

**RELATIONSHIP BETWEEN PROFIT WARNINGS AND STOCK RETURNS OF
COMPANIES LISTED AT THE NAIROBI SECURITIES EXCHANGE**

SUBMITTED BY:

FLORENCE ATIENO ABUOR

D61/70056/2007

SUPERVISOR

DR. JOSIAH. O. ADUDA

**A RESEARCH PROJECT SUBMITTED TO THE SCHOOL OF BUSINESS IN
PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF
MASTERS DEGREE IN BUSINESS ADMINISTRATION OF UNIVERSITY OF
NAIROBI**

NOVEMBER, 2014

DECLARATION

This research project is my original work and has not been presented for an academic award in any other institution of higher learning.

Signature.....

Date.....

FLORENCE ATIENO ABUOR

D61/70056/2007

This research project has been submitted for examination with my approval as the University Supervisor.

Supervisor's Signature.....Date.....

DR. JOSIAH. O. ADUDA

DEDICATION

This research project is dedicated in memory of my father the late Mr. Martin Abuor Odera who inspired me to attain my academic potential. To my husband Victor for his continued support and encouragement. To my children Liam and Arthur for bringing out the desire and need for me to achieve this milestone.

ACKNOWLEDGEMENTS

To the Lord God Almighty! I am not competent to claim anything for myself but my competence comes from God. Indeed he has been faithful to me and I give him all the glory

To the entire UON Business School Staff and MBA Co-ordination office for providing necessary information regarding the project and also for their support in completing the project. Special thanks to my supervisor Dr. Aduda for his precise and concise guidance in relation to the project.

I would like to extend my gratitude to all my friends and colleagues in the Financial Services industry who played a great role in helping with collection of secondary data necessary for the completion of my project. A big thank you for the effort and your time.

I would like to express my gratitude to my entire family for their continuous encouragement and support. Indeed you were the wind beneath my wings.

TABLE OF CONTENTS

DECLARATION	ii
DEDICATION	iii
ACKNOWLEDGEMENTS	iv
TABLE OF CONTENTS	v
LIST OF TABLES	ix
ABBREVIATIONS	x
ABSTRACT	xi
CHAPTER ONE	1
INTRODUCTION	1
1.1. Background of the Study.....	1
1.1.1 Profit Warnings.....	3
1.1.2 Stock Returns.....	5
1.1.3 Relationship between Profit Warnings and Stock Returns.....	7
1.1.4 The Nairobi Securities Exchange	9
1.2 Research Problem.....	10
1.3 Objective of the Study.....	11
1.4 Value of the Study.....	11
CHAPTER TWO	13
LITERATURE REVIEW	13
2.1 Introduction.....	13
2.2 Theoretical Review	13
2.2.1 Keynesian Theory.....	13
2.2.2 Resource-based view	13
2.2.3 Signalling Effect Theory	14
2.2.4 Efficient Market Hypothesis (EMH)	15
2.3 Empirical Review	16
2.3.1 Market Reaction on the Qualitative Warnings and Quantitative Warnings on Stock Returns.....	16
2.3.2 Information Content of a profit warning announcement and the market reaction	18
2.4 Event Study Methods	18

2.5 Summary	19
CHAPTER THREE	20
RESEARCH METHODOLOGY	20
3.1 Introduction.....	20
3.2 Research Design	20
3.3 Population	20
3.4 Data Collection	21
3.5 Data Analysis and Presentation	21
CHAPTER FOUR	24
DATA ANALYSIS AND PRESENTATION OF FINDINGS	24
4.2 Data Presentation.....	25
4.2.1 Year 2007	25
4.2.2 Year 2008	26
4.2.3 Year 2009	27
4.2.3 Year 2010	28
4.2.4 Year 2011	28
4.2.5 Year 2012	29
4.2.6 profit warnings.....	30
4.2.7 Summary statistics of Abnormal Returns.....	30
4.3: Summary and interpretation of Findings.....	33
CHAPTER FIVE : SUMMARY, CONCLUSIONS AND RECOMMENDATIONS	35
5.1 Summary	35
5.2 Conclusions	36
5.3 Policy Rrecommendations.....	37
5.4 Limitations of the study.....	38
5.5 Suggestions for further studies	38
References	39
Appendices	43
Appendix I: Companies that have issued profit warnings	43
Appendix II Stock Returns Data Collection Kit (Kshs ‘000)	44
2012	49

Appendix III :Actual profit warning..... 50

LIST OF FIGURES

Figure 4. 1: Abnormal Returns curve 33

LIST OF TABLES

Table 4. 1: Year 2007 Coefficients ^a	26
Table 4. 2 :Year 2008 Coefficients ^a	27
Table 4. 3: Year 2009 Coefficients ^a	27
Table 4. 4:Year 2010 Coefficients ^{a98}	28
Table 4. 5 :Year 2011 Coefficients ^a	29
Table 4. 6: Year 2012 Coefficients ^a	29
Table 4. 7:profit warnings.....	30
Table 4. 8 :Abnormal Returns.....	32

ABBREVIATIONS

CARs Cumulative Abnormal Returns

NSE Nairobi Securities Exchange

ABSTRACT

A profit warning is a public announcement saying that earnings for a reported period will not meet expectations (Bulkley & Herrerias, 2004). Firm managers tend to issue a profit warning when previous forecasts are believed to be too optimistic or unforeseen changes in economic or operational conditions have occurred. Stock markets need a flow of relevant and timely information to function efficiently. Most firms have the objective to actively inform the market and meet regulatory requirements. An example of a price sensitive event is a profit warning announcement. In Kenya, a lot of studies have been performed on NSE but a few studies have been done in Kenya. Muhoro (2004) and Ngigi (2006) found conflicting results on the application of value and growth styles at the NSE, this study therefore sought to establish the effect of profit earnings on stock returns applied by investors at NSE. The general objective of this study was to establish the relationship between profit warnings and stock returns of companies listed at the Nairobi Securities Exchange. In this study event study methodology was applied. An event study design was chosen because it enabled the researcher to generalize the findings to a larger population. The population of interest in this study consisted of all the firms quoted at the Nairobi Securities Exchange (N.S.E). The study therefore picked the 10 companies issued profit warnings in the year 2012 for the period 2007 - 2012. Creswell (2002) defines data collection as means by which information is obtained from the selected subjects of an investigation. The study utilized secondary data for the period 2007 to 2012. The study found out that from year 2007-2012 Book value /market and earnings/profit was found out to be positively related to daily returns and consequently the average return over the five years. The result of research Study indicates that profit warning has impact on the stock return in NSE and the impact is negative and significant for the period of pre-warning and post-warning and on the day of actual announcement. The study recommends that profit warning being the pure information, unscheduled, and unexpected corporate announcement should be issued prior to the actual earnings announcement with the purpose of informing the market thus reducing the negative impact of the earnings surprise.

CHAPTER ONE

INTRODUCTION

1.1. Background of the Study

Profit warnings are issued by companies that anticipate a forthcoming earnings outcome that will be significantly below current expectations. A study on the post-event stock performance following a first-time profit warning signal in US by Bulkley and Herrerias (2005) who studied stock returns following a first-time warning in the US between February 1998 and December 2000 show that stock returns continue to drift downward up to six months after an initial warning and attribute this evidence to market under reaction. Moreover, they show that the duration and magnitude of the drift is significantly different for qualitative and quantitative warnings. For qualitative warnings the drift lasts about six months with significant abnormal returns of 11, 78%. For quantitative warnings the drift last about three months with significant abnormal returns of -1.98%.

Elayan and Pukthuanthong (2009) studied post-announcement returns following a quantitative warning containing a point estimate. The results showed significant abnormal returns of -5% the first three months following a warning. In total the drift lasts for approximately eight months. Skinner (1994) study on voluntary earnings-related disclosure for 93 randomly chosen NASDAQ firms during the period 1981-1990. The results show that the majority (approximately 67%) of disclosure announcements contain bad news related to the upcoming quarterly earnings announcement. According to Skinner (1994) management issues an earnings warning in order to minimize litigation and reputation costs. Under the US security laws, shareholders have the possibility to sue a firm whenever it fails to disclose bad news in a timely manner. By disclosing bad news as soon as possible firms minimize the time frame for a shareholder to file a lawsuit. Moreover, it is more difficult for shareholders to accuse a firm from withholding bad news when the source of the voluntary disclosure is the firm itself.

Baginski, Hassel and Kimbrough (2002) examined the US and Canadian market and found a similar positive influence of litigation risk on the decision to warn. On the other hand, reputation costs arise as market participants are more reluctant to follow a firm which is known to withhold

unfavorable news. Consequently, failure to communicate bad news lowers the price and liquidity of a firm's stock price, which increases the cost of capital. In addition, Libby and Tan (1999) interviewed several stock market analysts and conclude they prefer warning firms over non-warning firms. Analysts perceive warning firms as more integer and are more likely to continue coverage. Furthermore analysts indicated that non-warning firms incur more damage to their reputation than warning firms.

In the Netherlands, Church and Donker (2010) also implemented the disclosure theory of Milgrom (1981). The main difference is that they treat firms that hold external factors responsible for the warning as partial disclosure and firms that hold internal factors responsible for the warning as full disclosure. The results show that for repeated warnings the market reaction is weaker for firms adopting a full disclosure policy. Furthermore, Church and Donker (2010) examined whether the market reaction differs for firms disclosing external or internal reasons as the motive for issuing a profit warning, whereas this study focuses on the difference between two types of warnings.

Conventional wisdom suggests that market participants, particularly shareholders and stock analysts, do not like to receive bad news, more especially when it comes as a surprise. Perhaps this explains why over the past five years an increasing number of companies are choosing to voluntarily issue profit warning statements. However, given the fact that these profit warning announcements merely serve to presage the later, official report of lower earnings, one might question why firms bother to issue the warning at all?

Another area of concern for some observers is that events are often not just information but are also decisions that have direct consequences for cash flows and the risk characteristics of the firm (Ikenberry and Ramnath, 2002). Profit warnings are an example of the discretionary disclosure of information by firms and therefore, as well as making a contribution to the general debate about under reaction, they are an event that is of particular interest in the context of the resurgence of interest in the question of how disclosures should be regulated (Milgrom, 1981; Grossman, 1981; Boot and Thakor, 2001; Admati and Pfleiderer, 2000). The two classes of warning allow us to test the well-known result in this literature (Milgrom, 1981) that a firm will only fail to fully disclose its information in the worst possible state, and the market will therefore

interpret lack of full disclosure as particularly bad news. We test whether qualitative warnings are indeed worse news than warnings that include an earnings forecast, and whether the market interprets them as such. We discuss below whether there is any evidence that firms that issue qualitative warnings are simply less well informed.

1.1.1 Profit Warnings

A profit warning is a public announcement saying that earnings for a reported period will not meet expectations (Bulkley & Herrerias, 2004). Firm managers tend to issue a profit warning when previous forecasts are believed to be too optimistic or unforeseen changes in economic or operational conditions have occurred. The content of the shortfall may be in terms of net profits, sales, and earnings before interest and taxes etc. The warning is issued prior to the mandatory scheduled earnings announcement (Malkiel, 2003). There are two features of profit warnings that make them an important event to investigate, apart from the size of their initial impact on prices. The first is that they are signals about a specific realization, and one which will be observed in the very near future. Approximately 90% of profit warnings precede the earnings announcements by less than three months. If there is any under reaction then the correction should be a fairly short and sharp process. The second feature is that warnings fall into two classes, those that present a new earnings forecast, either a point estimate or a range, and those that offer only the qualitative guidance that earnings will be below current expectations. This offers an opportunity to test not only whether the market under reacts to the new information, but also whether the scale of any under reaction depends on the precision of the sign (Church and Donker, 2010).

In order to determine the true value of firm, investors need credible, substantive, and timely value relevant information from firm (Ogden, Jen and O'Connor, 2003). Rules and mechanisms exist in the financial market to make such information available to investors. Disclosure rules are one way to reveal the information to the market. Disclosures provide information to investors so that they rationally value the firm, as result market price of a firm could be efficient (Ogden et al., 2003). As one form of information disclosure, profit warnings decrease the information asymmetry between markets and firms. It reveals the financial condition and result of the operation in advance of financial statement even though it has negative consequence (Eilifsen, Messier, Glover, Steven and Prawitt, 2009). Firms share the information with market that they will not meet the market expectation regarding the performance.

Bulkley & Herrerias (2004) called the profit warning as unexpected corporate announcement which prescriptive forthcoming period earnings will decrease below current expectations. They also pointed out an important opinion that profit warnings are pure information rather than a decision that the firm makes according to the direct material consequences. Namely the profit warnings are not the realization, but are the news before a specific and imminent realization, the earnings announcement.

Collett (2004) also categorized profit warnings into unscheduled announcements and claimed the profit warning is not actual results announcements. He investigated the market response to the scheduled and unscheduled announcements and identified unscheduled announcement resulted in greater reaction of market from 1995 to 2001, which is a bullish stock market conditions in UK. That means it was probably the good news dominated negative news in this period. Collett (2004) detected compared to the first profit warning, the second one will trigger more negative market reaction within half year period.

Studying returns following profit warnings naturally invites comparison with the literature which has investigated returns following scheduled earnings announcements. Abnormal returns in the months following an earnings announcement are usually found to be on average of the same sign as the initial surprise. For example Bernard and Thomas (1989) find the docile portfolio of stocks with the biggest negative surprises delivered cumulative abnormal returns of approximately -2.2% in the 60 days after the announcement. This latter figure is very similar to the negative abnormal returns reported here in the first three months following a quantitative profit warning. Bernard and Thomas also found that the under reaction was more pronounced for small firms, a result which is also confirmed here.

Abnormal returns are also traced for one year before the profit warning. Since these are for a sample constructed with the hindsight that a warning was eventually issued any abnormal returns found cannot be interpreted as a profitable trading opportunity. Nevertheless it may be of interest to see the performance of firms that issue profit warnings in a long-term context. For example do profit warnings come as a complete surprise or do they follow a string of negative public and/or

private signals, and if so for how long on average has the market been receiving negative news about these companies? Abnormal returns prior to warnings will contribute some evidence on these questions.

1.1.2 Stock Returns

Through media, analysts reach millions of individual investors. At the same time, analysts are also influential among institutional investors such as mutual fund managers that manage most of the capital under management. More importantly, banks rely on analysts to get investment-banking deals. To summarize, analysts can generate hefty trading commissions for their brokerage houses. While analysts perform many tasks, among the most important is generating earnings forecasts. One reason is because investors care about whether the firm will meet its earnings forecasts.

Analysts can more finely signal their views on stocks with earnings forecasts than with stock recommendations (Church and Donker, 2010). Based on survey analysis, Block (1999) presents evidence that investors regard earnings forecasts rather than recommendations as a highly important input into their valuation models. Analysts process a substantial amount of information, so their forecasts are superior to those derived from simple time-series models; see Brown and Rozeff (1978) and Brown, Griffin, Hagerman, and Zmijewski (1987). When firms report earnings that exceed analyst forecasts, their stock prices increase. By contrast, when firms report earnings that fall short of analyst forecasts, their stock prices decrease. The simple fact is that news creates surprises, and surprises create volatility and trading opportunity.

Until the 1980s, there was a general consensus among financial economists that stock prices follow a “random walk” —in other words, price changes are random and therefore unpredictable (Pesaran, 2010). This is consistent with the existence of an “efficient” market for stocks, which is defined by Fama (1970). An “efficient” market is a market in which stock prices immediately and fully reflect all the available information. In an efficient market, price changes must be a response only to new information. Therefore, it is impossible to earn abnormal returns by forecasting future stock returns, or in other words, it is impossible to outperform the market consistently (Malkiel, 2003). If stocks would be predictable, then investors would reap unlimited

profits by purchasing those stocks that, according to the model, were about to increase in price and by selling those stocks about to fall in price. Suppose the stock price is about to increase by 10 %; all investors would like to buy the stock, but no one would like to sell. Therefore, the stock price would immediately reflect the forecast news and would immediately increase by 10% (Bodie et al., 2009; Granger and Timmerman, 2004).

Subsequently, the efficient market has been categorized into three forms of efficiency, depending on the definition of the available information. The weak form efficiency states that the current stock prices reflect all the information contained in the past history of the stock prices. This implies that the past history of stock prices cannot be used to generate abnormal returns. The semi-strong form of efficiency asserts that the stock prices incorporate all publicly available information. Apart from the past prices (weak form), public information also includes macroeconomic information (inflation, money supply, interest rates), information of the firm's profit, dividends, etc. The strong form of efficiency determines that the stock prices reflect public as well as private information. Private information is information that is only available to company insiders (Bodie et al., 2009; Malkiel, 2003).

In the event of a corporate failure, the shareholders are last in line, behind all the other stakeholders, to get invested capital back. Thus their need for timely and accurate indications on the wellbeing of their investments is crucial (Holder - Webb & Cohen, 2007). The role of disclosures is, in principle, to provide timely information to avert the mispricing of stock by traders who would otherwise remain uninformed; and reduce the cost of capital for firms in general through the reduction of information risk (Collett & Hrasky, 2005; Graham, Harvey, & Rajgopal, 2005; Healy & Palepu, 2001).

Bhagat and Frost (1986) have all studied the costs of raising capital. Their study finds evidence of economies of scale in the offering process. That is, very large issues tend to enjoy a relatively lower cost of going public and very small issues tend to pay a relatively larger price to conduct an IPO. Additionally, for issues that are neither very large nor very small, Chen and Ritter (2000) document that over 90 percent of the issues pay a gross underwriter spread of exactly 7 percent.

The literature on the costs of going public cost is descriptive in nature. As such, this study reports the summary statistics of the total expenses required to take the firm public. The issue of firm size has become such a common element to use as a control variable in empirical corporate finance studies that it hardly receives any discussion in most research papers even though it is among the most significant variables. In international circles, evidence has been obtained to assert that leverage is cross-sectionally positively related to size. Obviously, firm size matters for a number of reasons.

1.1.3 Relationship between Profit Warnings and Stock Returns

According to the efficient market hypothesis (Fama, 1970) stock prices fully reflect all available information and change when new information arrives in the market. A firm that issues a profit warning discloses public information to investors that earnings will fall below expectation. If investors perceive this information as new and value relevant there should be a negative stock price reaction at the time of the announcement. Moreover the relevance of a profit warning is underlined by several studies (Jackson & Madura, 2003; Bulkley & Herrerias, 2005; Church & Donker, 2010), who provide evidence of strong negative abnormal returns at the time of a profit warning announcement.

The semi-strong efficient market hypothesis suggests that stock prices react quickly in an unbiased manner to public announcements. However, in the literature a vast amount of researchers (Bernard & Thomas, 2004) provide evidence that stock returns continue to drift downward after a negative earnings surprise reported at the scheduled earnings announcement date. The predominant explanation for this phenomenon is that markets under react to new information. Since profit warnings can be classified as unscheduled earnings information containing a surprise it is interesting to see whether there is a similar drift.

Bulkley & Herrerias (2004) examined the abnormal returns for stocks bought two days after a profit warning and held for the succeeding six months following qualitative and quantitative profit warnings respectively. In the beginning of this test, they preferred to choose the next twelve months after releasing profit warnings as the observation period. After tracing the abnormal returns over one year, they did not find significant abnormal returns between the sixth

and twelfth months. Therefore, they narrowed down the first six months to do research using the measurement methods of CARs and BHARs. No matter which methods they adopt, they found more negative abnormal returns following qualitative profit warnings than following quantitative ones. The result supports their opinion about the qualitative warnings are regarded as worse news than quantitative warnings.

Tucker (2006) did research on both warning and non-warning firms and raised the opinion against previous researchers' findings which the openness seems like punishment for warning firms by investors. Indeed, the author found the warning firms had lower returns than non-warning firms in short term window, five days after earnings warnings. However, returns were similar between warning and non-warning firm in long term like three months. Jennifer considered the reason was self-selection bias and identified around earnings warnings. Warning firms issued more non-earnings news than warning firms. This situation was always ignored in prior researches. Investors might not fully react on other bad news, which might affect the returns around earnings warnings.

Elayan & Pukthuanthong (2009) did research on US market from 1997 to 2002 and also found the market had negative respond for the profit warning, -16.59% cumulative average abnormal returns over the two-day announcement period. The reason was these warning announcements would probably be explained as bad news by the market participants. That resulted in significantly negative reaction from the market. Jackson & Madura (2003) tested the mean two-day cumulative abnormal return (CAR) following profit warnings and obtained the -14.72% of CAR which was 32 times of CAR following the succeeding earnings announcement. It proves the profit warning can reduce the blow of earnings surprises to the market before the earnings announcements are released. Moreover, they found the profit warnings were under reacted by the market at the announcement day since substantially negative CARs occurred till a four-day period after the announcement day. However, their other finding is different from other researchers' worry about the market overreaction. Even though the drastic market reaction happened at the warning announcement, there is no indication of a reversal in the following trading days and no evidence shows that market response to profit warnings is excessive. Therefore, they did not believe the market would overreact the profit warning.

1.1.4 The Nairobi Securities Exchange

The Nairobi Securities Exchange was formed in 1954 as a voluntary organization of securities brokers and is now one of the most active securities markets in Africa. The administration of the Nairobi Securities Exchange Limited is located on the “Exchange” on 55 Westlands Road, Nairobi. As a capital market institution, the Securities Exchange plays an important role in the process of economic development (www.nse.co.ke, 2013). The Nairobi Securities Exchange deals in both variable income securities and fixed income securities. Variable income securities are the ordinary shares, which have no fixed rate of dividend payable, as the dividend is dependent upon both the profitability of the company and what the Board of Directors decides. The fixed income securities include treasury and corporate bonds, preference shares, debenture securities - these have a fixed rate of interest/dividend, which is not dependent on profitability (www.nse.co.ke, 2013).

According to the Business Daily dated December 2nd 2012, Profit warnings at the Nairobi Securities Exchange on Friday rose to 10 in a performance that has investors who got only two such alerts last year lose billions of shillings through share price erosions. Agricultural firm Kakuzi joined Longhorn, Eaagads, Express Kenya, KenolKobil, Sasini, East African Portland Cement Company (EAPCC), Kenya Airways (KQ), Mumias and Kapchorua Tea, which all said their profits would drop by more than 25 per cent.

In 2011, only Total and CMC Holdings issued profit warnings. The increased warnings highlight the challenges corporate Kenya is facing in an economy that is feeling the weight of expensive credit, high inflation, and political jitters linked to next year’s General Election. Most of these companies have seen their market value decline at the Nairobi bourse over the past six months in a period that has seen the stock market gain 23.3 per cent, aided by the performance of most blue chip firms and increased foreign investor interest. The high profit alerts this year has been driven by the weak local and global economy besides other unique factors that have eroded earnings of individual firms. Investors in the companies that have issued profit warnings are set to get lower or no dividend this year, besides suffering share price erosion. This comes at a time when the market has gained 23.3 per cent over the past six months to a capitalization of Sh1.2 trillion from Sh1 trillion.

In the same period, EAPCC's share price dipped 31.2 per cent to Sh42 as KQ's share lost 18.5 per cent to Sh12.2. Other firms that recorded share price erosion in the same period include Eaagads and Kakuzi whose shares dropped 30.4 and 12.5 per cent respectively to Sh24.5 and Sh70 a piece. Investors in other companies that have posted strong profit growth have, however, seen their paper wealth rise by double digits, highlighting the negative impact of losses and slow earnings on investor wealth. Safaricom investors have benefitted the most, with the stock's price rising 50.7 per cent over the past six months to Sh4.9, with the company reporting a 98.3 per cent growth in net profit to Sh7.7 billion in first half ended September. City Trust, Pan Africa Insurance, and Standard Chartered Kenya are other top gainers that have seen their share rise by double digits. Eaagads made a net loss of Sh81.4m in the six months to September compared to a profit of Sh26.3 million the year before. This is the reason this study seeks to investigate the relationship between profit warnings and stock returns evident in selected companies in the Kenya market. This study will select all the companies listed in the NSE that have issued profit warnings in the period 2007 to 2012. This will make it relevant to investigate the relationship between the profit warnings and the stock returns.

1.2 Research Problem

Stock markets need a flow of relevant and timely information to function efficiently. Most firms have the objective to actively inform the market and meet regulatory requirements. An example of a price sensitive event is a profit warning announcement. Firm managers tend to issue a profit warning when previous forecasts are believed to be too optimistic or unforeseen changes in economic or operational conditions have occurred. Such a statement is an extremely visible signal to investors declaring a significant negative change in the performance of a firm. What effect does such an extreme disappointment have on stock returns? This research will examine the relationship between profit warnings and stock returns evident in selected listed in the NSE

Investors who participate in the capital markets expect that their investment will bring a high return in the future which will compensate for the related risks and expenses. Thus, they evaluate the investment; they calculate the benefits and the costs at the same time, which is the net present value calculation (Bodie et al., 2009, p.9). However, firms that sell their shares to investors will receive more funds if stock prices are high, so that these firms can grow and produce values or assets in the economy (Bodie, Kane, & Marcus, 2009, p.5). The stock prices play a signaling role

in the distribution of the economic resources from investors to firms. (Fama, 1970, p.383) From a broader perspective, in order to efficiently allocate the funds in society, it is important that the stock market valuation process and prices is correct (Arnold, 2008, p.567). The incorrect value of the stock today or tomorrow can be harmful in ten or twenty years and therefore impact the economy and society in terms of uneven allocation of resources. Today's and tomorrow's lower or higher than true value of the stock can be harmful in ten or twenty year's economy and society in terms of asset allocation thus value creation (Arnold, 2008, p.567).

In Kenya, for instance, a lot of studies have been performed on NSE but a few studies have been done in Kenya. Muhoro (2004) and Ngigi (2006) found conflicting results on the application of value and growth styles at the NSE, this study therefore sought to establish the effect of profit earnings on stock returns applied by investors at NSE.

1.3 Objective of the Study

The general objective of this study was to establish the relationship between profit warnings and stock returns of securities listed at the Nairobi Securities Exchange.

1.4 Value of the Study

The study will be useful to the commercial sector and to a larger extent other industries. It will help them understand the importance of profit warnings and how different firms can achieve stock returns.

The study will also help other managers to know the methods used in gathering and applying profit warnings; will help them improve their management styles. Since profit warning is a public announcement saying that earnings for a reported period will not meet expectations. Firm managers tend to issue a profit warning when previous forecasts are believed to be too optimistic or unforeseen changes in economic or operational conditions have occurred. Such a statement is an extremely visible signal to investors declaring a significant negative change in the performance of a firm. What effect does such an extreme disappointment has on stock returns? This research will examine the relationship between profit warnings and stock returns evident in selected companies in the Kenya market. Studying returns following profit warnings naturally

invites comparison with the literature which has investigated returns following scheduled earnings announcements. Abnormal returns in the months following an earnings announcement are usually found to be on average of the same sign as the initial surprise.

The study acts as a source of reference material for future researchers and other related topics; it will also help other academicians who undertake the same topic in their studies. The study highlights other important relationships that require further research; this may be in the areas of relationship between profit warnings and stock returns. Bank profit warnings represent a milder form of negative news than a bank failure. Yet, they may contain signals about a bank or its rivals because the information is transmitted when the bank believes that the market is overly optimistic about its future earnings. Thus, the profit warning serves as a means by which insiders of the bank can reduce the asymmetric information between the bank's insiders and its investors.

The profit warnings and stock returns in organizations are of interest to researchers and industry practitioners. This study will serve as a stepping stone for new research in relationship between profit warnings and stock returns. Besides, researchers and students in the field of strategic management who want to know more about profit warnings and stock returns will also find the study beneficial. The literature on the costs of going public cost is descriptive in nature. As such, this study reports the summary statistics of the total expenses required to take the firm public. The issue of firm size has become such a common element to use as a control variable in empirical corporate finance studies that it hardly receives any discussion in most research papers even though it is among the most significant variables. In international circles, evidence has been obtained to assert that leverage is cross-sectionally positively related to size.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter reviews literature that has been researched for the purposes of the study. The literatures will mainly aim to highlight relationship between profit warnings and stock returns evident in selected companies in the Kenya market.

2.2 Theoretical Review

2.2.1 Keynesian Theory

This study is guided by Keynesian theory that explores one aspect of the relationship between the system of production and the macroeconomic structure, namely, the role of Profitability in determining investment demand and the level of economic activity. Within the system of production, wages are a cost: the lower are profits per unit of production, the lower the stimulus to investment. In a Keynesian view of the macroeconomic structure, however, wages are a source of demand, hence a stimulus to profits and investment. In this view, aggregate demand provides the way out of the dilemma that high wages pose for the system of production. If demand is high enough, the level of capacity utilization will in turn be high enough to provide for the needs of both workers and capitalists. The rate of profit can be high even if the profit margin and the share of profit in output are low and the wage rate correspondingly high.

Profit squeeze presents a problem for this Keynesian solution. How do we reconcile the argument that profit squeeze was a major cause of the decline in growth rates that took place in the 1970's with Keynesian doctrine on the role of aggregate demand in reconciling the requirements of the system of production and those of the macroeconomic structure?

2.2.2 Resource-based view

This study is based on resource-based View. The core premise of the resource-based view is that resources and capabilities can vary significantly across firms, and that these differences can be stable (Barney and Hesterly, 1996). If resources and capabilities of a firm are mixed and deployed in a proper way they can create competitive advantage for the firm. The resource-based

view in outsourcing builds from a proposition that an organization that lacks valuable, rare, inimitable and organized resources and capabilities, shall seek for an external provider in order to overcome that weakness. Therefore the most prominent use of the theory is in the Preparation phase of the out sourcing process for defining the decision making framework and in the vendor selection phase for selecting an appropriate vendor. The theory has been also used to explain some of the key issues of the managing relationship and reconsideration phases.

2.2.3 Signalling Effect Theory

According to the Signaling Effect theory, managers use the change in cash dividends distributed rates as a means to deliver information to investors about the company (Denis et al., 1994). Supporters of this theory believe that the increase in the cash dividends rate is an effective means of delivering information to investors because competitors cannot follow the company's policy unless they have the same capacity to achieve future profit (see: Charest, 1978, Asquith and Mullins, 1983).

When Miller and Modigliani (1961) introduced their hypothesis about the Irrelevance Proposition about the effect of a company's cash dividend policy on the company's market value, one of their assumptions is that all investors have the same information and ability to understand and analyze the available information. Therefore, all investors have the same outlook concerning the company. Also, investors and managers have the same information and therefore they have the same expectations for the company. In practice, however, because of what is known as asymmetric information, (Bhattacharya, 1979), investors have different expectations and information with respect to the company's future profits and risks. Furthermore, by virtue of their position within the company and the nature of their work and career interests and duties, the managers have better and more accurate information and expectations than external investors regarding the company's profits and performance. As managers have information that may not be available to external investors, they can use the change in the cash distributed dividends rate as a way to deliver such information to investors to reduce the information gap between managers and investors with the aim of creating a greater demand for the company's shares, thereby influencing the company's market value and shareholders' wealth.

2.2.4 Efficient Market Hypothesis (EMH)

The efficient market hypothesis suggests that if a market is found to be efficient neither technical analysis nor fundamental analysis is worthwhile. A full discussion of the generally positive market reaction to an open-market repurchase would include the efficient markets theory. This theory can assist in explaining the indications of more than one underlying theory, specifically, the asymmetrical information hypothesis and the signalling hypothesis. In the case of an open-market buyback, an announcement can be viewed as a positive signal because managers have access to relevant and favourable information about the firm's value that is not known to other parties (Sander & Carpenter, 2003). In an efficient market, including the semi-strong form of market efficiency, stock prices fully reflect all available information. In the situation of a firm announcing a share repurchase, an efficient market would suggest that stock prices react efficiently and immediately in an unbiased manner to the new information conveyed in the announcement. In an efficient market, the new price would reflect the value of the new information and a wealth transfer would not occur between long-term stock holders and those willing to immediately sell shares. In an efficient market, the stock would not be over or undervalued after an announcement to repurchase shares.

Lorie and Hamilton (1973) qualify this by adding that the analysis will only be worthwhile "if there is sound originality in the process of analysis." Academicians have, over the years, done much to prove that stock prices move in a random and unpredictable way; hence there is no point to knowledgeable analysis and portfolio management. Professionals on the other hand know, purportedly from experience, that their expertise is by no means made obsolete by the fact that markets can be proved to be efficient. Since they have never had to decide on what to buy or sell, or had to explain an investment loss to an irate client, academicians – and their plethora of learned journals and seminars – are considered inherently and eminently 'unqualified to comment' on real world matters (Crowell, 1997). Investment analysts are normally divided into technical analysts and fundamental analysts, based on their tools of investment analysis. However, most of the investors do not use either of the two exclusively. For example, speculators may put more emphasis on technical analysis, but they are at the same time mindful of the economic environment and the fundamentals surrounding the shares they are speculating on. On the other hand, long-term investors are more concerned with the macroeconomic picture,

industrial (sectoral) prospects and company fundamentals, but as market timing is important technical analysis plays an important role in timing their purchases and sales (Lampen, 2001).

2.3 Empirical Review

2.3.1 Market Reaction on the Qualitative Warnings and Quantitative Warnings on Stock Returns

A profit warning is a description that analysts and journalists give to an unexpected corporate announcement that earnings for a specified future quarter will fall short of current expectations. Some corporate announcements that are described in the press as profit warnings do not explicitly refer to earnings but describe sales or revenues in such a way that lower earnings are implied. If earnings are not explicitly mentioned there may then be debate about whether a particular announcement should be described as a “profit warning”.

This study examines stock returns following profit warnings in order to contribute to the debate about the rationality of the market’s response to new information. An unresolved issue is whether markets under react to news in the short to medium term. Another contentious issue is whether there are long-term return reversals. Empirical evidence of under reaction to new information includes Ikenberry and Ramnath (2002) for stock splits, Loughran and Ritter (1995) for seasoned equity offerings, Cusatis et al. (1993) for spin-offs, Michaely et al. (1995) for dividend omissions and initiations, and Chan (2003) for general news stories. On the other hand, other studies have found abnormal returns of the opposite sign to announcement period returns, for example Dharan and Ikenberry (1995) for new exchange listings. Evidence from the time series of stock returns suggests long-run returns reversals (DeBondt and Thaler, 1985), but concerns have been expressed about their methodology (Conrad and Kaul (1993). Further, their time series results have not been underpinned by evidence of long-term reversals following specific information events. For example Chan, Jegadeesh and Lakonishok (1996) looked for, but could not detect, evidence of long-term reversals after the initial drift following earnings announcements.

Evidence is reported that qualitative warnings are chosen when the earnings outcome is relatively bad, relative to expectations five days before the warning is issued. This leads to the

question of whether the decision not to include a quantitative forecast in the profit warning reflects deliberate strategic management of news-flow. If it does, what is the motivation for such news management? For example if the aim is to allow the bad news to emerge gradually over time, then the negative post-event abnormal returns indicate that the policy is successful. However articulating a motivation for such a policy is not easy. Clearly a useful start would be an investigation of whether the choice of quantitative or qualitative warnings can be explained empirically Ikenberry and Ramnath (2002).

Profit warnings are perceived by the stock market as important new information. Stock prices drop on average by approximately 17% in the first two days after a profit warning. This is a much larger fall than the average initial response to a large negative surprise in the scheduled yearly earnings announcement. Bernard and Thomas (1989) report that the decline of stocks with the most disappointing earnings surprise delivered abnormal returns of approximately -2% in the announcement window. It is also a much larger fall than that following other unanticipated bad news studied in the event study literature. For example abnormal returns in the announcement window are estimated to be approximately -3%, for a seasoned equity offering (Spiess and Affleck-Graves (1995) and -7% for a dividend omission (Michaely, Thaler and Womack (1995).

Bulkley and Herrerias (2005) implemented the disclosure theory of Milgrom (1981) to profit warnings by examining whether the market reaction is more negative for qualitative warnings. They treat qualitative warnings as partial disclosure since it contains less information and quantitative warnings as full disclosure since it contains more information. According to Bulkley and Herrerias (2005) the choice for a qualitative warning cannot be attributed to an uninformed manager since the type of warning is chosen after they receive information that earnings for a reported period will not meet expectations. Based on this interpretation investors should perceive qualitative warnings as worse news compared to quantitative warnings resulting in a larger negative market reaction at the time of the announcement. However they found no significant different market reaction during an eleven-day event window although the market reaction was slightly more negative for qualitative warnings, respectively - 24,7 % and -20,7 %, Bulkley and

Herrerias (2005) conclude that this insignificant difference is evidence that the market does not understand that qualitative warnings are worse news.

2.3.2 Information Content of a profit warning announcement and the market reaction

According to the efficient market hypothesis (Fama, 1970) stock prices fully reflect all available information and change when new information arrives in the market. A firm that issues a profit warning discloses public information to investors that earnings will fall below expectation. If investors perceive this information as new and value relevant there should be a negative stock price reaction at the time of the announcement. Moreover the relevance of a profit warning is underlined by several studies (Jackson & Madura, 2003; Bulkley & Herrerias, 2005; Church & Donker, 2010), who provide evidence of strong negative abnormal returns at the time of a profit warning announcement.

If stock returns continue to drift downward after a profit warning signal it interesting to see whether the magnitude of this drift differs for qualitative and quantitative warnings. The behavioral theory of Daniel et al. (1998) predicts that psychological biases leading to market under reaction are enhanced when the precision of a signal decreases. Consistent with this theory Bulkley and Herrerias (2005) show that market under reaction is significantly more negative for less precise qualitative warnings compared to more precise quantitative warnings.

2.4 Event Study Methods

The profit warning is a complex event with advantages and disadvantages when it is issued; therefore, it is a challengeable consideration to the companies. As the companies can choose the type of profit warning then, they can alter the impact on the stock value. Moreover, firms of different sizes can also have different strategies of which the impact may not be the same. The economic power of the emerging markets is increasing and it plays an important role in the global financial market. Therefore, we believe it worth to do research covering this geographical area. In addition, there is no research conducted in this integrated area regarding profit warning. During the period of economic downturn the profit warning is issued more often than under normal economic conditions. Our research covers the period of global economic downturn. The profit warning was one of the common events in the financial world that impacted the stock value during this period that we can see often in the financial newspapers and magazines.

In practice, there are a few events that can trigger the movement of stock prices. Both Kasznik & Lev (1995) and Jackson & Madura (2003) believe the announcements of corporate control changes will affect the stock prices and the profit warning is not the only information that results in the market reaction. These corporate control announcements include mergers, acquisitions, dividend changes and stock repurchase. If a company issues both a profit warning and corporation control change information during the same time, it is hard to distinguish which information has caused the impact on stock price. The effect on stock returns may be more complicated. Therefore, in our thesis, we try to avoid other corporate control issues and pay attention solely to the event of profit warning.

During our selected cover period, some companies issued repeated profit warnings. These subsequent profit warnings may affect the stock returns continuously thus it makes impossible to measure the real impact. Therefore we excluded those companies that issued more than one profit warnings within one quarter that is our event window. Normally, the repeated profit warning, such as second or third one, may trigger more negative respond than the first one.

Moreover, we will study the impact of profit warning only on the common stock out of the financial securities. We exclude the impact of the profit warning on derivative securities such as options and futures contracts. Bodie et al. (2009) stated the value of derivative securities are derived from the prices of other assets like bond or stock.

2.5 Summary

The literature in this study aims to highlight the relationship between profit warnings and stock returns. The study will be guided by the Keynesian theory which explores one aspect of the relationship between system production and macroeconomic structure. Resource based view theory also guiding this study stipulates that resources and capabilities can vary significantly across firm and finally the Signaling effect theory which posits that management uses payment of cash dividends as a way of communicating to investors. Empirical review highlights on market reaction on quantitative and qualitative warnings as well as the information content on profit warning announcements and market reaction. This chapter also discusses in depth the inverse relationship between profit warning and leverage of the firm. We further discuss the role of disclosures in ensuring timely relay of information thus averting mispricing of stock and ultimately reducing cost of capital.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter describes the methods that will be used in the collection of data pertinent in answering the research question. It is divided into research design, study population, sample design, data collection and data analysis methods.

3.2 Research Design

Research design refers to the way the study is designed, that is, the method used to carry out a research. In this study event study methodology was applied. Descriptive Research is the investigation in which quantitative data is collected and analyzed in order to describe the specific phenomenon in its current trends, current events and linkages between different factors at the current time. An event study design is chosen because it enables the researcher to generalize the findings to a larger population. This study abled to generalize the findings to all companies listed at NSE. This study was a descriptive survey. This method had been successfully used by Kogi (2003) to study the effect of dividend policy on value of firms listed at the NSE. Event study measures the impact of a specific event on the value of the firm. Event is some change, development or announcement that may produce a relatively large change in the value of an asset over some period. This research design is valuable for detailed analysis. Young, (1960) and Kothari, (1990) concur that a case study often provides focused and valuable insights to a phenomena that may be vaguely known and less understood.

3.3 Population

Target population can be defined as a compute set of individuals, cases/objects with some common observable characteristics of a particular nature distinct from other population. Target population is defined as the population to which a researcher will generalize the result of a study. The population of interest in this study consisted of all the firms quoted at the Nairobi Securities Exchange (N.S.E). The study therefore picked the 10 companies that have issued profit warnings in the year 2012 for the period 2007 - 2012.

3.4 Data Collection

Creswell (2002) defines data collection as means by which information is obtained from the selected subjects of an investigation.

The study will utilize secondary data for the period 2007 to 2012.

3.5 Data Analysis and Presentation

Pearson product-moment correlation statistics procedure using SPSS statistical package was used to analyze and generalize the results of analysis to the population. This is because the variables the researcher studied are measured at ratio or interval scales and are continuous (Patton, 2002). To permit quantitative analysis data, must be converted into numeric codes representing attributes or measurements of variables. It is important that coding should include as much information as possible because once the coded data is entered into the computer, it is impossible to recover any details, which were omitted (Mugenda & Mugenda, 2003). Generalization is then done from the themes about the phenomena in question and interpreted in the light of the available literature (Kumar, 2005). Qualitative analysis is important since it supplements the quantitative analysis to create a better framework to the interpretation of the findings (Kothari, 2008). Reliability of the instrument was tested using the Cronbach's alpha. Regression analysis that sought to establish the relationship between profit warnings and stock returns evident in selected companies in the Kenya market will be done.

$$R_{jt} = \alpha + B_1(B/M) + B_2(E/P) + \varepsilon$$

An event study is the most commonly used method to analyse the effect of company-specific phenomena on equity markets. As this is a preliminary study, the methodology and diagnostics are kept as simple as possible. Daily trading returns R_{jt} (for any company j for day t) are collected in natural log form along with log-form returns on the market RM_t . A return expectation is generated by performing the following simple OLS regression employing these two variables on a 250-day estimation period.

$$R_{jt} = \alpha + BR_{mt} + \varepsilon$$

The expectation is then forecasted forward into the test period and into the event window in particular. An abnormal return is calculated for each day of interest by subtracting the forecasted return and cumulative abnormal returns are generated additively from these:

$$AR_{jt} = R_{jt} - (\alpha + BR_{mt})$$

The study classified the firms that has high ratio of book to market equity (B/M), earning to price (E/P), or cash flow to price as value stocks. Fama and French (1992, 1996) Lakonishok, Shleifer and Vishny (1994) show that there is high value premium on average returns. High B/M, P/E or C/P stocks have higher average returns than low B/M, P/E or C/P stocks. Fama and French (1992, 1996) Lakonishok, Shleifer and Vishny (1994) show that value premium is associated with relative distress. High B/M, P/E or C/P stocks tend to have persistently low earning and low B/M, P/E or C/P stocks tend to be strong (growth) firms with persistently high earning. In order to establish the profit earnings and stock returns of companies that have issued profit warnings listed at NSE the study will calculate the book to market ratio, earning to price ration and cash flow to prices ratio and then classify the firms as value stocks or growth stock

At the starting point the reciprocal of the price earning and the price to book value ratios was calculated so as to give the earning yield and book to market values at the end of each year 2007 through to 2012 to constitutes the portfolio formation dates. At these dates the companies were ranked according to E/P, B/M and D/P ratios. This ranking was form the criteria for classifying stocks into value and growth in each of the following years, since some companies' (well above 30%do not pay divide, this disqualifies the dividend yield as criteria for ranking and classifying stocks at NSE during the period of study. This classification was based on earning yield and book to market values .the top 30% (high E/P, B/M) will be classified as value stocks and bottom 30% (low E/P, B/M) was classified as growth stocks such that at each formation date there was two growth portfolio and two value portfolios each in respect of each variable.

As a starting point the end month price for stock classified as value or growth was calculated by getting the weighted average of the prices at which a stock was traded during the last day of trading in the month .the next step in the analysis was to calculate the monthly returns for each stock classified as value or growth for the period of 2007 to 2012 and since dividend are paid annually dividend will be spread across all months of the year.

The following formula will be used to calculate the monthly returns (R_t)

$$R_i = \frac{\text{dividend} + (\text{ending price} - \text{beginning price}) \times 100}{\text{Beginning price}}$$

The third step was to calculate average monthly returns for each stock for each of the five years.

$$\text{Average monthly returns for stocks } i \text{ at year } t (R_{it}) = 1/12 \sum_{i=1}^{12} R_i$$

The next step was to calculate the average monthly return for each portfolio as follows

$$\text{Average monthly return for equally weighted portfolio at year } t (R_{pt}) = 1/n \sum_{i=1}^n R_{it}$$

Where n is the number of stocks in the portfolio at year t

Having calculated the five years average monthly returns for the each portfolio for each of the five years the five years average monthly return will be calculated as follows:

$$\text{Five years average monthly returns} = 1/5 \sum_{t=1}^5 R_{pt}$$

Finally a comparison of the five years average monthly return for the two portfolios' was done by performing the test of significance to determine whether there is a significant differences between the average returns of each pair ,the Z statistics was used and was calculated as follows

$$Z = \frac{X_1 - X_2}{\sqrt{S_1^2 \frac{2}{n_1} + S_2^2 \frac{2}{n_2}}}$$

Where X1= the five years average monthly return for the value portfolio

X2= the five years average monthly return for the growth portfolio

S1= the standard deviation for the value portfolio

S2 =the standard portfolio for growth portfolio

$n_1 = n_2 = 3360 = 56 * 12 \text{ months} * 5 \text{ years}$

CHAPTER FOUR

DATA ANALYSIS AND PRESENTATION OF FINDINGS

4.1 INTRODUCTION

This chapter represents research findings as directed by the objective of the study which was to establish the relationship between profit warnings and stock returns of companies listed at the Nairobi Securities Exchange.

The study utilized secondary data for the period 2007 to 2012. Creswell (2002) defines data collection as means by which information is obtained from the selected subjects of an investigation. There are many advantages of using secondary data, such as resource, efficiency, capacity for evaluation, potential for comparative analysis and potential for new insights

According to Kasznik & Lev (1995, p.114), warning announcements are delivered to the public through alternative channels; such as a public announcement via the news wires or a conference call with analysts. The news wires consist of many channels like the Internet, the newspapers and the TV programs. We select the profit warnings via the Internet because it is convenient, fast, economic and publicly available. This data was collected from published financial statements of listed companies, Nairobi Securities Exchange website (www.nse.co.ke), Capital Markets Authority website (www.cma.or.ke) as well Libraries and websites of the mainstream media houses in Kenya (www.nationmedia.com, www.standardmedia.com) daily business reports.

4.2 Data Presentation

Reliability of the instrument was tested using the Cronbach's alpha. Regression analysis that sought to establish the relationship between profit warnings and stock returns evident in selected companies in the Kenya market was done.

$$R_{jt} = \alpha + B_1(B/M) + B_2(E/P) + \varepsilon$$

An event study was used to analyse the effect of company-specific phenomena on equity markets. As this is a preliminary study, the methodology and diagnostics was kept as simple as possible. Daily trading returns R_{jt} (for any company j for day t) were collected in natural log form along with log-form returns on the market RM_t . A return expectation was generated by performing the following simple OLS regression employing these two variables B/M and E/P on a 250-day estimation period. Significance value (P-value) was taken to be 0.05. P-values less than 0.05 implies that the study undertaken was statistically significant.

4.2.1 Year 2007

In order to establish the statistical significance of the independent variables on the dependent variable (daily returns) regression analysis was employed. The regression equation took the following form.

$$R_{jt} = \beta_0 + B_1(B/M) + B_2(E/P) + \varepsilon \dots \dots \dots \text{model 1}$$

Where;

R_{jt} = Daily trading returns

B/M = Book value /market

E/P =earnings/profit

β_0 = constant term

B_1 and B_2 = Coefficients of determinant

ε = error term

P-value = probability value

In the model 1 above, B_1 and B_2 was used to measure the sensitivity of the dependent variables (R_{jt}) to unit change in the predictor Variables (**B/M and E/P**). β_0 is the constant term that's used to measure the variation of the dependent variables when other factors (B_1 and B_2) are held constant. ε is the error term which captures the unexplained variations in the model.

From the findings E/P was positive and significantly related to daily returns (**B=.203, P-value=0.003**). This implies that an increase in E/P by one unit leads to an increase in returns by .203 units. Further B/M was found to be positive and significantly related of daily returns (**B=5.349, P-value=0.004**). This implies that an increase in B/M by one unit leads to an increase in returns by .203 units.

Model		Unstandardized Coefficients		Standardized Coefficients Beta	t	Sig.
		B	Std. Error			
1	(Constant)	5.571	2.248		2.478	.042
	B/M	5.349	4.765	-.390	-1.123	.004
	E/P	.203	.496	.142	.409	.0003

4.2.2 Year 2008

From the findings E/P was positive and significantly related to daily returns (**B=.059, P-value=0.002**). This implies that an increase in E/P by one unit leads to an increase in returns by

.059 units. Further B/M was found to be positive and significantly related to daily returns (**B=.074, P-value=0.004**). This implies that an increase in B/M by one unit leads to an increase in returns by .074 units.

Table 4. 2 :Year 2008 Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients Beta	t	Sig.
		B	Std. Error			
1	(Constant)	1.693	3.624		.467	0.001
	B/M	.074	.034	.593	2.188	0.004
	E/P	.059	.025	-.644	-2.379	0.002

4.2.3 Year 2009

From the findings E/P was positive and significantly related to daily returns (**B=.421 P-value=0.000**). This implies that an increase in E/P by one unit leads to an increase in returns by .421 units. Further B/M was found to be positive and significantly related to daily returns (**B=.055, P-value=. 003**). This implies that an increase in B/M by one unit leads to an increase in returns by .055 units.

Table 4. 3: Year 2009 Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients Beta	t	Sig.
		B	Std. Error			
1	(Constant)	8.446	3.741		2.258	.001
	B/M	.055	.044	.476	1.255	.003
	E/P	.421	.757	-.211	-.556	.000

4.2.3 Year 2010

From the findings E/P was positive and significantly related to daily return (**B=2.423, P-value=0.004**). This implies that an increase in E/P by one unit leads to an increase in returns by 2.423 units. Further B/M was found to be positive and significantly related to daily returns (**B=.332, P-value=.001**). This implies that an increase in B/M by one unit leads to an increase in returns by .332 units.

Table 4. 4:Year 2010 Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients Beta	t	Sig.
		B	Std. Error			
1	(Constant)	33.398	17.842		1.872	.003
	B/M	.332	.334	-.449	-.994	.001
	E/P	2.423	3.740	.292	.648	.004

4.2.4 Year 2011

From the findings E/P was positive and significantly related to daily return (**B=1.674,P-value=0.004**). This implies that an increase in E/P by one unit leads to an increase in returns by 1.674 units. Further B/M was found to be positive and significantly related to daily returns (**B=.397, P-value=.001**). This implies that an increase in B/M by one unit leads to an increase in returns by .397units.

Table 4. 5 :Year 2011 Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients Beta	t	Sig.
		B	Std. Error			
1	(Constant)	30.503	7.668		3.978	.004
	B/M	.397	.104	-1.017	-3.834	.001
	E/P	1.674	1.905	.233	.879	.004

4.2.5 Year 2012

From the findings E/P was positive and significantly related to daily return (**B=32.144, P-value=0.004**). This implies that an increase in E/P by one unit leads to an increase in returns by **32.144** units. Further B/M was found to be positive and significantly related daily returns (**B=.201, P-value=. 001**). This implies that an increase in B/M by one unit leads to an increase in returns by **.201** units.

Table 4. 6: Year 2012 Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients Beta	t	Sig.
		B	Std. Error			
1	(Constant)	55.350	77.802		.711	.504
	B/M	.201	1.008	-.039	-.199	.001
	E/P	32.144	7.251	.872	4.433	.004

4.2.6 Profit warnings

The study majored its research in 10 companies listed in the NSE that issue a profit warning .data was obtained from NSE data base www.nse.co.ke database as well as well firm websites where it needed clarifications. Kakuzi Limited issued 23% profit warning. Eaagads Limited, Kapchorua Tea Company Limited, Express Kenya, Mumias and Longhorn all issued a 25% profit warning. Kenya Airways, East African Portland Cement Company, Kenol Kobil and Sasini Tea And Coffee Limited issued 26%, 27% and 31% respectively.

Table 4. 7: profit warnings

Company	Average profit warning between 2007-2012(%)
1 Eaagads Limited	25
2 Kakuzi Limited	23
3 Kapchorua Tea Company Limited	25
4 Express Kenya	25
5 Kenol Kobil	27
6 Sasini Tea And Coffee Limited	31
7 Eaast African Portland Cement Company	27
8 Kenya Airways	26
9 Mumias	25
10 Longhorn	25

4.2.7 Abnormal Returns

Abnormal return is the difference between the actual return of a security and the expected return. In this study, the profit warning date was assigned day 0 if it happens on a trading day. If announcements are made on a non-trading day, the next available trading day is assigned day 0. The event period is taken to be 250 days before announcement to 250 days after announcement of profit warning. Abnormal returns are measured for the announcement period (day -250 to day +250) at 25 day intervals.

The average abnormal returns are presented in the table below for the entire sample of firms during the 250-event day window. From the findings, abnormal returns are statistically significant at the 0.05 level at the 50 day and 25 day intervals before the profit warning announcement, on the actual day of the profit warning announcement (day t) and 25 days after the profit warning announcement.

Before the announcement at the 50 day in interval, (t-value = -4.31, p-value =0.0134), at 25 day interval (t-value=-3.87, p-value=0.0035) and on the day of announcement (t=5.29, p=0.001). At the 25 day post announcement, (t-value= -3.35, p-value 0.0368)

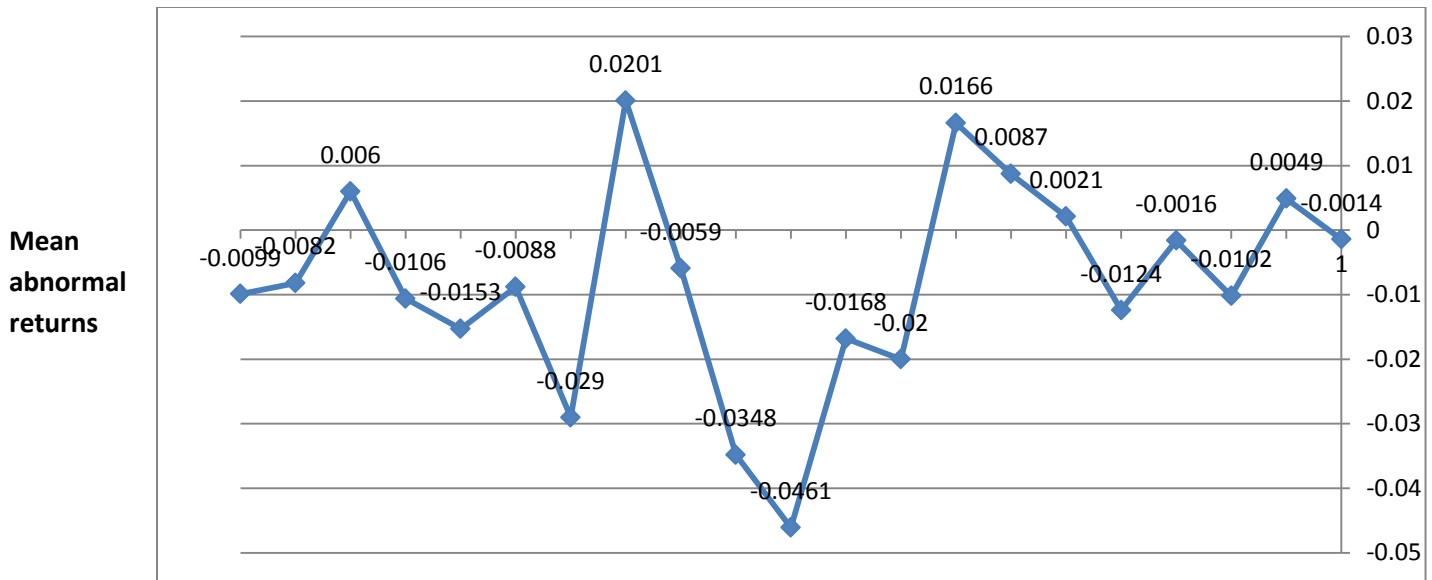
The p-value measures the level of marginal significance within a statistical hypothesis test, representing the probability of occurrence of a given event. T-value is a measure of the statistical significance of an independent variable (b) in explaining the dependent variable (Y).

Table 4. 8 : Abnormal Returns

Day	Average abnormal return	t-value	p-value
-250	-0.0014	-0.21	0.9513
-225	0.0049	0.84	0.5971
-200	-0.0102	-0.91	0.3792
-175	-0.0016	-0.19	0.7727
-150	-0.0124	-1.02	0.4521
-125	0.0021	0.15	0.8814
-100	0.0087	0.79	0.4457
-75	0.0166	1.48	0.1763
-50	-0.0200	-4.31*	0.0134
-25	-0.0168	-3.87*	0.0035
0	-0.0461	-5.29*	0.0001
25	-0.0348	-3.35*	0.0368
50	-0.0059	-0.43	0.6818
75	0.0201	1.57	0.1682
100	-0.0290	-1.57	0.1556
125	-0.0088	-0.77	0.4548
150	-0.0153	-1.69	0.1213
175	-0.0106	-1.49	0.1611
200	0.0060	0.69	0.5018
225	-0.0082	-0.99	0.3475
250	-0.0099	-0.945	0.03215

Abnormal Returns curve

The figure below shows that after the announcement day, the average abnormal returns resume their previous pattern exhibited before the announcement. Abnormal returns are lowest a day before announcement, the day of the announcement and one day after announcement implying negative market response before and after the profit warnings announcement.



Event window

Figure 4. 1: Abnormal Returns curve

4.3: Summary and interpretation of Findings

From the findings, two of the 250-eventday window Abnormal Returns is statistically significant at the 0.05 level. These are the Abnormal Returns 25 days before the announcement ($t=-3.87$, $p=0.0035$) and the day of announcement ($t=5.29$, $p=0.001$). From a theoretical point of view the results are inconsistent with the behavioral model of Daniel et al. (1998) where the magnitude of the drift increases as the precision of a signal decreases.

From findings (business daily) the Profit warnings at the Nairobi Securities Exchange on Friday rose to 10. Agricultural firm Kakuzi joined Longhorn, Eaagads, Express Kenya, KenolKobil, Sasini, East African Portland Cement Company (EAPCC), Kenya Airways (KQ), and Kapchorua Tea, which all said their profits would drop by more than 25 per cent this year. The increased warnings highlight the challenges corporate Kenya is facing in an economy that is feeling the weight of expensive credit, high inflation, and political jitters linked to next year's General Election. Most of these companies have seen their market value decline at the Nairobi bourse

over the past six months in a period that has seen the stock market gain 23.3 per cent, aided by the performance of most blue chip firms and increased foreign investor interest. The high profit alerts was driven by the weak local and global economy besides other unique factors that have eroded earnings of individual firms. Companies that did not issue profit warnings recorded negative or lower profit growth .compared to previous years. In the same period, EAPCC's share price dipped 31.2 per cent to Sh42 as KQ's share lost 18.5 per cent to Sh12.2. Other firms that recorded share price erosion in the same period include Eaagads and Kakuzi whose shares dropped 30.4 and 12.5 per cent respectively to Sh24.5 and Sh70 a piece.

There is substantial documented evidence on both over and under-reaction to earnings announcements. DeBondt and Thaler (1985, 1987) present evidence that is consistent with stock prices overreacting to current changes in earnings. They report positive (negative) estimated abnormal stock returns for portfolios that previously generated inferior (superior) stock price and earning performance. This could be construed as the prior period stock price behavior overreacting to earnings developments (Bernard, 1993). Such interpretation has been challenged by Zarowin (1989) but is supported by DeBondt and Thaler (1990). Bernard (1993) provides evidence that is consistent with the initial reaction being too small, and being completed over a period of at least six months. Ou and Penman (1989) also argue that the market underutilizes financial statement information. Bernard (1993) further notes that such anomalies are not due to research design flaws, inappropriate adjustment for risk, or transaction costs. Thus, the evidence suggests that information is not impounded in prices instantaneously as the EMH would predict.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary

This section mainly covers the summary of findings, conclusion, and recommendations in line with the topic of study that is to establishment of the relationship between profit warnings and stock returns of companies listed at the Nairobi Securities Exchange

The study found out that from year 2007-2012 Book value /market and earnings/profit was found out to be positively related to daily returns and consequently the average return over the five years.

From findings on profit warnings, the study found out that Kakuzi Limited issued 23% profit warning. Eaagads Limited, Kapchorua Tea Company Limited, Express Kenya, Mumias and Longhorn all issued a 25% profit warning. Kenya Airways, East African Portland Cement Company, Kenol Kobil and Sasini Tea And Coffee Limited issued 26%, 27% and 31% respectively.

The average abnormal returns as presented in the entire sample of firms during the 250-event day window showed that Two of the 250-eventday window Abnormal Returns were statistically significant at the 0.05 level. These are the Abnormal Returns 25 days before the announcement ($t=-3.87$, $p=0.0035$) and the day of announcement ($t=5.29$, $p=0.001$).

Finally the study found out that returns can be traced in the months before a warning. On average companies' stock prices fell since the issue of profit warning. The average daily rate over 250 days before the warning to one day before is -3.01% . Compounding this gives a loss in value for the average company. By the time, companies reach their low point six months after the warning they have lost on average 48% of their value since two years before the warning.

5.2 Conclusions

The result of research Study indicates that profit warning has impact on the stock return in NSE and the impact is negative and significant for the period of pre-warning and post-warning and on the day of actual announcement. The more significant is impact is noticed during the period from some days before to some days after the profit warning. It may indicate the information leakage prior to the profit warning and the market observes the information quickly thus reacts significantly during these days. This findings support the market efficiency assumption in the NSE. Moreover, such market response can be related to the weak economic condition during this period. During the 25 days before and the 25 days after the profit warning, the average share price response was -3.01% . The study concludes that all consistent with the existing literature the results show that profit warnings are highly relevant information events that are followed by large negative abnormal returns in the short term.

Overall the results show that contrary to the semi-strong efficient market hypothesis abnormal returns continue to drift downward after a profit warning signal a phenomenon that is usually attributed to market under reaction. Furthermore contrary to the theoretical model of Daniel et al. (1998) and the findings of Bulkley and Herrerias (2005) the results provide no evidence of a more negative market reaction for less precise profit warning in the medium term, on the contrary there seems to be an opposite relation.

5.3 Policy Recommendationns

Profit warning being the pure information, unscheduled, and unexpected corporate announcement should be issued prior to the actual earnings announcement with the purpose of informing the market thus reducing the negative impact of the earnings surprise. As the information, the profit warnings reduce the information asymmetry and improve the transparency in the market.

Further the study recommends the firms that operating or considering operating in the NSE, to be aware that a profit warning has a significant impact on the stock returns in this geographical area, especially during the period of the actual announcement. Moreover, the choice of the profit warning type can alter the impact thus managers should consider it in the decision making regarding the profit warning issue so that they manage the drastic decline in the firm value.

Evidence is reported that qualitative warnings are chosen when the earnings outcome is relatively bad, relative to expectations five days before the warning is issued. This leads to the question of whether the decision not to include a quantitative forecast in the profit warning reflects deliberate strategic management of news-flow. If it does, the management should gauge the motivation for such news. For example if the aim is to allow the bad news to emerge gradually over time, then the negative post-event abnormal returns indicate that the policy is successful. However articulating a motivation for such a policy is not easy. Clearly the study recommends that a useful start would be an investigation of whether the choice of quantitative or qualitative warnings can be explained empirically.

5.4 Limitations of the study

One of the major limitations of the study was the data collection process which disturbed the definition of a first-time profit warning in the beginning of the sample period. It is completely impossible to obtain profit warnings of companies in one file.

Second limitation is the rigorous analysis of the appropriate models to show evidence of profit warning. The consultancy of statistical experts is sought to enable smooth running of the analysis.

Resource limitations was a challenge and limited the researcher to visit to all listed firms to confirm directly, the existence of profit warning announcements events and individual reasons that may have motivated issuance of the profit warning announcements.

Some companies issued more than one profit warning announcements during the period of the study. This is likely to have some confounding effects on the results of the study.

5.5 Suggestions for further studies

The study focused on establishment of the relationship between profit warnings and stock returns of companies listed at the Nairobi Securities Exchange. Further study should be carried out on the impact of profit warning on the issuing firms.

There is also need to study further and establish extent to which the negative market response is temporary or permanent and the duration the negative effect can last.

An assessment of market reaction on the basis of how accurate management's earnings forecast via the profit warning is as compared to the actual earnings report when it is eventually made would be an another recommendation for further studies

References

- Nag, J. S., & Zhang, S. (2004). An Evaluation of Testing Procedures for Long Horizon Event Studies. *Review of Quantitative Finance and Accounting*, 23, 251-274.
- Baginski, S. P., Hassell, J. M., & Kimbrough, M. D. (2002). The Effect of Legal Environment on Voluntary Disclosure: Evidence from Management Earnings Forecasts Issued in U.S. and Canadian Markets. *The Accounting Review*, January: 25-50.
- Ball, R. (1992). The Earning-price Anomaly. *Journal of Accounting and Economics*, 15, 319-345.
- Ball, R., & Bartov, E. (1996). How Naïve is the Stock Market's Use of Earnings Information? *Journal of Accounting and Economics*, 21, 319-337.
- Ball, R., & Brown, P. (1968). An Empirical Evaluation of Accounting Income Numbers. *Journal of Accounting Research*, 6, 159-178.
- Ball, R., & Brown, P. (1968). An Empirical Evaluation of Accounting Income Numbers. *Journal of Accounting Research*, 6, 159-178.
- Barber, B. M., & Lyon, J. D. (1997). Detecting Long-run Abnormal Stock Returns: The Empirical Power and Specification of Test Statistics. *Journal of Financial Economics*, 43, 341-372.
- Barberis, N., Shleifer, A., & Vishny, R. (1998). A Model of Investor Sentiment. *Journal of Financial Economics*, 49, 307-343.
- Bernard, V., & Thomas, J. (1989). Post-Earnings Announcement Drift: Delayed Price Response or Risk Premium? *Journal of Accounting Research*, 27, 1-36.
- Bernard, V., & Thomas, J. (1990). Evidence That Stock Prices Do Not Fully Reflect the Implications of Current Earnings for Future Earnings. *Journal of Accounting and Economics*, 13, 305-340.
- Bernard, V., & Thomas, J. (2004). Evidence That Stock Prices Do Not Fully Reflect the Implications of Current Earnings for Future Earnings. *Journal of Accounting and Economics*, 13, 305-340.
- Bodie, Z., Kane, A. & Marcus, A. J. (2009). *Investments*. New York: Mc-Graw Hill.
- Brown, Lawrence D., and Michael S. Rozeff, (1978), The superiority of analyst forecasts as measures of expectations: Evidence from earnings, *The Journal of Finance* 33, 1-16.
- Brown, Lawrence D., Paul A. Griffin, Robert L. Hagerman, and Mark E. Zmijewski, (1987), Security analyst superiority relative to univariate time-series models in forecasting quarterly earnings, *Journal of Accounting and Economics* 9, 61-87.
- Bulkley, G., & Herrerias, R. (2005). Does the Precision of News Affect Market Under reaction? Evidence from Returns Following Two Classes of Profit Warnings. *European Financial Management*, 11, 603-624.

- Campbell, H. (2006). Just planning: The art of situated ethical judgment. *Journal of Planning Education and Research*, 26 (1), 92-106.
- Chordia, T., & Shivakumar, L. (2005). Inflation Illusion and Post-earning-announcement Drift. *Journal of Accounting Research*, 43, 521-556.
- Church, M., & Donker, H. (2010). Profit Warnings: Will Openness Be Rewarded? *Applied Economic Letters*, 17, 635-637.
- Collett, N. (2004). Reactions of the London stock exchange to company trading statement announcements. *Journal of Business Finance & Accounting*, 31(1/2), 3-35.
- Cox, B. G. (2010). "Research Methods." *Encyclopedia of Survey Research Methods*. ISBN: 978141.
- Creswell, J. W. (2002). *Research design: Qualitative, quantitative, and mixed method*
- Crowell, R.A., (1997). *Stock Market Strategy*. McGraw Hill Inc.
- Daniel, K., Hirshleifer, D., & Subrahmanyam, A. (1998). Investor Psychology and Security Market Under- and Overreactions. *The Journal of Finance*, 53 (6), 1839-1885.
- Diamond, D. & Verrecchia, R. (1991). Disclosure, Liquidity, and the Cost of Capital. *The Journal of Finance*, 46, 1325-1359.
- Edwards, W. (1968). Conservatism in Human Information Processing, in B. Kleinmuntz (ed.), *Formal Representation of Human Judgment*. John Wiley and Sons, New York, 17-55.
- Eilifsen, A., Messier, W.F., Glover, S.M., & Prawitt, D.F. (2009). *Auditing and Assurance Service*. 2 international ed. Maidenhead. Maidenhead: McGraw-Hill Education.
- Einhorn, H. J. (1980). Overconfidence in Judgment, New Directions for Methodology of Social and Behavioral Finance, 4, 1-16.
- Elayan, F. A., & Pukthuanthong, K. (2009). Why Warn? The Impact of Profit Warnings on Shareholder's Equity. *Investment Management and Financial innovations*, 6 (4).
- Fama, E. (1965). Random Walks in Stock Market Prices. *The Journal of Business*, 21(5), 55-59.
- Fama, E. (1970). Efficient Capital Markets: A Review of Theory and Empirical Work. *Journal of Finance*, 25(2), 383-417.
- Fama, E. (1996). Multifactor Explanations of Asset Pricing Anomalies. *Journal of Finance*, 51(1), 55-84.
- Fama, E. (1998). Market Efficiency, Long-term Returns, and Behavioral Finance. *Journal of Financial Economics*, 49, 283-306.
- Fama, E., Fisher, L., Jensen, M., & Roll, R. (1969). The Adjustment of Stock Prices to New Information. *International Economic Review*, 10, 1-21.
- Foster, G., Olsen, C., & Shevlin, T. (1984). Earnings Releases, Anomalies, and the Behavior of Security Returns. *The Accounting Review*, 59(4), 574-603.
- Garner, R. (2010). *A Short Guide to Introductory Statistics in the Social Sciences*. (2nd ed). Toronto: University of Toronto Press
- Granger, C. W.J. & Timmerman, A. (2004). Efficient Market Hypothesis and Forecasting. *International Journal of Forecasting*, 20 (1), 15-27.

- Helbok, G., & Walker, M. (2003). On the Willingness of UK Companies to Issue Profit Warnings: Regulatory, Earnings Surprise Permanence, and Agency Cost Effects. *Working Paper*, University of Manchester.
- Jackson, D., & Madura, J. (2003). Profit Warnings and Timing. *The Financial Review*, 38, 497-513.
- Jackson, D., & Madura, J. (2007). Impact of Regulation Fair Disclosure on the Information Flow Associated with Profit Warnings. *Journal of Economics and Finance*, 31.
- Kasznik, R., & Lev, B. (1995). To Warn or Not to Warn: Management Disclosure in the Face of an Earnings Surprise. *The Accounting Review*, 70, 113-134.
- Kothari, C. R. (2004). *Research Methodology*. New Delhi: New Age international.
- Lampen, G. (2001). Take Charge of Your Investments.
- Libby, R., & Tan, H. (1999). Analysts' Reactions to Warnings of Negative Earnings Surprises. *Journal of Accounting Research*, 37, 415-435.
- Liu, W., Strong, N., & Xu, X. (2003). Post-earnings-announcement Drift in the UK. *European Financial Management*, 9(1), 89-116.
- Lorie, J.H. and Hamilton, M.T., (1973), *The Stock Market: Theories and Evidence*. Illinois: Homewood, Irwin.
- MacKinlay, G., (1997). Event Studies in Economics and Finance. *Journal of Economic Literature*, 35, 13-39.
- Malkiel, B.G. (2003). The Efficient Market Hypothesis and Its Critics. *Journal of Economic Perspectives*, 17 (1), 59-82.
- Milgrom, P. R. (1981). Good News and Bad News: Representation Theorems and Applications. *Bell journal of Economics*, 12, 380-391.
- Mugenda, A. G. (2008). *Social Science Research: Theory and Principles*. Nairobi: Acts Press.
- Mugenda, O., M. & Mugenda, A. G. (2003). *Research Methods: Quantitative and Qualitative Approaches*. Nairobi, Acts Press.
- Mujis, M. (2004). *Doing Quantitative Research in Education*. London: Sage Publication.
- Ngechu, M. (2004). *Understanding the Research Process and Methods: An Introduction to Research Methods* Nairobi, Acts Press.
- Nocera, J. and Kover, A. (1997). Who really moves the market?, *Fortune* 136, 90-101.
- Ogden, J.P., Jen, F.C., & O'Connor, P.F. (2003). *Advanced Corporate Finance: Policies and strategies*. Upper Saddle River, NJ:Prentice Hall.
- Patton, M. Q. (2002). *Qualitative Research and Evaluation Methods* (3rd Ed). London: Sage Publications.
- Pesaran, M.H. (2010). *Predictability of Asset Returns and the Efficient Market Hypothesis*. IZA Discussion Papers, Institute for the Study of Labor.

- Pukthuanthong-Le, K. (2010) Why Should We Like Firms that Voluntary Disclose? Evidence from Profit Warning Firms. *Forthcoming Journal of Investing*.
- Sanders, W., & Carpenter, M. (2003). Strategic satisficing? A behavioral-agency theory perspective on stock repurchases program announcements. *Academy of Management Journal*, 46, 160-178.
- Skinner, D. J. (1994). Why firms Voluntary Disclose Bad News. *Journal of Accounting Research*, Spring, 38-60.
- Sofler, L. C. Thiagarajan, S. R., & Walther, B. R. (2000). Earnings Preannouncement Strategies. *Review of Accounting Studies*, 5, 5-26.
- Taffler, R. J., Lu, J., & Kausar, A. (2004). In Denial? Stock Market Underreaction to Going-concern Audit Report Disclosures. *Journal of Accounting and Economics*, 38, 263-296.
- Tucker, J. W. (2006). Is Openness Penalized? Stock Returns around Earnings Warnings. *Financial Accounting & Reporting Section (FARS) Meeting Papers*. Available at SSRN: <http://ssrn.com/abstract=744706>
- Xu, W. (2008). Market Reaction to Warnings of Negative Earnings Surprises: Further Evidence. *Journal of Business Finance & Accounting*, 35 (7) & (8), 818-836.

Appendices

Appendix I: Companies that have issued profit warnings

1. Kakuzi
2. Longhorn
3. Eaagads
4. Express Kenya
5. KenolKobil
6. Sasini
7. East African Portland Cement Company (EAPCC)
8. Kenya Airways (KQ)
9. Mumias
10. Kapchorua Tea
11. Central bank
12. City trust limited
13. Francis Thuo and partners limited
14. SIRET Tea company ltd
15. Pan African Insurance
16. SCAN Group
17. Total Kenya Limited
18. TransCentury ltd

Appendix II Stock Returns Data Collection Kit (Kshs '000)

2007								
	Company	Beginning share price	Dividend	Ending share price	Book value	Market value	Earnings per share	Price per share
	Eaagads Limited	-	0	0.00	0	28.39	2.12	65.00
	Kakuzi Limited	-	0.00	36.25	0.37	55.55	9.78	99.17
	Kapchorua Tea Company Limited	-	4.46	112.00	0.45	0.45	(0.24)	250.81
	Express Kenya	-	5.00	375.00	4.33	5.59	2.34	86.55
	Kenol Kobil	-	4.09	19.55	1.35	2.22	1.92	14.49
	Sasini Tea And Coffee Limited	-	0	17.50	0.93	18.76	(0.18)	17.32
	Eaast African Portland Cement Company	-	3.91	128.000	0.33	12.79	16.31	391.73
	Kenya Airways	-	0.67	57.00	1.18	48.32	7.85	0.67
	Mumias	-	0.35	15.35	1.73	29.08	1.27	8.89
	Longhorn	-	1.00	24.00	0.53	45.52	2.94	12.98

2008							
Company	Beginning share price	Dividend	Ending share price	Book value	Market value	Earnings per share	Price per share
Eaagads Limited	0.00	-	45.00	1.75	25.78	-0.19	65.00
Kakuzi Limited	37.00	4.35	23.00	0.20	55.21	14.43	114.98
Kapchorua Tea Company Limited	112.00	3.33	75.00	0.34	0.34	(17.84)	220.98
Express Kenya	375.00	10.00	305.00	3.85	3.95	14.11	79.19
Kenol Kobil	19.55	1.18	17.00	0.95	14.49	2.80	17.96
Sasini Tea And Coffee Limited	17.50		17.50	0.93		-0.21	28.22
Eaast African Portland Cement Company	128.000	0.87	57.500	0.15	17.36	(11.14)	377.36
Kenya Airways	57.00	0.67	45.00	0.75	60.00	9.64	0.67
Mumias	15.35	0.45	18.85	2.16	37.09	1.59	8.71
Longhorn	24.00	0	18.85	0.39	48.01	(11.80)	9.09

2009								
	Company	Beginning share price	Dividend	Ending share price	Book value	Market value	Earnings per share	Price per share
	Eaagads Limited	-	-	36.50	1.17	31.24	3.69	65.00
	Kakuzi Limited	25.00	7.87	31.75	0.25	57.32	23.04	125.52
	Kapchorua Tea Company Limited	75.00	9.56	68.00	0.28	0.28	17.87	245.71
	Express Kenya	305.00	7.50	305.00	5.41	3.84	22.47	56.38
	Kenol Kobil	17.00	4.50	11.10	0.56	17.96	2.48	19.83
	Sasini Tea And Coffee Limited	17.50		7.75	0.27		3.88	18.76
	Eaast African Portland Cement Company	57.500	8.51	47.00	0.22	12.01	12.55	212.81
	Kenya Airways	45.00	0.67	42.00	0.61	68.64	8.89	0.67
	Mumias	18.85	0.35	10.00	3.14	45.98	0.93	3.18
	Longhorn	18.85	0	24.0	0.43	56.08	(8.16)	7.09

2010							
Company	Beginning share price	Dividend	Ending share price	Book value	Market value	Earnings per share	Price per share
Eaagads Limited	37.00	1.80	36.00	1.14	31.57	1.47	65.00
Kakuzi Limited	33.00	3.07	81.50	0.56	60.29	19.88	144.64
Kapchorua Tea Company Limited	68.00	4.28	146.00	0.53	0.53	35.60	277.43
Express Kenya	305.00	7.50	300.00	2.45	7.97	62.37	122.59
Kenol Kobil	11.10	4.47	17.90	0.85	19.83	1.12	21.17
Sasini Tea And Coffee Limited	7.75		6.05	0.18		2.34	33.29
Eaast African Portland Cement Company	47.00	2.83	221.00	0.44	14.23	100.05	500.23
Kenya Airways	42.00	0.80	47.00	0.57	82.23	10.69	0.80
Mumias	10.00	0.20	12.95	1.28	50.98	0.70	10.09
Longhorn	24.0	0	19.00	0.49	38.61	(23.95)	8.73

2011							
Company	Beginning share price	Dividend	Ending share price	Book value	Market value	Earnings per share	Price per share
Eaagads Limited	36.00	0.00	69.50	1.64	42.33	8.93	65.00
Kakuzi Limited	82.00	5.40	69.50	0.39	66.67	32.88	176.85
Kapchorua Tea Company Limited	146.00	6.52	115.00	0.35	0.35	47.80	331.32
Express Kenya	300.00	7.50	335.00	2.16	18.29	33.74	154.80
Kenol Kobil	17.90	7.46	14.75	0.47	21.17	7.79	31.06
Sasini Tea And Coffee Limited	6.05		13.30	0.36		4.36	37.45
Eaast African Portland Cement Company	221.00	6.76	185.00	0.30	13.33	(46.74)	610.46
Kenya Airways	47.00	0.80	22.75	0.31	73.52	8.64	0.80
Mumias	12.95	-42.86	29.50	1.01	57.08	-24.64	12,98
Longhorn	19.00	0	21.00	0.38	42.98	(28.90)	6.90

2012							
Company	Beginning share price	Dividend	Ending share price	Book value	Market value	Earnings per share	Price per share
Eaagads Limited	70.00	0.00	93.06	1.86	44.67	506.39	65.00
Kakuzi Limited	70.00	4.30	-14.72	0.92	72.34	65.37	182.32
Kapchorua Tea Company Limited	115.00	7.00	(21.23)	0.74	0.62	34.29	372.54
Express Kenya	335.00	5.00	339.56	3.14	21.01	(45.91)	167.12
Kenol Kobil	14.75	8.02	-17.60	0.40	31.06	593.63	33.04
Sasini Tea And Coffee Limited	13.30	6.00	-9.40	0.31	14.97	1.97	38.93
Eaast African Portland Cement Company	185.00	7.50	(16.29)	0.51	13.01	(146.72)	722.36
Kenya Airways	22.75	0.00	-51.60	0.66	88.91	9.51	0.00
Mumias	29.50	0.22	38.91	3.16	66.03	0.68	14.76
Longhorn	21.00	0	15.98	0.26	32.91	(37.90)	5.76

Appendix III :Actual profit warning

KAKUZI LIMITED

PROFIT WARNING ANNOUNCEMENT FOR THE FINANCIAL YEAR ENDING 31ST DECEMBER 2012

Kakuzi Limited ('The Group') makes this announcement pursuant to the Capital Markets Authority regulations for publicly listed companies. The Group currently forecasts that earnings for financial year 2012 may be at least 25% lower than those of financial year 2011. This anticipated drop in full year earnings is, in part, as a result of:

- i) Downward pricing pressure for our export crops due to recessionary trends particularly in Europe and the strengthening of Kenya Shilling against the Euro from an average of Kshs 134 in the second half of financial year 2011 to around Kshs 108 in financial year 2012.
- ii) An exceptional release of a provision amounting to Kshs 109 million, as a result of the withdrawal of the Delmonte Kenya Limited claim, made in financial year 2011.
- iii) The Completion of the sale of the subsidiary company, Siret Tea Company Limited, on 31st August 2012 resulting in only eight months of trading being consolidated in 2012. The Group is taking all necessary measures to maintain the Group's profitability and positive cash flow for the financial year 2012.

This profit warning announcement is based on the performance indicated by the unaudited results to 30th September 2012 with reference to information currently available.

K W Tarplee
Chairman

Longhorn eighth firm to issue profit warning this year

Posted by RAWLINGS OTINI

on Thursday, September 13 2012 at 20:31



Now, the book publisher says that it expects its profit to fall by more than 25 per cent in the year to June due to Kenya's soft economy and reduced spend by the government—which is the largest buyer of books in Kenya. Longhorn's net profit stood at Sh136.3 million in the year to June 2011—which means the firm is expecting a maximum earnings of Sh102 million.

Express, which lost the lucrative East African Breweries Ltd (EABL) transport contract in July last year, reported a loss of Sh229 million for the year ending December from a net loss of Sh28 in 2010.

Kenol was hit by high operating expenses and foreign exchange losses to post a half year net loss of Sh3.8 billion compared to a profit of Sh2.2 billion last year.

rotini @ke.nationmedia.com

Express Kenya profit warning



NAIROBI, Kenya, Jul 12 – Express Kenya is anticipating a 25 percent decline in its 2011 full year earnings, citing business instability in the last year.

In a profit warning issued on Thursday morning, the logistics firm said the dip has been influenced by the economic downturn that has generally affected transporters and the loss of part of its core business in transportation.

Kenya's KenolKobil issues profit warning

20 June, 2012

By: Christian Primavera

CATEGORY: [KENYA](#)
[34470](#)

KenolKobil Ltd, Kenya's largest fuel-retailer by market value, has issued a profit warning for the first half ending June 2012, saying the company's performance will be affected by lower international oil prices, foreign exchange losses and higher financing costs.

In a statement published in the company's website on June 19, KenolKobil said the foreign exchange hedging positions it took last year to cushion the impact of foreign exchange volatility have resulted in losses during the first six months of 2012.

Sasini profit warning

Sasini coffee and tea products. The firm has issued a profit warning after half-year net profit dropped by 86 per cent. Photo/

NSE-listed agricultural firm Sasini issued a profit warning Friday after recording an 86 per cent drop in half-year net profit attributed to low tea prices and a decline in coffee.

The firm's after-tax profit for the six months to March 2014 fell to Sh28 million from Sh200m posted for a similar period last year.

“The results for the first six months are more than 25 per cent lower than for the same period last year. Consequently, there is good reason to expect that the result for the full year will also be more than 25 per cent lower than the previous financial year should the prices of tea remain depressed,” Sasini said in a statement.