ABSTRACT

Disclosure of information by firms is an essential component in the effective functioning of capital markets (Beaver[1989]). Money allocation in the stock markets, and their effective functioning depends on the timely availability of precise and accurate information about the performance potential of firms. Information disclosure can create value in two ways: directly, by narrowing the information gap thereby decreasing investors' uncertainty about the firm; and indirectly, by enhancing value-creating activities through a reduced cost of capital and improved suppliers' and customers' terms of trade [Lev 1992]. Corporate governing bodies, financial analysts, and academic researchers are paying an increasing amount of attention to information disseminated by firms through disclosures made in their annual reports and other media reports. Discussions about investor protection, corporate governance, and corporate disclosures have taken center stage in the recent past, as the quality of information disclosures by firms greatly influences the investment decisions of the investors [Elliot and Jacobson, 1994].

A cursory examination of a sample of media reports and corporate annual report of Indian firms indicates variations across firms. The reasons for the differences in disclosure between firms have been researched by several studies [Singhvi and Desai 1971, and Botosan 1997] for firms in several countries. Firm characteristics such as size of the firm, firm performance and other factors were identified to be the cause of differences in disclosures [Cerf 1961]. However, disclosure is also affected by several factors both internal and external to the firm [Gibbins et al 1990]. Our study aims to understand how a firm manages its disclosures in its annual report, and the influences on its disclosures, both internal and external to the firm.

We constructed a disclosure index on the basis of indices in the literature, using a sample of the annual reports of 92 firms, in order to understand the differences in disclosures between firms. Two firms were selected on the basis of their disclosure scores and firm characteristics to study the differences in their management of disclosures, and the influences on their disclosures. The disclosures made by the two firms in their annual reports over a period of five years were observed, and executives in the firm who were involved in the disclosures were interviewed to understand the influences on the disclosures of the firm.

Gibbins et al [1992] suggested that economic, organizational and institutional factors influence the disclosures of a firm. Economic factors are those that merit a cost benefit analysis by the manager of the firm in making disclosures. The influence of economic factors could be in product markets, financial markets, and labour markets. Organisational factors are the qualities and characteristics specific to a firm that could influence disclosures. These could be ownership, the status of the disclosure subunit in the organization, and firm values. In the context of disclosures, we use the term institutional factor to mean a certain set of formal or informal rules that the organisation has to follow in a particular context. The influence of each of these factors on the disclosures of the case firms was studied using the annual reports, and the interviews.

It was found that in both the case firms, every factor influences the firm differently in its disclosures. A brief example of one of the findings of the study is that the product markets influence the disclosures of Infosys and Titan in different ways. In the case of Infosys, it was observed that the firm used disclosures as a tool for competitive advantage. In the case of Titan, it was found that the firm was reluctant to make extended voluntary disclosures for fear of competitors using this information.

One of the contributions of the study has been in constructing a disclosure index to understand the disclosure levels of firms through the development of a disclosure index. The contribution has been in identifying a comprehensive list of items through the study of annual reports, rather than using previous literature and suggestions of analysts as had been done in previous studies.

The study has given an understanding of the management of disclosures within the firm that contributes to the disclosures made by the firm. The literature regarding the management of disclosures has focused on the influence of one factor over the disclosures of the firm. Our study is the first of its kind in studying the management of disclosures of a firm over a period of time, and in understanding the various influences acting on the firm's disclosure decisions.