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The Quality of Financial Information Disclosures and its Contribution to Financial Stability of Commercial Banks in Kenya

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Abstract

The purpose of this study was to explore the impact of the quality of financial information disclosures on the financial stability of commercial banks in Kenya. This study employed an unevenly balanced panel dataset, including 43 commercial banks in Kenya over the period from 2000 to 2021, which resulted in 789 observations based on bank years. The approach focused on disclosures related to stability, specifically analyzing risk, liquidity, and profitability. The study employed self-created measures for disclosures, assigning scores from 1 to 5 on an ordinal scale for each disclosed item. The awarding of scores was based on the assessment of usefulness of information provided by the financial information disclosed. The study findings established that risk related disclosures and liquidity related disclosures are positively related with financial stability while profitability related disclosures are negatively related with financial stability. The study findings underscore that high quality of financial information disclosures relating to risk and liquidity provide information to the management of commercial banks who finds value on the evaluation of financial stability for their banks. Research results provide important implications for regulators, bank managers and policy makers on the importance of financial information disclosures especially those relating to credit risk as per the requirement of IFRS 7 and IFRS 9.

Keywords: *Disclosure index, financial stability, financial information disclosures and IFRSs.*

1.0 Introduction

International Financial Reporting Standards stress the crucial role of comprehensive disclosures, as they empower users of financial statements to grasp and compare the content of financial information. This capability facilitates informed economic decision-making (IFRS, 2021). Financial information disclosure is the disclosure of the information, both quantitative and qualitative on timely basis about a company that can influence economic decisions that the annual report purports to represent (Egan, Ali, & Gregor, 2017). All parties are entitled to have equal access of financial information, which increases transparency and accountability of financial institutions and this enables them to evaluate the bank's financial stability and to react before the losses multiply (Elbadry, 2018). The major question is whether full disclosures of information can lead to transparency and accountability, which this study aims at answering.

Financial information disclosure mitigate the banks runs which is one of the major reasons that cause financial instability in commercial banks (Sarwar, Muhammad, & Azhar, 2021). In order to improve the asset quality, the financial information about the banks' clients should be screened on their ability to meet the obligation of principal and interest to reduce the failure of commercial banks (Mamatzakis, Zhang, & Hu, 2017). This study focuses on banking sector since banks act as financial intermediaries, performing important functions of allocating resources and deals with complex financial instruments which are greatly affected by deficiencies of financial information from its clients (Du, Song, & Wu, 2016). More importantly, after the global financial crises of the year 2007/2008, there was an increased need for having financial information disclosures in banking sector for accounting transparency and mitigating banks' failures (Boateng, 2016; Haddad & Alali, 2021; Bischof, Laux, & Leuz, 2021).

The banks may fail to provide adequate financial disclosures if the management judge it to be negatively affecting its financial performance (Du, Song, & Wu, 2016). Such withholding of information can only be for a short period of time and when such negative information accumulates the banks may disclose the information suddenly which can adversely affect the bank causing contagion among the banks making financial sector unstable (Haddad & Alali, 2021; Bischof, Laux, & Leuz, 2021). According to, too big to fail theory the government is more likely to bail out the large banks than small banks, and therefore financial information disclosures may differ among these banks (Polizzi & Scannella, 2020). To address the issue of large and small banks, the study will use the bank size as a control variable.

Disclosing financial information incurs costs, both in terms of producing and disseminating the information, and indirectly, when competitors leverage this information about the company to their advantage (Du, Song, & Wu, 2016). Secondly, information disclosure can be challenging on the nature and extent to which to disclose so that it can contribute to financial stability of commercial banks (Bischof, Laux, & Leuz, 2021). This study aims to underscore the significance of comprehensive disclosures and how financial information can be utilized by bank management and their clients to make informed economic decisions, contributing to the financial sector's stability. Additionally, the study intends to bridge the existing knowledge gap by examining the role of financial information disclosure in enhancing the financial stability of commercial banks in Kenya. It also evaluates the influence of bank-specific factors and macroeconomic variables on bolstering this stability during the period from 2000 to 2021.

1.1 Research Objective

The objective of this study is to establish the contribution of quality of financial information on the financial stability of commercial banks in Kenya.

1.2 Research Questions

i. How does financial information disclosure contribute to financial stability of commercial banks in Kenya?
ii. What is the effect of financial information disclosure on the financial stability of commercial banks in Kenya?
iii. Is there significant value created by complying to banks' disclosure requirement in enhancing financial stability in commercial banks in Kenya?
iv. How does bank specifics and macro-economic variables enhance financial stability of commercial banks in Kenya?

2.1 The Agency Theory

Agency theory, introduced by Michael Jensen and William Meckling in 1976, primarily addresses the agency problem and its solutions (Jensen & Meckling, 1976; Ross, 1977). Agency theory discusses the problems that surface in the firms due to the separation of owners and managers and emphasized that the problem can be solved through proper financial information disclosures (Jensen & Meckling, 1976). Through enhanced information disclosures and implementation of effective governance mechanisms that can control the agents' action in the jointly held corporations, the agency problem can be solved (Ross, 1977). The underlying issue is when the managers wants to satisfy their own interest instead of performing for the owners or themselves (Jensen & Meckling, 1976; Ross, 1977).

The proponents of agency theory, for example Ross (1977), have used the theory to address the agency problem by advocating for full disclosure of information while applying incentives to management (Ross, 1977). Meanwhile, Mitnick (1979) suggests that the agency problem could be solved if the owners have a strong and efficient institutional structure (Mitnick, 1979). Gibbons & Murphy (1992) used the theory by proposing that the incentive pay should be tied to performance and the management cash compensation (Gibbons & Murphy, 1992). Bebchuk et al. 2002 and Core et al. (2006) has used the theory in asserting that full information disclosures should be accompanied by equity-based compensation, by doing this the management will be providing the information even to themselves since they will part of the shareholders (Core, Guay, & Rusticus, 2006; Bebchuk, Fried, & Walker, 2002).

Agency theory can be used in financial asset management by commercial banks in Kenya through The disclosure of financial information can influence managerial attitudes toward risk-taking and hedging (Smith & Stulz, 1985). Use of off balancing financing through debts to take advantage of tax shields which has been major cause of instability due to financial distress can be eliminated through full information disclosures, owners are always aware of what is happening in their firms (Fite & Pfleiderer, 1995). Timely and always providing information that is relevant to the stakeholders can assist reduce the management appetite of taking too much risks and information asymmetries which can contribute to financial stability of the firms (Mayers & Smith, 1987). Better still the management can apply their fiduciary duty through oversight which can offer partial solution to agency problem and stabilize their firms (Hermalin & Weisbach, 2003).

2.2 Empirical Literature Review

The study by Boateng (2016) investigated the influence of information disclosure and corporate governance measures on bank stability in Sub-Saharan Africa. The primary aim of the study was to identify governance measures that could enhance disclosure and contribute to bank stability, providing valuable insights for policymakers. Analyzing data from banks across Sub-Saharan Africa from 2007 to 2012, Boateng's research illuminated the unique challenges faced by the region's banking sector and underscored the importance of implementing effective governance practices and disclosure mechanisms. The findings of the study highlighted the critical role that transparency and governance play in ensuring the stability and development of banks in Sub-Saharan Africa.

Polizzi & Scannella (2020) conducted a study to empirically investigate market risk disclosure practices and their potential improvements within Italian banks. The objective was to examine how large Italian banks disclose market risk information and how these practices could be enhanced to provide better insights into market risk. The study employed a mixed methodological approach, analyzing both qualitative and quantitative aspects of market risk disclosure in banking. Specifically, it focused on key documents required for risk disclosure, including management commentary, the Basel Pillar 3 disclosure report, and notes. The findings revealed that Italian banks do not fully capitalize on the opportunities presented by management commentary and the Pillar 3 disclosure report. Additionally, the study highlighted overlapping information across different financial reports, which undermines the overall clarity and relevance of bank risk reporting.

Mathuva, Kiragu, & Barako (2020) in their study on the determinants of corporate disclosures of anti-money laundering initiatives by Kenyan commercial banks, whose objective was to examine the extent and drivers of anti-money laundering (AML) disclosures in the audited annual reports of regional listed banks in Kenya. The authors used the AML disclosure index that is used to score the extent of AML disclosures by banks. The study used a sample of 15 listed regional banks in Kenya covering the period from 2007 to 2017. Using the sample, the authors performed fixed-effects regressions to identify the significant determinants of AML disclosures. The study found a low level of AML disclosures in the audited annual reports of sampled banks. The authors also found out that the AML disclosures are largely driven by corporate governance (board size and audit committee size) and the ratio of diaspora remittances to GDP (Mathuva, Kiragu, & Barako, 2020).

Bischof, Laux, & Leuz (2021) in their study on accounting for financial stability by evaluating bank disclosure and loss recognition in the financial crisis, whose objective was to examine banks' disclosures and loss recognition in the 2007–2009 financial crisis and identify core issues for the link between accounting and financial stability. The sample of the study contained 2,929 bank-years and 740 distinct banks from 38 countries and used the descriptive statistics through comparison of the volatility of capital ratios. The study found out that going into the financial crisis, banks' disclosures about relevant risk exposures were relatively sparse but such disclosures came later after major concerns about banks' exposures had arisen in the markets. Also, the study found out that the recognition of loan losses was slow and delayed relative to prevailing market expectations. The study concluded that banks' reporting incentives played a key role, which had important implications for bank supervision and the new expected loss model for loan accounting.

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Overall, the study revealed several significant challenges if accounting and financial reporting are to contribute to financial stability (Bischof, Laux, & Leuz, 2021).

Haddad & Alali (2021) in their study on risk disclosure and how it affects the financial performance comparing the Islamic and Conventional banks in the GCC, whose objective was to explore the extent of risk disclosure (RD) among conventional banks (CBs) and Islamic banks (IBs) listed on stock markets in the Gulf cooperation council (GCC) and examine the influence of RD on the banks' financial performance as measured by return on assets (ROA) and return on equity (ROE). The study used the content analysis to examine RD in the annual reports of 16 CBs and 14 IBs in the GCC for a sample of 240 firms-year observations covering the period between 2007 to 2014. The study found out that there are no significant differences between the RD reported in the annual reports of CBs and that of IBs. On average, a CB reported 234 sentences while an IB disclosed 244 sentences of RD in its annual report. Finally, the authors found out that there is a significant association between RD and both models of financial performance (ROA and ROE) for IBs, after controlling other variables. However, RD has a significant association with only ROE for CBs (Haddad & Alali, 2021).

3.0 Research Methodology

This section presents a detailed overview of the model used for the study. The section further provides an indepth examination of the variables used in the study, and the corresponding measurement of these variables. The study employed fixed effects panel data method to investigate the quality of financial information disclosures and its contribution to financial stability of commercial banks in Kenya. The study utilized data that provides information on financial disclosures, and the disclosure index evaluated whether stability has been enhanced as a result of improved quality of disclosed information. The study adopts an ontological position by applying positivism, which is a research philosophy in the science that seeks facts of social phenomena with little regard for the subjective status of an individual (Patton, 2015). The data is collected from commercial banks' aannual reports for a period of 22 years between 2000 and 2021.

Using panel data regression analysis, the relationship quality of information disclosed and financial stability is explored as shown in the equation below:

Y= F (Financial information disclosures, Bank-specific indicators and Macro-economic variables)

Where Y refers to the dependent variables that is bank's Z-score, RAROA and RAROE. More specifically the equations are:

$$Z-score = \beta_0 + \delta_1 Inf\_Dis_{it} + \delta_2 B\_siz_{it} + \delta_3 Lev_{it} + \delta_4 L\_qty_{it} + \delta_5 B\_Lty_{it} + \delta_6 F\_Owp_{it} + \delta_7 GDP + \delta_8 Inf + \varepsilon_i$$

$$RAROA = \beta_0 + \delta_1 Inf\_Dis_{it} + \delta_2 B\_siz_{it} + \delta_3 Lev_{it} + \delta_4 L\_qty_{it} + \delta_5 B\_Lty_{it} + \delta_6 F\_Owp_{it} + \delta_7 GDP + \delta_8 Inf + \varepsilon_i$$

$$RAROE = \beta_0 + \delta_1 Inf\_Dis_{it} + \delta_2 B\_siz_{it} + \delta_3 Lev_{it} + \delta_4 L\_qty_{it} + \delta_5 B\_Lty_{it} + \delta_6 F\_Owp_{it} + \delta_7 GDP + \delta_8 Inf + \varepsilon_i$$

Where:

- Z-Score = Bank's Z-score.

- RAROA = Risk Adjusted Return on Assets.
- RAROE = Risk Adjusted Return on Equity.
- $Inf\_Dis_{it} = Information\ Disclosure\ Index\ for\ each\ bank\ at\ time\ t.$
- $B\_Siz_{it} =$ $Bank\ size\ measured\ as$ natural log $total\ assets\ \ for\ each\ bank\ at\ time\ t.$
- $Lev_{it} = Bank\ leverage\ measured\ as\ TE\ to\ TA\ for\ each\ bank\ at\ time\ t.$
- $L\_Qty_{it} =$ $Loan\ quality\ measured\ as\ NPLs\ to\ total\ assets\ for\ each\ bank\ at\ time\ t.$
- $B\_Lty_{it} = Bank\ liquidity\ measured\ as\ loan\ to\ deposits\ for\ each\ bank\ at\ time\ t.$
- $F\_Owp_{it} = Foreign\ ownership\ for\ each\ bank\ at\ time\ t.$
- $GDP = Gross\ domestic\ product\ for\ each\ year.$
- $Inf = Inflation\ for\ each\ year.$
- $\varepsilon_{i=}\ Error\ term$

This research evaluated how financial information disclosed in the annual reports could contribute to the stability of commercial banks in Kenya, using data from the period between 2000 and 2021. Banks whose data was inconsistent for a period of more than three years were excluded from the study. Additionally, banks that liquidated or commenced operations within the study period were also excluded.

Banks' stability was measured using the default risk, that is Z-score, and is measured as the number of standard deviations earnings have to fall before the bank becomes insolvent (Stiroh & Rumble, 2006). Several scholars have used the Z-score, risk adjusted return on assets (RAROA) and risk adjusted return on equity (RAROE) to measure the financial stability in banking sector which include (Barra & Zotti, 2020; Nguyen & Dinh, 2021; Saif-Alyousfi, Asish, & Rohani, 2020). The equations are as follows:

$$Z - score = \frac{[ROA + \left(\frac{E}{A}\right)]}{\delta ROA}$$

$$RAROA = \frac{ROA}{\delta ROA}$$

$$RAROE = \frac{ROE}{\delta ROE}$$

Where:

$E = Total\ Equity$

$A = Total\ Assets$

$ROA = Return\ on\ Assets$

$ROA = Return\ on\ Equity$

$\delta ROA = Standard\ Deviation\ of\ the\ Return\ on\ Assets$

$\delta ROE = Standard\ Deviation\ of\ the\ Return\ on\ Equity$

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The higher the Z-score the more stable the bank is that is a higher Z-score implies a lower probability of insolvency. The higher the RAROA and RAROE value the more the stable the bank is.

Bank stability mostly depend on the level of quality of financial information disclosure that is providing the necessary information on timely basis which enables the management to take corrective measures before things go out of hand. Business entities may disclose their information in a number of ways which include: published annual reports; management discussion analysis (MDA) where they communicate material information; ad-hoc press briefing in which they communicate issue affecting the company for example, issue to do with profit warnings (Du, Song, & Wu, 2016). The measure of disclosure that was used in this study was disclosure index of nine categories related to risks, liquidity and profitability. Disclosure index was a method also used by (Du, Song, & Wu, 2016).

$$\frac{1}{45} = \sum_{i=1}^{45} \text{si}$$

Where: 45 (9x5) is the maximum attainable score on the sum of the sub-indices

: Si is related to one or more sources of risk

Higher values of this variable indicate higher levels of bank accounting disclosure. The table in appendix 1 provide more details.

The study utilized macroeconomic indicators, including the gross domestic product (GDP) and the inflation rate, as control variables. These indicators were essential for providing context and controlling for external economic factors that could influence the variables under investigation. Real economic growth was measured by the growth of GDP, with the data collected from the World Bank. The inflation rate data was collected from the World Bank. Positive growth in the real GDP with lower inflation rate are expected to improve the bank financial performance and therefore lowers the probability of insolvency.

4.0 Research Findings and Discussions

This section presents the study findings. Further, it provides a discussion of the findings. These findings are further corroborated by past literature on the study.

4.1 Summary Statistics

Table I below presents the summary statistics for the variables to establish the effect of financial information disclosure on the financial stability of commercial banks in Kenya which include dependent variable, robust check for financial stability variables that is RAROA and RAROE, financial information disclosures, firm specific variables, financial structure variables and macroeconomic variables. All the variables had an acceptable mean and standard deviation. Dependent variable for the study was Z-score as a measure for financial stability in the banking sector of which the higher the value, the higher the stability which was demonstrated in Table I that is a mean of approximately twelve percent (12%) and standard deviation of approximately eight percent (8%). This is an indication that most of Kenya commercial banks have been stable within the period of study, although some banks were financially unstable demonstrated by the minimum value of approximately negative eight point three percent (-8.3%). For robustness check

using risk adjusted return on assets (RAROA) and risk adjusted return on equity (RAROE) shows a mean of 1.695 and 1.468 respectively and standard deviation of 1.837 and 1.548 respectively, which is an indication that either could have been used to measure financial stability without changing the results materially.

The overall financial disclosures reported a minimum score of 11 and a maximum score of 38 out of 45, with an average score of approximately 25. These values indicate that the disclosures are of high quality and have a significant influence on financial stability. Disclosures categorized as risk reported a minimum score of 3 and a maximum score of 15 out of 15, with an average score of approximately 10. Disclosures categorized as liquidity reported a minimum score of 3 and a maximum score of 11 out of 15 with an average score of approximately 6. Disclosures categorized as profitability reported a minimum score of 3 and a maximum score of 15 out of 15 with an average score of approximately 9. These results indicated that disclosures categorized as risk and profitability has a higher quality compared with disclosures categorized as liquidity, however all of them influenced financial stability.

Equity to total assets was utilized as a measure of leverage, indicating the level of capitalization that controls the relationship between bank fragility and capitalization levels. According to Table I, Kenya commercial banks exhibited high leverage, with an average of approximately 17% and ranging from 5.13% to 95.41%. High levels of capitalization is an indication that commercial banks can absorb large shocks and shield banks when asset values decline, this enhances financial stability. Bank size, as defined by the natural log of total assets, is regarded as a significant predictor of bank diversity, fragility, and stability. Larger banks have better risk diversification due to the level of capitalization. From Table I it is evident that the level of capitalization has a great variation with an average of $19.41 billion and standard deviation of $1.483 billion. This explained why most of the banks had a low diversification since larger banks have a better risk diversification.

Bank concentration was measured by HHI and bank concentration, with higher values indicating higher concentration and low competition. The statistical summary indicates that Kenyan commercial banks have a low concentration, an average of approximately 7% and ranging from 5% to 11.6%. With low bank concentration, it means that the rate of competition is high and this can lead to banks' managers taking higher risks and this can be detrimental to financial stability. There is a balance between the foreign owned banks at 0.45 with local banks at 0.55 (1-0.45), indicating that there is a balance between the local banks and foreign banks. Kenyan commercial banks have a minimal asset growth rate at approximately mean rate of 16%, this indicates minimal investments is done by majority of the banks.

Table I: Descriptive Statistics

VARIABLES	N	Mean	s.d.	Min	Max
Dependent Variables (DV)					
Z-score	789	12.25	7.941	-8.309	41.47
RAROA	789	1.695	1.837	-4.066	8.33
RAROE	789	1.468	1.548	-4.14	5.856
Independent Variables (IV)					
FD Index	789	25.39	6.101	11	38
FD-Risk	789	9.896	3.739	3	15
FD-Liquidity	789	6.337	1.989	3	11
FD-Profitability	789	9.158	3.148	3	15
Control Variables					
Firm specific variables					
Bank Size	789	19.41	1.483	15.81	23.17
Bank Efficiency	789	0.696	1.978	0.0928	55.12
Leverage	789	17.19	11.26	5.13	95.41
Loan Quality	789	14.45	14.25	0.29	63.39
Foreign Ownership	789	0.456	0.498	0	1
Growth on assets	789	0.155	0.33	-0.531	5.209
Financial structure variables					
Bank Concentration (HHI)	789	0.0788	0.0176	0.0594	0.116
Macroeconomic variables					
GDP Growth Rate	789	4.224	2.209	-0.25	8.058
Inflation	789	7.578	3.201	1.966	15.11
Covid-19 Dummy	789	0.0938	0.292	0	1

Notes: N refers to number of observation; s.d. refers to standard deviation; Min refers to minimum; Max refers to maximum; RAROA refers to risk adjusted return on assets; RAROE refers to risk adjusted return on equity; FD refers to financial disclosures; and HHI refers to Herfindahl Hirschman Index.

4.2 The Effect of Financial Information Disclosures On Banks' Financial Stability Of Commercial Banks In Kenya

The objective of this study was to evaluate the quality of information disclosed in the notes to financial statements of commercial banks in evaluating the financial stability in Kenya. Stability disclosures based approach was used of which analysis was pegged to risk, liquidity and profitability. Self-constructed disclosure measures were employed, where scores were assigned on an ordinal scale ranging from 1 to 5 for each item in the list of disclosures. The allocation of scores was determined by assessing the usefulness of the information provided by the disclosed financial information. This method of self-constructed disclosure measures has been widely adopted by

various scholars to evaluate the quality of information disclosed in financial statements (Reeb & Zhao, 2013) and (Du, Song, & Wu, 2016). Disclosure index was constructed for the overall of the three classification, risk disclosures category, liquidity disclosures category and profitability disclosures category. Disclosures that contained high quality information based on the average industrial ratio was awarded a higher score. Under the agency theory by Jensen & Meckling, (1976), stated that if the firm's financial information disclosed is to be useful to stakeholders then it should be disclosed faithfully, that is the information should be complete, free from error and should not be bias.

The overall financial disclosures as demonstrated in Table 2 indicated that the financial disclosures index and several control variables such as bank size, leverage, bank efficiency, growth of assets, diversification and inflation are statistically significant when evaluating the quality of information disclosed in the financial statements for the commercial banks in Kenya and had influence on financial stability. The independent variable, the financial disclosure index, was found to be positively statistically significant. This suggests that financial information disclosures enabled the management of commercial banks to derive value from the information and assess the state of financial stability for their banks. These results are in line with several studies which include (Reeb & Zhao, 2013; Du, Song, & Wu, 2016; Boateng, 2016; Polizzi & Scannella, 2020; Bischof, Laux, & Leuz, 2021). All the values of the variables ranging from independent variables to control variables indicated that they were significant and could be used to evaluate the quality of information disclosed in the financial statements and whether it had an influence to financial stability.

Non-performing loans (NPLs) was positively statistically significant when evaluated with only RAROE implying that with high capital buffer the bank can absorb losses resulting from NPLs (Haddad & Alali, 2021). It is also an indication that with an increase in NPLs the banks become unstable, the financial information disclosure in this area can be crucial to the management which is in line with the study of (Boateng, 2016). Bank size measured as natural log of total assets was positively statistically significant, this is an indication that large commercial banks are more financially stable as compared to small banks and financial information disclosure was of high quality and had influence on financial stability. Leverage measured as equity to total assets was positively statistically significant, this is as indication that as the equity increases in proportion to the total assets the commercial banks become stable, information disclosures in this will enable the management to evaluate whether there is over capitalization which hinders financial stability and it is in line with the study of (Du, Song, & Wu, 2016). Bank efficiency as measured as costs to gross revenue was negatively statistically significant, this is as indication that information disclosed will enable the management to learn about the trend on costs since as the costs increases proportionally with revenue the commercial banks become financial unstable. Growth on assets was negatively statistically significant, this means that financial information disclosed enable the management to make decisions on growth of assets.

Generally, based on Table 2, it is evident that financial information disclosure allowed the researcher to determine that diversification had a negative statistical significance. This indicates that as commercial banks become more diversified, they tend to become financially less stable. Moreover, bank concentration, as measured by HHI, showed a positive statistical significance. This suggests that increased bank concentration enhances market power, leading to greater financial stability for commercial banks. Furthermore, inflation was negatively statistically significant and this suggests that, as the rate on inflation goes up many borrowers are unable to

meet their financial obligation increasing the NPLs and therefore making the commercial banks to be financially unstable. Lastly Covid-19 used as dummy was negative and statistically significant with financial stability indicating that during the Covid-19 pandemic, most borrowers defaulted increasing the NPLs and therefore making the commercial banks to be financially unstable.

Table 2: Regression Output for Overall Financial Information Disclosures

	FIXED EFFECTS		
VARIABLES	Z-score	RAROA	RAROE
FD Index	0.130***	0.140***	0.153***
	-0.02	-0.013	-0.01
NPL	0.005	0.005	0.014**
	-0.01	-0.005	-0.005
Bank Size	0.595**	0.302***	0.151*
	-0.259	-0.066	-0.077
Leverage	0.479***	0.035***	-0.002
	-0.047	-0.006	-0.007
Bank Efficiency	-0.288***	-0.060***	-0.005
	-0.057	-0.014	-0.011
Growth on Assets	-0.325*	-0.088	-0.047
	-0.193	-0.09	-0.102
Diversification	-4.366**	-0.149	0.779
	-1.72	-0.469	-0.568
HHI	13.239	7.612**	3.113
	-12.175	-3.141	-4.491
Inflation	-0.041**	-0.003	0.009
	-0.02	-0.009	-0.01
Covid-19 Dummy	-0.096	-0.159	0.124
	-0.245	-0.15	-0.135
GDP Growth Rate	-0.003	0.031***	0.034**
	-0.023	-0.011	-0.014
Constant	-9.559	-8.967***	-6.279***
	-6.099	-1.599	-1.95
Observations	789	789	789
R-squared	0.768	0.511	0.44
Number of banks	43	43	43

*Note: RAROA refers to Risk Adjusted Return on Assets; RAROE refers to Risk Adjusted Return on Equity; FD Index refers to financial disclosures index; NPL refers to non-performing loans; HHI refers to Herfindahl Hirschman Index; C-19 refers to Covid-19; and GDP GR refers to gross domestic growth rate. *** p<0.01, ** p<0.05 and * p<0.1 denote 1%, 5% and 10% level of significance respectively.*

Table 3 below displays the regression results of financial information disclosures regarding risk, which the study identified as the most significant contributor to financial stability. It is evident from the table that the financial disclosure index related to risk was positively statistically significant in relation to the financial stability of commercial banks in Kenya. This means that disclosures of financial information relating to risks enables the management and other stakeholders to understand the commercial banks. It was also an indication that these disclosures had influence on financial stability of commercial banks in Kenya. Table III provided a clear indication that the results replicated those of overall financial information disclosures apart from variables such as NPLs, growth of assets, inflation and Covid-19 when used as a dummy.

From Table 3, it is clear that financial information disclosed relating to risk enabled the researcher to conclude that the control variables used that resulted with positive correlation included bank size, leverage, bank concentration measured using HHI and GDP growth rate. Bank size measured as the natural log of total assets affects commercial banks in Kenya positively and is associated with bank stability when stability was measured using Z-score and RAROA. Commercial banks in Kenya also demonstrated that leverage measured as total equity to total assets is positively associated with bank stability when stability was measured using Z-score and RAROA. Bank concentration measured using HHI was only positively associated with bank stability in Kenya when stability was measured using RAROA. Further GDP growth rate affects commercial banks in Kenya positively and is associated with bank stability when stability was measured using RAROA and RAROE.

From Table 3, it is clear that financial information disclosed relating to risk enabled the researcher to conclude that the control variables used resulted with a negative correlation included NPLs, bank efficiency, diversification and Covid-19 when used as a dummy. Bank efficiency measured as cost to gross income affects commercial banks in Kenya negatively and is associated with bank stability when stability was measured using Z-score and RAROA. NPLs measured as NPLs to total assets was only negatively associated with bank stability in Kenya when stability was measured using RAROA. Diversification was only negatively associated with bank stability in Kenya when stability was measured using Z-score. Covid-19 used as a dummy was only negatively associated with bank stability in Kenya when stability was measured using RAROA.

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Table 3: Regression Output for Financial Information Disclosures Relating to Risk

	FIXED EFFECTS		
VARIABLES	**Z-score**	**RAROA**	**RAROE**
FD-Risk	0.098**	0.104***	0.125***
	-0.042	-0.022	-0.021
NPL	-0.011	-0.013**	-0.002
	-0.011	-0.005	-0.006
Bank Size	0.551**	0.254***	0.103
	-0.265	-0.083	-0.097
Leverage	0.486***	0.043***	0.007
	-0.047	-0.007	-0.007
Bank Efficiency	-0.291***	-0.063***	-0.008
	-0.058	-0.016	-0.013
Growth on Assets	-0.254	-0.012	0.036
	-0.18	-0.096	-0.098
Diversification	-4.526**	-0.319	0.575
	-1.743	-0.534	-0.626
HHI	15.086	9.526**	5.716
	-11.915	-4.29	-5.586
Inflation	-0.033	0.006	0.018
	-0.021	-0.011	-0.012
Covid-19 Dummy	-0.336	-0.419**	-0.145
	-0.286	-0.178	-0.183
GDP Growth Rate	0.013	0.048***	0.052***
	-0.023	-0.012	-0.016
Constant	-6.474	-5.612***	-2.866
	-6.313	-1.964	-2.336
Observations	789	789	789
R-squared	0.753	0.306	0.207
Number of banks	43	43	43

*Note: RAROA refers to Risk Adjusted Return on Assets; RAROE refers to Risk Adjusted Return on Equity; FD refers to financial disclosures; NPL refers to non-performing loans; HHI refers to Herfindahl Hirschman Index; C-19 refers to Covid-19; and GDP GR refers to gross domestic growth rate. *** p<0.01, ** p<0.05 and * p<0.1 denote 1%, 5% and 10% level of significance respectively.*

5.0 Conclusions

The objective of this study was to evaluate the quality of financial information disclosures and its contribution to financial stability of commercial banks in Kenya. Under the agency theory by

Jensen & Meckling, (1976), it stated that if the firm's financial information disclosed is to be useful to stakeholders then it should be disclosed faithfully, that is the information should be complete, free from error and should not be biased. The null hypothesis posited that there is no significant contribution of financial information disclosures to the stability of commercial banks in Kenya. However, based on the research findings, financial information disclosure was found to be statistically positively significant. Therefore, we reject the null hypothesis and conclude that there was a significant influence of financial information disclosures on the stability of commercial banks in Kenya. The study concludes that commercial banks in Kenya should introduce more disclosures, especially those relating to credit risk per the requirement of International Financial Reporting Standards number seven (IFRS 7) and International Financial Reporting Standards number nine (IFRS 9). The overall financial disclosures index was found to be statistically positively associated with the financial stability of commercial banks in Kenya. Therefore, enhancing the quality and scope of disclosures is recommended to bolster financial stability within the banking sector. This implies that the information disclosed was of high quality and contributed to the financial stability measured using the dependent variable that is Z-score and the robustness check that is risk adjusted return on asset (RAROA) and risk adjusted return on equity (RAROE). Further it meant that, the more the information that was disclosed the greater the bank stability was experienced.

Financial information disclosures relating to risk were constructed using three metrics: non-performing loans to gross loans, reserves for impaired loans to gross loans, and loan impairment charges to gross loans. The primary aim of these metrics was to evaluate how uncollectability and impairment loss of financial assets can affect commercial banks in Kenya. Additionally, the study aimed to assess the extent to which uncollectability and impairment loss of financial assets can cause financial instability among commercial banks in Kenya. Non-performing loans to gross loans represent loan quality, which was statistically negatively correlated with the financial stability of commercial banks. The study found that disclosures of this metric can enable bank management to develop policies to reduce the increase of non-performing loans, thereby enhancing the stability of commercial banks. The second and third metrics focused on reserves provided by banks for impaired loans and loan impairment charges. The main aim was to evaluate the adequacy of these provisions and their significance to bank management. The study found that the provisions made by banks were adequate, in line with regulations set by the Central Bank of Kenya (CBK). Additionally, commercial banks that scored high on these metrics proved to be financially stable.

Financial information disclosures relating to liquidity was constructed using three metrics that is loans to customer deposits, interbank assets to interbank liabilities and liquid assets to total assets. The main aim of this metric was to evaluate whether the commercial banks in Kenya were financial stable since commercial banks that are not liquid enough can be affected by financial shocks especially the one resulting from bank runs. The study found out that growth of customer deposits especially the fixed certificates deposits enabled the commercial bank to operate with a margin thereby increasing their financial stability. Additionally, the study found out that financial information relating to liquidity could result to a contagion effect mostly if the information gave negative publicity of the bank. From the study, it was found out that most of the banks provided information disclosures that adhered to the requirement of the CBK. Lastly, the commercial banks that scored high on these metrics proved to be financially stable.

Financial information disclosures relating to profitability were constructed using three metrics: return on assets (ROA), return on equity (ROE), and interest income to average earning assets.

The primary aim of these metrics was to evaluate the contribution of the earnings power of commercial banks in building up capital reserves or capital buffers. Capital buffers are utilized to hedge against financial shocks that may arise in the market due to unforeseen events. The study found that financial information disclosures relating to profitability were of great importance in enabling bank management to understand their bank and evaluate the necessity for external funding. If a commercial bank is more profitable with adequate revenue reserves, it can absorb any financial shocks, making it more financially stable. Additionally, the study found that it was necessary to reconcile the information generated regarding revenue reserves with the cash flows to enable the bank management evaluate the economic profit which is a true measure of the financial stability of the commercial banks. Lastly, the commercial banks that scored high on these metrics proved to be financially stable.

6.0 Recommendations

The study recommends establishing best practices for providing financial information in the banking sector to ensure that stakeholders, particularly investors, can better understand the information disclosed, especially when evaluating the financial stability of commercial banks. It suggests that timely, complete, unbiased, and error-free financial information is crucial for regulators and bank managers to effectively assess and manage risks. Furthermore, the study highlights the importance of enhancing bank financial information disclosures, particularly those related to risk and profitability, to increase overall financial stability. Therefore, it is recommended that commercial banks prioritize improving the quality and comprehensiveness of their disclosures in these areas to enhance investor confidence and mitigate financial risks.

The study recommends that business entities, including banks, should provide more detailed disclosures alongside their financial statements to ensure meaningful information for stakeholders. High-quality information, characterized by comprehensive disclosures, enables stakeholders to evaluate companies effectively and make informed economic decisions. Given the potential for information asymmetry to disrupt financial stability, particularly in the banking sector where it can lead to bank runs, the study suggests that full disclosures are essential. By providing all relevant information promptly and at no cost, businesses can mitigate the risks associated with information asymmetry, contributing to greater stability in the financial sector.

The study recommends that the Central Bank of Kenya (CBK) extend the disclosure requirements for commercial banks operating in Kenya to include provisions outlined in International Accounting Standard number twenty-four (IAS 24). Currently, commercial banks are mandated to provide risk disclosures under International Financial Reporting Standards number seven (IFRS 7) and number nine (IFRS 9). Extending these requirements to encompass IAS 24 would entail disclosing transactions with related parties, specifically loans advanced to related parties. By implementing these additional disclosure requirements, banks would undergo a more rigorous screening process for such loans, as they would be subject to regulatory evaluation. This enhanced scrutiny would serve to reduce credit risk and contribute to the overall financial stability of banks.

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