A Review of The Information Disclosure: Discussion
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Abstract. Corporate disclosure has consistently remained a significant subject of interest for both scholars and participants in the capital market. This study aims to conduct a thorough review of the existing body of literature on corporate disclosure and offer insights for prospective directions. In particular, our examination focuses on three key disclosure categories: MD&A (Management Discussion and Analysis), MFs (Financial Statements), and ESG (Environmental, Social, and Governance). The primary emphasis of this paper revolves around delving into the factors that influence disclosure, the determinants driving it, and the resultant economic implications. Concurrently, drawing from prior research, this paper posits that regional disparities could also exert an impact on disclosure outcomes, thereby highlighting potential avenues for further investigation.

Keywords: Disclosure; Information asymmetry; Management Discussion and Analysis; Management earnings forecast; ESG.

1. Introduction

Corporate disclosure is essential to the efficient functioning of capital markets. Generally, companies make two types of disclosures, first type is the mandatory disclosure, which mainly reflected in the financial reports, such as the financial statements, footnotes, management discussions and analyses, and other regulatory filings. In addition, some companies also engage in voluntary communications like management earnings forecasts, earnings conference calls, news websites and other reports. And in addition to the company’s own disclosure, external personnel sometimes also comment or disclose the company’s performance, a common way is by inviting professional financial analysts to make comments on the company’s performance.

In this paper, we review research on mandatory and voluntary disclosure of information by company’s management, summarize the key influencing factors, determinants as well as post-disclosure consequences, and identify areas for future work. Section 2 introduces a classic mandatory disclosure, Management Discussion and Analysis. Management Discussion and Analysis (MD&A) is an important section of financial reports, its objective is to provide and explain the details about the company’s performance for users, especially potential users. It can be said that MD&A is more like a supplementary part of financial statements, and its existence makes financial statements easier to understand. At the same time, compared to financial statements, MD&A also concludes non-financial data so it can convey the new information to users. Research on MD&A has continued for many years, in this paper, we review this research and summarize the key points in them. This section proceeds as follows. First, we introduce the quality of MD&A disclosure. We describe three major factors that influence MD&A disclosure quality: format, language (tone), and outside environment. And second part, we briefly describe the how MD&A disclosures differ in different countries and give some possible reasons for the phenomenon.

In section 3 and 4, we introduce two kinds of voluntary disclosure: Management earnings forecast and ESG disclosures. Just as its name implies, management earnings forecast (MFs) disclosure’s objective is to issue management’s expected earnings and stock price in future. The reason of this disclosure is important is that management can express their attitude by issuing their prediction for the company’s future, so it constitutes an important channel between management and market users, which may lead users keep an optimistic attitude to operating conditions and bring the ascension of the current stock price. In 1995, SEC introduced the Securities Litigation Reform Act to encourage voluntary management forecasting. Until now, although recent years, MFs disclosure becomes more important and used frequently in many companies, in many countries, MFs disclosure is still...
voluntary. Section 3 we first introduce the determinants for management choose voluntary MFs disclosure and then we summarize the consequences of it. Because of the differences in national systems and legal environments, the results of the same voluntary disclosure will also be different in regions. For example, MFs disclosure can also become a kind of mandatory disclosure in some countries, so we would compare different countries’ users’ reaction to MFs disclosure and introduce the potential reason of it. Section 4 ,we choose to review the research on ESG disclosure topic. This is because the demand for non-financial information on corporate social responsibility (ESG) activities has grown rapidly due to the explosion in the topic of sustainable investing. Investors, corporate managers, and regulators are increasingly concerned about corporate social responsibility activities. Over the past decade, a large number of companies have voluntarily disclosed much of this information. Similarly, along with the growth of topics, ESG research has improved significantly over the past 10 years. This section proceeds as follows. First, we summarize two key reasons that would lead managements to choose voluntary disclosure: reduce information asymmetry and maintain corporate reputation. Meanwhile, we emphasized that after the ESG disclosure, not only the positive consequence will be produced, but also is possible that the final consequence may not meet the management's initial expectations. We also summarized the research which analyzed this type of phenomenon. Also, we investigate the user' reaction from different countries to ESG disclosure and we also found that because of the culture and habitat, different countries’ users have various attitudes to ESG.

2. Literature Review

2.1 Management Discussion and Analysis

Management Discussion and Analysis (The latter is referred to as MD&A) is an important section, which can be found in annual report or SEC 10-K filing. MD&A section on the practices of the Securities and Exchange Commission (SEC) have been improving over the years. From the perspective of management, MD&A section provides all relevant information about the company, which contains financial information and non-financial information. In 1980, the first report that contained MD&A section were required in the annual reports of American listed companies. Reviewing the history of MD&A, the research on MD&A is very comprehensive. Some prior research on MD&A are descriptive, they reviewed the history and requirements of MD&A (Bagby et al. 1988). And after that, Gibson & Schroeder (1990) evaluated the difficulty for investors and regulators to understand the contents of MD&A and the concept of ‘readability’ of MD&A disclosure is proposed for the first time. They conclude that the MD&A is more difficult to comprehend than the president's letter. This is because even the MD&A section is mandatory by SEC, however, managers can still decide the contents, so the quality of MD&A is various and cannot be ensured. Since then, most studies have adopted on MD&A disclosure readability concept. The classical research, Cole (1990) first analyzed the format, length, context, and sector information provided in MD&A reports of S&P top 100 companies and concluded that most companies provide forward-looking statements. Generally, the length of MD&A section is longer, that means managers in company are more socially responsible because they are more voluntarily provide information to public, which reduce information asymmetry and build a good reputation to investors. Ben & Belgacem (2018) also agreed this concept and he indicated that the MD&A's textual complexity has a positive relationship with corporate social performance and this kind of companies would have a high ethical standard. In contrast, some research has different view, they argued that the longer and complexity of MD&A section sometimes does not mean that the higher the quality of the disclosure. SEC also comment on this issue, SEC states that some MD&A sections are redundant. In fact, CEO might use repetitive disclosures in annual report and these repetitive disclosures are not uninformative, which lead to decrease the quality of MD&A disclosures. To that point of view, Li (2019) argued that the repetitive disclosures are not totally uninformative, through her analysis, for individual investors, repetitive disclosures can be beneficial in helping them make investment decisions.
In addition to the format of MD&A disclosures, some research also focuses on the sentimental and outside factors which influence the readability and quality of MD&A disclosures. One popular topic now is focusing on the managers’ languages and tones used in MD&A section. For example, Rich et al. (2016) investigated 362 municipal disclosures in government reports then they concluded that positive language in municipal MD&A disclosures is a signal of confidence in financial reporting quality. Meanwhile, Caserio & Trucco (2019) proved that different tones have different means in companies. They found that for companies which have favorable performance, their tone is positive in MD&A section and would be more useful to explain and forecast company’s performance. On the contrary, for unhealthy companies, their tone may still positive, but it is not credible. But research is focused on different type of companies, and most of targeted companies are from financial industry, so we cannot conclude that whether in all type of industries, managers’ tones in MD&A section have same means.

In addition, there is a positive correlation between firm age, firm size, profitability and reporting quality, as older and larger firms want to maintain their reputational legacy and more profitable firms are willing to disclose more information in their reporting (Cohen et al, 2008). And likewise, the external competitive environment will make companies pay more attention to the quality of MD&A disclosure in order to maintain their reputation. Moreover, recent articles have also investigated the quality of MD&A disclosures in developing countries. They also measure the MD&A disclosures situation in developing countries. Ren & Lun (2021) found that the MD&A narratives produced by Chinese companies and American companies have a very different description styles and they inferred that some differences may have arisen from influence in the translation process and different language styles.

2.2 Management earnings forecast

As an important kind of voluntary disclosure, management earnings forecast (The latter is referred to as MFs) is the process that managers use the future and historical data to predict the firm’s future performance. In response to the demand of market (investors, analysts and so on), many firms worldwide now are providing the management earnings forecast disclosure. Comparing to the mandatory disclosure, MFs disclosure is also a critical and important kind of voluntary disclosure, since many researchers have investigated MFs disclosure can increase firms’ market value, which can reduce information asymmetry, cost of capital and periodical litigation risk (Houston & Stocken, 2019). In addition to the short-term effects, MFs disclosure can also bring the long-term benefits, Beyer & Dye (2012) found that through this disclosure, managers can enhance their reputations with investors even if it is an unfavorable information.

Since MFs is a critical voluntary disclosure mechanism, so in which circumstances, managers will choose it? In this part, we will review the key determinants of firms’ choice of voluntary MFs disclosure. In general, we know that voluntary MFs disclosure is in response to market demand. So the market environment seems like a key determinant, here we focus on whether the forecast environment influence managers’ MFs disclosure decision.

We classify the forecast environment into two categories: Macroenvironment and Individual behaviors. The Macroenvironment here include economic, legal, and regulatory environment and because people are also an important part in market, so we also discuss the individual’s behavior influence on MFs disclosure decision. Individual here include investors, stakeholders, and analysts.

First, for economic, legal, and regulatory environment. The consensus from this series of research is that even if MFs disclosure is voluntary, it is still subject to economic, legal, and regulatory influences. As Kim & Wasley (2016) argued that Macroeconomic uncertainty affect the MFs that managers do issue. They concluded that Macroeconomic uncertainty could influence characteristics of the MFs that managers do issue. When the Macroeconomic is highly uncertain, as opposed to issue the good earnings forecast, many firms tend to issue the neutral forecast and the earnings forecast will become more accurate but the frequency of it will decrease. Similarly, David and Matthew (2021) proved that management forecast accuracy increases during the economic downturns. Meanwhile,
due to the global impact of the COVID-19 epidemic, many studies have focused on whether the epidemic will affect the management's earnings forecast disclosure decision after its impact on the economy. Some researchers indicated that when the company's registry region is more severely affected by the COVID-19 pandemic, the company has less willingness to disclose its management earnings forecast and the quality of the disclosure is also unfavorable (Chen et al. 2022; Fu et al. 2022). At the same time, Wang & Zhang (2022) revealed the reasons behind it. The article indicates that the COVID-19 pandemic caused the managerial distraction, which increased management work burden, so the quality of earnings forecast drops accordingly. That’s why the quality of the MFs disclosure is unfavorable and the frequency also decrease.

Meanwhile, different legal and regulatory environment will also influence MFs disclosure decision. Prior research found that in less litigious environment, firms are more willing to issue earnings forecast and their forecast is more precise (Baginski & Kimbrough. 2002). For legal environment, Chan et al. (2007) suggests that in Australia, with changes in legislation, the disclosure of non‐routine management earnings forecasts increased, however, the routine MFs disclosure was not changed. So the researchers concluded that the change in legislation will only have an impact on the disclosure of bad news.

Second, other determinants also have the effects on firms’ MFs disclosure decision are what we called individual behavior indicators (investors, stakeholder, and analysts). What we mean here is that these people’s behavior has significant influence on MFs disclosure decision, so we name these people’s influence as Microenvironmental indicators. Prior research has already confirmed that investors, stakeholders, and analysts are sensitive to the companies which disclosed forward-looking information (Healy, et al. 1999). Recent research also confirmed this theory, Bozanic et al. (2018) identified that like earnings forecasts, many forward-looking statements generate significant investor and analyst responses.

Since investors are an important participant in the market, many firms will adjust their disclosures by observing investors' reactions. Hutton & Stocken (2009) documented that when a company has an established record of forecasting, investors are more sensitive to its forecasts, no matter good or bad news. This conclusion encourages companies to make prior forecasting disclosures, regardless of whether the disclosed information is good or bad. This conclusion has been supplemented by some recent studies, which suggest that companies should disclose differently in different circumstances. Emett (2019) found that when a company has poor performance, investors will more concentrate on whether the company focuses on the opportunities rather than the challenges in its disclosures because they believe that the company has a confident attitude toward the future. On the contrary, when a company performed well, investors focus more on whether companies tend to seek challenges rather than opportunities. Not only investors, but some research also found that the number of directors also influence the earnings forecast. They documented that if the proportion of outside directors in the management of the company is larger, company’s MFs disclosure will be more frequent and more precise because this type of company is more vulnerable to outside attention.

After our discussion of the determinants of company MFs disclosure choice, we turn our attention to the consequences of the MFs disclosure. Undoubtedly, one of the main purposes for companies to choose voluntary disclosure is to reduce information asymmetry. As a kind of voluntary disclosure, some early classical research has revealed that MFs disclosure reduce the information asymmetry. The researchers document a reduction in bid-ask spreads (a proxy for information asymmetry) as a consequence of providing management earnings forecasts (Coller & Yohn. 1997). Meanwhile, some research also reveals the relation between MFs and the cost of capital through quantitative analysis. Baginski & Rakow (2012) indicated that there is negative association between the quality of management earnings forecasting policy and cost of equity capital and Rakow (2010) detailly documented that less specific forecasts, pessimistic forecasts, and forecasts forecasting current losses are associated with higher levels of the cost of equity capital, while more timely forecasts and more informative forecasts are associated with lower levels of the cost of equity capital.
2.3 ESG (Environmental, Social, Governance)

In addition to MFs, some companies also use ESG disclosures. The full spelling of ESG is Environmental, Social, Governance. Since ESG was first proposed in 2004, although the US SEC has never required ESG as a mandatory disclosure part in firms’ annual report, from the current development trend, many enterprises regard ESG disclosure as an important part of the company's management strategy, and more pursue the quality of ESG disclosure.

The first thing we want to talk about is what are the key factors that would lead a company to make a voluntary disclosure? The first key factor is reducing information asymmetry. Cheng et al. (2006) proved that there is negative relation between voluntary disclosure and proxies of information asymmetry. That means higher levels of voluntary disclosure will reduce information asymmetry, and information asymmetry often makes it difficult for potential investors to discern the value of firms, which result in stock "underpricing". Also, other research found that disclosure also reduces the risk bearing capacity available through market makers (Diamond & Verrecchia. 1991). Therefore, firms are willing to choose voluntary disclosure to reduce information asymmetry and access a number of benefits.

As a kind of voluntary disclosure, ESG disclosure is supported by current literature. One key determinant of ESG disclosure in companies is to reduce information asymmetry. Cho & Pfeiffer (2013) investigated whether the CSR disclosure will reduce information asymmetry and they found that no matter the performance of CSR is positive and negative, there is a negative relation between CSR performance and information asymmetry. Moreover, Kim & Park (2023) once again proved that ESG performance reduced information asymmetry through quantitative analysis of a large set of US companies, which enhance the information credibility of ESG performance. However, some article argued that inappropriate ESG disclosure cannot reduce the information asymmetry. Although the initial purpose of the company's choice of ESG disclosure is to reduce information asymmetry, Hassani & Bahini (2022) believed that different companies should have different levels of ESG disclosure, otherwise it may be counterproductive.

Another key factor is firms’ reputation. Maintaining the company's reputation is an important long-term strategic plan of the company. Good company reputation can bring many potential benefits to the company.

Some research documented that when high-profile CSR misdeeds occur, companies that have previously disclosed CSR information suffer less negative stock price reaction than those that have not (Christensen. 2016). And Christensen et al. (2021) proved that CSR reporting may provide a kind of "insurance" in advance in case something goes wrong later. Moreover, some articles also have once again enhanced the credibility of this theory through the latest COVID-19 pandemic. Moalla & Dammak (2023) found that companies with high ESG performance have lower stock price volatility than companies with poor ESG performance during COVID-19 pandemic. Therefore, based on these studies, it would be better for companies to promote ESG disclosure, in order to avoid the unexpected risks and improve the corporate sustainability. However, some researchers claimed that not all companies need to promote ESG disclosure. They found evidence from pulp and paper companies, investors value the environmental capital disclosures of low polluters over those of high polluters because the spending of low polluters generates "green goodwill". That means even the high polluters have voluntarily disclosed their negative ESG performance, companies cannot expect investors have a strong reaction and they also need to bear the cost of disclosure.

Next, we examine the effects of ESG disclosure on companies. First, we talked about the positive effect. Many articles claimed that the ESG disclosure can affect firm values. ESG disclosure level has a positive association with firm value and ESG strengths increase firm value with the moderating effect of green innovation and weaknesses reduce it. And recent studies also investigated the effect of ESG disclosure in Chinese market. Cheng et al. (2023) use the Chinese datasets to investigate the effect of ESG disclosure on firm value after the COVID-19 pandemic. The evidence showed that disclosing ESG-related information significantly increases firm value. However, they also pointed
out that this result might only happen after the COVID-19 pandemic, so the result is not representative.

Second, we talked about the negative effect or no effect. Even though we have many articles have proved that the ESG disclosure has relations with firm value, but some researchers argue that it may not have an expected positive effect on firms. Christensen et al. (2022) indicated that greater ESG disclosure appears to lead to greater ESG rating disagreement, which may threaten to dampen confidence in ESG ratings. Tahani & Muhammad (2022) investigated the ESG disclosure effect in Europe instead of America, their result shows that the ESG disclosure indeed has a positive relation with firm value, however, European investors may be more concerned with a company's financial performance and economic outlook than with environmental initiatives. So in fact, ESG disclosure didn't have any positive impact on firm.

3. Conclusion

In this study, we conclude three types of disclosure: Management Discussion and Analysis, Management earnings forecast and ESG. First, MD&A disclosure is a form of mandatory disclosure that provides information about the company performance to supplement or explain the figures in the financial statements. As an early disclosure, prior research has delved into it and has documented the factors that influence the quality of MD&A disclosure. Our study classifies these factors into three categories: Textual, sentimental, and outside factors. For textual factors, we found that existing studies have different views about the length of MD&A section. And for sentimental factors, we confirmed that the language and tone used in MD&A section can indicate managers’ attitude towards financial statements. Also the firm size, firm age, profitability, competitive environment can also affect the quality of MD&A. Given the diversity of the research subjects, we suggest that future research might consider using more granular measures.

Moreover, in recent decades, global markets have increasingly valued non-financial information, so they pay more attention to the company’s voluntary. We conclude two types of voluntary disclosure in our study. For management earnings forecast (MFs), prior research has documented the determinants of MFs disclosure, the consequences of that disclosure, and the impacts of disclosure on firm. For determinants, we consider 2 main factors will influence managers’ decision. One is Macroevironment and another is individual behavior. The common opinion is that when the Macroevironment is bad or market participants have a strong desire for the information, managers are more likely and willing to issue more accurate MFs. Meanwhile, for the consequence of issuing MFs, much research found that MFs can effectively reduce information asymmetry and reduce cost of capital.

The final type of disclosure is the ESG. Recent years, ESG research has become very popular, which follow the growing awareness of the importance of ESG activities to corporate sustainability. We concern on two major determinants of ESG disclosure: reducing information asymmetry and maintaining firms’ reputation. Because ESG is a voluntary disclosure, under some circumstances, companies may need to enhance the credibility of performance information to attract and keep more investors. So here ESG disclosure is more like a supplement and investors can be more supportive of the company through ESG disclosure. However, for the ESG consequence, different research has different opinions. Someone pointed out that issuing MFs disclosure is not a "panacea" and sometimes it may increase the cost burden of company.

In summary, We believe that corporate disclosure will continue to be a rich field of empirical enquiry. Our paper mainly contributes to the literature on three types of disclosure and the determinants of management earnings forecasts and ESG. In this paper, we also emphasize investors’ reactions to disclosure in different countries. And based on this point, we suggest future research can take more account of the impact of regional differences on disclosure. Meanwhile, our paper also contains some limitations, like when we view MFs, in order to avoid confusion, we just follow SEC regulations and directly classify MFs into voluntary disclosure section.
References


