

## Explaining the accounting disclosure index of stock exchanges by foreign exchange market activity

Aziz Bakay<sup>a,\*</sup>, Murad Moqbel<sup>b,1</sup>

<sup>a</sup> Gediz University, Department of Management, Gazi Mustafa Kemal Mh., Kaynaklar Cd., No: 115, B-221, İzmir, Turkey

<sup>b</sup> Our Lady of the Lake University, Computer Information Systems and Security Department, 411 S.W. 24th St., San Antonio, TX 78207, USA

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### ABSTRACT

In this article, researcher-created accounting disclosure index of 23 stock exchanges for the year 1992 and its relationship with variables including foreign exchange turnover, economic and financial indicators were investigated. The accounting disclosure index of global stock exchanges crafted by Adhikari and Tondkar (1992) was regressed on foreign market turnover which was utilized as a proxy for foreign exchange market activity. The OLS results supported that along with the activity of foreign exchange market; GNI per capita, market capitalization, energy and electric consumption, number of listed companies were significantly related with the accounting disclosure index. The foreign market turnover was found to be positively influencing the accounting disclosure index. The models explained about 73% of the variation in the index with an *F*-ratio of 26.56 indicating the overall significance of the model.

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### 1. Introduction

Different social, political, regulatory environments create different accounting disclosure requirements for firms across the world. It is clear to expect variation in the requirements of information disclosure of public firms traded in a stock exchange market in Switzerland (SIX Swiss Exchange) compared to firms traded in the stock exchange market of Turkey (Istanbul Stock Exchange). Requirements for information disclosure in part reflect the transparency and accountability of the public firms.

Accounting standard setters are continuously maintaining the accuracy and transparency of the disclosures by monitoring and providing additional guidelines and issuance of new requirements. The Financial Accounting Standards Board (FASB) has issued recently new disclosure requirements pertaining to application of fair value measurement provisions of US GAAP (Pounder, 2010). Therefore the decision making mechanism might be twisted accordingly to new disclosure requirements. An earlier study found that by surveying the institutional investors, corporate issuers and market regulators, capital market decisions are affected by such diversity in the international markets (Choi & Levich, 1991).

Ahmed and Courtis (1999) investigated the literature on the association between the accounting disclosure levels and corporate characteristics. Among various factors, their meta-analysis results

supported that the corporate size, listing status and leverage were positively and significantly influencing the disclosure levels. The correlation coefficients of these variables with the disclosure level are 0.3, 0.3, and 0.2 respectively. On the other hand, the accounting disclosure levels—higher or lower—were determined regardless of the profitability of the corporation, and the size of the audit firm. Earlier studies examined the accounting disclosure comprehensiveness and levels along with the corporate characteristics in different countries including Hong Kong (Wallace & Naser, 1995), United Kingdom (Wallace, Choudhury, & Adhikari, 1999). The former study suggested that there is relationship between the mandatory information enclosed in the annual reports of corporations with the researcher-created indices of the comprehensiveness of accounting disclosure. Significant covariations with several indicators of firm, i.e. scope of the business and asset size were found. These variables are evidenced to be positively associated with the comprehensiveness index. Similarly, the latter study empirically proved that firm size was positively, return on sales was negatively related to the comprehensiveness of cash flow reporting.

Accounting disclosure index for the year 1992, which was used in the present study, was created by Adhikari and Tondkar (1992). The authors focused on its relationship with macro-level factors. These factors include degree of economic development, type of economy, size of the equity market (market capitalization), activity on the equity market (market turnover), and dispersion of stock ownership in the equity market. Findings suggested that among these factors, only market capitalization was significantly explaining the index. This index has scores for 35 exchange markets (Stock exchange—SE) all over the world including Austria (Vienna SE), Finland (Helsinki SE), Korea (Seoul SE), Portugal (Lisbon SE), Turkey (Istanbul SE)

\* Corresponding author. Tel.: +90 232 355 0000.

E-mail addresses: [aziz.bakay@gediz.edu.tr](mailto:aziz.bakay@gediz.edu.tr) (A. Bakay), [muradmoqbel@gmail.com](mailto:muradmoqbel@gmail.com) (M. Moqbel).

<sup>1</sup> Tel.: +1 620 340 0888.

along others (Table 1). The authors have picked only one stock exchange from each country. The index was crafted by the authors as the following: A survey that included 44 items asking about listing and filing information requirements of stock exchanges was designed. The design was completed after a thorough review of the literature on information disclosure requirements and review of the listing and filing requirements of the NYSE, London SE, Tokyo SE that are considered to be the most precise accounting disclosure and reporting practices. Survey was sent to 287 experts in international equity market in 41 countries (7 experts in each country). Fifty-two percent response rate was recorded. By giving weight to some information items more importance relative to the literature, the authors created both weighted and unweighted indices.

The accounting disclosure has been examined in many ways in earlier studies; however, the niche point in this particular study is that we are analyzing the association between the accounting disclosure index of selected 23 global stock exchanges and foreign exchange market activities in these countries. Thus, we utilized the aforementioned researcher-created index as our dependent variable. The rationale behind including the foreign exchange market turnover as a variable in our analysis is the following: Stock exchanges include firms operating in international environment in which exchange risk is of high importance. If a stock market is exposed to international exchange risk, then stock exchange receives more pressure to disclose information in detail and in more transparency. Hence, as the internationalization of a stock exchange builds up, the more qualified accounting disclosure requirements of stock exchanges are observed leading to better accounting disclosure scores.

2. Methodology

2.1. Variables

The accounting disclosure index was obtained from an earlier study by Adhikari and Tondkar (1992). In their study, scores are calculated for 35 stock exchanges across the world and we could include only 23

Table 1  
Accounting disclosure index.  
Source: Adhikari and Tondkar (1992).

Country	City of stock exchange	Weighted average	Unweighted average
1 Australia	Sydney	74.60	74.64
2 Austria	Vienna	54.17	53.52
3 Canada	Toronto	79.00	78.64
4 Denmark	Copenhagen	67.20	66.86
5 Finland	Helsinki	70.54	71.05
6 France	Paris	76.20	76.16
7 Germany	Frankfurt	67.20	66.86
8 Greece	Athens	60.00	59.41
9 Hong Kong	Hong Kong	77.04	75.77
10 Italy	Milan	68.46	68.39
11 Japan	Tokyo	77.68	77.68
12 Luxembourg	Luxembourg	66.62	66.64
13 Netherlands	Amsterdam	73.19	72.84
14 New Zealand	Wellington	67.13	65.91
15 Norway	Oslo	60.63	60.59
16 Portugal	Lisbon	65.68	65.50
17 Singapore	Singapore	80.89	80.32
18 South Africa	Johannesburg	74.50	73.48
19 Spain	Madrid	68.84	68.36
20 Sweden	Stockholm	60.54	60.05
21 Switzerland	Zurich	72.19	71.70
22 UK	London	86.21	84.86
23 US	New York	90.31	90.75

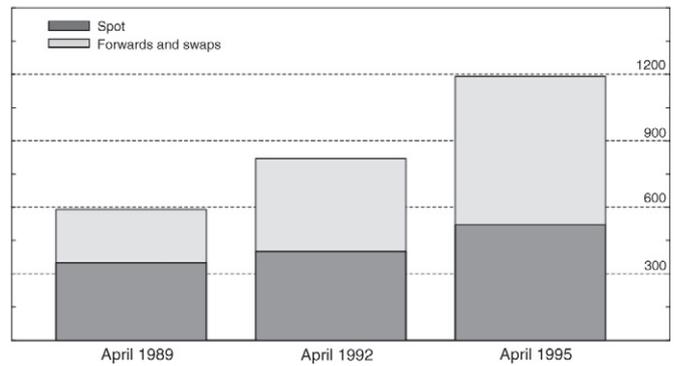


Fig. 1. Estimated global foreign exchange market turnover by market segment in April 1989, April 1992, and April 1995. Average daily turnover, in billions of US dollars. Source: Bank for International Settlements (1996).

of those due to data limitation. Unweighted index provided better results for this particular study and we disclosed the results of both unweighted and weighted. The aforementioned study was published in 1992, and observations of other variables for the year 1992 were obtained. Having only observations for the year 1992, might raise analytic problems as conducting regression with very limited number of observations (23 observations). Therefore, for the second stage of our data collection, we would assume that accounting disclosure index is valid for the years 1989 and 1995 in addition to the year 1992, for which we were able to pull the foreign exchange market turnover data. This would allow us to enlarge our data set to 64 observations.

As the focal relationship in the model, we utilized the foreign exchange turnover as a measure of the activity of the exchange market (Bank for International Settlements, 1996). The contracts are segmented into three categories of spot, forward and swaps. In the year 1992, almost half of the contracts are spot and the remaining was shared by forwards and swaps (Fig. 1). In 1992, foreign exchange turnover reached \$800 billion and in 1995 it reached just below \$1.2 trillion. 82% of all of these foreign exchange contracts have dollar as currency on side of the contract, followed by Deutsche Mark (40%) and Japanese Yen (27%) (Bank for International Settlements, 1996).

Great Britain as the financial center of the World ranked the highest in terms of the foreign exchange market turnover and it

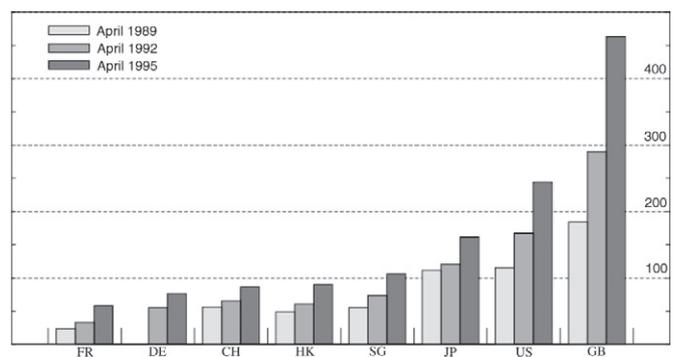


Fig. 2. Reported foreign exchange market turnover in major centers in April 1989, April 1992, and April 1995. Average daily turnover, in billions of US dollars. Source: Bank for International Settlements (1996).

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