

Moderating Effect of Firm Size on Financial Reporting and Share Price of Manufacturing Firms Listed at Nairobi Securities Exchange

Nyaundi Joel¹, Ondiek B. Alala², and Tibbs Charles³

¹MBA Student and ^{2,3}Lecturer, Department of Accounting and Finance, School of Business and Economics, Masinde Muliro University of Science and Technology, P.O. BOX 190-50100 Kakamega, Kenya

Received 01 Sept 2017, Accepted 02 Nov 2017, Available online 03 Nov 2017, Vol.5 (Nov/Dec 2017 issue)

Abstract

This study aims at establishing the moderating effect of firm size on financial reporting and share price of manufacturing firms. The study targeted the finance managers of all nine manufacturing firms listed in the Nairobi Securities Exchange. Secondary data was collected from the Nairobi Securities Exchange reports between 2012- 2016 through documents analysis. The study adopted a longitudinal research design approach. Reliability was achieved by pre-testing of the questionnaires and validity was ensured by discussing the relevance of the research instrument with the supervisor and testing using Cronbach's alpha coefficient at 0.7 which was acceptable. Data was analyzed through inferential and descriptive statistics. Quantitative data was analyzed by use of descriptive statistics. Regression analysis was used in determining whether the independent variable predicts the given dependent variable. The inferential results indicated that the coefficient for firm size is 29.243 with a significant level of 0.0064 hence significant. This is because the ANOVA findings conducted showed that the significance levels for firm size. The findings further showed that the researcher should reject hypotheses which stated that there is no significant moderating effect of relationship between firm size and the share price. The findings were presented in the form of tables. The study will be of importance to academicians, practioners as well as policy makers at the Nairobi Securities exchange. Further studies need to be done on the firms which are not listed and also on manufacturing firms listed in other countries.

Keywords: Firm Size, Financial Reporting, Share Price, Securities Exchange, Listed

Background of the Study

Share price of the firm refers to the price of a single share of a number of saleable stocks of that company, derivative or other financial asset. The share price is the highest amount someone is willing to pay for the share, or the lowest amount that it can be bought for. The stock market, like most markets, is demonstrated by the laws of supply and demand. In classical economics, prices rise where there are more buyers than sellers, and at the same time, prices fall where there are fewer buyers and sellers. Dye (1998) discussed on the frequency, quality, and information role of mandatory financial reports. The share price change indicates an imbalance between buyers and sellers. In highly regulated and liquid markets, it is assumed that all available information which might affect the price is known in the public domain. When information arrives which affects earlier assumptions built into the share price, it is likely to change (Earhart, Michael & Brigham, 2010).

Globally, the share price and its valuation has been studied and researched on for a long time. Srinivan (2012)

for instance studied on the determinants of equity share prices in India.

The evidences from his study showed that Earning Price per Share and Price Earnings ratio are the crucial determinants of share prices of manufacturing, pharmaceutical sector, energy, infrastructure and commercial banking sector and that size is a significant factor in determining the share prices of all sectors he had under consideration except manufacturing. He further observed that the book value per share positively influenced the share prices of pharmaceuticals, energy, information technology and infrastructure. Diermier & Solnik (2001) also studied on the share price specifically on the global pricing of equity. They observed that if a corporation is regarded as a portfolio of international factors its stock price should be influenced by those international factors in relation to the geographical breakdown of its activities rather than where its headquarter is located or its stock is traded. Fisher (1961) looked at the influence of dividends, undistributed profits and company size on share prices obtained from samples of equities quoted on the London Stock Exchange between 1949 and 1957.

*Corresponding author's ORCID ID: 0000-0000-0000-0000

In Africa, researchers like Kinsey (2006) have also studied on share price. Kinsey (2006) compared Johannesburg Stock Exchange in South Africa and Bolsa Mexicana de Valores Stock Exchange in Mexico found that on both, book value of equity and/or earnings are relevant in explaining stock prices.

In Kenya several studies on share prices have also been done. Among them is, Sifunjo & Mwasaru (2012) who examined the causal relationship between foreign exchange rates and stock prices in Kenya. The results showed that first foreign exchange rates and stock prices are non-stationary both in first differences and level forms and that the two variables are integrated of order one. Secondly the variables are co-integrated. After finding the variables to be co-integrated, they further used error correlation models and found out that exchange rate granger causes stock prices in Kenya. The main objective of every firm is to maximize shareholders wealth. It is therefore important that as the firms carry out the process of financial reporting and as the various bodies and committees form or make adjustments to the standards and regulations governing financial reporting, they ensure that firms do not deviate from this. Shareholders want to see the value of their investment growing. This is normally reflected by the share price of the firm. This study therefore looks at the moderating effect of Firm Size on the financial reporting and share price of listed Manufacturing firms at Nairobi Securities Exchange.

Statement of the problem

The development and advancement of accounting standards only began in the late 1970 and most of the approved standards were initially mere adoption of International Accounting Standards (IAS). Current reporting practices are largely based on and strongly influenced by statutes, such as the requirements of the Companies Act. International Financial Reporting Standards (IFRS) have been adopted as high quality accounting standards that will enhance the value of accounting information across international borders. Over 100 countries, including Kenya, require IFRS for domestic reporting and this adoption has to have various benefits. Share price also has been studied on broadly. Many factors such as news releases on earnings and profits, and future estimated earnings, dividends, introduction of a new product or a product, anticipated takeover or merger, change of management, foreign exchange rates among others have been concluded to affect the share price by many researchers. Studies have been done on the benefits of adoption of IFRS on financial reporting and on the factors that affect share price but little has been done to link financial reporting and share price. Therefore there is need to find out the moderating effect of financial reporting on share price of manufacturing firms listed the Nairobi Securities exchange. Public listed companies are required to report at least once annually in

accordance with the International Accounting Standards Board (IASB).

Objective

The main objective of this study was to examine the Moderating effect of firm size on financial reporting and the share price of the manufacturing firm listed in the Nairobi Securities Exchange.

Hypothesis

Ho: There is no significant Moderating Effect of Firm Size on financial reporting and share prices of manufacturing firms listed at Nairobi Securities Exchange

Limitations of the study

Some respondents failed to respond while others did not give accurate information because they wanted to highlight some aspects and downplay others depending on personal attitude. The respondents were assured that the research was purely academic and they will be guaranteed of confidentiality and anonymity as much as possible. Secondly, the study covered only companies listed in NSE and generalization may not include companies that are not listed.

Scope of the study

The study was carried out in Kenya and data collected from the financial reports of manufacturing firms listed in the Nairobi Securities Exchange. The study adopted both primary and secondary data which were collected for the previous five financial periods of each of the firms by use of questionnaires and document analysis. In this study, a longitudinal research design was used in determining whether financial reporting affected the share price of the firm. It was done in the months between January 2016 and September 2017. Data was collected through document analysis and questionnaires. Data was analyzed by use of descriptive and inferential statistics and presented in the form of tables and graphs.

This study assumed that the respondents knew the organization well and that the information they gave in the questionnaires were accurate and reliable and that the respondents were well versed with the questions being asked. It was also assumed that all the financial reports were available as per the requirements of the listed companies.

Methodology

Research Design

The researcher adopted Longitudinal Research design. A longitudinal survey is a correlation research study that involves repeated observations of the same variables over

long periods of time, often many decades. Longitudinal research design was deemed appropriate for this study since the researcher was looking for in-depth information on the effects of financial reporting on share prices of firms listed at NSE for the period 2012-2016.

The study was conducted in nine manufacturing firms listed at NSE for the period 2012-2016. The companies are spread throughout Kenya; however, most of them have their headquarters located in Nairobi. The listed firms have their head offices within Nairobi and the trading of their securities are at the NSE which is located at Nairobi Central Business District.

Census was used since the target population was small given that the finance managers were to give the relevant information on share price performance. All the nine managers participated in the research process. The researcher used both primary and secondary data.

The quantitative data was analyzed using descriptive statistics and Regression analysis was used in finding out whether the independent variable predicts the given dependent variable. Multiple regression formula was to determine whether the independent variables collectively predict the dependent variable at 5% significance level. The regression model is as follows;

Equation 1..... $Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \epsilon$
 Equation 2..... $Y = \beta_0 + \beta_1 X_1 M + \beta_2 X_2 M + \epsilon$

Where; Y is the Share price of the firm.
 X_1 is Compliance of financial reporting
 X_2 is Disclosure of the financial reports
 β_0 is the regression constant
 β_{1-2} are the regression coefficients or change induced in Y by each independent variable
 ϵ is the error coefficient.
 M is the moderating effect firm size

The researcher maintained high ethical standards and maintained confidentiality as it was agreed not disclose any confidential information about the companies and their clients to third parties. The researcher also sought for consent to carry research from the school of graduate studies and NACOSTI.

Results and Discussions

Descriptive statistics

Table 4.3: Level of Education

	Frequency	Percent	Valid Percent	Cumulative Percent
Doctorate	6	12.0	12.0	12.0
Masters	19	38.0	38.0	50.0
Bachelors	22	44.0	44.0	94.0
Tertiary	3	6.0	6.0	100.0
Total n=50 n=50	50	100.0	100.0	

Source: Field data (2017)

From table 4.3, it is evident that majority of the respondents at 44% had reached bachelor’s degree level, 38% at masters level, 12% were at doctorate level and 6% had reached tertiary level. This shows the respondents were literate and skilled therefore understood the questions and were able to give the intended responses.

Table 4.4: Length of time working for the organization

	Frequency	Percent	Valid Percent	Cumulative Percent
0 to 4 yrs	8	16.0	16.0	16.0
5 to 9 yrs	21	42.0	42.0	58.0
10 to 14 yrs	17	34.0	34.0	92.0
15 and above	4	8.0	8.0	100.0
Total n=50	50	100.0	100.0	

Source: Field data (2017)

Table 4.4 above shows that 42% of the respondents had worked in their respective organizations for 5 to 9 years. 34% had worked for 10 to 14 years, 16% had worked for less than 5 years and 8% had worked for more than 15 years. This shows that majority of the respondents had worked for more than five years meaning that they had adequate experience in the organization and therefore were able to give adequate information.

Inferential Statistics

Moderating Effect of Size of Firm on Financial Reporting and Share Prices of Manufacturing Firms listed at Nairobi Securities Exchange.

Table 4.5 ANOVA^b

Model	Sum of Squares	Df	Mean Square	F	Sig.
1 Regression	452743.784	3	150914.595	63.251	.0001 ^a
Residual	109753.947	46	2385.955		
Total	562497.731	49			

a. Predictors: (Constant), financial disclosure, compliance, firm size

b. Dependent Variable: share prices

Significance test for the model is represented in the ANOVA table under table columns F and sig. column. F value is the mean square regression divided by the mean square residual. These values were used to determine if the independent variables predict the dependent variable and thus the sustainability of the model. From table 4.5, the p value of 0.01 when compared to the alpha level of 0.05 is smaller hence we can conclude that financial disclosure, compliance, firm size combined reliably predicts the dependent variable.

Table 4.6 Coefficients^a

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
(Constant)	-251.564	34.019		-7.395	.000
Firm size	29.243	15.428	.135	1.895	.064
1 content of financial compliance	44.410	3.765	.836	11.794	.000
Disclosure of financial reports	.415	9.290	.003	.045	.965

a. Predictors: (Constant), compliance, financial disclosure, firm size
 b. Dependent Variable: share prices
 Source: Field data (2016)

From table 4.16, the following regression equation was established.

$$Y = (-251.564) + 29.243X_1 + 44.410X_2 + 0.415X_3 + 34.019$$

The coefficient for firm size is 29.243 with a significant level of 0.0064 hence significant.

The coefficient for compliance of financial reporting is 44.410 with a significance level of 0.001 hence significant.

The coefficient for disclosure of financial reports is 0.415 with a significance level of 0.965 hence not significant.

From the multivariate regression equation $Y = (-251.564) + 29.243X_1 + 44.410X_2 + 0.415X_3 + 34.019$,

Y is the share price of the firm.

-251.564 is the regression constant alpha which shows that in the absence of financial reporting, the share price would be -251.564.

β_1 is equal to 29.243 and it indicates that a unit change in frequency of financial reporting results in 29.243 times increase in share price.

β_2 is equal to 44.410 and it indicates that a unit change in content of financial reporting results in 44.410 times increase in share price.

β_3 is equal to 0.415 and it indicates that a unit change in timeliness of financial reporting results in 0.415 times increase in share price.

34.019 is the error term.

Coefficient variables are said to be correlated if the coefficient of correlation (p-value) is less than the alpha level of 0.05. In such a case, the null hypothesis is rejected.

The findings therefore indicate that frequency and content of financial reporting with p-values of 0.0064 and 0.0001 respectively are correlated to share price while timeliness of financial reporting with a p-value of 0.965 is not. This is in line with Ball (2001) who also argued that an economically efficient public financial reporting and disclosure system requires training an audit profession of adequate numbers, professional ability, and independence from managers to certify reliably the quality of financial statements which in effect affects the share prices.

Summary, Conclusion and Recommendations

The ANOVA findings conducted showed that the significance levels for firm size was less than 0.05 while

the significance level for compliance was above 0.05. The findings further showed that the researcher should reject hypotheses H_{03} which stated that there is no significant moderating effect of firm size between financial reporting and the share price.

Conclusion

The research focused on the moderating effect of firm size on financial reporting and share price of firms listed in the Nairobi Securities Exchange. The firm size and financial reporting were studied as the independent variables with the share price as the dependent variable. Finance managers of all the sixty four listed companies were targeted but as it had been anticipated, there was non-responsiveness of some with only fifty responding and hence the usable population.

From the findings of the study, the researcher concluded that firm size and financial reporting are significantly affecting share price

Recommendations

The standardization and regulations on financial reporting are improving day to day. From this study it is recommended that emphasis be put on the financial disclosure in these reports as they improve the share prices of the firms hence help the firms in achieving the goal of value maximization. Compliance with financial reporting although not found to be correlated should be considered but not with much emphasis as to disclosure. Listed firms are recommended to include as much information as they could in the reports and also to frequently publish the reports.

Recommendation for Further Research

This study although done may not have conclusively researched on the topic taking into consideration the limitations and the assumptions. First, the study was done only on listed firms in Kenya. Further studies need to be done on the firms which are not listed and also on firms in other countries. There is also need for research on other factors affecting the share price as only 80.4% could be explained by the independent variables in this study.

Finally, more research should be done on financial reporting to determine whether there are other variables like the timeliness of the reports and how they are affected by it except the share price.

References

[1]. Ahmed, K. (2003). A comparative study of timeliness of corporate financial reporting in South Asia. *Advances in International Accounting*, 16, 17-42.
 [2]. Aiman, A. & Mohammad, M. (2006). Accounting information, value relevance and investors behavior in the Egyptian equity market. *Review of Accounting*, 5(3), 279-297.

- [3]. Babbie, E.R. (2010). *The Practice of Social Research* (12th ed.). Wadsworth: Cengage Learning.
- [4]. Babbie, E. (2004). *The Practice of Social Research*. (3rd ed.). University of Michigan: Wadsworth Publishing.
- [5]. Buigut, K., Koskei, I., & Kibet, J. (2013). The effect of capital structure on share price on listed firms in Kenya. A case of listed companies in Kenya. *European Journal of Business and Management*, 5(9),
- [6]. CAAFR. (2008). *Improving the timeliness of financial reports*. UK:
- [7]. Chambers, A., & Penman, S. (1984). Timeliness of reporting and stock price reaction to earnings announcements. *Journal of Accounting Research*, 22, 21-47.
- [8]. Darskuviene, V(2015) *Financial Markets*, Leonardo da Vinci Program Project, Vytautas Magnus University
- [9]. Davies, R.B. (1994) 'From Cross-Sectional to Longitudinal Analysis', in Dale, A. and Davies, R.B. (Eds.) *Analyzing Social and Political Change. A Casebook of Methods*, London: Sage Publications.
- [10]. Dennis, S., & Sim, A. (1999). Share volatility with the introduction of individual share Collins, D., & Abraham, M. (2006). Measuring the cost of equity African financial markets. *Emerging Markets Review*, 7(1), 67-81. futures on the Sydney futures exchange. *International Review of Financial Analysis*,
- [11]. Diermier, J., & Solnik, B. (2001). Global pricing of equity. *Financial Analyst journal*, 57(4), 37.
- [12]. Earnhardt, M., & Brigham, E. (2010). Corporate Finance: A focused Approach. *Cengage Learning*, 275.
- [13]. Fisher, G. R. (1961). Some factors influencing share prices. *The Economic Journal*, 71(281), 121-141.
- [14]. Gay. (1992) Educational Research: An Introduction. New York: Pearson Education, Inc
- [15]. Gigler, F., & Hemmer, T. (1998). On the frequency, quality and informational role of mandatory financial reports. *Journal of Accounting Research*, 36,
- [16]. Glickstein, D., & Wubbels, R. (1983). *The Journal of Portfolio Management*, 9(3), 28-32.
- [17]. Jensen, M. (1993). The modern industrial revolution exit and the failure of internal control systems. *Journal of Finance*, 48, 831-880. Hamilton, William Peter, 1922, *The Stock Market Barometer: A Study of its Forecast Value Based on Charles H. Dow's Theory of the Price Movement*, Barrons, New York.
- [18]. Henriksson, Roy D. and Robert C., 1981, "On Market Timing and Investment Performance. II. Statistical Procedures for Evaluating Forecasting Skills," *Journal of Business*, 54:4, pp.513-533.
- [19]. Kinsey, J. P. (2006). Developing Countries converging with developed country Accounting Standards. *The International Journal of accounting*, 41(2), 141-162.
- [20]. Kisaka, S., & Mwasaru, A. (2012). The causal relationship between foreign exchange rates and stock prices in Kenya from november1993 to may 1999. *Research Journal of Finance and Accounting*, 3(7),
- [21]. Kothari, C. (2004). *Research methodology : Methods and techniques*. (2nd ed.). New Delhi, India: New Age International (P) Ltd.
- [22]. Leedy, P. (1993). *Practical research: planning and design*. (5th ed.). NJ: Prentice Hall, Inc.
- [23]. Marshall, C. & Rossman, G.B. (1995). *Designing Qualitative Research*. London: Sage Publications.
- [24]. Malkiel, B. G., & Cragg, J. G. (1970). Expectations and the structure of share prices. *The American Economic review*, 60(4), 601-617.
- [25]. McDaniel, L., Martin, R., & Main, L. (2002). Evaluating financial reporting quality : the effects of financial expertise vs. financial literacy. *The Accounting Review Supplement*, 153.
- [26]. McGee, R. (2007). Corporate Governance in Russia : A case study of timeliness of Financial Reporting in the Telkom Industry. *International Finance Review*, 7, 365-390.
- [27]. McGee, R. (2007, July). *Corporate governance and the timeliness of financial reporting : case study of the Russian energy sector*. Fifth international conference on accounting and finance in transition , London.
- [28]. Meznar, M., & Nigh, D. (1994). Effects of announcements of withdrawal from South Africa on stockholder wealth. *Academy of Management Journal*, 37(6), 1633-1648.
- [29]. Cowles, Alfred ,(1934) "Can Stock Market Forecasters Forecast?" *Econometrica*, pp.309-324.
- [30]. McCullagh, P. and J.A. Nelder, (1983), *Generalized Linear Models*, Chapman and Hall, Ltd., Cambridge, England.
- [31]. Rhea, Robert, 1932, *The Dow Theory*, Barron's, New York.
- [32]. Mugenda, & Mugenda, (2003). *Research Methods Nairobi: Acts Press*.
- [33]. O'Hara, M., & Macey, J. (2003). Solving the corporate governance problems of banks: A proposal. *Banking Law Journal*, 120(4), 326-348.
- [34]. Olweny, T., & Kimani, D. (2011). Stock market performance and economic growth: empirical evidence from Kenya using causality test approach. *Advances in Management and Applied Economics*, 1(3), 153-196.
- [35]. *Practical implementation of IFRS, lessons learned*. (2008). UN conference on trade and development.
- [36]. Ranganatham, M. (2006). *Investment Analysis and Portfolio Management*. India: Peason Education.
- [37]. Srinivasan, P. (2012). Determinants of equity share prices in India: A panel approach. *The Romanian Economic Journal, journal(xv)*, 205-206.
- [38]. Watts, R., & Zimmerman, J. (1990). Toward a positive theory of the determination of accounting standards. *Accounting Review*, 65, 131-156.