Earnings Quality and Firm Value Among Non-Financial Listed Firms in the Nairobi Securities Exchange

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Abstract:

Purpose*: The purpose of this study was to determine the effect of earnings quality on firm value among non-financial firms listed on the Nairobi Securities Exchange (NSE). The study was anchored on Signaling Theory, which posits that high-quality financial information serves as a credible signal of firm performance to investors.*

Methodology: *The study adopted a positivist research philosophy and employed an explanatory longitudinal research design. The target population comprised 40 non-financial firms listed on the NSE, of which 33 met the inclusion criteria between 2015 and 2024. Using 330 firm-year observations derived from audited financial statements, panel data were analyzed using descriptive statistics and fixed-effects regression models in STATA to evaluate the relationship between earnings quality and firm value.*

Findings: *The results revealed that earnings quality had a positive and statistically significant effect on firm value ($\beta = 1.363$, $p < 0.001$). This finding indicates that firms reporting transparent, consistent, and sustainable earnings achieve higher market valuations, suggesting that earnings quality is a key determinant of investor confidence and firm valuation in the Kenyan capital market.*

Conclusion: *The study concludes that high-quality earnings provide credible signals about managerial competence and financial stability, thereby enhancing investor confidence and firm value. Consistent and transparent financial reporting practices strengthen firms' reputation and market credibility, leading to improved performance and shareholder value.*

Value*: This study contributes to the empirical understanding of the relationship between financial reporting quality and firm valuation in emerging markets. It provides practical recommendations for managers to adopt consistent accounting policies, strengthen internal controls and audit oversight, and improve disclosure practices. Furthermore, regulators such as the Capital Markets Authority (CMA) and the Institute of Certified Public Accountants of Kenya (ICPAK) should reinforce compliance with international reporting standards to enhance financial transparency. Theoretically, the findings validate Signaling Theory by demonstrating that credible financial reporting acts as a market signal of reliability and long-term stability, influencing investor decision-making in developing capital markets such as Kenya.*

Keywords: *Earnings Quality, Firm Value, Non-Financial Firms, Financial Reporting*

Paper Type: *Research Article*

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1. Introduction

The primary Firm value represents the total worth of a company and serves as a central indicator of its financial health, investor appeal, and long-term performance. It is commonly measured through market capitalization, debt, and cash holdings, or by using Tobin's Q, which captures both past and expected future performance. High firm value reflects efficient management, sound financial decisions, and investor confidence, while low firm value signals potential governance or reporting weaknesses. Prior research emphasizes that firm value embodies not only the firm's profitability but also its capacity to create sustainable wealth for shareholders and attract new investors (Shuaibu et al., 2019; Bhullar, 2017; Gartenberg et al., 2019).

In the modern knowledge-based economy, earnings quality has become a critical determinant of firm value and competitiveness. High-quality earnings promote transparency, accountability, and confidence among stakeholders, while low-quality earnings often linked to manipulation or bias undermine investor trust and distort market valuation. Transparent financial reporting reduces information asymmetry between management and stakeholders, thereby facilitating better investment decisions and improving access to capital (Koo et al., 2017; Ogundajo et al., 2023). As a result, firms that maintain reliable earnings reporting tend to experience enhanced valuation, reduced financing costs, and stronger reputations in capital markets.

Earnings quality serves as a measure of the reliability and relevance of financial information used in decision-making. It captures how faithfully financial statements reflect a firm's performance and its ability to generate future earnings (Dechow et al., 2010; Fassas et al., 2023). High-quality earnings are characterized by minimal manipulation, consistency, and faithful representation of transactions, while poor-quality earnings may arise either from opportunistic managerial behavior or from inherent business model volatility (Norrman et al., 2013; Al-Haddad & Al-Ghoul, 2023). The absence of manipulation enhances decision usefulness and strengthens the credibility of reported financial information, thereby linking earnings quality directly to firm value.

Despite the recognized importance of financial reporting quality, empirical evidence on its impact on firm value remains limited and inconclusive, particularly in developing markets. In Kenya, the Nairobi Securities Exchange (NSE) has experienced significant fluctuations in firm value, with persistent declines in market capitalization and share indices over the past decade. The NSE 20 Share Index fell from 6,161.46 points in 2006 to 1,004.70 points in 2022, and several firms such as ARM Cement and Deacons (EA) collapsed or were delisted. These trends reflect deeper structural issues related to transparency, governance, and investor confidence, exacerbated by political uncertainty and external shocks such as the COVID-19 pandemic.

Overall, quality earnings play a pivotal role in shaping firm value by influencing investor perceptions, information asymmetry, and managerial behavior. Firms with high earnings quality typically enjoy greater investor trust, improved capital access, and sustainable market performance (Trinh et al., 2022; Harjanto, 2023). However, the inconsistency of prior findings points to the need for further empirical investigation into how accruals quality affect firm value within Kenya's capital markets. This study therefore contributes to the literature by examining these relationships among non-financial firms listed at the NSE, addressing the contextual gaps left by earlier research.

2. Theoretical Review

The relationship between earnings quality and firm value among non-financial listed firms in the NSE can be comprehensively explained through the lens of Signaling Theory. Originating from Spence (1973), the theory posits that firms convey credible signals to external stakeholders to reduce information asymmetry. In the corporate context, financial reporting serves as a key signaling mechanism through which management communicates the firm's intrinsic performance and stability to investors (Lu et al., 2024). High-quality earnings reporting signals managerial competence, operational efficiency, and long-term financial soundness, thereby increasing investor confidence and enhancing firm value (Bae et al., 2018). When financial statements are transparent and accurately reflect a firm's economic reality, they provide investors with reliable information to make informed decisions, reducing uncertainty about future performance. Conversely, poor earnings quality often linked to earnings manipulation or aggressive accounting sends a negative signal to the market, eroding investor trust and leading to undervaluation. For NSE-listed non-financial firms, where information asymmetry remains a challenge, maintaining high earnings quality becomes essential for building credibility and attracting investment (Mohammadiyan, 2024).

Empirical and theoretical evidence reinforces that firms with high earnings quality are better positioned to command higher firm value because investors interpret reliable earnings as an indication of sustainable profitability and effective governance (Tulhasanah & Nikmah, 2017). From the signaling perspective, quality earnings reports not only reflect the firm's past performance but also serve as predictive indicators of future cash flows and stability. As investors depend heavily on financial disclosures in their valuation decisions, consistent and high-quality earnings reporting reduces the perceived risk premium associated with investment, thereby raising market valuation. In the context of the NSE, where corporate governance standards and disclosure practices continue to evolve, signaling theory underscores the pivotal role of earnings quality as a trustworthy communication tool between management and investors. Firms that prioritize transparency and integrity in their financial reporting send strong positive signals to the market, leading to improved investor perception, reduced information asymmetry, and ultimately, higher firm value.

3. Empirical Review (Hypothesis Development)

Empirical studies across various markets have demonstrated a consistent link between earnings quality and firm value, though the magnitude and direction of the relationship vary across contexts. For instance, Intara et al. (2024) investigated firms listed in the Stock Exchange of Thailand's property and construction sector and found a statistically significant positive relationship between earnings quality and firm value. Similarly, Darmayanti et al. (2023), using data from financial firms on the Indonesia Stock Exchange, confirmed that higher earnings quality enhances firm valuation by promoting transparency and reliability in financial reporting. These findings suggest that firms with credible earnings attract greater investor confidence, leading to improved market performance.

Extending this evidence, Fassas et al. (2023) conducted a multi-country analysis involving 5,002 non-financial firms across 37 European nations between 2004 and 2019. They employed a multifactor measure of earnings quality encompassing accruals, cash flows, and operating efficiency. The results indicated a significant positive relationship between earnings quality and firm valuation, further showing that institutional governance quality and market development strengthen this relationship. Likewise, Asimakopoulos et al. (2020) found that

investors in the Athens Exchange placed a premium on firms with high-quality earnings, reinforcing that transparent and consistent financial reporting enhances firm value through investor trust and market credibility.

In emerging markets, similar trends have been observed. Dang et al. (2020) examined Vietnamese listed firms from 2010 to 2018 and established that earnings quality positively influences firm value. Their results also highlighted that firm size, asset investment, and dividend payout positively contribute to valuation, while leverage and revenue volatility diminish it. Correspondingly, Fajrina et al. (2022) emphasized that the adoption of improved accounting standards and the reduction of earnings management significantly strengthen the relationship between reported earnings and firm value. These findings underscore that high-quality earnings reporting serves as an essential mechanism for value creation, especially in markets where investor protection and disclosure standards are still developing.

Contrastingly, Cristina and Yasa (2024) found that earnings quality, measured using discretionary accruals, did not significantly affect firm value among Indonesian firms, although dividend payout exhibited a strong positive influence. This suggests that while financial reporting quality remains vital, other factors such as dividend policy, firm size, and leverage can mediate its impact on firm value. Overall, the reviewed studies largely support the premise that credible, high-quality earnings reporting strengthens investor confidence and firm valuation. Guided by this evidence, the current study hypothesizes that:

H_2: *Earnings quality has significant effect on firm value of non-financial firms listed in the NSE*

4. Methodology

The study adopted a positivist research philosophy and an explanatory longitudinal research design to examine the causal relationship between financial reporting quality, agency cost, dividend payout, and firm value among non-financial listed firms on the NSE. The positivist approach emphasized objective measurement and empirical validation of relationships between variables using quantitative data. The explanatory design enabled the identification of cause-and-effect relationships, while the longitudinal element allowed for the analysis of firm performance trends over a ten-year period (2015–2024). This design was appropriate because it utilized secondary panel data drawn from audited financial statements, which provided reliable, time-based evidence of how financial reporting quality and related factors influence firm value.

Sampling

The target population consisted of 40 non-financial companies listed on the NSE as of December 2024, covering various sectors including agriculture, manufacturing, construction, energy, and telecommunications. To ensure data completeness and consistency, the study applied purposive sampling, selecting only firms that had continuously traded on the NSE and maintained complete audited financial records for the entire ten-year period. As a result, 33 firms met the inclusion criteria, yielding a total of 330 firm-year observations (33 firms × 10 years). This sampling approach ensured that the selected firms were representative of the non-financial sector and provided high-quality, longitudinal data for robust statistical analysis and generalization of findings.

Data Collection

The study relied exclusively on secondary panel data, obtained from audited financial statements and published annual reports of non-financial firms listed on the Nairobi Securities Exchange (NSE) for the period 2015–2024. This method allowed for the use of already verified financial data to explore long-term trends and causal relationships between accruals quality and firm value. Data were systematically collected from company websites, the Capital Markets Authority (CMA) portal, and NSE handbooks to ensure accuracy and consistency. Key data were extracted from the statements of financial position and income statements, with a document review guide used to record relevant information such as total assets, liabilities, and market capitalization. Employing secondary data enhanced efficiency and objectivity, aligning with Polit and Beck's (2003) assertion that such data support the exploration of new insights and verification of existing relationships.

Measurement of Variable

This study measured independent variable (earnings quality) and dependent variable (firm value) as detailed. Tobin's Q is widely recognized as a key metric for assessing a firm's value, incorporating multiple dimensions such as the market-to-book value ratio, economic value added, market value added, net assets replacement value, and net market value. It remains the most frequently utilized benchmark for firm valuation (Al-Awawdeh & Al-Sakini, 2018; Crisóstomo, Lourenço, Carneiro Ferreira, & Silva, 2014; Jo & Harjoto, 2011). Numerous studies have employed Tobin's Q in their evaluations, including those by Buallay (2019), Nawaz (2017), Saidat, Silva, & Seaman (2019), Shamsudin, Abdullah, & Osman (2018), and Singh et al. (2018). This preference arises from its lower susceptibility to managerial manipulation and reduced sensitivity to differing accounting methodologies, compared to other accounting-based measures (Omar & Zallom, 2016). In this research, the Q-Ratio approximation was used as a proxy for firm value. Originally introduced by Chung and Pruitt (1994) as Approximate Q, this concept has been modified by the researcher as follows;

$$\text{Approximate } Q_{t+1} = \frac{MVE+DEBT}{TA} \quad \text{.....1}$$

where MVE represents the market value of equity, DEBT the total of short-term and long-term liabilities, and TA the book value of total assets. A Tobin's Q value below one indicates that a firm is undervalued, meaning its market value is lower than its book value—an attractive scenario for investors seeking growth opportunities. Conversely, a Tobin's Q value greater than one suggests that a firm is overvalued, implying that its market valuation exceeds the replacement cost of its assets (Robiyanto et al., 2021).

Earnings quality is a multidimensional concept that captures how accurately and reliably reported earnings reflect a firm's true financial performance and future prospects. According to Cornell and Landsman (2003), clarity in measuring earnings enables investors and stakeholders to understand operational revenues, costs, and capital requirements, which in turn supports accurate forecasting of future cash flows. Prior research has examined earnings quality in relation to its determinants, corporate governance, accounting changes, and its influence on cost of capital, debt, and market valuation (Bajra & Cadez, 2018; Hoang, 2014; Memis et al., 2012). Since earnings quality cannot be directly observed, this study adopts earnings persistence as a proxy, reflecting the sustainability and recurrence of earnings over time

(Francis et al., 2004; Penman & Zhang, 2002). Persistent earnings, which exhibit a strong autocorrelation between current and past earnings, are considered higher quality because they provide a more reliable basis for predicting future earnings. Such earnings are highly valued by investors as they signal stability, enhance valuation accuracy, and strengthen market confidence (Schipper & Vincent, 2003; Dechow & Schrand, 2004).).

$$NI_{i,t} = \beta_0 + \beta_1 NI_{i,t-1} + \mu_{i,t} \quad \text{.....2}$$

Where NI is earnings before extraordinary items scaled by lagged total assets during year t, $NI_{i,t-1}$ is earnings before extraordinary items scaled by lagged total assets during year $_{t-1}$ $\mu_{i,t}$ is the error term.

An estimate of β_1 closer to 1 implies high earnings quality, while a value of β_1 close to 0 implies highly transitory earnings quality.

The study controlled for firm size and firm age to account for their potential influence on firm value. Firm size was measured as the logarithm of total assets, following Tariverdi et al. (2014) and Laeven et al. (2014), with the expectation of a positive relationship between size and value. Firm age was determined by calculating the number of years since a company's incorporation up to 2015, based on prior studies by Berger and Udell (1998) and Boone et al. (2007), to capture the effect of a firm's maturity on its market valuation. Controlling these variables ensured a clearer assessment of how the independent, moderating, and mediating variables influenced firm value.

Table 1 Measurement of Variables

Variable Name	Measurement/Formula	Sources
Dependent Variable		
Firm Value	Tobin Q value,(MVE + DEBT) / TA	Chung & Pruitt (1994); Tobin & Brainard (1968)
Independent variable		
Earnings Quality	Earnings persistence measured through the autocorrelation of earnings, with high autocorrelation between current and past earnings being desirable regression: $NI_{i,t} = \beta_0 + \beta_1 NI_{i,t-1} + \mu_{i,t}$	Francis et al. (2004); Penman & Zhang (2002)
Control Variable		
Firm Size	Log of Total Assets	Tariverdi et al. (2014); Laeven et al. (2014)
Firm Age	Years since incorporation (2015 - establishment year)	Berger & Udell (1998); Boone et al. (2007)

Data Analysis and Model specification

Quantitative data were coded and analyzed using STATA due to its strong capability in handling panel and time-series data, unlike SPSS (Hayes, 2013). The analysis involved descriptive statistics, correlation, and multiple regression to examine data relationships, with results presented in tables and graphs. To test the direct effects of financial reporting quality

on firm value, both Fixed Effects and Random Effects panel models were applied. The Hausman test was then used to determine the appropriate model, where a probability value above 5% indicated preference for the random effects model, while a value below 5% supported the fixed effects model (Greene, 2008; Schmidheiny, 2014).

$$FV_{it} = \beta_0 + \beta_1 FA_{it} + \beta_2 FS_{it} + \beta_3 EQ_{it} + \varepsilon_{it} \quad \ldots\ldots 3$$

Where; FV - Is the measure of firm value., β_0 Is changes in Firm value that independent variables present in the model cannot explain. EQ Earnings Quality , ε Is the error term, i Companies/Firms, t Time

5. Results

Preliminary Analysis

The preliminary analysis presented in Table 2 summarizes the descriptive and correlation statistics for the key study variables firm value, earnings quality, firm size and firm age based on 330 observations. The results reveal wide variability in firm value, which ranged from 0.000 to 316.940 with a mean of 4.092 and a standard deviation of 19.839, indicating substantial differences in market valuation among listed non-financial firms. Earnings quality exhibited a minimum of -3.925 and a maximum of 10.432, with a mean of -0.006 and standard deviation of 0.981, implying that some firms displayed poor or volatile financial reporting practices that may affect investor confidence. Firm size remained relatively consistent, ranging between 4.806 and 8.474 with a mean of 7.086 and a standard deviation of 0.580, suggesting that larger firms dominate the NSE. Firm age varied between 19 and 155 years, with a mean of 75.320 and standard deviation of 31.788, highlighting that most firms are mature and have long operational histories. The correlation results show several statistically significant relationships at the 0.01 and 0.05 levels. Firm value is positively and significantly correlated with earnings quality ($\rho = .459$, $p < .01$) and firm age ($\rho = .196$, $p < .01$), suggesting that firms with high-quality earnings and longer market presence tend to command higher valuations. Conversely, firm value is negatively correlated with firm size ($\rho = -.409$, $p < .01$), implying that larger firms may face bureaucratic inefficiencies that reduce market performance. Additionally, earnings quality shows a weak negative association with firm size ($\rho = -.123$, $p < .05$), while firm age is negatively correlated with firm size ($\rho = -.315$, $p < .01$), indicating that older firms tend to operate on a smaller scale compared to relatively younger ones. The findings suggest that among NSE-listed non-financial firms, high earnings quality enhances firm value, while large firm size may limit performance due to inefficiencies. Mature firms appear to benefit from accumulated experience and established market credibility, reinforcing the importance of transparent financial reporting and sustained operational stability in driving firm value.

Table 2 Descriptive and Correlation Statistics

n=330	Min	Max	Mean	SD	FV	EQ	FS	FA
FV	0.000	316.940	4.092	19.839	1			
EQ	-3.925	10.432	-0.006	0.981	.459**	1		
FS	4.806	8.474	7.086	0.580	-.409**	-.123*	1	
FA	19.000	155.000	75.320	31.788	.196**	-0.015	-.315**	1

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

* Correlation is significant at the 0.05 level (2-tailed).

Unit Root Test

In panel data analysis, testing for stationarity is a critical preliminary step to ensure that variables maintain consistent statistical properties over time and that regression results are not spurious (Gujarati & Porter, 2009; Wooldridge, 2010). This study employed three widely recognized unit root tests—Levin–Lin–Chu (LLC), Harris–Tzavalis (HT), and Im–Pesaran–Shin (IPS)—to assess the stationarity of the variables: Firm Value (FV), Earnings Quality (EQ), Firm Size (FS), and Firm Age (FA). The null hypothesis (H_0) in each test assumed the presence of a unit root (non-stationarity), while the alternative hypothesis (H_a) proposed that the panels are stationary, either for all panels (LLC and HT) or for some (IPS) (Baltagi, 2021). The results, summarized in Table 3, reveal that all variables had p-values below the 0.05 significance threshold, indicating rejection of the null hypothesis. Specifically, FV ($p = 0.000$), EQ ($p = 0.000$), FS ($p = 0.000$), and FA ($p = 0.000$) were all found to be stationary at levels. These results confirm that the study variables are integrated of order zero (I(0)), implying that their means and variances remain constant over time. This finding enhances the reliability of the econometric analysis since stationary data prevent spurious correlations and ensure valid statistical inference. The absence of unit roots means that the regression models can be estimated without differencing or transformation, allowing for the exploration of meaningful long-term relationships between earnings quality and firm value among non-financial listed firms at the Nairobi Securities Exchange. The stationarity of the variables further reinforces the robustness of subsequent regression models, ensuring that the results accurately reflect the underlying economic relationships (Levin et al., 2002; Im et al., 2003).

Table 3 Unit root test

		Inverse chi-squared(66) P	Inverse normal Z	Inverse logit t(169) L*	Modified inv. chi-squared Pm
FV	Statistic	184.329	-4.822	-6.623	10.299
	p-value	0.000	0.000	0.000	0.000
EQ	Statistic	355.537	-10.503	-15.606	25.201
	p-value	0.000	0.000	0.000	0.000
FS	Statistic	488.532	-10.659	-21.082	36.777
	p-value	0.000	0.000	0.000	0.000
FA	Statistic	2309.762	-45.396	-111.145	195.294
	p-value	0.000	0.000	0.000	0.000

Source; (Field data, 2025)

Hypotheses Testing

Before estimating the regression model, several diagnostic tests were conducted to verify the suitability and reliability of the data. The normality test using Skewness and Kurtosis, Mardia's multivariate statistics, Doornik–Hansen, and Jarque–Bera tests confirmed that the residuals were normally distributed, with p-values greater than 0.05 (Skewness = 0.076; Kurtosis = 0.127; Jarque–Bera $\chi^2(2) = 5.442$, $p = 0.658$), indicating no violation of the normality assumption. The Wooldridge test for autocorrelation yielded $F(1,44) = 0.884$ and $p = 0.3541$, suggesting the absence of first-order autocorrelation. Likewise, the White's test for

heteroscedasticity reported $\chi^2(14) = 18.41$, $p = 0.1888$, confirming constant error variances and validating homoscedasticity. Finally, the Variance Inflation Factor (VIF) results ranged between 1.08 and 1.69 (mean VIF = 1.27), with Tolerance values between 0.591 and 0.924, indicating no multicollinearity. These outcomes confirm that the data met all key regression assumptions normality, independence, homoscedasticity, and low multicollinearity ensuring that the regression estimates were robust and unbiased.

The Hausman specification test was employed to determine whether the fixed-effects (FE) or random-effects (RE) model was more suitable for the analysis. The null hypothesis (H_0) stated that there was no systematic difference between the FE and RE coefficients, implying the appropriateness of the RE model. The test produced a chi-square statistic of $\chi^2(3) = 60.74$ with a p-value of 0.0000, leading to rejection of the null hypothesis. This indicates that the unobserved firm-specific effects were correlated with the explanatory variables, rendering the random-effects model inconsistent. Consequently, the fixed-effects model was selected as the most appropriate estimator for this study. The choice of the FE model ensured control for unobserved heterogeneity among firms, allowing the analysis to focus on within-firm variations in financial reporting quality and firm value over time.

Based on the Hausman test results, the fixed-effects model was estimated to analyze the relationship between earnings quality and firm value among non-financial listed firms at the Nairobi Securities Exchange. The model was statistically significant, with $F(6,281) = 27.38$, $p < 0.000$, indicating that the independent variables jointly explain variations in firm value. The within R^2 of 0.224 implies that 22.4% of the variation in firm value was explained by within-firm changes in earnings quality, firm size, and firm age. The between and overall R^2 values of 0.019 and 0.063, respectively, show that differences across firms and overall variations were modestly captured. The intra-class correlation coefficient ($\rho = 0.600$) suggests that 60% of the total variance in firm value was attributable to firm-specific factors. These results demonstrate that the fixed-effects model fits the data reasonably well, providing a reliable basis for hypothesis testing and interpretation of firm-level effects.

The study hypothesized that earnings quality has a significant effect on firm value among non-financial firms listed on the Nairobi Securities Exchange (***H_2***). The fixed-effects regression results confirmed this hypothesis, showing that earnings quality had a positive and statistically significant coefficient ($\beta = 1.363$, $t = 7.13$, $p = 0.000$). This indicates that firms with higher earnings quality reflected in reliable, transparent, and sustainable financial reporting tend to achieve higher market valuations. Investors interpret such credible earnings as a signal of sound management practices and stable financial performance, consistent with the predictions of signaling theory. Conversely, firm size (FS) recorded a negative and statistically significant relationship with firm value ($\beta = -8.718$, $t = -2.79$, $p = 0.006$), suggesting that as firms grow larger, they may face operational inefficiencies, bureaucratic rigidity, or increased agency costs that reduce market performance. Firm age (FA) exhibited a negative but statistically insignificant relationship with firm value ($\beta = -2.529$, $t = -1.62$, $p = 0.107$), implying that older firms do not necessarily enjoy higher valuations, possibly due to reduced growth opportunities or market adaptability. Thus, the results lead to the acceptance of the hypothesis (H_2), confirming that earnings quality significantly and positively affects firm value among non-financial firms listed in the NSE. These findings reinforce the notion that high-quality earnings serve as a credible signal of financial health, reduce information asymmetry, and enhance investor confidence in the Kenyan capital market.

Table 4: Fixed Effects Regression

Fixed-effects (within) regression Group variable: id			Number of obs = 330 Number of groups = 33		
R-sq:	Within	0.224	Obs per group	min	10
	Between	0.019		avg	10
	Overall	0.063		max	10
			F(6,281) =		27.38
corr(u_i,Xb) = -0.578			Prob > F =		0.0000

FV	Coef.	Std. Err.	t	P>|t|	[95% Conf.	Interval]
EQ	1.363	0.191	7.130	0.000	0.987	1.739
FS	-8.718	3.120	-2.790	0.006	-14.860	-2.576
FA	-2.529	1.564	-1.620	0.107	-5.607	0.550
_cons	24.900	6.728	3.700	0.000	11.656	38.143
sigma_u	1.571					
sigma_e	1.284					
rho	0.600	(fraction of variance due to u_i)				

F test that all u_i=0: F(32, 281) = 6.62 Prob>F= 0.0000

Source; (Field data, 2025)

6. Discussion of Findings

The analysis further established that earnings quality has a positive and significant effect on firm value. This implies that reliable, persistent, and sustainable earnings enhance market confidence and improve firm valuation by reducing uncertainty and information asymmetry. High-quality earnings act as credible signals of financial health and managerial integrity, which investors reward with higher firm valuations. This result aligns with Francis et al. (2004), who argued that earnings quality reduces the cost of capital and enhances firm performance through improved investor trust. Supporting empirical studies validate this outcome. Intara et al. (2024), in their study of Thai property and construction firms, documented a statistically significant positive relationship between earnings quality and Tobin's Q, demonstrating that quality earnings consistently drive higher valuations. Similarly, Darmayanti et al. (2023) found that earnings quality positively influences firm value in Indonesian financial firms, emphasizing the universal importance of transparent reporting across industries. Fassas et al. (2023) expanded this evidence to 37 European countries, confirming that robust earnings quality enhances firm value, though moderated by governance structures and market development levels. In emerging markets, Dang et al. (2020) established that earnings persistence and timeliness are critical drivers of valuation in Vietnam, further underscoring the relevance of quality reporting in contexts with weaker institutional frameworks. Even though some studies such as Cristina and Yasa (2024) suggested that discretionary accruals as a measure of earnings quality may not directly impact valuation, the broader consensus is that higher-quality earnings generally strengthen firm value. These findings converge to affirm that for NSE-listed firms, reliable earnings are a cornerstone of valuation, reinforcing their importance in sustaining investor confidence.

7. Conclusions

The study concludes that earnings quality plays a significant role in enhancing firm value among non-financial firms listed on the Nairobi Securities Exchange. Firms that consistently

produce reliable, transparent, and sustainable earnings are more likely to be perceived positively by investors, as credible financial information reduces information asymmetry and builds confidence in future performance. This finding suggests that investors in the Kenyan capital market value not just the profitability reported by firms but also the integrity and consistency of those earnings. High-quality earnings serve as credible signals of managerial competence and financial stability, leading to stronger market perceptions and firm valuation. In contrast, firms that present inconsistent or manipulated earnings may face reduced investor trust and lower market attractiveness.

8. Recommendations

The study recommends that firms strengthen their financial reporting systems to ensure that reported earnings accurately reflect economic reality. Management should adopt consistent accounting policies, uphold transparency, and minimize discretionary accounting practices that distort earnings. Internal audit units and audit committees should be empowered to oversee and maintain the integrity of financial statements, while external auditors should play a proactive role in identifying and discouraging earnings manipulation. Regulators such as the Capital Markets Authority and the Institute of Certified Public Accountants of Kenya should enhance monitoring and enforcement mechanisms to ensure compliance with international financial reporting standards. By prioritizing earnings quality, firms can attract more investors, reduce capital costs, and achieve sustainable growth in firm value.

Theoretical Implication

The results support Signaling Theory, which emphasizes that firms use financial reporting to communicate their credibility and quality to investors. High-quality earnings act as positive signals that reflect sound management practices and a firm's ability to generate sustainable returns. When investors interpret these signals as reliable, they respond with greater confidence, which in turn enhances firm value. The findings demonstrate that transparent and credible earnings disclosures remain a critical channel for reducing information asymmetry between managers and investors. This reinforces the theoretical view that effective financial communication not only strengthens investor confidence but also supports market efficiency in emerging economies such as Kenya.

Policy and Managerial Implications

From a policy standpoint, the study highlights the need for stronger disclosure frameworks and consistent enforcement of financial reporting standards. Regulatory authorities should ensure that listed firms adopt integrated reporting approaches that enhance transparency and comparability of financial information. For managers, the findings underscore the strategic importance of maintaining credibility through accurate and timely earnings reporting. Firms should embed transparency and accountability into their governance culture, as these attributes directly influence investor perceptions and long-term market performance. Emphasizing quality over short-term gains in financial reporting will help managers build sustainable investor relationships, foster trust in the capital markets, and ultimately enhance firm value.

9. Further Research

While this study provides valuable insights into the relationship between earnings quality and firm value among non-financial firms listed on the Nairobi Securities Exchange, several areas

warrant further investigation. Future research could expand the scope by incorporating other dimensions of financial reporting quality, such as accounting conservatism, accrual quality, and financial transparency, to provide a more comprehensive understanding of how these factors collectively influence firm value. Additionally, comparative studies between financial and non-financial sectors could offer deeper insights into sectoral differences in how investors interpret financial reporting signals. Researchers may also consider employing alternative methodological approaches, such as dynamic panel models or structural equation modeling, to capture long-term and causal relationships more accurately.

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