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## *Identifying the Gap between Voluntary Disclosures by Companies Listed in India and Stakeholders' Expectations*

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**Abstract:** *This study focuses on analyzing information gap between the expectation of various user groups and the actual level of voluntary disclosures in the annual reports of companies listed in India. Very often, there seems to be a gap between the expectations of the various user groups and the information provided voluntarily by the policymakers of the company in the Annual Reports. This study adopts a self-constructed voluntary disclosure index to measure the level of voluntary disclosures of the selected Nifty-200 companies. Various user groups rated the importance of these voluntary disclosures through questionnaire survey. The study reveals that there exists an information gap between the expectations of various user groups and the actual level of voluntary disclosures in the annual report. Specifically disclosures related to future performance of the company and projections about its earnings had major information gap. Overall it was observed that the primary purpose of Annual reports of providing valuable information regarding the financial position and performance of the business as well as its future prospects to help users in decision-making is only partially fulfilled in case of companies listed in India.*

**Keywords:** *Information Gap, Voluntary Disclosures, Role of Annual reports, Stakeholders' expectations.*

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### I. INTRODUCTION

Ho and Wong (2003) stated that, how information is shared among the participants deeply affects the functioning of capital markets. Investors and other stakeholders need accurate, timely and reliable information about the company to make effective investment decisions. Information about a company is available through various sources; however one of the most important sources of corporate information is annual report. The primary role of an annual report is to provide credible, useful and timely financial as well as non-financial information to investors, shareholders and other interested people about the performance of the business as well as its future prospects to help users in decision-making. The information provided in the annual reports can be classified into two categories: Mandatory disclosures and Voluntary disclosures.

Mandatory disclosures are those required by regulators such as SEBI, Companies Act 2013 and the accounting standards. The extent to which companies comply with legal and other regulatory requirements depends on the strictness of enforcement by these bodies. Voluntary disclosure is the disclosure of information in excess of the mandatory requirements. Companies disclose voluntarily when they perceive the benefits of disclosure outweighing the costs (Gray & Roberts, 1989 quoted in Marston & Shrivs, 1991). However, review of literature suggests that there is an information gap between what is disclosed voluntarily by the policymakers and what is expected by the various user groups of an annual report. The current research attempts to analyze this information gap in the annual reports of companies listed in India.

## II. LITERATURE REVIEW

Singhvi and Desai (1971) stated that the quality of corporate disclosure in annual report considerably influences the extent and quality of investment decisions made by investors. Annual reports are commonly regarded as an important means of acquitting accountability in the corporate and government sectors and often are one of the means by which sectors can improve stakeholders' perceptions of their accountability. Flack and Douglas (2007) reported that annual reports were known as the annual reporting behaviors of a corporation and it has ability to improve the perceptions of accountability among stakeholders and the wider community. In addition, information disclosure in annual reports is a strategic tool, which can enhance the company's ability in raising capital at the lowest possible cost (Lev, 1992; Healy and Palepu, 2001). Annual reports are used as a medium for communicating both quantitative and qualitative corporate information to shareholders, investors and other users (Al-Shammari, 2008).

On the other hand, Baker and Haslem (1973), Chang et al. (1983), Wallace (1988), and Yuen et al. (2009) have shown that, the annual reports have provided inadequate information to the users. They concluded that the available information on the performance of companies' annual reports is poor and the financial information required by different types of users is different. Buzby (1974) also argued that many items were inadequately disclosed and there has been a gap between the users' needs of information and the actual information supplied by companies' annual reports.

Haw et al. (2000) and Hooks et al. (2002) found that in actuality many annual reports introduce limited amount of information. A lot of voluntary items, which stakeholders believe to be important or even essential, are not being disclosed in the actual annual reports. Therefore, the agreement between the importance of relative items ranked by stakeholders and the actual disclosure level was small and there is an opportunity for expanding the extent and improving the quality of voluntary disclosure information in annual reports of listed companies. The extant literature focuses on the developed nations. The regulatory norms and stringency in conformity to laws differ from these developed nations as compared to India. Hence the current study focuses on analyzing the information gap for user groups in India.

## III. OBJECTIVES

- To identify the level of importance attached by various user groups to voluntary disclosures.
- To measure the actual level of voluntary disclosures by selected Nifty-200 companies.
- To identify the information gap between the expectations of various user groups and the actual level of voluntary disclosure.

## IV. DATA AND METHODOLOGY

The study is divided into three sections. The first section deals with identifying the importance attached by various user groups to the selected voluntary disclosures. The second section focuses on identifying the actual level of voluntary disclosures by companies listed in India. The last section identifies the information gap between the expectations of various groups and the actual level of voluntary disclosures by companies.

### A. *Identifying the importance attached by various user groups to selected voluntary disclosures*

The first part of the study focuses on identifying the importance attached by various user groups to voluntary disclosures. For this purpose, self-constructed voluntary disclosure index was prepared comprising of 25 voluntary disclosures. The disclosures are divided into 3 broad categories as General & Strategic information, Financial information and Futuristic information.

Sample size of 200 respondents, comprising of four user groups i.e. individual investors, financial analysts, stock brokers and fund managers were asked to rate the voluntary disclosures in terms of their importance on a Likert scale of 5 ranging from

Highly Important to Not Important through a structured questionnaire survey. Purposeful convenience sampling method is used to identify and select individuals or groups of individuals that are especially knowledgeable about or experienced with a phenomenon of interest.

### B. Identifying the actual level of voluntary disclosures

The second part of the research focuses on determining the actual level of voluntary disclosures by the selected Nifty-200 companies. Nifty-200 has been selected as a sample as it represents about 86% of the free float market capitalization of the stocks listed on NSE as on March 31, 2018. Of the total 200 companies, 39 banking and financial services companies were excluded of the purview of this study. Hence a total of 161 companies were analyzed through document analysis. These companies were rated on the self-constructed voluntary disclosure index on a dichotomous scale, allocating 1 if the disclosure is made and 0 if the disclosure is not present in the annual report attaining a maximum possible score of 25.

### C. Identifying Information Gap

The last section deals with identifying the information gap between the expectations of various user groups with respect to voluntary disclosures and the actual level of voluntary disclosures in the annual report.

## V. RESULT AND ANALYSIS

Respondents of various user groups were asked to rate the selected voluntary disclosures in terms of their importance on a scale of 1 to 5. Table I showcases the mean values of the ratings given by various user groups to the list of 25 voluntary disclosures divided into 3 broad categories of 'General & Strategic Information', 'Financial Information' and 'Futuristic Information'.

TABLE I: Mean Values for 'Importance of voluntary disclosures' by Various User Groups

Self-Constructed Voluntary Disclosure Index		Individual Investors	Mutual Fund Manager	Financial Analyst	Stock market broker	Overall Mean Value
<b>A. General &amp; Strategic Company Information</b>						
1	General Information about the economy	3.16	3.19	3.21	3.03	3.15
2	Brief History of the company	3.21	2.73	2.85	2.42	2.90
3	Description of major products/services	3.38	2.22	2.59	2.61	2.87
4	Analysis of Company's market share	4.15	3.76	4.08	4.13	4.06
5	Current business strategy	3.73	3.46	3.67	3.63	3.65
6	Methods of Quality Control	2.80	2.57	2.59	2.32	2.63
7	Significant Issues during the Year	4.37	4.43	4.54	4.63	4.47
8	Information on last year's performance	4.06	4.19	4.13	4.34	4.15
9	Chairman/MD's/ CEO's Letter to shareholders	4.12	4.05	4.28	4.05	4.13
10	General statement on Industrial Relation	2.73	3.27	2.95	2.50	2.83
11	Description of Human Resource Development	3.19	3.76	3.28	3.13	3.30
<b>B. Financial Information</b>						
12	Historical Summary of financial data of last 5 years or more	3.55	3.11	3.79	4.03	3.61
13	Review of current financial results	4.30	3.92	4.38	4.42	4.27
14	Value added statement	4.03	3.73	3.74	3.92	3.90
15	Share price information	3.62	3.62	3.51	3.58	3.59
16	Return on Assets	3.74	3.59	3.92	3.74	3.75
17	Return on Shareholders' funds	4.34	3.51	3.64	4.29	4.04
18	Liquidity Ratios	4.00	3.73	4.54	3.97	4.05
19	Leverage Ratios	3.97	4.16	4.31	3.84	4.05
<b>C. Futuristic Information</b>						
20	Factors that may affect future performance	4.12	4.27	4.46	4.45	4.28
21	New products/service development	4.26	3.86	4.10	3.97	4.10
22	Marketing Plan, distribution system, expansion plan	3.91	4.16	4.18	3.97	4.02
23	Cash Flow projections	4.27	4.41	4.33	4.34	4.32
24	Earnings Forecast	4.47	4.41	4.54	4.24	4.43
25	Planned Capital Expenditure	4.36	4.49	4.41	4.03	4.33

It can be observed from the table that voluntary disclosures like 'Significant Issues during the Year', 'Earnings Forecast', 'Cash Flow projections', 'Factors that may affect future performance' and 'Planned Capital Expenditure' were rated as

important by user groups across categories. It can be observed that they place a high importance on information related to the future plans of the company.

Categorically, Individual investors allot the highest importance to 'Earnings forecast' followed by 'Planned Capital expenditure', 'Significant Issues during the Year' and 'Return to shareholders' funds. This signals that Individual investors are more inclined towards knowing the earning potential of the company and the returns generated. Similarly, mutual fund managers rate disclosures like 'Planned Capital Expenditure', 'Significant Issues during the Year', 'Cash-flow projections' and 'Earnings forecast' as highly important. This signifies that they are more concerned with the current issues as well as the future growth plans of the company. Financial analysts allot equal importance to 'Significant issues during the year', 'Liquidity ratios' and 'Earnings forecast' followed by 'Factors that may affect the future'. This signals that financial analysts are concerned with the current issues, liquidity and sustainability of the company. Lastly, stock market brokers rate 'Significant issues during the year', 'Factors that may affect future performance' and 'Review of current financial results' as highly important. This proves the fact that they are concerned with the current financial performance of the company as well as the factors that may affect their future performance.

The analysis points out the fact that various user groups have diverse intentions and thus expect different voluntary disclosure from the companies to fulfill their objective of information.

The consequent study focuses on identifying the actual level of voluntary disclosures by the selected 161 companies. Table II discusses the voluntary disclosure categorical score attained by these companies.

Table II: Voluntary Disclosure Score of the selected 161 Companies

Category of Information	No. of companies	% of companies	Voluntary Disclosure Score
General & Strategic information (Maximum possible score: 11)	121	0.75	11
	31	0.19	10
	9	0.06	9
	<b>Total companies: 161</b>		<b>Weighted Average score: 11.01</b>
Financial information (Maximum possible score: 8)	86	0.53	8
	68	0.42	7
	7	0.04	6
	<b>Total companies: 161</b>		<b>Weighted Average score: 7.49</b>
Futuristic information (Maximum possible score: 6)	1	0.01	6
	2	0.01	5
	4	0.02	4
	32	0.20	3
	122	0.76	2
	<b>Total companies: 161</b>		<b>Weighted Average score: 2.31</b>

Table II shows that with respect to the maximum possible score in each category, 121 companies (75%) disclose 100% in the general and strategic information category, 86 companies (53%) disclose 100% in the financial information category and only 1 out of 161 companies disclose 100% in the futuristic information category. These statistics show the level of voluntary disclosures in the futuristic information category is extremely low of the companies listed in India.

Table III compares the 'ranks allotted as per the mean value of importance for each voluntary disclosure' with the 'actual level of disclosure' in the annual report. It signifies the information gap between the expectation level and the actual level of voluntary disclosures in the annual report by selected companies.

Table III: Comparison of Ranks as per the Importance with the Actual Level of Voluntary Disclosure

List of Voluntary Disclosures (As per self-constructed disclosure index)	Ranks as per Mean value of importance	No. of companies disclosing
Significant Issues during the Year	1	161
Earnings Forecast	2	2
Cash Flow projections	3	2
Factors that may affect future performance	4	1
Planned Capital Expenditure	5	2
Review of current financial results	6	161
Leverage Ratios	7	159
Information on last year's performance	8	161
Chairman/MD's Letter or CEO's Letter to shareholders	9	39

Liquidity Ratios	10	43
Marketing Plan, distribution system, expansion plan	11	58
Analysis of Company's market share	12	34
New products/service development	13	64
Major Industry Trends	14	21
Return on Equity /Return on Shareholders' funds	15	11
Value added statement (Statement of wealth created)	16	61
Return on Assets	17	37
Historical Summary of financial data of last 5 years or more	18	112
Company's current business strategy	19	94
Share price information	20	28
Awards/Achievements	21	161
Description of Human Resource Development	22	158
General Information about the economy	23	160
Information of member companies	24	161
Measures to control environment pollution	25	59
General statement on Industrial Relation	26	161
Brief History of the company	27	2
Description of major goods/products/services	28	2
Productivity	29	1
Methods of Quality Control	30	2

It is evident from the table that voluntary disclosures like 'Earnings Forecast', 'Cash Flow projections', 'Planned Capital Expenditure' which are ranked as highly important by user groups across categories have a very poor actual disclosure level. There are very few companies who disclose these Futuristic information' information voluntarily in their annual reports. Futuristic information helps external users investigate the forecasted financial and operational data, and thus assists them in decision-making. However, making commitments about future performance of the company is not only painstaking and difficult but also precarious if not achieved.

It can also be observed that information like 'General information about the economy, General statement on Industrial relations, 'Brief history of the company' and 'Significant Issues during the Year' provides information overviews of historical data and background of the company. This information is available elsewhere and not of great value in competition, thus competitors do not value this information much. This could be the reason why corporations disclosed these items in a high amount. This trend was also reported in Barako (2007) in Kenya, Al-Shammari (2008) in Kuwait and Hossain and Helmi (2009) in Qatar.

Similarly, information on 'General statement on Industrial Relation', 'Brief History of the company and 'Description of major goods/products/services' which are ranked as least important by the various user groups is disclosed by all the companies in their Annual report. This shows that a gap exists between the expectations of various user groups and the information provided by the companies.

#### A. Analysis of Information Gap

The information gap is considered between the actual level of voluntary disclosures by companies and the voluntary disclosures rated as 'Highly important' or 'Important' by the various user groups. Figure 1-1 shows the information gap analysis between the expectation of user groups and the actual level of disclosure.

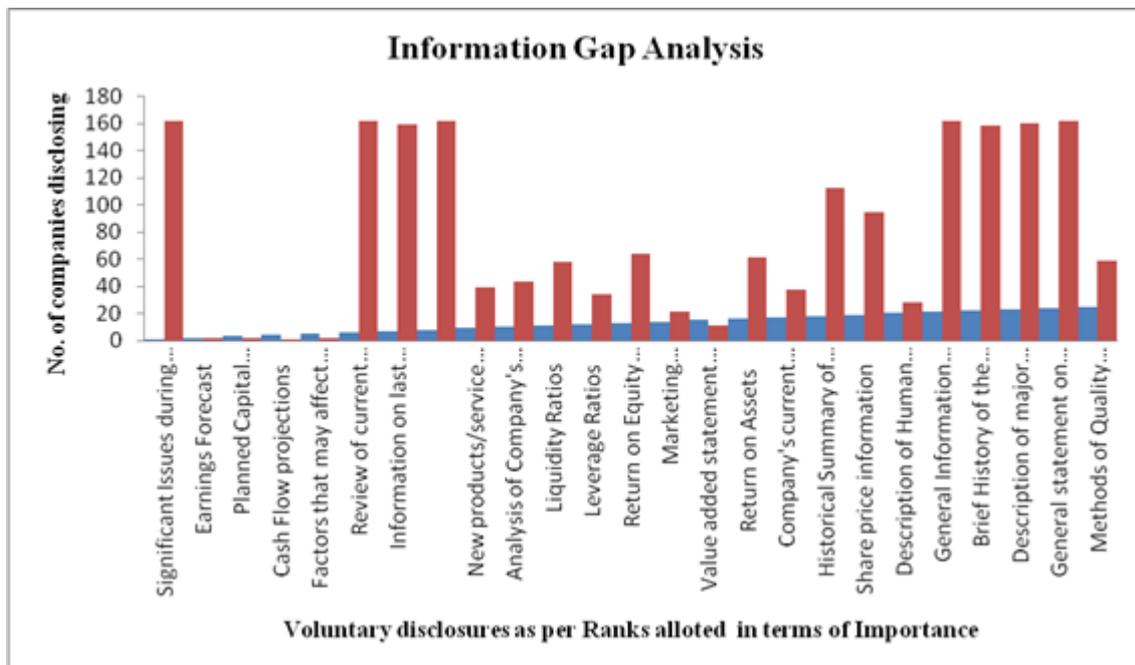


Figure 1-1 Information Gap Analysis

### B. Correlation Analysis

To further quantify this information gap, correlation analysis is conducted between the actual level of voluntary disclosures and the rating of voluntary disclosures rated by various user groups.

Table IV: Descriptive Statistics

	Mean	Std. Deviation	N
Ranks as per Importance	13.00	7.360	25
No. of companies disclosing	78.00	63.458	25

Table V: Correlations

		Ranks as per Importance	Voluntary Disclosure Level
Ranks as per Importance	Pearson Correlation	1	.282
	Sig. (2-tailed)		.172
	N	25	25
No. of companies disclosing	Pearson Correlation	.282	1
	Sig. (2-tailed)	.172	
	N	30	30

Correlation results show that there is low positive correlation of 0.282 between the ranks allotted as per the mean value of importance of voluntary disclosures and the actual no. of companies disclosing those voluntary disclosures. The low correlation suggests that there is a considerable gap of information between the expectations of various user groups and the information provided by the companies.

## VI. CONCLUSION

Results of the study suggest that there exists an information gap between what the user groups consider important and what the policymakers voluntarily disclose in the annual report. The lag may be due to more rapidly changing needs of users for data and the slower evolution of company disclosure practice. The reason for this gap also seemed to be the reluctance of management to disclose data that they consider sensitive as it could reveal companies' business secrets to competitors.

Darrough and Stoughton (1990) and Clinch and Verrecchia (1997) argued that divulging of sensitive information of companies to the public decreases their competitive ability since companies' competitors can collect more information on their inner workings. In addition, the high cost of releasing information to public is also one of the reasons that companies are

reluctant to disclose the information. The two types of disclosing costs are: the preparation cost of the financial statements borne by the company; and the analysis cost of the financial statements borne by the users of the information. From the economic perspective, managers only disclose information if the benefit exceeds the cost of disclosure (Maingot and Zeghal, 2008).

However, the increasing information gap results in decline in investors' confidence in the company and can thus increase the cost of capital and impact the market liquidity negatively. Thus, companies listed in India should focus on reducing the information asymmetry and keep the various stakeholders well-informed in order to attract both domestic as well as foreign investors.

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