

THE EFFECT OF INDEPENDENCE OF SECURITIES FIRMS ON SHARE PRICE FLUCTUATIONS AT THE NAIROBI SECURITIES EXCHANGE

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Abstract

Fluctuations in share prices due to changes in financial fundamentals is necessary to create opportunities for investors to trade. When share price, fluctuations become erratic, investors become jittery and exit the stock exchange. Securities firms employ financial analysts who work in a world with built-in conflict of interest and competitive pressures that lead to unethical trading and unfair trading ground. The study employed a survey methodology that incorporated a quantitative model to test Analysis of Variance (ANOVA) with the Pearson Chi-Square. Seventy (72) employees who provide at least four (4) different services participated in the study. The specific objectives of the research were; engagement in proprietary trades, membership of securities firms on the securities exchange, provision of multiple services by securities firms and long-term relationships between securities firms and other market participants as these influence share price fluctuations at the Nairobi Securities Exchange (NSE). The researcher rejects the null hypothesis and concludes that independence of securities firms has significant influence on share price fluctuations at the NSE based on a p-value of 0.018. The researcher recommends that the securities exchange should engage technologies that monitor all market activities in real-time to identify potentially abusive behavior to flag it out for investigation to increase market trust.

Keywords: Share Price Fluctuations, Conflict of Interest, Insider Information, Unethical Trading, Proprietary Interests, Information Asymmetry

INTRODUCTION

There are many causes of share price volatility including information asymmetry, agency issues between investors and mutual fund managers and other market imperfections such as disparate beliefs of investors (Kraus & Smith, 1994). Abnormal share price changes are of concern to investors. This paper explored into the effect of independence of securities firms on share price fluctuations at the NSE. Enormous daily or monthly unpredictable share price movements may not be closely related to macroeconomic factors (Bodie et al., 2000). Various factors influence share price fluctuations at the global level, Africa and at the NSE, Kenya. Greed and manipulation influence the stock market and this cause investors to start dumping their shares en-masse, which accentuates market crashes (Fisher & Lowell, 2006). Speculators also massively short sell shares to take advantage of the free fall of prices to further push up supply of shares (Jackson, 2005).

The Performance of the Nairobi Securities Exchange

The NSE started in 1954 as a voluntary association of brokers with the permission of the London Stock Exchange (LSE) to facilitate mobilization of resources for long-term capital to finance investments (Obienugh, 2010)). Through time, few traders (Ngugi, Amanja & Maina, 2009), have dominated trading at the NSE. Despite measures, the Government of Kenya (GOK) has put in place, NSE has not been a good performer in recent times compared to other emerging stock markets (Chepkoiwo, 2011). Private capital inflow from foreign investors in response to declining prices improves liquidity and stock market development (Nyang'oro, 2013). Despite the economic benefits of access to foreign savings and support for financial sector development, capital inflows can cause major challenges for policy makers (IMF, 2010)

Statement of the Problem

This paper investigated into the effect of independence of securities firms on share price fluctuations at the NSE. Securities firms have membership on the stock exchange which, enables them to vote on exchange policies and this gives them opportunities to fulfill self-interest and create a potential for unethical trading (Liaw, 2004). An unfair trading floor causes retail traders to exit the stock market. The NSE index as a measure of price movement continues to fluctuate in tandem with changing prices of securities (Yenkey, 2007). In 1994, the NSE 20 share index, the oldest on the exchange was at a high of 5030 points and in 1995, it averaged 3469. The index fell to an average of 1400 points in 2001 and in August 2002, the index dipped to a low of 1043 points (Kiremu, Galo, Wagala & Mutegi, 2013). In 2010, the NSE 20

share index, rose by 36.5 percent to close at 4432.6 points from 3247 points in 2009 (Kenya Economic Report, 2011).

In the years 2008, 2007 and 2006, the index averaged 3521, 5444 and 5646 respectively. The changes in percentage terms vary at -35.3% and -3.6% for 2008 from 2007 and for 2007 from 2006 respectively (KNBS, 2011). Comparative studies, just to mention a few: Aroni (2011), Muthike and Sakwa (2012), Olweny and Omondi (2012) and Kimani (2013) focus on macro and micro-economic variables that cause share price fluctuations. These studies fail to consider that fluctuations in share prices may go beyond economic variables, to incorporate actions of some market participants. Most of the research on share price fluctuations is on stock markets in developed countries.

Study Objective

The general objective of this study was to examine the effect of independence of securities firms on share price fluctuations at the NSE.

Specific Objectives were:

1. To determine the effect of engagement in proprietary activities by securities firms on share price fluctuations at the NSE.
2. To determine the effect of membership of securities firms on the securities exchange on share price fluctuations at the NSE.
3. To determine the effect of provision of multiple services by securities firms on share price fluctuations at the NSE.
4. To determine the effect of long-term relationships between securities firms and other market participants on share price fluctuations at the NSE

Research Hypotheses

HO1. Engagement in Proprietary activities by Securities Firms has no significant effect on share price fluctuations at the NSE

HO2. Membership of Securities Firms on the Securities Exchange has no significant effect on share price fluctuations at the NSE

HO3. Provision of Multiple Services by Securities Firms has no significant effect on share price fluctuations at the NSE

HO4. Long-term relationships between Securities Firms and other market participants has no significant effect on Share Price fluctuations at the NSE

LITERATURE REVIEW

Theoretical Framework

The price of a share may change rapidly from time to time and be said to be volatile (Brunetti, Buyuksahn & Harris, 2011). To estimate an indicator that is not stable is challenging not only for investors but also for the economy as a whole (Kotze, 2005). The theory that follows, provides insight into share price variations.

Fundamental Analysis

Fundamental analysis involves portfolio management and the aggregate market, industry and company analyses. Active managers time the equity market and can shift funds among different equity shares and other securities and industries before the rest of the market does. Equity managers can do stock-picking by looking at individual issues in an attempt to find undervalued and overvalued shares to buy low and sell high (Bodie et al., 2008). The security analyst or the prospective investor is primarily interested in analyzing factors such as economic influences, industry performance and pertinent company information related to product demand, earnings, dividends and management (Thomsett, 2006). The analyst uses such information to calculate an intrinsic value for the firm's securities. The investor then reaches an investment decision by comparing the intrinsic value with the current market price of the security (Thomsett, 2006).

Fundamental analysis allows investors to find "good" companies so they lower their risk premium and probability of loss. Prices of "bad" companies rise and fall creating opportunities for profits. Fundamental analysis allows one to make own decision on value and to ignore the market (Nincic, 1999). If the prevailing market price differs from the estimated intrinsic value by an amount enough to cover transaction costs, an analyst will buy if the market price is substantially below intrinsic value and sell if it is above (Jones, 2004). Investors who engage in fundamental analysis believe that occasionally, the market price and the intrinsic value differ but eventually investors recognize the discrepancy and correct it by a trade (Thomsett, 2006). Those investors who have superior estimation techniques consistently make superior market timing decisions. Investors acquire undervalued securities and generate above average returns (Bodie et al., 2008).

The vast majority of investors cannot consistently get new information before other investors, consistently process it correctly and quickly to make above average returns (Vause, 1997). Fundamental analysis depends on financial accounting statements that make the major source of information about the past performance of a firm or industry. Accounting statements lack a great deal of information needed by securities analysts. According to the generally accepted accounting principles (GAAPs), companies can choose among several procedures for

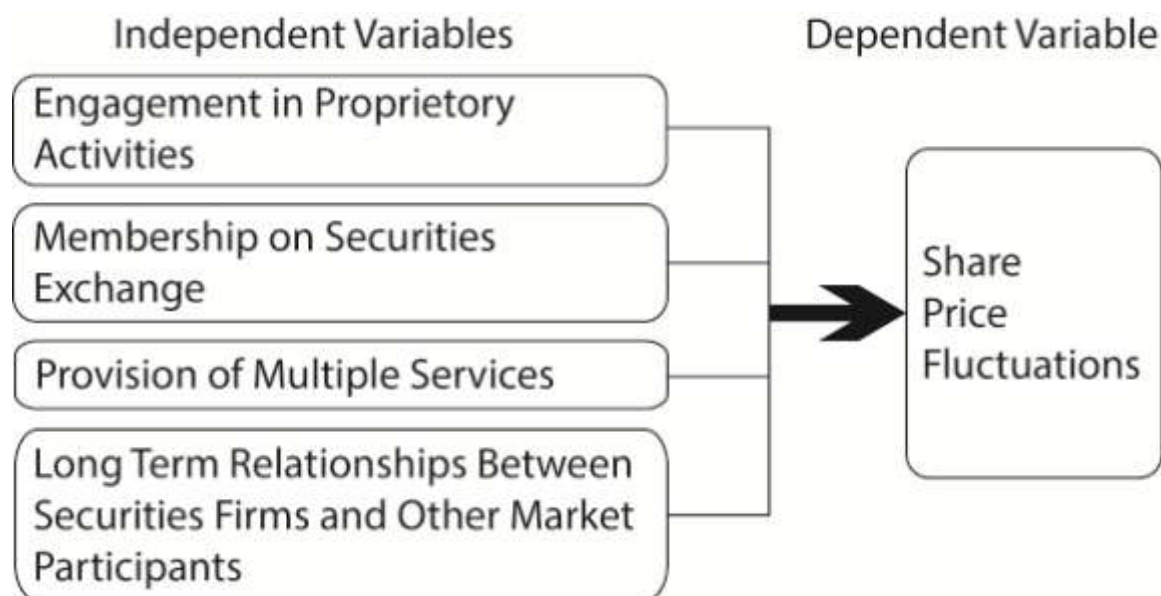
reporting expenses, assets or liabilities (Bourne & Bourne, 2011). Notably these alternative procedures can produce vastly different values for expenses, income, return on assets and return on equity. As a result, an investor can have trouble comparing the statements of two firms in the same industry, much less firms in different industries (Bourne & Bourne, 2011). Many psychological factors and other non-quantifiable variables do not appear in financial statements.

Conceptual Framework

The research involved investigation into the effect of independence of securities firms on share price fluctuations at the NSE as the dependent variable. Fluctuating share prices represent risk of the share value deviating from their equilibrium values (Mishkin, 2007). The factor postulated in this research, to influence erratic share price fluctuations at the NSE is the independence of securities firms, which refers to freedom from outside control or potential conflict of interest. Outside control, leads to an unfair investment field where share prices may be manipulated (Hopt & Wymeersch, 2005) and conflict of interest refers to competitive pressures (Jackson, 2005).

Five pre-coded response categories on a Likert-Scale measured the relationships between the concept and its relationships to the fluctuations of share prices at the NSE. Research participants responded to a set of questionnaire items in a survey. The following conceptual model in figure 1 summarizes the relationship between the constructs and the fluctuations of share prices at the NSE.

Figure 1. Conceptual Framework



Independence of Securities Firms and its Effect on Share Price Fluctuations

For a securities market to function smoothly, several institutions are involved. The institutions include brokers, dealers, investment banks and an organized exchange (Madura, 2011). The institutions act on behalf of clients, and also take positions of their own, more commonly referred to as proprietary trading that creates conflict of interest (Mishkin & Eakins, 2009). Brokerage firms have membership on stock exchanges, which allow them to vote on exchange policy, giving them opportunities to fulfill self-interest (Ohad, Madureira & Wang, 2009). Technological advances create new products that expand the scope of investment banking to include other activities that create potential for unethical trading (Liaw, 2004). Collaboration in merging financial services leads to collusion to undercut the stock market (Kidwell, Blackwell & Whidbee, 2005).

Provision of Overlapping Services and Conflict of Interest and their Effect on Share Price Fluctuations

Investment analysts assist with due diligence, research into the company whose shares are on offer, participate in investor road shows and help shape the offer deal (Cowen, Groysberg & Healy, 2006). Upbeat research reports and positive recommendations published after the offering is completed may “support” the new share issue. Client companies prefer favourable research reports and unfavourable analysts’ reports may hurt the firm’s efforts to nurture a lucrative long-term investment banking relationship (Cowen et al, 2006). Positive research reports induce a company to hire an investment bank that provided the report to underwrite securities and in the process, attract new business (Roni & Womack, 1999).

A company might be unlikely to hire an underwriter to sell its shares if the firm’s analyst has a negative view of their share. Hence, this impairs the credibility of analysts’ recommendations and influences share prices (Krugman, Shaw & Womack, 2001). At times analysts participate in employee share-purchase pools in companies (Lin & McNichols, 1998). There is a growing trend of venture investing where analysts or colleagues may acquire a stake in a start-up firm by obtaining discounted, pre-IPO shares. Such prices allow an analyst or the firm he works for to profit from owning securities in companies they cover (Mishkin & Eakins, 2009). According to Asquith, Mikhail and Andrea (2005), analysts exert considerable influence at the stock market. Analysts’ recommendations or reports can influence the price of a company’s share especially when such reports are widely disseminated through the electronic and the print media (Clarke & Subramanian, (2006).

Many analysts work in a world with built-in conflicts of interest and competitive pressures. The sell-side firms want their individual investor clients to be successful over time (Jackson, 2005)).

Satisfied long-term investors are a key to a brokerage firm's long-term reputation and success. There are queries on recent investment banking practices especially independent research. In the aftermath of Enron, observers queried how it was possible for research analysts to fail to discover the types of, off-balance sheet transactions the company was engaging in (Bodie et al, 2008; Mishkin & Eakins, 2009). Information leaked that the sell-side independent analysts recommended shares underwritten by their banks.

According to Odugbemi & Jacobson (2008), malpractices occur, where an investment bank oversees an issue while a business department of the same bank trades in those shares prior to an issue of the company. There are circumstances where analyst compensation for research work and investment banking businesses are connected (Lin & McNichols, 1998). Mallov et al. (2010), argue that share recommendations and research reports by securities analysts in major investment banking firms are usually overly optimistic. Very few analysts recommend that investors sell a share. The reasons for such advice emanates from unwillingness to say anything bad (Cowen, Groysberg & Healy, 2006). According to Roni and Womack (1999), if broker-dealers fail to identify, prevent and manage conflict of interest between brokerage and dealing business of the firm, there is the possibility of prejudicing the execution of client orders in favour of proprietary interests.

According to Chakravarty (2001), due to information asymmetry, investors may not know as much about securities offered for sale by firms as firm insiders such as brokers and dealers. When price-setting, mechanics settle on average prices for all securities based on lack of information, good securities disappear from the market and only poor and overpriced securities will be available for sale (Fishman & Hagerty, 1992).

With only poor securities offered for sale, the average price would fall. A market can eventually fail as the quality as well as the price of securities available on that market is low (Seyhun, 1986). When an investment bank serves two clients, one for research on possible investment and the other for underwriting, the bank serves both the issuer and the buyer at the same time (Clement, 1999). The issuer receives optimistic biased research and the buyer also gets the same information, yet proper unbiased information is required for the buyer (Clement, 1999). When potential underwriting revenues substantially exceed potential revenues from brokerage, the bank has an incentive to alter information to favour the issuing firm's needs (Mishkin, 2007).

Through the formation of investment pools and relationships with securities firms, investors manipulate the market (Hopt & Wymeersch, 2005). A group of investors may band

together and spread negative and damaging information to decline share prices. They may also spread positive false information to raise share prices. The intention of spreading false information to drive share prices down and up would be to purchase and later sell these shares (Bhattacharya & Daouk, 2002).

Insider Trading and its Effect on Share Price Fluctuations

According to Estrada (1995), one common way of abusing one's office position is through insider trading. What causes injury or loss to outsiders is not what the insiders knew or did; rather what the outsiders did not know. Their lack of knowledge exposes them to risk of loss, or denies them an opportunity to make a profit (Pike & Neale, 2006). Fisher and Robe (2004), argue that policy makers and commentators are concerned by the fact that insider trading undermines public confidence in the securities markets. If investors fear that insiders regularly profit at their expense, they will not be nearly as willing to invest (Fisher & Robe, 2004). Companies prefer that their securities trade in "thick markets" with many traders who have substantial capital and opportunities to trade at readily observable prices (Haddock & Macey, 1987).

An efficient securities market requires a level informational playing field. Speculators who contribute to the liquidity of the securities market and investors who invest their money will not be frightened away (Fishman & Hagerty, 1992). According to Moore (1995), there are those who support insider trading by arguing that, it is good for the market. The proponents argue that this accelerates the flow of both positive and negative information about a share to other investors. As a result, this information is absorbed in the share price, which is healthy for the market (Shaw & Barry, 2010). The proponents believe that since commentators do not cast aspersions on insider traders in markets for fine art, cattle, real estate, professional athletes and such other activities with substantial variations in price, the same applies to share trading (Shaw & Barry, 2010).

People with intimate knowledge about the worth of an asset can trade to cause price discovery (Shaw & Barry, 2010). According to Fisher and Robe (2004), an individual who has information, as an insider is guilty of insider-dealing, if in the circumstance of his function, he deals in securities that are price-affected securities in relation to the information (Haddock & Macey, 1987). Long-term relationships established among money managers, data vendors, company executives, investors and analysts may result in provision of background information from insiders to major investors or potential investors in the company (Weegen & Assmann, 1994).

Empirical Review

There is minimal research on erratic share price fluctuations in Africa, more so in Kenya. Research work by Aduda, Musila and Onsongo (2010) investigates the determinants of NSE market development. The researchers observe various macro-economic factors that include institutional quality to influence share price fluctuations at the NSE. Their investigation uses regression analysis and reveals that institutional quality represented by law and order, bureaucratic quality and democratic accountability in conjunction with corruption index are important determinants in stock market development.

Research by French and Roll (1986) shows that share volatility is higher during trading hours than during non-trading hours because public information is more likely to be, communicated during regular business hours. The share price captures private information through active trading when the exchange is open to increase volatility.

Critique of the Review

Fundamental analysis uses financial statements to forecast intrinsic values of shares. It is impossible to reflect all information about a firm in financial statements. The determinant of share price fluctuations in the study is the independence of securities firms. Securities firms provide multiple clients with diverse services. Subsequently, this has the effect of increasing revenues for these firms, a fact that creates conflict of interest. Securities analysts are not the only ones to blame for market inefficiency. The clients should also accept responsibility for compromising securities firms.

Research Gaps

Investors make systematic errors in processing information, a fact that makes them susceptible to exploitation by others. Investors, more so individual investors buy shares that recently caught their attention. Research on determining susceptibility to specific biases in trading of shares on the NSE is necessary. Investment advisors can utilize such a research to incorporate behavioral attributes into their wealth management practices.

Advisors can also apply diagnostic tests by use of diagnostic questions to determine the appropriate kind of investment for each investor. Use of mean-variance to determine standard portfolios, can be discarded in favour of investments derived from natural psychological preferences.

RESEARCH METHODOLOGY

Research Design

Survey research methodology employed a quantitative model testing that incorporated statistical analysis on opinions of research participants. The survey methodology provides description of items by interrogating participants selected on sample basis (Bryman, 2004).

Target Population and Sampling Frame

The researcher investigated a population of all the employees of active brokerage firms and investment banks at the NSE. The decision to use securities firms was because this group is knowledgeable with the functioning of the stock exchange. The sampling frame for the survey had all the technical employees of the brokerage firms and investment banks at the NSE as at the end of December 2012. The researcher interrogated seventy-two (72) respondents, selected on the basis of convenience (purposive sampling) to secure opinions of employees of securities firms supplying at least four different services including fund management, research, investment banking and financial analysis.

Data Collection and Analysis Methods

A self-administered questionnaire enabled the collection of data. The questionnaire design had statements and questions constructed to match the research objective. The questions in the questionnaire were close-ended to quantify data as per the researcher's response categories.

Data analysis entailed editing, coding and tabulation of primary data into manageable summaries. Data analysis entailed descriptive and inferential statistics using SPSS. Charts and tables with cross tabulations between the response and the respondent presented the data. Analysis of Variance (ANOVA) tested for the significance of the differences between more than two sample means (Levin & Robin, 2006). Variance analysis used the Pearson's Chi-square analysis, simple regression between each independent variable and share price fluctuations at the NSE and cross-correlation analyses to determine the strengths of relationships. The F-distribution table utilized confidence levels set at 95% or 5% significance.

ANALYSIS AND FINDINGS

Response Rate

The case processing summaries indicate that 61 out of 72 respondents, representing 84.7% response rate was utilized. The response rate is considered very good (above the threshold of 70%) and representative of the target population for the purpose of making generalization to the larger population (Punch, 2003).

Descriptive Statistics on the effect of independence of securities firms on share price fluctuations at the NSE

Most of the respondents at 49.2% support the statement that brokerage firms can improve their financial performance if they engage in proprietary activities at the NSE. Respondents at 19.7% dispute the statement. The results are in agreement with the arguments of Mishkin and Eakins (2009) that extreme competition at the market makes brokerage firms to take positions of their own in trading. Research participants at a response rate of 60.6% support the opinion that brokerage firms should have membership on the stock exchange to enable them vote on exchange policies. Ohad, Madureira and Wang (2009) negate this proposition by arguing that to vote on exchange policy gives firms opportunities to fulfil self-interest.

Majority of respondents at 54.1% affirm the proposition that brokerage firms should offer multiple services to remain relevant in the competitive world. Odugbemi and Jacobson (2008) argue that malpractices are likely to occur where overlapping services are provided. The two researchers refer to circumstances where an investment bank underwrites a share and a department in the same organization trades on the same share leading to conflict of interest. Respondents at 73.8% support the assertion that long-term relationships established among investors, company executives and financial analysts make them dialogue and exchange background information easily. The statement is in line with the argument by Weegen and Assmann (1994) that the “hallow effect” eases the provision of background information to potential investors thus creating a trading background that is not level.

Table 1: Descriptive Statistics on the effect of Independence of Securities Firms on Share Price Fluctuations at the NSE

	Performance by Proprietary	Brokerage Firms performance	Membership of Brokerage firms encourage	Long term relationships ease exchange of information
Strongly Disagree	3.3	4.9	4.9	3.3
Disagree	16.4	9.8	14.8	6.6
Neutral	31.1	24.6	26.2	16.4
Agree	29.5	42.6	34.4	57.4
Strongly Agree	19.7	18.0	19.7	16.4
Total	100.0	100.0	100.0	100.0

Normality tests

Normality tests were conducted and the results are shown in Table 2. The model passed the Jarque-Bera normality test with a p-value of 0.943, suggesting that the errors are normally

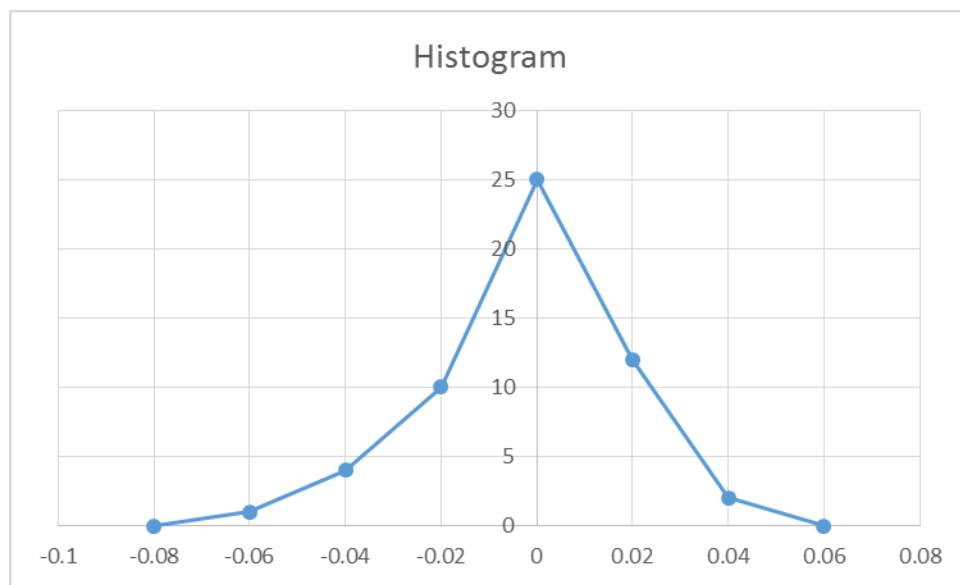
distributed. The RESET test indicated that the model was correctly specified with a p-value of 0.192. It is therefore on the basis of these tests that it was reasonable to claim that the models had a good statistical fit.

Table 2: Results of the Diagnostic Tests for the Model

Test Statistics	LM Version
Normality	CHSQ[2] = 0.118(0.943)

Note: p-values in parenthesis Based on a test of skewness and kurtosis of residuals

Figure 2: Histogram for data normality



The histogram plot was obtained by placing the data in regularly spaced cells and plotting each cell frequency versus the centre of the cell. The Figure 2 shows the histogram of residuals. The histogram illustrates an approximately normal distribution of residuals produced by the models through a calibration process.

Inferential Tests: Regression Analysis for the effect of Independence of Securities Firms at the NSE

Four (4) questionnaire item (X_{is}) were used in this variable to create the following equation that displays the beta coefficients (β_{is}) in both magnitude and direction.

$$Y = 2.553 - 0.120X_1 - 0.112X_2 - 0.031X_3 + 0.050X_4 \dots \dots \dots \text{Equation 1}$$

Where: Y= Share Price Fluctuations at the NSE

From the table β_0 is 2.553, which is interpreted to mean that when brokerage firms fail to engage in any of the activities mentioned in table below, the share price will stabilize at 2.553 as all X_{is} are equal to zero. The other **beta-values**, the slopes of the regression lines are; $\beta_1=-.120$, $\beta_2=-.112$, $\beta_3=-.031$ and $\beta_4=.050$. The implication is that if brokerage firms engaged in proprietary activities; have voting rights on the policies of the securities exchange and offered multiple services to remain relevant in a competitive world, the share price will decline by 0.120, 0.112 and 0.031 respectively for every unit increase in these predictor variables. Dialogue and ease of exchange of information among investors, company executives and analysts based on long-term relationship they have will cause the share price to rise by 0.050.

The researcher rejects the null hypothesis based on the questionnaire items and concludes that the independence of securities firms has significant influence on the fluctuations of share prices at the NSE, given $p = 0.018 < 0.05$. The results agree with the argument of Jordan (2005) that many financial analysts work in a world with built-in conflicts of interest and competitive pressures that lead them to operate in an unethical manner that lowers their independence in decision-making and this subsequently aids market manipulation. The higher the independence of securities firms, the better the stability in share prices.

Table 3: Results of Coefficients of Regression Model

Model	Unstandardized Coefficients		Standardized Coefficients		Sig.
	B	Std. Error	Beta	T	
1 (Constant)	2.553	1.040		2.453	.018
Brokerage Firms performance	-.120	.175	-.113	-.684	.497
Membership of Brokerage firms encouraged	-.112	.138	-.118	-.813	.420
Research Analysts earnings	.222	.160	.240	1.388	.172
Long term relationships ease exchange of information	.050	.199	.038	.251	.803

a. Dependent Variable: Share price fluctuations

Reliability Tests

According to Sekaran (2003) the external or internal reliability depends on consistency. Sekaran (2003), states that the reliability of a measure is an indication of the stability and consistency with which the instrument measures the concept and helps to assess the goodness of a measure. Validity, on the other hand is concerned with the extent to which an instrument

measures what it purports to be measuring. Reliability can be investigated directly from the test data. Judgment is required in assessing the validity of a measuring instrument and a measure that has validity will also have reliability (Sekaran, 2003). Of the four methods used to measure reliability, internal consistency is the most commonly used in assessing survey instruments and scales and hence it is the one used for this study.

Internal consistency is an indicator of how well the different items measure the same concept. This is important since a group of items purporting to measure one variable should indeed be clearly focused on that variable (Nunnally, 1978). The Cronbach's alpha (α) coefficient measures internal consistency reliability among group of items combined to form a single scale (Sekaran, 2003). It is a statistic that reflects the homogeneity of the scale of measurement. Generally, reliability coefficients of 0.70 or more ($\alpha \geq 0.70$) are considered good (Nunnally, 1978) and that was the benchmark used for this study.

The independence of securities firms has a Cronbach's alpha of 0.764, which is higher than the threshold of 0.700 and is considered to be good. None of the items could be deleted as this will lead to the lowering of the coefficient of reliability as shown in table below.

Table 4: Independence of Securities Firms Related Determinants Reliability Statistics

Cronbach's Alpha	Cronbach's Alpha Based on Standardized Items	N of Items
.759	.764	4

Table 5: Statistics for Independence of securities Related Determinants

	Cronbach's Alpha if Item Deleted
Brokerage Firms performance	.785
Membership of Brokerage firms encouraged	.726
Provision of multiple services	.509
Long-term relationships among stakeholders	.751

DISCUSSION OF FINDINGS

The effect of Independence of Securities Firms on Share Price Fluctuations on the NSE

The results of the research on the independence of securities firms broken shows that independence of securities firms has a significant influence on share price fluctuations at the NSE. To this effect the researcher rejects the null hypothesis based on a p-value of 0.018 to show that the regression model predicts share price fluctuations at the NSE.

The results support the argument by Jordan (2005) that many financial analysts work in a world with built-in conflicts of interest and competitive pressures that lower their independence in decision-making. Such an environment aids market manipulation and leads to erratic share price fluctuations.

Fundamental analysis theoretical framework supports the results of the study in the sense that equity managers in brokerage firms do stock-picking and analyse the issues to find undervalued and overvalued shares to buy low and sell high (Bodie et al., 2008). Fundamental analysts allow investors to make their own decisions on values of shares and ignore the market values (Nincic, 1999).

Employees of securities firms have real-time access to information on client orders and prices of shares compared to other market participants thus creating an unfair trading ground. These employees have non-public information that can enable them front-run orders placed by other investors. In circumstances where investors have accounts with the brokerage firms, employees of such firms may trade on these accounts by “buying and dumping” frequently for their own benefit without the knowledge of the account holders. The high frequency of trading leads to share price fluctuations that are erratic.

Institutional investors and investment pools can work in cohorts with brokerage firms to create a false appearance of the market activity by entering multiple non-bonafide orders on one side of the market at increasing or decreasing prices depending on whether their intention is to induce others to buy or sell at the prices fixed by the non-bonafide orders. The traders who have an undue advantage over others can place and execute orders shortly before the close of trading on any day to artificially affect the trading price of a share. Such traders can place successive small-amount “buy orders” in increasing prices to stimulate demand.

Mishkin and Eakins (2007) observe that brokerage firms’ pursuit of proprietary interest when at the same time trading on behalf of clients can motivate the firms to trade on insider information. The firms will not act in the best interest of the public to protect investors. A broker-dealer who fails to identify and prevent conflict of interest is likely to prejudice the execution of clients’ orders in favour of proprietary interest (Roni & Womack, 2008). As mentioned earlier, securities firms have price and order information since they are directly connected through their servers to securities exchanges. As a trader, a brokerage firm has a competitive advantage that will enable it earn excess returns and to act in the interest of a client would be a secondary objective. The right of securities firms to vote on exchange policy is subject to abuse to give the firms an edge over other traders. The securities firms will vote to fulfil self-interest (Ohad, Madeira & Wang, 2009).

CONCLUSIONS

The study established that independence of securities firms influences share price fluctuations at the NSE. Brokerage firms have access to real-time trading information that puts them at an advantage over other traders. Access to information that is not available to other traders creates an unfair trading ground. Fundamental analysis supports this results as it enables financial analysts to assist investors to make their decisions on market values of shares (Bodie eta al., 2008).

RECOMMENDATIONS

Upholding Liquidity at the NSE through Fair Trading

There is need for technologies that can monitor all market activities in real-time to identify potentially abusive behavior to flag it out for investigation to increase market trust. There should be audit trail data across the market for regulators to identify all activities that take place at the market such as direct market access and high frequency trading. The process enables the detection of market manipulation and other abusive strategies. Audit trail can prevent market manipulators from hiding their identities. A level and fair playing ground for all market participants at the stock market is important to uphold liquidity and more activity at the NSE.

If all investors receive, better spreads or returns rather than brokers and their accomplices receiving abnormal returns through illegal practices such as 'dump and pump' and 'trash and cash' price manipulation, frontier and emerging markets can build volume. Standardization of information at the stock market will make it difficult for market manipulators, to survive and thrive. Pricing efficiency is achievable in financial markets that are transparent, stable and less susceptible to disruptions. Detection, investigation and prosecution of market manipulators who create artificial appearance of the market will discourage the misleading transactions.

Recommendations for Further Research

In making investment decisions, psychology plays an important role as it influences human emotions and cognitive error that leads to irrational markets and erratic share price fluctuations. Being aware of the pertinent psychological biases is critical in finding success in investment at the stock market. A lot of research has been carried out on how economic and political factors affect the performance of the NSE. There should be further research on the intertwining of psychology and finance to explain individual investment decision-making. Specifically, there should be an empirical investigation into the effect of too frequent trading on share prices at the

NSE. Such an inquiry is possible if one can determine what an excessive trading volume is for traders who own discount brokerage accounts.

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