

Abstract

Prior empirical studies have identified the existence of various stock return anomalies in several countries stock markets. In Some stock markets, return anomalies are discovered and then they disappear once traders exploit them to earn excess returns. Further, some of the return anomalies are more pronounced in some stock markets than in other stock markets. The purpose of this study was to test the existence of size, value, momentum; profitability and investment stock return anomalies at the Nairobi securities exchange in Kenya. Explanatory research design was adopted in establishing the existence of stock return anomalies at the Nairobi securities exchange in Kenya. The target population was 45 companies that were listed at the Nairobi securities exchange by January 2009 (after excluding companies that were not trading consistently and those that were delisted). A census of 45 companies was used to construct stock portfolios between 2009 and 2014. The existence of stock return anomalies was explored using sorts of returns on anomaly variables and multivariate regressions. The results of the hypotheses tests lead to a conclusion that size stock return anomaly, value stock return anomaly and investment stock return anomaly existence is statistically significant while profitability stock return anomaly and momentum stock return anomaly have an insignificant existence at the Nairobi securities exchange. The developed six factors model incorporating market risk and the five stock return anomalies proxies has a high explanatory power and its F-statistic value indicates that it is an adequate model for explaining some of the stock portfolio return variations (not explained by CAPM) at the Nairobi Securities Exchange in Kenya. This study recommends a policy framework for enhancing factor investing strategies at the Nairobi securities exchange. Factor investing policy framework is based on stock return anomalies that have been proven empirically by researchers to earn a stock return premium in the long run. In adopting a factor investment strategy, investment advisors, retail investors and stock brokers at Nairobi securities exchange should allocate more investment resources to small cap stocks than in big cap stocks, invest more in value stocks than in growth stocks and invest more in stocks of firms with low growth in assets in the current period than firms with high growth in assets in the current period for stock return optimization.