

**THE USEFULNESS OF FINANCIAL INFORMATION IN
CAPITAL MARKETS INVESTMENT DECISION MAKING
IN TANZANIA: A CASE OF IRINGA REGION**

DR. A.S.K Norman*

ABSTRACT

The use of financial information in deciding to invest wisely is crucial in all undertakings of investment ventures. This article presents the research findings on the use of financial information in Tanzania a case of Iringa region. The intent of the study was to find out whether investors of stock exchange do consider financial information when deciding to invest. The study used mixed methodology of data collections strategies. However, questionnaire was the prominent collection strategy. The analysis of the findings used Descriptive methods. The study applied purposeful sampling methodology and the stratification of sample was in three categories: Small Investors (SI), Medium Investors (MI), and Large Investors (LI). The findings revealed three propositions: 1) That the use of financial information assimilated a direct relationship with the level of investment. 2) That small investors realized poor use of financial information compared to other groups of investors. 3) That large investors indicated that they were more sensitive to the use financial information when deciding to invest than other groups of investors. Generally, the findings reveal that only 12 percent of all investors use/consider financial information when deciding to invest.

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KEYWORDS: Stock exchange, investors, financial information

* Tumaini University, Faculty of Economics and Business Administration; and Kampala, International University, Department of Management.

INTRODUCTION

Tanzania government established a committee, under the leadership of Dr. Mboya for responding to the economic challenges, which faced Tanzania, including the absence of private ownership of firms, unproductive government firms, and need for direct local and foreign investment. The prime role of the committee was to lay the ground for the creation of stock exchange. Hence, in 1994 the Parliament endorsed the establishment of the Capital Markets and Securities Authority (CMSA). The legal framework for the regulation of the securities industry is the Capital Markets and Securities Act, 1994 [Act No. 5 of 1994 as amended by Act No. 4 of 1997].

The CMSA established the Dar es Salaam Stock Exchange (DSE) to facilitate the securities (shares and bonds) investment (DSE, 2008). The enactment of DSE came because of government's policy of transforming its economy from public government dominated economy to private sector driven economy. The exchange became operational in April 1998 with TOL Gas Limited listing as the first company followed by the Tanzania Breweries Limited (TBL) during the same year. The delay was due to the necessary background operational preparations that were inevitable such as training of brokers and formulation of issuance and trading rules (CMSA, 2007). Hence, a stock exchange is a secondary capital market where large and small investors can buy and sell securities (shares, bonds etc.). It is an organized market where buyers and sellers of securities meet as they are represented by dealers/brokers and acquire or dispose securities (DSE, 2007; Norman, 2006). It is a market which securities are traded by members of the exchange who may act as both agents (brokers) and as principal (dealers) (Benning, 2007).

The establishment of the DSE marked the beginning of the people in Tanzania indulging in purchase of shares as a strategy for investing consequently a need for proper decision-making on where to invest and why. It can be added that the establishment of the Capital Markets followed suit of many other changes which gave a signal for the need to transform the economy from government driven to private driven economy. For example the Tanzania ruling party Chama cha Mapinduzi devolved the popularly known Arusha Declaration at the expense of adopting a Zanzibar Revolution. The former had stipulated the need for leaders not to participate in businesses or investment from what was perceived as avoidance of conflict of interest.

The Arusha Declaration set it clear that one should choose to be a leader or to become a business person. It further made it clear that a leader should not be subjected into two pay jobs. The

essence was to protect conflicting interest that may arise from different dealings of business ventures. For example, it is hard for a business man who is also the minister for trade and industry or finance to fairly play the role of paying taxes and or being royal to other government procedures that will be required on importing, exporting and in general transactions. Since the creation of the Zanzibar Revolution leaders have been massively participating in business including investing in capital markets.

Therefore, investing needs a keen responsibility of why, where and when to invest, and at what amount. The where and why questions are vital, in particular, when observing the performance of the companies that were the first to list shares with the DSE market and reasons backed people to invest in such companies. The first company to list its shares with the DSE was the Tanzania Oxygen Company Gas Limited (TOL). The observation, however, reveal that those who purchased shares encountered what could be termed as loss, since the TOL Gas Limited share value dropped from TZS 500 in 1998 to TZS 290 in 2009. On the other hand there are companies that have flourished. Such companies include the Tanzania Tea Packers Limited (TATEPA), which experienced the rise of share value from TShs. 330 as an Initial Price Offer in the year 2000 to TZS 510 in 2009. Further, Breweries Tanzania Limited has her shares increased value from IPO of TZS 550 in 1998 to TZS 1850 in 2009 (DSE, 2009). Other company such as NICO has IPO of TZS 300 in 2005 as on 4th March, 2009 the price has decreased to TZS 2851.

The research problem attracted the researcher in several ways; including the new-fangled venture of investment, which has attracted many Tanzanians. Secondly is the potentials vested in the entire shares business, which seem to supersede the banking interest rate on various accounts by far. For example, those invested in the Tanzania Cigarette Company (TCC) have enjoyed the share value increase of about 400% from TZS 410 in 2000 as Initial Price Offer (IPO) to TZS 1740 as Closing Price Offer (CPO) in 2009 (DSE, 2009; DSE, 2005). Such money increase, if were deposited at Commercial Banks would not reach an interest of 5%. The normal rate of most banks in Tanzania for saving accounts is between 2% to 4%. Those who invested in the Tanzania Breweries Company Limited earned about 254% in the period of about five years. Therefore, the main purpose is to set out paradox of whether those investing in shares do consider financial analysis/information when investing.

¹ The prices were observed on 4th March, 2009 at the DSE in Dar es Salaam.

Background to the Problem

Informed investment is important for minimizing the risks associated with losing value for the money invested. It is the spirit of the government to ensure that people participate in programs that reduce poverty (Rural Development Policy, 2003). The essence of capital markets is imperative in the efforts of the government to improve the economy and reduce poverty. Capital markets enables individuals to own firms and multiply their incomes through investment that is managed by other people but with profits shared with many individuals – the poor and the rich. Capital markets are divided into two categories namely bonds and shares both are generically known as securities.

Most people with normal economic status have been able to boost their economic strength and improve livelihood through purchase of shares. For example about 153,630 people participated in purchasing shares at Initial Price Offer (IPO) in Tanzania in 14 listed companies (DSE, 2009). The descriptions of the firms and the number of people subscribed are TOL 10500; TBL 23000; TATEPA 2000; TCC 7508 Tanga Cement 14228; DAHACO 41025; Twiga Cement 18300; NICO 2986; TCB 5447; and NMB 28636. The number of subscribed in shares suggest that the multiplier effects is huge. Since stocks are purchased at lower price and sold at higher price. Hence the total number benefiting from the entire exercise of purchasing and selling of shares is bigger than 153,630. It is estimated that a third of those purchase shares at IPO do sell during first appearance at secondary market.

There are number of factors that enable people purchase shares of the listed firms. The factors include the perceived management – to what extent the management of the firm suggests future prospects. Another factor considered are owners of the firms listing shares – who own the firms listing shares. For example firms that solely belong to the government seem to automate reliability of the people to purchase shares. The figures of people subscribed shares in Tanzania supports the argument. The first five firms with big numbers of investors are those owned by the government. The logic behind this is the risk associated with any business. Buyers would confide the government than individuals (Norman, 2005).

Further, another factor considered pertinent is the performance of the firm realized through financial information regarding profits, dividends, ratios regarding assets versus liabilities, acidic ratios and so forth. Normally people are not much concerned with trends of the business and

other technical financial interpretation. Most individuals rank the firms by mere understanding the profits and hence dividends anticipated, which suggest the need for acquisition of financial information. Financial information is important to the management of firms in Tanzania. It is from financial information the management can decide to list shares. The financial information tells managers on what measures should be taken for the survival of the firms. It is financial information that gives among other information whether the firms can pay dividends, cover debts, purchase new machines, establish branches, go abroad, and increase capital, among others.

The studies on the performance of the organizations in Tanzania and the world over reveal that most firms face two huge problems: working capital and competent personnel (Mautz, 1968; Norman, 1996; 2005). Hence capital markets are the key to raising financial capital of the firms as opposed to loans from financial institutions such as banks (DSE, 2008; 2007). The importance of capital markets particularly on raising firms' capital is on the base that no interest is charged on the capital acquired. Most first listed shared in Tanzania have encountered more money raised compared to what was needed.

Therefore it can generally be argued that capital markets translate the policies of Tanzania government of alleviating poverty and finally improving the people's livelihood. It is the capital market, which adds values on number of employments which results from rejuvenation that emanate from increased working capital of the firms. The firms listed with the DSE pay taxes to the government hence improving the accumulated fund, which ultimately does the roads improvements, health services, schools and so forth.

The rest of the paper covers the following categories: 2) the literature review. 3) the data and methodology, which covers the sample, data collection methods/strategy and the design. 4) Empirical result is the fourth part. Finally is the conclusion and policy cum research implication.

LITERATURE REVIEW

Most studies indicate the general importance of financial information/financial statements analysis as opposed to the use of the same in capital markets and in particular stock exchange. To bridge the gape, this study has found out the use of financial information by investors of stock exchange. The study has also covered the evolution and the development of capital markets in Tanzania and has set the comparative analysis of the capital markets in East Africa. Hence while many studies have revealed the role played by the understanding of financial information/financial analysis the link has been on indicating the general use in investment and in decisions of various portfolios but not specifically on whether people investing in stock exchange consider the financial information when investing or purchasing shares. Financial statements analyses emphasize on developing financial information within the context of formal decisions models. For instance the study of Nasser and Nuseibeh (2003) on the usefulness of annual reports reveal that the user groups surveyed in the study rely mainly on information made directly available by the company and do not consult intermediary sources of corporate information in order to make informed decisions.

This may suggest that there could be same correlations if same study was to be carried in Tanzania, since, just like Saudi Arabia, Tanzania is perceived to have a limited number of listed companies and businesses and financial communities have many social and business links, resulting in relatively easy interaction between the user groups and related companies.

The expediency of information released by companies should be in a simple form and expressive language for consumption by any client. In this dimension, Norman (2006) suggests that to make annual reports adequate and readable, the information contained in these annual reports should be presented in an understandable manner and grouped and organized appropriately. Moreover, Epstein and Pava (1994) asserted that the language style might have a material effect on the readership, and influence the understandability of information that appears in annual reports. Wolk et al. (1992 in Nasser et al., 2003), however, suggested that even if users of annual reports

are assumed to be knowledgeable, the information itself could have different degrees of comprehensibility.

In all sense, the importance of Financial Statements Analysis, which is literary known as financial information, is inevitable to investors and most findings have indicated the imperativeness of these reports. Nasser and Nuseibeh (2003) provide a number of studies, which have investigated the usefulness of corporate information to the users and found the annual report to be important and primary source of information. These include, (Mautz, 1968; Briggs, 1975; Lee and Tweedie, 1975a,b, 1976, 1981; Epstein, 1975; Chang and Most, 1977; Anderson, 1981; Arnold and Moizer, 1984; Moizer and Arnold, 1984; Chang and Most, 1985; Epstein and Pava, 1993; Bence et al., 1995; Anderson and Epstein, 1995; Abu-Nassar and Rutherford, 1996; Bartlett and Chandler, 1997).

DATA AND METHODOLOGY

This study used combined/mixed strategy. This included case study strategy. However, mini survey analysis was employed to capture responses that would allow generalization, hence a combined research strategy. According to Robson (1993), there are three traditional research strategies for real world research; experiment, survey and case studies. However, Yin (1994), points out that research is made up of five primary strategies. These are experiments, surveys, archival analysis, histories and case studies. Additional strategies imposed by Yin suggest that knowledge is not static, it is dynamic and grows. Barnes (2001) argues that it seems unlikely that experiments are appropriate for investigating such a complex and multi-faceted phenomenon as the operation of a strategic process. Even if it were possible to manipulate variable to observe their impact on one another, it would prove impossible to control for all other possible variables.

Although the use of mini survey may suggest quantitative approach yet the combined research strategy allows both non-researchers to capture information presented and also enables the academicians to interpret through the use of figures and other cognitive values that will be depicted. Mini survey calls for the use of a consistent and logical approach towards what is being

investigated and uses statistical inferences and mathematical techniques for processing the data with emphasis on the measurements and analysis of causal relationships between variables (Thurston, 1956; Kothari, 2004). Quantitative methods are necessary to test the validity and general applicability of the research findings; the potential of in-dept quantitative studies diminishes rapidly as the underlying conditions change in a dynamic environment (Barnes, 2001).

The sample for the study was 50 investors drawn from the population of about 600 being total number of stock investors in Iringa region. The sample was thus 8.3% of the entire population. Population was drawn using purposeful sampling method, which focused on investors that would represent the three strata that were identified. Hence, 24 investors represented small investors; 20 represented medium investors and the big investors were represented by 6 investors (See table 1).

As narrated above categorization of responses was small investors, which include all investors who invested any amount below 10 million. The second category was investors who did so between 10 million but below 50 million. The third category involved investors who invested from 50 million and above. The reason for categorization was to ensure that all categories of investors were represented. The theory of Capital Assets Price Model asserts that risk is determined according to the amount of money invested. Hence different capital invested may lead to different responses in terms of sensitivity to risk. The concern is that the more the risk felt by an investor, the more the sensitivity to Information Asymmetry- that is an art of realizing that investors differ in knowledge accrued on investment. The theory of information asymmetry emphasizes the fact that investors knowledge differ. Some know more than others. Responding to risk may not be in conformity to CAPM rather can be pushed by other factors such as information asymmetry. Expectation theory asserts the fact that interest is what pushes the investors to invest more. The expectation theory emphasize that, interest rates can be used as a barometer for future interest rates. Investors expecting higher short term interest rates are more likely to buy bonds maturing in the short term. Fifty investors were involved in the study. Table 4 reveals the responses and the number of investors that participated in the study.

Table 1: The profile on consideration of financial information when investing

S/NO	Type of investor	Respondents	Yes	No	Percentage for yes

Small investors	24	0	24	0.00
Medium	20	2	18	10.00
Large Investors	6	4	2	66.66
Total	50	6	44	

This table presents the findings of the study, which was conducted in 2009 through 2010 in Iringa. The findings include 50 respondents and reveal that large investors are sensitive to the use of financial information than medium and small investors.

It was evident that small investors did not consider financial information when investing. Financial information was not considered by investors with capital below 10 million shillings. The analysis indicated that 0% considered financial information in deciding to invest. Further, the findings in Iringa revealed that only 10% of medium investors- those who invest between 10 million Tanzania shillings but below 50 million shillings considered financial information when investing. Further more, it was observed also that 66.6% of large investors considered financial information when investing in securities. The trend suggests that risk averse (sensitivity to risk) is proportional to amount of money invested. The more the money invested the more the sensitivity to risk, hence need to ensure investment is well taken. One large investor had this to say in Iringa:

To me securities are the business of a day. I have prospered because of securities. I like purchasing shares, and the most important credential towards investing in stocks is financial information of the firms. We must study financial performance of the firms and decide intelligently².

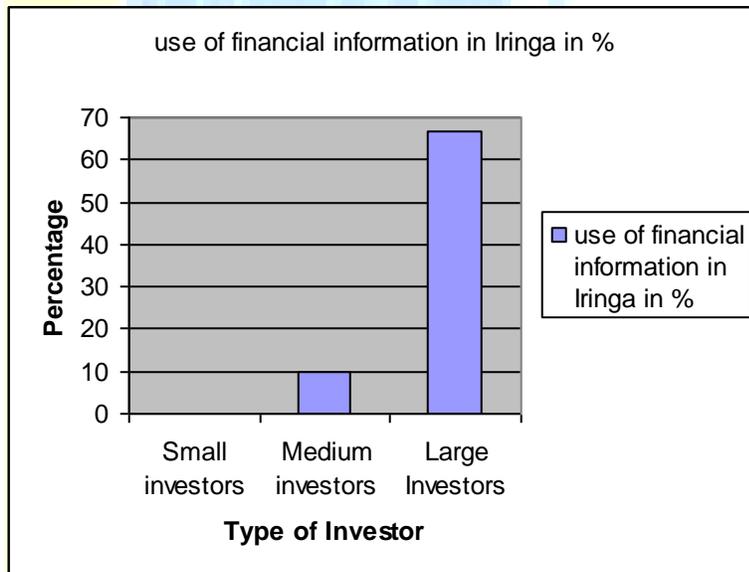
It was further observed that the category/strata that used financial information were the large investors. In this regard about 66.66% large investors interviewed used financial information when deciding to invest. The second group was the medium investors which attained a score of

² Respondent of Iringa regarding the use of financial information in securities investment

10% of those investigated under that stratum. The last group was the small investors which attains a zero percentage (figure 4.1).

On aggregate in Iringa it was noted that only 12% of all investors under the study did consider financial information when investing. The percentage reflects the total of 8 respondents being in favor of using financial information out 50. The observation revealed that 88% did not consider financial information when deciding to invest in securities. It can be concluded that in Iringa financial information is not considered when deciding to invest in securities. Figure 4.1 depicts the use of financial information in Iringa.

Figure 2: Investors use of financial information



This figure shows the use of financial information by three categories of investors. It further shows that large investors are sensitive to the use of financial information than small and medium investors.

CONCLUSION, RECOMMENDATIONS AND POLICY CUM RESEARCH IMPLICATIONS

To conclude therefore financial information is imperative in decision-making. This part has provided conclusions on the specific tendencies that were observed on whether investors in securities do consider financial information when deciding to invest.

From the findings, the following facts were revealed:

- a. The total use of financial information in Iringa for all investors stands at 12%. However, the use of financial information by strata of Small Investors (SI), Medium Investors (MI), and Large Investors (LI) stands at 0%, 10% and 66.7% respectively.

The value of financial information remains to be crucial, since it gives the investors to understand the anticipated profits and gains of the firms. Financial information also provides understanding on the prospective growth of the firm, hence investors of stocks could predict future investments plan for those who need growth of the value of shares at market. Financial information gives information regarding the ability of the firm to cover its liabilities, and thus enables investors to realize the true trend of the firms. Financial information further provides information on earning per share, hence enabling investors to understand the amount of growth their shares are likely to earn. Hence financial information is critical to any investor.

Recommendations

The study involved two key components which are stock exchange investment, and secondly the consideration of financial information. Hence the recommendations are divided into two those related to the use of financial information and those related to the need for investing in stocks/securities. Therefore the following is recommended:

Realizing the fact that the stock exchange business is benefiting many people, therefore Governments and all concerned stakeholders such as the DSE, CMSA and brokers should promote more firms to list shares with the DSE to enable more people enjoy the benefits for

investing in stocks at the same time providing unbiased, fair and coordinated financial information education in the area of stock exchange.

Recognizing that financial information education is needed in every dot of life, and to all people, therefore financial information education should start at primary school, since it is the fact that if people cannot be financial information literate, the impact will affect the government and other institutions. And such provision of financial information education can be attained through specific Web sites, free information services and newspaper, brochures, and Television for the purpose of enabling the majority people get advantage of investing in the Stock Exchange.

Policy cum Research Implications

- (i) The findings of this study have demonstrated that only 12% of the stock investors do use financial information. The policy implication on this situation calls for the ministry of education to ensure that financial education is taught at elementary stage of primary and secondary school, since financial education is imperative in all endeavors of finance.
- (ii) The findings of this study have revealed that barriers towards the use of financial information are lack of brokers in places other than Dar es Salaam. The policy implication in this situation is for the Capital Markets and Securities Authority (CMSA) and the Dar es Salaam Stock Exchange (DSE) to create rules and regulations that makes it mandatory for registered brokers to have branches in areas other than Dar es Salaam. Or the CMSA and /or DSE should create a structure in six zones of Tanzania for educating and providing advisory role on securities investment.

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BIOGRAPHY

Dr. Norman is a senior lecturer at Tumaini University, and Kampala International University both in Tanzania. He can be contacted at: Faculty of Business and Economics, Tumaini University P.O. BOX 200 Iringa, Tanzania; and Department of Business and Management, Kampala International University, Dar es salaam centre, P.O. BOX 9790, Dar es salaam, Tanzania.

