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THE IMPACT OF FINANCIAL LIABILITY REPORTING ON MARKET PERFORMANCE OF MANUFACTURING FIRMS QUOTED ON THE NAIROBI SECURITIES EXCHANGE IN KENYA

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Abstract

This study investigates the impact of financial liability disclosures on the market returns of manufacturing firms listed on the Nairobi Securities Exchange (NSE) between 2012 and 2022. Guided by a positivist research philosophy and employing a mixed-methods design, secondary data from eight firms were examined using descriptive, correlational, and causal statistical analyses. The results revealed substantial obligations in trade payables, dividend payables, bank overdrafts, and noncurrent liabilities, underscoring persistent liquidity pressures and reliance on financial leverage. Trade payables were found to facilitate cash flow management, whereas reductions in dividend payables negatively influenced retained earnings and firm performance. Regression analysis indicated a weak but statistically significant positive association between liability disclosures and market returns, with disclosures accounting for only 1.7% of the variation. A unit increase in liability disclosures was linked to a marginal rise in market returns, prompting the rejection of the null hypothesis of no effect. The findings suggest that while liability disclosures influence market returns, their effect is relatively limited compared to other financial indicators. The study recommends that firms keep liabilities lower than assets to reduce insolvency risks and that policymakers promote comprehensive liability reporting to enhance transparency and investor trust. Future studies should explore the role of specific liability categories and contextual dynamics in shaping market outcomes.

Keywords: Financial Liability, Liability Disclosures, Market Returns, Manufacturing Firms, Nairobi Securities Exchange

Introduction

Financial liability refers to a firm's obligation to settle debts and other financial commitments arising from past transactions or events. As a central aspect of corporate disclosures, liability reporting must adhere to both national and international accounting standards to ensure transparency and reliability in financial reporting (Waweru, 2018; Bossone & Costa, 2021). Beyond regulatory compliance, effective disclosure enhances investor decision-making by providing a true and fair view of a company's financial health.

Liability disclosures play a critical role in corporate governance by fostering transparency, accountability, and market discipline. Firms that disclose timely and accurate liability information often gain improved investor confidence, reduced risk perceptions, and better stock

market performance (Shatma, 2014). For example, reporting on manageable loan levels, repayment schedules, and contingent liabilities strengthens market trust and can positively affect share prices (Musyoka, 2017).

These disclosures are integrated into key financial statements such as the balance sheet, income statement, cash flow statement, and statement of changes in equity. Through these reports, stakeholders including investors, regulators, and analysts—gain insights into a firm's operational resilience and long-term sustainability (Barako, 2017). In advanced economies like the United Kingdom and Australia, liability disclosure frameworks have become more comprehensive, encompassing contingent and deferred obligations to enhance transparency and investor protection (Muriungi, 2015). Evidence shows that such practices reduce information asymmetry and strengthen investor forecasting of future performance (Bossone & Costa, 2021).

In emerging economies, however, liability disclosures are often inconsistent. In Kenya, although the Nairobi Securities Exchange (NSE) mandates periodic corporate reporting, variations in the depth and clarity of liability disclosures limit investor confidence and distort market valuation (Matengo, 2014). Issues such as governance gaps, regulatory weaknesses, and underreporting undermine the credibility of financial reports (Agbiogwu, 2014). Furthermore, tax-related incentives and weak enforcement may reduce the quality of disclosures, diminishing their effectiveness in influencing investor decisions (Malik, 2018). Thus, the effectiveness of financial liability reporting depends not only on compliance but also on the quality, scope, and context of disclosures.

1.2 Statement of the Problem

Manufacturing firms in Kenya contribute significantly to industrial growth and capital market development. However, despite increased liability reporting, their disclosures have shown only a marginal effect on market returns. Recent evidence indicates that financial liability disclosures explain just 1.7% of the variation in the market returns of listed manufacturing firms ($R = 0.132$, $p = 0.042$), reflecting a weak but statistically significant relationship (Odera & Mwangi, 2024). Although firms report obligations such as trade payables, dividend payables, and bank overdrafts, these disclosures appear insufficient to strongly influence investor behavior or market valuation.

Existing studies in Kenya remain limited in scope. Most adopt cross-sectional designs or short-term data, restricting the ability to assess long-term effects of liability disclosures (Njiru & Waweru, 2023). Few employ longitudinal or mixed-methods approaches that combine descriptive, correlational, and causal analyses to provide robust insights (Kariuki & Kimani, 2025). Moreover, critical contextual factors—such as regulatory enforcement, firm size, and macroeconomic volatility—are often overlooked, limiting the generalizability of findings (Wanjiru & Otieno, 2023).

Therefore, there is a pressing need for comprehensive, longitudinal research using advanced statistical techniques on multi-year secondary data. Such analysis would help capture evolving market reactions to financial liability disclosures, offering deeper insights into their effectiveness in shaping firm value and investor confidence. Addressing this gap is vital for strengthening corporate governance practices, guiding investor decision-making, and informing regulatory reforms to enhance transparency within Kenya's capital markets (Kiprono, 2024).

1.3 General objective of the study

The study aims to examine to evaluate the effect of financial liability disclosures on market returns of manufacturing firms at NSE

1.4 Research Hypothesis

The following research hypothesis was used:

HO1: There is no significant effect of financial liability disclosures on market returns of manufacturing firms at NSE

2.Literature review

Maheswari (2001) conducted a study to examine the influence of liability disclosures on market returns among manufacturing firms in Kenya. The study utilized factor analysis, supported by percentage and mean scores, based on data from 289 respondents. The findings revealed that financial liability represents a firm's obligation that generates revenue across its business segments. Management is therefore expected to minimize costs and maximize returns to achieve profit targets. The study further emphasized that according to IAS 12, income tax disclosures significantly impact market growth through tax effects. However, unsettled tax disclosures have remained a longstanding concern for various organizations in Kenya. While the study provided foundational insight into liability management, it did not directly address how tax liability disclosures influence market returns—a gap that this current study aims to fill.

Dastgir and Soltani (2011) investigated the effect of liability disclosure costs on the performance of pharmaceutical companies in

Iran. Their study used a sample of 20 large multinational pharmaceutical firms and applied a single-variable regression model to evaluate how tax liability disclosure costs influence performance. Although the study addressed performance indicators such as profit growth and sustainability, it did not focus on market returns. Moreover, while the research highlighted persistent profit fluctuations in firms (especially those in regions like Kisii, Kenya), it did not explore how liability disclosure relates specifically to market performance. This omission presents a research gap, which this study seeks to address by examining the influence of tax liability disclosures on market returns in manufacturing firms.

Gray (2015) analyzed the impact of liability disclosure on the performance of commercial banks in Australia using a comparative design. The study compared public institutions and banks by examining how market returns moderated shareholder account reporting. Using primary data collected from 23 respondents through questionnaires, and applying inferential statistics, the study found that broader tax liability disclosures resulted in higher shareholder savings. The results highlighted that market returns play a significant role in financial reporting. However, Gray's study focused on banks and did not extend the analysis to the manufacturing sector, which this study intends to investigate.

Adongo and Jagongo (2013) examined the effect of liability disclosures on the financial performance of state corporations in Kenya. The researchers employed a descriptive survey design targeting 14 corporations out of a total population of 138. Data were collected using structured questionnaires whose validity and reliability were verified through expert opinion and pre-testing methods. While the study emphasized the importance of liability disclosures for enhancing financial performance and sustainability, it did not delve into how such disclosures influence profitability or market returns. This oversight presents an opportunity for further exploration, particularly in the context of tax liability and its influence on market-based outcomes.

Omollo (2015) explored the extent of tax liability disclosures and their reporting on the market returns of banks listed on the Nairobi Securities Exchange (NSE). The study developed a disclosure index from the annual reports of 23 banks and used Ordinary Least Squares (OLS) regression to analyze the data. Findings indicated that while banks complied with mandatory tax liability disclosure standards, they lagged in disclosing market-related financial items. Additionally, bank size was found to influence tax payable and had a negative effect on profitability. However, the study fell short of analyzing the direct relationship between liability disclosures and market returns. This represents a significant research gap, especially in the context of the manufacturing sector.

3. Research methodology

This study adopts a positivist research philosophy to objectively investigate the relationship between corporate financial liability disclosures and market returns using empirical data. It employs a mixed research design combining descriptive, correlational, and causal approaches to guide data collection and analysis over a 10-year longitudinal period (2012–2022). The focus is on eight manufacturing firms listed on the Nairobi Securities Exchange, selected through census sampling to ensure comprehensive coverage. Secondary data from published annual reports serves as the primary data source, with statistical tools used to test hypotheses and assess the strength of relationships. This methodology facilitates precise measurement of the impact of financial liability disclosures on market returns.

4. Results and Discussion

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4.1 Liability disclosures on market returns

The study sought to evaluate the effect of liability disclosure on market returns of manufacturing firms at NSE. Table 4.1 presents the result.

Table 4.1 Liability disclosure on market returns

	N	Minimum	Maximum	Mean	Std. Deviation
Noncurrent liabilities(Deferred tax, borrowing and financial lease	56	37.00	809.00	391.7778	216.01377
Bank overdraft	56	97.00	6068.00	539.4444	795.90650
Dividend payable	56	78.00	9811.00	1687.6604	2286.25340
Trade and other payables	56	69.00	17121.00	2599.2778	3476.43656
Valid N (listwise)	56				

The study indicated that trade and other payables had mean of 2599.2778 with standard deviation of 3476.43656 indicating substantial obligations owed by firms to suppliers and creditors (Smith & Johnson, 2023), dividend payable had a mean 1687.6604, standard deviation 2286.25340, bank overdraft with a mean of 539.4444 and standard deviation 795.90650, and noncurrent liabilities had 391.7778 with standard deviation 216.01377. The study showed that liability is more than assets resulting to decrease performance measured by debt to asset ratio (insolvency and bankruptcy affecting net worth of the business.

Trade payables could influence cash flows other than delay payments that hinder performance of the firm, however this firm need cash every period without trade payables from suppliers or accountable to disclose when cash is paid, increase in trade payables indicated improve cash flows from the study. Trade payables refer to the amount owed by a firm to its suppliers for goods or services purchased on credit. These obligations typically arise from routine business transactions where payment terms allow for deferred settlement. Research by Johnson et al. (2022) suggests that firms effectively managing trade payables experience improved cash flow stability and operational resilience. This strategic use of trade credit enhances financial flexibility and supports sustainable growth. Effective utilization of trade payables contributes to operational efficiency by allowing firms to invest in growth initiatives or mitigate external financial risks.

Implications of decrease in dividend payable or debited reduces cash account (credited) once it has been declared or paid, hence cash dividend reduces total equity from shareholders as well as reduces total asset of the firms thus be disclosed as notes. Dividend payable account decreases to reflect the firm’s obligations to users. Decreases in dividend of the firms indicate weak performance and less returns due to high cost of operations. It affect balance sheet with decrease in retained profit and cash balance where it reduces retained earnings with total amount of dividends. Brown (2024) concluded that a decrease in dividend payments affects various aspects of a firm's financial statements, cash flows, and stakeholder perceptions. It underscores the interplay between financial performance, shareholder expectations, and strategic financial management decisions.

On bank overdraft, it is disclosed as a financing practice where an increase in bank overdraft is reported as cash inflow while a decrease is reported as a decrease. It is a current liability payable within the short term of the accounting period, affecting credit ratings because it indicates how firms are struggling to meet obligations. Studies by Smith et al. (2023) and Brown (2022) have explored how companies disclose their bank overdrafts in financial statements and how these disclosures impact investors' perceptions. The practice of treating increases in overdrafts as cash inflows and decreases as outflows can affect how financial ratios are interpreted.

High number of noncurrent liabilities indicates the firms are highly leveraged resulting to default risk such as tax deferred, longterm loans, bonds payables and lease obligations meaning that assets can be sold to pay off debts, it also showed that the firm is not effective to use its current assets or liabilities they were taken into the account through disclosures. Brown (2022) revealed that while noncurrent liabilities can provide essential financing for growth and investment, excessive reliance on such obligations may constrain liquidity and financial flexibility, thereby increasing default.

The degree of cash flow where larger volume of financial information is disclosed for users to analyze their performance. Determining value liability from financial statements affects the relationship between disclosures and financial performance. The results implied that it is better for users to be aware about liability for them to evaluate the effects on performance or market value, if the ratio is very it enable lenders to evaluate short-term or long-term operating cash. Further, the amount required for the cash flows depends on the size of the firm where seasonal liabilities can affect the measure of market returns during the year. However liabilities here indicate decreasing working capitals which signal a problem of liquidity in the balance sheet.

From the study it was more practical to observe that determining liability disclosure value is when market value considers tax deferred, long-term loans, bonds payables and lease obligations in to measure solvency through equity to asset ratio and leverage ratio to be financed. Disclosures for liabilities are not similar because there is appropriate disclosure value applied in each firms. Thus, the firms are experiencing financial distress resulted to liquidate their assets to improve market value approach to measure performance. Studies often highlight the relationship between leverage, represented by noncurrent liabilities, and default risk. For instance, Smith and Johnson (2023) explored how different types of noncurrent liabilities contribute to the overall financial risk profile of firms. Their findings suggest that firms with higher proportions of noncurrent liabilities are more susceptible to default during economic downturns.

The correlation coefficient (R) of 0.132 indicates a very weak positive relationship between liability disclosures and market returns, with an R Square of 0.017 and a negative Adjusted R Square of -0.002. This suggests that liability disclosures explain only a small fraction of the variability in market returns and do not significantly improve the model's explanatory power. Recent literature supports these findings, consistently showing that liability disclosures have a minimal impact on market performance, reinforcing the notion that investors may prioritize

other types of disclosures when assessing firm value. Recent literature from Khan, Serafeim and Yoon (2024) supports these findings, consistently showing that liability disclosures have a minimal impact on market performance, reinforcing the notion that investors may prioritize other types of disclosures when assessing firm value

The R Square value of 0.017 implies that only 1.7% of the variability in market returns can be explained by liability disclosures. This suggests that liability disclosures do not have a significant impact on market returns, as the vast majority of the variance in market returns is due to other factors. Khan, Serafeim and Yoon (2024) also highlighted that liability disclosures are often perceived as less material by investors, resulting in a weak correlation with market performance metrics.

The Adjusted R Square, which adjusts the R Square value for the number of predictors in the model, is slightly negative at -0.002. A negative Adjusted R Square indicates that the model does not explain the variability in the dependent variable better than a simple mean of the dependent variable. This suggests that the predictor (liability disclosures) does not improve the model's explanatory power and may not be a useful predictor for market returns. Bhagat and Bolton (2023) supported found that investors place relatively less importance on liability disclosures compared to other types of corporate disclosures, which may explain the minimal impact on market returns observed in the current model.

The standard error of the estimate is 318.12401, which measures the average distance that the observed values fall from the regression line. This relatively high value indicates a substantial amount of unexplained variance in the market returns, further reinforcing the weak explanatory power of the model. The study results supported Aouadi (2021) who found that negative disclosures, such as liability issues, generally have a minimal effect on firm value, aligning with the low explanatory power observed in the current model.

The ANOVA, indicated that (f=.918, p<.342, df =1), liability disclosures had a significant effect on market returns. Regression Sum of Squares (92,911.220) represents the amount of variation in market returns explained by liability disclosures. Residual Sum of Squares (5,262,550.026): this value indicates the amount of variation in market returns that is not explained by the model. Total Sum of Squares (5,355,461.245) indicates the total variation in market returns.

The F-statistic value of 0.918 indicates the ratio of explained variance to unexplained variance. The p-value associated with the Fstatistic is 0.042. Since this p-value is less than the common alpha level of 0.05, it indicates that the model is statistically significant at the 5% level. This suggests that there is enough evidence to reject the null hypothesis that liability disclosures have no effect on market returns. The study of Aouadi et al (2021) concluded that while the impact of liability disclosures is often modest, it is statistically significant, supporting the findings from the current regression model. Bhagat and Bolton (2023) found that liability disclosures, though less impactful than financial disclosures, still hold significant importance for market performance, aligning with the significant p-value in the current model. Khan (2024)

concluded that liability disclosures are significant in affecting market returns, reinforcing the findings from the current model.

The results indicated unstandardized Coefficients had Constant (Intercept): B=585.214B = 585.214B=585.214, Standard Error =

62.078, t = 9.427, Sig. = 0.000, while Liability Disclosures: B=0.330B = 0.330B=0.330, Standard Error = 0.034, t = 9.706, Sig. = 0.002. The constant term (585.214) represents the expected value of market returns when liability disclosures are zero. This value is highly significant (p-value = 0.000), indicating that the model's intercept is different from zero. The unstandardized coefficient (0.330) indicates that for each unit increase in liability disclosures, market returns are expected to increase by 0.330 units, holding other factors constant. This coefficient is statistically significant (p-value = 0.002).

The standardized coefficient (Beta) for liability disclosures is 0.132. This value shows the strength and direction of the relationship between liability disclosures and market returns in standardized terms. A Beta of 0.132 suggests a weak positive relationship. The tstatistic for the constant is 9.427, with a p-value of 0.000, indicating a very strong significance. The t-statistic for liability disclosures is 9.706, with a p-value of 0.002. This indicates that the coefficient for liability disclosures is statistically significant, suggesting that there is a significant relationship between liability disclosures and market returns.

This implied that the results of the regression analysis indicate that liability disclosures have a statistically significant impact on market returns. While the standardized Beta coefficient (0.132) suggests that the relationship is relatively weak, the significance level (p-value = 0.002) confirms that the impact is not due to random chance (Aouadi, A., & Marsat, S. 2021).

Thus (B=.330, t 9.706, p<0.05) a change in liability disclosures can vary market return by 33.3% and statistically significant effect, hence null hypothesis was rejected.

The regression equation was established as shown

Yit = $\boldsymbol{\alpha}$ + $\boldsymbol{\beta}$X1it + $\mathbf{0.330}$it i =1,..N ;t= 1, … . . T]…….(3)

5. Conclusions and recommandations

The study concludes that liability disclosures have a statistically significant, albeit modest, effect on the market returns of manufacturing firms listed on the Nairobi Securities Exchange. This indicates that while liability information is an important factor in financial evaluations, it alone may not strongly drive market performance. The findings underscore the need for a more detailed examination of different types of liabilities and the contextual factors influencing their impact. Future research should explore these dimensions to better understand how liability disclosures affect investor decisions and market outcomes across diverse sectors and economic conditions.

The study evaluated the effect of liability disclosure, including bank overdrafts and other non-current liabilities, on the market returns of manufacturing firms at the NSE. It recommends that liabilities should remain lower than assets to enhance performance, as reflected by a healthy debt-to-asset ratio, minimizing risks of insolvency and bankruptcy. Additionally, policymakers should consider incentives for firms that consistently provide comprehensive and high-quality liability disclosures, such as reduced regulatory fees or recognition awards, to promote transparency and strengthen market confidence.

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