
Gregor Hagemann

Financial Reporting Quality in Emerging Economies

Empirical Evidence from Brazil and South Africa

Contents

Index of figures	XVII
Index of tables	XIX
Index of abbreviations	XXIII
Index of symbols	XXIX
1 Introduction	1
1.1 Motivation and research questions.....	1
1.2 Scientific positioning of the study.....	7
1.3 Outline of the study.....	11
2 Conceptual foundation	13
2.1 Basis of financial reporting quality.....	13
2.1.1 Purpose and addressees of financial reporting	13
2.1.2 Definition of financial reporting quality	15
2.1.3 Measures of financial reporting quality	19
2.2 Emerging economies and their accounting environment.....	25
2.2.1 Definition of emerging economies.....	25
2.2.2 Role of emerging economies in the global economy.....	30
2.2.3 Accounting characteristics.....	33
2.2.3.1 Introduction.....	33
2.2.3.2 Economic policies.....	34
2.2.3.3 Culture.....	35
2.2.3.4 Historical development and accounting origins	37
2.2.3.5 Accounting regulation and enforcement.....	38
2.2.3.6 Accounting education.....	41
2.2.3.7 Financing systems and capital markets.....	42
2.3 Financial reporting environment in Brazil, South Africa and Germany.....	44
2.3.1 Overview	44
2.3.2 Brazil	45
2.3.3 South Africa.....	51
2.3.4 Germany.....	56
2.3.5 Conclusion	59

3	Review of prior research	62
3.1	Overview of research approaches.....	62
3.2	Financial reporting practice	64
3.2.1	Indirect measure studies.....	64
3.2.2	Direct measure studies	69
3.3	Determinants of financial reporting quality	74
3.4	Capital market consequences of financial reporting quality.....	80
3.5	Implications for this study	85
4	Theory and hypotheses development.....	89
4.1	Conceptual framework and theoretical foundation.....	89
4.1.1	Introduction	89
4.1.2	Contingency theory as conceptual basis	90
4.1.3	Culture approach.....	93
4.1.4	Societal effects approach	96
4.1.5	Institutionalism	97
4.1.5.1	Introduction.....	97
4.1.5.2	New institutional economics	99
4.1.5.2.1	Basic assumptions of new institutional economics	99
4.1.5.2.2	Agency and signaling theory.....	101
4.1.5.2.3	Financial reporting as solution for agency problems	103
4.1.5.3	Positive accounting theory and political costs	105
4.1.5.4	New institutional sociology	108
4.1.5.4.1	Basic assumptions of new institutional sociology	108
4.1.5.4.2	Legitimacy theory	110
4.1.5.4.3	Stakeholder theory	113
4.1.6	Summary.....	116
4.2	Hypotheses development	118
4.2.1	Introduction	118
4.2.2	Financial reporting practice	118
4.2.3	Determinants of financial reporting quality	120

4.2.4	Capital market consequences	127
4.2.5	Summary	129
5	Research design	131
5.1	The empirical field.....	131
5.1.1	Sample selection	131
5.1.2	Sample description.....	133
5.1.2.1	Industry composition	133
5.1.2.2	Company size	135
5.1.3	Research objects.....	141
5.1.4	Annual report characteristics	143
5.2	Methodology of financial reporting quality measures.....	145
5.2.1	Accruals-based earnings management measure.....	145
5.2.1.1	Magnitude of accruals	145
5.2.1.2	Modified-Jones model	146
5.2.2	Disclosure index measure.....	149
5.2.2.1	Basis of content analysis.....	149
5.2.2.2	Reliability and validity of content analyses.....	152
5.2.2.3	Self-construction of disclosure index.....	154
5.2.2.4	Content categories.....	156
5.2.2.5	Mandatory vs. voluntary reporting	159
5.2.2.6	Weights	161
5.2.3	Readability measure.....	165
5.3	Methods of analysis	168
5.3.1	Introduction	168
5.3.2	Analysis of financial reporting practice by descriptive and univariate statistics	169
5.3.3	Determinants analysis	170
5.3.3.1	Selection of variables	170
5.3.3.2	Bivariate correlation and multivariate analysis	173
5.3.4	Capital market analysis on the basis of information asymmetries	176
5.3.4.1	Conceptual considerations.....	176
5.3.4.2	Information asymmetries models and variables.....	177

6	Empirical results	182
6.1	Financial reporting practice	182
6.1.1	Accruals-based earnings management.....	182
6.1.1.1	Magnitude of accruals	182
6.1.1.2	Modified-Jones model	183
6.1.2	Annual reporting practice	185
6.1.2.1	Size of annual reports	185
6.1.2.2	Content-related analysis of annual reports	187
6.1.2.2.1	Total financial reporting quality.....	187
6.1.2.2.2	Background information	189
6.1.2.2.3	Financials.....	191
6.1.2.2.4	Non-financials	193
6.1.2.2.5	Sustainability	195
6.1.2.2.6	Value based management.....	196
6.1.2.2.7	Forward-looking information.....	198
6.1.2.2.8	Risks and opportunities.....	199
6.1.2.3	Interim conclusion	201
6.1.3	Readability of annual reports	202
6.1.4	Comparison of financial reporting quality measures	206
6.1.5	Critical evaluation of the results.....	209
6.2	Determinants of financial reporting quality	214
6.2.1	Correlation analysis of independent variables.....	214
6.2.2	Isolated analysis of determinants.....	216
6.2.2.1	Introduction.....	216
6.2.2.2	Company size	216
6.2.2.3	Company age	217
6.2.2.4	Profitability	218
6.2.2.5	Company valuation	219
6.2.2.6	Systematic company risk.....	220
6.2.2.7	Ownership concentration	220
6.2.2.8	Industry.....	222
6.2.2.9	Customer basis	225

6.2.2.10	Information environment	227
6.2.3	Simultaneous analysis of determinants	228
6.2.4	Sensitivity analyses and robustness tests	237
6.2.5	Critical evaluation of the results.....	238
6.3	Information asymmetries	247
6.3.1	Introduction	247
6.3.2	Descriptive statistics and correlation analysis	248
6.3.3	Results of multivariate regression analysis	251
6.3.4	Sensitivity analyses and robustness tests	256
6.3.5	Critical evaluation of the results.....	259
6.4	Discussion	262
7	Conclusions	268
7.1	Main findings and implications	268
7.2	Limitations and outlook	273
	Appendix	277
	Index of laws, standards and regulations	295
	References.....	297