Research in International Business and Finance 39 (2017) 625–639

Contents lists available at ScienceDirect

Research in International Business and Finance

journal homepage: www.elsevier.com/locate/ribaf

Full length Article

Sustainability disclosure, dominant owners and earnings informativeness

Carolina Bona-Sánchez, Jerónimo Pérez-Alemán*, Domingo J. Santana-Martin

University of Las Palmas de Gran Canaria, Spain

A R T I C L E I N F O

Article history:
Received 9 September 2015
Received in revised form 24 May 2016
Accepted 8 July 2016
Available online 18 July 2016

Keywords:
Corporate social responsibility
Earnings informativeness
Dominant owners

A B S T R A C T

Focusing on an environment where ownership concentration is prevalent and where sustainability disclosure is not a new phenomenon, we investigate the effect that communication via social responsibility reporting has on earnings informativeness. We further address the moderating role of the dominant owner's voting-cash flow wedge in the relation between sustainability disclosure and earnings informativeness.We show that communication via social responsibility reporting provides additional information to market participants to assess earnings informativeness. Furthermore, we show that the positive relationship between sustainability reporting and earnings informativeness intensifies as the dominant owner's voting-cash flow wedge increases. Our results are consistent with sustainability disclosure reducing investors' and other stakeholders' uncertainty, thereby helping them better interpret financial information.

© 2016 Elsevier B.V. All rights reserved.

1. Introduction and motivation

The increasing use of sustainability information in different stakeholders' decisions and the value society places on the socially responsible behaviour of companies have become essential determinants of sustainability reporting (*e.g.*, Prado-Lorenzo et al., 2009; Yip et al., 2011). Evidence from prior literature indicates that the relation between financial and sustainability disclosure is complementary because companies with high-quality financial information have incentives to reveal all types of information, including sustainability information (*e.g.*, Verrecchia 1990; Penno 1997; Francis et al., 2008; Martínez Ferrero et al., 2013). However, according to the arguments in Francis et al. (2008), the relation between financial and sustainability disclosure could be substitutive because companies with poor-quality financial reporting might disclose sustainability information to substitute the lack of high-quality financial information. In line with this latter perspective, Lang and Lundholm (1993) show a substitutive relation between earnings quality and voluntary disclosure. Therefore, the interactions between sustainability disclosure and financial reporting quality are unclear.

* Corresponding author at: Facultad de Economía, Empresa y Turismo, Campus Universitario de Tafira Baja, Spain.
E-mail address: jeronimo.perez@ulpgc.es (J. Pérez-Alemán).

http://dx.doi.org/10.1016/j.ribaf.2016.07.020
0275-5319/© 2016 Elsevier B.V. All rights reserved.

However, although sustainability information is becoming increasingly important, the empirical evidence for the real benefits of social responsibility reporting, particularly the degree to which reporting on sustainability might influence market participants' perceptions, remains relatively unaddressed in the academic literature. This paper aims to help fill this void by empirically studying whether sustainability reporting is expected to affect earnings informativeness. Furthermore, to shed some light on the settings for which sustainability disclosure might affect earnings informativeness, we examine how the sustainability disclosure-earnings informativeness relationship covaries with the dominant owneŕs voting-cash flow wedge. Thus, our second research objective relates to the moderating role of the dominant owner's voting-cash flow wedge in the relation between sustainability disclosure and earnings informativeness. We use the Global Reporting Initiative (GRI) guidelines to proxy for sustainability disclosure.

Our paper is motivated by two factors. First, no previous study has analysed the role of sustainability information in determining earnings credibility, and there is no research on the moderating role of the dominant owner's voting-cash flow wedge in the relation between sustainability disclosure and earnings informativeness. Second, the Spanish environment is particularly suitable to test this incidence for several reasons. Compared with firms in the USA, Continental European firms operate in an environment with weaker investor protection, less developed capital markets, and a larger presence of dominant owners with the ability and incentives to influence corporate decisions (*e.g.*, La Porta et al., 1998; Faccio and Lang 2002; Djankov et al., 2008). In this environment, dominant shareholders use pyramidal structures to acquire power (*e.g.*, La Porta et al., 1999; Claessens et al., 2000; Faccio and Lang 2002). Pyramids facilitate the accumulation of power because they allow dominant owners to obtain greater control rights than cash flow rights (*e.g.*, Friedman et al., 2003; Morck et al., 2004; Almeida and Wofenzon, 2006). Finally, in the European context, large Spanish companies have demonstrated a superior understanding of the impact of social and environmental issues on their business. In this sense, according to the 2009 GRI report, Spain leads the world in terms of GRI reports (128 reports), followed by the USA (100 reports). Furthermore, large Spanish companies achieve an average quality score for their social corporate responsibility reports of 79 out of 100, preceded by Italy (85 out of a possible 100) and followed by the UK (76 out of a possible 100).

Our results provide insights into whether sustainability disclosure provides incremental and additional information to investors and other relevant stakeholders to assess earnings informativeness. Overall, our results reveal a positive incidence of sustainability information on earnings informativeness. The results are consistent with sustainability disclosure being perceived by market participants as the dominant owner's attempt to promote long-term relationships with stakeholders and/or to manage reputational risk. The results are also consistent with sustainability disclosure reducing investors' and other stakeholders' uncertainty and, consequently, helping them better interpret financial information. Moreover, we find that the positive relationship between sustainability disclosure and earnings informativeness becomes stronger as the dominant owner's voting-cash flow wedge increases. This latter result is consistent with CSR disclosure revealing the controlling owner's desire to resolve agency conflicts with the different stakeholders as these shareholders' voting-cash flow wedges increase, and with sustainability disclosure emerging as a mechanism to address an increase in media attention. Finally, our results might also be explained by sustainability disclosure reflecting the dominant shareholder's stewardship orientation, with this information being relevant to stock market participants in their assessment of earnings credibility.

Our paper contributes to the literature in different ways. First, we provide novel evidence on the link between sustainability disclosure and earnings informativeness in a context in which ownership concentration is prevalent and where, according to the more recent KPMG International Survey of Corporate Responsibility Reporting (KPMG, 2013), sustainability reporting is not a recent phenomenon. Second, we analyse the moderating role of the dominant owner's voting-cash flow wedge in the relation between sustainability disclosure and earnings informativeness. Third, by using a theoretical approach that combines agency theory, stakeholder theory, signalling theory, and stewardship theory, we are able to better show the dynamics between sustainability disclosure, earnings informativeness and a particular corporate governance mechanism, namely, the dominant owner's voting-cash flow wedge. This integrated approach suggests that, rather than acting as an opportunistic device, as the dominant shareholder's voting-cash flow wedge increases, sustainability disclosure following the GRI guidelines is a mechanism available to this shareholder to reduce agency conflicts and/or to address an increase in media attention. Furthermore, in this latter setting, sustainability disclosure might also reflect the dominant owner's stewardship orientation. Finally, a feature of our research design is that our unit of analysis is the individual firm rather than the country. As King and Santor (2008) note, one limitation of existing international studies of ownership is that most of these studies feature countries with very different legal, regulatory, and market institutions, making it difficult to disentangle firm-level effects from country-level effects. By focusing on a single country, namely, Spain, we have greater confidence that our results pertain to firm-level effects.

The rest of this paper is structured as follows. The second section reviews the theoretical arguments on the effect of sustainability disclosure following the GRI guidelines on earnings informativeness and the role of sustainability reporting in the relation between the dominant owner's voting-cash flow wedge and earnings informativeness. Previous analysis ultimately serves to develop our main hypotheses. The third section describes our empirical methodology, and the results are presented in the fourth section. The fifth and final section discusses the results and presents the conclusions.

Download English Version:

https://daneshyari.com/en/article/6481268

Download Persian Version:

https://daneshyari.com/article/6481268

Daneshyari.com