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Effect of Corporate Disclosures on Market Returns of Commercial Banks Listed at the Nairobi Securities Exchange

Mercy Moraa Nyakundi [α] & Dr. Oluoch Oluoch [σ]

Abstract- This study aimed to assess the effect of corporate disclosures on market returns of commercial banks at Nairobi security exchange (NSE). Specific objectives were to assess the effect of environmental disclosures, social responsibility disclosures. The study adopted the institutional theory, market efficient theory and agency theory to support the literature review on corporate disclosures in looking at banks income statement, statement of financial position and additional notes to establish its profitability, liquidity over time frame annual reports. This study adopted descriptive research design. The study targeted 11 commercial banks. Secondary data was collected using data collection schedule. Data was analyzed using descriptive and inferential statistics, a multiple linear regression model was used to establish the relationship between variables. The study was of great importance to theory of development and literature for investors, shareholders, managers and law makers in making knowledgeable decisions and regulations considering the financing patterns and strategies of financial stability in Kenya, based on findings, recommendation and suggestions to further the study. The correlation analysis was used in this study and regression model to establish the effect between corporate disclosure and market returns of commercial banks. There was a positive effect between environmental disclosure and market returns. The study recommended that governance disclosure should be enhanced with other governance details. The study recommended that corporate social cost should be enhanced within social responsibility. The study was limited to corporate disclosure on market returns. Another limitation was based on data collection from annual reports and additional notes. Study findings were applicable to only commercial banks. The study suggested for future study to be conducted on the effect of corporate disclosures on market returns on other institutions.

I. Introduction

Corporate disclosure aims to communicate what the firm does to shareholders and stakeholders in terms of market returns to inform investors (Diamond, 2014). This communication is not only called for by shareholders and investors to analyze the relevance of their investments. Disclosure is the provision of relevant information that results in a transparent and accurate picture of a corporate operations, and governance (Simiyu, 2013). Corporate disclosure raises systematic risk for the banking disclosures through its annual reports which has been one of the rapidly growing areas fields (Dawkins, 2014).

In United Kingdom, corporate disclosure is known as the process of communicating social and environmental effects of organizations activities to particular groups at large (Kimani, 2015). Corporate disclosure is the communication of information by people from internal commercial banks towards external people (Namakonz & Inanga, 2014). This information is based on financial reports aimed at creating confidence of the customers and investors. Corporate disclosures prompt other investors and depositors of other banks to question their market returns. Corporate disclosure enable investors to get information about the failed bank and try predict the solvency of other banks to reflect shares prices (Omollo, 2014).

In European Union, the disclosing bank information is about their corporate performance by cost and incomes (Kahlenborn, 2012). However, while market returns may be imperfect, so that banks can apply regulation, or other firms are supported by own regulations, private lawsuits, and market discipline with adequate incentives to disclose information at socially optimal levels, but also by the other stakeholders (Polocheki, 2013). This is particularly for information about corporate social, environment, financial policies and human resource disclosures.

Market return is the income expected from the market above its risk free rate (Thielemann, 2012). Market returns are influenced by different factors such as government actions, and general economic conditions. Market returns in security performance in an economy takes different forms between disclosures among capital markets. Growth of market returns is influenced by financial disclosure, interest rates, exchange and inflation rate. The trading securities valuation affects disclosure of commercial banks on lending declaration before liquidation. They classify disclosures as strategic, non-financial and financial information. They classify the disclosures depending on what they are intended for the content (Roberts, 2013).

Kenyan commercial banks are licensed and regulated pursuant to the provisions of the Banking Act and the regulations and prudential guidelines issued by the Central Bank of Kenya. Currently banking sector is known as financial due diligence banking. Matengo

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Bansal, P. and I. Clelland: (2014) emphasized that corporate disclosures are associated with technology and has totally changed the banking system and that is further tuned by the competition in the banking industry in Kenya. Kahlenborn (2012) reflected that perplexing commercial environment surrounded by the banking system has formed more improvement in the fields of product, process and market. Information disclosed has given rise to new ideas in the product designing and their delivery in the banking and finance industries

a) Statement of the Problem

Corporate disclosures are meant to influence the interpretation of financial reports which later influences the market returns. In recent times, stocks have earned a lower rate of market return in share prices, thus, the lower rate of return. Fluctuation of share prices has led to low market returns, even though corporate disclosures are used it is not clear which disclosure can enhance it. It is evidenced by a study of Peter (2015) who noted that actual stocks of 7% real market return was recorded in its historical average in 2016. In the year 2017, market returns assumed some variation in its initial period followed by its decline rate to 6.3%. Therefore, corporate disclosure can be utilized to establish whether it influences market returns in commercial banks listed in Kenya. Thus, this study intends to investigate the effect of corporate disclosures on market returns on commercial banks at Nairobi security exchange.

b) Specific Objectives

The general objective was used with the following specific objectives;

i. To assess the effect of environmental disclosures on market returns of commercial banks in at Nairobi security exchange.
ii. To examine the effect of social responsibility disclosures on market returns of commercial banks at Nairobi security exchange.

c) Theoretical Literature Review

The study was guided by Institutional Theory which was modified by Dahawy, (2009). The theory states that the value of conformity with the institutional environment is the adherence to external rules and societal norms (Leuz, Verrecchia, Douglas et al (2014). The assumption of the theory is that contracts with institutions comply with institutional norms and requirements as a requisite for approval to operate in the public sphere. It assumes that the increased disclosure reflects corporate awareness of its responsibility to society and shows the extent to which the company has embraced the prevailing societal values. It is also a means of integrating companies with their stakeholders and strengthening the social bonds between the companies and their stakeholders (Dastgir, Haw Bowman, 2014).

FamaZareian, (2012) noted that managers who intend to make capital market transactions have motivations to disclose information voluntarily to decrease the information asymmetry problem and thus decrease the external financing cost. The capital need theory predicts that increased financial disclosure of information by the company's managers will enable them to lower the company's cost of capital through reducing investor uncertainty. This theory is relevant as it can be used to establish the relationship that exists between shareholders' interests and agent's interests. The management at the top act as the principles and trust the lowers management at the branch and subordinates in the assumptions of providing corporate disclosures. The theory of agency indicates that the principal expects to continue with corporate disclosures and his agents, but the agent interests vary.

d) Conceptual Framework

This is the diagrammatic representation of conceptual framework which shows how the variables are related. Environmental disclosure, social responsibility are independent variables but market returns is a dependent variable, which was measured by opening share price and closing share price on the occurrences of the said independent variables.

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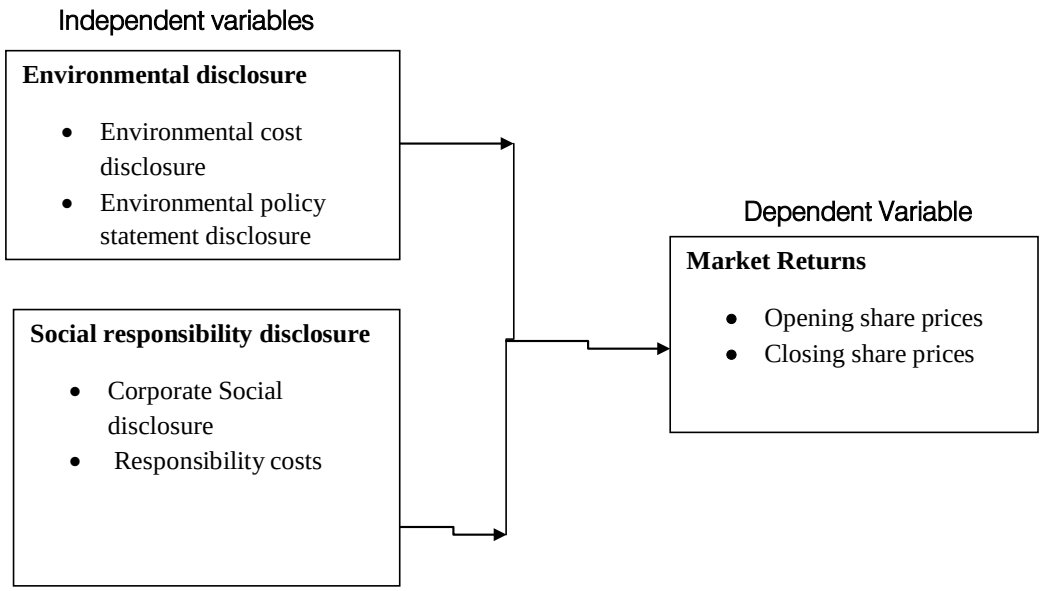


Figure 2.1: Conceptual framework

II. Empirical Literature

a) Environmental Disclosures

Environmental disclosure is the information about the firms' environments and how it influences or about its resources (Malik, 2018). Environmental disclosure affects financial accountability of firms. In agency theory with the intention of environmental disclosure is financially disclosed reports. It can increase the company financial reputations. It manages transparency and disclosure in all kinds of activities. Bank business environments are well briefed before disclosed meetings. Thus, there is need to emphasize in all practices and disclosure levels should not be restricted to annual reports. It is noted that large firms disclose more information as compared to small firms (Dawkins and Fraas, 2015). This study focuses on environmental disclosures in commercial banks.

b) Corporate Responsibility Disclosure

Corporate social responsibility is the business approach that contributes to sustainable development by delivery of economic, social and environmental benefit for all stakeholders (Odote 2013). Gray (2012) conducted a study on the effect of social responsibility disclosure reporting on financial returns of firms. The aim of the study was to examine the effect of social reporting on financial returns of firms. The study found that financial account to the owners of capital; in particular, shareholders affect financial returns. The company consistently disclose major and market sensitive information punctually, it publishes/announce semi-annual reports within two months of the end of the half-year. Such an extension is predicated upon the assumption that companies do have wider responsibilities than simply to make money for their shareholders.

III. Research Methodology

The study adopted descriptive research design. The proposed study comprised of the 11 commercial banks listed in the NSE. The study used annual published financial statements of the commercial banks. This was done by use of data collection sheet to collect secondary data. The data obtained was analyzed using descriptive and inferential statistics, correlation analysis and multiple linear regression analysis.

IV. Results and Discusion

a) Environmental disclosure

The study sought to determine the effect of environmental disclosures on market returns of commercial banks listed at Nairobi security exchange.

Table 1: Environmental Disclosures

	Minimum	Maximum	Mean	Std. Deviation
Environmental cost	2	473	100.56	134.190
Environmental policy	1	169	37.98	44.955

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The results showed that environmental cost had a minimum value of 2 to maximum value of 473 with a mean of 100.5 and standard deviation of 134.190. Environmental policy had minimum value of 1 to a maximum value of 169 as compared with a mean of 37.98 and standard deviation of 44.955.

b) Social Responsibility

The study sought to establish the effect of social responsibility on market returns of listed commercial banks.

Table 2: Social responsibility

	Minimum	Maximum	Mean	Std. Deviation
Corporate social cost	34	568	189.73	118.183
Responsibility costs	29	256	156.91	48.291

The results showed that corporate social cost with a mean of 189.73 and standard deviation of 118.183, responsibility cost had a mean of 156.91 and standard deviation of 48.291.

The calculated R and R^2 values was presented in table 3. The R value is the multiple Pearson's correlation coefficient and the study found it to be .383 which means that the correlation between predicted and observed values of market returns is relatively small. The R^2 value indicates how much of the total variation in the dependent variable (market returns) can be explained by the independent variables (Environmental Disclosure and Social Responsibility). In this case 14.6% (R Square = 0.146) of the variation in market returns can be explained by corporate disclosures regardless of their significance in the model. However, considering only the significant independent variables in the model, 10.9% (adjusted R Square = 0.109) of the variation in market returns could be explained by disclosures that were significant that is to say, the independent variables whose p-values for t-statistic were less than the standard threshold of 5%.

Table 3: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.383[a]	.146	.109	3.204

a. Predictors: (Constant), , Environmental Disclosure, Social Responsibility

Table 4: Regression Coefficients[a]

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	8.948	1.724		5.189	.000
Environmental disclosure	.913	.193		4.721	.000
Social responsibility	.271	.034	.556	8.019	.000

a. Dependent Variable: Market returns

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + ...\varepsilon$$

Which would be: $Y = 8.948 + .913\ X_1 + .271\ X_2$ Y=Dependent Variable (market returns)

x_1= environmental disclosure, x_2= corporate social responsibility

The regression analysis reveals that a unit increase in environmental disclosure increased market returns by 8.948 (p-value <0.0001) if a unit increase in social responsibility increases market returns by 0.913 (p-value <0.0001) if environmental disclosure, other factors held constant; a unit increased by .271 at p-value .000.

The general form of the equation can be used to predict market returns. For every unit increase in corporate disclosures (environmental disclosure, social responsibility with other factors held constant as reflected by the value (8.948) could improve to market returns and it was statistically significant at 5%.

V. Conclusion and Recommendation

The first objective sought to determine the effect of environmental disclosures on market returns of commercial banks in at Nairobi security exchange. Most commercial banks were not aware of environmental cost disclosures when disclosing their financial reports. There

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was a positive association between environmental disclosure and market returns.

The second objective sought to establish the effect of social responsibility on market returns of listed commercial banks. Based on correlation analysis, social responsibility had a positive association to market returns.

Based on the findings, the study recommended that commercial banks should manage environmental cost to improve market returns. The study recommended that corporate social cost should be enhanced within social responsibility. The study focused on disclosures of commercial banks, thus, there is need to conduct another study on the relationship between Social Responsibility using financial performance in general.

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