

**FACTORS INFLUENCING CHOICE OF INVESTMENT PRODUCTS BY FINANCIAL
MANAGERS OF FIRMS LISTED IN NAIROBI SECURITIES EXCHANGE, KENYA**



BY

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ABSTRACT

Investment products refer to investment avenues available for savers in any market. Behavioral finance and investment management literature show that investment products are influenced by both financial and non-financial factors. Previous studies focus on individual investor investment decision making processes in the developed economies. Kenyan investors have currently solved the problem of sources of funds for investment and now faced with the problem of how to invest, where to invest and when to invest. Currently, Kenya is ranked position 91 up from 108 in terms of ease of starting a business. Therefore, the purpose of this study was to analyze factors influencing the choice of investment products among firms listed in the Nairobi Securities Exchange, the firms being the role model on professionalism and decision making. The study was conducted between April 2015 and February 2016. Specific objectives of the study were to: establish the influence of investments' financial information on choice of investment products; determine the effect of the investment returns on choice of the investment products and to find out the effect of third party opinions on the choice of investment products. The study is anchored on prospect/loss-aversion theory. The study adopted a correlation research design. The target population was all the 66 listed companies in Nairobi Securities Exchange which was obtained using a census sampling technique. Primary and secondary data was obtained using semi-structured questionnaire and desk review respectively. Inter-rater reliability test was done using pilot method on 10 companies' financial managers who were excluded from the final sample of the study and a minimum threshold of 0.701 was met results being 0.789, 0.705, 0.850 and 0.765 among the tested constructs. Content validity test was done using expert reviewers. Data analysis was done using Pearson's correlation and multiple regression analyses. The unit of analysis was the companies listed in NSE. Data was presented using graphs and tables. The study findings were that; financial information was a positive significant predictor of investment product choice ($\beta = .353$ ($p = .000$)); investment returns was a positive significant predictor of investment product choice ($\beta = .215$ ($p = .018$)) and third party opinions was a positive significant predictor of investment product choice ($\beta = .449$ ($p = .000$)) implying that they are positive predictors of investment product choice. The study recommends that prospective investors consider and analyze financial information; investment returns and third party opinion to make prudent investments.

CHAPTER ONE

INTRODUCTION

This chapter outlines the background to the study, statement of the problem, objectives of the study, research hypotheses, scope of the study, justification of the study and the conceptual framework.

1.1 Background of the Study

Investment decisions require special attention because of the following reasons: first they influence the firm's growth in the long run, second they affect the risk of the firm and third they involve commitment of large amount of funds, that are irreversible or reversible at substantial loss and last but not least they are among the most difficult decisions to make. If the adoption of an investment increases average gain but causes frequent fluctuations in its earnings, the firm will become more risky. Thus, investment decisions shape the basic character of a firm (Copeland et al 2001).

Investment is the commitment of investors' funds to derive future income in the form of interest, dividend, premiums, pension benefits or appreciation in the value of their capital (Sharpe *et al.* 2001). On the other hand, investment products refer to investment avenues available for savers in any market. Some of them are marketable and liquid while others are non-marketable. Some of them are highly risky while others are almost riskless. The investor has to choose proper avenues from among them depending on his preferences, needs and ability to assume risk (Brigham et al., 2001). These investment avenues include: equity shares, corporate bonds, real estates, government securities and bank cash and deposits (Sharpe *et al.*, 2001).

Potential investors are interested in an investment product in total both on short and long term basis in particular the investment's ability to generate acceptable return on their money based on selected ratios which include dividend, return and gearing ratios. Copeland et al (2005) argue that investors are primarily concerned with expectations about the future, considering earnings projection and historical financial data to be of high interest to investors and that the general public faces problems in understanding financial reporting in the corporate sector. Pandey (2008)

note that both price and earnings volatility are the primary measures of risk employed by individuals, Copeland et al. (2005) observe professional fund managers exhibit considerable skill in their investment decision making compared to individual investors. According to Pandey (2008) individuals are described as “investors” rather than “traders” since they are long-term minded and give little interest to short-term yields whereas Copeland et al. (2005) note that investors' main source of information is through fundamental or technical analysis.

Prior studies on financial information and choice of investment products (Kadiyala and Rau, 2004 and Krishnan and Brooker, 2002) show that investor react to corporate event and financial information announcements when selecting investment products. While, some studies use descriptive research or exploratory research designs to study liquidity on the investments in the deposit-taking Saccos (Merikas *et al.*, 2003; Muraguri, 2014), Others (Hodge, 2003) employ random sampling techniques to investigate investors' perceptions of earnings quality, auditor independence, and the usefulness of audited financial information but focus on listed firms in Kenya using correlational research design remains unknown. On the contrary, others (Fischer and Gerhardt, 2007; Krishnan and Brooker, 2002 and Brown and Cliff, 2004) study individual investor investment decision making processes using exploratory research design and comparative analysis in the economies of Jordan, UK and Germany even though a comparative study to listed firms in Kenya is unknown. Therefore, the financial information as a factor influencing the choice of investment products among listed firms in Kenya is generally unknown

Investment returns refers to what accrues from an investment and it represents the sum of the products of the possible outcomes and the probabilities that those outcomes will be realized, (Pandey, 2008). Copeland *et al.* (2005) observes that an investment's expected return is an average of the possible returns from an investment where each of these returns is weighted by the probability that it will occur. Investors generally are expected to have a higher degree of knowledge as pertains to the various investments they make. Knowledge of past returns of asset categories is normally poorly understood by investors. The main result is that investors are generally unaware of gaps in their financial knowledge. However, they indirectly recognize these gaps by expecting to achieve returns below than or equal to those of the market index. Efforts are therefore required to allow investors to judge their level of financial knowledge objectively and improve that knowledge. It is evident that poor knowledge of the performance of categories and

of the concept of risk premium, calls into question investors' financial planning ability (Brigham *et al.*, 2001).

Reviewed literature (Hussein, 2007; Dimitrios, 2007) identify expected investment return as an important factor in determining choice of investment products. While, some studies use descriptive statistics, Friedman's test and factor analysis, to study investment returns (Muswenje, 2013; Greenwood, 2014), Others (Lubos and Stambargh, 2001) study the relationship between market wide liquidity and investment pricing using descriptive research design but similar studies on listed firms in Kenya using correlational research design has not been done. On the contrary, others (Merikas *et al.*, 2003 and Krishnan and Brooker, 2002) study the factors influencing the decisions of investor who use analysts' recommendation in the economies of UK and Greece but no study yet on listed firms in Kenya. Therefore, the investment returns as a factor influencing the choice of investment products among listed firms in Kenya has not been studied.

Third party opinion is defined as neutral or biased information obtained from a family member, a friend's recommendation and experts opinion on the investment product (Brigham *et al.*, 2010). Pandey (2008) observes that an investor who already holds an investment may respond to an analyst recommendation in one of four ways: the investor may hold the investment on a sell recommendation, the investor may sell the investment on a hold recommendation, the investor may hold the investment on a hold recommendation, or the investor may sell investment on a sell recommendation. Prior investment research has examined how the type of analyst and the nature of the analyst report affect investor behavior (Francis and Soffer, 1997). They found that because of the existence of incentives for analysts to issue favorable recommendations, investors weight other information in the analyst report more heavily when they observe a buy rather than a sell recommendation. This factor includes purchase recommendations from brokerage houses and individual stock brokers. Recommendations from friends or coworkers marginally loaded on this factor as well (Francis and Soffer, 1997).

Prior studies on third party opinions and investment product choice (Francis and Soffer, 1997 and Nagy and Obenberger, 1994) show that favorable third party opinions and recommendations influence the choice of investment products. While, some studies use descriptive research or

exploratory research designs to investors behavior (Dimitrios, 2007; Malmendier and Shanthikumar, 2003), Others (Hodge, 2003) employ random sampling techniques to investigate investors' perceptions of earnings quality, third party information from auditors and the usefulness of audited financial information but similar study on listed firms in Kenya using correlational research design has not been conducted. On the contrary, others (Fischer and Gerhardt, 2007; Krishnan and Brooker, 2002 and Brown and Cliff, 2004) study individual investor investment decision making processes using exploratory research design in the developed economies of Jordan, UK and Germany but a study in comparison to listed firms in Kenya is yet to be conducted. Therefore, the third party opinion as a factor influencing the choice of investment products among listed firms in Kenya is unknown.

In Kenya, listed shares are traded at the Nairobi Securities Exchange (NSE), which is the single major open capital market in the country. It differs from those developed markets in such characteristics as the ownership concentration, capital structure, asset structure, profitability, firm size and corporate governance standards making it a unique context of this study. The Nairobi Securities Exchange formerly known as Nairobi Stock Exchange was set up in 1953 in Kenya, as a regional exchange for Kenya, Tanganyika, Uganda and Zanzibar. After independence in these countries, it became Kenya's national stock exchange. The stock market has developed over the years with 66 listed companies by the close of 2015. The Nairobi Securities Exchange has also moved from the open-outcry trading system to Automated Trading System (ATS) in order to improve the Market's informational, allocative and functional (operational) efficiency. The exchange has twelve sectors namely: Agricultural, Commercial & Services, Telecommunications & Technology, Automobile & Accessories, Banking, Insurance, Investment, Manufacturing, Manufacturing and allied, Construction & Allied, Energy & Petroleum and Industrial & Allied sectors (NSE Hand Book, 2015).

1.2 Statement of the Problem

An investment refers to the commitment of investors' funds to derive future income in the form of interest, dividend, premiums, pension benefits or appreciation in the value of their capital. On the other hand, investment products refer to investment avenues available for savers in any market. Some of them are marketable and liquid while others are non-marketable. Some of them are highly risky while others are almost riskless. The Kenyan investors are faced with a challenge to choose proper avenues from among them depending on their preferences, needs and ability to assume risk. Currently investors are no longer having a problem with sources of finance but face a nightmare on what kind of investment to set up, how to set up and when to set up business investment. Therefore, important key decisions to be made before investing largely remains unknown to prospective investors in order to ensure profitability and professionalism.

1.3 Objectives of the study

The general objective was to analyze the factors influencing choice of investment products by financial managers of investment companies' listed in Nairobi Securities Exchange (NSE), in Kenya. Specifically the study sought to:

1. Establish the influence of investments' financial information on choice of investment products of investment companies listed in Nairobi Securities Exchange, Kenya.
2. Determine the effect of the investment returns on choice of the investment products of listed investment companies in Nairobi Securities Exchange, Kenya.
3. Find out the effect of third party opinions on the choice of investment products of listed investment companies in Nairobi Securities Exchange, Kenya.

1.4 Research Hypotheses

This study was guided by the following research hypotheses:

H₀₁: Investments' financial information has no influence on choice of investment products of investment companies listed in Nairobi Securities Exchange, Kenya.

H₀₂: Investment returns have no effect on choice of investment products of investment companies listed in Nairobi Securities Exchange, Kenya.

H₀₃: Third party opinions have no effect on choice of investment products of investment companies listed in Nairobi Securities Exchange, Kenya.

1.5 Scope of the study

The scope of this study was examined in terms of subject, geographical and time scopes. In terms of the subject scope, this study is limited to the broad finance field of behavioral finance in that it deals with the irrational decision making of prospective investors. Geographical scope is the second aspect of scope in this study. The study was carried out in Nairobi City. It is capital city and commercial hub of Kenya, where most listed firms are traded in. Specifically, the study focused on factors influencing choice of investment products. In terms of time scope, the study was conceived between April 2015 and February 2016.

1.6 Significance of the Study

The findings from this study are of significance to a number of partners in the investment community. First, the study is helpful to the investment policymakers, especially to prospective investors, to realize the need to factors that influence investment choice.

Secondly, the study has generated knowledge linking factors influencing choice of investments to investment products of listed firms which will guide financial managers in the planning for the limited financial resources allocated to the investment portfolios to investors.

Thirdly, the study may be helpful to all academicians in behavioral finance, investment and portfolio management in the furtherance of their studies in form of future research and in the actualization of investment goals.

Lastly, the study is of academic interest and it further contributes to the larger scholarly literature on investment theory in the investment and finance industry.

1.7 Conceptual Framework

Independent Variable

Factors influencing choice of investment products

- Financial information
- Investment returns
- Third party opinions

Dependent Variable

Investment Products

- Corporate bonds
- Real estate
- Government securities
- Equity shares
- Bank cash and deposits



Figure 1.1: Factors Influencing Choice of Investment Products

Source: Adapted from Hussein (2007)

Figure 1.1 shows the factors influencing choice of investment products. The independent variable is the factors influencing choice of investment products which has three dimensions namely, financial information, investment returns and third party opinions. These are variables that are stable and unaffected by other variables being measured.

The dependent variable is the investment products available which includes equity shares, bank cash and deposits, corporate bonds, government securities and real estates. They represent factors that depend on other factors that are being measured.

CHAPTER TWO

LITERATURE REVIEW

This chapter of the study reviews literature on the subject of financial investments. The specific areas covered are theoretical review and empirical review.

2.1 Theoretical Review

2.1.1. Regret-Theory

This theory was propounded by Pareto (1997) and it deals with the emotional reaction people experience after realizing they've made an error in judgment. Faced with the prospect of selling an investment product, investors become emotionally affected by the price at which they purchased the investment. So, they avoid selling it as a way to avoid the regret of having made a bad investment, as well as the embarrassment of reporting a loss. Regret theory can also hold true for investors who find an investment they had considered buying but never went up in value. Some investors avoid the possibility of feeling this regret by following the conventional wisdom and buying only investments that everyone else is buying, rationalizing their decision with "everyone else is doing it" (Pareto, 1997). When investors make a choice among investment products, they experience emotional reaction due to the fear of making an error in their judgment. Therefore prior evaluation financial information contains key attributes to investment choice.

2.1.2 Theory of Mental Accounting

This theory was coined by Thaler (2001) and it postulates that humans have a tendency to place particular events into mental compartments, and the difference between these compartments sometimes impacts our behavior more than the events themselves. An investing example of mental accounting is best illustrated by the hesitation to sell an investment that once had monstrous gains and now has a modest gain. During an economic boom and bull market, people get accustomed to healthy, albeit paper, gains. When the market correction deflates investor's net worth, they're more hesitant to sell at the smaller profit margin. They create mental compartments for the gains they once had, causing them to wait for the return of that gainful

period (Thaler, 2001). The concept of Investment returns in terms of expected dividends and interest paid derived from an investment is anchored on this theory.

2.1.3 Prospect/Loss-Aversion-Theory

This theory was proposed by Kahneman and Tversky (1979) who propounded that people express a different degree of emotion towards gains than towards losses. Individuals are more stressed by prospective losses than they are happy from equal gains. An investment advisor won't necessarily get flooded with calls from her client when she's reported, say, a Kshs 500,000 gain in the client's portfolio. But, you can bet that phone will ring when it posts a Kshs 500,000 loss! A loss always appears larger than a gain of equal size -when it goes deep into our pockets, the value of money changes. Prospect theory also explains why investors hold onto losing stocks: people often take more risks to avoid losses than to realize gains. For this reason, investors willingly remain in a risky stock position, hoping the price will bounce back. Gamblers on a losing streak will behave in a similar fashion, doubling up bets in a bid to recoup what's already been lost. So, despite our rational desire to get a return for the risks we take, we tend to value something we own higher than the price we'd normally be prepared to pay for it. The loss-aversion theory points to another reason why investors might choose to hold their losers and sell their winners: they may believe that today's losers may soon outperform today's winners. Investors often make the mistake of chasing market action by investing in stocks or funds which garner the most attention. Research shows that money flows into high -performance mutual funds more rapidly than money flows out from funds that are underperforming (Kahneman and Tversky, 1979).

2.1.4 Theory of Overconfidence

This theory was suggested by Tapia and Yermo (2007) and it postulates that people generally rate themselves as being above average in their abilities. They also overestimate the precision of their knowledge and their knowledge relative to others. Many investors believe they can consistently time the market. But in reality there's an overwhelming amount of evidence that proves otherwise. Overconfidence results in excess trades, with trading costs denting profits, (Tapia and Yermo, 2007).

is evident that poor knowledge of the performance of categories and of the concept of risk premium, calls into question investors' financial planning ability (Brigham *et al.*, 2001).

2.1.7 The Concept of Third Party Opinions

Brigham *et al.* (2010) defines third party opinion as neutral or biased information obtained from a family member, a friend's recommendation and experts opinion on the investment product.

Pandey (2008) observes that an investor who already holds an investment may respond to an analyst recommendation in one of four ways: the investor may hold the investment on a sell recommendation, the investor may sell the investment on a hold recommendation, the investor may hold the investment on a hold recommendation, or the investor may sell investment on a sell recommendation.

Prior investment research has examined how the type of analyst and the nature of the analyst report affect investor behavior (Francis and Soffer, 1997). They found that because of the existence of incentives for analysts to issue favorable recommendations, investors weight other information in the analyst report more heavily when they observe a buy rather than a sell recommendation. This factor includes purchase recommendations from brokerage houses and individual stock brokers. Recommendations from friends or coworkers marginally loaded on this factor as well (Francis and Soffer, 1997).

2.1.8 The Concept of Investment Products

Sharpe *et al.* (2001) defines investment as the commitment of investors' funds to derive future income in the form of interest, dividend, premiums, pension benefits or appreciation in the value of their capital. On the other hand, investment products refer to investment avenues available for savers in any market. Some of them are marketable and liquid while others are non-marketable. Some of them are highly risky while others are almost riskless. The investor has to choose proper avenues from among them depending on his preferences, needs and ability to assume risk (Brigham *et al.*, 2001). These investment avenues include: equity shares, corporate bonds, real estates, government securities and bank cash and deposits (Sharpe *et al.*, 2001).

Equity shares represent ownership capital. As an equity shareholder you have an ownership stake in a company. This means that you have a residual interest in income and wealth of the

investment in the company. Corporate bonds are also referred to as debentures represent long term debts instruments. The issuer of a corporate bond promises to pay a stipulated stream of cash flow in form of interest. Real estate refers to investment in land and other immovable properties such as a residential house, agricultural land, semi-urban land, commercial property or resort home. Government securities are issued by the government bodies like the public sector undertakings when borrowing money from the public. They are less risky avenues of investment because of the credibility of the government and government undertakings. Bank and cash deposits are deposits with banks such as savings accounts and fixed deposits. Savings deposits have low interest rates whereas fixed deposits have higher interest varying with the period of maturity (Sharpe *et al.*, 2001).

2.2 Empirical Literature Review

2.2.1. Financial Information and Investment Products

Kadiyala and Rau (2004) in India investigated investor reaction to corporate event announcements. The findings were that investors appear to under-react to prior information as well as to information conveyed by the event, leading to different patterns. The study confirmed one of the behavioral finance models of irrational investor behavior which postulates that investors have a tendency to under-react to information, leading to long-term return continuations when firms announce corporate events such as open-market share repurchases or cash-financed tender offers. However, the study was an event study opposed to checking the role of financial information influencing choice of investment products; studies on listed firms also remain unknown. It also uses an event study methodology as opposed to panel methodology, implying that behavioral models cannot explain the long-run abnormal return evidence since the overreaction of investors to some events and under-reaction to others implies that, on average, investors are unbiased in their reaction to financial information. In addition, investor under-reaction explains the positive long-run abnormal returns following a share repurchase, a conclusion based on the financial information conveyed by the share repurchase.

Another study by Nagy and Obenberger (1994) in Jordan investigates the extent to which listings of 34 factors influence shareholders' perception and provide evidence of a role for a mix of financial and non-financial factors in choosing investment products to invest in. The findings

were that investor's behavior is influenced by available accounting and financial information, investment returns, neutral information, individual risk profile, market characteristics and self image/firm image coincidence. However, the study looked at the extent to which these factors influenced investors' decision to invest. Studies on financial managers of listed firms using a panel methodology to consider financial information as a key factor in choosing investment product are yet to be researched in Kenya.

Epstein (1994) in the United Kingdom examined the social information disclosure and individual investor behavior using descriptive research design. The results indicated the annual reports were extremely useful to corporate shareholders. Furthermore, a majority of the shareholders surveyed also indicated that they would want the company to report on corporate ethics, employee relations and community involvement. However, the study explored social information. Financial information effect has not been studied in relation to financial managers of listed firms using a panel methodology.

Wambua (2013) in Kenya studied the relationship between the profitability and the liquidity of commercial banks using descriptive research design for 44 commercial banks operating in the years 2008 to 2012. The study found a positive insignificant relationship between profitability and liquidity of commercial banks in Kenya. However, finance managers of commercial banks need to maintain a balance between the level of liquid assets and long term assets to reinforce each of the conflicting objectives of maintaining adequate liquidity and sustainable profitability. However, the study only focused on investment liquidity and profitability of commercial banks in Kenya. A gap remains on studies unavailability on financial information as a factor influencing choice of investment products among listed companies. Previous studies have been done using descriptive research and non on correlational research design and panel methodology.

Using descriptive and regression analyses, a study by Muraguri (2014) on the effect of liquidity on the investments in the deposit-taking Saccos in Nairobi, found a positive and significant relationship between liquidity and the return on investments in the Saccos while capital adequacy had a negative but insignificant influence on the return on investments. The study recommendations were that the regulations regarding management of liquidity in the deposit-taking Saccos be reviewed to allow the Saccos diversify their investments in high earning

portfolios such as listed companies and a central depository fund for Saccos be set up to help Saccos have a cheaper avenue for short term borrowing to help address seasonal liquidity challenges. However, liquid assets such as cash and government securities generally have a relatively low returns, hence holding them imposes an opportunity cost. However, the study only focused on liquidity and investments of deposit- taking Saccos in Nairobi. Financial information factors influencing choice of investment products among listed companies are yet to be studied on the same field of study.

Using exploratory research design, Krishnan and Brooker (2002) analyzed the factors influencing the decisions of investor who use analysts' recommendations to arrive at a short-term decision to hold or sell a stock. The results indicate that a strong form of the analyst summary recommendation report, i.e. one with additional information supporting the analysts' position further, reduces the disposition error for gains and also reduces the disposition error for losses as well. However, the study looked at investment decisions at household level as opposed to firm level. Hence listed firms correlational research designs related financial information and choice of investment products are still unknown.

Another study by Merikas *et. al.* (2003) analyzed factors influencing Greek investor behavior on the Athens Stock Exchange. The results indicated that individuals base their stock purchase decisions on economic criteria combined with other diverse variables. The authors did not rely on a single integrated approach, but rather on many categories of factors. The results also revealed that there is a certain degree of correlation between the factors that behavioral finance theory and previous empirical evidence identify as the influencing factors for the average equity investor, and the individual behavior of active investors in the Athens Stock Exchange (ASE) influencing by the overall trends prevailing at the time of the survey in the ASE. However, the study looked at investment decisions at household level as opposed to firm level. Similar researches are yet to be done on listed firms in Kenya. More so there is need to employ correlational research design and to consider financial information as a determinant of investment product choice.

Fisher and Statman (2000) studied the sentiments of Wall Street strategists and revealed that the strategists' sentiments were unrelated to the sentiment of individual investors or that of

newsletter writer (another category of investors provided by them), although the sentiment of the individual investors and newsletter writers groups were closely related. They concluded that sentiment can be useful for tactical asset allocation and that a negative relationship between the sentiment of each of these three groups and future stock returns and the relationship was strategically significant for Wall Street strategists and individual investors. However, the study only explores sentiments as opposed to financial information.

A study by Fischer and Gerhardt (2007) in Germany analyzed individual investor investment decision making process and found that individual investor investment decisions deviate from recommendations of financial theory. They show that these deviations lead to considerable welfare losses. The study conclusions were that financial advice is potentially correcting factor in investment decision making process, there was no support for the overreaction hypothesis, and investor over-reaction to a long series of bad news could produce predictable mispricing of Stock, classical wealth-maximization criteria are important to investors, the recommendations of brokerage houses, individual stock brokers, family members and Co-workers go largely unheeded, investors exhibit a strong demand for information about product safety and quality and about the company's environmental activities and there exist strong forms of the analyst summary recommendation report, i.e. one with additional information supporting the analysts' position further. However, no other study has been conducted employing correlational research design.

Prior studies (Kadiyala and Rau, 2004 and Krishnan and Brooker, 2002) show that investor react to corporate event and financial information announcements. While, some studies use descriptive research or exploratory research designs to study liquidity on the investments in the deposit-taking Saccos (Merikas *et. al.*, 2003; Muraguri, 2014), Others (Hodge, 2003) employ random sampling techniques to investigate investors' perceptions of earnings quality, auditor independence, and the usefulness of audited financial information but focus on listed firms in Kenya using correlational research design is still unknown. On the contrary, others (Fischer and Gerhardt, 2007; Krishnan and Brooker, 2002 and Brown and Cliff, 2004) study individual investor investment decision making processes using exploratory research design and comparative analysis in the economies of Jordan, UK and Germany. Therefore, the financial

information as a factor influencing the choice of investment products among listed firms in Kenya is unknown

2.2.2 Investment returns and Investment products

Using exploratory research design, Hussein (2007) in Saudi Arabia investigated factors influencing individual investors' behavior and found that expected corporate earnings, get rich quickly, stock marketability, past performance of the firm's stock in terms of returns, government holdings, and the creation of the organized financial markets are the investors considerations. However, similar studies employing correlational research design are not explored.

A study by Dimitrios (2007) on determinants of investors behavior in the Athens Stock Exchange using descriptive research design and random sampling technique found that individual investors rely more on newspapers/media and noise in the market when making their investment decisions, while professional investors rely more on fundamental and technical analysis and less on portfolio analysis. Market participants are exposed to a constant flow of information, ranging from quantitative financial data to financial news in the media, and socially exchanged opinions and recommendations. However, the study focused on individual investors as opposed to listed firms, used descriptive research design as opposed to correlational research design which has been employed in this study.

Using descriptive statistics, Friedman's test and factor analysis, Muswenje (2013) explored the factors influencing investment decisions at the Nairobi Stock Exchange. The study was conducted on the 42 investors out of 50 investors that constituted the sample size. The respondents were the individual investors. The study found that the most important factors that influence individual investment decisions were: reputation of the firm, firm's status in industry, expected corporate earnings, profit and condition of statement, past performance firms stock, price per share, feeling on the economy and expected dividend by investors. However, the study looked at individual investors as opposed to corporate financial managers of firms hence need to conclusively research; used descriptive research design as opposed to correlational research

design employed in this research and did not test the effect of investment returns on the choice of investment products.

Greenwood (2014) analyzed time series of investor expectations of future stock market returns from six data sources between 1963 and 2011 and found that the six measures of expectations are highly positively correlated with each other, as well as with past stock returns and with the level of the stock market. Further however, investor expectations are strongly significantly negatively correlated with model-based expected returns. The study concluded that any investment's return prospects should be judged in a way that incorporates all knowledge, including historical experience, financial and behavioral theories, and current market conditions, without being overly dependent on any of these. However, the study looked at individual investors as opposed to corporate financial managers of firms listed and did not test the effect of investment returns on the choice of investment products.

A study by Lubos and Stambargh (2001) on the relationship between market wide liquidity and investment pricing using descriptive research design found that expected stock returns are related to the sensitivities of returns to fluctuations in aggregate liquidity. The monthly measure, an average of individual stock measure estimated with daily data relied on the principle that order flow induces greater returns reversals when liquidity is lower. Over 34 year's period, the average return on stock with high sensitivities to liquidity exceeds that from stocks with low sensitivities by 7.5% annually. Now expected return frequently trips people up in two ways. I.e. it may have been estimated poorly in the first place, using poor estimates of probability for each outcome; or even if it was calculated correctly, outcomes that are dramatically different from the expected return can still occur. The study concluded that the expected outcomes become more and more likely over longer periods and that no matter how fancy our calculations there's no way to truly calculate the probability of any given outcome. However, the study looked at market liquidity and investment returns as opposed to how investment returns influence the choice of investment products among financial managers of listed firms.

Using exploratory research design, Krishnan and Brooker (2002) analyzed the factors influencing the decisions of investor who use analysts' recommendations to arrive at a short-term

decision to hold or sell a stock. The results indicate that a strong form of the analyst summary recommendation report, i.e. one with additional information supporting the analysts' position further, reduces the disposition error for gains and also reduces the disposition error for losses as well. However, the study looked at investment decisions at household level as opposed to firm level, did not cover listed firms and did not employ correlational research design to relate investment returns and choice of investment products among listed firms.

2.2.3 Third Party Opinions and Investment products

Using exploratory research design, a study by Francis and Soffer (1997) examined how the type of analyst and the nature of the analyst report affect investor behavior and the study found that because of the existence of incentives for analysts to issue favorable recommendations, investors weight other information in the analyst report more heavily when they observe a buy rather than a sell recommendation. This factor includes purchase recommendations from brokerage houses and individual stock brokers. Recommendations from friends or coworkers marginally loaded on this factor as well. However, the study used exploratory research design as opposed to correlational research design.

Using exploratory research design, Malmendier and Shanthikumar (2003) tried to answer the question: Are small investors naïve? They found that large investors generate abnormal volumes of buyer initiated trades after a positive recommendation only if the analyst is unaffiliated. Small traders exert abnormal buy pressure after all positive recommendations, including those of affiliated analysts. Using the NYSE Traders and Quotations Database, they found that large traders adjust their trading response downward. However, the study did not explore whether financial information determines investment product choice. There is also need to conduct similar researches on listed firms in Kenya and to employ correlational research design.

Fischer and Gerhardt (2007) in Germany analyzed individual investor investment decision making process and found that individual investor investment decisions deviate from recommendations of financial theory in that the recommendations of brokerage houses, individual stock brokers, family members and co-workers go largely unheeded. However, the

fate of listed firms in Kenya in relation to third party opinion using correlational research design remains unknown.

A study by Dimitrios (2007) on determinants of investors behavior in the Athens Stock Exchange using descriptive research design and random sampling technique found that individual investors rely more on newspapers/media and noise in the market and socially exchanged opinions and recommendations when making their investment decisions, while professional investors rely more on fundamental and technical analysis and less on portfolio analysis. However, the study focused on individual investors in Athens as opposed to listed firms in Kenya which raises the need for the research, and use of correlational research design as opposed to descriptive research design.

Epstein (1994) in the United Kingdom examined the social information disclosure and individual investor behavior using descriptive research design. The results indicated the annual reports were extremely useful to corporate shareholders. Furthermore, a majority of the shareholders surveyed also indicated that they would want the company to report on corporate ethics, employee relations and community involvement. However, the study explored social information as opposed to third party opinion.

A study by Hodge (2003) analyzed investors' perceptions of earnings quality, auditor independence, and the usefulness of audited financial information. He concluded that lower perceptions of earnings quality are associated with greater reliance on a firm's audited financial statements and fundamental analysis of those statements when making investment decisions. However, the study did not cover listed firms in Kenya and did not employ correlational research design. Another study by Brown and Cliff (2004) in India investigated investor sentiment and its relation to near-term stock market returns. They find that many commonly cited indirect measures of sentiments are related to direct measures (surveys) of investor sentiment. However, past market returns are also an important determinant of sentiment. Although sentiment levels and changes are strongly correlated with contemporaneous market returns, the tests in this study show that sentiment has little predictive power for near-term future stock returns. Finally, the

evidence does not support the conventional wisdom that sentiment primarily affects individual investors. However, the study did not employ correlational research design.

Prior studies (Francis and Soffer, 1997 and Nagy and Obenberger, 1994) show that favorable third party opinions and recommendations influence the choice of investment product. While, some studies use descriptive research or exploratory research designs to investors behavior (Dimitrios, 2007; Malmendier and Shanthikumar, 2003), Others (Hodge, 2003) employ random sampling techniques to investigate investors' perceptions of earnings quality, third party information from auditors and the usefulness of audited financial information but fail focus on listed firms in Kenya using correlational research design. On the contrary, others (Fischer and Gerhardt, 2007; Krishnan and Brooker, 2002 and Brown and Cliff, 2004) study individual investor investment decision making processes using exploratory research design in the developed economies of Jordan, UK and Germany as opposed to listed firms in Kenya. Therefore, the third party opinion as a factor influencing the choice of investment products among listed firms in Kenya is unknown

CHAPTER THREE

METHODOLOGY

This chapter presents the research method to be adopted for the study and discusses the techniques and activities undertaken to actualize the study objectives.

3.1 Research design

This study adopted a correlational research design. This is because the researcher was interested in measuring the degree of association between the independent and dependent variables. A correlational study determines whether or not two variables are correlated. This means to study whether an increase or decrease in one variable corresponds to an increase or decrease in the other variable. Positive correlation between two variables is when an increase in one variable leads to an increase in the other and a decrease in one leads to a decrease in the other. Negative correlation is when an increase in one variable leads to a decrease in another and vice versa. No correlation is when two variables are uncorrelated when a change in one doesn't lead to a change in the other and vice versa.

3.2 Study Area

The study area was Nairobi City, the capital of Kenya. It is located at coordinates 1.28° S 36.82° E at altitude of 1,724 m (5,656 ft) with a population of 3,038,553 (GoK, 2009) covering an area of 684 km². It is a commercial and industrial hub where most listed firms have head offices. The city and its surrounding area form the Nairobi County. The city was founded as a railway camp in 1899. It is so big that it is considered as one of the biggest in the whole of Africa.

3.3 The population of study

The target population was the entire group a researcher is interested in; the group about which the researcher wishes to draw conclusions. The target population in this study was all the 66 listed companies in various sectors of NSE market. All the companies were considered hence this study used a census sampling technique.

3.4 Data Collection Methods

The researcher employed both primary and secondary data. A questionnaire (see Appendix I) with closed and open-ended questions were used to collect the primary data. The questionnaire was pre-tested with two academic advisers and 10 finance managers of 10 listed firms to confirm clarity of the questions. Secondary data was collected using desk review method.

3.4.1 Sources of Data

Primary data was collected from the financial managers from each firm and secondary data was be collected using desk review mainly from audited financial statements of these firms, journals, books and magazines.

3.4.2 Data Collection Procedure

A pilot test was carried on 10 respondents who were excluded from the main study. The data was collected using a questionnaire and this is chosen because it is quite efficient. Section one of the questionnaires asked questions relating to a brief background of respondents in the study while section two consisted of questions relating to the investment products and factors influencing choice of investment products. The questionnaires were dropped and picked up later from the respondents.

3.4.3 Reliability Test for Data Collection Instrument

Inter rater reliability test of the questionnaire was done using a pilot test which seeks to answer the question, does the questionnaire consistently measure whatever it purports to measures? When a questionnaire is used, establishing reliability commonly involves administration of the questionnaire or portions of the questionnaire to the same respondents at different times or under different circumstances in order to assess how stable the answers are. The questionnaire was pre-tested with two academic advisers and 10 finance managers of 10 listed firms to confirm clarity of the questions. The 10 firms were however excluded from the final sample of the study leaving an effective sample of 56 firms. The instrument was deemed to be reliable at Cronbach's Alpha of .701.

Table 3.1: Summary of Pilot Results Based on Cronbach's Alpha Reliability Test

Construct	No. of Items	Cronbach's Alpha
Investment products	6	0.789
Financial information	2	0.705
Investment returns	2	0.850
Third party opinions	2	0.765

Source: Survey Data, 2016

All the variables had alpha values of above 0.701, indicating strong internal consistency among measures of variable items.

3.4.4 Validity Test for Data Collection Instrument

Validity is the amount of systematic or built-in error in measurement (Norland, 1990). Validity was established using a panel of experts /academic advisers. The basic principle for establishing validity is the same as for corroborating audit observations and conclusions generally, that is, compared to evidence from different sources and of a different nature.

3.5 Data Analysis

The study adopted a correlational research approach which is used to summarize the characteristics of the respondents. The quantitative data was analysed by use of both the descriptive and inferential statistics. Secondary data was analyzed by use of time series analysis and simple linear regression. Only the factors influencing the choice of financial products by the investment managers were investigated. The descriptive statistics involves the use of mean, frequency, percentages and standard deviation while inferential statistics entailed use of Pearson correlation and multiple regression analyses.

3.5.1 Model Specification

In order to exhibit the influence of factors affecting investment product choice of listed firms, the estimation procedure used by Hussein (2007) was adopted and modified as:

$$Y = \beta_0 + \beta_1 X_{1i} + \beta_2 X_{2i} + \beta_3 X_{3i} + e_i \quad (3.1)$$

Where: /

Y_i = is Investment product (for $i = 1 \dots 5$)

β_0 = refers to time-invariant firm-specific effects.

β_1 , β_2 , and β_3 = Coefficients.

X_1 = scores on financial information.

X_2 = Scores on Investment returns

X_3 = Scores on Third party opinions.

e = is a random disturbance.

The correlation model used in the study is: (3.2)

$$r = \frac{N\sum xy - (\sum x)(\sum y)}{\sqrt{[N\sum x^2 - (\sum x)^2][N\sum y^2 - (\sum y)^2]}}$$

Where:

- N = number of pairs of scores
- $\sum xy$ = sum of the products of paired scores
- $\sum x$ = sum of x scores
- $\sum y$ = sum of y scores
- $\sum x^2$ = sum of squared x scores
- $\sum y^2$ = sum of squared y scores

We use the symbol r to stand for the correlation.

3.6 Data Presentation

Data was presented using descriptive statistics involving the use of frequencies and percentages was used to summarize data which were presented in tables, graphs and pie charts.

CHAPTER FOUR

RESULTS AND DISCUSSIONS

4.1: Demographic Characteristics

The demographic characteristics considered were financial managers' years of service and highest level of academic qualification.

Table 4.1: Financial Managers years of experience as the investment decision makers

Years of experience	Frequency	Percent	Valid Percent	Cumulative Percent
Less than 1 year	12	21.4	21.4	21.4
1-3 years	18	32.1	32.1	53.6
Over 3 years	26	46.4	46.4	100.0
Total	56	100.0	100.0	

Source: Survey data, 2016

Table 4.1 shows the financial managers experience as the investment decision makers. The results indicate that majority 46.4 % of financial managers had worked in their respective companies for over 3 years which is an indication of low labor turnover, 21.4 % had worked for the period less than 1 year while 32.1 % had worked for a period between 1- 3 years. This implies that the data was obtained from respondents who had gotten experience on investment decisions of their organizations.

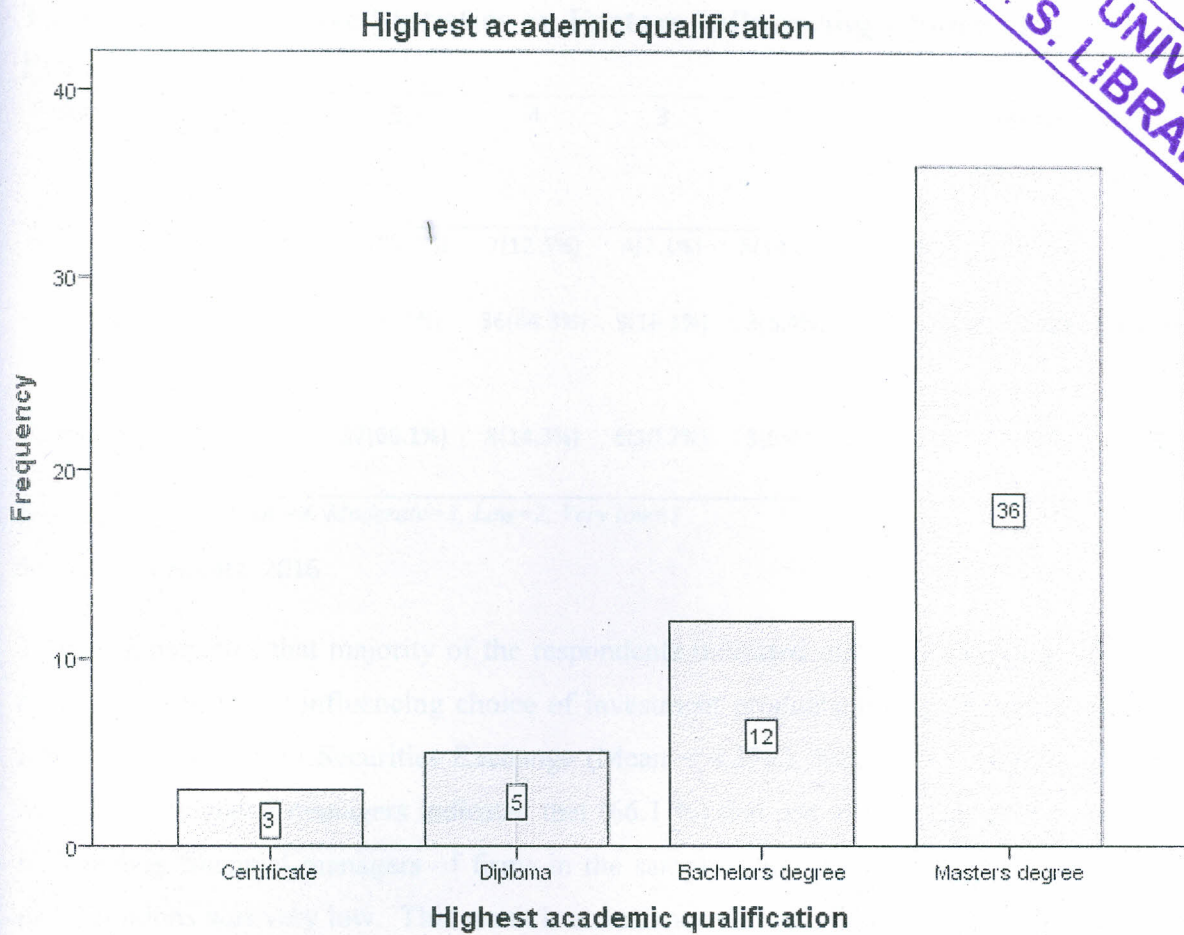


Figure 4.1: Financial Managers' Highest Academic Qualification

Figure 4.1 indicate that 36 (64.3 %) of the respondents are masters degree holders, 12(21.4%) are bachelors degree holders while only 3(5.4%) have attained certificate education level. This implies that data for the study was obtained from learned respondents who are seasoned in investment decisions hence the reliability of the data.

Table 4.2: Descriptive Statistics on Factors Influencing Choice of Investment Products

Factors	5	4	3	2	1	Mean	Std. Dev
a. Financial information	32(57.1%)	7(12.5%)	4(7.1%)	8(14.3%)	5(8.9%)	3.9464	1.43235
b. Investment returns	6(10.7%)	36(64.3%)	9(16.1%)	3(5.4%)	2(3.6%)	3.7321	0.86321
c. Third party opinions	37(66.1%)	8(14.3%)	6(10.7%)	3(5.4%)	2(3.6%)	4.3393	1.10003

Key: *Very high=5, High =4, Moderate=3, Low=2, Very low=1*

Source: Survey data, 2016

Table 4.2 indicates that majority of the respondents indicated that third party opinions was the most prevalent factor influencing choice of investment products among financial managers of firms listed in Nairobi Securities Exchange (Mean = 4.3393, Std.dev = 1.10003). Specifically, majority of financial managers indicated that (66.1 %) that use of third party opinions was very high among financial managers of firms in the sample. Only 3.6 % indicated that use of third party opinions was very low. This result is at variance with the findings of Fischer and Gerhardt (2007) who analyzed individual investor investment decision making process and found that individual investor investment decisions deviate from recommendations of financial theory in that the recommendations of brokerage houses, individual stock brokers, family members and co-workers go largely unheeded.

Table 4.3: Descriptive Statistics on Investment Products

Investment products	5	4	3	2	1	Mean	Std. Dev
a. Quoted securities	35(62.5%)	7(12.5%)	9(16.1%)	2(3.6%)	3(5.4%)	4.2321	1.17537
b. Government securities	12(21.4%)	34(60.7%)	3(5.4%)	3(5.4%)	4(7.1%)	3.5000	1.221
c. Fixed deposits	6(3.6%)	8(14.3%)	4(7.1%)	12(21.4%)	30(53.6%)	1.9286	1.23373
d. Fixed income securities	32(57.1%)	12(21.4%)	5(8.9%)	4(7.1%)	3(5.4%)	4.1786	1.19251
e. Cash and demand deposits	37(66.1%)	4(7.1%)	6(10.7%)	3(5.4%)	6(10.7%)	4.1250	1.40211
f. Immovable properties	12(21.4%)	34(60.7%)	3(5.4%)	3(5.4%)	4(7.1%)	3.8393	1.05790

Key: *Very high=5, High =4, Moderate=3, Low=2, Very low=1*

Source: Survey data, 2016

Table 4.3 indicates that majority of the respondents indicated that quoted securities was the most prevalent investment products among firms listed in Nairobi Securities Exchange (Mean = 4.2321, Std.dev = 1.17537), followed by fixed income securities, cash and demand deposits, immovable properties, government securities and fixed deposits. The results are with the findings of Krishnan and Booker (2002) that identified these as the most common investment products by individual investors.

4.2 Influence of investments' financial information on choice of investment products

To assess the influence of investments' financial information on choice of investment product, Pearson's correlation and multiple regression analyses were performed and the results are summarized in the Tables 4.4 and 4.5.

Table 4.4: Correlations of financial information and investment products

Variables	Financial Information	Quoted Securities	Government Securities	Fixed deposits	Fixed Income Securities	Cash and demand deposits	Immovable properties
Financial Information	1.000	.958**	.941**	.564**	.953**	.954**	.810**
Quoted Securities		1.000	.145	.101	.156	.153	.049
Government Securities			1.000	.164	.287	.129	.352
Fixed deposits				1.000	.228	.178	.118
Fixed Income Securities					1.000	.143	.288
Cash and demand deposits						1.000	.360
Immovable properties							1.000

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

Source: Survey data, 2016

Table 4.4 indicates that investment products had a positive and significant association with financial information ($r > .564$, $p = .000$). This implies that investment products associate positively with the use of investments' financial information. These findings are in tandem with previous studies (Nagy and Obenberger, 1994; Epstein, 1994) who report a positive association between investment's financial information and investment avenues. However, the results are at variance with the findings of Kadiyala and Rau (2004) who found a negative association between investment products and financial information. This Means that the investment's financial information positively influences choice of investment products

Table 4.5: Multiple Regression Analysis Estimation Results on the Factors Influencing Choice of Investment Products

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Collinearity Statistics	
	B	Std. Error	Beta			Tolerance	VIF
(Constant)	.089	.171		.523	.604		
Financial information	.353	.064	.430	5.479	.000	.125	7.995
Investment returns	.215	.088	.158	2.448	.018	.186	5.385
Third party opinions	.449	.100	.421	4.482	.000	.087	11.440
R	.980						
R ²	.960						
Adj.R ²	.958						
Durbin-Watson	1.88						

a. Dependent Variable: Investment Products

Source: Survey data, 2016

Table 4.5 exhibits the results of the multiple regression analysis. The results indicate that investment financial information was a positive significant predictor of investment product choice ($\beta = .353$ ($p = .000$)). This value is statistically significant since the p-value is less than 0.01. It can be inferred from this value that a unit change in investment financial information leads to an increase in investment choice of 0.353, all things being fixed. This result corroborates the findings of Nagy and Obenberger (1994) and Krishnan and Booker (2002) who found that the relationship between use of financial information and investment products was positive and significant. However, the findings are at variance with those of Kadiyala and Rau (2004) who found a negative and significant ($p = 0.001$) relationship between financial information and investment products. From the findings of objective one, it can be concluded that the investment's financial information positively influences choice of investment products made by financial manager

4.3 Effect of the investment returns on choice of the investment products

To assess the influence of investment returns on choice of investment product, Pearson's correlation analysis were performed and the results are summarized in the Tables 4.6.

Table 4.6: Correlations of investment returns and investment products

Variables	Investment returns	Quoted Securities	Government Securities	Fixed deposits	Fixed Income Securities	Cash and demand deposits	Immovable properties
Investment returns	1.000	.905**	.906**	.579**	.877**	.869**	.888**
Quoted Securities		1.000	.118	.100	.126	.078	.049
Government Securities			1.000	.124	.186	.117	.216
Fixed deposits				1.000	.228	.178	.118
Fixed Income Securities					1.000	.234	.158
Cash and demand deposits						1.000	.300
Immovable properties							1.000



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

Source: Survey data, 2016

Table 4.6 indicates that investment products had a positive and significant association with investment returns ($r > .579$, $p = .000$). This implies that investment products associate positively with the investments' returns expected from an investment. Multiple regression (Table 4.5) results indicate that investment returns was a positive significant predictor of investment product choice ($\beta = .215$ ($p = .018$)). This value is statistically significant since the p-value is less than 0.05. It can be inferred from this value that a unit change in investment returns leads to an increase in investment choice of 0.215, all things being fixed. This result corroborates the findings of Hussein, 2007 and Muswenje (2013) who found that the relationship between use of investment returns and investment products was positive and significant. From the findings of objective two, it can be concluded that use the investment returns in decision making leads to

increased investment product choices made by financial managers of the firms listed in Nairobi Securities Exchange.

4.4 Effect of third party opinions on the choice of investment products

To analyze the influence of third party opinions on choice of investment product, Pearson's correlation analysis were performed and the results are summarized in the Tables 4.7.

Table 4.7: Correlations of third party opinions and investment products

Variables	Third party opinions	Quoted Securities	Government Securities	Fixed deposits	Fixed Income Securities	Cash and demand deposits	Immovable properties
Third party opinions	1.000	.935**	.902**	.965**	.900**	.951**	.962**
Quoted Securities		1.000	.105	.309	.206	.253	.099
Government Securities			1.000	.213	.200	.179	.345
Fixed deposits				1.000	.108	.188	.210
Fixed Income Securities					1.000	.103	.328
Cash and demand deposits						1.000	.340
Immovable properties							1.000

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

Source: Survey data, 2016

Table 4.7 indicates that investment products had a positive and significant association with third party opinions ($r > .900$, $p = .009$). This implies that investment products associate positively with the use of third party opinions in investments decision making processes of listed firms.

Multiple regression analysis results (Table 4.5) indicate that third party opinions was a positive significant predictor of investment product choice ($\beta = .449$ ($p = .000$)). This value is statistically significant since the p-value is less than 0.01. It can be inferred from this value that a unit change

in third party opinions leads to an increase in investment choice of 0.449, all things being fixed. This result corroborates the findings of previous studies (Nagy and Obenberger, 1994; Francis and Soffer, 1997; and Dimitrios, 2007) who found that the relationship between use of third party opinions and investment products was positive and significant. However, the findings are at variance with those of Fischer and Gerhardt (2007) who found a negative and significant ($p = 0.001$) relationship between third party opinions and investment products. From the findings of objective three, it can be concluded that use of third party opinions leads to increase in better investment product choices among financial managers of firms listed in Nairobi securities Exchange.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

This chapter presents a summary of study findings, conclusions and recommendations based on the major findings of the study.

5.1 Summary of the Findings

From the findings of objective one, it is concluded that the investment's financial information positively influences choice of investment products made by financial managers of firms listed in Nairobi Securities Exchange. From the findings of objective two, it can be concluded that use of the investment returns in decision making leads to increased investment product choices made by financial managers of the firms listed in Nairobi Securities Exchange. Lastly, from the findings of objective three, it can be concluded that use of third party opinions leads to increase in better investment product choices among financial managers of firms listed in Nairobi securities Exchange.

5.2 Conclusions of the Study

The study concludes that the investment's financial information positively influences choice of investment products; use of the investment returns in decision making leads to increased investment product choices and use of third party opinions leads to increase in better investment product choices among financial managers of firms listed in Nairobi securities Exchange.

5.3 Recommendations

Based on conclusion of objective one, prospective investors should uphold using financial information when making choice of investment products.

From the conclusion of objective two, prospective investors should intensify considering investment returns when choosing amongst various investment products.

Similarly, from conclusion of objective three, prospective investors should evaluate and make use of third party opinions in their decisions on investment product choice.

5.4 Limitations of the Study

Based on the methodology and conceptual scope of this study, the following limitations are evident; the outcome of the study cannot be generalized to all firms in Kenya since the study was limited to listed firms in Nairobi Securities Exchange. The study adopted a correlational research design. The use of predetermined questions may have brought in biases in answering them.

5.5 Suggestions for Future Research

For purposes of improving this study, the researcher would like to suggest the following for further research. An exclusive study on the investment criteria used by listed firms in Kenya should be carried out. Future research should be conducted on determinants of investment mix of firms listed in Nairobi Securities Exchange and compare the results across the sectors in the economy.

Further research could be conducted based on external factors that influence investment performance in terms of risk-return trade off. Lastly, future research efforts could dwell on listed firms in East Africa and use more robust research designs such as panel and time series.

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