Effect of Financial Transparency on Financial Performance of Companies Listed in East Africa Securities Exchanges

Boniface Muriithi Wanjau Willy Mwangi Muturi Patrick Ngumi
Department of Accounting, Finance and Economics, School of Business, Jomo Kenyatta University of Agriculture and Technology

Abstract
Financial performance is normally viewed as how best managers have been able to utilize the resources available to the firm to enhance value. The main goal of shareholders in any company is to maximize their wealth which is enabling when a firm is performing well from time to time. The current sought to examine the effect of financial transparency on financial performance of companies listed in East Africa. Specifically, the study sought to find out the effect of financial policy, investment policy and liquidity disclosures on financial performance. Correlation research design and purposive sampling was used to select 73 which were listed from 2006 to 2015. Descriptive, correlation and regression analysis were used to analyse secondary data. Results of the study revealed positive and significant relationship between financial policy, investment policy, financial liquidity and financial performance.
Keywords: Financial Transparency, Financial Policy, Investment Policy, Financial Liquidity, Financial Performance.

Introduction
Financial transparency entails full disclosure of the financial information to reduce information asymmetry between the companies. The tenet of any corporate governance system is based on the goal of good financial reporting which compliance with the complex accounting standards in conjunction with other regulatory requirements around the world (Fung, 2014). Financial reports full and prompt disclosure help shareholders goal of maximization of wealth to be pursued by managers since any unlawful pursuit is properly scrutinized to limit the top managers' discretion of following their own interest. With more financial transparency, investors are able to invest wisely since they will be well informed as to the right choice of capital which as result reduces cost of financing through the decreased liquidity premium.

Financial performance is normally viewed as how best managers have been able to utilize the resources available to the firm to enhance value. The main goal of shareholders in any company is to maximize their wealth which is enabling when a firm is performing well from time to time. Financial performance is reflected in the securities of company that is trading shares and debts. Though an increase in the value of securities is not always as result of improved performance but studies have shown a positive relationship between the financial performance and securities (Fung 2014; Jahanshad et.al, 2014). Good reputation which is enhanced in one way by the consistency of the company's performance explains the change in the market value of securities.

There exist several ways of measuring performance both in financial and non-financial measures. To get the complete picture of how firms are performing for a certain duration the two measure are necessary however financial measures according to (Santos & Brito, 2012) are sufficient and are as well influenced by the non-financial measures. According to Damodaran (2008) the three important decisions that a firm has to make are on investment, financing and dividend which explains all about firm performance. Managers of a firm ought not to compromise any of these decisions since performance is in these fronts. Investment in assets should offer return; a good principle on financing should balance the debt and equity finances and in firm ought to return some returns made to the shareholders as dividends.

Pagach and Warr (2008) posits that firm performance can be assessed by financial and operation efficiency in using resources. Tobin's q measure of financial performance explain different corporate phenomena: over a given period of time, it tells a change made investment and diversification decisions; assess the management equity ownership and value on the firm; also serves to explain the different policies such as financing, compensation and dividend policies. Benchmarking as form of performance checks and balances helps compare companies' performance with others in the same industry. Market share as an indicator for benchmarking will ensure company achieve greater scale in the operations and increase profitability of the firm (Santos & Brito, 2012).

The study was guided by the following objectives:

i. To find the effect of financial policy on financial performance of companies listed in East Africa securities exchanges.
ii. To examine the effect of investment policy on financial performance of companies listed in East Africa securities Exchanges.
iii. To establish the effect of financial liquidity on financial performance of companies listed in East Africa

securities exchanges.

Literature Review

An examination of a Nigerian study to investigate the link between financial policy and corporate performance of companies listed in Nigeria was carried out in Salawu, Asaolu and Yinusa (2012). Secondary panel data was retrieved from annual financial statements of 70 companies listed from 1990 to 2006. Pooled effects, fixed effects and generalized methods moments were applied to analyse the data. Results of the study revealed positive and significant relationship between financial policies adopted on financial leverage, tangibility, corporate tax rate, dividend policy, stock market development and financial performance.

Kipkorir, Namiinda and Njeje (2013) investigated the impact of investment decisions on financial performance of savings and credit societies in Baringo County. The study adopted descriptive research design, stratified sampling technique to select 177 respondents. Primary data was collected through use of structured questionnaires. Data was analysed using both descriptive and regression analysis. Results of the study revealed that 10% of financial performance was influenced by investment decisions. It would have been appropriate to adopt secondary data rather than use primary data.

Nyabuti and Alala (2013) investigated the relationship between working capital policy and financial performance of listed firms in Kenya. The study adopted descriptive research design. Purposive sampling was used to select five companies which were listed from 2008 to 2012. Secondary data was retrieved from annual financial statements. Descriptive, correlation and regression analysis were used to analyses the data. Results of the study revealed positive and significant relationship between investment policy and financial performance.

Musyoka (2017) investigated the effect of voluntary disclosure on financial performance of firms listed in Nairobi securities exchange. Voluntary disclosure was categorized into financial, investment, growth and development and research and development disclosure. Correlational research design was adopted and purposive sampling was used to select 43 companies which were actively trading from 2006 to 2015. Regression analysis was used to analyse the data. Results of the study revealed positive and significant relationship between financial, investment, sales growth, research and development and financial performance.

Data and Methodology

The study employed secondary panel data for the period 2006 to 2015. Purposive sampling was applied to select 73 companies which were listed in securities exchanges hailing from East Africa, they were Kenya, Uganda, Tanzania and Rwanda. Data was sourced from annual financial statement and voluntary disclosure check index was used to estimate levels of voluntary disclosure. Regression and correlation analysis were used to analyse the data.

The regression model in the study was as follows:

$Y_{it} = \alpha + \beta_1 X_{1it} + \beta_2 X_{2\,it} + \beta_3 X_{3\,it} + \acute{\varepsilon}$.

Where; Y_{it} represent financial performance

X_{1it} represent Financial Policy Disclosure for firm i in period t

X_{2it} represent Investment Policy Disclosure for firm i in period t

X_{3it} represent Financial Liquidity Disclosure for firm i in period t

$\acute{\varepsilon}$ represent error term.

Results and Discussion

As shown in Table 1 the average return on asset was 9.9% with a minimum loss of 70% and maximum profit of 58%. Further the distribution was skewed to the right since the skewness coefficient was 0.196; the data was not normally distributed because the p value for Jarque Berra was less than 0.05. Although, there were fluctuations on financial performance as accounted for by standard deviation of 0.127, the ventures were generally profitable and they gave returns to investors. The average financial policy voluntary disclosure was 69%, with a maximum of 100% and minimum of 2%. Regarding, investment policy disclosure the average was 58% with a maximum of 89% and some firms did not disclose their investment policy in some periods. The average financial liquidity disclosure was 62% with some firms not disclosing their financial liquidity in some periods. Failure of firms to disclose their investment and liquidity policies may hamper the levels of investors' confidence.

Table 1: Descriptive Statistics

	Financial Performance	Financial Policy	Investment Policy	Financial Liquidity
Mean	0.099	0.69	0.58	0.62
Maximum	0.58	1	0.89	0.96
Minimum	-0.7	0.02	0.00	0.00
Std. Dev.	0.127	0.291	0.284	0.21
Skewness	0.196	-12.44	-8.70	-9.23
Kurtosis	8.07	8.29	10.78	9.72
Jarque-Bera	785.26	697.33	754.70	691.65
Probability	0.00	0.00	0.00	0.00

Correlation Analysis

Pair wise correlation was carried to identify the strength of the relationship between variables. There was a positive and significant relationship between financial policy disclosure and financial performance among companies listed in East Africa securities exchange (rho = 0.512, p value <0.05). Secondly, there was a positive and significant relationship between investment policy disclosure and financial performance of companies listed in East Africa securities exchange (rho = 0.429, p value <0.05). Thirdly, there was a positive and significant relationship between financial liquidity disclosure and financial performance of companies listed in East Africa (rho = 0.612, p value <0.05). A close of interrelationship between independent variables revealed that none of them was highly correlated with each other since there correlation coefficients were less than 0.7.

Table 2: Correlation Analysis

	Financial Performance	Financial Policy	Investment Policy	Financial Liquidity
Financial performance	1			
Financial Policy	.512**	1		
Investment Policy	.429**	.123**	1	
Financial Liquidity	.612**	.207**	.171**	1

** Correlation is significant at the 0.01 level (2-tailed).

Regression Analysis

Fixed effects regression was fitted to show the nexus between financial transparency and financial performance of companies listed in East Africa securities exchanges. Results of the study revealed that 60 % of the variations in financial performance can be explained by financial policy, investment policy and financial liquidity while the remaining percentage can be explained by other factors which were excluded in the model. The relationship was significant and at least one of the slope coefficients was non zero since F statistics was 24.36 and p value of 0.00. There was a positive and significant relationship between financial policy disclosure and financial performance (β = 0.234, p value <0.05). This implies that a unit change in financial policy disclosure increase financial performance by 0.234 units while holding investment policy disclosure and financial liquidity disclosure constant.

Secondly, there was a positive and significant relationship between investment policy disclosure and financial performance of listed companies in East Africa (β = 0.216, p value <0.05). This implies that a unit change in investment policy disclosure increases financial performance by 0.216 units while holding financial policy disclosure and financial liquidity disclosure constant.

Thirdly, there was a positive and significant relationship between financial liquidity and financial performance of companies listed in East Africa (β = 0.228, p value <0.05). This implies that a unit change in financial liquidity increases financial performance by 0.228 units while holding financial policy disclosure and investment policy disclosure constant.

Table 3: Financial Transparency and Financial Performance

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.08	0.02	4.012	0.000
Financial Policy	0.234	0.066	3.563	0.000
Investment Policy	0.216	0.076	2.845	0.000
Financial Liquidity	0.228	0.078	2.912	0.000
R-squared	0.60	Mean dependent variable		0.099
Adjusted R-squared	0.594	S.D. dependent variable		0.127
S.E. of regression	0.092	Akaike info criterion		-2.025
Sum squared residual	7.425	Schwarz criterion		-1.039
Log likelihood	1027.76	Hannan-Quinn criterion.		-1.005
F-statistic	24.36	Durbin-Watson stat		1.684
Prob (F-statistic)	0.00			

Discussion and Conclusion

Positive and significant relationship between financial policy disclosure and financial performance was in support of signaling hypothesis and agency theory since disclosing financial policy adopted by listed companies can be purported to show adherence to shareholders wealth maximization policy. Moreover, those companies which can willingly share financial performance history in clear format elaborated quantitatively and qualitatively can be purported to signal superior performance. All listed companies have adopted the culture of disclosing information and this will ultimately boost investor's confidence.

Since there was positive and significant relationship between investment policy disclosure and financial performance of listed companies, this was in support of agency theory and would ultimately maximize shareholders wealth. Indeed, this approach has end result of minimizing monitoring and agency costs. Through this savings financial performance of listed companies would increase.

Thirdly, there was positive and significant relationship between financial liquidity and financial performance of listed companies in East Africa. This was in support of signaling hypothesis as a liquid company can be perceived to signal superior performance in future.

Although, financial decisions hold the backbone of organization performance there is need to evaluate the effect of other types of voluntary disclosure for example the effect of risk transparency, governance transparency, social transparency, and sales growth transparency and research and development disclosure amongst others since there contribution effect on organization performance cannot be overlooked. Secondly, there is need to adopt a long period of time rather than collecting data for a ten year period. Thirdly, there is need to consider specific industry companies or country so as to evaluate unique industry or country characteristics effects on transparency against financial performance. Finally, unbalanced panel data ought to be adopted since there are firms which could be delisted, suspended or listed within the period under consideration.

References

Damodaran, A., (2008). Risk Management: A corporate governance manual, Accessed online on http://people.stern.nyu.edu on 23/5/2016.

Fung, B. (2014). The Demand and Need for Transparency and Disclosure in Corporate Governance. *Universal Journal of Management,* 2(2), 72-80.

Jahanshad, A., Heidarpoor, F., & Valizadeh, Y. (2014). Relationship between Financial Information Transparency and Financial Performance of Listed Companies in Tehran Stock Exchange. *Research Journal of Recent Sciences*, 3(3), 27-32.

Kipkorir, R. D., Namiinda, B. M., & Njeje, D., (2013). Influence of Investment Decisions on the Financial Performance of SACCOS: A Survey of Registered SACCOS in Baringo County, *International Journal of Science and Research*, 5(4), 904-914.

Musyoka, M. M. (2017). *Effect of Voluntary Disclosure on Financial Performance of Firms Listed at Nairobi Securities Exchange,* Master of Commerce Thesis, Unpublished (KCA University).

Nyabuti, W. M. & Alala, B. O., (2014). The Relationship between Working Capital Management Policy and Financial Performance of Companies Quoted at Nairobi Securities Exchange, Kenya. *International Journal of Economics, Finance and Management Sciences*, 2 (3), 212-219.

Pagach, D. & Warr, R. (2010). The Effects of Enterprise Risk Management on Firm Performance”. Social sciences Research Network. Retrieved from http://papers.ssrn.com/ on 25/2/2017.

Salawu, R. O., Asaolu, T. O., & Yinusa, D. O., (2012). Financial Policy and Corporate Performance: An Empirical Analysis of Nigerian Listed Companies, *International Journal of Economics and Finance*, 4(4), 175-181.

Santos, J. B., & Brito, L. A. (2012). Toward a Subjective Measurement Model for Firm Performance. *Brazilian Administration Review*, 9 (5), 123-132.