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EFFECT OF DISCLOSURE LEVEL ON FINANCIAL PERFORMANCE OF LISTED STATE CORPORATIONS IN KENYA

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Abstract: *Kenya, as a country, has adopted the International Financial Reporting Standards, and is a requirement for all entities owned by the government to apply these standards. Therefore, it is of interest to know the extent of compliance to the standards applicable to listed state corporations given that a number of them have been reporting poor financial performance. The objective of the study was to assess the effect of disclosure level on financial performance. A descripto-explanatory research design was adopted alongside positivism paradigm and quantitative approach. All the five state corporations which are listed and actively trading on the NSE were targeted. In particular, the finance, accounting and management staff working in these corporations are projected to participate in the study. A sample of 385 respondents was drawn from the study population using both purposive and simple random sampling techniques. A structured questionnaire and data collection sheet were employed in collecting primary and secondary data respectively. The Statistical Package for Social Sciences was used to facilitate the analysis of the collected data. Descriptive statistics and inferential statistics were used in the analysis. Findings were that disclosure level had a positive and significant effect on financial performance of (β= -.216, $p < 0.05$). The study concluded that disclosure level affects the financial performance of listed state corporations in Kenya. The study recommended that state corporations should continue to make sufficient disclosure in financial statements and reports.*

Keywords: *International Financial Reporting Standards, Disclosure Level, Financial Performance*

1.0 Introduction

State corporations play a crucial role in the implementation of government ministries' agenda. Some of the corporations are listed at the NSE and, essentially, bring on board investors both at individual and corporate levels. Apparently, their financial performance is very paramount due to the fact that investors are always interested in the dividends accruing from their investments. The aforesaid can only be positively realized when the corporations post good financial performance (particularly in terms of return in equity (ROE), return on investment (ROI), Return on Assets (ROA) and dividend payout ratio. However, several of these state corporations have lately been recording either declining or negative financial performance expressed using the aforementioned indicators. A case in point is the Kenya Power Company which has recorded 0% ordinary dividends for three years in a row (2019/20, 2020/21, and 2021/22) as well as negative earnings per share (-0.48) in the financial year ending 30thJune 2020 (Kenya Power, 2020).

East African Portland Cement (EAPC) reported loss before tax for FY2018/19 and FY2019/20 at Ksh 2.96 billion and Ksh 2.80 billion respectively. The ROE for each of the two years was -15% while EPS was -37.35

and -30.77 respectively (EAPC, 2020). On the other hand, Kenya Reinsurance Corporation Limited recorded a decline in profit before tax from Ksh 4.18 billion in 2019 to Ksh 3.98 billion in 2020 (Kenya Reisurance Corporation Limited, 2021). The foregoing statistics are a clear indication of financial problems facing listed state corporations in Kenya. The negative or declining financial performance is a problem to the shareholders since they receive reduced or negative EPS and/or reduced or no dividends at all. For instance, shareholders of the Kenya Power Company did not receive any dividends for 3 consecutive years (Kenya Power, 2020). The EPS for EAPC was negative for two financial years in a row (EAPC, 2020).

When there is declining or negative financial performance, the state corporations are likely to witness reduced shareholding and/or investment. An example is the reduced ordinary shareholders' equity at the Kenya Power Company for 4 consecutive financial years. The ordinary shareholders' equity reduced consistently from 63.3 million to 60.6 million to 56.2 million to 54.9 million between the FY 2016/17 and FY 2019/20 (Kenya Power, 2020). This is due to the fact that investors are always interested in positive EPS and to enjoy dividends from their equity. When the corporations post declining financial performance, it is apparent that EPS and dividends will equally be compromised thus resulting in reduced investment. The operations, activities, programmes and/or projects which are financed by these entities are affected substantially.

The revenue collected from the corporation in terms of payable taxes also reduces. When state corporations underperform, they contribute to the inefficient allocation of resources in the broader economy which lead to additional strains on already depressed public budgets. Downsizing of the staff is another probable effect of the aforestated problem as the corporations take measures to restructure in an attempt to turn around their falling financial fortunes. The empirical studies conducted so far have fallen short of adequately and explicitly illustrating how the financial performance of listed state corporations in Kenya is affected by IFRS. The research gap necessitates an empirical investigation into the effect of disclosure level on financial performance of listed state corporations in Kenya. To achieve this objective, the study focused on disclosure level and how it affects the financial performance of state corporations listed at Nairobi Securities Exchange, Kenya. The remainder of this article is as follows; section 2 cover literature review and hypothesis development, section 3, research methodology, section 4, results & discussions and section 5, conclusion and recommendations.

2.0 Literature Review & Hypothesis Development

2.1 Disclosure Level and Financial Performance

Admittedly, the hitherto review on academic research has indicated the existence of high levels of non-compliance as well as high volatility across entities, with some returning very poor disclosure levels of far below the average (Hellman, Carenys, & Gutierrez, 2018). There is notable methodological problem of measuring compliance with disclosure principles. The compliance level is subject to the incentives given to entities with regard to provision or withholding information alongside prevailing local conditions for primary users. Arguably, increased reliance on entities to act in good faith in their compliance with disclosure requirements is, to a considerable extent, risky especially on how well the IFRS protect primary users from poor disclosers (Hellman et al., 2018).

A greater use of disclosure principles is likely to affect specific IFRS standards disclosure requirements in only one specific instance (IASB, 2017a). Pertinently, in the event that a principle included in a general disclosure standard, it can potentially lead to deletion of specific requirements in the described standard. The IASB made a decision to carry out a targeted standards-level review of disclosure requirements that involved the formulation of guidance for the Board to employ when coming up with disclosure requirements as well as testing this guidance on one or two identified IFRS standards (IASB, 2018a). In respect of individual users, analysts are in a position to make a clear distinction between complex language that is needed to convey information regarding the business transactions of an entity from complex language to the aspect of managerial obfuscation (Bushee, Gow, & Taylor, 2017). The importance of disclosure is pegged on the fact that primary users do not wish to receive less financial statement information. Yet, investors and analysts who take part in roundtable discussions and interviews are only interested in footnotes of financial statements (Erkens, 2016).

A study commissioned by the International Accounting Standards Board (IASB) Research Forum (2017), and which was conducted by Hellman, et al., (2018) evaluated the effects of introducing more principles of disclosure in line with the IASB disclosure initiative. The objective was to assess the effects of introducing more high-level principles of disclosure in IFRS. The study adopted desk research that involved literature review of pertinent academic research. According to the findings, there were high levels of non-compliance and also high volatility across entities. It was also revealed that there was no clear pattern regarding higher compliance for IFRS. The study concluded that entities in capital market (that is, listed firms) were likely to be in more high incentive situations, and as such, had low costs of non-compliance. It was recommended that there is need to ensure that the disclosure requirements are both auditable and enforceable in order to secure a particular minimum threshold or level of disclosure.

A comparative study on government-linked and non-government-linked firms focused on the disclosure practices of large Malaysian publicly listed companies (Che & English, 2016). The study employed unweighted disclosure index based on IFRS extant in each year. It adopted a sample of Malaysian firms selected from Bursa Malaysia. The government-linked firms were 9 while an equal number constituted non-government-linked entities. The requisite data were obtained from the firms' annual financial reports beginning 2011. It was found that the average firm score was 46% as per the disclosure index stipulated by the IFRS with a lower bound and upper bound of 33% and 59% respectively. The study concluded that the overall compliance was not predictable and varied considerably between standards.

In Ghana, a study by Assenso-Okofo, Ali and Ahmed (2021) examined the political, economic, and legal systems, and institutional factors influencing the accounting and disclosure practices in the country. In the wake of Ghana completing adoption of IFRS in 2007, the objective of the study was to assess the impact of the aforesaid standards on disclosure. Longitudinal country case design was adopted. The study established that both the accounting and reporting practices were significantly influenced by institutional, legal, political, and economic factors. It was also revealed that the regulatory environment was neither effective nor efficient as results of the weak enforcement and monitoring of compliance.

An empirical study conducted by Bova and Pereira (2017) examined factors that influence compliance of IFRS following its adoption in Kenya. The objective was to examine the factors that influence IFRS compliance, and whether the compliance improved information environment of a firm. The required data were obtained from Kenya's Financial Reporting Awards for 2006. Regression analysis was employed where the disclosure measure was the dependent variable. The collected data were obtained from the annual financial reports of 48 private and 30 publicly traded Kenyan firms. The study findings indicated that there was 71% of the disclosure index as espoused by IFRS with regard to the publicly traded firms. It was inferred that in spite of the fact that both private and public firms are required to abide with IFRS, public entities exhibit greater adherence to IFRS compliance.

Another local study by Kipchoge (2015) analyzed the effect of corporate attributes on IFRS disclosure level amongst firms listed on the Nairobi Securities Exchange. The specific objectives included to examine the effect of profitability, liquidity, firm size, and leverage on corporate IFRS disclosure level. Explanatory research design was adopted with the aim to establishing cause-effect relationship between predictor and outcome variables. The study involved a sample of 30 companies listed on the NSE from which panel data spanning from 2007 to 2011 were obtained. The panel data were specifically sourced from the annual financial reports of the aforestated firms. Both descriptive and inferential statistics were employed in the data analysis. The results of the analysis indicated that profitability, firm size, and liquidity had a positive and significant effect on IFRS disclosure level. The study recommended that there ought to be corporate policies and legal framework that can guide as well as obligate all firms to disclose IFRS as required by the IASB. Literature reviewed led to development of the following hypothesis statement.

H_{01}: *There is no significant effect of disclosure level on financial performance of listed state corporations in Kenya.*

3.0 Research Methodology

The study adopted a descripto-explanatory research design. This design involves both descriptive survey and explanatory research designs (Pandey & Pandey, 2021). In support of descripto-explanatory design, this study put into perspective IFRS and financial performance phenomena and in respect of listed state corporations in Kenya. Additionally, in tandem with the stipulations of the aforementioned design, the effect of IFRS on financial performance as well as the relationship between the two constructs were examined. In addition to the descripto-explanatory research design, positivist philosophy and quantitative approach were adopted. The target population was 11065 staffs of the respective state corporations considered in this study while the accessible population was 700. The sample size was 385 accounting, finance and management staff working at the head offices of the 5 listed state corporations in Kenya. The study adopted both purposive and simple random sampling methods. Two sets of data were collected in the study, that is, primary and secondary data. The collected data was analyzed with the aid of the Statistical Package for Social Sciences (SPSS) tool. The data was electronically analyzed by employing descriptive as well as inferential statistics. Notably, the following regression model was adopted.

$$Y = \beta_0 + \beta_1 X_1 + \varepsilon \qquad (1)$$

Where; Y is financial performance; β_0 represent the constant, X1 disclosure level, β_1 regression coefficient of disclosure level ε is the error term or precision level. The results of the analyses were presented in tabular form.

4.0 Results & Discussions

4.1 Descriptive Statistics

The study sought to examine the effect of disclosure level on financial performance of listed state corporations in Kenya. The indicators of disclosure level adopted in this study were; defaults and breaches, net gain/net losses, impairment of financial bassets and hedging fund. Findings are presented in Table 1.

Table 1: Disclosure Level

n=323		SD	D	NS	A	S. A	Mean	Std. Dev
Our corporation makes sufficient disclosure in its financial statements and reports	F	27	40	34	115	107	3.7276	1.27082
	%	8.4	12.4	10.5	35.6	33.1		

In accordance with both internal and external audit reports, our corporation always secures at least minimum level of disclosure	F	34	38	25	82	144	3.8173	1.38338
	%	10.5	11.8	7.7	25.4	44.6		
Our corporation makes disclosure of information concerning the significance of financial instruments to our entity	F	39	41	33	56	154	3.7585	1.45658
	%	12.1	12.7	10.2	17.3	47.7		
Our corporation makes disclosures on the nature and extent of risks emanating from financial instruments used here	F	44	27	27	84	141	3.7771	1.42727
	%	13.6	8.4	8.4	26.0	43.7		
Our corporation makes specific disclosures on transferrable financial assets	F	58	29	27	83	126	3.5882	1.51210
	%	18.0	9.0	8.4	25.7	39.0		
In making relevant disclosures, our corporation categorizes financial instruments in classes that are similar in line with the information presented	F	37	45	26	142	73	3.5232	1.29329
	%	11.5	13.9	8.0	44.0	22.6		

The study was interested in determining whether the corporation makes sufficient disclosure in its financial statements and reports, 222(68.7%) agreed while 67 (20.7%) disagreed. Sufficient disclosure in its financial statements and reports was further found to affect financial performance with (mean=3.7276, std. Dev. = 1.27082). Findings are similar to that of Hellman, et al. (2018) that sufficient disclosure in financial statements and reports affect financial performance. On whether the corporation always secures at least minimum level of disclosure in accordance with both internal and external audit reports, 226(70.0%) agreed while 72(22.3%) disagreed. Securing at least minimum level of disclosure in accordance with both internal and external audit reports was further found to affect financial performance with (mean=3.8173, std. Dev. = 1.38338). The study is in agreement with that of Bushee et al., (2017) that securing at least minimum level of disclosure in accordance with both internal and external audit reports affect financial performance.

Out of the total respondents, 210(65.0%) agreed that the corporation makes disclosure of information concerning the significance of financial instruments to their entity while 80(24.8%) disagreed. Making disclosure of information concerning the significance of financial instruments to an entity was further found to affect financial performance with (mean=3.7585, std. Dev. = 1.45658). The study is in agreement with Erkens (2016) that making disclosure of information concerning the significance of financial instruments to an entity affects financial performance. In regards to whether the state corporation makes disclosures on the nature and extent of risks emanating from financial instruments used in the entity, 225 (69.7%) agreed while 71(22.0%) disagreed. Making disclosures on the nature and extent of risks emanating from financial instruments used in the entity was further established to affect financial performance of state corporations with (mean= 3.7771, std. Dev. = 1.42727). Findings resemble that of Hellman, et al. (2018) that making disclosures on the nature and extent of risks emanating from financial instruments used by a state corporation affects financial performance.

In regards to whether the corporation makes specific disclosures on transferrable financial assets, 209 (64.7%) agreed while 87(26.9%) disagreed. Making specific disclosures on transferrable financial assets was further established to affect financial performance of state corporations with (mean= 3.5882, std. Dev. = 1.51210).

Findings resemble that of Bushee et al., (2017) that making specific disclosures on transferrable financial assets affects financial performance of state corporations. The study wanted to find-out whether in making relevant disclosures, state corporation categorizes financial instruments in classes that are similar in line with the information presented, 215(66.6%) agreed while 82(25.4%) disagreed. Making relevant disclosures, state corporation categorizes financial instruments in classes that are similar in line with the information presented was further established to affect financial performance of state corporations with (mean= 3.5232, std. Dev. = 1.29329). Findings are similar to that of Bushee et al., (2017) that making relevant disclosures, categorization of financial instruments in classes that are similar in line with the information presented affects financial performance.

4.2 Inferential Statistics

4.2.1 Correlation Analysis

Correlation analysis is adopted to determine whether there is any relationship between international financial reporting standards and financial performance. It also helps to determine how strong the relationship is. Findings are presented in Table 2.

Table 2: Correlation analysis

n=323		Performance	Disclose
Performance	Pearson Correlation	1	
	Sig. (2-tailed)		
Disclose	Pearson Correlation	.775*	1
	Sig. (2-tailed)	.000	

*. Correlation is significant at the 0.05 level (2-tailed).

Disclosure level was found to have a significantly strong positive relationship with financial performance of ($r = .775$, p-value < 0.05). This implies that disclosure level contributes to improvement in financial performance. The study agrees with that of Hellman et al., (2018) that disclosure level has a strong significant positive relationship with financial performance.

4.2.2 Simple Linear Regression Analysis

Simple regression was adopted to determine how disclosure level predict the dependent variable (financial performance). Findings for simple linear regression analysis were presented in Table 3, 4 and 5. The regression model summary results were presented in Table 3.

Table 3: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.567[a]	.321	.313	2.54326

a. Predictors: (Constant), Disclosure level

The value of the adjusted R-square is 0.313 which implies that the model explains 31.3% of financial performance can be predicted by disclosure level. In order to assess the goodness of fit test of the regression model, Analysis of variance (ANOVA) was adopted. The findings were presented in Table 4.

Table 4: ANOVA

	Model	Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	973.762	1	243.440	37.637	.000b
	Residual	2056.882	321	6.468		
	Total	3030.644	322			

a. Dependent Variable: Financial performance

b. Predictors: (Constant), Disclosure level

The F-ratio was 37.637 at 1 degree of freedom which is the variable factor. This represented the effect size of the regression model and the model was significant at 95% confidence level (p=0.000) which indicates that financial performance can be predicted from disclosure level. Regression coefficient analysis was done so as to find-out beta that was used to show the extent to which the independent variable affects the dependent variable. Findings were presented in Table 5.

Table 5: Regression Coefficients

		Unstandardized Coefficients		Standardized Coefficients	F	Sig.
		B	Std. Error	Beta		
1	(Constant)	.696	1.317		.529	.597
	Disclosure level	.216	.042	.259	5.073	.000

a. Dependent Variable: Financial Performance

Disclosure level had a positive and significant effect on financial performance of (β= -.216, $p < 0.05$). This implies that an increase in disclosure level by one unit increases financial performance by .216 units when share-based payments, fair value measurement and accounting estimates are kept constant. Findings led to rejection of the null hypothesis that there is no significant effect of disclosure level on financial performance of listed state corporations in Kenya. Findings are similar to that of Bushee et al., (2017) that disclosure level has a significant effect on financial performance.

5.0 Conclusions & Recommendations

The study concluded that disclosure level financial affects the financial performance of listed state corporations in Kenya. Making sufficient disclosure in financial statements and reports affects financial performance. Securing at least minimum level of disclosure in accordance with both internal and external audit reports as well as making disclosure of information concerning the significance of financial instruments to the entity affects financial performance of state corporations. Making disclosures on the nature and extent of risks emanating from financial instruments that are used by state corporations affects financial performance. Making specific disclosures on transferrable financial assets and categorization of financial instruments in classes that are similar in line with the information presented affects financial performance of state corporations. The study recommended that state corporations should continue to make sufficient disclosure in financial statements and reports. State corporation should secure at least minimum level of disclosure in accordance with both internal and external audit reports as well as making disclosure of information concerning the significance of financial instruments to the entity. State corporations should continue to make disclosures on the nature and extent of risks emanating from financial instruments that are used by them. State corporations should continue to make specific disclosures on transferrable financial assets and categorization of financial instruments in classes that are similar in line with the information presented.

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