL	**TELECOMMUNICATION AND TECHNOLOGY**
Eaagads Ltd	AccessKenya Group Ltd
Kapchorua Tea Co. Ltd	Safaricom Ltd
Kakuzi	**AUTOMOBILES AND ACCESSORIES**
Limuru Tea Co. Ltd	Car and General (K) Ltd
Rea Vipingo Plantations Ltd	CMC Holdings Ltd
Sasini Ltd	Sameer Africa Ltd
Williamson Tea Kenya Ltd	Marshalls (E.A.) Ltd
COMMERCIAL AND SERVICES	**BANKING**
Express Ltd	Barclays Bank Ltd
Kenya Airways Ltd	CFC Stanbic Holdings Ltd
Nation Media Group	Diamond Trust Bank Kenya Ltd
Standard Group Ltd	Housing Finance Co Ltd
TPS Eastern Africa (Serena) Ltd	Kenya Commercial Bank Ltd
Scangroup Ltd	National Bank of Kenya Ltd
Uchumi Supermarket Ltd	NIC Bank Ltd
Hutchings Biemer Ltd	Standard Chartered Bank Ltd
Longhorn Kenya Ltd	Equity Bank Ltd
INSURANCE	The Co-operative Bank of Kenya Ltd
Jubilee Holdings Ltd	**MANUFACTURING AND ALLIED**
Pan Africa Insurance Holdings Ltd	B.O.C Kenya Ltd
Kenya Re-Insurance Corporation Ltd	British American Tobacco Kenya Ltd
CFC Insurance Holdings	Carbacid Investments Ltd
British-American Investments Company (Kenya) Ltd	East African Breweries Ltd
CIC Insurance Group Ltd	Mumias Sugar Co. Ltd
INVESTMENT	Unga Group Ltd
City Trust Ltd	Eveready East Africa Ltd
Olympia Capital Holdings ltd	Kenya Orchards Ltd
Centum Investment Co Ltd	A.Baumann CO Ltd
Trans-Century Ltd	**ENERGY AND PETROLEUM**
CONSTRUCTION AND ALLIED	KenolKobil Ltd
Athi River Mining	Total Kenya Ltd
Bamburi Cement Ltd	KenGen Ltd
Crown Berger Ltd	Kenya Power & Lighting Co Ltd
E.A.Cables Ltd	
E.A.Portland Cement Ltd	