

## Malaysian Institutional Investors' Annual Reports Information Needs

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### ABSTRAK

*Rencana ini mengkaji keperluan maklumat daripada laporan tahunan bagi pelabur institusi di Malaysia. Data dikumpulkan melalui borang soalselidik, daripada sampel yang terdiri daripada 286 pelabur institusi di Malaysia (meliputi agensi kerajaan dan industri swasta) dan dianalisis untuk melihat perbezaan dan hubungan sejauhmana tahap penggunaan dan anggapan kepentingan laporan tahunan di kalangan pelabur institusi di Malaysia. Hasil kajian menunjukkan terdapat perbezaan yang signifikan dalam tahap penggunaan dan anggapan kepentingan setiap item dalam laporan tahunan yang diuji di kalangan pelabur institusi.*

### ABSTRACT

*This paper examines annual report information needs of Malaysian institutional investors. Data were collected from a sample of 286 institutions (comprising government agencies and private industries) through questionnaires, and were analysed to test for differences and relationships in the extent of usage and perceived importance of annual reports in Malaysia. The results indicate some significant differences in the extent of usage and in the perceived importance of items in annual reports between institutional investors.*

### INTRODUCTION

Much of the literature on financial information needs has been concerned with the experience of information users in industrialized countries such as countries in Europe, Japan and the United States. The focus of this research is on the need for financial information in a developing country in the Asia Pacific region, specifically Malaysia; Malaysia and the countries previously studied have different cultures and environments (Hofstede, 1984; Gray, 1988).

This paper attempts to accomplish two objectives: firstly, to examine the extent of usage of annual reports by Malaysian institutional investors in making their investment decisions, and secondly, to examine the perceived importance of items of information in annual reports by these investors.

The paper is organized in four sections. The first section describes previous research, the second section presents the research methodology, and the third and the fourth

sections discuss results and conclusions respectively.

### PREVIOUS RESEARCH

Published annual reports disclose accounting information and fulfill the information needs of those external users who have limited authority, ability, or resources to obtain information [Financial Accounting Standards Board (FASB), 1980]. The FASB noted that adequate annual reports should contain useful information to serve as important input into users' decision models. The concept of 'decision-usefulness' emphasizes the importance of providing adequate financial reports that would fulfill users' information needs (Dopuch and Sunder, 1980). However, previous studies have suggested that annual reports fail to provide adequate information to various users (e.g., Baker and Haslem, 1973; Chang, Most and Brain, 1983; Wallace, 1988). These studies have also shown that different users require

different financial information. Hence, what kind of information is needed by the users from an annual report when making an investment decision? To identify an annual report that adequately provides useful information is difficult. However, many studies have been undertaken to discover what users believe to be adequate information in annual reports, that can be used in their decision-making. By measuring the extent of usage and the perceived importance of items in annual reports, we would be able to assess the information needs of those users.

There have been several attempts to measure the importance and the extent of disclosure of information in annual reports. These studies include Singhvi and Desai (1971), Baker and Haslem (1973), Buzby (1974), Benjamin and Stanga (1977), McNally, Eng and Haseldine (1982), Chang et al. (1983), Wallace (1988), and Tan, Kidam and Cheong (1990). Research in this area has increased in depth and magnitude since the pioneer study of financial disclosure by Mautz (1968), as users are becoming more aware of the importance of accounting information in their economic decision-making. For example, Singhvi and Desai (1971) developed an index of disclosure in annual reports by corporations. Buzby (1974) expanded the study to include small and medium sized companies in his work on determining the disclosure practices and the extent of importance of items of information listed in annual reports. The study anticipated an expansion of the extent of disclosure in annual reports.

Following these studies, more research has been undertaken to examine disclosure practices in annual reports and needs of different user groups. For example, Benjamin and Stanga (1977) compared the perceived information needs of commercial bank loan officers and professional financial analysts. The results suggest that there were differences between the two primary users on the perceived importance of information. McNally et al. (1982) studied the information needs of external decision-makers and how these needs are satisfied by financial reporting in New Zealand. The findings were consistent with earlier studies conducted in other developed countries. The study looked into the relationships

between corporate characteristics and the quality of corporate disclosure practices. It was found that large companies prepared more comprehensive financial reports; nevertheless, the superior practices (i.e., preparing comprehensive reports) were relatively low when compared with levels desired by professional external users. Disclosure practices by companies had to be improved to provide adequate information for users.

Chang et al. (1983) studied the utility of annual reports for investment decisions internationally. The study investigated three user groups, namely, individual investors, institutional investors, and financial analysts, on the importance of corporate annual reports as a source of information for investment decisions. Findings indicated that institutional investors and financial analysts were a homogeneous group but individual investors were very diverse in their decisions.

All the studies cited above were conducted in developed countries such as Australia, New Zealand, the United Kingdom and the United States. These countries were grouped as having similar cultural systems (Hofstede, 1984). Few studies in the area of financial information disclosure and importance have been carried out in developing countries such as Malaysia. One study, Tan et al. (1990) investigated the extent of importance of items of voluntary information in Malaysian corporate annual reports. The results of this study implied that voluntary information disclosed in annual reports was relatively small compared to other countries in the region and that disclosure practices needed to be improved. However, the paper provided only some of the information needs of users in Malaysia.

The purpose of this study is to complement and expand the previous studies. It aims to examine the domestic users' need for information from public companies' annual reports. We argue that domestic users' information needs for useful economic decision-making are inadequately provided by annual reports of Malaysian public companies. The study attempts to answer the following research questions:

1. What is the extent of Malaysian institutional investors' use of information from the annual reports of public companies for

investment decisions in stock and/or bonds?

2. How do the institutional investors perceive the importance of items disclosed in the annual reports in making their investment decisions?

## METHODOLOGY

### *Sample*

Data were collected by means of a survey conducted on a sample of 286 institutional investors. The population of the study was confined to institutional investors, one of the primary users of annual reports. Stratified random sampling was used to select institutions since the population, listed in the directory obtained from the Ministry of Finance, is divided into two sub-samples, i.e., government-owned institutions and private corporations.

### *Questionnaire*

A list of items of information disclosed in annual reports was developed based on a disclosure index constructed by Douppnik (1987). This index was used because of its comprehensiveness and because it was used by many other studies conducted in the area of financial information disclosure. However, the questionnaire developed was modified to take into consideration the differences in Malaysian practices and environment. The selection of items in the index to be included in the questionnaire was based on, among others, the disclosure requirements derived from legislation - the Malaysian Companies Act 1965 and/or ordinance, professional accounting bodies, and the rules of the Kuala Lumpur Stock Exchange (for the listed companies). The purpose of the selection was to limit the items of information to be included in the questionnaire and to add a degree of homogeneity to the items. The index was then pre-tested for reliability and validity.

The questionnaire sought to gather data relating to the source of information used in investment decision-making, the degree of extensiveness in using the different segments in the annual reports and the perceived importance of different segments in the annual reports. A pilot study was conducted

on a group of financial managers to test the questionnaire.

Of the 286 questionnaires sent to various institutions in the sample, twenty-two were excluded from the analysis (seventeen questionnaires were returned due to respondents' change of address and fifteen others provided incomplete data). A total of 113 usable questionnaires (42.8%) were returned. These consist of responses from government-owned agencies (29%), private industries (41.5%) and other private sectors (29.5%).

Data were analyzed using nonparametric statistics. Rankings were used to measure the extent of usage of segments in annual reports and a five-point Likert scale was used to measure the perceived importance of items of information in the annual reports. Frequency distributions of the preferences of each group were used to compute the overall mean score for each factor. The f-test was then used to test for significant differences in these means between and within user-groups.

## RESULTS

Table 1 reports the mean scores on the degree of extensiveness in the use of annual reports by institutional investors when making decisions to invest in stocks. The table shows that the mean scores for government agencies are lower than for private investors. However, there were significant differences among the six segments of the annual reports ( $p < 0.01$ ) between the sectors.

Table 2 reports the mean scores on the perceived degree of extensiveness of institutional investors' use of annual reports when making decisions to invest in bonds. The table shows that the mean scores from the four segments (namely, corporate information, financial highlights, auditors' reports and notes to account) are significantly different among the sectors.

Table 3 provides the mean scores in the ranking of segments in annual reports in the order of importance. The table shows that in the government sector, the consolidated balance sheet is ranked as the most important segment in annual reports. However, in the private sector, that segment is less important

TABLE 1. Extensiveness in Using Different Segments in Annual Report  
When Making Decisions to Invest in Stocks

Segments	Mean Score			F	Signifi- cance
	Government	Industry	Others		
Corporate Management Information on Management Team	1.333	2.912	2.588	14.499	0.000
Financial Highlight	1.778	2.529	2.294	2.454	0.095
Chairman's Statement	2.000	3.029	2.647	5.781	0.005
Director's Report	1.444	2.177	2.000	2.214	0.118
Auditor's Report	1.444	2.177	1.824	1.867	0.163
Balance Sheet	1.444	2.794	2.471	5.967	0.004
Profit and Loss	3.222	3.647	3.588	1.899	0.159
Consolidated Balance Sheet	3.222	3.735	3.706	3.135	0.051
Consolidated Profit and Loss	3.222	3.618	3.647	1.314	0.276
Statement of Source and Applications of Funds	3.222	3.677	3.706	1.926	0.155
Notes to Account	2.556	3.500	3.059	3.494	0.037
List of Major Properties Held	2.556	3.471	3.235	3.726	0.030
Other Information	2.000	2.618	2.824	2.217	0.118
	1.000	1.559	1.118	2.617	0.081

TABLE 2. Extensiveness in Using Different Segments in Annual Reports  
When Making Decisions to Invest in Bonds

Segments	Mean Score			F	Signifi- cance
	Government	Industry	Others		
Corporate Information Information on Management Team	1.600	2.812	1.800	4.812	0.0179
Financial Highlight	1.400	2.312	2.200	1.903	0.1719
Chairman's Statement	2.000	3.063	2.800	5.079	0.0149
Director's Report	1.400	2.437	1.800	3.024	0.0683
Auditor's Report	1.200	2.063	1.600	1.703	0.2043
Balance Sheet	1.000	2.875	2.000	6.312	0.0065
Profit and Loss	3.000	3.688	3.400	4.618	0.0206
Consolidated Balance Sheet	3.000	3.688	3.400	4.618	0.0206
Consolidated Profit and Loss	3.000	3.688	3.200	2.498	0.1043
Statement of Source and Applications of Funds	3.000	3.688	3.400	2.014	0.1564
Notes to Account	1.800	3.563	2.600	8.349	0.0019
List of Major Properties Held	2.000	3.188	2.000	4.448	0.0233
Other Information	1.000	1.560	2.000	1.323	0.2868

TABLE 3. Ranking of Segments in Annual Reports by Institutional Investors

Segments	Mean Score			F	Significance
	Government	Industry	Others		
Corporate Information	9.778	7.941	7.790	1.160	0.3204
Information on Management Team	9.779	9.176	9.316	0.142	0.8674
Financial Highlight	8.889	6.324	8.211	3.933	0.0249
Chairman's Statement	11.778	9.352	10.421	2.503	0.0905
Director's Report	11.222	10.205	10.368	0.592	0.5561
Auditor's Report	9.222	9.088	9.536	0.163	0.8496
Balance Sheet	2.778	4.088	3.211	1.997	0.1449
Profit and Loss	3.333	3.412	2.526	1.088	0.3435
Consolidated Balance Sheet	1.667	3.765	4.000	3.144	0.0504
Consolidated Profit and Loss	2.222	2.941	3.210	0.788	0.4594
Statement of Source and Applications of Funds	6.222	6.118	6.474	0.075	0.9274
Notes to Account	5.667	6.706	6.367	0.676	0.5124
List of Major Properties Held	7.222	9.412	10.105	3.926	0.0250
Other Information	12.444	10.118	9.000	0.959	0.3890

TABLE 4. Relationship Between Extensiveness of Use of Annual Reports and Perceived Importance of the Annual Reports By Malaysian Institutional Investors in Investment Decisions

Correlations:	B/S	P/L	A/F	Notes	CB/S	CP/L	D/R*
Invest in stock	.015	.060	.045	.376	.643	.362	.062
Invest in bond	.085	.031	.087	.471	.655	.417	.121
Overall	.050	.046	.066	.428	.659	.395	.092

- \* B/S - Balance Sheet
- P/L - Profit and Loss
- A/F - Statement of Source and Application of Funds
- Notes - Notes to Accounts
- CB/S - Consolidated Balance Sheet
- CP/L - Consolidated Profit and Loss
- D/R - Director's Report

TABLE 5. Perceived Importance of Item of Information in Annual Reports

Information Item	Mean Score			F	Significance
	Govt.	Industry	Others		
1. The basis on which fixed assets are stated should be disclosed.	4.462	4.277	4.217	0.790	0.456
2. Fixed assets should be shown by categories i.e. land & building, plant & equipment.	4.385	4.234	4.478	1.170	0.314
3. When fixed assets are stated in historical cost statement, depreciation based on the revaluation amount should be charged to income.	4.307	3.340	3.261	9.060	0.000
4. When fixed assets are stated in historical cost statements, at an amount in excess of cost, the basis for revaluation should be disclosed.	4.539	4.043	4.130	3.354	0.039
5. Fixed assets should be written down if the value to their business is lower than net book value.	4.306	4.021	3.696	1.811	0.169
6. Depreciation charges disclosed should reflect the estimated salvage value at the estimated useful life.	4.115	3.936	3.606	1.720	0.184
7. Depreciation charges disclosed should be on a systematic & rational basis.	4.306	4.149	4.348	0.576	0.564
8. Depreciation methods should be disclosed.	4.423	4.489	4.348	0.257	0.773
9. The amount of accumulated depreciation should be disclosed.	4.462	4.468	3.826	7.011	0.001
10. Comparative figures for previous period should be disclosed.	4.423	4.319	4.862	1.482	0.232
11. Statement of changes in financial position should be disclosed.	4.616	4.319	4.304	1.450	0.239
12. Investment in 50% owned companies should be accounted for on the equity.	4.577	4.000	3.967	5.401	0.006
13. Investment in less than 50% owned companies, over which the investor can exercise significant influence should be accounted for on equity basis.	4.308	3.979	3.826	1.671	0.193
14. When an investment is accounted for on the equity basis, adjustments such as the elimination of intercompany profits should be made.	4.500	3.851	3.826	3.350	0.039
15. When the market value of quoted investment is different from their carrying amount, the market value should be disclosed.	4.654	4.383	4.473	1.555	0.216
16. The methods of accounting for leases should be disclosed.	4.115	4.064	4.044	0.045	0.955
17. Receivables should be reduced by provision to cover possible collection cost and other losses on unspecified as well as specified accounts that on the basis of past experience and general business knowledge, may be incurred.	3.769	4.319	4.174	2.578	0.061
18. Receivables from affiliated companies should be disclosed.	3.692	4.085	3.869	1.645	0.196
19. The basis on which inventories are stated should be disclosed.	3.923	4.447	4.130	3.913	0.023
20. Inventories should be stated at lower of cost or market value.	4.461	4.447	4.044	3.153	0.047
21. The method of determining the cost of inventories should be disclosed.	3.577	4.296	3.826	5.055	0.008
22. When a liability is secured on the company's assets, this fact should be disclosed.	4.346	4.617	4.478	1.437	0.242
23. The amount of firm contracts for future capital expenditure not accrued at the date of the financial statement at an amount in excess should be credited to revaluation reserve.	3.423	3.170	2.565	2.863	0.020
24. Sales and other revenues should be disclosed.	3.846	4.575	4.522	6.339	0.002
25. Cost of sales should be disclosed.	4.269	4.213	4.067	0.279	0.756
26. Separate disclosure of the advertisement expenditure for the past year should be disclosed.	3.077	2.806	2.696	0.973	0.381
27. Separate disclosure of the R & D expenditure for the past year should be disclosed.	3.154	3.234	2.783	1.841	0.164
28. Unusual & extraordinary gains /& losses should be taken directly to shareholder's equity.	2.808	3.702	3.000	6.716	0.004
29. Number and type of employees at year end should be disclosed.	2.348	2.861	2.478	1.945	0.148
30. Rights and preferences to dividends and to principals should be disclosed.	3.986	4.043	3.870	0.299	0.741
31. Accounting practices adhere strictly to tax requirements should be disclosed.	3.789	4.021	3.862	1.397	0.252
32. Deferred taxes should be recorded.	3.848	3.957	3.478	2.283	0.107
33. Primary earning per share should be disclosed.	4.289	4.086	3.870	1.114	0.332
34. The identity of the ultimate parent company should be disclosed.	4.289	4.170	4.391	0.686	0.670
35. Consolidated financial statements, together with the corporate financial statement of a parent company should be prepared for shareholders.	4.308	4.468	4.364	0.383	0.683

TABLE 5. Perceived Importance of Item of Information in Annual Reports

Information Item	Mean Score			F	Significance
	Govt.	Industry	Others		
36. Intercompany transactions' profits and losses should be eliminated in consolidated financial statement.	4.639	4.298	4.273	0.726	0.487
37. An accounting principle of method chosen from two or more available QAAP to meet a given circumstance should be disclosed.	3.885	3.967	3.966	0.081	0.940
38. When accounting principle & method have not been applied on the same base from period to period in the determination of results of operation of financial position, the effect of the change should be disclosed.	4.500	4.698	4.182	2.489	0.129
39. Departures from the consistency concept should be disclosed.	4.500	4.532	4.136	2.469	0.090
40. The basis of translating foreign currencies should be disclosed.	4.385	4.192	4.136	0.753	0.474
41. In translating foreign currency financial statement, the closing exchange rate should be applied to all assets and liabilities.	4.270	4.192	4.046	0.406	0.667
42. Breakdown of net income or profit by decision or individual companies or geographical area should be disclosed.	3.423	3.761	3.620	1.102	0.336
43. Description of main activities and new investments in each foreign country or geographical area should be disclosed.	3.885	3.891	3.818	0.053	0.948
44. Amount of foreign assets analysed by individual country should be disclosed.	3.806	3.739	3.273	3.077	0.050
45. Amount of foreign long-term debt analysed by currency should be disclosed.	3.923	4.064	3.783	0.972	0.382
46. Amount of foreign assets analysed by continent or grouping by countries should be disclosed.	3.077	3.532	3.174	2.267	0.109
47. Amount of foreign assets subject to high political risk should be disclosed.	3.962	4.149	4.067	0.387	0.680
48. Number & type of employees at year end breakdown by geographical area should be disclosed.	2.346	2.596	2.348	0.881	0.418
49. Amount of transfers between geographical segments should be disclosed.	3.423	2.851	2.609	4.442	0.014
50. Amount of foreign short term debt analysed by currency should be disclosed.	3.692	3.787	3.522	0.595	0.553
51. Amount of foreign assets analysed by major product line should be disclosed.	3.039	3.383	2.957	2.426	0.094
52. Breakdown of total sales by customers served or individuals served should be disclosed.	2.269	3.106	2.913	5.162	0.007
53. Amount of transfers between product or line of business segments should be disclosed.	2.962	3.170	2.696	1.899	0.155
54. Breakdown of total sales by major product line should be disclosed.	3.692	3.936	3.391	2.130	0.124
55. Breakdown of net income or profit by major product line should be disclosed.	3.500	4.149	3.435	4.787	0.010
56. Breakdown of total sales by division or individual companies should be disclosed.	3.077	3.745	2.957	7.086	0.001
57. Number & type of employees at year end breakdown by line of business should be disclosed.	2.692	2.809	2.435	1.217	0.300

than consolidated profit and loss. In general, the figures indicate that accounting numbers (quantitative information) in the annual reports are perceived as more important than qualitative information.

Table 4 reports the relationship between the extent of usage of annual reports and the perceived importance of annual reports by the institutional investors. The table shows a positive correlation between extensiveness of usage and perceived importance of the segments in the annual reports, especially in the segments 'consolidated balance sheet', 'notes to account' and 'consolidated profit and loss'.

Table 5 reports the mean scores of the perceived importance of each item of information for the three user groups. Out of the 57 items of information, ten items have mean scores that are significantly different among sectors. In general, Malaysian institutional investors are homogeneous in their perception of the importance of items of information; they agree on the same items in the questionnaire.

### CONCLUSION

This study examined the extent of usage and perceived importance of items of information in the annual reports by Malaysian institutional investors. The results indicate that there are some significant differences in the extensiveness of use of annual reports between the groups of institutional investors. There are also some significant differences in the perception of the importance of segments in annual reports. However, institutional investors are consistent in their perceptions of the importance of items of information in the annual reports. The results suggest that external users (i.e., institutional investors) believe that annual reports provide information for investment decision-making, and the investors use annual reports, especially segments with accounting numbers information, as important input in their decision models. These findings imply that the information needs of institutional investors in Malaysia are quite similar to those in the countries cited earlier. However, disclosure practices need to be improved to allow users to adequately

utilize information regarding public corporations in Malaysia.

The study has some limitations. First, the responses may not be true since the use of subjects' perceptions as a substitute for institutions' perceptions may not be accurate. It may be true that the way an individual perceives situations often influences how he or she deals with them, but the perceptions of individuals and how their organizations deal with the perceived situations may not be congruent. In addition, statistical techniques and analysis may not be sufficient to allow the imputation of causation.

The results of the study may be of interest to those who are concerned with upgrading the quality of annual reports in Malaysia. The importance of users' information needs should not be underestimated. It is an important task of accounting to provide concerned persons other than management with information about the status and probable progress of a corporation. Further research is needed to determine the impact of utilization of items in annual reports on the investment decision-making process in Malaysia.

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