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Original Research Article

Effective Integrated Reporting <IR> Practices of the Malaysian Public Companies in the Industrial Products Segment of the Malaysian Stock Exchange

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Abstract

Introduction: Sustainability issues and initiatives are gaining emphasis to address shareholder interests and attract investment. Malaysian public listed companies (PLCs) are encouraged to adopt Integrated Reporting <IR> framework for disclosing both financial and non-financial information in their annual reports. This paper presents the findings of research on the adoption of <IR> by Malaysian PLCs. ***Methodology:*** Data was collected from 213 PLCs for the period 2010 – 2016. Based on the literature, a conceptual model was developed and tested by four hypotheses on the relationship between financial performance, strategy disclosure, governance disclosure, performance disclosure and prospects disclosure. The data was analyzed by descriptive statistics and multiple regression analysis. ***Results:*** The results indicated that the firms' prospects (future outlook) disclosure and organizational strategy disclosure make significant contributions to the average market value of the firms. Therefore, it is important for the firms have the competences to effectively engage in the <IR> using the <IR> framework. ***Conclusion and Recommendations:*** It is recommended that the Malaysian authorities should make the <IR> mandatory and provide training on <IR>. Malaysian PLCs should provide periodic integrated reports, comply with environmentally friendly standards and implement sustainability practices to fully participate in global supply chains.

Keywords: Integrated reporting, financial performance, Disclosure, Strategy, Governance.

INTRODUCTION

A robust corporate governance (CG) framework centred on transparency and disclosure is important for promoting investor's confidence and addressing stakeholder's concerns [1]. The Asian Financial Crisis, which witnessed multitude corporate failures in Malaysia and the region, was largely due to poor CG practices [2, 3]. The Malaysian Government took measures to improve CG practices and these included the Malaysian Code on Corporate Governance (MCCG) first issued by Securities Commission (SC) in Year 2000, duly revised in Year 2007, 2012 and 2017. The SC became responsible for all market operations [4] with Bursa playing a key role in the equity structure of the capital market [5].

The concept of corporate social responsibility (CSR) was the response to the demands of civil society; requiring companies to adhere to high standards of social and environment care [6]. The emphasis then shifted to corporate responsibility and sustainability reporting frameworks including the triple bottom line [7], and the <IR> framework issued in 2013 [8]. Malaysian PLCs are adopting <IR> to fulfil statutory compliance [9], and this paper aims to determine the extent of the adoption of <IR> by PLCs in the industrial product segment of the Malaysian stock exchange.

The paper is structured as follows. The next section reviews the pertinent literature on the evolution of <IR> commencing with the corporate governance framework, the shift to CSR and the transition from Corporate Responsibility (CR) to <IR>. This is followed by an outline of brief discussion on the research methodology, the data collection tools and analysis. The findings are then presented with a final section on recommendations and discussion.

LITERATURE REVIEW

CG can be defined as the way in which supplier and finance to a firm ensure themselves a good return [10]. Following the Asian financial crisis largely stemmed from poor financial disclosure and weak CG practices, corporations were pressured to provide timely and reliable disclosure of financial information. Consequently, CG has become more complex and dynamic because of increased regulatory requirements, greater scrutiny and the increased responsibility of board of directors to comply with rigorous governance standards [1].

Firms face increasing pressure from governments, competitors and employees to address a wide array of environmental social governance (ESG) issues. These range from climate change to obesity to human rights in the supply chain under the unprecedented transparency of internet connectivity [11]. Since these challenges converge on their corporate reputation, firms have to take full account of ESG issues and report to stakeholders on a growing spectrum of concerns [12]. Stakeholders include providers of financial capital, employees, customers, suppliers, business partners, local communities, NGOs, environmental groups, legislators, regulators and policy-makers [8]. Sustainability needs continual engagement of key stakeholders to achieve specific sustainability goals [13].

Several frameworks have evolved to guide how organisations can manage and disclose performance [14]. These frameworks offer a basis for continuous improvement as well as cross-industry comparisons while some firms utilised a mix of relevant frameworks and adopt or adapt them to suit their context and needs [15]. These include the Integrated Reporting (<IR>) framework which was introduced in December 2013 by the International Integrated Reporting Council (IIRC) with <IR> combining environment, social and government (ESG) concerns in the firms' Annual Reports [16].

The aims of <IR> are to improve corporate communication about value creation, advance the evolution of corporate reporting and to make a lasting contribution to financial stability and sustainable development. Well suited to enable stakeholders to make well informed decisions [17, 18, 19], <IR> is a precursor of a paradigm shift in corporate reporting [20]. Trade liberalization is resulting in stakeholders, in particular investors demanding greater transparency and disclosure on valuable information for both financial and non-financial concerns [21, 22, 16, 23].

The Institute of Internal Auditors (IIA) in its feedback to <IR> implemented in Malaysia in April 2017, viewed it is a reliable instrument to assess the firm's ability to create value in the short, medium and long-term and in its value for sustainability. Strongly supported by the ACCA and the Malaysian Institute of Accountants (MIA) regarded it as a tool to drive better reporting and responsible corporate practices in view of the multiplicity of non-financial reporting requirements, standards and frameworks [9].

Bursa published its first Annual stand-alone Sustainability Report (SR) with the G3 then G4 guidelines issued by the GRI in 2016. Bursa's SR reporting, in line with the Global Reporting Initiative (GRI) new GRI Standards for sustainability reporting. It also embeds sustainability throughout the Malaysian capital market and business operations. PwC Malaysia (2015) conducted an analysis on the top 50 PLCs' 2014 Annual Reports on the adoption of <IR> and the findings suggest that because of the challenges that they face for <IR> adoption, the majority merely report for compliance purpose.

There are several theories and models relating to CG, CSR and CS [24, 10, 25, 26, 27, 28, 29, 30]. There was much prior research on CG practices in Malaysia and on the Code of Corporate Governance [25, 4, 31]. There was also adequate literature on CSR reporting and frameworks for sustainability reporting frameworks [32, 33, 34, 35, 8, 36, 15].

In Malaysia, prior research has been conducted on the significance of the Global Reporting Initiative (GRI) [37, 38] and the <IR> [22, 16, 19]. The findings suggest that <IR> enables firms to report on their value creation process to their employees, customers, suppliers, business partners, local communities, regulators and policy makers. Simnett, Vanstraelen and Wai [39] examined reporting and assurance standards, and found that assurance provides confidence to stakeholders that the reporting is complete, accurate and balanced [40].

In Malaysia, prior research has been conducted on CR, sustainability practices and reporting regulations [41, 42, 43]. The Companies Act 2016 and the Financial Reporting Act 1997 as well as the MASB Approved Accounting Standards have also been critical reviewed [44, 42]. While, there is limited research on <IR> adoption in Malaysia. Lok [45] examined the impact of <IR> on the share prices by investigating the relationship between <IR> and the financial performance of PLCs in Malaysia.

Based on the literature, a conceptual model was developed with financial performance as the dependent variable and the independent variable comprising organizational strategy, governance, performance and prospects as shown in Figure 1.

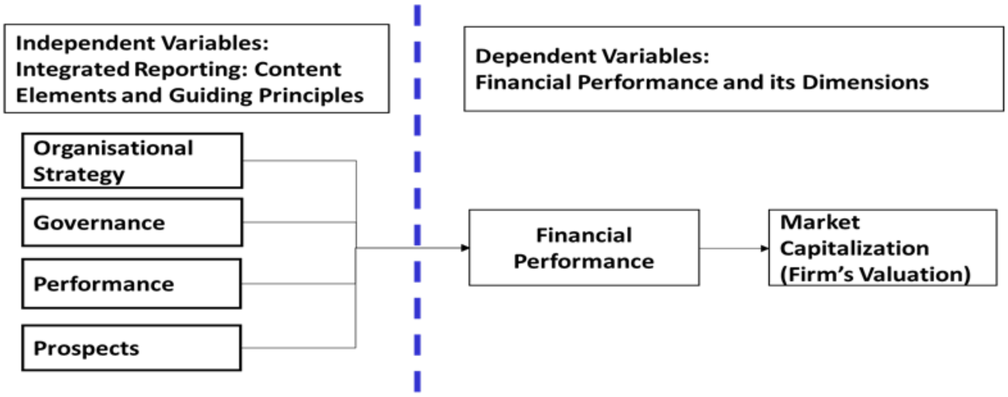

Fig-1: The conceptual Model
Source: Developed for this Paper

Four hypotheses as listed below were tested and these related to the relationship between the dependent variable of financial performance and the independent variables of strategy disclosure, governance, performance disclosure and prospects disclosure.

- **Hypothesis 1**
  H_0: The firm's <IR> strategy disclosure has no significant contribution to the financial performance of PLCs in Industrial Products segment.
  H_1: The firm's <IR> strategy disclosure has contribution to the financial performance of PLCs in Industrial Products segment.
- **Hypothesis 2**
  H_0: The firm's <IR> governance disclosure has no significant contribution to the financial performance of PLCs in Industrial Products segment.
  H_1: The firm's <IR> governance disclosure has significant contribution to the financial performance of PLCs in Industrial Products segment.
- **Hypothesis 3**
  H_0: The firm's <IR> performance has no significant contribution to the financial performance of PLCs in Industrial Products segment.
  H_1: The firm's <IR> performance has significant contribution to the financial performance of PLCs in Industrial Products segment.
- **Hypothesis 4**
  H_0: The firm's <IR> prospects disclosure in the context of its external environment has no significant contribution to the financial performance of PLCs in Bursa Malaysia's Industrial Products segment.
  H_1: The firm's <IR> prospects disclosure in the context of its external environment has significant contribution to the financial performance of PLCs in Bursa Malaysia's Industrial Products segment.

METHODOLOGY

A descriptive quantitative methodology was used as appropriate for testing contributory relationships using numerical evidence assigned to variables [44]. This approach is common in testing accounting or finance theories [46]. Prior studies [47, 46, 48, 49, 50, 51] with broadly similar objectives adopted a quantitative methodology with content analysis of the secondary data collected from the PLCs' Annual Reports [52, 44]. The accounting data was collected from the Annual Reports of 213 PLCs in the Bursa Main Market's Industrial Products segment for the period 2010-2016. The excluded PLCs were those PLCs that had changed their financial year-end during the period studied or suspended from listing pending restructuring or delisting including the ACE Market [53].

The Ohlson [54] model, often used in market-based accounting research for investigating the value-relevance of non-financial variables [55-61] was used to calculate the means, the median, the mode, the minimum, the maximum and the standard deviation for testing the hypotheses. . The following equation was used for the multiple regression analysis:

$$MV_{jt} = \alpha_0 + b_1\,BVE_{jt} + b_2 NI_{jt} + b_3 CS_{jt}$$

MV_{jt} = Market value of a firm j at the financial period (t).
BVE_{jt} = Value of net asset at the end of the financial period (t).
NI_{jt} = Net profit tax for firm j for financial period (t).
CS_{jt} = Compliance score with self-constructed index for firm j for financial period (t).
α_0 = the value of the outcome when the predictor is zero.
b_1, b_2, b_3 = the regression coefficient associated with the predictor variable.

Data Analysis

Descriptive statistics were used to analyse the pooled sample characteristics for the mean, minimum, maximum and the standard deviations. Multiple regression analysis was used to determine the relative importance of each of the independent variables in the prediction of the dependent variables to make inferences on their contributions.

The Mean and Median of organizational strategy (MMOS) for the seven years and/or all the years under observation except Year 2010 was marginally below two (2) points. For the analysis for future look (MMFO), all Mean and Median for the seven years were above two (2) points. Governance analysis (MMGV), in Year 2010, the Mean increased marginally from 1.7769 to 1.7784 in Year 2011, it grew by 4.8% to above 1.8637 in Year 2012 before decreasing to 1.8237 in Year 2016. The average Mean for the seven years was 1.8371 while the average Median was 1.8492. The Median trended lower from 1.8056 in year 2011 to 1.7778 before increasing to 1.8889 in Year 2012. It maintained this level before decreasing marginally to 1.8333 in Year 2016. For the Performance Analysis (MMPF) analysis, the average Mean and Median for the seven years and/or was low and closer to a one (1) point. The low standard deviation indicated that the data points tended to be closer to the mean of the dataset in most of the years without significant outliers.

The multiple regression analysis used an Analysis of Variance (ANOVA) table and an F-test in respect of i) Average Market Value; ii) Growth Difference in Market Value; iii) Average Market Value (Modified); and iv) Growth Difference in Market Value (Modified).

FINDINGS

The findings and the conclusions of each research hypotheses as listed below are based on the findings of the literature review and the statistical analysis.

- Hypothesis 1 was to determine the relationship between financial performance and strategy disclosure which comprises the firms' elements of its business model, risk and opportunities, strategy and resource allocation. The findings revealed the goodness of fit of the regression model depicted variance in the dependent variable is explained by the variation in the independent variable which is explained. It follows that the null hypothesis is rejected and therefore, the independent variable of <IR> strategy disclosure makes a highly significant contribution to the financial performance of PLCs.

- Hypothesis 2 was to determine the relationship between governance disclosure and financial performance which includes the basis for the preparation and the presentation of the elements in the firms' governance. The findings did not indicate significant contribution to the market value of the Firm. However, this finding may not be conclusive as the findings from the extant literature review did indicate firms' <IR> governance disclosure significantly contributed to the market value of the firm.

- Hypothesis 3 was to examine the relationship between financial performance and firms' <IR> performance. The statistical analysis indicated a firm's <IR> performance disclosure has no significant contribution to the financial performance of PLCs. However, this may not be conclusive as prior research findings as discussed in the extant literature review revealed that a firm's <IR> performance disclosure contributes to its financial performance of PLCs.

- Hypothesis 4 was to examine the relationship between prospects disclosure and financial performance which comprises of the firms' future outlook and the organizational overview and the external environment.The extant literature review findings revealed that research strategy disclosure contributes to the financial performance of PLCs. This is consistent with the findings of the statistical analysis that the firms' <IR> prospect disclosure significantly contributes to financial performance.

DISCUSSION AND RECOMMENDATIONS

This paper discussed the importance of the adoption of <IR> practices by Malaysian PLCs in line with the <IR> framework issued by the <IR> as it is a reliable instrument to assess the firm's ability to create value and to enhance the created values with the strategic allocation of resources in the short and medium terms. The findings affirm the need for PLCs to effectively implement <IR> and not merely adopt it for compliance purposes. The research yielded insights into the issues involved in the implementation process. Based on the findings, two sets of recommendations are offered.

The first is for considerations by the Government and the regulatory bodies. It is recommended the <IR> should be made mandatory with the amendments being made to the Companies Act 2016 to include <IR> as part of the disclosure or compliance in the Directors' Report and the Financial Statements. Since effective implementation of <IR> requires competence staff, the authorities should support short training courses for the accounting fraternity on <IR> that is aligned with global standards. The Government provides financial support and tax incentives to help them acquire the necessary certifications on <IR> to ensure compliance to global accounting standards and auditing.

The second related to managerial practices. PLCs are recommended to promote strong inter-firm linkages and communication within their own value-chain paradigms to enhance integration with advanced technologies to track value-creation. They have to insure that product offerings comply with environmentally friendly standards and be certified in accordance to global standards for participating in global supply chains and gaining global reputational advantage. It is also recommended that PLCs emphasize on developing human capital with skills for effective <IR> implementation.

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