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Audit Quality and Financial Performance of Companies Listed in Nairobi Securities Exchange

Violet Nyaboke Matoke [*], Dr. Jane Omwenga [**]

[*] MBA Finance Degree, Jomo Kenyatta University of Agriculture and Technology, Kenya
[**] College of Human Resource Development, Jomo Kenyatta University of Agriculture and Technology, Kenya

Abstract- This study sought to establish the relationship between audit quality and financial performance of listed companies in Nairobi Securities Exchange. The specific objectives were: to examine the influence of size of the audit firm on the financial performance of listed companies in NSE, to determine the effect of auditors independence on the financial performance of listed companies in NSE, to establish the effect of attributes of the audit team on the financial performance of listed companies in NSE and to establish how the auditor's experience influences financial performance of listed companies in NSE. The theoretical framework encompassed a review of the auditors' theory of inspired confidence, agency theory and stakeholders' theory. This study adopted a descriptive research design. The sampling frame of this study was drawn from directories of the Nairobi Securities Exchange Limited; consisting of all the 9 listed companies in Kenya. Data from the ICPAK indicate that there are a total of 826 CPAs working in the 9 listed companies in Kenya. The study used simple random sampling to select 89 respondents since the study population was homogenous. Both primary and secondary data was used. Piloting was carried out to test the validity and reliability of the instruments. To establish the validity of the research instruments the researcher sought the opinion of experts in the field of study. The study used Cronbach (Alpha – α) model to test the reliability of the data. Quantitative and qualitative data that was collected using questionnaires was inspected for errors and gaps. The data was then well examined and checked for completeness and comprehensibility. After inspection, the data was coded and analysed by the use of descriptive statistics using SPSS. Data was analysed by multiple linear regression analysis. Findings of the study indicate that the effect of audit quality on financial performance is positive and significant and the greater the degree of an auditors independence, the greater the propensity of a firm making substantial net profit margins. The impact of auditor size was also positive and significant, although, its impact was lesser that of auditor independence. It is recommended that the management of listed parastatals should employ the services of one of the big audit firms and where this is not possible, management should go for an audit firm whose character and integrity is beyond question. Due to the importance of having high quality audit, further studies should explore the areas that relate to audit quality such as customer service satisfaction, customer loyalty, auditors switching and auditors turnover. This will go along incorporating quality and independence of management and board membership; internal audit considerations.

Index Terms- Audit Quality, Financial Performance, Listed Firms

I. Introduction

An auditor has the responsibility for the prevention, detection and reporting of fraud, other illegal acts and errors (Oluwagbemiga, 2010). This is one of the most controversial issues in auditing, and has been one of the most frequently debated areas amongst auditors, politicians, media, regulators and the public. This debate has been especially highlighted by the collapse of both small and big corporations across the globe.

The financial statement audit is a monitoring mechanism that helps reduce information asymmetry and protect the interests of the various stakeholders by providing reasonable assurance that the management's financial statements are free from material misstatements. The societal role of auditors should be a key contribution to financial performance, in terms of reducing the risks of significant misstatements and by ensuring that the financial statements are elaborated according to preset rules and regulations (Heil, 2012). Lower risks on misstatements increase confidence in capital markets, which in turn lowers the cost of capital for firms (Heil, 2012).

Zureigat (2010) examined the effect of financial structure among Jordanian listed firms on audit quality. Using a sample of 198 companies, his analysis of logistic regression shows a significant positive relationship between audit quality and financial structure. Nam (2011), examined the relationship between audit fees as a proxy for auditor independence and audit quality of firms in New Zealand. Employing three multiple regression models for a sample of New Zealand companies, his study discovered that the provision of non-audit services by the auditors of a firm comprises the auditor's independence, abnormal audit fee change rate is negatively associated with audit quality and auditor's independence of the previous year impacts on the audit fee that is negotiated in the current year.

Audit quality can be defined in two dimensions: first, detecting misstatements and errors in financial statement and second, reporting these material misstatements and errors. Due to the fact that these characteristics are largely unobservable, different proxies have been used by researchers to measure audit quality like: audit size, audit hours, audit fees, reputation, litigation rate and discretionary accruals (Krishnan & Schauer, 2000).

Audit quality is subject to many direct and indirect influences. In tandem with the stakeholder theory (Khan, 2006), perceptions of audit quality vary amongst stakeholders depending on their level of direct involvement in audits and on the perspective through which they assess audit quality.Audit quality may be perceived from any of three fundamental perspectives: inputs, outputs, and context factors. Inputs to audit quality, apart from auditing standards, include the auditor's personal attributes such as auditor skill and experience, ethical values and mind-set.

Increased concerns regarding corporate accountability in various developed nations have been associated with the need for appropriate Audit which involves risk management and internal control systems (Beekes & Brown, 2006). Audit Quality is recognized to influence financial reporting and strongly impact on investors' confidence (Levitt, 2008). Conventionally, external auditors play critical and highly challenging roles in assuring the credibility of financial reports.

Geiger and Raghunandan (2002) measured audit quality as whether the auditor had issuedagoing-concernqualificationinthepprioryearforUSclientsthatdeclared bankruptcy. They found that auditors are less likely to issue a going concern opinion during the initial years of engagement but not in later years, contrary to the expressed concern that a long auditor-client relationship negatively affects audit quality. Zureigat (2010) examined the effect of financial structure among Jordanian listed firms on audit quality. Using a sample of 198 companies, his analysis of logistic regression shows a significant positive relationship between audit quality and financial structure.

Maiteka (2010) undertook a study of the influence of risk based audit on corporate governance in public sector in Kenya focusing on selected ministries. From the findings, risk based auditing was found to assess risks facing government ministries on time and concentrate on high risk areas in order to increase transparency and accountability, hence enhancing good governance. Kasiva (2010) carried out a study on the impact of risk based audit on financial performance in commercial banks in Kenya. None of these studies has looked at the relationship between Audit Quality and Financial Performance in Listed State Corporations in Kenya. Therefore there existed a research gap that was to be filled by this study on the effects of the quality of audit on the financial performance of listed state corporations.

The general objective of the study was to establish the relationship between audit quality and financial performance of listed companies in Nairobi Securities Exchange. The specific objectives were: to examine the influence of size of the audit firm on the financial performance of listed companies in NSE, to determine the effect of auditors independence on the financial performance of listed companies in NSE, to establish the effect of attributes of the audit team on the financial performance of listed companies in NSE and to establish how the auditor's experience influences financial performance of listed companies in NSE.

II. LITERATURE REVIEW

2.1. Theoretical Framework

2.1.1. Auditors' Theory of Inspired Confidence

Developed by the Limperg Institute in Netherlands in 1985, the theory of inspired confidence states that the auditor, as a confidential agent, derives his broad function in society from the need for expert and independent examination as well as the need for an expert and independent judgement supported by the examinations. Thus, accountants and auditors are expected to know and realize that the public continues to expect a low rate of audit failures. This requires that the auditors must plan and perform their audit in a manner that will minimize the risk of undetected material misstatements. The accountant is under a duty to conduct his work in a manner that does not betray the confidence which he commands (Limperg Institute, 1985).

The importance of the theory of inspired confidence isthat the duties and responsibilities of the auditors are a derivation from the confidence that are bestowed by the public on the success of the audit process and the assurance which the opinion of the accountant conveys. Since this confidence determines the existence of the process, a betrayal of the confidence logically means a termination of the process or function. Carmichael (2004) in discussing the social significance of the audit stated that when the confidence that society has in the effectiveness of the audit process and the audit report is misplaced, the value relevance of that audit is destroyed. Therefore, auditors are expected to maintain reasonable quality assurance especially given that an audit failure is effectively a career-ending event. Audit provides assurance to the owners and management of companies and to investors and stakeholders, and along with financial reporting, corporate governance and regulations, supports confidence in the capital markets.

2.1.2. Agency Theory

Agency theory has been widely used in literature to investigate the information asymmetry between principals (shareholders) and agent (management). This study uses the agency theory to determine the impact of audit quality on the financial performance of listed state corporations in Kenya. Sarens and Abdolmohammadi (2007), states that according to the agency theory, a company consists of a set of linked contracts between the owners of economic resources (the principals) and managers (the agents) who are charged with using and controlling these resources. Jensen and Meckling (1976), states that in agency theory, agents have more information than principals and this information asymmetry adversely affects the principals' ability to monitor whether or not their interests are being properly served by the agents.

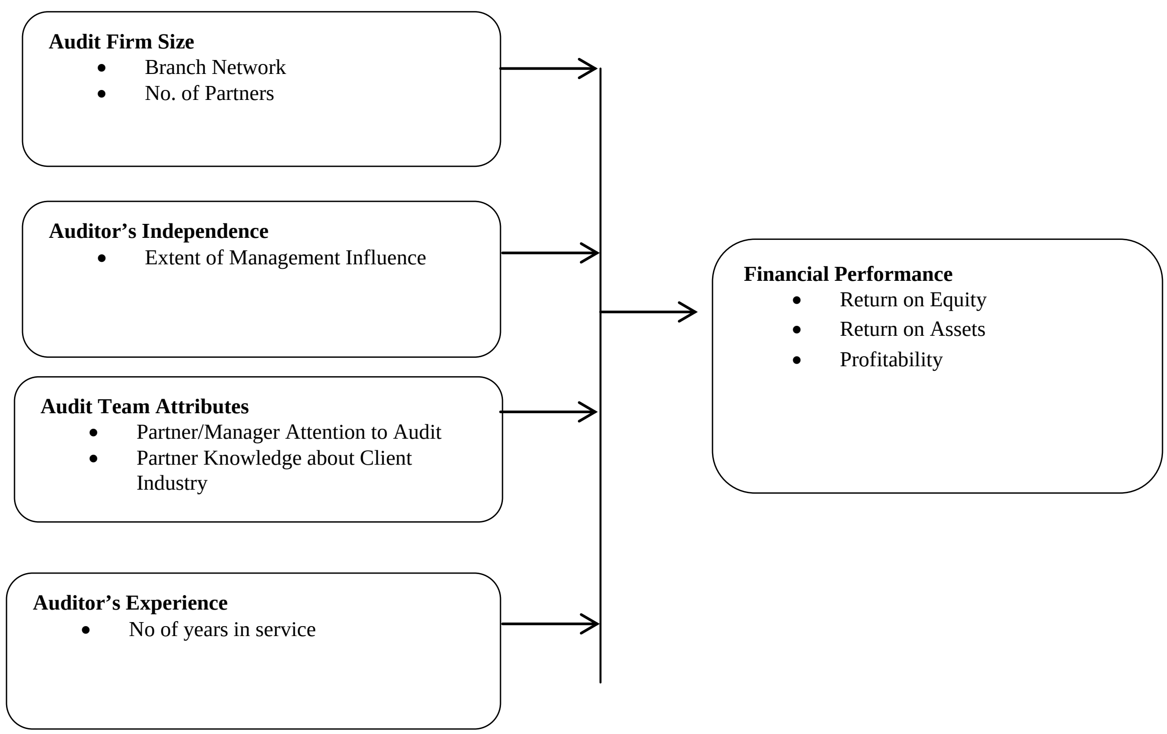
Jensen and Meckling (1976) opine that moral hazard constitutes a situation where to maximize their own wealth; agents may face the dilemma of acting against the interests of their principals. Since principals do not have access to all available information at the time a decision is being made by an agent, they are unable to determine whether the agent's actions are in the best interest of the firm. To reduce the likelihood of the moral hazard, principals and agents engage in contracting to achieve optimality, including the establishment of monitoring processes such as auditing. The principal-agent relationship as depicted in agency theory is important to understanding how the role of an auditor has developed. Principals appoint agents and delegate some decision making authority to them. In so doing, the principals place their trust in their agents to act in the principals' best interests. However, as a result of information asymmetries between principals and agents differing motives, principals may lack trust in their agents and may therefore need to put in place mechanisms, such as the audit, to reinforce this trust. Agency theory therefore, is a useful economic theory of accountability, which helps to explain the development of audit quality.

2.1.3. Stakeholder Theory

Stakeholders can be defined as any group or individual who can affect or is affected by the achievement of the organization's objectives. The theory begins with the assumption that values are necessarily and explicitly a part of doing business. Wheeler et al, (2003), posits that the stakeholder theory was derived from a combination of sociological and organizational disciplines. Stakeholder theorists suggest that managers in organizations have a network of relationships to serve – these include the suppliers, employees, lenders and other business partners.

Accordingly, Sundaram and Inkpen (2004) acknowledge that the stakeholder theory attempts to address the group of stakeholders that require management's attention. Many firms have developed and run their businesses in terms highly consistent with stakeholder theory. Firms such as J & J, eBay, Google, Lincoln Electric, AES, and the companies featured in Built to Last and Good to Great (Collins 2001, Collins & Porras, 1994) provide compelling examples of how managers understand the core insights of stakeholder theory and use them to create outstanding businesses.

2.2. Conceptual Framework



Independent variables **Dependent variables**

Figure 2.1: Conceptual Framework

2.3. Empirical Review of Literature

Many studies test perceived audit quality due to the difficulty of measuring actual quality directly. DeAngelo (1981) analytically demonstrates that the larger the auditor, the less incentive the auditor has to behave opportunistically and the higher the perceived quality of the audit. Teoh and Wong (1993) test whether perceived audit quality is different between Big 8 and non-Big 8 accounting firms.

Chen (2003) investigated the relationship between Risk Based Internal Audit and corporate governance structures. It was found that there existed a significant positive relationship between the level of RBIA used and corporate governance bank's board size. The findings of this study indicated a significant negative correlation existed suggesting that a small board size seems to be more effective, and is more likely to use RBIA, as a complementary mechanism. On contrary Krishnan, (2005) carried out an empirical analysis on the role of risk based audit on internal corporate governance and found that the percentage of non-executive directors and supervisors on the board of directors was significant negative associated with the use of RBIA indicating that the higher level of independent directors and supervisors on the board presents better corporate governance, hence may not employ higher percentage of RBIA for monitoring of risk management.

Okibo and Kamau (2011) carried out a study to explore internal auditors' compliance with Quality Assurance Standards: A case of state owned corporations in Kenya and found out that there is generally low compliance with quality assurance standards among most internal audit units in state owned corporations in Kenya. The research identified some of the reasons that led to low compliance to include; lack of awareness of standards; non-membership with IIA; non-adoption of IPPF; age and experience of the internal audit department and understanding of the quality assurance standards.

Woodland and Reynolds (2003) examined the association between indirect measures of audit quality and financial statement analysis using multivariate regression analysis. They found that audit fees is positively associated with financial statements but do not find evidence that auditor size, tenure or industry specialization are associated with audit quality in the directions predicted. Their results provide new evidence as to the current usefulness of these indirect measures in predicting audit quality.

A survey was conducted by Abu Bakar et al., (2005) among 116 loan officers in Malaysia. The results showed that 75.60 per cent of the respondents indicated that the size of the audit firm did affect the auditor independence and 74.40 per cent of them mentioned that the level of competition in the audit service market influenced the auditor independence. Furthermore, the results indicated that the provision of MAS had a negative effect on the auditor independence in Malaysia.

Zureigat (2010) examined the effect of financial structure among Jordanian listed firms on audit quality. Using a sample of 198 companies, his analysis of logistic regression shows a significant positive relationship between audit quality and financial structure. Nam (2011), examined the relationship between audit fees as a proxy for auditor independence and audit quality of firms in New Zealand. Employing three multiple regression models for a sample of New Zealand companies, his study discovered that the provision of non-audit services by the auditors of a firm comprises the auditor's independence, abnormal audit fee change rate is negatively associated with audit quality and auditor's independence of the previous year impacts on the audit fee that is negotiated in the current year.

2.4. Critique of Existing Literature Relevant to the Study

Although considerable research has been done on the Audit and Financial Performance, most studies have concentrated their research on the influence of external audit and internal audit on performance.Other researchers have concentrated on the effect of Audit on cooperate governance.

Maiteka (2010) undertook a study of the influence of risk based audit on corporate governance in public sector in Kenya focusing on selected ministries. From the findings, risk based auditing was found to assess risks facing government ministries on time and concentrate on high risk areas in order to increase transparency and accountability, hence enhancing good governance. Kasiva (2010) carried out a study on the impact of risk based audit on financial performance in commercial banks in Kenya.

None of these studies looked at the relationship between Audit Quality and Financial Performance in Listed State Corporations in Kenya. Therefore there existed a research gap that was to be filled by this study on the effects of the quality of audit on the financial performance of listed state corporations.

2.5. Research Gaps

The studies carried out have concentrated so much on establishing the existence of an audit expectation gap in various countries. Other studies have also looked at details about the origin and solutions to the problem of audit quality. A few other studies have interrogated the causes of audit quality and even developed the quality model to show its different components.This study interrogated the determinants of audit quality using a multiple regression model approach.The review of literature suggests that there are researches that have been carried out mostly from USA, Malaysia, Egypt, Iran, India, Nigeria, Singapore, etc. Not much of the studies have been carried out on the audit quality in Kenya's perspective. This study contributed towards filling this gap.

III. RESEARCH METHODOLOGY

This study adopted a descriptive research design. The choice of this method stems from the fact that it has been successful in research of this nature. The unit of analysis for this study compromised of Certified Public Accountants of all the nine listed companies. The ICPAK membership as at December 2014 was 9,968, out of which; 5,283 are in business, 3,391 in public practice, 697 are retired while 597 are based overseas. Out of the 3,391 in public practice, 826 work for the 9 listed companies.

The sampling frame of this study was drawn from directories of the Nairobi Securities Exchange Limited; consisting of all the 9 listed companies in Kenya. Data from the ICPAK indicate that there are a total of 826 CPAs working in the 9 listed companies in Kenya. The study used simple random sampling to select 89 respondents since the study population was homogenous.

Primary data was collected through semi-structured questionnaires with both open and closed ended questions. Secondary data was collected by way of review of published materials and the published Annual Reports from the selected listed State Corporations. The researcher administered the questionnaires personally and through e-mail system to the firms.

Piloting was carried out to test the validity and reliability of the instruments. This study used content validity because it measures the degree to which the sample of the items represents the content that the test is designed to measure. A pilot study was conducted by the researcher taking some questionnaires to selected Certified Public Accountants in Nairobi. From this pilot study, the researcher was able to detect questions that needed editing and those that were ambiguous. The final questionnaire was then printed and used to collect data for this study.

To establish the validity of the research instruments the researcher sought the opinion of experts in the field of study. The study used Cronbach (Alpha – α) model to test the reliability of the data. Brown (2002) noted that the Cronbach's alpha reliability coefficient normally ranges between 0 and 1.0. The closer the coefficient is to 1.0, the greater the internal consistency of the items in the scale. SPSS application will be used in the calculation of the Cronbach's alpha for reliability analysis.

Quantitative and qualitative data that was collected using questionnaires was inspected for errors and gaps. The data was then well examined and checked for completeness and comprehensibility. After inspection, the data was coded and analysed by the use of descriptive statistics using SPSS. The study used the Likert type scale as the rating scale in questionnaires. Data was analysed by multiple linear regression analysis using Return on Assets (ROA) and Return on Equity (ROE) as proxy for the firm's financial performance as dependent variables and independent variables comprising of Size of the Audit Firm, Independence of the Auditor, Qualifications of the audit team and the auditor's experience.

$$Y=\beta_0+\beta_1X_1+\beta_2X_2+\beta_3X_3+\beta_4X_4+e$$

Where;
β_0 - Constant
Y- Dependent variable (financial performance)
X_1=Independent variable (audit firm size)
X_2= Independent variable (auditor's independence)
X_3= Independent variable (audit team attributes)
X_4= Independent variable (auditor's experience)
$\beta 1 - \beta 4$ = Regression coefficient for each independent variable

This being a descriptive research, descriptive statistical measures including, frequency distribution and percentages were used to present the quantitative data. The qualitative data was analysed using in-depth descriptive analysis. This entailed relating pertinent information through interpretative analysis and presenting the data using qualitative matrices.

IV. RESEARCH FINDINGS AND DISCUSSIONS

4.1 Response Rate

An analysis of the study's response rate was carried out showing the actual number of participants who took part in the study. The sample size for this survey was 89 certified public accountants working for the 9 listed state corporations. The researcher dispatched 89 questionnaires to the companies but only 78 accountants duly filled and submitted the completed questionnaires. This translates to a response rate of 87.6% which the researcher considered adequate for analysis. According to Cooper and Schindler (2003), a response rate of between 30% and 80% of the total sample size is sufficient for use in making generalizations about the entire population.

4.2 The Designation of Respondents

The study targeted certified public accountants who are currently employed by listed state corporations as auditors, managers or accountants. Figure 4.1 indicates that 58% of the respondents were accountants who are employed by listed companies while 25% are managers and 17% being auditors of the listed companies. However, it is important to note that all the people who filled the questionnaires are Certified Public Accountants of Kenya

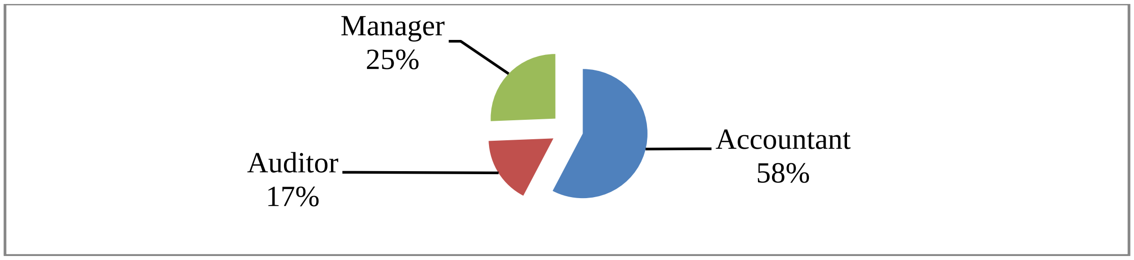


Figure 4.1: Designation of respondent

4.3 Results of the Pilot Study

A pilot test was carried out to establish the reliability and validity of the data collection tools. The pilot test aims at establishing construct validity and reliability of the data collection instruments (Mugenda &Mugenda, 2003).A total of 20 respondents took part in the pilot study. According to Cooper and Schindler (2003), the pilot group can range from 15 to 100 subjects depending on the method to be tested but it does not need to be statistically selected. This was in line with a qualitative research design methodology employed in this research project.

4.3.1 Reliability Test of Constructs

In this study to ensure the reliability of the instrument Cronbach's Alpha was used. Cronbach Alpha value is widely used to verify the reliability of the construct. Therefore, Cronbach Alpha was used to test the reliability of the proposed constructs. The findings indicated that Size of the Audit Firm had a coefficient of 0.704; Qualification of the Audit Team had a coefficient of 0.763, and Experience of the Auditor of 0.729. All constructs depicted that the value of Cronbach's Alpha are above the suggested value of 0.7 thus the study was reliable (Nunnally& Bernstein, 1994; Nunnally, 1974). On the basis of reliability test it was supposed that the scales used in this study is reliable to capture the constructs.

4.3.2 Construct Validity

Construct validity is established by relating measuring instruments to a general theoretical framework in order to determine whether the instrument is tied to the concepts and theoretical assumptions they are employing (Nachmias & Nachmias, 2008). SPSS version 20 programme was used as the tool of analysis to test the relationship between the dependent variable and the four independent variables. As most item total correlations were reasonably high, the construct validity of the instruments was considered reasonable (Brown, 2000).

Table 4.1: Study variables' Construct Validity

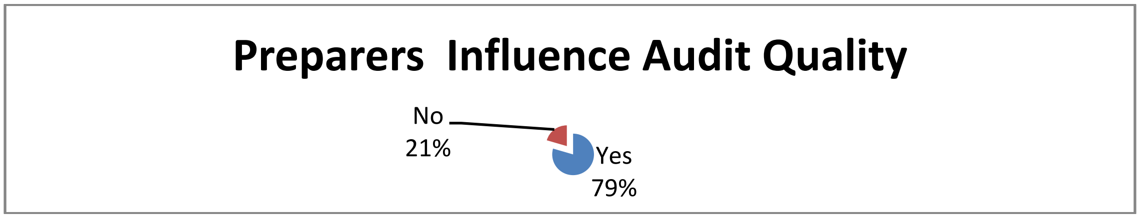
	Mean	Std. Deviation	N
Size of the Audit Firm	4.0000	.98033	20
Qualifications of the Audit Team	4.1795	.87895	20
Auditor's Experience	4.4615	.69679	20

4.4 Preliminary Questions

4.4.1 Preparers of Financial Statements Have an Influence on the Audit Quality

The study sought to establish whether the preparers of financial statements have an influence on the quality of the audit. Results from the study as indicated by Figure 4.2 below indicate that majority of the residents (79%) agreed that there is an influence whereas 21% of the respondents said there was no influence on the audit quality by preparers of the financial statements.

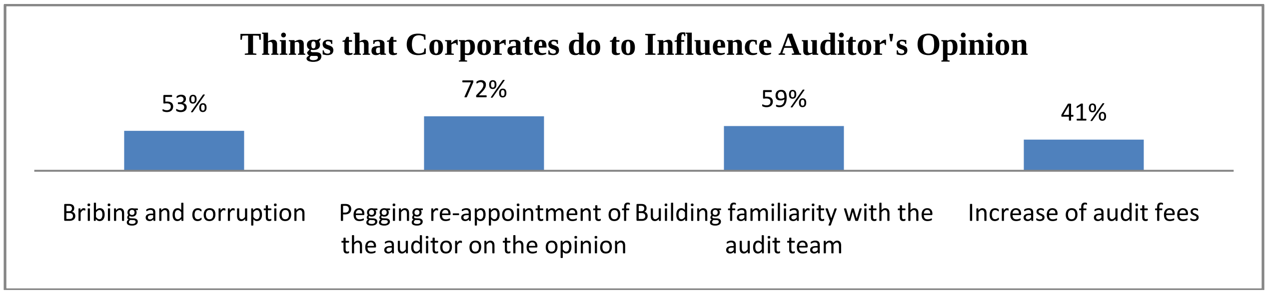
Figure 4.2: Influence of preparers of financial statements on the audit quality



4.4.2 Things Done by Corporates to Influence Auditor's Opinion

Results of the study indicate that majority of the respondents (72%) think most corporates peg re-appointment of the auditors on their opinion hence influence their opinion, 53% of the respondents were of the opinion that corruption and bribes received from corporates influence the auditor's opinion; 59% opined that corporates influence the Auditor's opinion by building familiarity with the audit team whereas 41% thought increase of audit fees by corporates would influence the auditors opinion. Findings of the study are summarised in Figure 4.3. overleaf.

Figure 4.3: Things Done by Corporates to Influence Auditor's Opinion

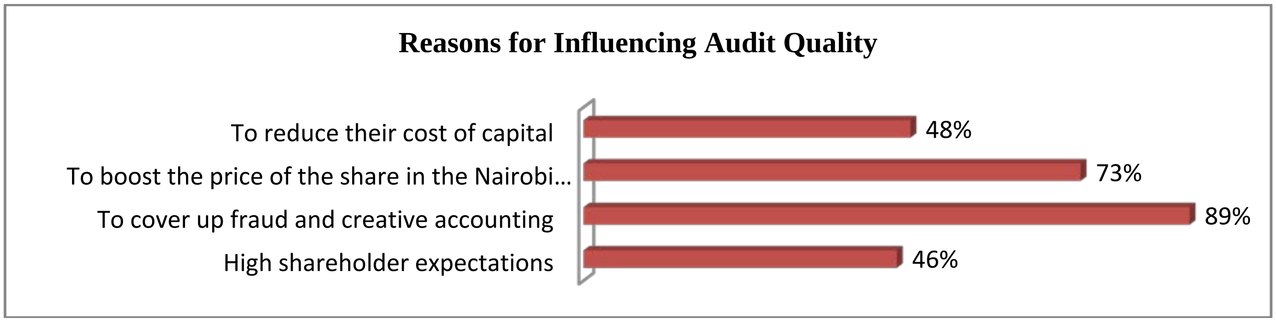


4.4.3 Reasons for Influencing the Quality of Audit by Corporates

Findings of the study as shown in figure 4.5 indicate that, most of the respondents (89%) were of the opinion that most corporates influence the quality of audit to cover up fraud and creative accounting. Other respondents gave varying Reasons for Influencing the Quality of Audit by Corporates including; to boost the price of the share in the Nairobi Securities Exchange (73%); High shareholder expectations (46%), and To reduce their cost of capital (48%).

The findings of the study augment with the findings of Karamanou and Vafeas (2005), who found out that audit quality is associated with an increased probability of management earnings forecast updates, more informative good news forecasts, and more positive stock market reactions to management forecasts.

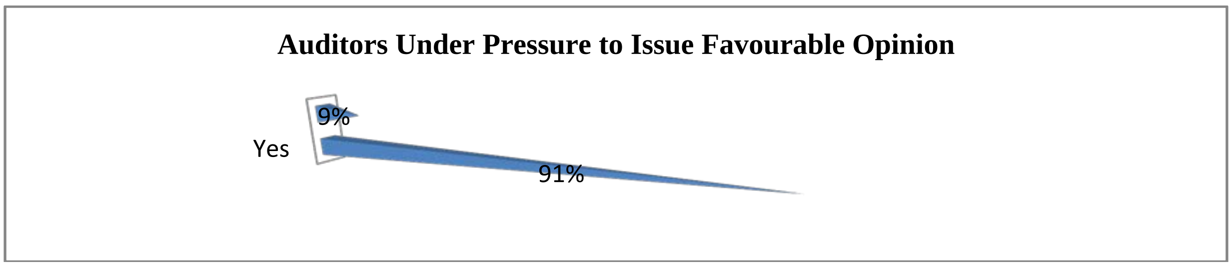
Figure 4.4: Reasons for Influencing the Quality of Audit by Corporates



4.4.4 Auditors are Under Pressure to Declare Favourable Audit Opinion on the Financial Performance

91% of the respondents in the study agreed that auditors are under pressure to declare favourable audit opinion on the financial statements.

Figure 4.5: Whether auditors are under pressure to issue favorable opinion



4.5 Study Variables

The descriptive statistics for each of the variables were determined to show the minimum, maximum, mean and standard deviation values. Descriptive statistics helps readers to understand the measures of central tendency and measures of variances associated with the variables of the study.

4.5.1 Size of the Audit Firm

Findings from the study indicate that majority of the respondents (86%) are of the opinion that the audit firm size has an influence on the firm's profitability reporting. Findings are summarised in the table below. The findings of the study augment with the findings of Bouaziz (2012), who examined the relationship between auditor size and financial performance on a sample of 26 Tunisian firms listed on the Tunis Stock Exchange. The result shows that auditor size has an important impact on the financial performance of firms in terms of return on assets and return on equity.

Table 4.2: Auditors' size

	Strongly agree	Agree	Neither agree nor disagree	Disagree	Strongly disagree
The audit firm size has an influence on the firm's profitability reporting	62%	24%	14%	0%	0%
The audit firms branch network affects the firm's profitability reporting	48%	46%	5%	1%	0%
The audit firms number of partners has an impact on the firm's profitability	42%	51%	6%	1%	0%

4.5.2 Independence of the Auditor

Findings of the study as indicated in the table below show that 96% of the respondents opine that the auditor's remuneration is tied to the financial performance of their organization. 93% of the respondents agreed that the branch network of the audit firm influences the quality of audit.

Table 4.3: Independence of the Auditor

	Strongly agree	Agree	Neither agree nor disagree	Disagree	Strongly disagree
The auditors remuneration is tied to the financial performance of this firm	72%	24%	4%	0%	0%
The management of the firm have an influence on auditors decision making	48%	36%	15%	1%	0%
The Management would retain an auditor when the financial performance is favourable	52%	41%	6%	1%	0%

4.5.3 Qualification of the Audit Team

Results of the study indicate that 81% of the respondents were in agreement that the qualification of audit partners has an influence on the audit quality of reported. A summary of the findings are shown in the table overleaf.

Table 4.4: Qualification of the Audit Team

	Strongly agree	Agree	Neither agree nor disagree	Disagree	Strongly disagree
The qualification of audit partners has an influence on the audit quality of reported financial results	67%	14%	19%	0%	0%
The Membership to professional bodies has an impact on the audit quality of reported financial results	38%	25%	13%	24%	0%
The number of auditors who are professionally qualified impact on the quality of reported financial report	22%	32%	9%	37%	0%

4.5.4 Auditor's Experience

Findings from the study indicate that 82% of the respondents agree that audit firms' number of years in existence has an influence on the quality of reported financial reports. However 18% were indifferent. Further, results of the study indicate that 64% of the respondents who took part in the study agree that the number of experienced auditors in the team will impact on the quality of reported financial reports. A further 64% of the respondents also agreed that auditor's international experience affects the audit quality of reported financial performance. Findings of the study are summarised in table 4 overleaf.

Table 4.5: Auditor's Experience

	Strongly agree	Agree	Neither agree nor disagree	Disagree	Strongly disagree
The audit firms number of years in existence has an influence on the quality of reported financial reports	46%	36%	18%	0%	0%
The number of experienced auditors in the team will impact on the quality of reported financial reports	28%	36%	9%	27%	0%
The auditor's international experience affects the audit quality of reported financial performance	18%	46%	8%	28%	0%

4.6 Multivariate Correlation

Correlation between sets of data is a measure of how well they are related. The most common measure of correlation in statistical data is the Pearson Correlation. Pearson Correlation also known as the Product Moment Correlation or PPMC shows the linear relationship between two sets of data. In other words, the Pearson correlation answers the question, on whether a line graph can be drawn from the results to represent the data. The results of a Pearson correlation are usually between -1 and 1. The closer the value of the Pearson correlation is to zero, the greater the variation the data points are around the line of best fit. A high correlation is indicated by values between 5 to 1.0 or -0.5 to 1.0 while medium correlation is represented by values between.3 to .5 or -0.3 to .5

The research conducted a Pearson product moment correlation to establish the correlation between the variables of the study. The findings of the study indicate that there is a high correlation between all the study variables and Financial Performance. The Pearson correlation is presented in

Table 4.6: The Pearson correlation

		Size of the Audit Firm	Qualification of the Audit Team	Auditor's Experience
Size of the Audit Firm	Pearson Correlation	1.000	0.151	0.513
	Covariance	0.961	0.130	0.351
	N	**78**	**78**	**78**
Audit Team Attributes	Pearson Correlation	0.151	1.000	0.033
	Covariance	0.130	0.773	0.020
	N	**78**	**78**	**78**
Auditor's Experience	Pearson Correlation	0.513	0.033	1.000
	Covariance	0.351	0.020	0.486
	N	**78**	**78**	**78**

V. SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

5.1. Summary of Findings

The study examined the relationship between audit quality and financial performance through the proxies of auditor size and net profit margin, Audit Team Attributes and auditor experience and net profit margin of listed parastatals in Kenya. Series of concepts, principles and contrasting views of scholars were discussed. An extensive review of literature on audit fees, auditor size, financial performance and net profit margin was undertaken.

Increasing auditor fees gives auditors a sense of responsibility which is an added advantage for the affected parastatals. The auditing firm would be obliged to send experienced auditors who will not be in a rush to finish the audit process considering the amount being paid. It should be remembered that audit firms normally bill their clients based on the number of the hours worked. Thus, quoted parastatals that pay high remunerations to their auditors are more likely to get audit quality when compared to those who pay relatively low remunerations to their auditors.

The findings of the study augment with the findings of Bouaziz (2012), who examined the relationship between auditor size and financial performance on a sample of 26 Tunisian firms listed on the Tunis Stock Exchange. The result shows that auditor size has an important impact on the financial performance of firms in terms of return on assets and return on equity. Findings show that 96% of the respondents opine that the auditor’s remuneration is tied to the financial performance of their organization. 93% of the respondents agreed that the branch network of the audit firm influences the quality of audit. Results of the study indicate that 81% of the respondents were in agreement that the qualification of audit partners has an influence on the audit quality of reported. Findings from the study indicate that 82% of the respondents agree that audit firms’ number of years in existence has an influence on the quality of reported financial reports. However 18% were indifferent. Further, results of the study indicate that 64% of the respondents who took part in the study agree that the number of experienced auditors in the team will impact on the quality of reported financial reports.

5.2. Conclusion

Findings of the study indicate that the effect of audit quality on financial performance is positive and significant and the greater the degree of an auditors independence, the greater the propensity of a firm making substantial net profit margins. The impact of auditor size is also positive and significant, although, its impact is lesser that of auditor independence.

5.3. Recommendations

5.3.1 Policy Recommendations

It is recommended that the management of listed parastatals should employ the services of one of the big audit firms and where this is not possible, management should go for an audit firm whose character and integrity is beyond question. Audit firms who have a solid reputation will be less likely to employ auditors who will be willing to compromise their stand; the audit firm itself would not like to engage in any activity that will soil its name. This is a plus for the management of the parastatals and the Government alike, because rest assured, their interests will be duly protected.

5.3.2 Recommendations for Further Research

Due to the importance of having high quality audit, further studies should explore the areas that relate to audit quality such as customer service satisfaction, customer loyalty, auditors switching and auditors turnover. This will go along incorporating quality and independence of management and board membership; internal audit considerations.

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AUTHORS

First Author – Violet Nyaboke Matoke, MBA Finance Degree, Jomo Kenyatta University of Agriculture and Technology, Kenya
Second Author – Dr. Jane Omwenga, College of Human Resource Development, Jomo Kenyatta University of Agriculture and Technology, Kenya