Shareholder Activism and Earnings Management: Evidence from Kenya

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Abstract

Earnings management has in the recent past attracted a significant scholarly attention, especially in the wake of global financial misstatements which is detrimental to the firm stakeholders who rely majorly on the financial reports for decision making. In response to this shareholder activism has sprouted in the modern organizational setup where active shareholders directly engage the management on issues about financial reporting. Shareholders' role within the company is grounded by the agency theory. A panel data analysis was conducted using secondary data collected from the yearly audited financial reports of 65 firms registered at the Nairobi Stock Exchange. The research concentrated on the firms that were consistently in operation at the NSE for the periods between 2004 and 2017, with an overall of 490 firm-annum observations. An explanatory research design was used in the study as a guide towards arriving at the conclusions. Statistical techniques, specifically the mean, standard deviation, correlation and regression were used to analyze the data. Harris-Tzavalis test was used to check for unit root, while Hausma's test was employed to choose between random and fixed effect models. Shareholder activism is a significant corporate governance mechanism that performs a vital role in earnings management. The findings indicate that blockholder activism performs a very vital role in the firm by lowering earnings management (β= -2.546, $p<0.05$). As suggested by the agency theory, blockholder activism is a desirable monitoring mechanism in a firm meant to reduce the self-interests of the management. Institutional shareholder activism was found to increase (β=3.01, $p<0.05$) earnings management due to their transient nature. It is further recommended for the institutional investors to refrain from exerting more pressure for short-term performance by the management since it results in earnings management.

Keywords: Blockholder Ownership, Earnings Management, Institutional Ownership, Discretionary Accruals

INTRODUCTION

Earnings management is the act by aggressive accounting to raise (or reduce) earnings, incomes or profits for varying types of shares. Opportunistic earnings management refers to management of earnings through accounting estimations as well as methodologies that does not have direct bearing on the cash flows. Due to the adverse selection between the internal and the external stakeholders of a firm, individuals in the entity may count on their influence on the financial statements as well their access to the firm's financial details to overestimate the profits or to conceal undesirable outcomes (Lin & Hwang, 2010). As much as financial disclosure is relied upon by investors in portraying a true reflection of the firm performance and asset information, the management may engage their discretion to portray a false impression of good firm performance for their own benefits. On the other hand, real earnings management is the manipulating of earnings via operating activities having direct influence on the cash flows as reported by Sun, Lan and Liu (2014). The management might

impact on conveyed earnings by choosing accounting options or through discretionary operational judgments (Kang & Kim, 2011).

Earnings management comprises of two perspectives, that is opportunistic and the informative earnings management. The opportunistic view is that executives purposely mislead interested parties by altering reported earnings in order to achieve their individual utilities (Burgstahler & Dichev, 1997; Healy & Wahlen, 1999; Z. Lin, Liu, & Noronha, 2016), while the information perspective maintains that earnings management practices are mechanisms through which the management convey their forecasts regarding future cash flows and profitability of the company (Bajra & Cadez, 2018). Management could apply various ways such as concealing changes in economic conditions by setting up reserves for deferred revenue, thereby lowering revenue fluctuations (Hijazi & Al-Thuneibat, 2015; Leuz, Nanda, & Wysocki, 2003). According to Sun et al. (2014), executives can reduce research along with development, advertisement, as well as maintenance expenses so as to achieve earnings goals, although such deeds might damage the company's value in the future.

This act of reported earnings manipulation by the management results in agency problems among the owners who are the principals and the agents who are the management. The agency dispute between the parties originates almost naturally because of detachment of ownership with control which is evident in the today's business environment, therefore placing the management in a better place that offers them with the leeway to make choices which could either intersect or reinforce the company's goal of maximizing shareholder wealth (Hassan & Ahmed, 2012). Agency theory therefore proposes that in the event of an agency conflict, the shareholders should develop a mechanism through which the agents' actions could be monitored and this could be achieved through shareholder activism. Where the shareholders along with the management each seek to maximize their utilities, then it is reasonable to conclude that somehow the agent might not represent the interests of the principal (Jensen & Meckling, 1976). Therefore, by providing sufficient rewards to the agent, the principal may restrict the latter's deviation from his interest by accruing monitoring costs meant to reduce the agent's aberrant actions. It is more tough for the owners to monitor managers because of a high level of information imbalance, hence firms with unclear information are similarly to involve in more earnings management (Jiraporn, Kim, Davidson, & Singh, 2006).

Agency theory suggests that a good corporate governance mechanism such as shareholder activism could be a most suitable monitoring device to limit the divergence of interests ensuing amid the shareholders (principals) and the managers (agents), which is more likely to arise due to earnings management. Corporate governance therefore may be categorized into binary classifications: Company boards of directors as well as ownership structures (Denis & McConnell, 2003), whereby the boards and their roles are classified as internal corporate governance while the ownership structures are the external mechanisms. Institutional and blockholder shareholders have been noted as the active owners. The research focused on the implication of external firm governance devices on earnings management. Other ownership structures have been captured by previous studies, but only the active shareholders have been documented to provide an effective monitoring the management more than the dormant shareholders. For instance Bradbury, Mak, and Tan (2004) advocates that block holders along with institutional owners perform an vigorous role in monitoring management against divergence of interests for their own benefits. Shareholder activism could be having an implication on the managerial behavior in a firm since active shareholders who are the institutions and the large shareholders maintain a close monitoring on managerial activities. It is therefore more likely from the foregoing that good

corporate governance mechanisms that monitor managers' opportunistic actions would undoubtedly render accounting earnings increasingly accurate and transparent to stakeholders, thus increasing the firm value (NAZIR & AFZA, 2018).

In Kenya, Corporate Governance including ownership structures have been expressed as the structure and process utilize in directing as well as managing the firm's business matters so as to improve success as well as corporate accounting with the definitive objective of achieving definitive value for stakeholders when putting into consideration the interests of additional stakeholders (Authority, 2002). The Kenyan Corporate governance policies as well as practices promote the concept of separation of ownership and control, especially in the listed firms. Separation of ownership and control often results in agency costs and agency problems between shareholders and the management, where managers can participate in earnings management. Corporate governance in Kenya is mainly informed by the Anglo-US model, which is identifiable by individuals and institutions ownership, as well as a legal mechanism which defines stakeholder rights and obligations (Koech, Namusonge, & Mugambi, 2016).
The stakeholders to the firms' financial reporting are the boards of directors, management, shareholders, government agencies (usually regulators), and consultancy firms that provide advice to companies on corporate governance. However, shareholders are the main stakeholders in Kenya. The research aimed to investigate the effect of shareholder activism (blockholders and institutions), who have been singled out by extant literature to closely monitor managerial activities.

LITERATURE REVIEW

Agency Theory

The theory by Michael Jensen and William Meckling proposes that, where there is a discrepancy of interest (agency conflicts) between the principal (shareholders) and the agents (management), monitoring should be conducted by the shareholders achieved through shareholder activism. The firm owners may achieve this monitoring through activism executed by the blockholders and the institutional shareholders. In earnings management, the managers manipulate financial reports for their own personal interests bringing about the agency conflicts between the parties. The investors' main goal would be to recover their capital on investment, but the management are more likely to concentrate on their particular individual priorities, including that of the consummation of the position's privileges as noted by Jensen and Meckling (1976).

The conflict of interests arising between agent and the principal can be avoided or minimized through the implementation of a good governance mechanism (Lukito Setiawan, 2006), such as active ownership structures and other internal controls. The agency model indicates that, as a consequence of self-interest, the principals have little or no justifications for trusting their agents, and they might strive to overcome such problems by establishing mechanisms that harmonize their interests with those of their agents. The tendency to manage earnings is reduced once the interests of the administration/management and that of the shareholders are aligned via effective governance mechanisms (Cheng & Warfield, 2005; NAZIR & AFZA, 2018).

Blockholder Ownership and Earnings Management

The role of ownership structure, specifically large shareholding on earnings management has become a topic of a continuing philosophical discussion. Financial reporting acts as a crucial instrument for information transfer between the top management and firm shareholders in the capital markets. According to Dou, Hope, Thomas, and Zou (2014), a

few information is recognized concerning the effects of blockholder ownership on the firms' financial reportage, and interestingly extant literary works provide mixed reactions and conclusions about the connection between large shareholders and earnings management.

Jensen and Meckling (1976) in their seminal paper argued that monitoring of management by external blockholders reduces agency costs. Additionally, subsequent studies (e.g. Bos & Donker, 2004; Marrakchi Chtourou, Bedard, & Courteau, 2001; Yeo, Tan, Ho, & Chen, 2002) emphasized on the role of outside blockholders in effectively controlling financial statements preparation process, which diminishes the propensity to modify the outcomes by managers who might exercise their discretion in reporting firm performance.

Ho_1: *Blockholder ownership has no significant effect on Earnings Management among publicly listed firms in Kenya*

Institutional Ownership and Earning Management

Institution ownership refers to the shares held by the government, institutional legal entities, financial institutions, foreign trusts and institutions, and other institutions by the close of the year (Widigdo, 2013). Existing literature indicate mixed views on the impact of institutional ownership on earnings management. Other scholars present a positive association with income-increasing earnings management whereas others evidence a negative connection. Firstly, is the point of view where institutional investors are identified as 'transient' owners whose eyes are excessively fixed on current earnings, who pressure management for short-term profit goals, resulting into earnings management (Rajgopal, Venkatachalam, & Jiambalvo, 1999). This therefore means that there is a rise in earnings management in the presence of higher institutional ownership. The argument that institutional shareholders are transient in nature suggests a positive association between the institution's share of stock and the absolute value of discretionary accruals (Rajgopal et al., 1999).

The second point of view is that of an oversight function that institutional investors execute. Scholarly works have equally registered a negative relationship between earnings management and institutional investors. Institutional ownership is considered better in lessening the actions of earnings management. This is because institutional shareholders are known to be active investors and the management do not fool them easily (Kusumaningtyas, 2012). Institutional investors directly link with the top management making them well positioned to raise concerns where necessary, especially on matters about financial reporting.

HO_2: *Institutional ownership has no significant effect on Earnings Management among publicly listed firms in Kenya*

Conceptual Framework

The research sought to investigate the effects of shareholder activism on earnings management. Blockholder and institutional shareholder activism were the independent variables, while earnings management was the dependent variable. The study controlled for firm size and firm age.

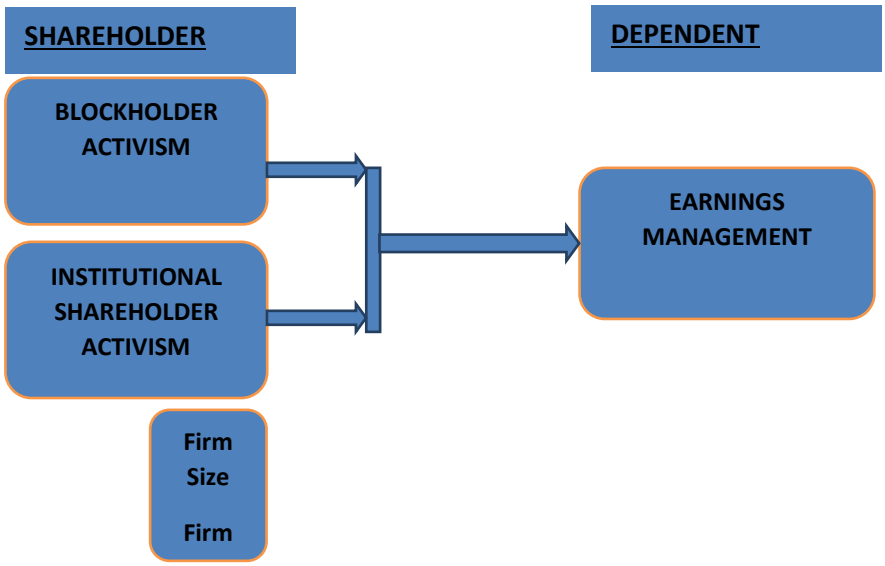

Figure 1: Conceptual Framework

METHODOLOGY

The study adopted a positivism philosophical approach towards arriving at the conclusions on the research problem. A positivist philosophy accepts ideas regarding reality and truth. It suited the research as it comprises of the objectivity assumption, which considers the researcher as being an objective observer and a data reporter by sample collection procedures, variables measurement and statistical analysis (Vanderstoep & Johnson, 2008).

An explanatory research design and a panel approach were used in arriving at the study's conclusions. This research design was suitable as the study sought to explain the cause-effect relationship between the research variables. A research design has been stated as a strategy, structure and plan of examination so regarded as to find responses to research the queries or problems (Kumar, 2011).

The study focused on a target population of 35 firms recorded at the NSE that were consistently in operation during the study period. The data set was 490 firm-annual comments for firms recorded and operational at the Nairobi Securities Exchange for fourteen consecutive years between the periods 2004 to 2017. Secondary data attained from the yearly audited financial reports of firms recorded at the Nairobi Stock Exchange were analyzed.

The dependent variable of the study is earnings management while the independent variable is shareholder activism whose constructs are blockholder and institutional ownership structures. The study controlled for Firm size and firm age as they might have an implication on the firms' level of earnings management. *Earnings management (EM)* was evaluated by discretionary accrual which was given by the residuals of the Non-discretionary accruals expectation model in line with the improved Jones model developed by Dechow, Sloan, and Sweeney (1995). The expectation model was used to obtain the

coefficients α_1, α_2 and α_3 which gave the predicted Non-discretionary accruals for different firms. The model is indicated in Equation 1:

$$\frac{TA_{it}}{A_{it-1}} = \propto_1 \frac{1}{A_{it-1}} + \propto_2 \frac{\Delta REV_{it} - \Delta REC_{it}}{A_{it-1}} + \propto_3 \frac{PPE_{it}}{A_{it-1}} + \varepsilon_{it} \text{.....Equation 1}$$

Where:

TA_{it} Refers to the Total Accruals in year t

A_{it-1} Refers to firm i's Total Assets at the end of year t-1

ΔREV_{it} Refers to firm i's revenues in year t less revenue in year t-1

ΔREC_{it} Refers to firm i's Receivables in year t less receivables in year t-1.

PPE_{it} Refers to the gross property plant and equipment at the end of year t

$\propto_1, \propto_2$ and $\propto_3$ are the firm specific parameters

Blockholder Ownership (BOWN) as noted in Worldscope/Disclosure (1997) is the fraction of adjacently apprehended shares. It was measured by shares held by owners holding greater than 5% of the total shares (Al-Fayoumi, Abuzayed, & Alexander, 2010;Dou et al., 2014; Isenmila & Afensimi, 2012).

Institutional Ownership (IOWN) was evaluated by the number of shares possessed by the institutions, non-individuals in relation to the overall number of supplied as well as traded shares in the market of the stock exchange for every company (Maswadeh, 2018).

Firm size was evaluated as the natural logarithm of total assets (Elsayed, 2007), while *Firm age* was indicated by the year of observation minus the company's launching date, in order to determine the number of years it had been integrated before (Gregory, Ingram, & Brklacich, 2005). These measurements were adopted from previous studies on the research variables.

The overall multiple regression model for the study is presented in Equation 2 as:

$$Y_{it} = \alpha + C + \beta X + \mathcal{E} \text{.....Equation 2}$$

Where:

Y is the Dependent variable

α is the constant term or the intercept

C is the Control variable

β are the beta coefficients of the equation

X is the predictor variable

$\mathcal{E}$ is the error term

Data analysis and hypothesis testing were achieved through both descriptive and inferential statistical techniques. The hypotheses were tested at a 5% significance level. Correlation and regression analysis techniques were used to infer and to arrive at the conclusions. The specific regression model for the study is presented in (Equation 3) as:

$$EM_{it} = \beta_0 + \beta_1 FSIZ_{it} + \beta_2 FA + \beta_4 BOWN_{it} + \beta_5 IOWN_{it} + \mathcal{E}_{it} \text{.....Equation 3}$$

Where:

EM	=	Earnings Management
FSIZ	=	Firm Size
FA	=	Firm Age
□□□□	=	Blockholder Ownership
□□□□	=	Institutional Ownership
□$_{0.....}$□$_{7}$□	=	Coefficients of the equations
ε	=	error term
t	=	time
i	=	Firm

RESULTS

Descriptive Results

Table 1 indicates that the overall number of observations for the study was 490. The outcomes further show that earnings management had a mean (median) of -0.138 (0.005) which is analogous to that in Puat Nelson and Devi (2013), and Albersmann and Hohenfels (2017), where they found a negative average discretionary accrual. This is an indication that the firms involve in earnings management as well as that on average they participate in income-reducing earnings management though at minimum levels.

The study also conducted a univariate analysis on Blockholder Ownership (BOWN). Majority of the firms had blockholders with an average of 64.1% of the total shares. This is relatively adequate to conduct a monitoring role so as to reduce opportunistic managerial discretion that is directed on the reported earnings of firms.

On the other hand, Institutional Ownership had a mean of 65.1% of the total shares. The average indicates that the ownership structure by institutional investors is on the higher side, which is beneficial to the firms in terms of activism. Institutional investors in a firm have been previously reported by literature to play a crucial role in pressurizing management for better performance as well as in conducting a monitoring role to the management.

Firm size had a mean of 7.056 natural log of total assets. The results indicate much disparity in the size of firms recorded at the NSE. The firms operating at the NSE proved heterogeneous in terms of size and were highly dispersed. Firms recorded at the NSE are relatively old with the minimum being 18 years old and the oldest being 148 years. The results further shows a greater dispersion in the age of the firms, which is comparable to that of Sun et al. (2014).

Table 1: Descriptive results

Stats	N	Mean	Min	Max	Sd
EM	490	-0.138	-3.401	1.997	0.842
BOWN	490	0.641	0.200	0.980	0.182
IOWN	490	0.651	0.050	0.990	0.190
FS	490	7.056	4.806	8.747	0.713
FA	490	67.700	18.000	148.000	27.505

Unit Root

A time-series data is alleged to be stationary if its variance and mean are persistent over period (Gujarati, 2003). Hence, the series incline to drift about its mean because of the limited variance. The series may be displaying a trend (of a deterministic nature) or randomly determine (of a stochastic nature). To conduct a unit root test, the Harris –Tzavalis test was applied. This technique holds the assumption that: Ho: All panels comprise of unit root, and Ha: Panels are stationary. It is evident in Table 2 that for all the *p*-values, the null hypotheses were rejected at a 0.05 significance level for all the variables. This means there is no unit root in the data (stationarity holds). It implies that the means and variances in the data are independent on time and therefore the employment of the regression model can yield meaningful outcomes (Gujarati Damodar, 2012).

Table 2: Unit root test results

	Harris-Tzavalis Unit-root test		
	Statistic	**Z**	**p-value**
EM	0.5881	-6.121	0.000
BOWN	0.0003	-23.094	0.000
IOWN	0.6900	-3.176	0.001
FSIZ	0.0004	-22.625	0.000
FAGE	0.0000	-11.223	0.000

Fixed and Random Effects

The application of a panel data model utilizes any of the fixed effects or the random effects models to estimate the dependence relationship/association amid the variables. Panel data may suffer from the effects of the errors that result due to different firms within different sectors. Therefore, to determine whether to conduct the regressions using either the random or fixed effects models, a Hausman's test was carried out. The Hausman's test null hypothesis (Ho) states that random effect is suitable while the alternative hypothesis (Ha) states that the fixed effects model is appropriate.

The table 3 indicates that the chi-square value and its *p*-value (chi2= 3.98; p>0.05) were not significant. Hence, the null hypothesis stating that the random effect model is appropriate was not rejected. The Hausman's test concluded that, for the subsequent regression models to be conducted, a random effects model is suitable.

Table 3: Hausman's test results

	---- Coefficients ----			
	(b)	**(B)**	**(b-B)**	**sqrt(diag(V_b-V_B))**
	Fe	**Re**	**Difference**	**S.E.**
BOWN	-0.002	-0.000	-0.001	0.001
IOWN	1.353	1.073	0.280	0.209
FS	0.224	0.178	0.046	0.084
FA	-0.006	0.003	-0.009	0.009

b = consistent under Ho and Ha; obtained from xtreg

B = inconsistent under Ha, efficient under Ho; obtained from xtreg

Test: Ho: difference in coefficients not systematic

chi2(4) = (b-B)'[(V_b-V_B)^(-1)](b-B)

= 3.98

Prob>chi2 = 0.4082

Correlation Results

Pearson correlation was applied to indicate the strong point and the route of linear association between shareholder activism, control variables and earnings management. Table 4 illustrates that there is a negative as well as significant (r = -0.194) relationship between blockholder ownership and earnings management. Thus, it can be claimed from the foregoing that as the proportion of blockholders increase in a firm, then earnings management practices decrease significantly. The findings agree with the view of agency theory, where blockholders who are the largest owners closely monitor the activities of the management therefore reducing opportunistic earnings management. The same was echoed by Bharath, Jayaraman, and Nagar (2013) that blockholders danger of departure upon

realization of divergence of interests aligns managers' interest as well as shareholders' interests.

Institutional ownership alternatively was established to be having a positive and significant (r= 0.171) association with earnings management. This therefore can be interpreted to mean that higher proportion of institutional investors in a firm triggers an upward trend in earnings management. This observation is mainly because of the reality that institutions pressure the management for short-term performance, thus resulting into earnings management as a means of meeting targets. In support of the study findings, Latif and Abdullah (2015) also discovered a positive along with significant connection between institutional ownership and discretionary accruals.

Further, firm size showed a positive and significant (r= 0.123) relationship with earnings management. It follows therefore that a rise in firm size also raises firm earnings management. This is interpreted to mean large firms are extra possibly to get involve in earnings management actions as compared to small firms. The same findings were also evident in the previous studies of Puat Nelson and Devi (2013) and Gull, Nekhili, Nagati, and Chtioui (2018).

The output also indicate that firm age is positively and significantly (r= 0.219) correlated with earnings management. This is an indication that as the age of a firm increase, the likelihood of earnings management also increases. Thus, from the findings, it may be contended that older firms incline to participate in more earnings management as compared to younger firms which are still growing. This observation could be motivated by performance, where large firms are deemed to have more pressure to perform well at the declining stage, therefore compelling management to participate in earnings management so as to record impressive results.

Table 4: Correlation results

	EM	BOWN	IOWN	FS	FA
EM	1				
BOWN	-0.194**	1			
IOWN	0.171**	0.714**	1		
FS	0.123**	-0.279**	-0.153**	1	
FA	0.219**	0.136**	0.380**	-0.176**	1

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

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

Regression Results

A panel regression analysis was conducted to test the hypotheses for the effects of blockholder ownership (BOWN) and institutional ownership (IOWN) on earnings management (EM), when controlling for the effects of Firm Age (FA) and Firm Size (FS). Table 5 indicates that the overall model, was significant (F-value = 522.88; $\rho<0.05$), indicating the model was fit. The results also confirms that Blockholder Ownership (BOWN) has a negative and significant effect (β= -2.546, $\rho<0.05$) on earnings management. The p-value was less than 0.05 which is interpreted to mean that the null hypothesis stating blockholder ownership has no significant effect on earnings management was rejected. It is therefore concluded that the percentage of blockholding in a firm significantly affects earnings management. The negative coefficient means that a unit rise in the proportion of blockholder ownership reduces earnings management by 2.546 units. Blockholders are always viewed as activists, unlike small shareholders who give up easily and sell their shares when they detect any disappointment in the firm. Since blockholders have large

stakes in the firm, their proposals and queries are always taken into consideration by the management. This therefore makes the large shareholders to be an oversight and monitoring mechanism towards reducing agency problems, where management might participate in earnings management for their self-interests and hence the reduction in earnings management in the presence of higher blockholding. These results agree with the discoveries in Dou et al. (2014) and Bharath et al. (2013) where they also realized a negative influence of large shareholders on earnings management.

Institutional Ownership (IOWN) has a positive and significant effect (β= 3.01, $\rho<0.05$) on earnings management. It is therefore concluded that the proportion of institutional shareholders has a significant effect on earnings management. A positive coefficient on the other hand, indicates that a unit rise in the ratio of institutional ownership in a firm increases earnings management by 3.01 units. Institutional shareholders are transient investors who pressure the management for short-term performance, compelling them to engage in actions that increase income. For instance, management will involve in income-increasing earnings management so that they can achieve the short-term targets and impress their employers. Companies having elevated transient institutional ownership are additionally likely both to manage earnings skyward as well as direct projections downward so that adverse earnings surprises are avoided (Matsumoto, 2002). Likewise, income-decreasing actions such as income smoothing to indicate consistent growth may be the result. Institutional investors therefore compel management to participate in income-raising or income-reducing earnings management. These findings are consistent with that of Koh (2003); Matsumoto (2002),and Tehranian, Cornett, Marcus, and Saunders (2006), whose studies found a positive and significant effect between institutional shareholding and discretionary accruals.

The control variable Firm size (FS) had a positive and significant (β=0.171; $\rho<0.05$) effect on earnings management. Its positive coefficient indicates that a unit increase in firm size increases earnings management by 0.171 units. This therefore justifies for the need to control for firm size. It can therefore be argued that large firms manage earnings more as compared to small firms. This is because of the reality that the managements of great firms are beneath intense pressure to produce impressive results. The management therefore will manage earnings upwards or downwards to suit their targets. These findings are consistent with those found in Klein (2002), Xie, Davidson III, and DaDalt (2003), Puat Nelson and Devi (2013) and Reyna (2018), who found out that firm size has a positive and significant effect on earnings management.

Firm Age (FA) had a positive and significant (β=0.006, $\rho<0.05$) effect on earnings management. The positive coefficient shows that a unit increase in firm age increases earnings management by 0.006 units. This therefore justifies the need for controlling the effect of firm age in the model. From the results, it can be concluded therefore that older firms participate in extra earnings management as related to young firms. The firms' life cycle justifies the fact that they perform well during early stages and experience continued growth until the declining and maturity phase where they are older enough to start experiencing declining performance. This refers to the situation where managers are under pressure to register continued growth in performance irrespective of maturity of the firm. They are consequently compelled to take part in earnings management so as to maintain an impressive image of the firm.

Table 5: Regression results

		Number of obs	=	490		
Random-effects GLS regression		Number of groups	=	35		
Group variable: firmid		Obs per group: min	=	14		
R-sq: within	= 0.4714	Avg	=	14		
between	= 0.4045	Max	=	14		
overall	= 0.4417	Wald chi2(4)	=	522.88		
corr(u_i, X)	= 0 (assumed)	Prob> chi2	=	0.000		
	Coef.	Std. Err.	z	P>z	[95% Conf.	Interval]
BOWN	-2.546	0.293	-8.690	0.000	-3.120	-1.971
IOWN	3.010	0.274	10.990	0.000	2.472	3.546
FS	0.171	0.077	2.22	0.027	0.020	0.322
FA	0.006	0.003	1.99	0.047	0.000	0.012
Cons	-1.754	0.570	-3.08	0.002	-2.871	-0.637
sigma_u	0.350					
sigma_e	0.381					
Rho	0.458	(fraction of variance due to u_i)				

CONCLUSION

Shareholder activism; specifically active blockholders and institutional owners have a significant effect on earnings management. An increase in blockholder ownership in a firm reduces earnings management significantly. This observation provides support for an agency theory proposition which suggests a shareholder initiative through monitoring as a means of solving agency conflicts. Blockholders are viewed as activists who show more concern for managerial decisions due to their large stake of shares in the firm, unlike small shareholders who sell their shares easily if not impressed by managerial actions. Blockholders stick to the firm and raise concerns, thereby reducing managerial discretionary accruals management.

The study also sought to determine the effect of institutional ownership on earnings management. The findings conclude that institutional investors increase the tendency for managerial engagement in earnings management due their transient nature. Institutional investors exert more pressure to the management, therefore compelling them to participate in income-increasing or income-reducing earnings manipulation so as to meet the targets. This therefore generates a positive association between earnings management and institutional investors in a firm. An elevated ratio of institutional investors means higher earnings management. It is therefore the recommendation of the study for institutional investors to desist from being myopic in nature since this may trigger more earnings management in the firms. Blockholders should be influencing rather than selecting the firms' financial reporting practices. This is because their activism goes a long way in executing the crucial role of constraining earnings management within the firms.

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