The Determinants of Forward-Looking Information Disclosure

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Abstract

The main objective of this paper is to empirically establish the level of forward-looking information disclosure in companies listed on the Jordanian stock exchange and further to establish the determinants of forward-looking information disclosure. This information will assist company shareholders to make informed decision about the company's future performance. The level of will be determined by extracting financial and other information using company annual reports. Disclosure index methodology was adopted, that is awarding one for a disclosed item and zero if undisclosed. Five variables are employed to establish the level forward-looking information disclosure; these are sector type (manufacturing and services), company size, leverage, profitability, and auditor type (with or without international affiliation).

Keywords: Forward-looking Information, Disclosure, Company Characteristic, Jordanian Listed Companies;

1. Introduction

Forward looking information refers to business predictions about the future of the business state of affairs that eventually provide shareholders with useful information about the company's future prospects; this can be found in the company chairman's report. Company shareholders frequently question the management about the future prediction of the company in the sense that what is going to happen to the company in the future. It is obvious that the management can not predict or gives a certain answer to what is going to happen to the company in the future; but they are in a good position to observe most recent market trends and then present the shareholders with explanations about what the company is proposing or intending to do.

In spite of the implied comprehension that particular statements of the company's annual statement are considered speculative. Listed companies are obligated by the Securities exchange commission to comprise a disclaimer proviso on all management debates, disputes and discussions with shareholders with the intention to stress this point. Generally speaking, if and when a disclaimer proviso is stressed correctly, the shareholders may well not undertake legal action against the company's management for providing imprecise forward looking information (Healy and
Palepu, 2001; Kent and Ung, 2003). For example, the Private Securities Litigation Reform (PSLR) Act of 1995 in the United States offers specific security conditions against fraudulent allegation in dealing with forward looking information. Forward looking information disclosure includes information about financial forecasts of the company, such as revenues prediction, cash flows, and sales volume; it further includes information about non financial forecasts such as factors that may affect the company's future performance for instance risk, future business ambiguity, analysis and evaluation, agency relationship, operations, and general relevant information about the company (Celik, 2002; Beretta and Bozzolon, 2004; Celik et al. 2006; Aljifri and Hussainey, 2007; Uyar and Kilic 2012). Forward-looking information disclosure in most cases reduces asymmetry of information between shareholders and companies, which assist interested users or parties making, better informed investment decisions (Alkhatib, 2012; Alkhatib and Marji 2012; Uayar and Kilic, 2012). Company annual reports are considered the most superior means of communicating this information to interested users in which forward-looking information are presented. There are various terms or key words that are included in the company chairman's report in the company annual report that represent the forward-looking information disclosure; to name some, these terms may include, predicting, expecting, foreseeing, estimating, hoping, forecasting, coming period.

The rest of this article will be constructed as follows; while the second section includes a review of the relevant literature, section three will describe data collection and research methodology, section four will include analysis and results, the conclusion will be included in section five.

2. Literature review

Previous studies on forward-looking information disclosure have focused on forecasting future earnings (Clarkson et al., 1999, 1994; Frankel et al., 1995; Lev and Penman 1990). Other studies established an association between forecasting future earnings with firm-specific characteristics to discover that large sized corporations are likely to provide more supplementary and high quality information regarding future earnings than those smaller corporations (Kent and Ung, 2003; O'Sullivan et al. 2008). On the other hand, some companies disclose forecasting future earnings voluntarily without any obligatory motives which could be in order to attract investors to construct informed decision making (Celik, 2002; Wagenhofer, 1990; Akert et al. 1998; Eaton and Stanga, 2000; Dutta and Trueman, 2002; Baginski et al., 2004; Celik et al. 2006; Lim et al. 2007; Uyar and Kilic, 2012). Furthermore, there are economic, financial, and social benefits in disclosing forward-looking information (Drake and Peavy, 1995; Lang and Landholm, 1996; Krishnam, 1996; Botosan, 1997; Sengupta, 1988). There are some companies tend to avoid the advantage of insider information and agency relationship by voluntarily disclosing good and bad news equally (Clarkson et al., 1994; Hutton et al., 2003; Johnson et al., 2001). While in some developed countries, some companies are disinclined to disclosure forward-looking information and has been considered costly and less revealing (Cooke, 1992; Frost, 1996; Choi et al., 1999; Lam and Du, 2004; Leuz and Verecchia, 2000), in other developed countries forward looking information are considered important, beneficial, and significant (Vanstraalen et al., 2003). However, if there is a high demand for forward looking information disclosure that benefits shareholders and other interested users such as financial analysts, then the company ought to consider performing a cost benefits analysis (Skinner, 1994; Botosan, 1997; Morton and Neil, 2001; Celik, 2002; Baginski et al., 2004; Uyar and Kilic, 2012).

3. Data collection, variables, and research methodology

Since the aim of this article is analyze the effect of firm specific characteristics on the level of forward looking information disclosure of 125 companies listed on the Jordanian stock exchange for 2011, this analysis will present interested users such as financial analysts and investors with important input of decision-making information.

For analyzing data in this article, content analysis methodology is adopted. Content analysis is described as scientific and quantitative methodology in social science research, which depends on the comprehension of human
communication; for example through writing. This means that the ability to comprehend written texts, phrases, or terms (Campbell and Abdul Rahman, 2010; Uyar and Kilic, 2012).

**Sector type**

Sector type has in past studies been considered as a major determinant of corporate information disclosure (Cooke, 1992; Soh, 1996; Botosan, 1997; Inchausti, 1997; Sengupta, 1998; Marston and Leow, 1998; Craven and Marston, 1999; Ahmed and Courtis, 1999; Haniffa and Cooke, 2000); Marston and Wu, 2000; Brennan and Hourigan, 2000; Ferguson et al. , 2002; Celik et al., 2006; Mitchell et al., 1995; Aljifri and Hussainey, 2007; Alkhatib, 2012, Alkhatib and Marji, 2012. Mixed statistical significant results were achieved. For the purpose of identifying the sector type, dummy variables were employed by awarding one to represent the services sector two to represent the industrial sector.

**Company size**

The company size variable is used in almost all previous studies on information disclosure; it is a proxy of a company's total assets. Large sized companies tend to disclose more information then smaller ones (Alsaeed, 2006; Uyar and Kilic, 2012). Furthermore, studies established an association between company size and the level of disclosure (Wallace, 1988; Cooke, 1989; Cooke, 1991; Lang and Lundholm, 1993; Wallace et al., 1994; Clarkson et al., 1994; Meek, et al., 1995; Hossain et al., 1995; Inchausti, 1997; Owusu-Ansah, 1998; Ahmed and Courtis, 1999; Ashbaugh, 2001; Patel and Dallas, 2002; Celik et al., 2006; Alsaeed, 2006; Aljifri and Hussainey, 2007; Uyar and Kilic, 2012; Alkhatib, 2012; Alkhatib and Marji, 2012).

**Leverage**

Leverage is considered as part of the company's capital structure and in some cases referred to as gearing ratio of a company. It is the total liabilities divided by the total assets. Leverage refers to the ability of a company to meet it financial obligations as they mature. Highly leveraged companies may deal with higher agency costs due to higher auditing fees; therefore, they will have to disclose more information (Inchausti, 1997; Alsaeed, 2006; Aljifri and Hussainey, 2007; Alkhatib, 2012; Uyar and Kilic, 2012)

**Profitability**

Profitability is described as the ability of a company to generate revenues. In most previous studies, profitability showed a significant relation with the level of disclosure. Companies with high profits tend to disclose more information and give signals good performance in order to attract investments and gain shareholders confidence (Inchausti, 1997; Watson et al. 2002; Alsaeed, 2006; Aljifri and Hussainey, 2007; Alkhatib, 2012; Uyar and Kilic, 2012).

**Auditor type**

Firms with international affiliations perform their auditing more efficiently than those without international affiliations. For the purpose of identifying the auditor type, dummy variables were employed by awarding one to represent audit firms with international affiliation, and zero to represent audit firms without international affiliation. Firms with international affiliation are also help in improving the disclosure quality and the level of disclosure of a company. (Inchausti, 1997; Hail, 2002; Alsaeed, 2006; Naser et al. 2007; Hail, 2002; Alkhatib, 2012; Uyar and Kilic, 2012)
In order to determine the extent of forward-looking information, data were manually extracted from annual reports of listed companies on the Jordan stock exchange. A disclosure index is then designed on the bases of an item/phrase does exit (used) or does not exist (not used) in the annual reports that refers to forward looking information (Johnson et al. 2001; Celik et al. 2006; O'Sullivan, 2008; Uyar and Kilic, 2012). For the purpose of this article, dummy variables are assigned to represent whether or not an item is used, if an item is used 1 is assigned to that item and zero if an item is not used. The values assigned are then summed up to represent the total score for each company. This is mathematically presented as follows:

The disclosure index = Total forward looking items disclosed / Maximum items disclosed for each company

**Regression analysis**

A model of the regression analyses was developed to measure the relationship between the forward-looking information and the explanatory variables used in this study; the model is formulated as follow:

\[ \text{FWLSCOR} = B_1 \text{Sector} + B_2 \text{Size} + B_3 \text{Leverage} + B_4 \text{Profitability} + B_5 \text{Auditor} \]

Where:
- **FWLSCOR** = Maximum forward looking disclosed items scored for a company
- **Sector** = Dummy variable 1 represents the services sector, 2 to represents the industrial sector
- **Size** = Company size measured by total company assets
- **Leverage** = Company leverage measured by Total liabilities/Total assets
- **Profitability** = Company return on total assets
- **Auditor type** = Dummy variable 1 represents audit firms with international affiliation, 2 represents audit firms without international affiliation

**4. Study results and analysis**

Tables 1 and 2 below represent the descriptive statistics of the total index values of forward looking information disclosed obtained for the services sector, while tables 3 and 4 for the industrial sector. The results show that total assets variable is the most significant variable that has an impact on the level of forward looking information disclosure for the services sector as seen in table 1. Table 3 shows the results of the analysis for the industrial sector; it is revealed that the auditor type, total assets, and profitability variables have significant relationship with the level of forward looking information items disclosure.

**Regression Analysis (Services Sector)**

**Table 1**

| Coefficientsa | Unstandardized Coefficients | Standardized Coefficients |
|---------------|-----------------------------|---------------------------|
|               | B                                  | Std. Error    | Beta     | t                        | Sig.   |
| 1             | (Constant)                        | 7.298         | .595     | 12.260                   | .000   |
| Auditor type  | .633                               | .591          | .112     | 1.071                    | .289   |
| Total assets  | 1.087E-8                           | .000          | .576     | 5.230                    | .000   |
| Profitability | .000                               | .000          | -.069    | -.661                    | .511   |
| Leverage      | .013                               | .010          | .152     | 1.403                    | .167   |

a. Dependent Variable: Num
Table 2

Residuals Statistics

|                | Minimum | Maximum | Mean   | Std. Deviation | N  |
|----------------|---------|---------|--------|----------------|----|
| Predicted Value | 7.3115  | 15.6527 | 9.0000 | 1.58639        | 56 |
| Residual       | -3.73292| 2.90415 | .0000  | 1.71404        | 56 |
| Std. Predicted Value | -1.064  | 4.194   | .000   | 1.000          | 56 |
| Std. Residual  | -2.097  | 1.632   | .000   | .963           | 56 |

a. Dependent Variable: Num

Regression Analysis (Industrial Sector)

Table 3

Coefficients

| Model | Unstandardized Coefficients | Standardized Coefficients |
|-------|----------------------------|---------------------------|
|       | B     | Std. Error | Beta | t     | Sig. |
| 1     | (Constant) | 6.422       | .584 | 11.002 | .000 |
| 1     | Auditor type | 1.472       | .575 | .238 | 2.562 | .013 |
| 1     | Total assets | 6.746E-9    | .000 | .463 | 4.909 | .000 |
| 1     | Profitability | .014        | .004 | .294 | 3.059 | .003 |
| 1     | Leverage | .005        | .008 | .065 | .688 | .494 |

a. Dependent Variable: numb

Table 4

Residuals Statistics

|                | Minimum | Maximum | Mean   | Std. Deviation | N  |
|----------------|---------|---------|--------|----------------|----|
| Predicted Value | 4.3113  | 16.8029 | 7.8873 | 1.73772        | 71 |
| Residual       | -3.75407| 4.76921 | .0000  | 1.94099        | 71 |
| Std. Predicted Value | -2.058  | 5.131   | .000   | 1.000          | 71 |
| Std. Residual  | -1.878  | 2.386   | .000   | .971           | 71 |

a. Dependent Variable: numb

5. Conclusion

This article was set out to determine the level of forward-looking information disclosure in company annual reports of listed Jordanian companies on the Jordanian stock exchange. To establish the factors that affect the disclosure, five company characteristics were employed, sector type, auditor type, total assets, profitability, and leverage. The data were manually extracted and calculated from company annual reports. The study provided mix results, in both sectors; the results revealed that the profitability seems to be the most effective variable, while the auditor type and the total assets found to a significant impact on forward looking information disclosure only in the industrial sector. This concludes that profitable companies tend to disclose more information. Moreover, large sized companies and who are audited by internationally affiliated audit firms disclose are likely to disclose more information than those who are not been audited by internationally affiliated audit firms due to the aggressive
audit standards. These findings will hopefully assist in improving factors that have an impact on the disclosure levels of the forward-looking information disclosure of listed Jordanian companies.

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