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Abstract

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Keywords

Annual Reports; Narrative sections; Users' information needs; Iranian companies

Users' Information Requirements and Narrative Reporting: The Case of Iranian Companies

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Abstract

This paper investigates whether the narrative section of Iranian companies' annual reports satisfies the information requirements of financial analysts employed by institutional investors. Taking a group of stakeholders (i.e. financial analysts) as the sample, a questionnaire survey was conducted to identify their top three information needs from the narrative sections of company annual reports in each of three information categories: Present, Analytical and Prospective. Following this survey, a checklist was prepared to analyse whether Iranian companies are disclosing this information required by financial analysts. Overall, the results partially support stakeholder theory as there is a general lack of information flow on the part of Iranian listed companies in meeting their stakeholders' information needs.

Keywords: Annual Reports; Narrative sections; Users' information needs; Iranian companies.

JEL Classification: M400

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1. Introduction

Recent corporate failures around the globe have highlighted the significance of corporate disclosure. The only statutory formal communication medium between business organisations and their interested parties are annual reports (Santema et al. 2005; Stanton, Stanton & Pires 2004). Hence annual reports have been the centre of attention of a large number of researchers (Santema et al. 2005; Stanton, Stanton & Pires 2004; Stanton & Stanton 2002).

Annual reports comprise two main sections: the voluntary section and the mandatory section (Stanton, Stanton & Pires 2004). The voluntary section provides narrative information together with tables and graphs, while the mandatory section is prepared in accordance with the legislation of the jurisdiction. The voluntary section of annual reports contains twice the amount of information than the mandatory section (Smith & Taffler 2000). As the voluntary section is not governed by regulations, information items are included at the discretion of management (Clatworthy & Jones, 2001).

The narrative section of annual reports is of considerable value to different user groups of annual reports such as financial analysts and other investors (Barlett & Chandler 1997; Mirshekary 2005; Tiexiera 2004). It is significant to financial analysts in particular that their information requirements be fulfilled by the narrative section (Graham, Cannice & Sayre 2002). This is because most financial analysts have a significant influence on the market valuation of public firms. As a result, prudent executives can increase shareholder value by disclosing the information items required by these analysts in a clear and comprehensive manner (Graham, Cannice & Sayre 2002). Analysts are influential and knowledgeable users of annual reports and their information requirements are the same as those of their client investors (Ho & Wong 2004).

Given the volume of voluntary information in annual reports and its use by different users, it is interesting to examine the actual usefulness of such information in investment decisions. It can be argued that the mere supply of abundant information does not necessarily fulfil or meet users' needs or enhance the quality of reporting. Therefore, rather than engage in information overload, only information that is relevant and useful should be reported – i.e. those information items which satisfy shareholders' information requirements (Cook & Sutton 1995; International Accounting Standards Board 2006; Joshi & Abdulla 1994).

There are very few studies which investigate whether narrative sections of annual reports contain the information items required by annual report users. The dearth of research in this area is even more evident in the case of Islamic countries. Hence the aim of the present study is to investigate whether the narrative section of Iranian companies' annual reports satisfies the information requirements of financial analysts employed by institutional investors. The reason behind concentrating on Iran is due to the call for increased foreign and domestic investment.

Prior studies have demonstrated that financial analysts' information requirements have not been met in Iranian companies' annual reports (Mirshekary 2005; Mirshekary & Saudagaran 2005). Mirshekary and Saudagaran (2005) reported that, in 1997, several user groups (including bank loan officers, bank investment officers, auditors, tax officers, stockbrokers, institutional investors and academics) were concerned that their information requirements were not being met by Iranian companies' annual reports. Mirshekary (2005) further confirms this concern and states that Iranian companies are not disclosing the information items that are required by bank investment officers, bank loan officers, corporate investors and stockbrokers.

Mirshekary and Saudagaran (2005) surveyed users (including institutional investors), about their perception of present information disclosed in Iranian companies' annual reports. Mirshekary (2005) investigated the degree of consensus between the present information disclosed in Iranian companies' annual reports and users' information requirements. However, these studies did not include the users' requirement of analytical and prospective information. The present study fills this gap by including this information in its survey of financial analysts employed by institutional investors.

This paper is organised into seven sections. The following section outlines previous literature investigating users' information requirements of corporate annual reports and the extent to which these reports satisfy the users' information needs. The third section discusses corporate reporting regulations of annual reports in Iran. The next section discusses the adoption of 'stakeholder theory' as a framework for analysis. The fifth section discusses the research methods and data analysis used in this study. The following section explains the results, and the final section presents our conclusions and outlines some directions for future research.

2. Literature Review

There are several studies that have investigated the information requirements of annual report users (CPA Journal 1994; Estep 1987; Ho & Wong 2004; Mozier & Arnold,1984). Estep (1987) has suggested that some of the information requirements of security and/or financial analysts to estimate the expected returns of stock could include Return on Equity (ROE), growth in equity and price-to-book value of stock. However, Estep (1987) did not survey the security and/or financial analysts themselves.

Ho and Wong (2004) examined the usage and perceived usefulness of corporate annual reports in Hong Kong by one major group of external users – investment/financial analysts. These analysts suggested that factors affecting the future financial results, future prospects of the company, product market share, acquisition and disposal activities, and information provided in the *China Business Review* were the five voluntary disclosure items most significant to them. Similarly, Mozier and Arnold (1984) surveyed investment analysts to identify their information requirements from company information. They classified investment analysts in the United Kingdom (UK) into two groups – portfolio managers and information intermediaries – to better understand their information requirements from companies. Analysts considered dividend yields, various financial ratios, and the company's net assets in their evaluation of a company's performance. Both groups suggested including geographical analysis of a company's results in that company's accounts as well as analysis of the company's different lines of business. However, these additional disclosure items were more strongly favoured by information intermediaries than by portfolio managers. Similarly, CPA Journal (1994) reported that 44% of responding Chartered Financial Analysts (CFAs) in Australia perceived that, in making investment decisions, more information (such as budgets for the next five years and forecasts of earnings per share (EPS)), needed to be disclosed in company annual reports.

The above studies did not report whether corporate annual reports actually contained the information required by financial analysts. Some studies have reported the status of corporate annual reporting based on the information requirements of annual report users (Chatterjee 2007; Hooks, Coy & Davey 2002; Joshi & Abdulla 1994; Stanga 1976). Joshi and Abdulla (1994) conducted a survey in India of both 'sophisticated' investors (including professional chartered accountants and accounting teachers-cum-investors), and 'non-sophisticated' investors (including those who were neither chartered accountants nor teachers-cum-investors), to investigate their information requirements of corporate annual reports. While they found that both investor groups attached a high significance to value-added statements and cash profit per share, the Indian companies did not disclose both of these information items at the same time. Joshi and Abdulla (1994) concluded that either Indian companies were unaware of the information requirements of users or that these companies did not attach much importance to their investors' information requirements. Chatterjee (2007) raised a similar concern of the non-fulfilment of users' information requirements in Indian companies' annual reports. This study reported that Indian companies diverted the attention of annual report users to favourable information items in order to create a good public impression while they disregarded the disclosure of information items that were perceived to be significant by investors.

The information requirements of financial analysts (including security analysts) have been studied by various authors. After investigating 79 information items that were considered significant by CFAs in 80 companies from the 'Fortune 1,000' for 1972-1973, Stanga (1976) revealed that the published annual reports of large industrial firms were deficient in providing information items considered significant by those CFAs in their study sample. Hooks, Coy, & Davey (2002) also report similar evidence in New Zealand – such as New Zealand electricity companies that did not disclose those information items considered important by various stakeholders.

Following the concerns raised by the above studies that companies are not disclosing the information required by investors (Joshi & Abdulla, 1994; Chatterjee, 2007), financial analysts (Stanga, 1976), and other stakeholders (Hooks Coy & Davey, 2002), this study aims to investigate whether the narrative section of Iranian companies' annual reports satisfies the information requirements of financial analysts employed by institutional investors.

Annual reports are perceived to be significant in Islamic countries (Al-Razeen & Karbhari, 2004). Al-Razeen and Karbhari (2004) investigated the perception of five groups of external annual report users in Saudi Arabia of annual reports compared to other sources of corporate information, such as interim reports, specialists' advice, friends' advice, newspapers and magazines, specialised publications, direct information from companies and market rumours. These groups of external users include individual investors, institutional investors, creditors, governmental officials and financial analysts. The results indicate that these users perceived annual reports as the most important source of information. However, there is a dearth of research investigating whether annual reports in Islamic countries actually contain the information required by various stakeholders (Meek & Thomas 2004).

Abu-Nassar and Rutherford (1996) investigated the perceptions of external users of corporate financial reports in Jordan – a country which has a moderately well-structured capital market. These users were institutional shareholders, bank loan officers, stockbrokers, academics and individual shareholders. Abu-Nassar and Rutherford (1996) concluded that both income statements and balance sheets were read thoroughly by all of these five groups as well as the directors' reports and statistical summary sections. All of these user groups agreed that the information disclosed by companies in Jordan was inadequate.

Similar to Abu-Nassar and Rutherford (1996), Naser, Nuseibeh & Al-Hussaini, (2003) investigated the perceptions of different user groups of financial information about corporate reporting in Kuwait. The groups comprised institutional investors, individual investors, financial analysts, bank loan officers, government officials, auditors and stock market brokers. The respondents agreed that the information contained in these annual

reports was useful to make informed investment decisions and to evaluate these companies' performances. Voluntary disclosure items such as earnings per share and investments in shares and bonds were assigned a high importance by these respondents.
Mirshekary and Saudagaran (2005) investigated the perceptions of Iranian user groups comprising bank loan officers, bank investment officers, auditors, tax officers, stockbrokers, institutional investors, and academics in 1997 regarding corporate annual reports. Although the majority of respondents indicated annual reports as the most important source of information, the published annual reports were deficient in providing the required information items due to a lack of adequate detail and a delay in publishing. The respondents ranked cost of goods sold, total revenue and breakdown of different sources of revenue, the breakdown of operating income and extraordinary gains or losses as their top three required important items.

Abu-Nassar and Rutherford (1996) and Naser, Nuseibeh and Al-Hussaini, (2003) did not investigate whether corporate annual reports in Jordan and Kuwait disclosed the information required by stakeholders. Similarly, Mirshekary and Saudagaran (2005) did not investigate whether corporate annual reports in Iran contained this required information. The study by Mirshekary (2005) is the only study that has investigated the association between actual disclosure and the stakeholders' information needs.

Mirshekary (2005) measured the association between actual disclosure and the rankings provided by bank investment officers, bank loan officers, corporate investors and stockbrokers for various information items. The results showed a low level of association, suggesting that the information requirements of these user groups were not met by Iranian companies in their annual reports. These user groups were more interested in the narrative section of annual reports than the financial statements section. However, as previously mentioned, even this study (Mirshekary 2005) only included present information, and it did not investigate users' required analytical and prospective information.

Following this dearth in research concentrating on the narrative section of annual reports in Islamic countries, the present study investigates whether the narrative section of Iranian companies' annual reports satisfies the information requirements of financial analysts employed by institutional investors. It also investigates financial analysts' required analytical and prospective information needs. As previously stated, the reason for concentrating on Iran is due to its call for increased foreign and domestic investment. The next section explains the regulation of annual reporting in Iran.

3. Annual Reporting Regulation in Iran

The regulatory framework in an emerging economy like Iran is not as developed as that of the international standard. Iran is termed as a code-law country, having a weak equity market, a lack of investor protection, judicial inefficiencies, ineffective enforcement mechanisms and a low quality of financial reporting (Mashayekhi & Mashayekh 2008; Molkararee 2004; Noravesh & Dianati 2003; Poorjalali & Meek 1995). The capital market in Iran is new and inefficient. Iran has only one stock exchange, the Tehran Stock Exchange (TSE), which commenced its operation in February 1967 with only six companies (http://www.iranbourse.com). The corporate governance issue was first addressed in early 2000 (when an internal governance structure was dominant) and only a few external control mechanisms are in place (Mashayekhi & Mashayekh 2008).

At present more than 420 domestic companies are listed in the TSE and are governed by the securities act (approved 2005) and the listing rules (approved 2007). The major growth in the number of listed companies from 6 to 105 took place during 1967-

1978. However, Islamic revolution and war lead to major decreases in TSE trading, and the number of listed companies fell to 56. In 2006, the number of listed companies on the TSE increased to 422. The TSE became a member of the Federation of Euro-Asian Stock Exchanges (FEAS) and the World Federation of Exchanges (WFE) in 1995 and 1994, respectively. Foreign investments in TSE are divided into indirect investments (Foreign Portfolio Investment) and direct investments (participation in management of the company). Both types of foreign investors need to comply with specific regulations. For indirect investments, investors should comply with the regulation on Paragraph C, Article 15 of the fourth Economic, Social, and Cultural Development Plan of the Islamic Republic of Iran (Annex.1). Direct Foreign Investments are regulated by the Organization for Investment, Economic and Technical Assistance of Iran (OIETAI) (http://www.iranbourse.com).

Until recently there were no financial reporting nor national accounting standards in Iran, although prior to 1979 financial reporting was influenced by Anglo-Saxon practices (Mirshekary & Saudagaran 2005). Disclosure requirements were based on tax law, corporate law, and stock exchange regulations, of which tax law requires firms to prepare a balance sheet, income statement and a list of shareholders (Mashayekhi & Mashayekh 2008). The regulatory framework governing the preparation of corporate annual reports in Iran is as follows.

The Accounting Profession and Accounting Standards

Accounting standards in Iran are pronounced by the Iranian Audit Organisation (www.audit.org.ir). The organisation is financially independent but affiliated to the Ministry of Economic Affairs and Finance.[i] These accounting standards have been adapted from the International Financial Reporting Standards (IFRS) since 1997, and are modified taking Iranian taxation rules and customs into consideration.

Iranian accounting standards are framed by the Accounting Standards Setting Committee of the Audit Organisation. The Accounting Standards Setting Committee has nine members, and includes five representatives in senior management positions and members of the Board of Executive of the Audit Organisation, two representatives from the Iranian Association of Certified Public Accountants (IACPA) (a professional accountancy body), one representative from the Security Exchange Agent Organisation, and one representative from industry.

The Iranian Institute of Certified Accountants (IICA) is another professional accountancy body which was established in 1972. The IICA contributes towards the training and education of accountants and auditors at different levels but is not represented in the Accounting Standards Setting Committee of the Audit Organisation.

Stock Exchange Regulation

The significance of having a stock exchange and capital market in Iran was identified in the 1930s (Mashayekhi & Mashayekh 2008). This led to the formation of the Iranian Stock Exchange, known as the Security Exchange Agent Organisation. The stock exchange requires each company to comply with accounting standards pronounced by the Audit Organisation. The Security Exchange Agent Organisation is a non-governmental institute with legal and financial independence. The organisation is funded by service charges and admission fees collected from companies listed on the exchange together with revenue from other sources. As stated before, the organisation is represented in the accounting standards setting process.

Commercial Code

The first Iranian commercial code was introduced in 1925 and has been amended twice since then. The first amendment occurred in 1932 and the second amendment occurred in 1968. The code is limited to minimum accounting and disclosure provisions. For example, Articles 232-242 of the code require each company's Board of Directors to prepare a balance sheet and income statement at the end of each fiscal year. These reports should be accompanied by a director's report explaining the company's activities and affairs. The code emphasises consistency in drawing accounts and evaluation methods across different accounting periods. The code is very limited and provides limited guidance in regard to corporate financial disclosures, measurement and evaluation methods. The code requires mandatory audit of financial statements for joint-stock companies.

The regulations mentioned above relate to the preparation of financial statements. The commercial code mandates the disclosure of a director's report for joint-stock companies, but does not specify the content of this report. Hence, it is voluntary for all Iranian companies to disclose any information in the narrative section of their annual reports. The next section outlines the theoretical framework adopted for the present study.

4. Theoretical Framework

This paper uses stakeholder theory, which is appropriate to the aim of investigating whether the narrative section of Iranian companies' annual reports satisfies the information requirements of financial analysts employed by institutional investors.

The ethical branch of stakeholder theory argues that organisations should treat all stakeholders fairly irrespective of their power. On the other hand, the managerial branch of this theory posits that company management is expected to meet the expectations of those stakeholders who are more powerful than others (Deegan 2006). The managerial branch states that the specific stakeholder group who has greater power differs between organisations. Such power may be related to the control of limited resources, including: finance and labour, access to the media, the ability to take legislative action against the company, or the ability to influence the goods and services consumed by the company (Deegan 2006). The theory has both a descriptive aspect and normative uses. The descriptive aspect explains the present, past or future states of a company's affairs and its stakeholders. On the other hand, normative uses of the theory explain and explore relationships, such as the relationship between stakeholder management and its effect on corporate performance (Donaldson & Preston 1995).

Sternberg (1997) criticises the ethical branch of stakeholder theory, and suggests that by requiring managers to balance the interests of various stakeholder groups, the stakeholder theory may lead managers to violate their obligations to owners who employ them. The author also suggests that because a business is a property of its owners, it is only accountable to them. By arguing that organisations are equally accountable to all stakeholders, the stakeholder theory may lead to organisations not being accountable to anyone.

Following the criticism of Sternberg (1997) the present study adopts the managerial branch of stakeholder theory. A similar view was expressed by Boesso and Kumar (2007), who suggest that companies will only voluntarily communicate those key performance indicators (KPIs) that are required by their principal stakeholders. Our study describes the status of narrative disclosure by Iranian companies and is hence aligned to the descriptive realm of the theory.

Stakeholder theory has been applied by many researchers to explain voluntary disclosure by companies (see Boesso & Kumar 2007; Roberts 1992; Smith, Adhikari & Tondkar 2005; Yongvanich & Guthrie 2005). Boesso and Kumar (2007) adopted stakeholder theory in explaining the drivers of voluntary disclosure by a sample of companies listed on the Milano-Mercato Ordinario (Italy) and the New York Stock Exchange. Boesso and Kumar (2007) also found that the volume and quality of disclosure by these companies was related to the emphasis provided by these companies on stakeholder engagement.

Roberts (1992) investigated whether stakeholder theory could explain corporate social responsibility disclosure, by taking a sample of 130 major companies that were investigated in 1984, 1985 and 1986 by the Council on Economic Priorities (CEP). The author found strong evidence that stakeholder theory is appropriate in empirically analysing corporate social responsibility disclosures.

Qu and Leung (2006) applied stakeholder theory to explain the disclosures by a sample of Chinese companies in their 2003 annual reports' corporate governance disclosures. They found that Chinese listed companies were willing to disclose corporate governance information in addition to that required to be disclosed by Chinese governmental agencies. These companies disclosed information voluntarily to their stakeholders (including shareholders and employees).

Yongvanich and Guthrie (2005) conducted content analysis of annual reports of a sample of Australian mining companies to assess their voluntary disclosure of both intellectual capital and non-economic performance information in 2002. They suggest that Australian mining companies only disclosed some environmental performance indicators, social performance indicators, and information items such as information technology, innovative processes and capacity and willingness-to-act sub-categories. Hence their result provides partial support for stakeholder theory.

Smith, Adhikari and Tondkar (2005) applied stakeholder theory in explaining differences in corporate social disclosure among countries. They conducted content analysis of 1998 and 1999 annual reports of 32 Norwegian/Danish companies and 26 US companies belonging to the electric power generation industry. The authors found that large companies from Norway/Denmark disclosed a higher volume and quality of corporate social information compared to the US companies. They suggest that the reason behind such a disclosure pattern was due to firms belonging to countries which have a strong emphasis on social issues, such as Norway and Denmark, and which also have a stronger stakeholder orientation compared to US companies, which have less emphasis on social issues.

Like previous studies (Boesso & Kumar 2007; Qu & Leung 2006; Roberts 1992; Smith, Adhikari & Tondkar 2005; Yongvanich & Guthrie, 2005), the present study adopts stakeholder theory to investigate whether the narrative section of Iranian companies' annual reports satisfies the information requirements of financial analysts employed by institutional investors.

5. Research Method and Data Analysis

The research method included administering survey questionnaires to a sample of financial analysts in Iran in May-June of 2007 to gain insights into their information requirements from the narrative section of Iranian companies' annual reports.[ii] This questionnaire was first drafted in English and then translated into Persian for distribution. Retranslation of the questionnaire was not performed as two of the authors are conversant in both English and Persian. Annual reports for 2005-2006 of a sample of Iranian companies were examined to gain insight as to whether these annual reports contained those information items that were top-ranked by these financial analysts. We used a checklist approach of the availability/non-availability of the three top-ranked items: present, analytical and prospective information items respectively out of 11 present and analytical information items and 5 prospective information items respectively was adopted. The purpose of concentrating on the top three items required by financial analysts from each of the three information categories is to identify the most valued information items in the narrative section of Iranian companies' annual reports and thus to ensure quality reporting by avoiding information overload. However, a possible limitation of concentrating on the top three information items in all information categories is that while both present and analytical information category contains a total of 11 information items, the prospective information category contains only five information items due to its very nature.

Sample

An invitation to participate in the survey was sent to all institutional investors listed in the Tehran Stock Exchange. Ten institutional investors out of 11 agreed to participate in the survey. The sample of participants consisted of all 60 financial analysts employed by these institutional investors. The top 50 Iranian companies by market capitalisation listed on the Tehran Stock Exchange as of 21st December 2005 were selected to explore whether the narrative section of their reports contained those information items which were top-ranked by the financial analysts. The top 50 companies were selected because larger firms possess the expertise and resources to meet the diverse requirements of stakeholders (Ahmed, 1994). Market capitalisation as being representative of firm size has been adopted widely in previous literature (see Beattie & Jones, 2000; 2001). Only 50 companies were selected because obtaining a ranking for more Iranian companies was not available at the time of the study.

Development of the Questionnaire

All of the items in the questionnaire were adapted from previous studies by Joshi and Abdulla (1994), Stanga (1976), Graham, Cannice and Sayre, (2002), Ho and Wong (2004) and Mozier and Arnold (1984). As reported in previous studies all of these information items were perceived to be significant by various user groups of annual reports such as investment analysts and investors in different countries. Hence, the inclusion of the selected information items in the questionnaire was considered appropriate. Respondents were asked to rank specific information items under each category, such as 'present information,' 'analytical information' and 'prospective information.' For example, the 'present information' contained 11 information items. Respondents ranked these items between '1' and '11,' where '1' referred to the 'most important' information item. Similarly, respondents ranked 'analytical information' items between '1' and '11', and 'prospective information' items between '1' and '5'. The last question of the questionnaire was open-ended to incorporate any other information item(s) that might be considered significant by the respondents, but which was not included on our list. The questionnaire was accompanied by an introductory letter to participants.

Profile of Financial Analysts

Most of the respondents (73%) had more than 5 years experience in investing in equity shares. 69% (35 out of 51) possessed a Master's degree or equivalent, 25% had a Bachelor's degree or equivalent, and 6% had a PhD or equivalent. About 82% (42 out of 51) were qualified in commerce related disciplines, and 59% (30 out of 51) were also associated with a professional accounting body. Of these 30 respondents, 16 were members of the IICA and 14 were members of the IACPA. All respondents considered the narrative section of annual reports to be significant to them in making investment decisions (53% providing very high significance, 39% providing high significance and only 8% providing moderate significance).

Data Analysis

The proportions and ranks allocated by financial analysts to the information items was analysed using statistical frequencies. The pre-specified weight is determined subjectively by the researchers in the absence of any specific guidelines in the literature. However, such arbitrary imposition of 'weight' or 'value/range' to information items is not uncommon in the literature considering the importance of information content (see Morck, Shleifer & Vishny, 1988; Sarkar & Sarkar, 2000; Steiner, 1996). The rationale of using weight is to ensure that all responses are valued properly – i.e. that none of them are omitted in analysing the financial analysts' required top three 'present', 'analytical' and 'prospective' information items. Since the objective is to identify the top three information items under each of the three categories required by the financial analysts (out of 11 present and analytical information items and 5 prospective information items), more weight is allocated to 'rank 1' (0.50) than to 'rank 2' (0.25), 'rank 3' (0.15), and 'rank 4-11' (0.10). Thus, the top three ranks, (i.e. rank 1, 2 and 3) cover 0.90 of the total weight 1. It is reasonable that 'rank 1' receives the highest priority, and then 'rank 2' and so on. Therefore, 50% of the weight is allocated to 'rank 1', 25% to 'rank 2' and 15% to 'rank 3'. It also appears that the weight differences between 'rank 1', 'rank 2' and 'rank 3' range from 40% to 70%. Because of of their lower importance or value, 'rank 4 to 11' (for present and analytical information) and 'rank 4-5' (prospective information), are allocated the minimum weight (10%) as they are outside the domain of targeted top three information items required by the Iranian financial analysts. Most of the information items also received 'rank 0' at varying frequencies indicating their lack of value-adding to the respondent analysts.

Based on the given weight for each 'rank' and the associated frequencies of information items, the numerical value for all of the information items is calculated for all ranks – i.e. 'rank 1-11' for present and analytical information, and 'rank 1-5' for prospective information. The total score is computed by adding the numerical values of all ranks for each item of information. By comparing the total scores within each of the 3 categories of information items, the top 3 information items required by the financial analysts are identified in each information category (Table-II).

6. Results and Discussion

Response Rate

Fifty-one completed questionnaires were received out of 60 which were distributed to financial analysts employed in ten institutional investors. This provided a response rate of

85%. The reason for such a high response rate is that the questionnaires were distributed directly to the participants and collected from them by one of the researchers. Also the consent of the institutional investors (employers) to participate in the study might have affected their employees' (financial analysts) response rate.

Information Requirements of Financial Analysts

Table-I in the Appendix presents rank-wise frequencies of information items from the survey questionnaire. Overall it shows a fairly diverse opinion of the Iranian financial analysts regarding their information needs from the narrative section of company annual reports.

Table-II in the Appendix presents rank-wise values as well as aggregate scores of all of the information items based on pre-specified weights for each ranking. It is significant to note that for 'rank 0' column in Table-I, no weight is provided in Table-II. The total score column in the table clearly identifies the top 3 information items in each information category.

In Table-II, in the 'Present' information category, the total score for individual information items varies from the lowest at 3.45 to the highest at 15.45 while the sum total is 76.9. Similarly, in the 'Analytical' information category the sum total is 75.9 and scores for individual information items vary from the lowest at 1.90 to the highest at 18.10. Finally, the 'Prospective' information category shows the sum total is 55.8 with scores for individual information items ranging from the lowest at 5.45 to the highest at 20.50.

Following the high scores in Table-II, Table 1 below summarises the three top information items under the categories of Present information, Analytical information and Prospective information required by the sample of Iranian financial analysts in the narrative section of company annual reports.

Table 1
Top 3 Information Items required by Iranian Financial Analysts

Information Item	*Top 3 Information Items and Their Total Scores*		
	1	**2**	**3**
Present information:	Proposed dividend (15.45)	Profit after deducting interest and tax (13.90)	Reported cash flow (8.45)
Analytical information:	Earnings growth (18.10)	Return on equity (10.65)	Cash profit per share (8.65)
Prospective information:	Projected earnings for the next fiscal year (20.50)	Cash flow forecast (16.35)	Projected sales for the next fiscal year (7.55)

Disclosure of Required Information by Iranian Companies

Based on the above discussion of the top three information requirements of financial analysts, Table 2 below shows the number of sample companies and their disclosure percentages of the above-mentioned (Table-III) top three information items required by financial analysts. This analysis assesses whether the top ranked information items are adequately disclosed by the sample companies.

Table 2 shows that under the 'Present information' category, about 60% of companies (30 out of 50) disclosed 'proposed dividend', which was ranked first by the respondents. 70% of Iranian companies disclosed 'profit after deducting interest and tax', which was ranked second by the respondents. Only 26% of Iranian companies disclosed 'reported cash flow', which was ranked third by the respondents.

Table 2
Disclosure of Information Items by Iranian Companies

Information Items	*No. of Companies Disclosing Out of 50 Companies*	*Disclosure Percentage*
PRESENT INFORMATION:		
Proposed Dividend	30	60%
Profit after deducting interest and tax	35	70%
Reported cash flow	13	26%
ANALYTICAL INFORMATION:		
Earnings growth	17	34%
Return on equity	19	38%
Cash profit per share	11	22%
PROSPECTIVE INFORMATION:		
Projected earnings for the next fiscal year	48	96%
Cash flow forecast	1	2%
Projected sales for the next fiscal year	48	96%

The number of Iranian companies disclosing the financial analysts' required Analytical information was lower than Present information. 'Return on equity', which was ranked second by the respondents, was disclosed by 38% of companies, followed by 'earnings growth', disclosed by 34% of companies. 'Earnings growth' was ranked the first by respondents. Finally, the third-ranked item 'cash profit per share' was disclosed by 22% of companies. Here 'cash profit per share' refers to net cash inflow per share based on the cash flow statement.

Under the Prospective information category, almost all companies (96%) disclosed 'projected earnings for the next fiscal year', and 'projected sales for the next fiscal year'. 'Projected earnings for the next fiscal year' was ranked first by the respondents, followed by 'Projected sales for the next fiscal year'. However, 'cash flow forecast', which was ranked third by respondents, was only disclosed by one company (2% of the sample companies).

From the above discussion, it is evident that all types of 'cash' related information were not disclosed by the large majority of companies in Iran although such information is highly required by a group of stakeholders (financial analysts). This also indicates that Iranian firms are more aligned to following an 'accrual-based' accounting system and related disclosures rather than a 'cash-based' accounting system and disclosures. Table 2 reveals a consistent pattern of a low disclosure level of cash related information, such as 26%, 22% and 2% for reported cash flow under the 'Present information category', cash profit per share under the 'Analytical information category', and cash flow forecast under 'Prospective information category' respectively. The percentage of companies disclosing 'earnings growth' and 'return on equity' was also low.

A non-parametric correlation test is conducted to find the relation between 'information items required by Iranian financial analysts' and 'disclosure of information items by Iranian companies'. For the former, the 'percentage of weighted value on ranks' is calculated from Table-II. Here, for all category of information items (i.e. present, analytical and prospective), the score of each of the top three information items are valued in percentile form based of the total score of each category of information item (i.e. 76.9, 75.9 and 55.8 respectively). For the latter, the 'percentage of annual report disclosure' is taken directly from Table 2. As reported in Table 3 below, the non-parametric correlation check indicates a non-significant (1-tailed) relation between 'percentage of weighted value on ranks' and 'percentage of annual report disclosure', both in Spearman (correlation coefficient 0.224 with significance level 0.281) and Kendall's Tau_b (correlation coefficient 0.145 with significance level 0.298) correlation tests. These tests are conducted using the SPSS software package. These results support the view expressed above that Iranian companies are only meeting some of the information requirements of financial analysts and hence there is a lack of information disclosure by Iranian companies.

Table 3
Non-parametric Correlation of Information Items between 'Percentage of Weighted Value on Ranks' and 'Percentage of Annual Report Disclosure'

Information Items	*Percentage of Weighted Value on Ranks*	*Percentage of Annual Report Disclosure*
Proposed Dividend	20%	60%
Profit after deducting interest and tax	18%	70%
Reported cash flow	11%	26%
Earnings growth	24%	34%
Return on equity	14%	38%
Cash profit per share	11%	22%
Projected earnings for the next fiscal year	37%	96%
Cash flow forecast	29%	2%
Projected sales for the next fiscal year	14%	96%

Overall, our results provide partial support for stakeholder theory, including a group of stakeholders (i.e. financial analysts) in the sample. In regard to Prospective information, most companies disclosed those information items required by financial analysts, thus providing high support for stakeholder theory (except for a very low disclosure of cash flow forecasts at just 2%). On the other hand, the disclosure of financial analysts' required Present information items provided a mixed result and hence the disclosure pattern of Iranian companies in this regard provides only partial support to stakeholder theory. Finally, most companies did not provide those Analytical information items required by financial analysts and hence this disclosure pattern provides a low level of support for stakeholder theory. From this finding, it can be stated that Iranian companies have partially fulfilled their stakeholders' information needs. Possible reasons for not disclosing such information could be a lack of regulatory enforcement and a lack of incentives for the companies to do so.

7. Conclusions and Direction for Future Research

This paper investigates whether the narrative section of Iranian companies' annual reports satisfies the information requirements of financial analysts employed by institutional investors. The study uses a questionnaire-based survey of these financial analysts to illuminate their specific information needs in the narrative section of company annual reports. A pre-determined weight is applied to each survey response. Then a statistical frequency is used on the information content of each of the three information categories (Present, Analytical and Prospective information) to determine the top three information items required by the financial analysts. This is followed by content analysis of the top 50 Iranian companies' annual reports to examine whether such information is disclosed by these companies. This match-pairing analysis provides an assessment of the relationship between corporate engagement in supplying the required information and the stakeholders' information needs in the Iranian market.

The results show that most of the Iranian companies did not disclose the information items under 'Analytical information', whereas the information items under 'Present information' were disclosed by a greater percentage of the sample companies. Information items under 'Prospective information' are disclosed by most companies except for the cash flow forecast. These findings provide partial support to stakeholder theory. The non-parametric correlation test – Spearman and Kendall's Tau_b correlation check between 'percentage of weighted value on ranks' and 'percentage of annual report disclosure' – also supports this finding, and shows a statistically insignificant relationship. This should neither be encouraged nor continued for the smooth growth of the ailing Iranian economy. Iranian policymakers should adopt greater regulatory change on the disclosure and governance requirements of listed companies to ensure that these companies fulfil the information requirements of stakeholders, and in particular the information needs of financial analysts. This is essential to attract more investment from both national and international investors.

The present research has a number of limitations. Firstly, it is focused on the narrative section of annual reports and considers only the information requirements of one group of stakeholders – financial analysts. Secondly, the study is limited by its sample size, both in regard to the number of survey respondents and the number of companies selected for match pairing. Future studies may also include other groups of stakeholders as well as a larger sample of Iranian companies. Future studies that include the financial statements section of annual reports in addition to the narrative section are also suggested. Another good research topic is investigating whether Iranian companies are aware of their stakeholders' information requirements, and specifically those of financial analysts. Future studies could also concentrate on other ways that Iranian companies communicate with financial analysts (such as private meetings), that may supplement disclosure in their annual reports.

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Appendix

Table I

Frequencies of Information Items from Survey Questionnaire

Information Items	*Frequencies of Ranks Out of 51 Response*				
	Rank 1	**Rank 2**	**Rank 3**	**Rank 4-11 or 4-5**	**Rank 0**
PRESENT INFORMATION:					
Proposed dividend	23	8	5	12	3
Past trend of dividends	3	10	8	26	4
Trends in share prices in last 12 months	0	3	6	36	6
Reserves and surplus	0	0	1	40	10
Reported cash flow	4	9	10	27	1
Reported earnings	4	3	1	14	29
Operating expenses	0	1	2	29	19
Loans and mortgages	0	0	2	45	4
Pre-Interest profit	0	1	4	29	17
Pre-tax profit	0	5	5	36	5
Profit after deducting interest and tax	17	11	7	16	0
ANALYTICAL INFORMATION:					
Dividend payout ratio	2	5	9	29	6
Current market value per share	4	6	4	34	3
Return on equity	6	18	11	15	1
Price-earnings ratio	3	5	11	28	4
Cash profit per share	5	10	9	26	1
Debt equity ratio	0	1	3	38	9
Earnings growth	30	6	4	10	1
Product contribution margin	1	0	0	37	13
Aging of debtors balance	0	0	0	23	28
Geographical source of earnings	0	0	0	44	7
Name(s) of stock exchanges where securities are listed	0	0	0	19	32
PROSPECTIVE INFORMATION:					
Projected earnings for the next fiscal year	31	20	0	0	0
Projected sales for the next fiscal year	1	6	23	21	0
Planned capital expenditures for the next fiscal year	0	0	9	41	1
Planned research and development expenditures for the next fiscal year	0	3	12	34	2
Cash flow forecast	19	22	7	3	0

Table II
Values of Information Items Based on Weights of Ranks

Information Items	*Values Based on Weights of Ranks*				
	RANK 1 (0.50)	**RANK 2 (0.25)**	**RANK 3 (0.15)**	**RANK 4-11 (0.10)**	**TOTAL SCORE**
PRESENT INFORMATION:					
Proposed dividend	11.50	2.00	0.75	1.20	**15.45**
Past trend of dividends	1.50	2.50	1.20	2.60	7.80
Trends in share prices in last 12 months	0	0.75	0.90	3.60	5.25
Reserves and surplus	0	0	0.15	4.00	4.15
Reported cash flow	2.00	2.25	1.50	2.70	**8.45**
Reported earnings	2.00	0.75	0.15	1.40	4.30
Operating expenses	0	0.25	0.30	2.90	3.45
Loans and mortgages	0	0	0.30	4.50	4.80
Pre-Interest profit	0	0.25	0.60	2.90	3.75
Pre-tax profit	0	1.25	0.75	3.60	5.60
Profit after deducting interest and tax	8.50	2.75	1.05	1.60	**13.90**
Total Score					76.9
ANALYTICAL INFORMATION:					
Dividend payout ratio	1.00	1.25	1.35	2.90	6.50
Current market value per share	2.00	1.50	0.60	3.40	7.50
Return on equity	3.00	4.50	1.65	1.50	**10.65**
Price-earnings ratio	1.50	1.25	1.65	2.80	7.20
Cash profit per share	2.50	2.50	1.35	2.60	**8.65**
Debt equity ratio	0	0.25	0.45	3.80	4.50
Earnings growth	15.00	1.50	0.60	1.00	**18.10**
Product contribution margin	0.50	0	0	3.70	4.20
Aging of debtors balance	0	0	0	2.30	2.30
Geographical source of earnings	0	0	0	4.40	4.40
Name(s) of stock exchanges where securities are listed	0	0	0	1.90	1.90
Total Score					75.9
PROSPECTIVE INFORMATION:					
Projected earnings for the next fiscal year	15.50	5.00	0	0	**20.50**
Projected sales for the next fiscal year	0.50	1.50	3.45	2.10	**7.55**
Planned capital expenditures for the next fiscal year	0	0	1.35	4.10	5.45
Planned research and development expenditures for the next fiscal year	0	0.75	1.80	3.40	5.95
Cash flow forecast	9.50	5.50	1.05	0.30	**16.35**
Total Score					55.8

[i] In 2003, in order to comply with Article four (4) of the Third Economics, Social and Cultural Development Plan, the organisation's by-laws were revised and as a result its present legal status is a State Owned Limited Company.
[ii] For the brevity of the paper the questionnaire is not included. It can be obtained on request from the corresponding author.