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Association between firm-specific characteristics and levels of disclosure of financial information of rural banks in the Ashanti region of Ghana

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Abstract

This study was conducted to investigate the influence of firm-specific characteristics which include firm size, profitability, debt equity ratio, liquidity and audit firm size on voluntary disclosure level of rural banks in the Ashanti region of Ghana.

The research was conducted through detailed analysis of the disclosures of the financial statements of the rural banks for the year 2009. Descriptive analysis was performed to provide the background statistics of the variables examined. This was followed by regression analysis which forms the main data analysis. The results indicate that profitability represented by Return on Capital Employed (ROCE) is positively related to the disclosure level, whilst debt equity ratio,

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liquidity, firm size and audit firm size were insignificantly related to the disclosure level.

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1 Introduction

A significant feature of the Ghanaian economy during the past three decades has been the growth of the retail financial services sector. One of the major developments has been the introduction of rural banks t mobilize funds in the communities they operate and to help in the development of the communities they operate.

This study provides evidence on the relationship between firm-specific characteristics and disclosure of financial information by rural banks in the Ashanti Region of Ghana. Several researchers have provided operational definitions of disclosure. Bushman and Smith ([10], p.207) defined disclosure as "firms making available specific information to people outside publicly-traded firms". Dubbink *et al.* [19] on the other hand defined disclosure as the communication of information allowing economic actors to obtain information on a firm's activities and condition.

Financial information disclosure is defined as the release of information concerning the economic performance, position or prospects particularly as measured in monetary terms [21]. These definitions bring to the fore the concept of information asymmetry which has played great roles in the current disclosure debates.

The primary objective of financial reporting is to provide high-quality financial reporting information concerning economic entities useful for economic decision making (IASB, 2008).

The International Accounting Standards (IAS) define the minimum level of disclosure in corporate annual reports expected by regulatory forces and they are stated in distinct sections of each standard and prescribe what information should be presented in the financial statements.

The Institute of Chartered Accountants Ghana (ICAG) requested in 1999 that all companies in Ghana should comply with International Accounting Standards (IAS). With the development of the International Financial Reporting Standards (IFRSs), 2007 was set by the Institute of Chartered Accountant Ghana (ICAG) as the deadline for compliance with the IFRS. Fekete [21] states that IFRS disclosure compliance literature can be considered as part of disclosure research. It is on the basis of this statement and the fact that The Chartered Institute of Chartered Accountants Ghana (ICAG) expects all companies in the country to comply with these regulations that this study is being undertaking to check whether Ghanaian companies are complying with the disclosure requirements of International Accounting Standards 1(IAS 1). IAS 1 requires that an entity whose financial statements comply with IFRSs make an explicit and unreserved statement of such compliance in notes. Financial statements shall not be described as complying with IFRSs unless they comply with all the requirements of IFRSs (including interpretations) (IAS 1.16).

The disclosure of financial information in corporate annual reports and their determinants has attracted considerable attention by researchers in recent years. Despite this concern most of the work have been done in developed economies to the detriment of the less developed ones. A review of the literature on the subject shows that only a handful of work have been carried out in developing countries on the issues of disclosure and its determinants. Some of the researches conducted on determinant factors of disclosure include: Switzerland [40], Hong Kong [45], Japan [12] and France [16]. Therefore, very little is known about the degree of disclosure and corporate attributes influencing it in the less developing economies in West Africa.

Based on extant literature, firm size, liquidity, leverage, auditor size and profitability are predicted to influence the level and quality of these disclosures. This study contributes to the literature on corporate financial reporting in several ways. First it contributes to the corporate governance literature on whether firm-specific characteristics found to be significant in developed economies are similar to those in the rural banks in the Ashanti Region of Ghana.

The next thing is that, the disclosures serve as critical information for the several users of financial statements hence providing factors influencing the disclosure requirements cannot be taken for granted.

Finally, the study enhances the understanding of corporate financial reporting in Ghana as it explores the determinants that help explain voluntary disclosures in Ghana.

Research questions are the bedrock of research hence Bryman and Cramer [9] emphasized the importance of a well formulated research question. They stated that questions which have not been adequately thought out and placed within the proper context of previous research will lead to unsatisfactory outcomes for a study. The research questions for this study are:

1. What is the relationship between firm size, profitability, liquidity, audit firm size and debt ratio and financial information disclosure?
2. To what extent do the above factors affect disclosure levels?

2 Theoretical background and hypotheses development

The first study conducted on disclosures was done by Cerf [12] when he examined 527 corporate annual reports against a disclosure index comprising thirty one information items. He found that level of disclosure was positively associated with corporate size and listing status but not with profitability.

Following closely after Cerf [12], Singhvi [44] also found that disclosure quality was associated with asset size, number of stockholders, rate of return, earnings margin, security price fluctuations, listing status and CPA firm.

Many studies have examined the relationship between firm-specific characteristics and voluntary disclosure level. Naser *et al*. [39], Jensen and Meckling [28], Fama and Jensen [20], Camfferman and Cooke [11], Donnelly and Mulcahy [18], studied the association between company's firm size, debt ratio, owner ship and auditor firm size and the level of disclosure.

Alsaeed [6] argued that firm size, profitability and auditor firm size influence the level of voluntary disclosure.

Other researchers like Meckling (1976) have argued that agency theory provides a framework that link disclosure behaviour to firm-specific characteristics like corporate governance. To them corporate governance mechanisms are introduced to control the agency problem and ensure that managers act in the interests of shareholders.

In theory, the impact of internal governance mechanisms on corporate disclosures may be complementary or substitutive. If it is complementary, agency theory predicts that a greater extent of disclosures is expected since the adoption of more governance mechanisms will strengthen the internal control of companies and provide an "intensive monitoring package" for a firm to reduce opportunistic behaviors and information asymmetry [29].

Managers are not likely to withhold information for their own benefits under such an intensive monitoring environment, which lead to improvement in disclosure comprehensiveness and quality of financial statements [5].

On the contrary, if the relationship is substitutive, companies will not provide more disclosures for more governance mechanisms since one corporate governance mechanism may substitute another one. If information asymmetry in a firm can be reduced because of the existing "internal monitoring packages," the need to install additional governance devices is smaller. These apparently conflicting viewpoints on the impact of corporate governance have not been totally resolved.

According to Bushman and Smith [10] the reduction of information asymmetry following the provision of voluntary accounting disclosures would tend to reduce the related agency and political costs, and lead to lower costs in issuing equity capital [44] and debt [41].

Size;

Studies by Wallace and Naser [47], Raffournier [42], Owusu-Ansah [40] and Alsaeed [2] found a significant relationship between the size of a company and the level of disclosure. The explanations provided by these writers can be summarised as follows:

- It is expected that the media and financial analysts focus more on financial statements of large forms and may consider a low level of disclosure as a signal for hiding bad news. Therefore, such firms would be more motivated to increase the level of disclosure to gain investors' confidence.
- The costs of dissemination of financial information is lower in large firms that have more expertise and financial resources compared with small firms.
- For financing purposes, large firms are more likely to disclose more financial information.

Cooke [13] on the other hand suggests that larger companies, requiring more funding than smaller companies, have a need to raise capital at the lowest cost, and to do this companies will increase their voluntary and compliance with mandated disclosures like is stated in IAS 1.

Based on the above findings the second and third hypotheses state as follows:

H1: There is a significant positive relationship between company`s size and voluntary disclosure level of rural banks in the Ashanti Region of Ghana.

Leverage

Several studies have examined the association between the debt equity ratio and the level of disclosure. These studies found a positive relationship between the debt equity and the level of disclosure. Firms with high debt equity may have more incentives to disclose more financial information to suit the needs of their creditors. Such firms are therefore expected to be monitored more by financial institutions which drive them to disclose more than firms with low debt equity. From the above the following hypothesis will be tested:

H2: There is a significant positive association between debt equity ratio and voluntary disclosure level of rural banks in the Ashanti Region of Ghana.

Profitability:

A positive relationship between profitability and the level of disclosure has been found by a number of studies [25, 45]. These studies found that firms with high profitability would be more motivated to send good news to the market than firms with low profitability. IAS1 requires more disclosure about the source of earnings (e.g. continuing, discontinuing, acquired operations, individually significant items, etc.). The implication is that firms that are not performing well are not likely to voluntarily abide by the requirements of IAS 1. On the other hand firms that are doing well would be inclined to comply with IAS 1, in order to provide evidence of superior managerial ability.

Following from the above studies the following hypotheses would be tested:

H3: There is a significant positive relationship between firm profitability and voluntary disclosure level.

Audit Firm Size:

Several studies have tested the relationship between the size of audit firm and the level of disclosure. Wallace and Naser [47] postulate that bigger accounting firms are "backed by the expertise of the international firms to which they affiliated" and that a "theory of association" exits, suggesting that the contents of annual reports "are not only audited but also influenced by auditors".

However, different results reported by Owusu-Ansah [40] that auditor size is not significant associated with level of disclosure. This leads to the fourth hypotheses of this study:

H4: There is a significant positive relationship between audit firm size and voluntary disclosure level.

Liquidity:

Liquidity refers to a firm's ability to meet its short-term obligations when they fall due. Cooke [13] argued that the soundness of the firm as portrayed by high liquidity is associated with greater disclosure level. Belkaoui and Kahl [8] found no relationship between liquidity and disclosure level, Wallace and Naser [47] on the other hand found a significant negative association between liquidity and disclosure level for unlisted Spanish companies. From the foregoing the following hypothesis can be developed:

H5: There is a significant positive relationship between liquidity of rural bank and voluntary disclosure level.

3 Data and methodology

This section describes the research design of the study including sample description, variable measurement, data collection and empirical model.

In the business of research, a universe or a population represents a group of potential participants relevant to the research project and a sampling frame or a working population is the list of population elements that can be worked with operationally. A sample is a subset or some part of a larger population. The process of sampling, therefore, involves any procedure using a small number of items or parts of the whole population to make conclusions regarding the entire population. The process of sample selection must be aimed at minimizing bias in the sample.

The study is a small scale study which has relatively few respondents. It is therefore, imperative that all respondents are suitable. As the study is restricted to Ashanti region all the 21rural banks qualified to form the population and sample for the study. The sample selected is therefore, purposive and biased to the extent that it includes only rural banks in the Ashanti region. Data were therefore collected from the 2009 annual reports of the 21 rural banks in the sample. In this study, the collection of information and analysis of corporate disclosure is based on content analysis.

3.1 Measurement of the Variables

The dependent variable in this study are, the extent of disclosure made by the rural banks. This variable captures the amount of voluntary disclosures in the annual reports. The study adopted the checklist used by Alsaeed [2]. Only those items from the checklist which were applicable according to IAS1 and Ghana Companies Code were used. A dichotomous scoring scheme was utilized whereby an item is scored 1 if it is disclosed and 0 if otherwise.

The checklist used for the study is shown in Appendix 3 .

The disclosure index can be mathematically shown as follows;

$$EOD = \frac{TD}{M} = \frac{\sum_{i=1}^{m} d_i}{\sum_{i=1}^{n} d_i}$$

where

EOD = Extent of disclosure

TD = Total Disclosure Score

M = Maximum disclosure score for each company

di = Disclosure item i

m = Actual number of relevant disclosure items ($m \leq n$)

n = Number of items expected to be disclosed

Alternatively can be expressed as:

$$EOD = \frac{\text{total number of items disclosed}}{\text{total possible number of items to be disclosed}}$$

where EOD = Extent of voluntary disclosure.

3.2 Independent variables

Based on the related literature reviewed, five independent variables were identified; firm size, debt equity ratio (leverage), profitability, audit firm size and current ratio (liquidity). The selection of these independent variables was based on prior literature on disclosure studies.

The multivariate test used is the standard multiple regression analysis and the regression model is:

$$Y = a + \beta 1\ X1 + \beta 2\ X2 + \beta 3\ X3 + \beta 4\ X4 + \beta 5\ X5 + e$$

Where:

Y = Disclosure index.

a = constant

X1 = Company size (value of net assets).

X2 = Leverage / Debt equity ratio (total liabilities divided by total assets).

X3 = Profitability/ return on equity (net profit divided by equity).

X4 =Liquidity (Cash divided by total assets).

X5 = A dummy variable for audit firm size (audit firm affiliated with international audit firm = 1 and 0 = audit firm with no affiliation with an international audit firm).

e = error term.

In testing the hypotheses SPSS 14.0 was used for data processing purposes. The results and their discussion are based on the outputs generated by the software.

4 Discussion of results

The results of the study are reported and the empirical methods used to examine the research hypotheses of this study are covered in this section.

4.1 Descriptive statistics

Table 1 depicts the dependent variable, Extend of Disclosure (EOD). As one can see the level of disclosure varies closely from 0.5926 (Kwamanman rural bank) to 0.8519 (Atwima Kwanwoma rural bank).

Based on the descriptive analysis as summarised in Table 2 below, the mean value of firm size is ¢1,358,195 with a standard deviation of ¢819,009.62 . This shows that there is little variation in the size across the companies in the sample.

The mean value of profitability (ROCE) is 24.13% which means that the bank's profitability ratio was high because the minimum value is 13% and the maximum is 42.50% . Besides there are small differences between values of profitability ratio because the standard deviation (8.31129) is low.

The mean debt equity ratio is 23.67% with a standard deviation of 23%. It can thus be said that sample banks in this study are lowly levered.

None of the sampled rural banks is being audited by any of the internationally recognised auditing firms like, Pricewaterhouse coopers, and KPMG.

The mean value of disclosure index is 0.71 with a standard deviation of 0.88. The maximum is 0.85 with a minimum of 0.48.

Table 1: Dependent variable values and its components

LIST OF BANKS	Actual	Possible	Disclosure index
Amanano	20	27	0.7407
Kwamanman	16	27	0.5926
Amansie West	22	27	0.8148
Atwima Kwanwoma	23	27	0.8519
Sekyedomase	17	27	0.6296
Juaben	19	27	0.7037
Okomfo Anokye	21	27	0.7778
Adansi	22	27	0.8148
Sekyere	21	27	0.7778
Asokore	18	27	0.6667
Otuasekan	20	27	0.7407
Odotobiri	18	27	0.6667
Akrofuom	19	27	0.7037
Asante Akyem	19	27	0.7037
Bosomtwe	20	27	0.7407
Atwima	17	27	0.6296
Ahafo Ano	18	27	0.6667
Kumawuman	20	27	0.7407
Atwima Mponua	20	27	0.7407
Nsutaman	19	27	0.7037
Nwabiagya	20	27	0.7407

Table 2: Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
RETURN ON CAPITAL EMPLOYED	21	13.00	42.50	24.1362	8.31129
DEBT EQUITY RATIO	21	.01	1.00	.2367	.23001
CURRENT RATIO	21	.20	1.00	.6667	.21802
NET ASSETS	21	136768.0	3316607.	1358195.	819009.62
AUDITOR TYPE	21	.00	.00	.0000	.00000
EXTENT OF DISCLOSURE	21	.4815	.8519	.717810	.0887960
Valid N (list wise)	21				

4.2 Correlation analysis

Before running the regression analysis there was the need to verify the correlation between the variables. Table 3 reports on the Spearman's rho correlation indices for all the test variables. The Spearman's rho is very commonly used by researchers. This has been used because of the small sample size and the Spearman's rho will help in getting a clear result. It has been suggested by Bryman and Cramer [9] that Spearman's rho is a powerful non-parametric method dealing with data, which means they can be used in a wide variety of contexts since they make fewer assumptions about variables.

The analysis shows that current ratio has a significant relationship with debt equity ratio at 5% level (p=0.016). The other variables do not seem to have relationship among each other. This results indicate the need to pay attention to possible multi-colinearity problem in the regression analysis.

4.3 Regression analysis

A regression analysis was performed on the dependent and independent variables to check on the existence of the multi-colinearity problem. In a multiple regression model, multicollinearity exists when two independent variables are perfectly correlated with each other. The result is shown in the Table 4 below.

The variable inflation factor (VIF) in excess of 10 should be considered an indication of harmful multi-colinearity according to Neter et al. (1989). All the VIF are less than 10 and the average VIF is 1.185 therefore it can be said that there is no multi-colinearity problem for the model. The results of the regression analysis can therefore be interpreted with a greater degree of confidence.

The Durbin-Watson value of 2.038 indicates that the data has no serial correlation or autocorrelation problem.

Table 3: Spearman's rho correlations

		ROCE	DER	CUR	NA	AUD	EOD
ROCE	Correlation Coefficient	1.000	-0.088	0.055	-0.045	0.348	0.143
	Sig. (1-tailed)		0.352	0.407	0.422	0.061	0.001
	N	21	21	21	21	21	21
DER	Correlation Coefficient	-0.088	1.000	0.469*	-0.225	-0.107	-0.143
	Sig. (1-tailed)	0.352		0.016	0.163	0.321	0.268
	N	21	21	21	21	21	21
CUR	Correlation Coefficient	0.055	0.469*	1.000	-0.189	-0.067	0.256
	Sig. (1-tailed)	0.407	0.016		0.206	0.386	0.132
	N	21	21	21	21	21	21
NA	Correlation Coefficient	-0.045	-0.225	-0.189	1.000	0.161	0.047
	Sig. (1-tailed)	0.422	0.163	0.206		0.243	0.420
	N	21	21	21	21	21	21
AUD	Correlation Coefficient	0.348	-0.107	-0.067	0.161	1.000	0.312
	Sig. (1-tailed)	0.061	0.321	0.386	0.243		0.085
	N	21	21	21	21	21	21
EOD	Correlation Coefficient	0.143	-0.143	0.256	0.047	0.312	1
	Sig. (1-tailed)	0.269	0.268	0.132	0.420	0.085	
	N	21	21	21	21	21	21

* Correlation is significant at the 0.05 level (1-tailed).

Results of the multiple regression in Table 4 above, show that the F-ratio is 1.069 ($p=0.416$). The result therefore, statistically supports the significance of the model. The adjusted R^2, the goodness of fit test, for all the regression analysis performed are less than 8% indicating that only 7.7% of the variation in disclosure level of rural banks in Ashanti region is explained by the explanatory variables in the study.

Table 4: Regression results

Variable	B	t-value	sig	VIF
Constant		6.208	0.001	
ROCE	0.042	0.180	0.006	1.023
DER	-0.301	-1.145	0.269	1.285
CUR	0.340	1.263	0.149	1.347
NA	-0.116	-0.478	0.639	1.087

Model Summary	
R	0.372
R^2	0.138
Adjusted R^2	0.77
F value	1.069
Sig	0.416
Durbin - Watson	2.038

Table 5 above reports on the results of the determinable variables on the extent of disclosure. The only variable having acceptable correlation with the disclosure index is return on capital employed (profitability). The sign of the coefficient (0.006) shows that the higher the profitability, the higher is the disclosure level.

The findings of this study suggests that only profitability represented by return on capital employed is associated on a statistically significant level of disclosure. Therefore only hypothesis 3, *H3: There is a positive relationship between firm profitability and voluntary disclosure level,* is accepted and the others cannot be accepted. The findings is consistent with earlier research by Wallace and Naser [47]; Raffournier [42]; and Alsaeed [2].

The result that firm size, represented by net assets is insignificantly related to disclosure level suggests that bigger rural banks do not disclose more than smaller rural banks. This may be due to the less variation in the size of the rural banks as shown in the descriptive analysis. The findings of this research is inconsistent with other earlier studies, for example, Haniffa and Cooke [25]; Ghazali and Weetman [22] and Al-Shammari [4] have all found positive relationship between firm size and level of voluntary disclosure.

Table 5: The multiple correlation coefficient and the coefficient of determination

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.372(a)	.138	.077	.0921589	2.038

a Predictors: (Constant), RETURN ON CAPITAL EMPLOYED

b Dependent Variable: EXTENT OF DISCLOSURE

None of the 21 rural banks were audited by any of the "big 4" audit firms. Thus the variable was not included in the regression analysis. The importance of audit firm size in determining the extent of voluntary disclosure is due to the fact that audit firms that have international exposure, and experience and higher reputation have the power to affect the extent of voluntary disclosure compared to smaller audit firms.

With regards to the debt equity ratio, the study found that there is no significant positive relationship between debt equity ratio and the level of disclosure of rural banks in the Ashanti region of Ghana. This finding is inconsistent with the agency cost theory which argues that leverage imposes some good governance mechanisms which helps to control, conflict of interest between management and debt holders. Ahmed and Courtis [1] found a significant positive relationship between leverage and disclosure levels but this study found otherwise.

4.4 Conclusions

The results of the disclosure level, mean of 71%, indicate that most of the firms listed on the Ghana Stock Exchange did not overwhelmingly comply with the IAS 1 disclosure requirements. Whilst the findings are not encouraging, they are consistent with Street and Gray [45], Barako [7] and Dahawy [15] who found similar results for compliance from companies in many countries.

The key relationships examined are between extent of disclosure and company size, profitability, liquidity, leverage and auditor size. The results of the multiple regression analysis shows that only profitability is associated on a statistically significant level as far as the extent of disclosure is concerned. The results did not provide support for a positive relationship between company size, liquidity, leverage and auditor size. This result is consistent with that of Raffournier [42], Wallace and Naser [47], Alsaeed [2] and Haneh [24].

The research contributes to our understanding in several ways. First this is the first attempt to measure the extent of voluntary disclosure based on rural banks in Ashanti region of Ghana.

It also contributes to the literature on whether the firm characteristics that researchers have found to be significant in developed countries can be applied in a developing country like Ghana. This has been achieved as results are consistent with some of the research conducted in the developed economies.

4.5 Limitations and future research direction

The main limitation of this study is that the findings are based on rural banks in the Ashanti region of Ghana which may limit the generalizability of the results to other rural banks in Ghana. To overcome this shortcoming, a study can be taken on all the rural banks in Ghana. The main explanatory variable, profitability (ROCE) can be considered in further studies. In addition the influence of the reporting year on voluntary disclosure should also be researched into to assess the progress of disclosure levels in the rural banks.

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Appendices

Table 1A: Coefficients (a)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	0.659	0.106		6.208	0.001		
	RETURN ON CAPITAL EMPLOYED	0.000	0.003	0.042	0.180	0.006	0.978	1.023
	DEBT EQUITY RATIO	-0.116	0.102	-0.301	-1.145	0.269	0.778	1.285
	CURRENT RATIO	0.139	0.110	0.340	1.263	0.149	0.742	1.347
	NET ASSETS	-1E-08	2.6E-08	-0.116	-0.478	0.639	0.920	1.087

a Dependent Variable: EXTENT OF DISCLOSURE

Regression of results of selected variables on the disclosure level.

Table 2A: ANOVA(b)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.041	5	.008	1.069	.416(a)
	Residual	.116	15	.008		
	Total	.158	20			

a Predictors: (Constant), AUDITOR TYPE, DEBT EQUITY RATIO, NET ASSETS, RETURN ON CAPITAL EMPLOYED, CURRENT RATIO
b Dependent Variable: EXTENT OF DISCLOSURE

Table 3A: Voluntary disclosure items used adapted from, Alsaeed [2]

No.	Disclosure items
1	Strategic information
2	Brief history of company
3	Information on events affecting future year’s results
4	Basic organisation structure/description of corporate structure
5	Details about the chairman (other than name/title)
6	Picture of board chairman
7	Board directors' names
8	Number of BOD meetings held and date
9	Top management names
10	Chairman's/MD's/directors report
11	Majority shareholders
12	Information statistics for more than two years
13	Information on dividends policy
14	Information on future expansion projects
15	Forecasted profits
16	Competitive environment
17	Information on events affecting current year’s results
18	Market share
19	Statement of corporate goals and objectives
20	Information on social and environmental activities
21	Information on training and workers development
22	Information on risk management committee
23	Information on assets-liability management committee
24	Brief discussion and analysis of financial position
25	Disclosure of accounting standards used for the accounts
26	Graphical presentation of performance indicators
27	Information on donations to charitable organisations