EFFECT OF FINANCIAL STRUCTURE ON FINANCIAL STABILITY OF NON-FINANCIAL FIRMS LISTED AT THE NAIROBI SECURITY EXCHANGE

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DECLARATION

I declare that this dissertation project is my original work that has never been previously published or submitted elsewhere for award of a degree. I also declare that this project contains no material written or published by other people except where due reference is made and author duly acknowledged.

Signature…  Date **November 2025**

Kabasa Denis Mbori

I do hereby confirm that I have examined the master's dissertation of

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And have certified that all revisions that the dissertation panel and examiners recommended have been adequately addressed.

Sign: ……. Date: ……..

Dr. Peter Kariuki.

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ABSTRACT

Non-financial companies listed on the NSE significantly contribute to the nation's economic growth by providing goods and services. However, these companies' financial soundness has been deteriorating in recent years. Poor financial structure consideration is the cause of this. Therefore, the study aimed to examine how financial structure affected the financial stability of non-financial companies listed on the Nairobi Securities Exchange in Kenya. Among its specific goals were to ascertain the impact of short-term debt on the financial stability of listed non-financial firms at the Nairobi Securities Exchange, the impact of retained earnings on the financial stability of listed non-financial firms at the Nairobi Securities Exchange, and the impact of long-term debt on the financial stability of non-financial firms listed at the Nairobi Securities Exchange. Pecking order theory, trade-off theory, and signal theory served as the study's guiding theories. This study employed a descriptive research design. The 44 non-financial companies listed on the NSE were the primary focus of this study. With panel data spanning 2018 through 2022, secondary sources were used to collect information on financial stability and structure. STATA 17 was used to analyze the data using statistical techniques such as multiple regression, correlation, and descriptive statistics. Diagnostic tests were conducted to check for heteroscedasticity, autocorrelation, multicollinearity, normality, and the Hausman test. Tables were then to be used to present the data. Following data analysis, the study found a positive and substantial relationship between the financial health of the non-financial enterprises listed on the NSE and retained earnings and long-term loans. However, there was no statistically significant correlation between short-term debt and the firms' financial soundness. Therefore, aside from short-term debts, the study's research showed that the financial structure components utilized to determine their association with the financial stability of non-financial enterprises listed on the NSE were statistically significant. This confirmed that the components of the financial structure in this instance had an impact on non-financial firms listed on the NSE; thus, according to the hypothesis, short-term debts had a negligible impact on financial stability, whereas long-term and retained earnings had a significant impact. Therefore, the study concluded that long-term and retained earnings had a strong and positive relationship with financial stability, while short-term earnings had a negligible impact. It also suggested that future research should investigate extrapolating other financial structure components and whether they will affect the financial stability of non-listed financial firms in the NSE. Their upcoming studies could also improve this to assess the difficulties non-financial companies listed on the NSE encounter when conducting business using various financial structure components.

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DEDICATION

I dedicate this piece of work to dear parents. A special sense of gratefulness to my wife and children who have been of great help through comforting and ensuring that I have ample time to carry out this research at a conducive atmosphere.

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ACRONYMS AND ABBREVIATIONS

ASEA African Securities Exchange Association

ERB Ethics Review Board

JSE Johannesburg Stock Exchange

NSE Nairobi Securities Exchange

NACOSTI National Commission of Science Technology and Innovation

OPERATIONALIZATION DEFINITION OF TERMS

Financial stability : This is the financial health of non-financial firms which is mostly enhanced through effectively an efficiency to enhance them operationalization's which is mostly supported by non-financial structures (Musau, 2018)

Financial structure : This is the method to which an entity funds its assets (Harjan, 2020).

Long term debts : In a firm, these are the debts which mature in more than one year (Václav & David (2017).

Retained Earnings : These are the earnings which are retained by the firm for the purpose of being ploughed back for investment or for repaying debts thereafter (Junya ,2018).

Short term debts : These are debts which mature within a period of one year (Major, 2018)

CHAPTER ONE

INTRODUCTION

1.1 Background of the study

Non-financial companies listed on the NSE manage financial assets by allocating investor savings to venture projects that are deemed worthwhile. In order to prevent a crisis, this helps to improve their financial stability (Nshimiyimana & Zubeda (2017). These businesses are consequently regarded as extremely critical as they are unable to operate when confronted with a financial crisis, which could impede their advancement. Their financial soundness is, consequently, crucial to the expansion of Kenya's economy since they are seen as one of the major contributors to overall economic development (Kalunda, 2015).

This is founded on the idea that these businesses, which do not deal with the financial context of their operations, have a significant impact on the country's well-being, particularly through raising the gross domestic product (Meshak & Nyamute, 2016). By providing a range of goods and services to both corporate and non-corporate clientele that are financially solid, this thereby facilitates economic growth overall (Mulwa, 2015). Therefore, non-financial companies listed on the NSE must have sound financial standing in order to stimulate the expansion of the Kenyan economy.

Globally, the Bangladeshi Dhaka stock exchange is having trouble because of financial problems brought on by operational instability, according to Islam et al. (2018). Haque et al. (2018) confirmed that economic uncertainty was the cause of the rise in listed financial institution failures in Bangladesh. According to the Pakistan Stock Exchange's experience, 12 industrial sectors were deregistered from the PSE as a result of financial difficulties (Ahmed, 2019). Canara Bank, one of

the important banks listed on the Indian stock exchange, experienced a financial catastrophe as a result of poor debt management (Koum, 2021). Kiriri (2018) confirmed that the wisest course of action for negatively impacted Block (SQ), a publicly traded company in the US, was to put the business under receivership because it was in a debt crisis and could not have continued to trade in the US.

In a regional context, the impact of the financial system on financial stability has also been observed in a number. According to Olatunde and Rasaki (2020), the retained earnings crisis was the primary cause of the difficulties Nigeria's banking institutions were confronting. Ifeanyichukwu (2021) asserts that retained earnings and dividend disbursements have an impact on share price numbers. From a similar perspective, Onyekwelu and Lucy (2019) observed that profits allowed businesses to make more capital investments, creating more assets for the company and influencing share price dynamics. Wehncke (2018) highlights the impact of retained earnings on market volatility while discussing the financial performance environment in South Africa. According to Wehncke (2018), this viewpoint maintains that economic performance has an impact on share price stability, which in turn affects financial performance attributes. Investors would be able to understand the company's prospects through decisions about dividend payments or earnings retention.

In local context, different studied have revealed the essence of financial structure as in the case of Odundo and Orwaru (2018) who established that bank size has an impact on the financial stability of Kenya's commercial banks thereby effectively inducing their operationalizations. Due to their sufficient assets, which have allowed them to remain financially secure, commercial banks listed on the NSE have been ranked among the best-performing institutions with effective operating capital (Wangila, 2017). According to Odundo & Orwaru (2018), Sasini and other listed

agricultural companies on the NSE have experienced operational issues as a result of financial volatility. Economic difficulties have been ascribed to the banking industry's incapacity to jeopardise its operations due to credit risk exposure to its central bank loans (King'ori et al., 2017). Dembel (2020), who confirmed that Kenya Airways Limited's cash problems have caused operational concerns since they are unable to satisfy their financial obligations, has also underlined this.

1.1.1 Financial Structure

The study employed use of retained profits, short-term debts, and long-term debts as components of financial structure. Financial structure has many components which can be utilized at different intervals but this study due to study time limitations and the aspect of non-composure to an inclusive to all components, it therefore considered use of the most convenient and direct components in order to inclusively and exhaustively considered. Because they have a direct effect on the financial stability of non-financial firms, strategic decision-making and overall financial performance may be impacted by the correlation between a company's financial and governance structures (Kiiru, 2018). Financing decisions are critical since the optimal debt-to-equity ratio influences a company's valuation and stock price on the stock exchange (Vătavu, 2020). Determinants of short-term and long-term debt are different; for example, collateralizable assets affect long-term debt but not short-term debt, and short-term debt is unaffected by the trade-off between tax benefits and bankruptcy costs (Ruri & Omagwa, 2018). Because it is thought to be less expensive, short-term debt is frequently chosen (Njanja & Pellisier, 2017).

Throughout a company's life cycle, financial structure is essential since it affects growth and increases shareholder wealth (Ishaya & Abduljeleel, 2018). Retained earnings, share capital, long- and short-term debt, forward contracts, convertible bonds, lease finance, and bond swaps are

just a few of the financing alternatives available to businesses (Dare & Sola, 2019). While equity capital finances only a percentage of an organization's assets, it is complemented by a variety of long-term financial liabilities, including bonds, bank loans, and trade payables (Gambacorta et al., 2020). Studies conducted in European nations have demonstrated a noteworthy inverse correlation between short-term debt ratios and financial success (Mokhova & Zinecker, 2019).

Retained earnings, or undistributed profits, and short- and long-term debt have a big impact on financial stability (Junya, 2018). Another crucial source of funding is sharing capital, which is the money obtained through the issuance of shares (Achieng et al., 2018). Businesses combine these sources to address their short- and long-term finance needs (Major, 2018). A company's debt-to-equity ratio, which is essential for evaluating business risk, is determined by its financial structure (Hamam et al., 2020; Islam et al., 2019). Fundamentally, the combination of debt and equity utilized to fund corporate operations is referred to as the financial structure. Short- and long-term debt and equity are the main constituents. One important measure of financial risk is the debt-to-equity ratio, which shows how well internal and external funding are balanced (Harjan, 2020). Businesses can maximize market value and attain financial stability by managing their financial structure well.in this study, retained earnings was used as on3e of the component of share equity due to the fact that retained earning directly impact on a company through aspects such as supporting growth and reinvestment hence becoming cost effective financing.

1.1.2 Financial structure and financial stability

Non-financial companies' long-term viability and operational success are greatly influenced by their financial stability. A company's capacity to sustain liquidity, solvency, and profitability in the face of financial shocks and economic volatility is reflected in its financial stability which is mostly evaluated through current ratios, quick ratios and cash ratios (Musau, 2018). Financial

Stability is directly impacted by a company's financial structure, which includes the proportion of debt and equity used to finance assets. Making efficient use of financial resources boosts investor confidence and operational effectiveness (Liu & Zhang, 2018). Accordingly, companies can reduce financial risks and maintain long-term growth by carefully balancing debt and equity financing (Brei et al., 2018).

The ability of businesses to carry out their activities effectively demonstrates the connection between financial stability and financial structure. According to Onuonga (2014), a balanced financial structure guarantees the best possible resource allocation, enabling businesses to fulfil their immediate and long-term commitments. Choosing the right financial structure is crucial for increasing operational effectiveness and reducing financial strain, claims Luseka (2021). The relationship between stability and financial intermediation emphasizes how important it is for businesses to match their financing plans with the demands of their particular industries and the state of the economy (Mostak & Sushanta, 2015). In addition to protecting businesses from excessive financial risk and promoting stability, regulatory frameworks also require financial prudence (Köhler, 2015).

An excessive dependence on debt finance frequently causes operational difficulties for non-financial businesses. Over-reliance on debt raises financial risk and can cause a company's position to become unstable during recessions (Berger & van Helvoirt, 2018). Businesses are nonetheless susceptible to funding limitations that impede asset acquisition and growth, even when they use financial intermediation to boost investor trust. This emphasises how crucial sound financial management is to maintaining long-term operations. In order to reduce risks and maintain long-term growth, listed non-financial companies on the Nairobi Securities Exchange (NSE) must

have strong financial structures. These companies operate in a variety of industries, including manufacturing, retail, and construction (Mwaura & Nyambura, 2022).

Key factors that determine a firm's capacity to meet its financial obligations, including liquidity, profitability, leverage, and solvency, are frequently used to evaluate financial stability (Ndegwa et al., 2021). Maintaining investor trust and competitiveness in a dynamic market requires striking a balance between operational efficiency and financial resilience (Wanjiru, 2023). The decision between debt and equity funding greatly impacts the financial health of a company. Excessive leverage can result in financial trouble, especially during economic downturns, even while debt financing might offer quick resources (Muturi & Ngugi, 2021). Equity finance, on the other hand, provides financial stability but may also reduce ownership control; therefore, companies must use strategic financial planning to ensure long-term viability (Wainaina, 2023).

Macroeconomic factors such as interest rates, inflation, and currency rates aso impact financial stability. Growing inflation has a detrimental impact on cash flow and profitability by reducing purchasing power and raising operating expenses (Kimani et al., 2021). Businesses engaged in import and export operations are exposed to currency risks as a result of exchange rate volatility. Businesses must use effective risk management techniques since interest rate fluctuations also impact borrowing costs (Kariuki & Kamau, 2022; Njenga, 2023). By encouraging responsibility, openness, and wise financial decision-making, robust corporate governance frameworks also contribute to financial stability (Otieno, 2022).

Another important factor that determines financial stability is cash flow management. Effective cash flow management techniques enable businesses to pay for debt repayment, cover operating costs, and reinvest in expansion, all of which contribute to long-term viability (Karanja, 2023). However, inadequate cash flow management can lead to liquidity issues, which compel

businesses to rely on costly outside funding. Businesses can preserve stability even in times of economic uncertainty by putting strong cash flow forecasting and working capital management techniques into practice (Waweru & Mwangi, 2020; Nyaga & Mutiso, 2021). By evaluating a company's capacity to maximize resource utilization and produce enough returns, profitability and efficiency ratios are also important markers of financial stability (Muthoni & Kamau, 2022; Ochieng, 2023).

Financial Stability is greatly impacted by industry performance and market conditions. To maintain revenue growth, businesses in competitive industries must constantly innovate and adjust to changing market needs (Muiruri et al., 2021). Strategic financial adjustments are necessary due to the impact of economic recessions, regulatory changes, and changing consumer preferences on profitability (Githinji & Njiru, 2020). Businesses can manage financial uncertainty and preserve stability by implementing cost-control and revenue diversification strategies (Wambugu, 2023). Furthermore, financial resilience is improved by putting risk management techniques like hedging, diversification, and financial instrument investment into practice (Kamau, 2023).

In conclusion, non-financial companies listed on the NSE must have strong financial standing since it affects their capacity to attract capital, maintain operations, and handle difficult economic times (Wanjohi, 2023). A company's financial resilience is influenced by a number of factors, including capital structure, market dynamics, corporate governance, cash flow management, profitability, risk management, and macroeconomic conditions (Ndung'u et al., 2022). A comprehensive strategy that combines external market changes with internal financial strategies is necessary to achieve long-term financial stability and guarantee corporate sustainability (Mutinda & Wainaina, 2021).

Key elements of the financial structure, such as short-term, long-term, and retained earnings, lie at the heart of financial stability. As an internal source of capital, retained earnings lessen the need for outside investment and lower the danger of financial crisis (Myers & Majluf, 1984; Graham & Harvey, 2021). By highlighting that moderate debt levels improve financial stability while excessive leverage raises hazards, the Trade-off Theory clarifies how to balance the benefits of debt with the costs of financial distress (Kraus & Litzenberger, 1973; Titman & Wessels, 1988). Despite being necessary for managing working capital, short-term debt raises liquidity risks and necessitates close supervision to avoid financial instability (Keynes, 1936; Diamond, 1991).

Examining the choice and effects of retained earnings, long-term debt, and short-term debt can help one grasp how financial structure affects the financial stability of non-financial companies listed on the NSE. A balanced financial structure improves operational effectiveness, promotes sustainable growth, and guarantees resilience against market swings. By combining good corporate governance, risk management, and financial planning, businesses can maximize their financial structure and attain long-term competitiveness and financial stability.

1.1.3 Non-Financial Firms Listed in NSE

The Societies Act of 1954 established the Nairobi Securities Exchange (NSE) as a voluntary association of stockbrokers in 1954. Its goals were to establish a securities market and standardize stock trading. When it started, commerce was conducted over the phone, and agreements decided processes. It comprised sixty-six equities that were quoted on public markets throughout the continent of East Africa. There have been a lot of changes, such as listing and automation (Yemi & Seriki (2018)).

Apart from being a member of the African Securities Exchange Association (ASEA), NSE enjoys being the fourth largest stock market globally regarding market capitalization and trading volume. For this reason, NSE enjoys large sectoral indices from every economic sector whose shares are doing well (Buigut & Soi, 2020). Currently, there are sixty-three (63) firms that are listed at NSE categorized into thirteen (13) different sectors comprising agricultural, automobiles and accessories, banking, commercial and services, construction and allied, energy and petroleum, insurance, investment, investment services, manufacturing and allied, telecommunication and technology, real estate investment trust and exchange-traded fund (NSE, 2022). Of the 63 listed firms at NSE, 44 are non-financials firms whereby the rest are financial firms. To determine whether financial structures have any bearing on the origins of financial stability, this study will concentrate on non-financial listed firms in NSE.

1.2 Statement of the problem

Non-financial firms play a crucial role in resource allocation, fostering economic growth, and enhancing a country's gross domestic product (Hasanovic, 2017; Dembel, 2020). These firms contribute significantly to per capita income and overall economic prosperity (King'ori et al., 2017). Despite their importance, many non-financial firms listed on the Nairobi Securities Exchange (NSE) face financial instability due to vulnerabilities associated with their financial structures, raising concerns among industry stakeholders (Fletcher et al., 2018).

The growth rate of non-financial firms listed on the NSE has declined, impacting their return on equity. According to NSE (2023), the return on equity for these firms fell from 27.3% in 2020 to 26.72% in 2022, largely due to the economic downturn triggered by the COVID-19 pandemic. This decline has reduced their income streams and return on investment, contributing

to financial instability. For instance, Kenya Power and Lighting Company reported significant losses, highlighting the impact of financial structure vulnerabilities on firm stability.

Existing studies have examined financial stability in different contexts. Onuonga (2014), Wangila (2017), and Karugu et al. (2018) found that capital levels significantly affect the stability of commercial banks. Githinji (2016) observed that operational efficiency influences financial stability in Kenyan banks, while Mennawi (2020) reported a negative correlation between credit, financial leverage, and the performance of Islamic banks in Sudan. Additionally, Mafumbo (2020) noted that loan management significantly impacts the financial performance of Uganda's commercial banks. However, these studies focused on different financial sectors and geographic contexts, leaving a gap in understanding the financial stability of NSE-listed non-financial firms. This study aims to bridge that gap by examining the effect of financial structure on the financial stability of non-financial firms listed on the NSE.

1.3 Objectives of the study

The study was guided by both general and specific objectives

1.3.1 General Objective

To establish the effect of financial structure on the financial stability of listed non-financial firms at the Nairobi Securities Exchange, Kenya

1.3.1 Specific Objectives

i. To examine the effect of retained earnings on the financial stability of listed non-financial firms at the Nairobi Securities Exchange.
ii. To investigate the effect of long-term debts on the financial stability of non-financial firms listed at the Nairobi Securities Exchange.
iii. To determine the effect of short-term debt on financial stability s of listed non-financial

firms at the Nairobi Securities Exchange.

1.4 Research Hypotheses

H_{01}: Retained earnings do not significantly affect the financial stability of listed non-financial firms at the Nairobi Securities Exchange.

H_{02}: Long-term debt does not significantly affect the financial stability of listed non-financial firms at the Nairobi Securities Exchange

H_{03}: Short-term debt does not significantly affect the financial stability of listed non-financial firms at the Nairobi Securities Exchange.

1.5 Significance of the study

Non-financial firms are very critical entity in the economic development of a country. This is based on the fact that their existence drives the development of the financial firms especially in offering financial services in times of crisis as well as in return they refund the loan with interest which is a direct proportion operational benefit. Therefore, non-financial firms deal with goods and services hence their financial stability is determined by the source of their finances.

Businesses need to be aware of how their financial arrangements affect their overall financial health. This is based on the notion that people who are not obligated to think about the financial ramifications of their obligations to others eventually run into financial difficulties. This implies that in order to understand any repercussions that may lead to financial difficulties, the majority of publicly traded non-financial enterprises should routinely evaluate the basic concepts associated with economic structure. It is important to recognize that this study may be useful to a wide range of stakeholders, including managers who might notice early indicators of declining performance.

By educating managers about potential hazards associated with economic systems, this study will help them take proactive measures and lower the possibility of a financial crisis. It is possible to see the companies' economic structures. Investors can steer clear of risky enterprises by understanding the fundamental components (financial structure) that lead to financial distress. Investors can determine whether a company's economic issues are improving by examining trends in its economic structure. Lenders should be able to assess the firm's financial health accurately and seek warning indicators of imminent financial troubles to prevent capital losses and counterparty risk costs. Creditors may also monitor economic patterns to determine whether a financially troubled company is headed in the right direction.

Government agencies and listed company regulators, such as the CMA and NSE, use the results to develop stricter standards to enhance bankrupt businesses' performance. The study's recommendations may lead to a reinforcement of the financial structure funding policy. Future researchers in this area might broaden the conceptual and contextual scope of the study. Future research can expand and analyze the topic based on the research gap identified in this study, which has yet to be fully utilized and filled.

1.6 Scope of the study

The research aims to connect financial stability and financial structure in non-financial firms on the Nairobi Securities Exchange. The factors that match the investigation are retained earnings and long-term and short-term debts. Forty-four non-financial companies listed on the NSE were the subject of this investigation. Five years of audited financial records from 2018 to 2022 were used to collect secondary data. The study spanned five years to include the most recent data, align with the business cycle, and emphasize the trend over a longer time frame. Furthermore, five years are

often allocated for developing business strategic plans. Due to the public and verifiable nature of the listed firms' voluntary disclosures, they will be chosen.

CHAPTER TWO

LITERATURE REVIEW

2.1Introduction

This chapter evaluates the literature review of the particular study objectives. The themes and connections between retained profits, short- and long-term debt, and financial stability were all explored in the reviewed literature. The chapter also covers the operationalization of variables and the different theoretical frameworks supporting the particular goals of the study.

2.2 Theoretical Review

This study considered the Trade-Off Theory, pecking order theory and signal theory. Details about them are provided below.

2.2.1 Trade off theory

A fundamental idea in corporate finance, the trade-off theory of capital structure describes how businesses weigh the advantages and disadvantages of debt versus equity financing. The idea, which was first put forth by Kraus and Litzenberger in 1973, advises businesses to balance the tax benefits of debt—such as interest tax shields—against the costs associated with financial instability brought on by excessive leverage. This hypothesis was developed as a counterargument to the Modigliani-Miller theorem (1958), which maintained that capital structure had no bearing on a perfect market. The trade-off perspective emphasizes that businesses maximize tax benefits while limiting bankruptcy risks to optimize their debt-equity ratio, while acknowledging market flaws.

Many academics have contributed to the Theory's development, such as Myers (1984), who compared it to the Pecking Order Theory. The notion that businesses adhere to an ideal debt level

rather than steadily raising leverage has been validated by empirical study. Critics counter that while firms frequently exhibit lower leverage than the model predicts, real-world corporate behavior does not always match rigorous trade-off projections. Notwithstanding its drawbacks, the Trade-Off Theory is nevertheless a vital framework for comprehending business finance choices and has a lasting impact on financial study and policy.

The stability and financial structure of non-financial companies listed on the Nairobi Securities Exchange (NSE) are explained mainly by the Trade-Off Theory. According to the Theory, businesses aim to strike the best possible balance between the advantages of debt, including tax shelters, and the dangers of financial difficulty (Kraus & Litzenberger, 1973). According to studies on Kenyan companies, an ideal capital structure improves financial stability by guaranteeing sustainable leverage levels that do not expose businesses to excessive bankruptcy costs (Tale, 2014). For example, retained earnings reduce reliance on external debt and mitigate financial instability by acting as an internal financing mechanism. In line with the first research goal, which is to examine the impact of retained earnings on financial stability at the NSE, companies that prioritize retained earnings exhibit greater financial resilience (Ateya, 2023).

The second study goal is also supported by the Trade-Off Theory, which holds that businesses purposefully employ long-term debt to maximize financial stability. Long-term debt can improve liquidity and operational efficiency by providing investment money without the pressure of quick repayment (Oanda, 2021). However, if businesses cannot maintain sustainable debt servicing levels, high long-term debt may undermine financial stability. The notion that companies with well-structured long-term debt portfolios typically demonstrate higher financial stability than those that primarily rely on short-term financing is supported by empirical findings

from NSE-listed corporations (Moiro, 2022). This supports the idea that businesses actively balance the tax advantages of debt with the dangers of financial hardship to preserve stability.

Finally, in line with the third study goal, the Trade-Off Theory sheds light on the relationship between short-term debt and financial stability. Although short-term debt can increase flexibility and liquidity, it exposes businesses to working capital limitations, interest rate swings, and refinancing concerns (Mukumbi & Eugine, 2020). Because they find it challenging to roll over debt at advantageous terms, NSE companies with high short-term debt ratios are more vulnerable to financial instability, particularly during recessions (Irungu, 2022). According to the argument, businesses should restrict short-term borrowing to prevent severe financial hardship and bolster overall stability. Policymakers and managers of NSE-listed companies can balance profitability and risk exposure using the Trade-Off Theory to inform their financial structuring decisions.

2.2.2 Pecking Order Theory

This theory was proposed by Majluf and Myers (1984), the pecking order theory explained how a firm's choices affect how it finances its operations. As a result, the group would use its funds to cover its operations, with outside funding as the last resort. According to the hierarchy, activities would be financed by new debt first, retained earnings, and new equity (Rahma, 2021). Suppose the project's financial needs are smaller than the money raised internally, such as retained earnings. In that case, the company will use up all its cash reserves before looking into outside funding sources. Before seeking equity capital, external finance will first look for securities.

According to this theory, a firm cannot have a planned financial structure; its economic structure results from numerous short-term funding choices. One of these short-term financial decisions is selecting the funding option at a specific hierarchy stage (Simatupang et al., 2019). Profitable businesses utilize debt financing less frequently since they have significant retained

earnings over time. Furthermore, employing controlled earnings reduces business ownership or comes at minimal expense. As a result, they require less outside finance in the form of short- or long-term debt.

The pecking order theory also covers the cost features of the funding sources that influence the business's financing choices (Marimuthu & Singh, 2021; Simatupang et al., 2019). Regarding retained earnings, the company's sizeable retained earnings help to offset the additional expenses related to financing new initiatives. Retained earnings can be used by businesses to fund their operations and initiatives. By using retained earnings as the foundation for funding, businesses can reduce the time and expenses associated with starting new initiatives. Instead of aiming for a specific debt-to-equity ratio, the idea suggests that businesses base their financial decisions on a hierarchical process (Endri et al., 2021). Retained earnings-using businesses are at the top of the hierarchy, while external and debt funding are at the bottom.

The optimal financial structure is determined by the relative costs of raising these funds and the difficulties posed by aspects of information asymmetry. According to Andow and Wetsi (2018), the pecking order hypothesis explains how financing choices impact dividend payouts and mediates share price volatility and swings. Businesses typically retain their revenues rather than pay dividends because they prefer to use them to satisfy their financial obligations. The pecking order is crucial since this study looks at the relationship between retained profits and financial stability. Accordingly, this Theory will be crucial when non-bank companies listed on the NSE consider the hierarchical idea of pecking order through the connections between financial stability, long-term debt, short-term debt, and retained earnings.

The Pecking Order Theory (POT) highlights businesses' financing preferences, which greatly influence financial stability. According to the hypothesis, businesses would rather use

internal capital, or retained earnings, before pursuing debt financing, and only then would they consider equity financing as a last alternative. Because they rely on internal capital rather than excessive debt, organizations that adhere to the pecking order logic may have stronger financial stability regarding non-financial firms listed on the NSE. An excessive dependence on foreign debt raises financial leverage, which in turn raises the likelihood of financial hardship and has a detrimental effect on stability (Frank & Goyal, 2003). Companies with steady earnings and high retained profits are more financially stable because they are less vulnerable to changes in interest rates and pressures to repay debt.

2.2.3 Signaling Theory

The signaling theory was first proposed by Arrow and Akerlof in 1970. They had written an essay called "The Market for Lemons: Quality Uncertainty and Market Mechanism." The Theory was first created to explain how information asymmetry functions in labor markets and as a foundation for decision-making. Michael Spencer made significant contributions to the concept through a series of essays titled "Informational Aspects of Market Structure: An Introduction," which included Job Market Signaling Spence (1978), Spence (1976), and Spence (1974). A signal is also an action taken by a corporation that communicates information about its capabilities; according to Elkanah (2019), a signal is an observable activity or structure that represents a quality feature and is supposed to leave a positive impression on the recipient.

Information asymmetry exists when a company conducts business with its investors (Al-Najjar & Kilincarslan, 2018). The firm uses informational disclosures through various channels to reduce the material imbalance between the company's management and potential investors. The disclosures help reduce information asymmetries between the company's management and potential investors, as these asymmetries impact and influence share investments (De Jong et al.,

2019). As a result, investors are expected to base their evaluations of the firm's financial situation and growth prospects on less information asymmetry (Ahmad et al., 2018).

The signaling theory states that performing firms can differentiate themselves from underperforming firms by showcasing their value to the capital markets. Suppose the non-performing firm cannot replicate the signal generated by the performing firm. In that case, the performing firm will benefit from the signal of strong performance and the firm's value (Jaara et al., 2018). The cost of trying to replicate the signal produced by the performing business is the situation that results in the non-performing firm's incapacity to replicate the signal produced by the performing business.

Agency and moral hazard issues could cause firm management's actions to send the wrong signals, according to the concept. This concept has been questioned because of concerns about Authea Corporation's many signals and how those signals should be interpreted. In this environment, both performing and non-performing firms may present specific signals because it is difficult to distinguish between them, which complicates investment decisions (Ahmad et al., 2018).

Applying the signaling theory in this investigation is informed by the fact that it has been widely used to study the relationship between financial stability and structure. Several scholars have used the concept to explain the economic concept, including Pelcher (2019), Islam et al. (2019), Naz and Siddiqui (2020), Kengatharan and Ford (2019), and Wehncke (2018). The idea is relevant to our research because investors may receive the potential signals from the ratio of short- and long-term debt commitments. These commitments to short- and long-term debt inform the shareholders about the firm's financial stability, influencing their investment levels.

Financial managers must carefully structure capital to ensure that external financing choices reflect strong financial health, reinforcing long-term stability. Spence (1973) asserts that firms with strong financial performance signal their stability and creditworthiness by maintaining an optimal mix of equity and debt. For non-financial firms listed on the NSE, choosing a low-leverage structure sends positive signals to investors and creditors, indicating financial resilience and reducing the perceived risk of default. In contrast, firms that increase debt without strong earnings growth may signal distress, resulting in higher borrowing costs and financial instability.

2.3 Empirical Review

2.3.1 Retained Earnings and Financial Stability

According to Darmawan and Supriyanto (2020) study on the financial difficulties faced by Indonesian mining companies in order to forecast bankruptcy, keeping earnings in the asset ratio improved the financial difficulties of the company. The study also discovered that when internal funds are not utilized to pay for expenses like taxes, an organization's chances of avoiding financial difficulties increase. Due to its concentration on Kenyan companies registered on the Nairobi Securities Exchange, the study, which looked at Indonesia's mining sector, presented a contextual research gap.

With an emphasis on the connection between dividends and different indicators of financial stability, Neelanjana and Hassan (2019) examined how dividend policies affected the financial results of Malaysian manufacturing firms. Using multiple panel regression analysis, the study discovered a statistically significant negative correlation between market fluctuations and dividend payouts, a negative correlation between dividend payouts and financial success, and a significant correlation between systemic risk volatility and shareholders' financial stability. The study did not,

however, explore the apparent connections between retained earnings and the NSE-listed non-financial enterprises' financial stability.

In Okeke (2018) ex post facto study, which looked at the dividend policy and performance of a few public firms in Nigeria between 2010 and 2016, the explanatory variables were the dividend payout ratio (DPR), retained earnings (RE), and cash dividend (CD). According to the study, DPR and RE had significant and positive effects on performance, whereas CD had a negative and insignificant effect. Because the design struggles with determining if a particular occurrence is or is not an example of reverse causation, the current study employed a new research methodology to get around this restriction and extend the time scope.

Yemi and Seriki (2018) investigated the market value and retained earnings of Nigerian companies, modeling the estimation to take into consideration the dynamic nature of performance using a two-step system GMM. A random and fixed effects model was used to assess the panel data, which included 75 non-financial companies listed on the Nigerian stock exchange. The findings showed that whereas retained earnings, dividend payout, and earnings per share all had positive and substantial relationships with Tobin's Q, financial leverage had a positive but negligible relationship with it.

Naz and Siddiqui (2020) examined the effects of dividend policy on some parameters of financial performance. One of the topics covered was to consider the effect of dividend payments on volatility of Pakistani stock market. The study has used multiple regression analysis. Volatility that was used in the study was measured by the square root of the inequality between the greatest in addition to the less daily volatility in stock prices. This value was subsequently divided by the average volatility experienced in the price of stocks per day. The sample consisted of 10 businesses that were paying dividends at least during the last two years preceding commencement of study.

These business entities are publicly traded and are listed on Pakistan Stock Exchange. Based on the research, the actual payment of dividends had significant influence on several stock price volatility indicators. This was because of the announcements in relation to the payments of dividends where investors were enlightened about their chances of investing in the companies listed in the Pakistani stock exchange. The study also indicated a research vacuum on the effect of retained earnings on the financial stability of the non-financial enterprise listed on the NSE, not in Pakistan.

Lydia (2019) looked into how dividend policies affected the financial performance of businesses that were listed on the Johannesburg Stock Exchange Limited (JSE). After looking at data from 40 publicly traded firms from 2007 to 2016, the research panel concluded that the financial performance metrics were positively impacted by the dividend distribution. The study disproved the applicability of the agency theory by attributing the findings to the inclusion of 40 respectable JSE companies in its sample, whose shareholders trusted the management. The management of these businesses is trusted by the shareholders to distribute and pay dividends suitably.

By examining the impact of dividend policy on particular aspects of stock price volatility, Provaty and Siddique (2021) built on the research of Naz and Siddiqui (2020) and Lydia (2019). They discovered that investors were at risk of systemic harm as a result of the company's stock price volatility. Assuming that investors holding common shares in the study would bear systematic risks based on the rate of change in the share price over time, which was used to define financial performance, the study's methodology involved analyzing secondary data from 53 financial services companies listed on stock exchanges and calculating the payout as a percentage of annual earnings. Companies can enhance their financial performance by giving dividends

priority, according to the study's conclusion that dividend distribution had no discernible effect on the measures of stock price volatility studied.

The current research focuses on Kenyan non-financial enterprises listed on the NSE; hence, the study's analysis of Indonesia's mining industry creates a contextual research gap. Darmawan and Supriyanto (2020) investigated how Indonesian mining companies' financial difficulties affect their ability to predict insolvency. One of the study's conclusions was that a company's financial difficulties are lessened by retaining earnings in the asset ratio; it also discovered that when internal funds are not used to pay for expenses like taxes, the organization's chances of avoiding financial difficulties rise.

Yemi and Seriki (2018) investigated how retained earnings are related to the stock's valuation of publicly traded firms in Nigeria. Financial leverage, earnings per share and the dividend distributions were all measured during the examination. These modifications consider all the effects that might arise on the correspondence of market value and retained profits. The data from the analysis was sourced by considering 75 non-financial companies listed in the Nigerian Stock Exchange during a period of 2003-2014. The unbalanced panel data content of the study contained cross-sectional data, time series data. This information was obtained out of the annual financial reports in various companies. The principal techniques to identify the nature of the underlying relationship were descriptive analysis and multiple regression models. The study was able to find strong and positive correlations between firm value, dividend payments, retained earnings, and earnings per share. Even when the market value had a positive association with the financial leverage, it proved not to be statistically significant. This research was intended to address a gap in the existing literature by focusing on the empirical link between retained profitability and the firm market value, the context being what is observed in emerging countries.

Omotosho, Oladele, and Adeniyi (2017) also assessed the relationship between the performance of the stock market and the capital structure of the listed manufacturing companies in Nigeria between 2004 and 2013 within a setting of a multiple regression model. Conclusions of the study presented the impact that capital structure has on the financial performance of Nigerian listed bodies in the manufacturing sector. Collectively, these variables give an insight on the duration that the businesses can survive. The capital structure did not have any impact on the return on equity, but the revenue growth, earnings per share and the return on assets were highly affected.

Omagwa and Kasomba (2020) relied on panel regulation to examine how Kenya domestic commercial airlines perform in the market in relation to their financial frameworks. The study found out that, the utilization of lease financing did not affect the performance of the Kenyan domestic commercial airlines in the market, the financial performance of the Kenyan domestic commercial airlines was of great significance with the utilization of share financing, the financial results of the domestic commercial aviation sector in Kenya were of great significance when utilizing debt financing, and that the utilization of retained profits was of great importance in the market performance of Kenyan domestic commercial airlines.

To predict financial difficulties in the organization, Nketiah (2020) used the Altman model to explore the decision-making framework of the enterprise in relation to investments of US listed gas and petroleum companies over the panel data recorded between 2010 and 2019. As the dependent variable, the study looked at the connections between financial difficulty and working capital, retained earnings, pre-interest and tax income (EBIT), sales, capital market value, and economic disruption. The association between financial difficulty and working capital, income retained, and EBIT was investigated using panel-retrieval models; it was shown to be negative and significant. It has been demonstrated that retained earnings are less likely to result in financial

difficulties. The investigation looked at non-financial aspects, including working capital, in addition to retained earnings. In contrast to Nketiah's (2020) research, this study focuses on how a financial structure affects the financial stability of non-financial companies that are listed on the NSE.

In another study on financial distresses in companies in the context of Nigeria, Fredrick (2019) took several variables into consideration, including the size of the organization, its age, tangibility, debt ratio, profitability, and retained earnings. The PCSE has shown the connection of capital structure with the tangibility of the assets of listed corporations, profitability and financial troubles. But the variables used in the present study are theoretically different due to the fact that the present study uses the retained earnings and the financial stability of non-financial firms listed in the NSE as the primary elements of the study.

2.3.2 Long-Term Debts and Financial Stability

To get a stronger insight into the correlation between dividend policy and financial stability, Haque et al. (2019) performed a comprehensive analysis of long-term debt impact on the financial performance within the framework of the Dhaka stock exchange platform. The researchers considered secondary data of annual reports in 35 listed industrial corporations between 2004 and 2018. The findings of the study demonstrate the fact that long-term debt positively and insignificantly affects the financial stability indicators. This can be linked to the effect of businesses, which procure long-term loans at low dividends payment, which affects the volatility components.

In the Vietnamese setting, Bui (2019) looked into how long-term loans affected financial performance. The study examined the connection between financial success and dividend policy. Data for the study were gathered during six years, spanning the fiscal years 2011–2016, and 141

listed companies at the Ho Chi Minh Stock Exchange (HOSE) were used for sampling. The Long-Term Debt Ratio (LTD), a measure of long-term debts divided by total assets, was used to identify long-term loans. It was demonstrated that, however slightly, long-term debt enhanced the financial stability indicators. Because the current study is being conducted in Kenya, the study conducted in Vietnam revealed a contextual gap.

Lidivolo (2023) investigated the impact of long-term debt financing on the profitability of Kenyan commercial airlines. A cross-sectional research design was employed in the study. Eight airlines that operate in Kenya made up the target population. Using a secondary data gathering form and the census sampling technique, the secondary data for this study was obtained from the published accounts. Descriptive statistics included the mean, minimum, standard deviation, and maximum values. Correlational analysis, the Hausman test for fixed and random effects, and random effects models were examples of inferential statistics. The study's findings demonstrated that long-term debt financing has a statistically significant impact on Kenyan commercial airlines' profitability. Because the current study was based on non-financial enterprises registered in the NSE, the research design was different from the one used in this examination. Consequently, the results of different studies may differ.

Using a descriptive research approach and 10 domestic airlines operating in Kenya as the target population, Musangi (2022) examined the effect of funding and investment choices on the profitability of Kenyan airlines. A secondary data collecting sheet was used to look into descriptive statistics, and inferential statistics, like regression and correlation studies, were utilized to assess how strongly the variables were related to one another. The study identified a research gap since it concentrated on Kenyan Airlines, whose results would be very different from those of the current study, which was based on non-financial companies listed on the NSE.

Islam et al. (2019) looked at how long-term debt affected the bottom line and how dividend policy affected the Dhaka Stock Exchange's financial performance. Data from 14 distinct company categories at the Dhaka Stock Exchange were gathered for the study using a cross-sectional research design between 2012 and 2018. It discovered a negative correlation between financial success metrics and debt growth. The present investigation will attempt to clarify the relationship between debt and the elements of financial stability of non-financial enterprises listed on the NSE, which was not covered in the study. The study came to the conclusion that the total of the returns on share price increases and losses can be used to evaluate economic performance.

Mselmi et al. (2020) investigated the connection between company size, solvency ratio, profitability, and economic hardship in French SMEs using Logit, Vector Support, and Hybrid Models. Empirical studies have demonstrated that financially troubled organizations have lower levels of resourcefulness, repayability, and solvency, as well as poorer liquidity, profitability, and solvency ratios (high long-term loans). There are contextual anomalies because the study was carried out among French SMEs that were not listed. This study contrasts a contextual viewpoint, in which non-financial companies listed on the NSE will be the focus of the current investigation.

A model that could be used to forecast financial troubles in farming enterprises across Europe was created by Václav and David (2017). Long-term debt ratios, profitability, and liquidity were among the study's criteria, along with logistic regression, adaptive boost, vector support, and decision-making grounded in decision-making theories. The researchers discovered that while there is a high association between financial issues and long-term debt, the average accuracy of financial crisis projections declines as bankruptcy draws near. While the study focuses on financial hardship prediction models, the current study is based on financial stability based on long-term

loans. A conceptual research gap is revealed by the study's emphasis on long-term debt and other financial structural indicators.

In addition to macroeconomic, accounting, and industrial aspects, Khoja et al. (2019) looked at financial ratios using the fluidized analysis hierarchy (AHP) technique and the decision-making strategy (MCDM). Long-term debt and operating revenue per air kilometer are two important factors in this industry that could cause problems, according to the study, which identified and grouped these crucial components according to their relative importance. The research examined industrial, macroeconomic and long-term loan problems. The financial structure includes long-term debts and this is the key topic of the present research. The existence of this structure affects the financial nature of non-financial listed companies on NSE. As a result, the lack of conceptual research is present. Conversely, the analysis found out a positive association between long-term to total debt ratio and market success of the firm.

In the study by Vu et al. (2020), the authors examined the market performance of non-financial enterprises listed on the Hanoi Stock Exchange over the period of 2010-2017 through the prism of the distribution of the maturity 22 schedules of the firms. As per the results of the study, the long-term debt financing eroded the advantages of investing in a firm, which had a detrimental effect on its overall success in the market. In a large sample of annual financial statements of private enterprises in Belgium, De Meyere, Vander and Cauwenberge (2018) addressed the question of the association between the maturity pattern of the company debt and the quality of subsequent profit forecasts with privately owned companies. The results yielded that there was a positive relationship between debt long term and total debt and between the probability of long-term debt and profit quality. Also, they showed that the average percentage of exposure by creditors was higher when it comes to small businesses and this lowers down the risk which is

related to the theory of the banks being excessively exposed to low businesses and the SMEs having received more benefit in these networks than the larger enterprises, particularly those privately owned.

Using data from the 2008 subprime mortgage crisis, Adjei (2019) investigated the connection between a company's debt dependence and its resilience to a financial catastrophe. The study discovered that the more debt a company took on during the crisis, the worse its performance was, and that a company's pre-crisis to crisis performance declines as its level of debt dependence increases. The study discovered no connection between the new loans that low-debt businesses took out during the crisis and their financial performance.

Ismiyanti and Mahadwartha (2018) looked into how the market performance of enterprises was affected by the types of debt linked to debt-constraint expropriation (DCE) and debt-facilitated expropriation (DFE). To bolster the primary concerns in DCE and DFE, they also evaluated other ownership structures, including group and no-group-affiliate ownership. With DFE having a negative correlation and DCE having a positive correlation, it was evident that DCE and DFE had opposing effects on leverage and performance. Due to risk-reduction tactics, connected firms' debt had less of an influence on their DFE performance than that of independent businesses, while debt had the strongest positive effect on the DCE performance of group-affiliated businesses.

The impact of corporate financial structure on the stock market performance of companies listed on the Nigerian Stock Exchange was investigated by Onwe, Mustapha, and Yahaya (2020). The study's data came from audited annual financial statements, and market performance was examined using the ratios of long-term debt to equity and short-term and long-term debt to total assets. The data suggests that return on assets and short-term debt as a percentage of total assets are statistically and negatively correlated; this relationship establishes a reciprocal link between

short-term debt and total assets. Even if it is not significant, the long-term debt-to-equity ratio has a positive impact.

The primary finding of the study was the substantial positive relationship between management compensation, the debt ratio, and the market performance of publicly traded Kenyan manufacturing companies. In order to ascertain the connection between market performance and debt levels, Njoroge, Mathenge, and Omurwa (2020) looked at publicly traded Kenyan manufacturing companies. Using secondary sources and a census-based technique, information was gathered on 15 businesses that were involved in the sector between 2010 and 2018. It shows how Kenyan industrial companies listed on the Nairobi Securities Exchange's pay-performance mix are impacted by debt.

Using multiple regression, Songhor (2018) examined a number of variables in addition to financial architecture to evaluate financial challenges. The study found that financial challenges were negatively correlated with the financial leverage measurement method, but positively correlated with liquidity, productivity, solvency, and asset utilization. It also examined the impact of debt financing on the financial difficulties faced by Nairobi Securities Exchange companies. There is a conceptual research gap because, although both short- and long-term debt ratios have been employed, other factors not included in this study have been omitted.

2.3.3 Short-Term Debt and Financial Stability

The topic of financial stability has drawn the attention of numerous scholars. The impact of Vietnam's dividend program on the country's financial performance and the connection between debt and economic results were examined by Nguyen et al. (2020). Data for the study came from the Hochiminh Stock Exchange (HOSE) in Vietnam, specifically the financial records of 260 businesses between 2009 and 2018. Short-term debt and economic outcomes were found to be

correlated by the study's computation of the ratio of short-term loans to total assets. But it's important to explain this discovery and highlight a knowledge gap that the current study will try to fill.

Regression analysis produced the debt-to-equity ratio and return on equity, which are stand-ins for capital structure and financial performance, respectively, according to Kaumbuthu (2019). To the degree that this study seeks to do so, multiple areas had to be included in order to generalize the findings. Discovered that between 2004 and 2008, the NSE's industrial and allied sectors suffered from capital structure and financial stability due to ROE and the debt-to-equity ratio. Consequently, the results imply that industrial sector companies favor equity over debt, which calls into question the pecking order theory once more.

Okeyo's (2022) study, which employed a descriptive research approach, looked at the connection between short-term debt financing and Kenyan airlines' profitability. It found that retained earnings, share capital, and both short-term and long-term debt financing had a beneficial effect on Kenyan airlines' financial performance. Ten airlines that operate in Kenya made up the study's population, and a secondary data collection sheet was used to gather secondary data from published accounts. The secondary data were analyzed using STATA version 15 as the descriptive and inferential statistics were employed to assess it, and the results were presented in a table and figures form. Nevertheless, there was a geographical gap that the study under consideration attempted to overcome due to the fact that the case study of the research was not the same as that of the current one.

In the study by Karuma (2023), the researcher applied descriptive design to assess the impacts of debt financing on the financial performance of industrial firms listed in Kenya. The implications of the study revealed that debt financing had a positive and notable impact on the

financial performance of listed industrial firm in Kenya. The target audience of the study were the nine manufacturing companies listed on the NSE in the period between 2013 and 2017. Data collection sheet was designed on a secondary basis to collect the data regarding the study and relationship between the independent and the dependent variable was examined with the help of a linear regression model. Since the research was conducted among industrial firms and not non-financial companies on the NSE, there is likelihood that the findings could be different to the current study thus doubtful.

According to Mwangi et al.'s (2019) analysis of the association between working capital management and non-financial firms listed on the NSE an aggressive financing approach considerably enhanced ROE and ROA. A non-experimental explanatory study approach was employed to analyze secondary panel data from non-financial enterprises from 2006 to 2018.

Makori and Jagongo (2019) investigated the connection between the profitability of manufacturing and construction firms listed on the NSE and working capital management. They discovered that whereas profitability and the cash conversion cycle were negatively correlated, profitability and the number of days of inventory and days receivable were positively correlated. Data from 2006 to 2018 were analyzed using ordinary least squares regression models and Pearson's correlation. Since the current study will aim to specifically examine the impact of short-term debt on the financial stability of non-financial enterprises listed in the NSE, this study highlights a research gap.

After being adjusted for market comparability, Maina, Olweny, and Wanjau (2018) studied short-term debt. They specifically wanted to assess the importance of observable leverage. The study sample consisted of 35 non-financial subsectors out of the 65 listed companies on the NSE. The 18 companies in the banking and insurance sectors were not included in this investigation.

These 20 businesses were excluded due to the stringent capital structure requirements for these sectors. Every variable's information was extracted from the secondary data collection sheet using the listed companies audited financial statements from 2006 to 2015. The observed leverage, which stands for the Loan to Debt Ratio (LDR), and the performance measures exhibit a positive and statistically significant link, according to the panel regression approach. When Troubled Debt Restructuring (TDR) is utilized as a lever, performance metrics decline. Consequently, it may be said that listed companies are implementing debt and noncallable bonds to enhance market performance. This is because long-term debt instruments have a longer lifespan than short-term money market securities.

Ganiyu et al. (2019) looked into the relationship between capital structure and market performance in Nigeria. They also took into account the anticipated U-shaped correlation between ACF product capital structure and market performance. The idea states that when companies depend too much on loan capital, the relationship will break down. The sample, which employed a dynamic panel model, consisted of 115 publicly traded non-financial enterprises from Nigeria. The Generalized Method of Moments (GMM) was employed in this study to assess the persistence of the dependent variable. This was accomplished by adding the variable's lagged value as an explanatory variable to the regression model. The most significant results, which are in line with benchmark findings, demonstrate a robust relationship between capital structure and market performance when only slightly more debt financing is used. The authors found evidence of a U-shaped relationship between market performance and capital structure. This is the situation because Nigerian enterprises frequently use debt finance.

In order to assess the impact of the debt structure, a component of capital structure, on the market performance of banks listed on the Ghana Stock Exchange between 2010 and 2019, Gatsi

(2020) used a panel dataset that was large enough. Data shows that the funding structure of listed Ghanaian banks is only 17.77% equity and 82.23% debt. Over 81% of the debt held by publicly traded Ghanaian banks is short-term, whereas only about 9% is long-term. Short-term debt improves the market performance of Ghanaian listed banks, whilst long-term debt has the opposite impact.

A study on the effect of capital structure on the return on assets, stock price, and market value of companies listed on the Nigerian stock exchange was carried out by Uwalomwa and Uadiale (2018). The sample consisted of 31 companies that were listed on the Nigerian stock exchange. To examine the claims, they estimated models using Ordinary Least Squares (OLS). The information was extracted from annual reports published from 2005 to 2017. The study showed how short-term borrowings and shareholder capital enhanced market performance for publicly traded companies in Nigeria. Studies have shown that the performance of a business in the market decreases when it possesses high debt. Nyamita, Dorasamy, and Garbharran (2015) were interested in ascertaining the impact that debt financing made on the performance of the Kenyan state-owned businesses in 2015. They compared the total assets and deducted the equity covering the period 2002 and 2012 in order to determine the financial risk that the state-owned enterprises assumed. Market performance indices (ROA, ROI, and ROE) were incorporated as the dependent variable through panel data regression models, (i.e., Fixed Effects (FE), Random Effects (RE) and Generalized Method of Moments (GMM) models). The results indicate that Kenyan SOEs run on debt financing which has a negative impact on their performance on the market.

Kholisoh and Dwiarti (2020) examined the correlation between the significant organizational characteristics and the macroeconomic indicators to model the financial stability.

This had them raising that the amount of slight effect between capital structure and present assets was large compared to inflation and interest rates.

Zulkarnain (2015) developed a model that was used to predict financial issues in the business environment and implemented the model to observe the likely death of Malaysian businesses that were already in financial distress. Some of the main areas of focal points included cash on total assets, inventory sales, asset turnover, total asset stock and short-term loans on total assets. This study was carried out in Malaysia, which is a developed nation with highly developed securities markets, and hence the findings of the study cannot be implemented in Kenya, thus a research gap exists. In checking the relation of short-term commitments to assets, as a measure of liquidity, to financial trouble, the data analysis of Z, provided an inverse relation

2.4 Overview of the Review of Literature and Knowledge Gap

The association between financial competence and financial structure metrics, including retained profits, long-term debts, and short-term debts, is found to have a number of gaps, according to the literature review. The four types of knowledge gaps are conceptual, theoretical, methodological, and contextual. Appendix II contains this information.

2.5 Conceptual Framework

In order to answer the exploratory questions, this study used a conceptual framework, which has one independent component and three dependent components. Reichel and Ramey (2017) discussed how important it is to set research goals and ensure that they are consistent with each other to arrive at reasonable findings. A conceptual framework can help make adjustments that enhance the study by streamlining the interpretation of results when the research is easy to understand (Smyth, 2018). The study described financial structure as a function of retained

earnings, long-term debts, and short-term debts. The underling concept for using retained earnings over the other source of capital in this study was because it offers cost free, internal funding source for growth, avoiding interest payments and loan restrictions unlike external debt or equity. More to that, retained earnings provide flexibility for investing in opportunities and acts as a financial cushion for stability and resilience during tough economic times and therefore non-financial firms listed in NSE can easily utilize retained earnings in case of operational crisis and be able to redeem themselves.

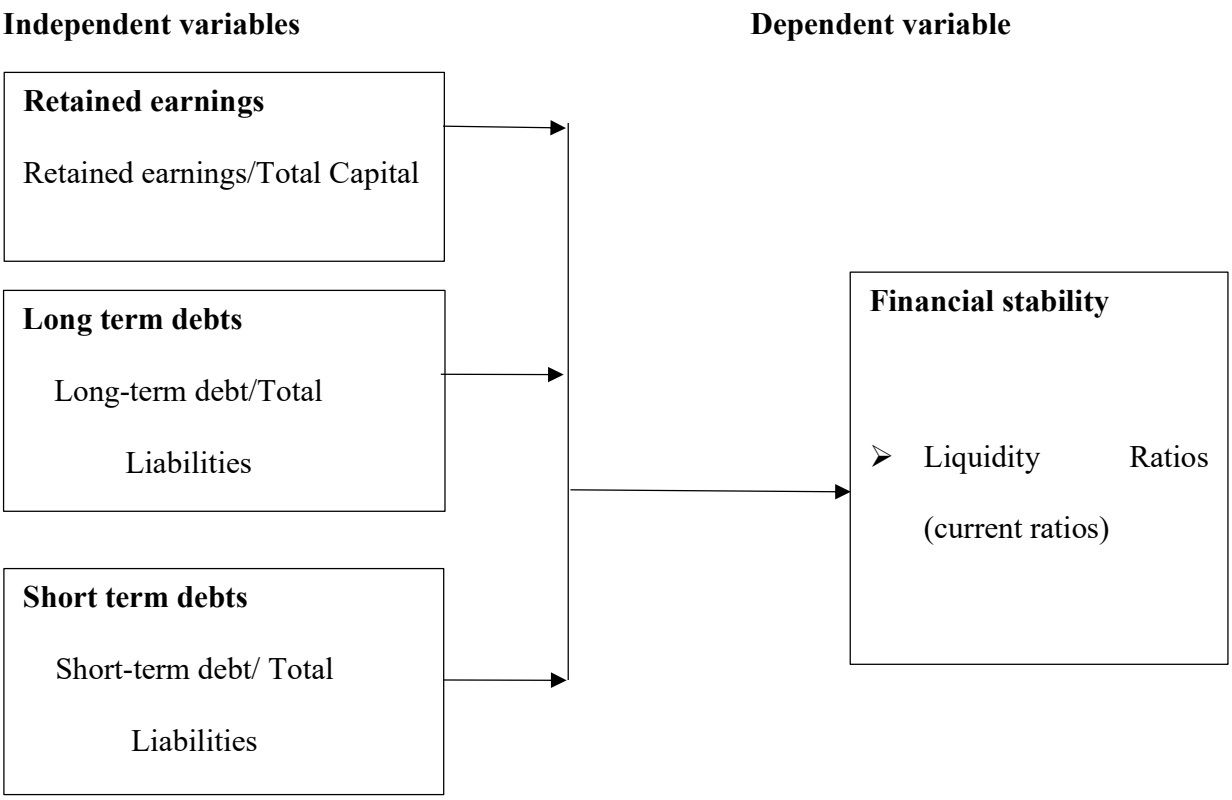

FIGURE 1

Conceptual Framework

2.6 Operationalization of variables

The first stage in operationalizing a variable or concept is to identify it so that it can be measured or articulated quantitatively or qualitatively, according to Mugenda & Mugenda (2013). Because

some variables are inherently difficult to measure, operationalizing them is essential. The design's quality and effectiveness are enhanced by precisely describing the variable. When the study's variables are operationalized, they become more robust, transparent, and often utilized. This section explains the methodology for measuring the identified variables using the data collection tool displayed in Table 1.

TABLE 1

Operationalization of variables

Variable	Type of Variable	Indicators	Measurement Tool	Source
Financial stability	Dependent Variable	Current ratios	Ratio scale	Musau (2018)
Retained earnings	Independent Variable	Retained earnings/Total Capital	Ratio scale	Okeke and Okeke's (2018), Fredrick (2019)
Long term debts	Independent Variable	Long-term debt/Total Liabilities	Ratio scale	Bui (2019), Khoja et al. (2019)
Short term debts	Independent Variable	Short-term debt/ Total Liabilities	Ratio scale	Nguyen et al. (2020) Maina, Olweny, and Wanjau (2018)

2.7 Research Gaps

The existing literature on financial stability in non-financial firms listed on the Nairobi Securities Exchange (NSE) presents several research gaps. Contextually, studies such as Darmawan and

Supriyanto (2020) on Indonesian mining firms and Neelanjana and Hassan (2019) on Malaysian manufacturing enterprises are not directly applicable to Kenyan non-financial firms. Similarly, studies by Naz and Siddiqui (2020) and Lydia (2019) focused on dividend policies in Pakistan and South Africa, respectively, but did not examine the role of retained earnings in financial stability, leaving a conceptual gap. Provaty and Siddique (2021) analyzed dividend policy effects on stock price volatility but overlooked retained earnings, while Nketiah (2020) used the Altman model to assess U.S. gas and petroleum firms, making the findings less relevant to NSE-listed non-financial firms. Fredrick (2019) examined financial challenges in Nigerian firms but focused on capital structure rather than retained earnings, reinforcing the need for further research in the Kenyan context.

Additionally, studies on financial stability and long-term debt also present notable gaps. Haque et al. (2019) examined long-term debt but did not assess retained earnings' influence on financial stability in NSE-listed non-financial firms. Bui (2019) and Mselmi et al. (2020) studied long-term debt in Vietnam and France, respectively, highlighting a contextual gap. Islam et al. (2019) and Khoja et al. (2019) analyzed long-term debt but did not link it to financial stability, while Václav and David (2017) focused on financial distress rather than stability.

Furthermore, gaps exist regarding short-term debt and financial stability. Studies by Nguyen et al. (2020), Kaumbuthu (2018), Mwangi et al. (2014), and Makori & Jagongo (2013) overlooked short-term debt’s direct impact. Kholisoh & Dwiarti (2020) and Zulkarnain (2015) emphasized macroeconomic factors and financial distress, respectively, rather than financial stability. These gaps underscore the need for further research on retained earnings, long-term debt, and short-term debt in NSE-listed non-financial firms.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter covers the research design, sampling, and demographics. In addition, data collection procedures, data analysis and diagnostic test were discussed.

3.2 Research Design

A research design is a plan or framework that directs data collection, measurement, and analysis in order to address a specific study phenomenon. Therefore, the goal of the research design is to logically, systematically, and orderly arrange and consider the many components of research to address the research phenomenon (Mugenda & Mugenda, 2019). The study design clarifies the actions required to achieve the research objectives. Causal (explanatory) research design using a panel data approach was employed in fulfilling the purpose of the study. This design was suitable because it allows for an in-depth examination of the relationship between financial structure (retained earnings, long-term debts and short-term debt) and financial stability (liquidity ratios, solvency ratios, Z-score) over time.

3.3 Target Population

The target population is the set of people or things about which the researcher intends to generalize the findings. The common characteristic that the things or people usually have in common is what the researcher is interested in (Mugenda & Mugenda, 2019). It has also been proposed that the target population represents the study area of interest based on the dependent variable which is the key determinant in expiating the target population concentration. The target population for this study was all the 44 non-financial firms listed in the NSE based on financial stability consideration

as presented in appendix II. The reason as to why the study considered using non-financial firms listed in NSE over the financial firms was because non-financial firms do not directly engage in financial activities but evaluate on different concepts to ensure they have the finance with them while as financial firms ;listed in NSE basically deals with financial services and therefore they offer financial products thereby when we consider aspect of long term debts, short term debts they are usually the one whom offer loans to other institution/firms hence could not be best suited in this study.

3.4 Sample and Sampling Technique

The term sample is a portion or subset of the target population in which the researcher intends to make inclusions based on the study area. Thus, the sampling procedure has been defined as selecting a subset of the target population to identify and derive additional inferences about the target population based on the sample's features (Giedre & Sliogeriene, 2020). The sampling procedure aims to find a subset of the population with characteristics typical of the population's features. A sample is considered representative if its results are consistent with what would be found in the population (Nallaperumal, 2014).

This study used a census to collect data. Census considers the fact that every unit in the target population is inspected for analysis (Gathii et al., 2019). The census is usually used with the target population is small. It has been expressly recommended that when the target population is less than 100, census sampling technique best suites the study analysis. The census has been linked to several advantages, including enhanced validity of the data collected, reduced probability of sampling errors, and the capacity to investigate a subject in depth. The census approach was used in this study to include all 44 non-financial firms listed in the NSE.

3.5 Research Instrument

A research instrument is a tool that will be used to collect data from the study's intended audience in order to achieve its objectives. The choice of data-gathering instrument is also influenced by the type of data that needs to be collected. For this study, secondary data which is published on non-financial firms listed in the NSE based on financial structure was used to determine their financial stability. After the data was acquired from secondary sources of the publicly available financial reports for a period of five years from 2018-2022, it was entered into a data collection sheet.

3.6 Data Collection Procedures

The data collection procedures entail a detailed description of all the methods and processes to be utilized to collect data for analysis. The researcher therefore proceeded to collect the required data and summarize it in a data collection sheet.

3.7 Data Analysis and Presentation

After data collection, STATA 17 was used to carry out multiple linear regression, correlation analysis, and descriptive statistics. The regression coefficients statistical significance was evaluated using the t-statistic at the 5% significance level.

For this study, the regression model listed below will be employed:

$$FS_{it} = \beta_0 + \beta_1 RE_{it} + \beta_2 LTD_{it} + \beta_3 ST_{it} + \varepsilon_j$$

Where:

FS_{it} is Financial Stability for each firm i and year t;

RE is the Retained earnings

LTD is long term debt

STD is short term debt

3.8 Diagnostic Tests

These are based on the linear regression's normality and linearity assumptions.

3.8.1 Normality Test

A normality data distribution is required for multiple regression analysis. Thus, skewness, kurtosis, and normality statistics were used to evaluate this claim. Skewness, a measure of a value distribution's deviation from the mean symmetry was used to determine whether the data was average (Dudovskiy, 2019). In the case of a positive value, there are disproportionately many minimal values; in the case of a negative value, there are many large values. The distribution is symmetrical if the value is zero. When the kurtosis value is about 0, the data shape will be nearly normal. A negative number indicates a flatter-than-normal distribution, whereas a high kurtosis indicates a more peaked-than-normal distribution. The skewness and Kurtosis statistics of + / -1.96 suffice for statistical analysis. A low p-value in the present test indicated significant skewness, suggesting that the data was normally distributed (Brooks, 2008).

3.8.2 Multicollinearity

In statistics, multicollinearity refers to the situation where several independent variables in a regression model exhibit high correlation (Park, 2018). This can result in issues with the dependability and usability of the model. This investigation's multicollinearity test employed the use of Variance Inflation Factor (VIF). A high VIF value denotes a significant linear relationship between the predictors and the norm, and a VIF value greater than 10 denotes a significant multicollinearity event (Alin, 2010). Generally speaking, multicollinearity is considered acceptable when the VIF is less than 5. If multicollinearity emerges, a few steps were taken to prevent it (Senaviratna & Cooray, 2019). One possible solution is to exclude a significantly

correlated independent variable—or variables—from the study. Creating a single variable out of all the associated variables was another tactic. Finally, while maintaining most of the data, dimensionality reduction techniques like principal component analysis can also reduce the number of independent variables.

3.8.3 Autocorrelation

The connection between a variable's past and current values is called autocorrelation in statistics. This could lead to problems with the model's accuracy and interpretation (Uyanto, 2020). Autocorrelation transpires when data exhibit a discernible trend over time. In this instance, the statistics reveal specific patterns in the rate of change across various time intervals. Models exhibiting autocorrelation indicate that they are inadequately specified, implying the absence of essential variable(s) from the model. Autocorrelation does not affect the unbiasedness and linearity of the estimators. The sole recognized effect is that it violates the properties of Ordinary Least Squares (OLS), resulting in erroneous outcomes in hypothesis testing (Gujarati, 2004). The study employed the Breusch-Godfrey test to determine if the gathered data exhibits serial autocorrelation.

3.8.4 Heteroscedasticity

The regression model requires the variance of the error term to remain constant throughout time to maintain homoscedasticity. If this supposition is false, the data shows heteroscedastic behavior. Gujarati (2003) clarified that skewed standard errors may arise and result in inconclusive significance tests if Heteroscedasticity needs to be recognized and addressed before executing a regression model. The Breusch-Pagan test was employed to determine if heteroscedasticity was present. The variance of error terms in null hypothesis is considered constant. If Heteroscedasticity will be detected, the study will employ the Feasible Generalized Least Squares (FGLS) model to

adjust for it. Wooldridge (2002) asserts that the FGLS method performs better than the GLS technique. The GLS estimator is, therefore, neither practical nor feasible. Because of FGLS's superiority, estimators may be relied upon to be reliable and accurate, which qualifies them for significant tests.

3.8.5 Hausman Specification Test

According to Field (2008), panel data analysis can be divided into three essentially independent approaches: random effect models, which assume that there are unique, time constant attributes of individuals that are the result of random variation and do not correlate with individual regressors; fixed effects models, which assume that there are unique attributes of individuals that are not the result of random variation and that do not vary over time; and pooled panels, which assume that there are no unique attributes of individuals within the measurement set and no universal effects across time. This approach is more suitable for concluding the population than the research group. The Hausman test was used to choose between fixed and random effects.

CHAPTER FOUR

FINDINGS AND DISCUSSIONS

4.1 Introduction

This chapter makes an effort to use econometric statistical models to explain the findings and observations. For ease of interpretation, the study's results were displayed in tables after data analysis using STATA software. The right data must be collected to provide accurate results that are deemed sufficient for the objectives of this investigation. The results can be gathered at different times while staying consistent because the data collection process is constant. The findings were then compared to previous studies carried out by other researchers. The discussion also includes a comparison of the concepts used in this study.

4.2 Panel data analysis

The panel data analysis uses particular tests that must be adhered to in order to produce the output and evaluate the results. The test shows that the data meets the criterion test for panel data analysis, is largely balanced, covers the years 2018–2022, and was properly arranged. Every organization or corporation in this scenario has measurements with values across every period, according to the balanced panel data analysis.

4.3 Descriptive statistics

It explains the characteristics of the data used in the study. The study generated statistics regarding the research data variables' mean, standard deviation, minimum and maximum values, kurtosis, skewness, and number of observations. The analysis in Table 2 was based on 220 observations of 44 non-financial enterprises listed on the NSE and in continuous operation from 2018 to 2022. The mean for long-term debt was .529 with a standard deviation of .612, the mean for short-term debt

was .422 with a standard deviation of .507, and the mean for retained earnings which was considered as the most cost effective in terms of internal funding due to no repayment or interest was .523 with a standard deviation of .608. Furthermore, the financial stability mean was 0.23, and the standard deviation was 0.30. These findings were based on the impact of financial structure on the financial stability of non-financial firms listed on the NSE.

TABLE 2

Descriptive statistics

Variable	Obs	Mean	Std. Dev.	Min.	Max.
Retained earnings	220	.5234545	.6084811	.01	8.53
Long term debts	220	.5291818	.6124763	.01	8.48
Short term debts	220	.4221818	.5073791	.01	5.32
Financial stability	220	. 2293869	. 3031448	. 0051541	2.56

Source: Researcher (2025)

4.4 Diagnostic Test

To make sure the data is suitable for analysis, a diagnostic test is carried out. Diagnostic tests for normality, multicollinearity, autocorrelation, heteroscedasticity, the Hausman Test, and stationarity were all part of the research evaluation.

4.4.1 Multicollinearity test

The purpose of the test is to ascertain whether the independent variables have a high degree of correlation with one another. The study was evaluated by the researcher using the correlation matrix, and Table 3 displays the test results. The Variance Inflation Factor (VIF) was used in this study's multicollinearity test. Under normal circumstances, multicollinearity is indicated by a VIF

greater than 10. According to the findings in Table 3, the VIF of long-term debts was 1.20, that of retained profits was 1.19, and that of short-term debts was 1.04. The VIF overall was 1.14. demonstrating that multicollinearity is not present.

TABLE 3

Multicollinearity test

Variable	VIF	1/VIF
Retained earnings	1.20	0.832623
Long term debts	1.19	0.839481
Short term debts	1.04	0.964456
Mean VIF	1.14	

Source: Researcher (2025)

4.4.2 Normality Test

Kurtosis and skewness were the primary determinants for the Shapiro-Wilk test, which was employed in the study to evaluate the normalcy test. The findings were shown. Regression analysis was used in this work with the assumption that the residuals were normally distributed. To ensure the correctness and dependability of the data and to confirm the achievement of normality, a Shapiro-Wilk test was performed. According to Field (2023), if the normalcy of residuals is not achieved, the results may become inaccurate and unreliable depending on the phenomenon studied.

Thode (2022) went on to confirm that the Shapiro-Wilk Test has limited capacity to evaluate and identify values in normality testing, and as a result, researchers should be advised accordingly. Additionally, as the sample size in this study was larger than 200, a single Shapiro-

Wilk Test for normality was adequate because non-normality would not significantly affect parametric tests (Winter, 2013). According to Barton Peat (2022), a low number indicates that the sample population is not normally distributed, which means the null hypothesis—which assumes a normal population distribution—must be rejected. According to the study's results, the kurtosis and skewness values for the variables under investigation were both between +1.96 and -1.96, indicating that the data were regularly distributed.

TABLE 4

Normality Test

.sktest financial stability short term debts long term debts retained earnings

Skweness/Kurtosis tests for Normality

----------joint……..

Variable	***obs***	***Pr(Skewness)***	***Pr(Kurtosis)***	***Adj ch2(2)***	***Prob>chi2***
Financial S~y	220	0.0000	0.0000	.	0.0000
Shorttermd~s	220	0.0004	0.0100	16.11	0.0003
Longtermde~s	220	0.0124	0.0000	27.40	0.0003
Retained~s	220	0.0123	0.2213	7.29	0.0262

Source: Researcher (2025)

4.4.3 Autocorrelation

In statistics, autocorrelation illustrates the relationship between the variables under examination. The Breusch-Godfrey test was used in the study to look for autocorrelation. This is how Table 5 shows it. To determine whether the data deviates from the Ordinary Least Squares (OLS) assumptions, which could produce inaccurate results in hypothesis testing, an Autocorrelation Test

was conducted. To ascertain if the gathered data demonstrates serial autocorrelation, the study used the Breusch-Godfrey test for serial correlation.

With an F-test value of 93.528 and a P-value of 0.000, the Breusch-Godfrey test for autocorrelation appears to be statistically significant at the 5% level. It was concluded that the residuals are autocorrelated as a result of the null hypothesis regarding the presence of autocorrelation being upheld. The researcher employed the difference transformation method, which uses a distinct transformed variable, to address autocorrelation. In order to address the autocorrelation problem in the model, this necessitated using Cochrane-Orcutt AR (1) regression with iterated estimates using the prais command. This was shown in Table 4.5, where the autocorrelation significance level was set at 0.8333, which was higher than the significant threshold of 0.05 and so indicated the lack of autocorrelation.

TABLE 5

Autocorrelation

.estat bgodfrey, lag(5)

Breusch-Godfrey LM test for autocorrelation

Lags(p)	**Chi2**	**df**	**Prob>chi2**
5	93.528	5	0.0000

H0:no serial correlation

Source: Researcher (2025)

4.4.4 Heteroscedasticity

It is assumed that the variance or error term difference in regression models remains constant across observations. The random variable is referred to as heteroscedastic if this presumption is

broken. The analysis is incorrect if heteroscedasticity is the control model. With the assumption that the data was homoscedastic, this study employed the Breusch-Pagan test to determine whether heteroscedasticity existed in the data. Since the reported value for the chi2 (1) was 69.14 with a p-value of 0.000, which was less than the required 0.05, the analysis's results in Table 4.5 showed that the hypothesis was thus rejected at a critical p-value of 0.05. Therefore, there was statistically substantial heteroscedasticity in the data. To deal with data that doesn't show statistically significant heteroscedasticity, which means that the errors' variance is constant at all independent variable levels. The study thus takes into consideration the usage of the RAM effect model to exclude heteroscedasticity from the data in order to mitigate it. As a result, Table 6 showed that Prob>chi2 = 0.7364, indicating that there was no heteroscedasticity because the p-value was significant and greater than 0.05.

TABLE 6

Heteroscedasticity

Breusch-Pagan/ cook-Weisberg test for heteroskedasticity

H0: Constant Variance

Variables: fitted values of financial stability

Chi2(1) =	69.14
Prob>chi2=	0.0000

Source: Researcher (2025)

4.4.5 Hausman's specification Test

To evaluate the consistency of the estimator against a different, less effective estimator, the Hausman specification test was used. According to Green (2008), a Hausman specification test is necessary to determine whether to use fixed effects or random effects, with the random effects model being the null hypothesis. To determine which of the random and fixed effects models was the best estimating model, the Durbin-Wu-Hausman Test was applied to the data. The results are shown in Table 4.6, which supports the premise that random effects are preferable to fixed effects. At the five percent significance level, the Hausman test revealed a chi-square value of 0.10 with a p-value of 0.9916, indicating that the chi-square result is statistically insignificant. The fixed effect model was then used because the H0, and the researcher did not rule out the possibility that the random effects model is better than the fixed effects model. The p-value was higher than 0.05, but H_1 was less than 0.05; consequently, the fixed effect model was chosen because the alternative hypothesis produced a significant level.

TABLE 7

Hausman's specification Test

Test: Ho: difference in coefficients not systematic

Chi2(3) = (b-B)' [(v-b-v_b) ^ (-1)] (b-B)	
=	0.10
Prob>chi2 =	0.9916

4.5 Inferential statistic

4.5.1 Correlation analysis

To determine the rate at which the independent variables (retained earnings, short-term debt, and long-term debt) influenced the dependent variable (financial stability) of the non-financial firms

listed in the NSE, the researcher employed Pearson's Correlation Coefficient to establish the correlation among the study variables. The study's conclusions showed that short-term debt had no discernible impact on the non-financial companies listed on the NSE in terms of their financial viability. The fact that the p-value (0.5146) was higher than 0.05 took this into account. This suggested that the non-financial enterprises' financial stability dropped by 4.42% (r=-0.0442) for every unit increase in retained earnings.

There was a p-value that was greater than 0.05 which was reflected by the finding that the level of statistical significance of the study result on the influence of long-term debt on financial stability was found to be insignificant. This indicated that a one unit increase in long term debt led to 1.38. lower values in the financial stability (r=-0.0138). According to the methodology, the research had found the lack of significant correlation between financial stability and the retained earnings. This was because the p-value (0.5307) was greater than significance level of 0.05. It also established that 4.25 percent decrease in financial stability was due to unity increase in retained earnings (r=-0.0425).

TABLE 8

Correlation Analysis

.pwcorr financial stability short term debts long term debts retrained earnings, sig star (0.01)

	Financial S~y	*Shorttermd~s*	*Longtermde~s*	*Retained~s*
Financial S~y	1.0000			
Shorttermd~s	-0.0442	1.000		
	0.5146			
Longtermde~s	-0.0138	0.1717	1.0000	
	0.8390	1.9197		
Retained~s	-0.0425	0.1431	0.39478*	1.0000
	0.5307	0.0339	0.0000	

4.5.2 Feasible Generalized Least Squares Regression Model

To fit the model, the feasible generalized least squares regression model, which is based on contemporaneous correlation, was used. The study values for R-Squared from the model were 0.234, which showed that 23.4% of the financial stability of non-financial firms listed in the NSE was influenced by independent variables (retained earnings, long-term debts, and short-term debts), while the remaining 76.4% was influenced by factors outside the study variables during the 2018–2022 study period. This was because the panel data set posited autocorrelation and an aspect of heteroscedasticity in the analysis.

Additionally, the results showed that short-term indebtedness had a statistically significant negative impact on the financial stability of non-financial enterprises listed on the NSE (-0.246, p-value<0.0039). Furthermore, the analysis's results showed that long-term indebtedness had a favorable but negligible impact on the NSE-listed non-financial enterprises' financial stability (0.427, p-value>0.0623). Lastly, the study found that retained earnings had a statistically significant and favorable impact on the non-financial enterprises listed on the NSE in terms of their financial stability (0.6251, p-value>0.0435).

The model therefore becomes

$$FS_{it} = \beta_0 + \beta_1 RE_{it} + \beta_2 LTD_{it} + \beta_3 ST_{it} + \varepsilon_j \quad \text{.....(1)}$$

$$FS = 27.270 + 0 \cdot 625RE + 0 \cdot 427LT - 0 \cdot 246\ ST$$

TABLE 9

Regression Model

Cross-sectional time -series FGLS regression

Coefficients: generalized least squares

Panels: Homoscedastic

Correlation: no autocorrelation

Estimated covariance	= 1	Number of obs.	= 220
Estimated autocorrelations	= 0	Number of groups	= 44
Estimated Coefficients	= 4	Time periods	= 5
		Wald chi2 (3)	= 694.732
Log likelihood	= -004597.61	Prob >chi2	= 0.0000

Financial S~y	**Coef.**	**Std.err.**	**z**	**p>/z/**	**[95% conf. interval]**	
Longtermde~s	.4273210	.0977345	0.27	0.062	.0448165	.0216176
Shorttermd~s	-.2463771	.0089595	-0.52	0.039	-.0006841	.013464
Retained~s	.6251181	.330354	0.58	0.043	.0292808	.0046566
_cons	27.26943	.8684276	3.42	0.001	-12.52178	236542

4.6 Discussion of findings

4.6.1 Effect of retained earnings on the financial stability of listed non-financial firms at the Nairobi Securities Exchange.

Examining how retained earnings affect the financial soundness of non-financial firms listed on the NSE was the initial goal of the study. This was done to unequivocally confirm whether it was a substantial factor in bringing about financial stability in such a run-down economy that was little affected by the start of the coronavirus, which caused the economy to slumber. Given that the p-

value was less than 0.05 (5%) of the necessary significant threshold, the study concluded from the analysis that retained earnings had an impact on financial stability; hence, the significance level. Because of these results, the study was able to confirm that retained earnings were important and that there was a possible relationship between them and financial stability.

Retained earnings have been shown to have a lower likelihood of causing financial difficulties, according to Nketiah's (2020) findings, which were based on panel data collected between 2010 and 2019 and examined the investment decision-making process in US-listed gas and petroleum businesses in order to predict organizational financial hardship. Furthermore, it was consistent with the results of Darmawan and Supriyanto (2020), who examined the effects of the financial difficulties faced by mining companies in Indonesia. One of the study's conclusions was that a company's financial difficulties are alleviated by retained earnings in the asset ratio. As a result, the study's conception confirmed that there is a considerable association between retained earnings and the financial stability of non-financial enterprises; hence, the term "significant relationship."

4.6.2 Effect of long-term debts on the financial stability of non-financial firms listed at the Nairobi Securities Exchange

Evaluating the impact of long-term debt on the financial viability of non-financial companies listed on the NSE was the second study goal. The research indicated that long-term debt did not have any appreciable influence in the extent of financial stability of non-financial firms listed at the NSE. The research results revealed that the effect of long-term debt was statistically significant as it related to the stability of finances. Moreover, a great connection existed between the financial stability and long-term debt. The study findings did not agree with those of Islam et al. (2019) that involved considering the influence of dividend policy and the presence of long-term debt impact

on the bottom line and financial performance in the Dhaka stock exchange. They also found out that the indicators of success in finances were negatively correlated to increase in long-term debt.

In addition, it validated the findings of Bui (2019) who examined the correlation between dividend policy and financial success to assess the effect on financial performance in the Vietnamese setting caused by the long-term loans. Bui found out that the long-run debt enhanced the financial stability metrics although modestly. It was also in line with the findings of Haque et al. (2019), which aimed at gaining better insight into the link between the dividend policy and financial stability through focusing on the Dhaka stock exchange. They found out that long-term debts possessed a positive but non- significant effect on the financial stability measurements. It also backed the similarities identified by Vaclav and David (2017) desiring to establish a model that can be employed in financial analyses to signify events of financial hardship inside farming enterprises across Europe and found out that long-term debt had a significant correlation with financial woes.

4.6.3 Effect of short-term debt on financial stability s of listed non-financial firms at the Nairobi Securities Exchange

Examining the impact of short-term debt on the financial health of non-financial companies listed on the Nairobi Securities Exchange was the third objective. It was shown that short-term debts had little bearing on the financial soundness of non-financial companies listed on the NSE. The results of the study showed that there was no statistically significant relationship between short-term debt and financial stability. This implied that the p-value was higher than 0.05. Financial stability and short-term indebtedness do, however, have a slight but positive association. Nguyen et al. (2020), who examined the effect of Vietnam's dividend program on the nation's financial performance and the relationship between debt and economic outcomes, found that short-term debt has a somewhat

optimistic correlation with a few financial metrics. This finding, however, was at odds with their findings.

Furthermore, it went against the findings of Zulkarnain (2015), who in 2017 developed a model to forecast financial issues in business settings and used it to track the probable demise of financially troubled Malaysian companies. The results confirmed that employing Z's data analysis revealed an inverse relationship between financial trouble and the ratio of short-term commitments to assets, a measure of firm liquidity. Since the primary focus of the current study was the financial stability of non-financial firms listed on the NSE, the empirical review's conclusion confirmed that the current study's findings contradicted those of earlier studies, even though those studies were conducted in a diverse economy and therefore could not be applied to the current study.

CHAPTER FIVE

SUMMARY OF THE FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1Introduction

The findings, study limitations, conclusions, and recommendations are outlined in this chapter. It also discusses possible directions for future research by academics who wish to examine the impact of financial structure on the financial stability of non-financial firms listed on the NSE, which is the main focus of this study. The study would also be essential in helping the non-financial sector to efficiently plan and carry out strategies to encourage financial stability among non-financial firms that are listed on the NSE.

5.2 Summary of the Findings

The results and tests carried out using STATA software, which were free of mistakes and manipulations and accurately represented the circumstances of non-financial firms listed on the NSE, are included in the summary of the findings. Significant variation in the financial stability metrics across periods was revealed by the trend analysis. For instance, short-term debt was found to be unstable, fluctuating from year to year, and continuing this trend into succeeding years. The STATA regression analysis revealed a statistically insignificant lack of a linear relationship between the variables. The results were examined as described below.

5.2.1Effect of long-term debts on financial stability of non-financial firms listed in NSE.

The highest mean from the examined data suggests that long-term debts have a considerable impact on the financial health of non-financial firms listed on the NSE, according to the descriptive statistics. This means that non-financial firms have enough long-term debt to increase their holdings, which improves their financial stability. Furthermore, the results of the regression model

showed that long-term debts had a significant impact on financial stability because of the positive significance level. This was confirmed by the fact that long-term debts increased from early 2018 to 2020, before the start of COVID-19, but then sharply declined in the year that followed, and then increased again for two years, from 2021 to 2022. After 2020, long-term debt among non-financial companies listed on the NSE began to fall after reaching its peak.

This demonstrates a typical variance in the amounts of debt accumulated by non-financial companies listed on the NSE. These findings were consistent with those of Islam et al. (2019), who examined the impact of dividend policy and long-term debt on the bottom line and financial performance at the Dhaka stock exchange. They discovered a negative correlation between financial success indicators and an increase in long-term debt. Furthermore, it went against the results of Bui (2019), who investigated the relationship between dividend policy and financial success in order to determine how long-term loans impacted financial performance in the Vietnamese context. Bui discovered that long-term debt financial stability metrics, albeit slightly.

Haque et al. (2019) researched the Dhaka stock exchange setting to better understand the relationship between dividend policy and financial stability. They discovered that long-term debt has a positive and statistically insignificant effect on financial stability metrics, which contradicted the findings of their study. Additionally, the study disagreed with the findings of Václav and David (2017), who developed a model that could be used to predict financial difficulties in farming enterprises throughout Europe and discovered a high correlation between long-term debt and financial troubles.

5.2.2 Effect of short-term debts on financial stability of non-financial firms listed in NSE

A normal fluctuation between short-term debts and the degree of financial stability during the study period was found by analyzing descriptive data about the impact of short-term loans on financial stability. Short-term debt for non-financial firms steadily declined in the first year, but the COVID-19 pandemic caused a sharp decline in the second year. Furthermore, among all non-financial firms listed on the NSE, short-term loans steadily increased throughout 2018, leveled in 2019, peaked at the beginning of 2020, then declined as a result of the global economy coming to a standstill before declining later in 2022. The findings of the diagnostic test show that, among non-financial companies listed on the NSE, short-term debts show a typical pattern in terms of financial stability. This implies that the level of financial stability of non-financial firms is not sufficient influenced by their NSE value that is based on short-term indebtedness.

These findings were opposite to those of Nguyen et al. (2020) who consider the impact of the dividend program imposed in Vietnam on the financial performance of the country and the correlation between debt and financial performance. They discovered that short term debt had a relatively positive correlation with some financial measures. Moreover, it contradicted the work done by Zulkarnain (2015) who, in 2017, established a model to predict financial problems in business environments and applied it in predicting the likely collapse of the Malaysian companies facing the problem of finance. The findings revealed that with the data of Z, the ratio between the short-term commitments to assets as a gauge of firm liquidity displayed an inverse relationship with financial trouble.5.2.3Effect of retained earnings on financial stability of non-financial firms in the NSE

According to descriptive statistics, retained profits have fluctuated, which indicates that they are not constant. The results of the regression model showed that retained earnings had a positive and

significant level influence on financial stability, indicating a high goodness of fit (R-squared) for retained earnings. This suggests that the trajectory of retained earnings has been erratic. The results showed that the financial stability of non-financial companies listed on the Kenyan Stock Exchange (NSE) steadily increased. This, in turn, had a notable beneficial impact on the level of financial stability in the first year, although the two years prior saw a normal fluctuation. This suggests that between 2020 and 2021, non-financial companies listed on the NSE could increase the financial stability of their investments. However, in 2022, non-financial firms saw a minor improvement in management's grasp of the financial concept, which led to an improvement in financial stability.

According to the data, retained earnings for non-financial companies listed on the NSE vary normally. This suggests that there is a substantial impact on the financial soundness of non-financial companies listed on the Kenyan Stock Exchange. The results of this study were in line with those of Nketiah (2020), who determined that retained earnings have a lower propensity to cause financial difficulties. Nketiah used panel data collected between 2010 and 2019 to study the investment decision-making process in US-listed gas and petroleum businesses in order to predict organizational financial hardship. It also deviated from the conclusions of Darmawan and Supriyanto (2020), who examined the effects of the financial difficulties faced by Indonesian mining companies. One of the study's conclusions was that a company's financial difficulties are alleviated by retained earnings in the asset ratio.

5.3 Conclusions

Given the aforementioned data, it can be said that long-term debt and retained earnings significantly affected the financial stability of non-financial companies listed on the Kenyan Stock Exchange (NSE), whereas short-term debts had no discernible impact on the financial stability of

those companies. The commencement of COVID-19, which brought the world economy to a halt and caused variance, was a contributing factor to the dramatic drop in the level of financial stability among non-financial enterprises listed on the NSE in 2020 and 2021. The findings indicate that financial stability position of non-financial enterprises contemplated in the NSE is not sustainable.

The level of incapacity of sustainability severely affects the variation in the values of long-term debts and retained earnings in non-financial firms of the NSE listed among them. This has led to financial stability as many firms have performed less and solicit more long-term loans in order to balance off the retained earnings in order to offset short term debts. Significant short-term fluctuation is associated with the low level of investment and the low operational efficiency of non-financial enterprises listed in the NSE. In summary, aspects like long-term debts, short-term debts, and retained earnings form part of the components that determine the degree of financial stability in non-financial enterprises listed in the Kenyan Stock Exchange.

5.4 Recommendations

There should be a clear outline to enhance financial structural indicators effectiveness and implementation of longer-term debts, short-term loans, and retained earnings of the non-financial firms listed on the Kenyan stock market (NSE) in acquiring an elevated level of financial stability. Reduction in cost is not a sustainable success strategy that a non-financial company listed in NSE should only take into consideration. To improve their level of financial stability, a fair plan can allow the listed firms that are not finances on the NSE to enhance their efficiency in operations and to enhance their capacity to satisfy the market and make investments to face the future. Policy makers are advised to enhance the regulatory environment to get high degree of requirements in retained earnings that is able to endure political and economic shocks.

Regulations need to be altered so as to make sure that non-financial companies under the NSE are sufficient in terms of capital buffers and risk management systems. Next, the promotion of financial stability and the establishment of an environment that stimulates the long-term economic growth and stability of non-financial firms listed at the NSE, should be considered as the necessities. A stable business and working environment can counter the negative impact of political unrest on the economy and other firms that are not listed on financial markets but listed on the NSE. The non-financial companies listed on NSE are in correspondence with the risk appetite of the institution. Special attention should be paid to retained earnings since such companies pay special attention to the quality of the assets included in their portfolios.

Through effective operational review mechanisms, a healthy loan portfolio is able to be maintained at any level. Also, sustaining the financial stability of such companies during economic turndown necessitates that appropriate management practices are employed. In an effort to ensure unexpected economic challenges do not arise, it is important to monitor and change the amount of retained profits in line with the fluctuation of risk-weighted assets. Further studies ought to be conducted to investigate the different factors that make the non-financial businesses listed at NSE become financially stable. This may necessitate a close look on the impact of political unrest on the financial stability. Much information would be derived via longitudinal studies that would examine how aspects of financial stability develops and its implications over time. Scholars can also compare between countries to draw more comprehensive findings as far as financial structures in Kenya and the world at large are concerned in enhancing financial stability to advance further the global debate on financial structures in terms of financial stability.

Most elements of financial structures like long-term debt, short-term debt, liquidity and retained earnings are the aspects on which finance and economics students should be keen to

develop great understanding of the fundamentals. The components should be part of the curriculum as they are required in smooth running of the non-financial businesses. By offering case studies on the institutions which have effectively used these components, the students can attain pragmatic training on the effective financial frameworks within non-financial businesses that have been listed in the NSE processes. It would also help them to gain the skills necessary to solve industry issues and become future employees of this sector of non-financial businesses.

By encouraging research to augment industry knowledge, facilitating informed decision-making, and providing students with the necessary skills and insights to contribute effectively to listed non-financial firms and advance the finance domain, these recommendations aim to cultivate a stable and sustainable level of financial stability in Kenya.

5.5 Limitations of the Study

The study's conclusions shouldn't be applied to every area of the Kenyan economy. Only secondary data from 44 listed non-financial companies in Kenya's NSE, as reported by the Capital Market Authority as of December 31, 2022, is used in the survey. As a result, the research findings are not generally applicable because they only apply to the non-financial companies that are listed on the NSE and do not apply to other important financial sectors. Furthermore, the potential advantages of including primary data may have been underestimated because the majority of the data used in this study came from secondary sources. Lastly, it is important to note that this study only looked at how the three financial structure indicators—short-term, long-term, and retained earnings—affect the level of financial stability in non-financial firms that are listed on the NSE.

5.6 Suggestions for Further Studies

To determine whether the influence of financial structure indicators on the degree of financial stability may be comparable across other sectors, future research in this area must cover a wide

range of industries. Only the three financial structure metrics short-term, long-term, and retained earnings were looked at in this study. Future investigations might look into other topics not included in this study. Due to the lack of source data that would have provided a more thorough topic analysis, this study mostly uses secondary data. Therefore, in order to supplement secondary data and provide a more comprehensive view of the current study, primary data must be included in the future.

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APPENDICES

Appendix I: Non-financial firms listed in the NSE

Category	Firms
Agriculture	1. Sasini Ltd 2. Williamson Tea Kenya Ltd 3. Rea Vipingo Plantations Ltd 4. Limuru Tea Co. Ltd 5. Kakuzi 6. Kapchorua Tea Co. Ltd 7. Eaagads Ltd td Ord
Automobiles and accessories	1. Car and General (K) Ltd
Commercial and services	1. Express Ltd 2. Sameer Africa PLC 3. Kenya Airways Ltd 4. Nation Media Group 5. Standard Group Ltd 6. TPS Eastern Africa Limited 7. WPP Scanford Group 8. Uchumi supermarket limited 9. Longhorn Publishers Ltd 10. Deacons (East Africa) Plc **11.** Nairobi Business Ventures **Ltd**
Construction and Allied	1. Athi River Mining 2. Bamburi Cement PLC 3. Crown Paints Kenya PLC

	4. E.A.Cables PLC **5.** E.A.Portland Cement **Ltd**
Energy & Petroleum	1. Kengen Co. Plc 2. Kenya Power & Lighting Co. Ltd 3. Total Kenya Ltd **4.** Umeme Ltd
Insurance	1. Britam Holding Plc 2. CIC Insurance Group Ltd 3. Jubilee Holdings Ltd 4. Kenya Re Insurance Corporation Ltd 5. Liberty Kenya Holding Ltd **6.** Sanlam Kenya Plc
Telecommunication and technology	1. Safaricom PLC
Manufacturing & Allied	1. B.O.C Kenya Plc 2. British American Tobacco Kenya Plc 3. Carbacid Investment Ltd 4. East African Breweries Ltd 5. Frame Tree Group Holdings Ltd 6. Kenya Orchards Ltd 7. Mumias Sugar Co. Ltd **8.** Unga Group Ltd
Real estate investment trust	1. Stanlib Fahari I-Reit

Appendix II: Summary of literature ad Research Gaps

Variable/Source	Objective	Methodology	Findings	Gaps Established	How to Address Gaps
Retained earnings					
Neelanjana and Hassan's (2019)	Effect of dividend policies on the financial performance of Malaysian manufacturing enterprises	Multiple-panel regression model	there was a strong correlation between the volatility of the systemic risks that shareholders experienced and their financial stability	Methodological gap: Lack of clarity in methodology.	Provide a clear description of the research methodology, sample size, and data sources to enhance comparability.
Naz and Siddiqui's (2020)	To analyze how different financial performance metrics were affected by	Multiple-panel regression model	dividend payments significantly impacted a variety of stock price	Methodological gap. Lack of which methodology was applied	The current study will seek to expiate the design to be used to gather the data

	dividend policy		volatility measures.		
Nketiah (2020)	To investigate the investment decision-making process in US-listed gas and petroleum businesses to predict organizational financial hardship	Altman model	Retained earnings have been demonstrated to have a lower likelihood of causing financial difficulties.	Methodological gap: Lack of clarity in methodology.	Expatiate the kind of data to be collected based on the area of jurisdiction.
Fredrick (2019)	To examine the effect of financial structure on the financial	Multiple-panel regression model	The PCSE has demonstrated a relationship between capital	Conceptual gap: Lack of clarity in the relationship between financial	Comprehensively investigate how financial structure exposes financial

	challenges of listed firms in Nigeria		structure and the tangibility of listed companies' assets, profitability, and financial difficulties.	structure and financial challenges.	challenges to entities.
Long-term debts					
Haque et al. (2019)	To analyze the relationship between dividend policy and financial stability	Panel data	long-term debt has a positive and statistically insignificant effect on financial stability metrics	Conceptual gap: lack of adequate conceptualizatio n of the study variables	Effectively analyse how long-term debt affects financial study through a critical literature review
Islam et al. (2019)	To examine the effect of long-term debt on the	cross-sectional research design.	An increase in debt was found to be negatively	Conceptual gap. Lack of clear explanation on how long-term	Comprehensively conduct a literature review on how long-term debts

	bottom line in addition to the effect of dividend policy on financial performance at the Dhaka stock exchange		correlated with financial success indicators	debts affect financial performance	affect financial stability
Mselmi et al. (2020)	investigated the association between corporate size, solvency ratio, profitability, and financial hardship in France's SMEs	Logit, Vector Support, and Hybrid Models	Liquidity, profitability, and solvency ratios (high long-term loans) have all decreased.	Conceptual gap: There is a limited explanation of how long-term loans have decreased	Offer clarity on why long-term loans may decrease or increase.

Khoja, Chipulu, and Jayasekera (2019)	To examine the effect of financial structure on financial challenges in multiple countries	Detailed macro-economic factors	long-term debt and operating revenue per air kilometer are two significant elements in this industry that could lead to difficulties	Conceptual gap: lack of clarity on how macroeconomic factors induce financial challenges	To incorporate macroeconomic factors such as interest rates to establish how long-term debts may induce financial stability.
Short-term debts					
Nguyen et al. (2020)	To determine the impact of Vietnam's dividend program on the country's financial performance as well as the connection between debt	Panel regression model	study found a correlation between short-term debt and financial outcomes	Theoretical gap: There is no explanation of the theories that were applied in the study	Comprehensively include theories to explain the relationship between short-term debts and financial stability.

	and financial outcomes				
Makori and Jagongo (2013)	To examine the relationship between working capital management and profitability of NSE-listed manufacturing and construction companies	Panel data regression model	there was a negative correlation between profitability and the cash conversion cycle but a positive correlation between profitability and the number of days receivable and the number of days of inventory	Conceptual gap: Limited explanation of how capital structure induces profitability	Analyse financial structure to enhance financial stability, which is measured through components of profitability

Appendix III: Data Collection Sheet

Year	Retained earnings	Long term debts	Short term debts	Financial Stability
2018				
2019				
2020				
2021				
2022				