

Does Financial Crisis Affect Good and Bad News Disclosure?

Abstract

The objective of this paper is to examine the impact of financial crisis on financial reporting of good news and bad news in the UK annual report narrative sections. We use the manual content analysis to measure levels of good news and bad news information for a sample of 110 chairman statements of financial institutions. Our sample covers a five year period (2006–2010), which represents the global financial crisis year (2008), two years before the crisis and two years after the crisis. Our regression analysis shows that UK financial companies disclose more good news information than bad news information. We also find that the crisis affects the financial reporting of good news and bad news. These results suggest that after controlling for other firm characteristics and corporate governance mechanisms, UK financial companies disclose more bad news information during and after the crisis period, while they disclose less good news during these periods.

1. INTRODUCTION

The 2008 Global Financial Crisis, hereafter abbreviated to (the crisis), is argued to have an impact on global economy that could be worse than the Great Depression of the 1930s (Eichengreen and O'Rourke, 2009). The crisis that started in the USA resulted in the collapse of large financial institutions such as Lehman Brothers. The failures in these institutions led to freezing in global credit markets (Erkens et al., 2012). Governments around the world were forced to have rescue packages for bailing out financial systems, especially for sectors that are affected directly by the crisis; such as: banks, financial services, insurance companies and real estate investment trusts (REIT).

In October 2008, the British government announced a bank rescue package on loans and guarantees totalling £500 billion, because of the implications of the crisis (Erkens et al., 2012). Northern Rock's failure was evidence that British banks were also affected by the crisis (Kirkpatrick, 2009). The crisis also affected stock markets in the UK, Swaine (2008) contended that the FTSE index experienced two falls in 29th September and 8th October 2008, that were considered amongst the worst FTSE falls in history.

Additionally, the crisis resulted in losing thousands of jobs and led to a credit squeeze in the UK. It has also had an impact on the UK's industries and services, which was estimated to be highly damaging (House of Commons, 2009).

In a recent paper, Keusch et al. (2012, p.623) found that "a crisis situation leads to more extensive use of self-serving bias as adverse external economic conditions are used by managers to present themselves in the best possible light". This motivates us to examine the impact of financial crisis on the tone of narrative disclosure in the UK context. Our paper investigates the financial reporting of good news and bad news (hereafter, abbreviated to (good/bad news)) in chairman statements during, pre and after the crisis. We investigate the influence of the crisis on the levels of good/bad news information. We choose these statements because they considered as the most important sources of information for professional users (Bartlett and Chandler, 1997). These statements are also extensively used by investors (Smith and Taffler, 2000), and influence their decisions because these statements have a higher degree of readability (Clatworthy and Jones, 2006).

To date, the chairman statement in the UK context is a voluntary section of the annual report narratives which is "...unaudited and firms can lie, credibility becomes an issue" [Gigler, (1994), p.225]. Therefore, "...the chairman statement is subject to impression management techniques..." [Clatworthy and Jones, (2006), p.493].

Using a sample of 110 UK chairman statements for the period 2006 – 2010, we contribute to existing disclosure studies by providing evidence that bad news disclosure is positively associated with the crisis suggesting that risky and poor performing financial institutions provided a more negative tone during the crisis. In addition, we find that managers attribute their bad news information to the crisis. Meanwhile, we find that good news information is inversely associated with the crisis. Good news disclosure findings suggest that managers are not using chairman statements to communicate good news information. They might prefer to use a more timely communication channel such as interim reports, press release, conference calls or internet reporting.

The paper is organized as follows: Section 2 reviews the literature and develops the hypothesis. Section 3 presents the research design. Section 4 presents the empirical findings. Section 5 concludes.

2. LITERATURE REVIEW & HYPOTHESIS DEVELOPMENT

Chairman statements are considered amongst the most important information sources for financial reports users and also the most read section in the annual report (Bartlett and Chandler, 1997). These statements have prime positions within annual reports (Clatworthy and Jones, 2003). Based on Arthur Andersen 2001; Beynon et al. (2004) argued that, the chairman statement is considered as one of the most popular forms of narrative disclosure. The importance of narratives disclosure in financial reports is increasing, as a 57% of 100 UK companies' annual report is devoted to accounting narratives comparing to 45% only in 1996.

There are always incentives for managers to disclose information in chairman statements. Clatworthy and Jones (2006) studied the influence of financial performance on chairman statement narratives, particularly whether the financial performance affects companies' strategies disclosure. Their paper studied a sample of 100 chairman statements of profitable and unprofitable UK listed companies. They found that companies' financial performance affects the content of chairman statements as these statements are subject to impression management techniques. They also found that chairman statements focus on the future performance rather than past performance when companies are not profitable. Hence, studying the impact of the crisis on the content of chairman statements might be interesting, because of the popularity of these statements for users.

Impression management literature focuses on financial graphs, photographs and accounting narratives in annual reports. Companies use impression management to attractively present their performance, especially when their performance is bad. However, there is a threat that impression management lead to not producing neutral and unbiased annual reports. 'Recent corporate collapses in the US (such as Enron and WorldCom), which were a combination of fraud (e.g. Rosner, 2003) and impression management (e.g. Davidson et al., 2004) illustrate this point' (Clatworthy and Jones, 2006:494).

Prior research examined the motives of chairmen and the usefulness of the information disclosed in chairman statements. Clatworthy and Jones (2003:183) found that '...Management therefore uses the chairman statement to place a positive emphasis on financial performance and

attempts to deflect attention away from their responsibility for poor financial results'. As chairman statements are unaudited, but auditors only insure the consistency with financial results, therefore 'this issue is worthy of future regulatory attention' (Clatworthy and Jones, 2003:183). They also examined the effects of companies' performance on the good/bad news disclosure in chairman statements. They found that companies prefer to emphasize positive performance by accounting narratives disclosure, as companies want to benefit from good news disclosure, while blaming the outside environment in bad news narratives.

Clarke (1993) analysed accounting narratives in chairman statements of 32 investment companies, and found clear inferences between chairman statements and the investment companies' mission. Schleicher and Walker (2010) measured the tone of forward- looking narratives by manually reading the narratives in the outlook section, the 'meaning-orientated' content analysis approach. They found that the larger impending performance the more decline that bias the tone in the outlook section. In addition, firms' forecast tone are more positive when firms make loss or more risky. Meanwhile, firms forecast are more negative when earnings decline. Smith and Taffler (2000) used both 'form oriented' objective analysis and 'meaning oriented' subjective analysis, for evaluating the statistical models based on words and themes stated in chairman statements, to explain company's failure. They found an association between the form and the contents of future forecast narratives that disclosed by managements.

The crisis had a gloomy and global impact on markets, which could be worse than the 1930s Great Depression (Eichengreen and O'Rourke, 2009). The crisis is originated in the United States US (Adams, 2012). The US financial markets used to be taken as a model in terms of: well-organized, regulated, good governance and investor protection. It resulted in dramatic collapse of Lehman Brothers, in addition to many US financial institutions (Adams, 2012). Therefore, the US government rescue programme bailed out many institutions during the crisis. Hence, the crisis might influence the content of tone disclosure in chairman statements of affected institutions.

By mid-2008 the crisis was associated by liquidity squeeze (Kirkpatrick, 2009), and had an impact on financial institutions, especially banks, in both the US and Europe, in addition to many other countries (Tandrayen-Ragoobur, 2011). Kirkpatrick (2009) argued that the failure of financial institutions during the crisis could be attributed to the weaknesses and

failures of corporate governance system. The crisis surprised many parties including governments and markets. Adams (2012) argued that the crisis was predicted by few people only, both internal and professional parties such as firms' boards, academics, regulators, financial analysts and financial firms' directors failed in predicting the crisis. Therefore, the crisis could have an impact on good/bad news disclosure in chairman statements of many financial institutions.

Financial markets in the United Kingdom (UK) score high in terms and measures of investor's protection, and could be taken as a model (Adams, 2012). But a £500 billion bank rescue package was announced in loans and guarantees by British government in October 2008, because of the consequences of the crisis (Erkens et al., 2012). Northern Rock ended up becoming nationalised, even though the directors' of Northern Rock acknowledged reading the UK's FSA warnings in early 2007 about liquidity risk (Kirkpatrick, 2009).

The FTSE 100 index had a dramatic fall during the crisis. Adair et al. (2009) stated that '...in the UK the benchmark FTSE 100 index recorded the worst performance since its launch 24 years ago, closing at 4,434.17, down 31.3%...'. The House of Commons report (2009) provided examples for a dramatic falls in the market capitalization: In April 2007, £316.9 billion was the capitalisation amount of the listed nine banks. By 7th April 2008, £245.1 billion only became the market capitalisation of the only listed seven banks, as Bradford & Bingley and Northern Rock had dropped out the FTSE 100 index as a consequence of the crisis. After that in 6th April 2009, the value of the five remaining listed banks under the FTSE 100 banking sector became £138.1 billion only. Therefore, The FTSE 100 index might be appropriate for the current research as the crisis affected the index and many listed financial institutions.

Reinhart and Rogoff (2009) argued that the crisis unfortunately would not be the last financial crisis. They also argued that as financial crises strike markets very often and there are remarkable similarities with past experience from history and from other countries. Studying the impact of the crises on good and bad news disclosure might be an interesting research topic. Our paper contributes to existing disclosure literature by examining the impact of the crisis on the good and bad news disclosure in chairman statements.

Prior literature showed that loss making and risky firms disclose a positive tone when earnings increase, while they disclose a negative tone with earnings decline (Schleicher and Walker, 2010). In addition, the literature showed that companies prefer to use bad news disclosure to blame the external environment, meanwhile emphasise their positive performance by good news disclosure (Clatworthy & Jones, 2003). The crisis could be considered as an instance of an extraordinary environment that carried gloomy expectations to financial markets as per the House of Commons report (2009).

Therefore, the crisis that had a gloomy impact on financial markets might affect the disclosure of good news/bad news information in chairman statements. The current research treats this investigation as a purely empirical question and offers no prior theoretical predictions as to degree to which the crisis affects the disclosure of good/bad news information. Therefore, our main research hypothesis is:

There is an association between financial crisis and the publication of good/bad news information in chairman statement of UK companies.

3. RESEARCH DESIGN

Sample Selection

We focus on a sample of UK listed financial institutions. We choose FTSE 100 index since the highest market capitalization companies are listed under this group. Erkens et al., (2012:389) stated that 'an unprecedented large number of financial institutions collapsed or were bailed out by governments during the global financial crisis'. The banking sector market capitalization in the UK experienced dramatic collapse to become 245.1 billion sterling pounds on 6 April 2008, falling from 316.9 billion sterling pounds on 2 April 2007 (House of Commons, 2009). The number of listed banks also decreased as well as two listed banks, Bradford & Bingley and Northern Rock, dropped out of the index (House of Commons, 2009). Kirkpatrick (2009:4) stated that 'in the UK, there had been a run on Northern Rock, the first in 150 years, ending in the bank being nationalised'. Financial services sector also had difficulties as 'thousands of jobs in the financial services sector have been lost. The full implications of the credit squeeze on the UK's industries and services remains unclear but its impact is likely to be highly damaging' (House of Commons report, 2009:7). The crisis also affected real estate investment trust (REIT) listed companies, by affecting

their investments in both the UK commercial property market and the US real estate residential market. Finally, the investments of the insurance listed companies were affected by the crisis too.

Based on the above, we choose the following financial sectors: banks (IT1), financial services (IT2), life insurance (IT3), non-life insurance (IT4) and real estate investment trust (IT5). We collect a sample of 110 chairman statements to test our research hypothesis for years 2006-2010; the sample included almost all the firms' chairman statements that listed under these industry sectors. The sample period covers five years. We choose the year of the crisis (2008) and two years before and after the crisis.

Finally, the explanatory and control variables data is collected from Thomson One Banker database, while annual reports were downloaded from the companies' websites. The London Stock Exchange website also provided relevant data, such as: industry classifications, companies' websites addresses and fundamental information.

Research Variables and the Model

This paper uses the content analysis approach to identify good/bad news disclosure in chairman statement. We identify the number of good news statements, the number of bad news statements and then we calculate the percentage of bad news to good news information. We use these variables as dependent variables in our regression model.

The crisis gloomy impacts on financial markets might be relevant to this research. The crisis is considered as an instance of an extraordinary environment that carried miserable expectations to financial markets (House of Commons report, 2009). During extraordinary environment, companies prefer to use bad news disclosure to blame the external environment (Clatworthy and Jones, 2003). We consider, therefore, crisis as the main explanatory variable.

We consider a number of control variables. We control for firm size. Kang and Gray (2011:406) argue that 'firm size is perhaps the most consistent corporate-specific characteristic found to be positively associated with the level of voluntary disclosure'. There are several reasons for that positive relationship (Hassan et al., 2006). Large listed financial institutions are required to avoid any agency conflicts by voluntary disclosure (Barako et al., 2006). Therefore in accordance with agency theory, large firms should disclose more information.

Another control variable is profitability. Prior research found that firms' profitability affects disclosure. Agency theory suggested that managers of profitable companies disclose more information to magnify their success and to increase investors' confidence in company's management. In addition, managers might desire to promote positive impressions using management impression techniques to attract many parties such as potential lenders and investors. However, management might disclose less information because of loss or lower profitability, as managers wish to vague such poor performance results (Kun Wang et al., 2008).

We also control for leverage. Leverage is also considered as an incentive for companies to disclose more information as this reduces agency costs (Kang and Gray, 2011). Agency theory suggested that leveraged companies reduce these agency costs by increasing their disclosure, which might satisfy creditors and might reduce the agency conflicts (Barako et al., 2006).

Growth is another incentive for companies to disclose more information to reduce the gap between companies' market value and book value (Kang and Gray, 2011). Therefore, we control for growth opportunity in our model.

We control for dividends and audit quality. Companies' managers that distributed dividends during the crisis supposed to emphasize their performance, liquidity and their managerial abilities to perform well. During the crisis time, firms might not be able to pay dividends for shareholders, and then they might use alternative mechanisms to inform their shareholders about their future prospects. One of these mechanisms is the increase in the level of voluntary disclosure as suggested by signalling theory (Hussainey and Aal-Eisa, 2009). Based on the agency theory, auditors may play a role in improving companies' strategies of financial reporting and in reducing the agency problem. Kun Wang et al. (2008:18) stated that '...the choice of an external auditor can serve as a signal of firm value'.

During the crisis, it seems that corporate governance mechanisms did not sufficiently play the safeguard role against risk. Therefore, risk management systems failed in many financial services institutions (Kirkpatrick, 2009). Since the board approved strategies, it is the board responsibility to monitor implementation and the consequences. The crisis can be attributed to weaknesses and failures in corporate governance according to Kirkpatrick (2009). The agency theory recommends some

incentives for disclosure (Donnelly and Mulcahy, 2008), including: Board size. Based on stakeholder theory, board composition is one of the determinants of disclosure. Empirical research shows that non-executive independent directors advance the board's capacity to improve agency conflict. Since, they play a reliable governance mechanism that would raise the voluntary disclosure in companies' annual reports (Erkens et al., 2012).

Finally, following prior research (Wang and Hussainey, 2013 and Elshandidy et al, 2013), we control for industry type in our regression models.

Table 1 presents a summary of our control variables.

Insert Table 1 about here

Content Analysis:

We use the manual content analysis approach to identify both good news and bad news disclosure in chairman statements. The approach is a subjective analysis that '...focuses on analysis of the underlying themes in the texts under investigation...' (Smith and Taffler, 2000:627).

Hence, applying the manual content analysis involved counting the thematic contents for the meaning oriented. However, the reliability of the manual content analysis became a main concern. And because of the need for user's judgment in counting narratives and in determining conveyed messages, the following dimensions were applied to classify the contents characteristics (Smith and Taffler, 2000):

- a. Evaluative: (positive/negative) and/or (beneficial/adverse).
- b. Potency: (strong/weak) and/or (tangible/intangible).
- c. Activity: (active/passive) and/or (dynamic/static).
- d. Manageability: (expected/unexpected).

The test excludes sentences and paragraphs that disclose any information about: board members welcome and goodbye, any staff changes review, and any congratulation for well done work.

It is relevant to realise that some few disclosures are subjective and required user's judgment to determine messages conveyed. These few sentences are

considered as good and bad news disclosure in same time. As different users' groups, such as: existed investors, potential investors, agencies, clients and customers might find it good news disclosure while others might find it bad news. For instance,

'...there has been a sharp increase in capital market issuance and demand has been weak in the teeth of the recession. As a result we have not achieved our £16 billion net lending target. Even so, we are ready, willing and able to lend, and approved 85% of loan applications during 2009, a rate consistent with previous years.' (RBS Group Annual Report, 2009:3).

The example is considered as good news disclosure because the bank was ready, willing and able to lend. However, it is also considered as bad news because the recession prevents the bank from achieving the targeted lending.

Following Breton and Taffler (2001), Table 2 summarizes the themes' groups. This table shows the classification of the dimensions of the manual content analysis. Some real examples from chairman statements are as follows:

The following example discusses the economy conditions as follows:

'we believe that we are well positioned to benefit from the encouraging signs of economic recovery, albeit we believe the UK economy will grow at below trend levels over the next few years...' (Lloyds Banking Group Annual Report, 2009:7)

The second example discusses the impact of financial crisis as follows:

'2009 has been another difficult year for a number of the major economies in the world and this has continued to impact not just the banking industry, but also our customers and our clients.' (Barclays PLC Annual Report, 2009:7)

In the following examples, financial companies discussed issues related to profitability, growth and the strategic plan as follows:

'Earnings per share improved strongly, rising by 115 per cent to reach US\$0.73 per share.' (HSBC Holdings plc. annual report, 2010:4)

'I can report that Standard Chartered delivered another year of good income and profit growth in 2008...' (Standard Chartered plc annual report, 2008:6)

'In this difficult environment, we missed our profitability targets.' (HSBC Holdings plc. annual report, 2008:9)

'To achieve its objectives, the company needs to change not just the business we do but how we do business.' (RBS Group annual report, 2008:3)

Table 2 shows the classification of the dimensions of the manual content analysis.

Insert Table 2 about here.

Reliability and Validity:

The reliability of the manual content analysis is an essential consideration in all types of researches. This current research uses stability and reproducibility for assessing the reliability of the used content analysis (Krippendorff, 2004).

Stability can be achieved by coding the same chairman statement more than once by the researcher. Therefore, the chairman statement of Barclays plc. 2010 is coded and recoded for this purpose and results show stability.

Reproducibility is another type of reliability assessments. Reproducibility recodes the same chairman statement by more than one researcher to measure the reliability of different researchers' understanding. A random sample of chairman statements was coded by the first and second authors independently. The correlation between the disclosure scores produced by the first author and the second author was quite high (95%) and statistically significant at the 1% level.

In terms of the validity of our disclosure scores, we follow Botosan (1997)'s measure of validity by looking at [1] correlations between components of disclosure; [2] correlations between disclosure and some determinants of

disclosure as suggested by prior literature. We find that there is a positive and statistically significant association between our scores for good news information and bad news information. As reported in Table 4, the correlation between the two classes of information is 18.6% significant at the 5% level. Additionally, each class of information is highly correlated with the bad news-to-good news ratio (correlation between 29.6-55.1%, significant at the 1% level). Finally, as reported in prior research, our disclosure measure is correlated with leverage (the correlation is 17.2%, significant at the 10% level) and board size (the correlation is 21.9%, significant at the 5% level).

The Model

Many prior research suggested the use of ordinary least square (OLS) to examine the determinants of corporate disclosures (e.g. Aljifri and Hussainey, 2007; Francis et al., 2008; Smith and Taffler, 2000; Adams, 2012; Erkens et al., 2012). This research uses the following OLS models:

$$\begin{aligned} \text{Good News Disclosure} &= a + b1 (\text{CRISIS}) + b2 (\text{SIZE}) + b3 (\text{ROE}) + b4 (\text{LEV}) + \\ &b5 (\text{GROWTH}) + b6 (\text{DIV}) + b7 (\text{AUDIT}) + b8 (\text{BOARD}) \\ &+ b9 (\text{COMPOSITION}) + b10 (\text{INDUSTRY}) + e. \end{aligned}$$

$$\begin{aligned} \text{Bad News Disclosure} &= a + b1 (\text{CRISIS}) + b2 (\text{SIZE}) + b3 (\text{ROE}) + b4 (\text{LEV}) + \\ &b5 (\text{GROWTH}) + b6 (\text{DIV}) + b7 (\text{AUDIT}) + b8 (\text{BOARD}) \\ &+ b9 (\text{COMPOSITION}) + b10 (\text{INDUSTRY}) + e. \end{aligned}$$

$$\begin{aligned} \text{Bad to Good News Disclosure} &= a + b1 (\text{CRISIS}) + b2 (\text{SIZE}) + b3 (\text{ROE}) + b4 (\text{LEV}) + \\ &b5 (\text{GROWTH}) + b6 (\text{DIV}) + b7 (\text{AUDIT}) + b8 (\text{BOARD}) \\ &+ b9 (\text{COMPOSITION}) + b10 (\text{INDUSTRY}) + e. \end{aligned}$$

4. EMPIRICAL RESULTS

Descriptive Statistics

Table 3 presents the descriptive statistics. Panel A shows that, on average 11 sentences in the chairman statements contain good news information with a minimum of 1 statement and a maximum of 36 statements. On the other hand, on average about 5 sentences in the chairman statements contain bad news information with a minimum of zero statements and a maximum

of 28 statements. On average, the firm size (SIZE) is about 299,047.2 million, with a minimum of 78.3 million and a maximum of 2,394,570 million. Profitability ratio varies between companies with a maximum ROE of 85.99 and minimum ROE of -77.63. The average ROE is 15.78. The average leverage (LEV) ratio is 15.42, with a minimum of 0 and a maximum of 57.08. The average growth rate is 2.76 with a maximum value of 23.73. The average dividends per share is .18, with a minimum of zero dividend payments and a maximum of .80 dividend payments. Minimum board size in our sample is 5 members, while the maximum board size is 22 members. The average board size is 12 members. The board composition varies between a minimum of 40% non-executive directors and a maximum of 89%, comparing to the average composition ratio which is 66.23%.

Table 3 - panels B present categorical variables, the frequency results show that 60% of the sample chairman statements are published during and after the crisis, while 40% of the sample is before the crisis. Finally, the financial statements of our selected sample firms are audited by one of the big four audit firms.

Insert Table 3 here

Correlation Analysis

Table 4 shows the correlation analysis. As discussed previously, our good news and bad news disclosure scores are positively correlated. Both classes of information are also correlated with the bad-to good news ratio. The table also shows that there is no serious multicollinearity problem between independent variables as the correlations between these variables are less than 70%.

The VIF results reported in Tables 5, 6 and 7 show that all independent variables are smaller than 4, results support that there are no multicollinearity between the independent variables (Akhtaruddin et al., 2009).

Insert Table 4 here

Empirical Findings

The first regression shows that there is an inversely association between the good news disclosure and the crisis which is significantly different from zero, and results suggest not to reject the main hypothesis. The second regression analysis shows that bad news disclosure in chairman statements is positively associated with the crisis. The third regression results show that, the crisis is significant explanatory variable with positive association, which suggest not rejecting the crisis main hypothesis.

Table 5 shows the findings for the first regression model which, proposes that good news disclosure in chairman statement is the only explained variable. While the control variable (industry type) is excluded in panel A, it is included in panel B. The CRISIS dummy variable is our variable of interest. The dummy variable AUDIT is omitted as the entire sample has assigned the big four audit firms.

Panels A and B show that the crisis variable is significantly different from zero which suggest not to reject the main hypothesis; results also show that there are an inversely association between the good news disclosure and the crisis. The crisis variable results are consistent with prior research (e.g. Schleicher and Walker, 2010; Clatworthy and Jones, 2003); as there is association between good news disclosure in chairman statements and the crisis impacts. The findings for firm size are consistent with prior researches and the agency theory (Kang and Gray, 2011) as smaller firms rely on chairman statements more than bigger firms which uses other channels for good news disclosure. The dividends variable results are consistent with prior research (e.g. Hussainey and Aal-Eisa, 2009) as firms that faced a decline in their dividends during the crisis, might increase the level of disclosure based on disclosure signaling theory. The board size variable results are consistent with prior studies (e.g. Donnelly and Mulcahy, 2008), and are in line with agency theory. Also, the board composition results are consistent with prior studies (e.g. Erkens et al., 2012) and they are in line with the stakeholder theory.

The profitability variable results are inconsistent with both prior research and agency theory; this could be logic as management might rely in these crisis extraordinary circumstances on management impression techniques and other channels to disclose their good news information (such as the increase in profits). The leverage variable results are consistent with some prior studies (e.g. Aljifri and Hussainey, 2007), but inconsistent with others. The growth ratio variable results are inconsistent with prior studies (e.g. Kang and Gray, 2011), which suggest the high growth companies might use

more timely disclosure channels during the crisis period to signal their performance.

Insert Table 5 here

The second regression analysis considers bad news disclosure as the only explained variable, results are presented in table 6.

In the table, we note that the crisis variable is significantly different from zero. Therefore, bad news disclosure in chairman statements is positively associated with the crisis. Therefore, in the case of bad news disclosure, chairman statements positively increased the bad news narratives because of the crisis. These results are consistent with Clatworthy and Jones (2003) indicating that companies blame the external environment for any bad news. The chairman of the RBS plc., for example, states that: 'Our disappointing financial results reflect these circumstances and our exposure to them...' (RBS Group Annual Report, 2009:2) and 'In recognition of the crisis in global financial services and the unprecedented losses incurred by the RBS Group in 2008...' (RBS Group Annual Report, 2009:3). As reported in Table 5, we find a relationship between bad news disclosure in chairman statements and the financial crisis. We also find, firms that faced decline in their dividends during the crisis, might increase the level of disclosure in accordance with disclosure signaling theory (Hussainey and Aal-Eisa, 2009). However, companies' managements prefer not to disclose bad news in chairman statement if these narratives have negatively effects.

Insert Table 6 here

Table 7 presents the last regression analysis results considering the bad news to good news disclosure percentage as a dependent variable.

Both results in panels A and B confirm that, the crisis is significant explanatory variable with positive association. Hence, our results suggest not rejecting the crisis main hypothesis, which is supported by Clatworthy and Jones (2003) that external environment are being blamed for any bad news. This third regression analysis is considered as a sensitivity analysis, as results confirmed the second regression. The crisis variable results are consistent with prior researches (e.g. Schleicher and Walker, 2010; Clatworthy and Jones, 2003); these results confirm the consistency of the

crisis variable with bad news disclosure in accordance with signalling theory. Also, all other variables results are insignificant confirming the fact that managements do not use chairman statements to disclose bad figures.

Insert Table 7 here

Discussion

Our paper examines incentives for good/bad news disclosure in chairman statements during the crisis. Results show an association between the crisis and good/bad news disclosure in chairman statements. The first regression shows an inverse association between the crisis and good news narratives in chairman statements. The second and the third regressions show a positive association between the crisis and bad news narratives in chairman statements. All these results suggest that risky and poor performing financial institutions provide more negative tone during the crisis, which is consistent with Schleicher and Walker (2010) findings.

Also results show that, firms' managements prefer to blame the crisis, as an external extraordinary environment, for any bad news (Clatworthy and Jones, 2003). For example: In the HSBC annual report it is argued that:

'2008 was the most extraordinary year for the global economy and financial services in well over half a century. It marked the first crisis of the era of globalised securitisation...' (HSBC Group plc. annual Report and accounts, 2008:8).

Further examples support our findings as follows: In the 2007 RBS plc. chairman statement, it is stated that:

'RBS enjoyed another successful year in 2007...despite some of the most challenging market conditions in the financial and credit markets for some time. The hard work of our employees allowed us to deliver a strong financial and operational performance...' (RBS plc. annual reports and accounts, 2007:8)

In the following year, we noted in the 2008 RBS Plc's chairman statement that the chairman argued:

'...an exceptionally difficult period in the history of The Royal Bank of Scotland Group... Our disappointing financial results reflect these circumstances and our exposure to them... In recognition of the crisis in global financial services and the unprecedented losses incurred by the RBS

Group in 2008... We recognise that our reputation has been damaged by the events of the last year'. (RBS plc. annual report and accounts, 2008:2).

So what if the crisis influences the good/bad news disclosure in the popular chairman statement? This would suggest that as chairman statements are unaudited and firms could lie, managements would benefit from using impression management techniques. For instance, it is stated that:

'We at HSBC were not immune from the crisis. But we have built our business on very strong foundations and are able to report results which demonstrate our ability to withstand the storm' (HSBC Group plc. annual report and accounts, 2008:8).

Also, the crisis might motivate corporate management to overly blame the external environments in order to distort users' perceptions towards management actual performance; particularly, these risky and poor performing financial institutions that provided a more negative tone during the crisis. For example, it is stated in one of the chairman statements that:

'... Our combination of clear strategic goals and a commitment to continuous operational improvement positions us well in a changing environment...we believe our business is robust, capable of generating sustained profitable growth and value, and increasingly well positioned competitively for the future'. (Legal & General Group plc. annual report and accounts, 2007:5).

However, Legal and General Group plc. reported in the next year statement that:

'The credit crisis and its consequences ... It has had a heavy impact on our share price and on your returns... Total Shareholder Return (TSR) for 2008 was negative 38% (2007: negative 14%). This reflects a fall of 31% in the FTSE All-Share Index and a decline of 40% for the life insurance sector during the year'. (Legal & General Group plc. annual report and accounts, 2008:4).

It also worth noting that, many of good performing firms would emphasise their management performance by referring to their ability to perform well while working in a difficult financial environment using chairman

statements, which could be considered as cheap talk. For example, British Land plc. stated that:

'What a difference a year makes! A year ago, real estate markets were close to all-time highs...Today, doom and gloom is widespread and fears of the impact of the global 'credit crunch' are not yet receding...While it is true that the current down-cycle has been unusually fast and severe in its effects... It's a time for cool heads, long-term clarity, a robust business model and 'business as usual' for our management team' (British Land plc. annual report and accounts, 2008:6)

In the following year, British Land plc. stated that:

'...we have felt the impact of a global recession...In the year to March 2009 our portfolio declined 28% in value. Taking the Rights Issue into account, this valuation reduction took our net asset value down from 1114 pence to 398 pence per share'. (British Land PLC Annual Report and accounts, 2009:6).

On contrary, large firms use alternative channels to communicate with financial reports users.

5. CONCLUSIONS

This paper examines the impact of financial crisis on corporate disclosure of good and bad news narratives in chairman statements. By analysing the contents of 110 UK chairman statements to identify levels of good and bad news information. For the period that covers 5 years (2006-2010).

The study results suggest that the crisis is considered as significant incentive for good/bad news disclosure in chairman statement. The crisis is associated inversely with good news disclosure in chairman statement. A possible explanation is that financial institutions disclosed good news using other reporting channels than chairman statements. While the crisis is positively associated with bad news disclosure, as there is an increase in bad news narratives in the sample chairman statements. In addition, results show that risky and poor performing financial institutions in the sample provided a more negative tone during the crisis.

The results of good and bad news disclosure in chairman statement attributable to the crisis are reasonably justified on the grounds that many

accounting narratives in the sample blamed and declared the impact of the crisis. For instance: (HSBC Holdings plc. annual report, 2008:8) in chairman statement section stated that '2008 was the most extraordinary year for the global economy and financial services in well over half a century. It marked the first crisis of the era of globalised securitisation'. It is possible that, some chairman statements increased bad news accounting narratives blaming the crisis as external environmental factor for any bad financial performance. Moreover, findings also suggest that management emphasised their managerial performance by disclosing good/bad news narratives in the chairman statement, by referring to their ability to perform well while working in a difficult financial environment, such as the crisis; possibly using impression management techniques.

What if any of the users of annual reports relies on chairman statement for taking investing or financing decisions during the crisis? We are afraid that users might be misled; such as relating bad performance to the crisis not to company's management. This leads to taking wrong decisions that cost users big losses. Moreover, this highlight on the usefulness of relying on accounting narratives in chairman statement when taking decisions under the impact of extraordinary crisis, which could affects whether the good/bad news narratives reflect or do not reflect fairly and reliably the truth about the financial position of firms and their management performance.

What is the impact upon society? Evidences of any influence of the crisis on good/bad news narratives in chairman statement will help users to carefully consider our paper findings when using chairman statement during extraordinary crisis for taking decisions. Also, these evidences would encourage and enhance managements, auditors and other parties to disclose and monitor the chairman's narratives in annual reports carefully. Then the more reliable chairman statements, the better improvement in the usefulness of accounting narratives and information, which leads to better ability to take good decisions, and avoid losses as a result of misleading narratives. Consequently, the society will benefit from better business environment. In conclusion, reliable information is power.

These findings are prominently interesting for the users of chairman statements, and other members in the society, as these statements are considered as a popular source of information for annual reports users. The paper findings highlight on the usefulness of issues using accounting narratives in chairman statement during extraordinary business environment, such as the crisis. The research findings open up another

potentially interesting point for research. Given that these extraordinary circumstances might motivate corporate management to overly blame the external environments in order to distort users' perceptions towards management actual performance. In turn, analysis of impression management techniques within the chairman statement would reveal interesting insights that benefit managements, not users or the society; which is an issue that might be considered as a fruitful research topic for further studies in the future that find out how to prevent misusing good/bad news narratives in chairman statements to improve their reliability

There are still some limitations in this research. Firstly, the use of manual content analysis for collecting good/bad news narratives in chairman statement is possibly subjective. So it is recommended to apply a mix of qualitative and quantitative methodologies for measuring the good/bad news disclosure in chairman statements, such as: manual and computerized content analysis, surveys, interviews and multiple OLS regression analyses.

Secondly, the sample included only 110 chairman statements from the FTSE 100; hence results might not be generalized. In the future, a cross-country large sample drawn from countries heavily exposed to the crisis. A sample of more than 250 firms would be chosen from about 25 countries, which were at the center of the crisis, including UK and European Countries. That sample could ensure more reliable and generalizable outcomes (i.e. the larger the sample, the better reliable results). Finally, to identify disclosure scores for good and bad news information for a large sample of companies over longer time periods, we suggest that researchers should consider using computer-based content analysis (i.e, NVivo Software) to count the number of good and bad news sentences, This requires the creation of a reliable keyword lists that covers both good news and bad news information.

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Tables

Table 1 presents a summary of the used explanatory variables.

Variable		Measurement	Source
Crisis	CRISIS	1=If year 2008, 2009, 2010; 0=If year 2006, 2007.	-

Firm Size Profitability Leverage Growth Dividends	SIZE ROE LEV GROWTH DIV	Log total assets. ROE, the return on equity ratio. Debt to total assets. Price-to-book value ratio (PBR). Dividend per share.	Thomson One Banker
Auditor reputation Board Size Composition	AUDIT BOARD COMPOSITION	1=If auditor is Big4; 0=If not. The total members of the Board. Non-Executive managers to the Board percentage.	Annual Reports
Industry type	INDUSTRY	IT1 to IT5 for representing the sectors under FTSE 100.	Londonstock-exchange.com

Table 2 Classification of the dimensions of the manual content analysis

The Dimension Of Content Analysis	Good News Disclosure	Bad News Disclosure
Market Conditions & Expectations	<ul style="list-style-type: none"> - Increase in markets activities. - Stable or active economy. - Positive fundamentals. - Future positive expectations in the market. 	<ul style="list-style-type: none"> - Decrease in markets activities. - Unstable or inactive economy. - Not positive fundamentals. - Future negative, uncertainty or gloomy expectations in the market.
Impact of the Crisis	<ul style="list-style-type: none"> - Not effected by the crisis. - Even though the crisis, achieved good results. 	<ul style="list-style-type: none"> - Effected by the crisis. - Because of the crisis, achieved bad & negative results.

Profitability	<ul style="list-style-type: none"> - Increase in profitability figures. - Achieving or exceeding the targeted profitability. - Positive results, returns, profits and earnings. 	<ul style="list-style-type: none"> - Decrease in profitability figures. - Increase in profitability figures, but not achieving the target. - Losses, costs and negative results.
Growth	<ul style="list-style-type: none"> - Growth achievements in several activities. - Additions, developments, acquisitions and investments. 	<ul style="list-style-type: none"> - Non growth in several activities. - Negative figures for activities. - Disposals.
Financial Position	<ul style="list-style-type: none"> - Strong financial position. - Stable financial position. - Better gearing, capital, liquidity and dividends. 	<ul style="list-style-type: none"> - Weak financial position. - Unstable financial position. - Financial support was needed. - Not good positions as per: gearing, capital, liquidity and dividends.
Strategic Disclosure	<ul style="list-style-type: none"> - Acquisitions future plans that lead to growths. - Managements, Productivity, Competitive Innovative and developments plans. - Any other positive strategic disclosures. 	<ul style="list-style-type: none"> - Recovery and Restructures plans. - Not achieving planned Acquisitions or expanding plans and projects. - Cancellation of planned projects because of an outsider forces.
<p>Note: Sentences or paragraphs in the chairman statement that disclose the following are excluded:</p> <ol style="list-style-type: none"> 1. New board members welcome and goodbye. 2. Staff changes review. 3. Congratulation for work well done. 		

Table 3 Descriptive statistics

Panel (A) Continuous Variables			
Variable	Mean	Min	Max
GOOD NEWS	11.49	1	36
BAD NEWS	5.27	0	28
SIZE*	299,047.2	78.3	2,394,570
ROE	15.7814	-77.63	85.99
LEV	15.4152	0	57.08
GROWTH	2.7585	.33	23.73
DIV	.1762	0	.80
BOARD	11.78	5	22
COMPOSITION	.6623	.40	.89
Panel (B) Categorical Variables (Frequency)			
Variable	Number		Number
CRISIS	66 after the crisis		44 before the crisis
AUDIT	110 Big4		0 Non Big4

Firm size (total assets) in million. The definitions of the variables are reported in Table 1.

Table 4 Correlation analysis

	Good News	Bad News	Bad-to-Good News	Size	ROE	LEV	RB	DIV	Board	Composition
Good News	1									
Bad News	.186 .056	1								
Bad-to-Good	-.296** .002	.551** .000	1							
SIZE	-.141 .150	.169 .084	.170 .081	1						
ROE	.009 .924	-.475** .000	-.367** .000	-.403** .000	1					
LEV	.172 .083	.283** .004	.032 .748	.194* .046	-.488** .000	1				
GROWTH	-.043 .664	-.279** .004	-.247* .011	-.592** .000	.618** .000	-.397** .000	1			
DIV	.060 .544	-.107 .277	-.097 .324	-.088 .359	.060 .533	.020 .834	.112 .248	1		
BOARD	.219* .024	.184 .059	-.009 .924	.688** .000	-.238* .014	.363** .000	-.408** .000	.216* .025	1	
COMPOSITION	.070 .478	.171 .079	.246* .011	.341** .000	-.164 .091	.041 .675	-.272** .004	.079 .417	.303** .001	1

* indicates that the correlation is significant at the 0.05 level

** indicates that the correlation is significant at the 0.01 level

The definitions of the variables are reported in Table 1.

Table 5 Good news disclosure regression analysis

Variable	Panel A. Good News without Industry Type			Panel B. Good News with Industry Type	
	B	Sig	VIF	B	Sig
Constant	13.285	.016	-	6.229	.440
CRISIS	-3.579	.004	1.178	-3.262	.005
SIZE	-4.491	.000	3.041	-2.673	.057
ROE	-.010	.720	1.976	-.031	.278
LEV	-.001	.973	1.626	-.110	.312
GROWTH	-.290	.173	2.261	-.250	.270
DIV	-8.735	.049	1.339	-12.056	.008
BOARD	1.323	.000	2.816	1.558	.000
COMPOSITION	12.052	.094	1.195	13.698	.055
INDUSTRY TYPE	No			Yes	
	R2	.330		R2	.461
	Adjusted R2	.273		Adjusted R2	.388
	F Value	5.736		F Value	6.345
	Observation	110		Observation	110

The definitions of the variables are reported in Table 1.

Table 6 Bad news disclosure regression analysis

Variable	Panel A. Bad News without Industry Type			Panel B. Bad News with Industry Type	
	B	Sig	VIF	B	Sig
Constant	4.915	.263	-	11.912	.091
CRISIS	2.556	.011	1.178	2.405	.017
SIZE	-.717	.308	3.041	-1.740	.151
ROE	-.084	.000	1.976	-.105	.000
LEV	.017	.631	1.626	-.061	.516
GROWTH	.006	.974	2.261	-.147	.456
DIV	-5.847	.103	1.339	-6.647	.088
BOARD	.182	.478	2.816	.199	.444
COMPOSITION	2.666	.644	1.195	.726	.906
INDUSTRY TYPE	No			Yes	
	R2	.328		R2	.376
	Adjusted R2	.271		Adjusted R2	.292
	F Value	5.686		F Value	4.474
	Observation	110		Observation	110

The definitions of the variables are reported in Table 1.

Table 7 Bad news to good news disclosure percentage regression analysis results

Variable	Panel A. Bad to Good News without Industry Type			Panel B. Bad to Good News with Industry Type	
	B	Sig	VIF	B	Sig
Constant	-.064	.925	-	1.072	.331
CRISIS	.427	.007	1.178	.397	.013
SIZE	.073	.503	3.041	-.161	.398
ROE	-.009	.016	1.976	-.010	.011
LEV	-.005	.333	1.626	-.016	.277
GROWTH	-.009	.724	2.261	-.024	.434
DIV	-.152	.783	1.339	-.140	.818
BOARD	-.043	.277	2.816	-.059	.151
COMPOSITION	1.248	.165	1.195	1.145	.238
INDUSTRY TYPE	No			Yes	
	R2	.280		R2	.311
	Adjusted R2	.218		Adjusted R2	.218
	F Value	4.510		F Value	3.351
	Observation	110		Observation	110

The definitions of the variables are reported in Table 1.

Keywords

Good/bad news disclosure, chairman statement, the global financial crisis, FTSE 100 index.