

Information Needs of Users of New Zealand Capital Markets Entity Reports

**An External Reporting Board research conducted on its behalf by
Massey University**



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February 2016

List of Abbreviations

CFA	Chartered Financial Analyst
EFRAG	European Financial Reporting Advisory Group
EPS	Earnings per share
EU	European Union
FMA	Financial Markets Authority
GPFR	General purpose financial reports
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
NBDT	Non-bank deposit takers
NZX	The New Zealand stock exchange, NZX Limited
PwC	PricewaterhouseCoopers
RBNZ	Reserve Bank of New Zealand

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Executive Summary

Motivations and objectives of the research project

In April 2014, the External Reporting Board (XRB) released a strategic plan, which sets out priorities for the five-year period ending in June 2019. A key objective of this plan is to ensure that accounting, auditing and assurance standards are based on the user-needs approach.

Whether current reporting meets users' needs has been assessed by reviewing existing literature relating to user needs and by reporting on the results of a survey of users of General Purpose Financial Reports (GPFR) of New Zealand for-profit entities that apply Tier 1 accounting requirements (NZ IFRS) in preparing their GPFR (Tier 1 for-profit entities)¹. This includes a focus on whether the information needs of users of for-profit entities operating in the New Zealand domestic capital market differ from those of users of for-profit entities operating in international capital markets. In particular, this research report addresses the question of whether New Zealand equivalents to International Financial Reporting Standards (NZ IFRS) are fit-for-purpose and enable preparation of general purpose financial reports that satisfy user needs.

The outcome of this research should assist the XRB in its application of the user-needs approach to evaluate current accounting standards, and to identify priorities, if any, for improving financial reporting.

Literature review

Most user-needs studies have been conducted in developed countries including Australia, the United Kingdom (UK), the United States of America (US), and the European Union (EU). There are very few studies researching New Zealand users, a factor which emphasises the importance of the empirical stage of this research project.

Previous research focuses mainly on the needs of equity investors and to a lesser extent on those of debt investors and other creditors. The findings in previous research support the decision-usefulness of financial reports and their important role in the accountability process.

In summary, prior research indicates that:

- (a) Professional investors are more heavily reliant on financial statements than individual investors. They require that accounting policies be easy to find, and disclosures be company-specific with a useful level of detail;
- (b) Bankers value information differently and specify different information needs regarding contribution margin reporting, segment reporting, profit forecasts, interim reporting, and balance sheet values; and

¹ "Tier 1 For-profit entity" means a reporting entity that applies Tier 1 For-profit accounting requirements, namely NZ IFRS. A Tier 1 for-profit entity includes an entity that has "public accountability", is deemed to have public accountability or is a large for-profit public sector public benefit entity (Refer to XRB A1 *Application of the Accounting Standards Framework* (XRB A1) for the definition of "public accountability" and large for-profit public sector public benefit entities).

- (c) There is increasing evidence of calls from users for prospective information, summarised reporting, and meaningful management commentary on firm performance.

Overall, this suggests that up-to-date, transparent, entity-specific and future-oriented information is preferred by individual investors, investment professionals and bankers alike. There is little research relevant to user needs since the 1970s, highlighting the importance of updated information such as that offered by this research project.

Survey of key user groups

An online questionnaire was developed that contained 13 questions exploring the usefulness of financial statements and the other sources of information used in making decisions.

Before launching the online survey, a pilot test of the questionnaire was conducted to identify and resolve potential issues such as ambiguity or bias.

Primary users of for-profit GPFR were determined with reference to:

- (a) The New Zealand Equivalent to the IASB Conceptual Framework for Financial Reporting 2010 (New Zealand Framework), which identifies: existing and potential investors (equity and debt), and lenders and other creditors (i.e., trade creditors or suppliers);
- (b) Prior literature, which identifies other external users who are also interested in GPFR including: intermediaries and advisors, such as financial analysts, stock brokers, and fund managers; and financial market regulators, including prudential regulators; and
- (c) A variety of approaches were used to reach the different user groups and encourage high response rates. These included publicising links to the survey through various digital, print and social media channels to attract individual equity/debt investors. Email invitations were sent to selected top 100 shareholders of entities listed on the NZX; bank lending officers of major NZ banks; and to advisors, brokers, and fund managers; as well as to regulators of New Zealand capital markets.

The final sample consists of 145 responses, including 45 investors, 22 lenders, 70 intermediaries and 8 regulators. However, most respondents have multiple roles.

Most respondents have above average levels of knowledge, skills, and experience in reading, understanding and analysing financial statements.

About three quarters of the respondents are interested in both domestic and international markets, 23% are interested in entities operating solely in the domestic market, and only 1% are interested in entities operating solely in the international market.

To gain further insights and a deeper understanding of users' information needs, in-depth interviews were conducted with 10 selected representatives of the four identified primary user groups.

Findings

Q1. Use of financial reports

Most (79%) respondents indicate that they use the information in corporate financial reports in their decisions relating to investments and/or corporate performance. Most of those who indicated that they are not using financial reports, explained that they relied on information provided by in-house analysts or research teams, who analyse annual reports in depth rather than directly referring to financial reports. These 'non-users' tended to have negative views about financial statements (e.g., too lengthy, too complex, convoluted in layout and terminology, hid important information, ambiguity).

Q2. Types of decisions for which financial reports are used

Overall, the greatest proportion of users (45%) indicate that they use financial reports for equity investment. This is true for the investor (64%) and intermediary (50%) groups. As expected, the majority of lenders use financial reports for lending or extension of credit (71%). Regulators use financial reports mainly for monitoring financial soundness, regulatory compliance and consistency of published data with corporate reporting returns, as well as for assessing financial risk and performance.

These results indicate that different user groups use financial reports for different types of decisions and have different information needs.

Q3. Usefulness of components of financial statements

Although all financial statement components are rated as useful by the respondents, the statement of profit and loss, and the statement of financial position are ranked as the two most useful. The statement of changes in equity is rated as the least useful.

Analysis of significant correlations among these usefulness ratings and users' knowledge, skills and experience provide additional insights. In particular, the more knowledge and skills users have, the more useful they tend to find the income statement and cash flow statement. Significant relationships are also identified between usefulness of the income statement and balance sheet; and between usefulness of the cash flow statement and the notes to the financial statements.

Q4. Information provided in financial statements but not useful to users

Most respondents (76%) indicate that all information in financial statements was useful. Comments supporting these views are well summarised in the statement from a respondent: *'all helps to build a picture'*.

Respondents who indicate that there is information in financial statements which is not useful to them tend to suggest that the notes to the financial statements could be simplified, shortened or even placed online only.

Q5. Information not provided in financial statements that would be useful to users

Overall, a small majority of respondents (54%) do *not* require additional information. However, most investors (73%) indicate the opposite. Comments from such individual

investors, unsurprisingly, focus on the performance of their investments (e.g., suggestions that comparisons to earnings targets and budgets, would be a helpful, as well as earnings projections; enhanced segment reporting; and information about sales margins and business activity).

A small majority of lenders also indicate the need for disclosure of additional information (e.g., more detailed cash flow information as well as additional details regarding loans, terms of borrowing, security over borrowing and credit facilities).

Q6. Improving information

Most respondents had no further suggestions for improving financial statements, but suggestions from those who did may be summarized as follows:

- (a) Lenders suggest that greater consistency in formatting and presentation of financial statements would be desirable;
- (b) Individual investors generally suggest simplification and standardisation of reporting so that the performance results can be easily compared between companies. Suggested improvements include transparency (particularly regarding contingencies, guarantees, obligations and related party transactions); aggregation of common information to highlight items of material importance (e.g., key performance indicators, and five year comparatives) and forecasts;
- (c) Intermediaries who did make comments suggest improved consistency and transparency in financial reporting, as well as normalisation of reported earnings; and
- (d) Regulators suggest that simplification of the language used in financial statements, more structured and consistent reporting and disclosures between companies, and improvements to timeliness of published information would be welcome additions to current reporting requirements.

Q7. Information sources

Overall, advisors and analysts reports are rated as the most important source of information (34%), with corporate financial statements a close second (30%). Interestingly, lenders ranked corporate financial statements as their most important source of information (60%).

Q8. Interest in supplementary information

The majority of investors (64%), lenders (55%), and regulators (75%) indicate a need for supplementary information, while only 31% of intermediaries indicate such a need.

Q9. Usefulness of supplementary information

Respondents who indicate an interest in supplementary information were then asked to indicate the level of usefulness of supplementary information types in financial reports. Overall, respondents ranked all supplementary information types as being useful, with the most useful being business strategies and future prospects, followed by narratives that explain financial performance and position of a reporting entity.

Additional analysis

Comparing users with non-users of financial statements

Users' average knowledge, skills and experience are significantly higher than non-users for all user groups and the total sample.

Users of financial statements source their information significantly more from financial statements and management commentary and analysis, while non-users tend to rely significantly more on advisors and analysts' reports.

Comparing users operating in domestic vs international markets

Respondents who are interested in the domestic market only are not significantly different from those also interested in the international market².

The main differences between the two groups are that domestic users are more likely to use financial reports for lending decisions than international users, and international users are more likely to use advisors and analysts' reports than domestic users.

Conclusion

The findings of this research are broadly consistent with the few recent overseas studies, as well as with much of the earlier literature.

Overall, a significant majority of respondents do use financial reports in making various types of decisions, and most users are satisfied with the quality of current financial reports in meeting their information needs.

All components of financial reports are perceived, on balance, to be useful. In general, respondents rank the statement of profit or loss and the statement of financial position as the two most useful components, while the statement of changes in equity is considered to be least useful. Only a quarter of respondents indicate that the financial statements contain information that is not useful.

Most respondents do find notes to the financial statements useful when making their decisions. Consistent with prior studies, a number of respondents suggest improvements in disclosure of expectations about future performance. Some respondents suggest better disclosure (e.g., segment reporting, and/or reporting on sustainability), and others suggest simplification, standardisation, and transparency to current financial reporting.

As regards sources of information, our findings are consistent with the more recent European study by EFRAG (2009), showing that both analysts' reports and financial statements are rated as the most important sources of information. This may indicate the improvement in the quality of financial statements in recent years and an increase in the sophistication of users.

² The international market group is made up of all the participants who have an interest in international markets in addition to the domestic market (110 subjects) or the international market only (2 subjects).

Our results are also consistent with the some of the earlier studies that show that investors are more reliant on advisors' reports than financial reports. This finding is associated with the level of sophistication of the users. Investors, lenders, and regulators are more interested in supplementary information than intermediaries.

Overall, users appear satisfied with the current state of financial reporting for Tier 1 for-profit entities, although this study does identify some useful insights as to where future efforts for improvement could focus.

Recommendations

Based on the findings in the survey and interviews we propose improvements to financial reporting overall and to some specific items. These improvements include simplification, standardisation, comparison with budget and targets, dashboard reporting, supplementary information, segment and financial instruments disclosures.

1. Introduction

The New Zealand Accounting Standards Framework requires the application of all NZ IFRS by for-profit entities that have public accountability, are large for-profit public sector entities,³ or that opt to apply NZ IFRS in preparing General Purpose Financial Reports (GPFR)⁴. It is appropriate to question whether these standards are fit-for-purpose and satisfy user needs.

This research report addresses these questions by contributing insights on the information needs of various users of GPFR of New Zealand Tier 1 for-profit entities⁵. This includes a focus on whether the information needs of users of for-profit entities operating in the New Zealand domestic capital market differ from those of users of for-profit entities operating in international capital markets.

Prior literature on capital market studies in developed countries reveals that users of GPFR have diverse objectives, interests and information needs. This diversity is reflected in the myriad of users' roles, the sources of information they use and their varying levels of sophistication. Indeed, New Zealand's move to a multi-sector, multi-tier reporting approach is an initial step in the recognition of such diversity. The existing literature supports continuing efforts to investigate and respond to user needs in order to improve the extent to which financial reporting is fit-for-purpose.

Section 2 sets out the background, which provides important context for this study. The sections which follow describe the research objective (Section 3), primary user groups of GPFR (Section 4), research methodology (Section 5) and review of the extant literature (Section 6). Sections 7, 8 and 9 describe the results of the survey questionnaire and follow-up interviews, while the final sections set out the research limitations (Section 10) and conclusions (Section 11).

2. Background on the "user-needs" approach to standard-setting

In April 2014, the External Reporting Board (XRB) released a strategic plan, which sets out priorities for the five year period ending in June 2019. A key objective of the plan, is to ensure that accounting, auditing and assurance standards are based on user needs.

Under this user-needs approach, financial reports prepared in accordance with the New Zealand accounting standards framework should provide the information that is needed by users of financial reports for accountability, and decision-making purposes.

The user-needs approach is based on the primary principle that GPFR should "... provide information to external users who have a need for an entity's financial statements but are unable to demand them".⁶ This principle requires that accounting standards be fit-for-

³ Refer to External Reporting Board (XRB) Standard A1 *Application of the Accounting Standards Framework* (XRB A1) for definitions of public accountability and large for-profit public sector entities.

⁴ "General purpose financial reports" (GPFR) means financial reports that are intended to meet the needs of users who are not in a position to require an entity to prepare reports tailored to their particular information needs. See also XRB A1.

⁵ "Tier 1 For-profit entity" means a reporting entity that applies Tier 1 For-profit Accounting Requirements, namely the requirements of NZ IFRS in full.

⁶ XRB, 2012, p. 22

purpose and satisfy user needs. The XRB recognises that different users have different information needs and that it is important to reflect these needs appropriately in the reporting requirements, hence the strategy to divide reporting entities into different sectors and different reporting tiers.

3. Research objective and outcome

The objective of this research is to investigate the information needs of users of New Zealand capital market entities' financial reports. Specifically, this study aims to understand the extent to which current financial reports under NZ IFRS meet the information needs of the key users of New Zealand Tier 1 for-profit entities, and to identify what improvements may be necessary to satisfy the diversity of user needs.

The outcome of this research should assist the XRB in its application of the user-needs approach to evaluate current accounting standards, and to identify priorities, if any, for improving financial reporting. This study also contributes to the XRB's 2014-2019 strategic plan.

4. Primary user groups

The New Zealand Equivalent to the IASB Conceptual Framework for Financial Reporting 2010 (New Zealand Framework) sets out the following as the primary users of for-profit GPFR who are involved in making decisions about providing capital, loans or extending credit to an entity:

- existing and potential investors (equity and debt);
- lenders and other creditors (i.e., trade creditors or suppliers).

Prior literature identifies other external users who are also interested in GPFR including:

- intermediaries and advisors, such as financial analysts, stock brokers, and fund managers; and
- financial market regulators, including prudential regulators.

This study therefore targets the four major user groups identified above, while recognising a warning in the literature that such user groups may not be homogeneous. For example, equity investors may be further sub-classified into private/individual equity investors and professional/institutional equity investors due to differences in their levels of sophistication.

5. Literature on information needs

A growing body of research and related literature has evolved with developments of IFRS and can be categorised broadly as: studies of IFRS accounting properties' effects, IFRS value relevance effects, and IFRS capital market effects. As suggested by this categorisation, IFRS research to date is focussed on effects rather than user needs. These studies do, however, provide some indirect insights related to user needs, such as challenges due to increased complexity (Jermakowicz et al., 2007) and benefits arising from improved comparability (Brochet et al., 2013), as well as forecast accuracy (Byard et al., 2011; Horton et al., 2011;

Tan et al., 2011). The focus of this study is on prior research which is directly related to user needs, as described in the sections below.

The aim of GPFR is to provide users with information that reflects a true and fair view of the economic condition of an entity. Such information is considered to be useful as it enables users to make decisions about the allocation of resources to and within an entity, and claims against the entity, as well as about making later changes to such decisions. For example, users need information to assist them in deciding whether to make new allocations (investment), or to determine whether their past decisions have been justified. Another benefit of GPFR from users' and particularly stakeholders' points of view is that GPFR is a means of accountability between those charged with governance in the reporting entity and the stakeholders, as well as a means of evaluating management performance.

The International Accounting Standards Board (IASB)'s Conceptual Framework suggests relevance and faithful representation as the two fundamental qualitative characteristics of information contained in GPFR. For users to consider information to be useful, it must be relevant to the decision-making and faithfully represent the economic phenomena it represents.

The New Zealand Framework defines four more characteristics that enhance decision-usefulness, including comparability, verifiability, timeliness, and understandability. Fulfilling these characteristics is a complex process, because of the diversity of users and their varying needs.

Prior research tends to focus on the needs of equity investors, rather than those of debt investors and other creditors. Also, most studies that examine user information needs are somewhat outdated, having been conducted mostly during the 1970s and 1980s. These studies provide valuable insights, but the relevance of their findings is likely to diminish with the passage of time, due to the globalisation of capital markets, changes to financial reporting regimes, advances in information technology and other significant changes in the business environment in recent years. There is a notable absence of more recent research, highlighting the importance of this research project.

A summary of studies that examine user information needs is presented in [Appendix 1](#) and a second summary of studies that identify users' primary sources of information is provided in [Appendix 2](#). The following sections provide a brief discussion of the findings from these studies and a comparison of the information needs of equity investors, debt investors, and other creditors.

5.1 Information needs of equity investors

Financial information is useful to investors for at least two reasons: equity valuation, and/or evaluating management performance (Kothari et al., 2010). The former is known as the "valuation" or "decision-usefulness" role of accounting information, and the latter is known

as the “stewardship” or “accountability” role⁷. Equity investors (shareholders) are generally concerned with the inherent risk and the return of their investments. The agency relationship arising from the separation of management and ownership is at the basis of a popular theory explaining why equity investors need timely and reliable information to assist in making efficient investing decisions and in effectively monitoring management actions (Armstrong et al., 2010).

For equity valuation purposes, investors seek information about firms’ current and prospective performance. A common concern is that GPFs provide limited information on future prospects, a theme which is particularly prominent in earlier studies.

Several early studies examine user information needs in the US, UK, and Australia and focus on private/individual investors. They find that equity investors are primarily concerned with expectations about future earnings and cash flows (Baker & Haslem, 1973; Lee & Tweedie, 1975a; Chenhall & Juchau, 1977; Anderson, 1981).

In the US, Baker and Haslem (1973) examine whether the information provided in financial statements meets the needs of individual investors. They find that US investors are primarily concerned with expectations about future earnings. Providing profit forecasts, as part of prospective information, reduces investor uncertainty regarding future returns. Similarly, Lee and Tweedie (1975a) find that the economic prospects of a company are considered to be the most important items of information to UK individual investors. A survey by Chenhall and Juchau (1977) suggests that Australian investors consider seven factors to be important. Three of these relate to prospective matters – expected future increase in share price, future economic outlook of the company and industry, and expected future growth in earnings per share (EPS).

A stream of studies also examines the information needs of professional/institutional equity investors, who are generally considered to have more expertise and resources for analysis of financial information than private/individual investors. Baker and Haslem (1973) comment that individual investors appear to have different information needs from professional analysts and rely less on financial statements than professional analysts do. However, individual investors are found to be dependent on the advice provided by professional analysts. Subsequent studies (Barker, 1998; Imam et al., 2008) reach similar conclusions.

The use of equity valuation models requires information on future earnings or future cash flows. Anderson (1981) finds that institutional investors in Australia need information about future prospects to be reported in annual reports. Many years later, Gassen and Schwedler (2010) conduct an online survey to investigate opinions of professional investors and their advisors from 22 countries on the decision-usefulness of different accounting measurement concepts. They find that their respondents consistently rank mark-to-market fair value as the most decision-useful, but it is also important to note that they rank mark-to-model fair

⁷ In July 2005, the IASB and the Financial Accounting Standards Board in the US (FASB) removed stewardship as a separate financial reporting objective in their converged Conceptual Framework. Instead, the stewardship role is subsumed under the decision-usefulness role (O’Connell, 2007).

value as the least decision-useful.⁸ Up-to-date information using market relevant performance indicators is shown to be highly relevant to institutional equity investors.

Chandra (1974) uses a questionnaire to examine whether public accountants (as the preparers of financial information) and security analysts (as users of financial information) agree on the importance of various information items in equity investment decisions. He finds that accountants generally do not value information in the same way as security analysts do. For example, they differ with respect to the need for details and breakdown of inventories, investments, earnings from subsidiaries and operating expenses.

More recently, PwC (2014a, 2014b) conducted a series of surveys to investigate the needs and opinions of investment professionals with regard to maximising the effectiveness of corporate reporting. Based on interviews with 85 professional investors around the world, PwC (2014a) finds that the majority of professional investors consider adjusted performance measures (non-GAAP) helpful for their analysis, but they recommend improved transparency of disclosure. PwC (2014b) finds that there is little consensus among professional investors about their preferences for presentation, format, and layout of financial reports. Professional investors indicate that accounting policies should be easy to find, and that disclosures should be company-specific with a useful level of detail.

CFA UK (2015) conducted a survey of more than 290 investment professionals on the importance of the annual reports and other forms of company reporting. The results of that most recent study show that 60% of respondents believe financial reports contain too much irrelevant information, while 55% think financial reports omit some important information, 47% think the disclosure of risks and uncertainties should be improved, providing evidence that perceived importance of information is very much a reflection of personal preference. However, overall most respondents agree with the improved quality of financial reporting over the last 10 years. Coincidentally, that is also the period since IFRS adoption in a large number of countries around the world.

Overall, the literature on equity investor information needs suggests that up-to-date, transparent, entity-specific and future-oriented information is preferred by both individual investors and investment professionals.

5.2 Information sources of equity investors

Investors, whether individual or professional, rely on a variety of sources to satisfy their information needs. [Appendix 2](#) provides a summary of 10 studies examining and ranking the importance of various information sources by various user groups.

Much of the evidence in prior literature on sources of equity investor information shows that individual investors are more likely to use public media, analysts' advice, and advice from friends and family members than to use financial reports as their main sources of

⁸ Mark-to-market refers to fair values based on market prices in an active market; while mark-to-model refers to fair values based on valuation models in the absence of observable market prices in an active market.

information for investment decisions. There is little consistency in prior studies as to how these sources are ranked between the studies concerned.

In an early US study, Baker and Haslem (1973) find that individual investors consider stockbrokers and advisory services as the most important sources for their investment information, and attach minor importance to published financial statements as a source of information. On the other hand, in the UK, Lee and Tweedie (1975a) find that most respondents regard annual reports as an important source of information for investment decisions, and that financial press reports, followed by stockbrokers' reports are also considered particularly important.

The results in Lee and Tweedie (1975a) elaborate on how investors use annual reports, suggesting that private shareholders tend to skim through them and focus on the chairman's report. Bartlett and Chandler (1997) partially replicate the Lee and Tweedie (1975a) study in examining the readership of annual reports for a sample of UK private shareholders. Their results indicate that annual reports are not widely read by private shareholders, despite significant changes in financial reporting since the 1970s. Lee and Tweedie (1975b) investigate private shareholders' understanding of accounting practice, and find that those shareholders with more knowledge or experience of accounting are more able to understand financial reports than those with a lesser knowledge or experience. A later survey by Elliot et al. (2008) finds that less experienced non-professional investors who use unfiltered (raw) information, earn lower returns than more experienced investors.⁹

In general, the evidence from the literature indicates that professional investors are more heavily reliant on financial statements than individual investors. This observation supports Baker and Haslem (1973) who suggest that summary information should be provided to average individual investors, while more comprehensive financial statements with detailed information should be directed to professional analysts.

Anderson (1981) finds that Australian institutional investors rank annual reports as the most important source of information, followed by sharebrokers' advice and company visits. The most widely read sections of the financial report are the balance sheet, profit and loss statement, notes to the accounts, and chairman's address. Similarly, Day (1986) finds that UK investment analysts perceive the annual report to be an important document, but not a timely source of price sensitive information. Further, surveys by Vergoossen and Amsterdam (1993) in the Netherlands, and by Conesa and Martinez (2004) in Spain, find that the annual report appears to be vital to investment analysts, who emphasise the importance of the consolidated balance sheet and income statement. More recently, Gassen and Schwedler (2010) also find that professional investors and their advisors in 22 countries generally view annual financial statements as the most relevant information source, followed by direct

⁹ Elliot et al. classify information as "filtered" and "unfiltered". Filtered information is information packaged by a professional intermediary for consumption by investors (e.g., analysts' reports) while unfiltered information is information disclosed by management and unaltered by professional intermediaries (e.g., a firm's annual report).

personal contact with investee management, notes to the financial statements, and quarterly financial statements.

One possible explanation for the increased perceived usefulness of financial statements, at least for professional investors, is the adoption of IFRS around the world and evidence in the literature supporting consequent improvements in the quality of reported financial information.

In New Zealand, McNally et al. (1982) find that professional users, as compared to financial editors and stock exchange members, attribute different importance levels to more detailed disclosure of specific items, but that few of these differences are statistically significant.

More recently, the European Financial Reporting Advisory Group (EFRAG) (2009) conducted a survey of users in 10 European countries. This survey indicates that most users consider financial statements and management commentary as the most useful sources of financial information, compared to press releases, economic surveys, and market information.

PwC (2011a)¹⁰ finds that while the annual report is still seen by many as an invaluable source for providing detailed information about firm performance, it is no longer viewed by investment professionals as the document of record that provides the cornerstone for all valuation work. In particular, to improve the quality of disclosure, investment professionals indicate a need for more disaggregation in segment reporting, and more coherent, consistent information between narrative sections of the annual report and the audited financial statements.

The CFA UK (2015) study reveals that investment professionals use annual reports as the most useful source of financial information, followed by databases (e.g., Bloomberg) and sell-side research reports.

While this literature review concentrates on GPFR and financial information, it is appropriate to note the calls in the literature from individual investors for summarised information (Baker & Haslem, 1973), and more recently the emphasis by these users on management commentary (EFRAG, 2009). There is also the need for better integration between narrative sections of the annual report and financial statements (PwC, 2010). The growing importance of management commentary on a business and its results is evident in various developments around the globe. Examples include requirements in the US for management discussion and analysis to accompany the financial report, in the UK for directors' reports to include a business review, in Australia for an "operating and financial review" to be included in the annual report (ASIC, 2013), and in South Africa for listed entities to produce an integrated report (Stent & Dowler, 2015).

New Zealand requirements are currently lagging in this regard. Requirements for the contents of an annual report are specified in section 211 of the Companies Act 1993¹¹.

¹⁰ PwC (2011a), 'The Role of the Annual Report', retrieved from http://www.pwc.com/en_GX/gx/audit-services/corporate-reporting/publications/investor-view/pdf/pwc-role-of-the-annual-report.pdf

¹¹ Companies Act 1993, extracted 15/4/2015 from <http://www.legislation.govt.nz/act/public/1993/0105/latest/DLM321118.html>

There is no specific requirement for a director's report or management discussion and analysis, although the board of directors is required to provide details of material changes in the nature or classes of the business of the company (Deloitte, 2011). Listed entities on the NZX are required to provide commentary on the results for the period in a preliminary announcement in respect of a full year. Many entities meet this requirement by including the necessary information in a chairman's or director's report (Deloitte, 2011).

In summary, financial statements are seen by both individual and professional investors as a valuable source of information for investment decision making, but more so by professional investors. There is a perceived need for further integration of financial information with narratives and other corroborative data about reporting entities so to better assist in investment decision making.

5.3 Information needs of debt investors and other creditors

Similarly to equity investors, debt investors also seek information about the firm's ability to generate earnings and about operating cash flows. Their information needs and purposes however, are different (Ball et al., 2008; Kothari et al., 2010). Compared to equity investors, who are residual claimants, debt investors and other creditors have higher priority in liquidation and bankruptcy and often have security over the firm's assets (Armstrong et al., 2010). A consequence of this difference is that debt investors (such as bankers) generally demand financial information about the value of the firm's assets in the event of liquidation, the extent of other claims, and firm performance (Kothari et al., 2010). Their information needs are driven by their need to assess the firm's ability to make interest and principal payments under debt contracts, and the probability that the firm may not be able to repay debts when they fall due.

In some situations, conflicting interests arise between equity investors and debt investors, such as when there is asset substitution, under-investment, claim dilution, and dividend payment (Smith & Warner, 1979). Benjamin and Stanga (1977) compare the perceived information needs of equity investors and debt investors by conducting a survey of a sample of bankers and financial analysts. They find that bankers do not seem to value information in the same manner as financial analysts. They attribute these differences to variations in the types of decisions these two groups make as well as differences in their levels of sophistication. Backer (1971) also compares the information needs of bankers and financial analysts, through in-depth interviews. He finds that although both groups use financial statements as a source of information, these two user groups have different information needs regarding contribution margin reporting, segment reporting, profit forecasts, interim reporting, and balance sheet values.

Other creditors (such as suppliers and trade creditors) usually provide goods and capital to a business entity. They generally require financial information to assess the likelihood that the amounts owed to them will be paid on time. However, there is a lack of research evidence regarding the information needs of this group.

Overall, it appears that, as with equity investors, debt investors also rely on the financial statements, but their emphasis regarding what information is needed is driven by the different purposes for which their decisions are made.

5.4 Summary of literature

Previous research focuses mainly on the needs of equity investors and to a lesser extent on those of debt investors and other creditors. There is undoubtedly evidence in previous research about the decision-usefulness of financial reports and about their important role in the accountability process. Main findings of previous research indicate that professional investors are more heavily reliant on financial statements than individual investors. They require that accounting policies that are easy to find, and disclosures that are company-specific with a useful level of detail. Bankers, on the other hand, value information differently and specify different information needs regarding contribution margin reporting, segment reporting, profit forecasts, interim reporting, and balance sheet values. The previous literature also highlights the call from users for prospective performance information about reporting firms. Increasingly, there is also evidence of a need for summarised reporting and meaningful management commentary on reporting firm performance.

Overall, however the literature on user information needs suggests that up-to-date, transparent, entity specific and future-oriented information is preferred by individual investors, investment professionals and bankers alike. There is a notable absence of more recent research, highlighting the importance of this research project.

6. Methodology

The research project was undertaken in three distinct stages:

6.1 Literature review

This first stage reveals that most user-needs studies were conducted in developed countries including Australia, the United Kingdom (UK), the United States of America (US), and the European Union (EU). There are very few studies researching New Zealand users, a factor which emphasises the importance of the second stage of this research project, namely the empirical research regarding user needs in New Zealand.

6.2 Survey of key user groups

The second stage began with the development of an online questionnaire to assess the information needs of users within each of the primary user groups identified in the previous section.

Before launching the online survey, a pilot test of the questionnaire was conducted to eliminate, as far as possible, any potential issues such as ambiguity or bias.

The questionnaire was launched online using Qualtrics, a leading provider of online research software. In theory, this enabled us to make the survey accessible to the entire population of GPFR users in each of target user groups identified earlier. The questionnaire was identical for all user groups. A variety of approaches were used to reach the different user groups and encourage high response rates:

- Links to the survey were publicised through various digital and print media channels to attract individual equity/debt investors that included Facebook, LinkedIn, New Zealand Herald, interest.co.nz, a press release on line, and hard-copy community newspaper;
- Email invitations were sent to shareholders of the top 100 entities listed on the NZX Limited (NZX), as well as to bank lending officers in major banks in New Zealand (e.g., ANZ Bank, ASB Bank);
- Email invitations were also sent to advisors, brokers, and fund managers within leading firms offering these services;
- Assistance was sought from various professional organisations to access their members such the Shareholders Association, Chartered Financial Analysts, and the Institute of Finance Professionals New Zealand; and
- Email invitations were sent to major regulators of New Zealand capital markets (i.e., the Financial Markets Authority (FMA), the Reserve Bank of New Zealand (RBNZ) including NBDT supervisors, and NZX).

The final sample consists of 145 responses, including 45 investors, 22 lenders, 70 intermediaries, and 8 regulators. However, most respondents have multiple roles. Table 1 shows respondents' average self-rated knowledge and skills, and level of experience. On average, the respondents have above average levels of knowledge, skills, and experience in reading, understanding and analysing financial statements (3.7 out of 5).

Table 1: Participants' knowledge, skills and experience

	Investors	Lenders	Intermediaries	Regulators	Overall
Average self-rated knowledge and skills (1- 5)	3.6	4.1	3.7	3.4	3.70
Average experience rating	3.5	4.1	3.8	3.4	3.71
Number of responses	45	22	70	8	145

Table 2 shows the extent to which respondents are involved in either domestic or international markets, or both. About three quarters of the participants have interests in both domestic and international markets, 23% are interested in entities operating solely in the domestic market, and only over 1% of the participants are interested in entities operating solely in the international market.

Table 2: Participants' interest in domestic and international markets

<i>Interest</i>	Investors		Lenders		Intermediaries		Regulators		Overall	
	<i>%</i>	<i>Responses</i>	<i>%</i>	<i>Responses</i>	<i>%</i>	<i>Responses</i>	<i>%</i>	<i>Responses</i>	<i>%</i>	<i>Responses</i>
Domestic	24.4%	11	54.6%	12	11.4%	8	25.0%	2	22.8%	33
International	4.4%	2	0.0%	0	0.0%	0	0.0%	0	1.4%	2
Both	71.1%	<u>32</u>	45.5%	<u>10</u>	88.6%	<u>62</u>	75.0%	6	75.9%	<u>110</u>
Number of responses		45		22		70		8		145

In order to gain further insights and a deeper understanding of users' information needs, in-depth interviews were conducted with 10 selected representatives of the four identified primary user groups, as well as sub-classifications of these groups. Interviewees included an individual investor, three lenders, a sell-side and a buy-side analyst, and each of the regulatory bodies (RBNZ, FMA, NZX and NBDT supervisor). The interviews were based on the interviewees' earlier responses to the online questionnaires. Each interview was about an hour in length, allowing the researchers to ask open-ended "why" and "how" questions to supplement the limited information available from closed questions of the online questionnaire. All interviews were recorded and transcribed with the consent of the interviewees.

6.3 Results analysis

The final stage of this research project compares the results of the above survey with the information needs of users in international markets, as identified in the literature review.

7. Survey Results

There are 13 questions in the questionnaire used in this study: Questions 1–9 explore the usefulness of financial statements and what other sources of information are used in making decisions. Respondents who indicate that they do not use corporate financial reports in Question 1, automatically skip to Question 7, as the questions on usefulness of financial statements are irrelevant to them. Questions 10–13 relate to the background information of the participants. A sample questionnaire is provided in [Appendix 3](#).

Questions 3 and 9 use a Likert scale of 1 to 5, where 5 indicates the most important, and 1 indicates the least important. The arithmetic mean is used to generalise as to the degree of importance indicated by users for these questions (e.g., a factor with a mean of 4-5 indicates high importance, 3 indicates reasonably important, and 1-2 low importance).

Q1. Use of financial reports

In Question 1, participants are asked to indicate whether they use the information in corporate financial reports in their decisions relating to investments and/or corporate performance. Table 3 shows the extent of usage of financial reports by each user group. Overall, a significant majority of respondents (79%) gave a positive answer to this question.

The proportion of intermediaries (74%) who use financial reports is slightly lower than other user groups. Most of those who indicated that they are not using financial reports, explained that they relied on information provided by in-house analysts or research teams, who analyse annual reports in depth rather than directly referring to financial reports (10 respondents in the intermediary group replied in this manner). Two respondents also stated that they use managed funds and therefore do not need to rely on financial reports. Only one intermediary stated that he was not using financial statements and had a rather negative view of them. While these views may not be widely shared, they contain important insights of some negative perceptions relating to the corporate financial report:

“Not really as it is too out of date and too variable and unknown as to basis of preparation. Also accountants and business try to hide or accentuate different things that reflect the story they wish to portray. All this makes them hard to understand and believe. Hardly, the financial reports can provide the basis for sound and prudent investment decisions at a business buying level or a share market level. Mainly though they are simply too out of date in the modern communications world to be relevant.”

The 18% of individual investors who do not use financial reports and responded to this question also had rather negative views about financial statements. Explanations included contentions that financial reports were of “no value” as they are too lengthy, too complex, convoluted in layout and terminology, hid important information and were filled with avoidance and ambiguity. One respondent in this category stated that they use financial advisors to make their investment decisions on their behalf.

Lenders and regulators that participated in this survey and commented on the reasons for not using financial reports stated that examining financial reports are not part of their work portfolios.

Table 3: Usage of financial reports by user groups

Usage	Investors		Lenders		Intermediaries		Regulators		Overall	
	%	Responses	%	Responses	%	Responses	%	Responses	%	Responses
Yes	82.2%	37	86.4%	19	74.3%	52	87.5%	7	79.3%	115
No	17.8%	8	13.6%	3	25.7%	18	12.5%	1	20.7%	30
Total %/ Responses	100%	45	100%	22	100%	70	100%	8	100%	145

Q2. Types of decisions for using financial reports

Respondents who answered “yes” to Question 1 were asked to indicate for what types of decisions they used financial reports and to allocate 100% between the types of decisions to indicate the importance of each.

Table 4 below shows the average percentage (level of importance) allocated to the various types of decisions by each user group. A majority of investors use financial reports for equity investment (64%), and a majority of lenders use financial reports for lending or extension of credit (71%). Intermediaries mainly use financial reports for equity investment and debt investment (50% and 26%, respectively), and regulators mainly use financial reports for monitoring financial soundness, monitoring regulatory compliance and consistency of published data with corporate reporting returns, and assessing financial risk and performance. Consistent with prior studies (e.g., Backer, 1971; Chenhall & Juchau, 1977; Benjamin & Stanga, 1977; etc.), our results indicate that different user groups use financial reports for various types of decisions with different information needs.

Table 4: The types of decisions for which financial reports are used

	Average level of importance				
	Investors	Lenders	Intermediaries	Regulators	Overall
Equity investment	64.1	6.0	50.0	7.1	44.7
Debt investment	8.2	5.8	26.2	3.6	15.7
Lending or extension of credit	1.2	70.8	4.7	0.0	14.2
To monitor/assess performance for governance	11.4	8.3	4.6	25.7	8.6
To monitor/assess performance for management	10.8	9.1	8.9	23.6	10.4
Other	4.3	0	5.6	40.0	6.4
Total %	100%	100%	100%	100%	100%
Total number of responses	37	19	52	7	115

Q3. Usefulness of components of financial statements

Respondents to this question were asked to assess the usefulness of each financial statement component in making decisions, using the scale 1 to 5, where 5 is the most useful, and 1 is the least useful. Table 5, Panel A shows the average rating for each of the financial statement components and the explanatory notes while Panel B shows the proportion of participants who rated the financial statement components as 4 or 5 (highly useful).

The findings are reasonably consistent across user groups and indicate that all financial statement components are rated as useful (3 or more). Consistent with an Australian study by Anderson (1981), the statement of profit and loss, and the statement of financial position are ranked as the two most useful statements (4.3). These are followed by the cash flow statement (3.9), and notes to the financial statements (3.8), with the statement of changes in equity rated as least useful (3.0). These findings are consistent with the results in Panel B which shows the proportion of respondents who rate the financial statements as highly useful.

Table 5: Usefulness of components of financial statements

Panel A: Average score

	Investors	Lenders	Intermediaries	Regulators	Overall
	<i>Average</i>	<i>Average</i>	<i>Average</i>	<i>Average</i>	<i>Average</i>
Statement of financial position	4.2	4.6	4.1	4.4	4.3
Statement of profit or loss and other comprehensive income	4.2	4.9	4.3	4.3	4.3
Statement of changes in equity	2.7	3.4	3.1	2.6	3.0
Statement of cash flows	3.8	3.9	4.1	2.6	3.9
Notes to the financial statements	3.7	3.8	3.8	3.6	3.8
Number of responses	37	19	52	7	115

Panel B: The proportion of participants who rated the usefulness of components of financial statements as 4 or 5

	Investors	Lenders	Intermediaries	Regulators	Overall
	<i>%</i>	<i>%</i>	<i>%</i>	<i>%</i>	<i>%</i>
Statement of financial position	83.78	94.74	86.54	71.43	86.09
Statement of profit or loss and other comprehensive income	83.78	100.00	88.46	85.71	88.70
Statement of changes in equity	27.03	47.37	32.69	28.57	33.04
Statement of cash flows	72.97	73.68	78.85	42.86	73.91
Notes to the financial statements	56.76	73.68	65.38	28.57	61.74
Number of responses	37	19	52	7	115

We also assessed the associations between these usefulness scores and the levels of knowledge and skills, and experience of participants in reading, understanding, and analysing the financial statements. Figure 1 shows the significant associations (Spearman's

rank correlations with $p \leq 0.05$)¹² using bi-directional arrows for the total sample, individual investors, lenders and intermediaries.

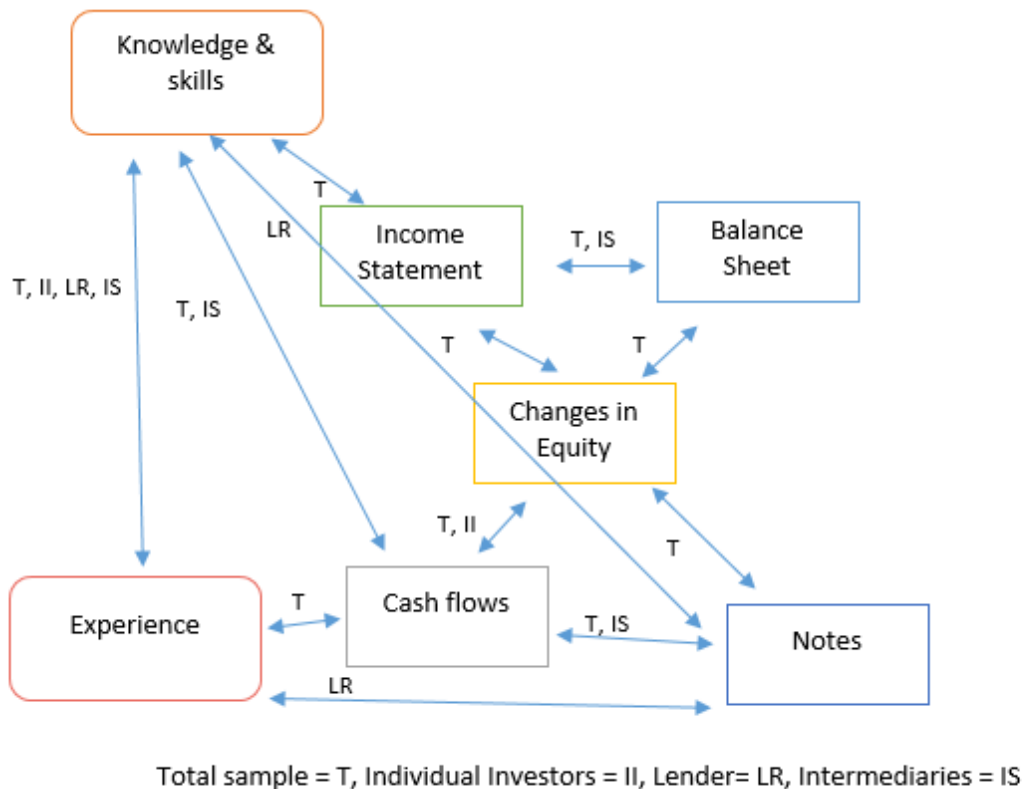
In the total sample, the usefulness of the income statement is positively correlated with users' knowledge and skills; while the usefulness of the cash flow statement is positively correlated with users' knowledge and skills, as well as experience. It is interesting to find that the usefulness of the balance sheet is positively correlated with the usefulness of income statement, and that the usefulness of cash flow statement is positively correlated with the notes to the financial statements. These relationships indicate that users integrate various components of the financial statements and find them complementary to each other. Further, the more knowledgeable and experienced the user the more useful the income statement, cash flow statement, and notes.

For the investor group, the usefulness of the balance sheet is positively correlated with the usefulness of the income statement, and the usefulness of the cash flow statement is positively correlated with changes in equity. For the lender group, the usefulness of the notes is positively correlated with users' knowledge and skills while for the intermediary group, the usefulness of the cash flow statement is positively correlated with users' knowledge and skills. This suggests that the usefulness depends on the roles of users and their knowledge and experience.

These findings are consistent with Lee and Tweedie (1975b), Bartlett and Chandler (1977), and Elliot et al. (2008), where the results indicate that the usefulness of financial statements is associated with users' accounting sophistication. The more knowledgeable and experienced the user, the more likely they would be able to read, understand and analyse the financial statements.

¹² Spearman's rank correlation coefficient is a measure of the relationship between two variables.

Figure 1: Significant associations between usefulness scores of components of financial statements and also participants' knowledge and skills, and experience



Q4. Information provided in financial statements but not useful to users

Table 6 describes the extent to which respondents indicate that financial statements included information which was not useful to them.

Most of the 24% of respondents who indicate that there is information in financial statements which is not useful to them, make reference to the notes to the financial statements. Examples include comments on the length of these notes and perceptions that this detracts from the usefulness of other more relevant information, and suggestions that some notes could be simplified, or that the notes should be placed online only. These comments are consistent with CFA UK (2015) that financial reports may contain irrelevant, excessive, and redundant information and omit some important information.

However, most respondents (76%) indicate that all information in financial statements was useful. Comments illustrating these views include: “all helps to build a picture”, “best to get more disclosure rather than less”, “not merely what is there, but what can be inferred is highly relevant”, “a lot of the information is not used, but it is reassuring to know that it is available and that management have had to follow due process / standards in preparing the financial statements”. These findings are consistent with literature on decision-usefulness and stewardship role of financial statements (Kothari et al., 2000).

Table 6: Information in financial statements that is not useful

	Investors		Lenders		Intermediaries		Regulators		Overall	
	%	Responses	%	Responses	%	Responses	%	Responses	%	Responses
Yes	40.5%	15	15.8%	3	13.5%	7	42.9%	3	24.3%	28
No	59.5%	22	84.2%	16	86.5%	45	57.1%	4	75.7%	87
Total %/ responses	100%	37	100%	19	100%	52	100%	7	100%	115

Q5. Information not provided in financial statement that would be useful to users

Table 7 describes the extent to which users indicate that there is useful information which is not provided in financial statements.

Most investors (73%) and lenders (53%) indicate they require information that is not currently included in the financial statements. In contrast, most intermediaries (75%) and regulators (57%) indicate the opposite.

Individual investors, unsurprisingly, focus on performance of their investments, suggesting that companies should provide information about future performance, particularly as compared to earnings targets and budgets, would be a helpful addition to conventional financial statements. Further comments suggested include: earnings projections; earnings outlooks; information about debt covenants; enhanced segment reporting; and information about sales margins and business activity. These suggestions are consistent with prior studies that investors are primarily interested in information about the future prospects of the firm, and suggestions that companies should disclose budgetary data, such as earnings forecasts and cash flow forecasts (Baker & Haslem, 1973; Lee & Tweedie, 1975a; Chenhall & Juchau, 1977). Three respondents in this group saw information on hedging strategies and financial contracts, as well as off-balance sheet exposures, as desirable additions to the current information content of financial statements. Two respondents also suggest that more information about executive remuneration would be useful.

Lenders suggest more detailed cash flow information as well as additional details regarding loans, terms of borrowing, security over borrowing and credit facilities. They also indicate a need for more narratives to accompany earnings regarding the business events that affect financial results, more detail about earnings and expenses, some key performance ratios as well as details about the solicitors and accountants involved with the company. These findings align with prior literature (Armstrong et al., 2010; Kothari et al., 2010) in that lenders focus on debt and debt related information as well as the earnings potential of companies.

Similar to CFA UK (2015), which suggests that disclosure of risk and uncertainties need to be improved in the annual reports, we find that intermediaries who indicate a need for additional information to be included in financial statements tend to value future oriented information, such as projections and forecasts. Other suggestions from these intermediaries

include additional disclosures on debt cost and debt covenants, segment information, and sustainability matters.

Regulators suggest that additional information about securities on issue, share allotments, net asset positions, and historic as well as current financial ratios would be of benefit. One respondent in this category suggests that disclosures are often incomplete, particularly when it comes to financial instruments and that this should be a focus for improvement efforts.

Table 7: Information not provided in financial statement that would be useful

	Investors		Lenders		Intermediaries		Regulators		Overall	
	%	Responses	%	Responses	%	Responses	%	Responses	%	Responses
Yes	73.0%	27	52.7%	10	25.0%	13	42.9%	3	46.1%	53
No	27.0%	10	47.3%	9	75.0%	39	57.1%	4	53.9%	62
Total %/ Responses	100%	37	100%	19	100%	52	100%	7	100%	115

Q6. Improving information

Respondents were then asked if they had any other suggestions for improving financial statements.

Individual investors generally suggested simplification and standardisation of reporting so that the performance results could be easily compared between companies. Generally, the respondents in this category indicate that IFRS unnecessarily complicates the presentation of financial statements. Suggested improvements include improving transparency, particularly regarding contingencies, guarantees, obligations and related parties transactions. Further suggestions are to aggregate common information to highlight items of material importance, include key performance indicators, and five year comparatives and forecasts.

About half of the responding lenders had no further suggestions for improvements while the other half suggested that greater consistency in formatting and presentation of financial statements would be desirable.

Most intermediaries (58%) had no further suggestions for improvements of currently prepared financial statements. Consistency and transparency in financial reporting, as well as normalisation of reported earnings are common suggestions from intermediaries who did make comments. Other suggestions include: that data published in the financial statements should be presented as a one page snapshot including forecasts; that directors' reports be expanded; additional information about equity and debt ratios; better disclosure of the business model; more cross-referencing of information in the financial statements; discussion of valuations; greater emphasis on cash flows; more commentary about industry,

company prospects, market share and competition; commentary on ethical matters; and simplified terms and bullet points to help the layperson's understanding.

Regulators suggest that simplification of the language used in financial statements, more structured and consistent reporting and disclosures between companies, and improvements to timeliness of published information would be welcome additions to current reporting requirements.

These findings are broadly consistent with those of PwC (2014a, 2014b), in particular, the suggestions for improvements regarding simplification, standardisation, and transparency of current financial reporting.

Q7. Sources of information

This question sought to determine what key sources of information were used in making decisions. Participants were asked to allocate 100% between these sources of information to indicate their relative importance. Table 8 summarises these results by reporting the users' average percentage of importance for each source of information.

Overall, advisors and analysts reports are rated as the most important source of information (34%), a finding driven by the two largest user groups, namely investors and intermediaries (30% and 47%, respectively). Similarly, corporate financial statements are ranked second overall (30%), as well as by the investor and intermediary user groups (23% and 23%, respectively). This is consistent with both Baker and Haslem (1973) and Curtis (1982), with respect to their finding that US and Australian individual investors considered stockbrokers and advisory services as the most important sources of information for investment analysis; but not with respect to their finding that financial statements are perceived as being of minor importance. Different to Bartlett and Chandler (1977), who find that annual reports are not widely read by UK private shareholders, the results of this study, however, support the findings of another more recent survey conducted by EFRAG (2009) which found that most users in European countries consider financial statements as one of the most useful sources of financial information. Therefore, the findings of this study and other more recent studies such as EFRAG (2009) indicate the increasing sophistication of individual investors over the last 30 years when using financial statements.

Both of the other two user groups (lenders 60%; regulators 46%), however, ranked corporate financial statements as their most important source of information. This result is likely due to the differences in sophistication levels between lenders and regulators on the one hand as compared with investors and intermediaries on the other (e.g., Question 12 shows that lenders' average knowledge and skills (4/5) and experience (4/5) are higher than those of investors (3.6/5 and 3.5/5 respectively)).

Regulators ranked other sources as next most important (33%). The other sources include interactions with management and boards of governance, private reports, and other confidential and sensitive information. An important observation in this regard is that regulators have the power to demand information from corporates. Lenders often have

similar powers, however most other users of GPFR do not have this ability. The findings below are therefore somewhat counter-intuitive and ironic, as those who have greater power to demand private information appear to place greater reliance on GPFR.¹³ However, a possible explanation is that regulators rely on more regular private reports and information and use GPFR to confirm the information from private reports. The confirmatory role of financial statements were mentioned by a number of interviewees.

Table 8: Sources of information

	Investors	Lenders	Intermediaries	Regulators	Overall
	<i>Average</i>	<i>Average</i>	<i>Average</i>	<i>Average</i>	<i>Average</i>
Corporate financial statements	23.0	60.3	23.1	46.3	30.0
Management commentary and analysis including directors' reports	20.7	17.0	16.1	12.5	17.4
The press, media and other on-line source	16.4	8.0	9.7	4.4	11.2
Advisors and analysts reports	30.1	11.9	46.8	3.8	33.9
Others	10.5	3.0	4.4	33.1	7.7
Total %	100%	100%	100%	100%	100%
Number of responses	45	22	70	8	145

Q8. Interest in supplementary information

All respondents were asked whether they require supplementary information that is currently not included in financial reports. Table 9 shows the level of interest in supplementary information.

The majority of investors (64%), lenders (55%), and regulators (75%) indicate a need for such supplementary information. In contrast, only 31% of intermediaries indicate such a need.

Table 9: Interest in supplementary information

	Investors		Lenders		Intermediaries		Regulators		Overall	
	%	Responses	%	Responses	%	Responses	%	Responses	%	Responses
Yes	64.4%	29	54.55%	12	31.43%	22	75.0%	6	47.6%	69
No	35.6%	<u>16</u>	45.5%	<u>10</u>	68.6%	48	25.0%	<u>2</u>	52.4%	<u>76</u>
Total	100%	45	100%	22	100%	70	100%	8	100%	145

¹³ As noted in Section 2, the user-needs approach is based on the primary principle that GPFR should "... provide information to external users who have a need for an entity's financial statements but are unable to demand them" (XRB, 2012, p. 22).

Q9. Usefulness of supplementary information

If the respondents answered yes to Question 8, they were then asked to indicate the level of usefulness of supplementary information types in the financial statement, using a scale of 1 to 5, where 5 indicates the most useful information, and 1 indicates the least useful information. Table 10, Panel A shows the extent of usefulness of the various types of information while Panel B shows the proportion of participants who rated this information as highly useful (4 or 5).

Overall, respondents rank all supplementary information types as being useful (>3), with the most useful being business strategies and future prospects (4.4), followed by narratives that explain financial performance and position of a reporting entity (4.2). This is consistent with the proportion of respondents who rated this information as highly useful in Panel B.

Table 10: Usefulness of supplementary information

Panel A: Average score

	Investors	Lenders	Intermediaries	Regulators	Overall
	<i>Average</i>	<i>Average</i>	<i>Average</i>	<i>Average</i>	<i>Average</i>
Information about entity's business	3.3	4.3	3.9	2.8	3.6
Narratives that explain entity's performance and financial position	4.3	4.8	4.0	3.3	4.2
Information on business strategies, and prospects for future financial years	4.4	4.4	4.4	3.8	4.4
Summary financial information	3.3	3.8	3.6	2.3	3.4
Others	1.7	1.2	1.1	1.0	1.4
Number of responses	29	12	22	6	69

Panel B: The proportion of respondents interested in supplementary information who rated it as highly useful (4 or 5)

	Investors	Lenders	Intermediaries	Regulators	Overall
	<i>%</i>	<i>%</i>	<i>%</i>	<i>%</i>	<i>%</i>
Information about entity's business	55.17	91.67	77.27	33.33	66.67
Narratives that explain entity's performance and financial position	82.76	100.00	68.18	66.67	79.71
Information on business strategies, and prospects for future financial years	75.86	91.67	86.36	83.33	82.61
Summary financial information	48.28	66.67	63.64	0	52.17
Others	20.69	8.33	22.73	16.67	18.84
Number of responses	29	12	22	6	69

8. Additional analysis

Additional statistical analysis was conducted to assess if there are significant differences among the user groups, and between domestic and international users.

8.1 Comparing users with non-users of financial statements

We compared the skills and knowledge, and experience with users and non-users of financial statements. Table 11 shows this comparison and indicates users' average knowledge, skills and experience are significantly higher than non-users for all user groups and the total sample.¹⁴

Table 11: Comparing knowledge, skills and experience of users and users of financial statements

	Investors	Lenders	Intermediaries	Regulators	Overall
	<i>Average</i>	<i>Average</i>	<i>Average</i>	<i>Average</i>	<i>Average</i>
Knowledge and skills:					
– Users	3.78	4.16	3.92	3.43	3.89
– non-users	2.88**	3.33**	3.00***	3	3.00***
Experience:					
– users	3.76	4.16	3.92	3.43	3.88
– non-users	2.50***	3.33**	3.28***	3	3.07***
Number of responses:					
– users	37	19	52	7	115
– non-users	8	3	18	1	30

Significant level at 0.01***, 0.05**, 0.1*

We also compared the information sources of users and non-users of financial statements. Table 12 provides this comparison and indicates that users of financial statements source their information significantly more from financial statements and management commentary and analysis, while the non-users of financial statements (except lenders) rely significantly more on advisors and analysts reports.¹⁵

¹⁴ T-tests were conducted to compare the mean differences of knowledge, skills, and experience between users and non-users of financial statements.

¹⁵ T-tests were conducted to determine the significance level of the mean differences between users and non-users of financial statements about information sources.

Table 12: Comparison of sources of information for users and non-users of financial statements

	Investors <i>Average</i>	Lenders <i>Average</i>	Intermediaries <i>Average</i>	Regulators <i>Average</i>	Overall <i>Average</i>
Corporate financial statements					
– User	27.43	72.37	30.15	40.00	36.85
– non-user	2.50***	18.33***	4.44***	90.00	8.17***
Management commentary and analysis including directors' reports					
– User	23.92	20.68	21.29	13.57	21.57
– non-user	5.63***	11.67	5.00***	5.00	5.83***
The press, media and other on-line source					
– User	16.07	8.95	9.96	4.29	11.33
– non-user	17.86	11.67	9.17	5.00	11.00
Advisors and analysts' reports					
– User	23.32	14.05	42.73	4.29	29.41
– non-user	61.25***	18.33	64.17**	0.00	56.67***
Others					
– User	9.51	4.11	4.23	37.86	7.87
– non-user	15	10	6.11	0.00	8.33
Number of responses					
– User	37	19	52	7	115
– non-user	8	3	18	1	30

Significant level at 0.01***, 0.05**, 0.1*

8.2 Comparing users operating in domestic vs international markets

T-tests¹⁶ were conducted to compare the mean differences between respondents who are interested in the domestic market only ('Domestic users' – 33 subjects), and those who are also interested in the international market ('International users' – 112 subjects)¹⁷. However, the mean differences are not significant between the two groups. The exceptions are two exceptions, (1) regarding types of decisions for using financial statements, domestic users are more likely to use financial reports for lending decisions than international users, and (2) for sources of information, international users are more likely to use advisors and analysts' reports than domestic users.

¹⁶ A t-test is a statistical hypothesis test used to assess if two sets of data are significantly different from each other.

¹⁷ The international market group is made up of all the participants who have interest in international markets in addition to the domestic market (110 subjects) or the international market only (2 subjects).

8.3 Comparing the primary user groups

A one-way ANOVA¹⁸ was conducted to compare primary user groups. The results show that primary user groups use financial reports for a diverse range of decisions which reflect their interests. For example, investors and intermediaries use financial reports mainly for equity investment, but intermediaries also use financial reports for debt investment. Lenders use financial reports mainly for lending or extension of credit, while regulators use financial reports mainly to monitor performance for governance and other purposes. Lenders are also more reliant on corporate financial statements than the other groups. Intermediaries and investors are more reliant on advisors and analysts' reports than lenders and regulators. In terms of the components of the financial reports, the mean score for the usefulness of the cash flow statement for intermediaries is significantly higher than the other three groups. Further, lenders rated 'information about the entity's business' more highly, than did the other groups. The mean score for information 'not provided in financial reports that is useful' is much lower for the intermediary group than for the other three groups, while the mean score is significantly higher for the investor group, indicating that investors seek more while intermediaries demand less additional information which is not currently provided in financial reports. The mean scores for 'not useful information' on the other hand, are significantly higher for investors and regulators than for lenders and intermediaries.

Overall the ANOVA results support the previous main findings of the study. These results also opened matters for discussion with a selected number of interviewees. Ten interviews were conducted with representatives from each of the user groups, including individual investors, lenders, sell- and buy-side analysts, and users with oversight/regulatory functions so to gain further insights and a deeper understanding of users' information needs,

9. Vignettes of usage of financial statements

Interviews were conducted with a range of users to gain insights into their views on and usage of financial statements. These users comprise: an individual investor, buy and sell-side financial analysts, business lenders and regulators.

9.1 Individual investor

INV is an individual investor focusing on small capital market entities primarily in New Zealand and Australia, although Australia is a major focus because of the size of the market. Currently, his portfolio is about three quarters Australian and one quarter New Zealand. INV keeps a watch list of about 100 entities. He manages his own portfolio of investments and engages in about 250 buy and sell transactions annually. His investment portfolio is about 90% equity and 10% debt instruments although sometimes he increases his debt investment if the equity market is unattractive. He avoids investment in volatile industries such as

¹⁸ Analysis of variance (ANOVA) is a statistical model used to analyse the differences among group means and variation" among and between groups. It provides a statistical test of whether or not the means of several groups are equal, and therefore generalizes the t-test to more than two groups.

mining and includes property companies because of their stable performance. His intention is to be a long-term investor, but he reacts to market movements and sentiments. He has held investments for as long as 10 to 15 years, but not recently as he is not comfortable in the current equity market.

INV uses financial statements in managing his investment portfolio. He rates the cash flow statement as the most useful component of financial statements, followed by the profit and loss statement and notes to the financial statements. He does not regard the balance sheet as useful, particularly with the various valuation methods used. However, he does review the balance sheet to look at the extent of liabilities (leverage), calculate the current ratio, and to confirm the quality of cash.

INV describes himself as an investor who is looking for earnings surprises: financial statements are useful in this respect for developing future predictions. When he considers earnings he looks at whether they are backed up by cash flows. He looks at the underlying earnings and strips out extraordinary items and other one-off items when constructing his discounted cash flow models. He attempts to forecast the future performance of his investments by using financial statements. He believes that: "You can't get a good short-term investment outcome unless you've got a good long-term story."

INV reads parts of the notes to the financial statements as they provide further insights. He is not concerned about the volume of the notes as he skims through most of them. He reads the audit report and looks for going concern issues. INV does not look at the statement of changes in equity as it does not provide him with additional insights.

In managing his investment portfolio INV uses a variety of information sources, about a third from financial statements, a third from management commentary and analysis, and a third from media reports. He also interacts with other individual investors through social media groups. He regards financial statements as valuable even though not timely because they provide confirming information. He believes that financial reporting keeps management honest.

INV finds information about the business, management strategy, and narratives that explain performance useful as this information contextualises reported earnings and forecasts. He believes that: "Investment in capital markets is not about what is going on now, but it is based on a best guess for the future."

INV is a sophisticated user of financial statements in the management of his personal investment portfolio of New Zealand and Australia shares.

9.2 Bank commercial lending manager

BAM is a bank manager at a regional city with 18 years' experience. His key role at the bank involves reviewing and analysing financial statements to understand and establish whether his clients are borrowing propositions that the bank would be willing to undertake. He manages 90 clients with borrowings between \$0.5 million to \$3 million. In his lending decisions, BAM considers three factors: people (their trustworthiness, their management

experience); security (whether there is sufficient security for the borrowings); and the financial statements to assess serviceability of the debt by the borrower.

The bank requires regular reporting by clients. As a manager, BAM monitors and assesses clients and to do so, he uses the balance sheet and focuses on the equity section. He also uses the balance sheet to assess how the client would be able to withstand adversity. He assesses changes in retained earnings and the working capital position. In the profit and loss statement he considers earnings before tax, depreciation and amortisations to assess the ability of a client to repay the debt with cash available for servicing the debt. He also assesses whether there have been material movements in gross margins. The higher the amount of borrowing, the more comprehensive and rigorous his analysis becomes. For cash flows, the bank systems create cash flow statements, particularly for clients who do not prepare such statements.

BAM uses the information in the financial statements of his clients and information from other sources in making lending decisions.

9.3 Bank property lending manager

At the time of the interview, PLM was a manager at a major bank in a large city specialising in commercial property lending of over \$2 million. He has a long career in the finance industry dating back to the early 1980s. His role was the funding of either construction or long-term investment of commercial properties such as shopping centres or office buildings. The majority of his clients were highly geared (up to 50%). Apart from the property valuation, the annual accounts were his most important source of information. All clients are required to provide their annual accounts for an annual review of their risk ratings and how they perform against budgets. The bank also requires clients to provide detailed information as part of the loan document.

The profit and loss statement is the first financial statement component which PLM reviews on receiving the financial statements, focusing initially on the bottom line. He considers the movements in expense items. He reviews the notes to the financial statements to obtain more detailed information. The balance sheet is also important to him, as it shows the level of debt. He uses the cash flow statement to project future cash flows.

PLM is a user of the financial statements of his clients in making commercial property lending decisions. He uses all the information in the financial statements to assess the initial and ongoing ability of his clients to service their borrowings. In particular, accurate and timely financial statements are necessary to annually measure clients' compliance with two key loan covenants, namely interest cover (IC) and loan to value ratio (LVR). These two covenants are common to all commercial and property loan facilities provided by banks.

9.4 Financial analyst: sell-side

FAS is an Equity Analyst with a large investment firm. He has been a stock broker and equity analyst for 19 years and also had three years' experience analysing debt securities.

He has commerce and law qualifications. FAS is tasked with valuing listed companies and, on the basis of these valuations, recommending portfolio positions in New Zealand equities for institutional and overseas investors. His key role is to make calls on whether or not a stock is market weight, over, equal or under. If a stock is market weight the institutional investor should hold an index weighting. This work sounds relatively simple, but it involves a reasonable amount of trawling through financial reports. It also involves talking with competitors, regulators, suppliers, and the company executives to get an idea of where the earnings and, more importantly, the cash flows of the companies are going in order to value that company. It is an institutional, wholesale role as he does not directly deal with 'mum and dad' investors.

FAS works for one of the largest brokers in the country. FAS is a 'sell-side analyst' (i.e., a broker) as opposed to a 'buy-side analyst' (i.e., responsible for analysing an equity investment as a fund manager). On average, a New Zealand sell-side analyst like FAS would probably monitor approximately ten stocks. Companies report on a semi-annual basis and every time they do that, FAS updates his financial forecasts and re-casts his evaluation. Often he re-casts more frequently than that depending on what other information is coming out on companies which he is monitoring. In simple terms, he uses financial statements at least 20 times a year to recalibrate free cash flow forecasts.

FAS distils company information down to the cash flows that are available to pay a dividend or pay down debt, i.e., free cash flow. The cash flow statement is therefore more interesting to him than other financial statement components. As regards the profit and loss statement, he believes earnings can be distorted through a number of means, depreciation being a classic example where there is a great deal of flexibility around how quickly or not companies can depreciate assets. Similarly, provision movements and revenue recognition may distort earnings particularly, in the former case, of companies that are continuously restructuring but take those charges below the line. FAS indicates that he does not obtain much information from the movement in equities statement. However, he rates the balance sheet as critical because he needs to understand the face value of debt rather than the reported debt numbers and the notes to the financial statements explain that. Other items in the balance sheet alert him to debt that is quickly coming to maturity and provide him with insights about refinancing costs or benefits. One of the things that he spends a lot of time doing is reconciling earnings back to operating cash flows. He does so by using the earnings in the profit and loss statement to distil this and reconcile it back to the reported operating cash flow, attempting to net out and understand the non-cash movements.

FAS, as a sell-analyst with a major broker uses primarily the information in the cash flow statement and the balance sheet in developing and revising his valuation models of shares.

9.5 Financial analyst: buy-side

BYI is an analyst with a major institutional investor with substantial investment in the New Zealand and overseas markets. He has been an analyst for over 15 years and has spent

six years with his current employer. He describes his role as developing and refining financial models based on information in the financial statements. As soon as financial statements are released he combs through them and compares them to what he would have anticipated the company would achieve in terms of its earnings and the state of its balance sheet and cash flows. He uses that information to forecast forward and form a view of value on that basis. Refinements to his financial models are assisted by information he obtains from meetings with chief executives of the companies they invest in, his own research and research from third parties including share brokers.

BYI's valuation models typically start with valuing the firm and then deducting the value of debt to arrive at the value of equity. BYI always starts his analysis with the profit and loss statement but the cash flow statement and the balance sheet (working capital and debt position) are important in assessing the quality of a company's earnings and its financial risk. He reviews the notes to the financial statements for further details, such as for depreciation and amortisation. He does not look at the Statement of Other Comprehensive Income as the details are frequently non-cash and not relevant for valuation purposes.

BYI is not convinced about the merits of fair value measurement as he feels it adds complexity and volatility to the financial statements and he is often not certain what the amounts actually represent. He prefers a balance sheet to be based on historical cost. Although he sees some value in the information based on fair values, his preference is that this information is provided in the notes rather than at the face of the balance sheet. He contends that when analysts value companies they ignore fair value adjustments in the financial statements.

9.6 Regulators

Three regulators have oversight responsibilities and use financial reports of New Zealand capital market entities, RBNZ, FMA and the NZX. In addition, trustees of non-bank deposit takers (NBDT) have oversight over finance companies and other non-bank deposit takers.

9.6.1 RBNZ

The RBNZ supervises about 25 registered banks and about 100 insurance companies operating in New Zealand. It has teams of supervisors for these two industries (about 15 bank and about 10 insurance supervisors). The RBNZ adopts a three pillars approach to prudential supervision: regulatory discipline, market discipline, and self-discipline. It has a disclosure regime which interfaces with financial reporting and audit to assist in monitoring liquidity and capital adequacy. Financial statements and other disclosures are used in assessing performance, assessing management, and assessing financial soundness. However, bank supervisors substantially rely on the monthly reporting returns which registered banks are required to provide privately to the RBNZ. The RBNZ is developing the systems for regular reporting by insurance companies and has recently launched a data collection system for quarterly information under the Insurance (Prudential Supervision) Act 2010. No bank or insurance entity operating in New Zealand has its own equity listed in New Zealand, so there is generally no continuous disclosure regime that applies to them.

However, there are a few regulated insurance entities that make up the majority of the business of a listed entity and therefore the listed entity would need to comply with continuous disclosure obligations.

The balance sheet is an important statement for the supervision of banks and the insurance industry. The balance sheet, with some adjustments, is the foundation for assessing capital requirements. However, for banks the monthly private reports have become more important than the annual financial statements. These monthly reports are reconciled with the annual financial statements to ensure consistency.

The notes are important. An interviewee commented: ‘the balance sheet with no notes is not very useful.’ The statement of changes in equity receives some attention: as an interviewee noted, ‘we look at it because we’re not otherwise told necessarily about payments of dividends or new issues of capital raising, so it just gives a little bit of an insight into that.’ The cash flow statement receives little attention as it shows the flows over the whole year. In the banking sector, the focus of the RBNZ is on the cash outflows over the next week or month, given the importance of liquidity risk for banks.

The RBNZ uses the annual financial statements and other monthly reporting to carry out its responsibilities in ensuring a sound banking and insurance industry in New Zealand.

9.6.2 FMA

The FMA’s remit covers issuers including the 200 NZX listed entities as well as other entities with public accountability, such as banks and insurers, building societies and those who have made an offer to the public at some point. The FMA promotes fair, efficient and transparent financial markets, including financial reporting, and in doing so they conduct thematic reviews and individual reviews. The FMA’s ongoing monitoring looks at a sample of listed issuers as well as some unlisted entities, but they also review the financial reporting of other listed issuers in response to complaints, or referrals from other FMA teams, auditor oversight reviews or other matters that come to their attention during the year. One of the FMA teams looks at new offers coming to market, so there is also review of financial reporting in the offer documents.

The FMA regards all aspects of the financial statements as useful in promoting fairness and transparency of the New Zealand capital market. There is some concern about the notes to the financial statements where there is a ‘tendency to include a lot of information that is not always useful to users of the financial statements.’ There is some concern about segment reporting where there is aggregation of information into single segments, which would be more useful if disaggregated so that users could better understand historical performance and also so that they are useful for forecasting performance. The FMA also observe notes to the financial statements that are not tailored for the business, for example: interest rates sensitivity disclosures which don’t seem to have any relevance, assumptions which don’t seem to make sense given current or recent economic conditions, and risk-management policies which are ‘boiler-plated’ and not well thought through. However, the FMA also observes examples of good disclosure, particularly the move

towards cutting clutter in financial statements which is encouraging. They note that there is a need to continue in this direction for a few more years.

The FMA takes the view that whilst there are improvements that can be made, overall financial reporting in NZ is in a good state.

9.6.3 NZX

NZX has a dual 'personality' in that it has oversight over companies listed on the stock exchange and is, itself, such a listed company (although the Special Division of the NZ Markets Disciplinary Tribunal oversees the activities of NZX as a listed company). For financial reporting the exchange is not required to exercise any particular oversight over the quality of reporting other than ensuring that listed companies provide the information required under the Listing Rules, which include requirements for financial statements. The financial information required for companies listed on NZX's securities markets includes preliminary half and full year financial statements, an interim report and an audited annual report.

NZX offers an archival service where data from financial statements is physically extracted and recorded on a database. This database feeds the information out to clients who subscribe for detailed financial data.

9.6.4 NBDT Supervisor

Under Part 5D of the Reserve Bank of New Zealand Act 1989, the RBNZ is charged with the enforcement of the credit rating and prudential requirements applying to non-bank deposit takers (NBDTs) in New Zealand that include finance companies, credit unions and building societies. NBDTs are required to have a trustee appointed and a trustee has to be a supervisor licensed by the FMA.

NBS worked as managing director for such a trustee and this firm supervises about 100 NBDT clients. The trustee has a responsibility to monitor the activities of each NBDT to ascertain whether it is compliant with the terms of its Trust Deed and with the terms of the offering documents under which it has raised money from others. Each NBDT has a number of requirements relating to liquidity ratios and capital ratios included in its trust deed. To perform its duties, the trustee requires a range of reporting from the NBDT and central to that reporting is financial information of which the annual financial statements form an important part. NBDT reporting requirements include monthly management reports (which are not required to be in compliance with GAAP) and certifications that they have complied with their trust deed, including the metrics and the various ratios.

In general, NBS views annual financial statements as giving a combination of a point in time snapshot of the financial position as well as the performance of an entity over a period. He focuses on the financial position in particular of the business, but also draws together how the business has performed over the previous year and uses that to compare against the other information he receives over the course of the year. NBS regards the cash flow statement as the most useful financial statement component. NBS notes that "it's always the cash flow statement that we turn to first" and that "profit's an opinion, cash is a fact."

10. Limitations

While the overall sample size of this study compares favourably with other studies, the relative sample size of each of the user groups represented in the study may influence the overall findings. For example, the 70 intermediaries represent 48% of the total sample and their views greatly influence the overall findings.

11. Conclusions

This report focuses on the information needs of key user groups of New Zealand Tier 1 for-profit entities, including investors, lenders, intermediaries, and regulators. An online survey was conducted, along with in-depth interviews with selected representatives from each user group.

The findings of this research are consistent with overseas findings by EFRAG (2009) and CFA UK (2015), showing that overall, a significant majority of respondents use financial reports in making various types of decisions, and most users are satisfied with the quality of current financial reports in meeting their information needs. For example, investors and intermediaries use financial reports mainly for making and advising on equity and debt investment decisions; lenders use financial reports mainly for making lending decisions, and regulators use financial reports mainly for monitoring purposes. All components of financial reports are perceived, on balance, as useful. In general, respondents rank the statement of profit or loss and the statement of financial position as the two most useful statements, while the statement of changes in equity is considered to be least useful. Only a quarter of respondents indicate that the financial statements contain information that is not useful.

Although Courtis (1982) in Australia found that notes to financial reports were the least read and the least important to individual investors, our results show that most respondents do find it useful to refer to the notes to the financial statements in making their decisions.

To improve the usefulness of information, consistent with prior studies (Baker & Haslem, 1973; Lee & Tweedie, 1975a; Chenhall & Juchau, 1977), a number of respondents suggest improvement in disclosure of expectations about future performance. For example, they would like to see earnings/cash flow forecasts, future prospects, and changes in market conditions disclosed in the financial reports. Some respondents suggest more disclosure of information, such as segment reporting, and/or reporting on sustainability, and some others suggest simplification, standardisation, and transparency to current financial reporting.

As regards sources of information, our findings are different to the earlier UK study by Bartlett & Chandler (1997) that annual reports were not widely read by shareholders, while are consistent the more recent European study by EFRAG (2009), showing that both analysts' reports and financial statements are rated as the most important sources of information. This may indicate the improvement in the quality of financial statements in recent years. Our results are also consistent with the some early studies (eg., Baker and Haslem, 1973; Courtis, 1982) that investors are more reliant on advisors' reports than financial reports. This finding is associated with the level of sophistication of the users. Investors, lenders, and regulators are found to be more interested in supplementary

information than intermediaries. A likely explanation for this finding is that intermediaries tend to use their own analyses.

12. Recommendations

This study provides evidence of the application of a user-needs approach by the XRB and that, in general and overall, users are satisfied with the current state of financial reporting for the Tier 1 for-profit entities. In addition, this study provides useful and up-to-date insights as to where future efforts for improvement could focus. These improvements include enhancements to reporting in general and disclosure of particular items in the financial statements.

12.1 Reporting in general

Improvements that could be made to reporting in general include:

- (a) Simplifying further the financial statements to enhance the user's ability to understand them, e.g., notes to financial instruments;
- (b) Standardising further the presentation of financial statements to enhance the user's ability to compare information across organisations;
- (c) Providing guidance for:
 - (i) Comparing actual results with budget and target figures, if a reporting entity releases budget or financial targets, including prospective information;
 - (ii) Preparing and reporting 'dashboard' style of key financial information including significant ratios; and
 - (iii) Disclosing non-financial information, in particular management's discussion of business strategies and future prospects, as well as information that assists users in better understanding the entity's current financial performance and position.

12.2 Reporting of specific items

Improvements that could be made to specific items in the financial statements include:

- (a) Improving segment reporting that leads to more detailed disclosure of material segments, as there is a perception that entities avoid providing required segmental information using 'commercial sensitivity' as a rationale; and
- (b) Improving financial instrument disclosure by discouraging boilerplate reporting and focus disclosure on what would facilitate users' comprehension.

Appendix 1: A summary of studies of user information needs

Authors (Year) / Country	Research Objectives	User Group	Sample	Methods	Findings / Results
Backer (1971) / US	To determine how financial reporting is relevant to investment decision making.	<ul style="list-style-type: none"> • Bank officers; • Security analysts; • Corporate executives. 	74 bank officers, 72 security analysts, and 109 senior corporate executives in 70 large industrial corporations.	Interview.	Different user groups expressed different views regarding contribution margin reporting, segment reporting, company profit forecasts, interim reporting, and balance sheet values.
Baker & Haslem (1973) / US	To determine whether the information provided in the financial statements meets the needs of individual investors. This study also identifies important sources of information used by investors.	<ul style="list-style-type: none"> • Individual investors. 	A sample of 1623 individual investors was drawn from the customer lists of five stock brokerage firms. From the sample survey, 851 completed questionnaires were received.	Survey questionnaire including 33 factors used in investment analysis and selected socio-economic variables. Use a five-point scale to indicate the relative importance of each factor. The interpretation of the findings was based on the average (arithmetic mean) response and its standard deviation for each of the 33 factors.	<ol style="list-style-type: none"> 1. Investors are primarily concerned with expectations about the future. The findings support the action that permits companies to include voluntary sales and earnings forecast in the reports. 2. Comparisons with other research findings suggest that individual investors may have different information needs than professional analysts. 3. Individual investors consider stockbrokers and advisory services as the most important sources for their investment information, and attach minor importance to financial statements as a source of information.

Authors (Year) / Country	Research Objectives	User Group	Sample	Methods	Findings / Results
Chandra (1974) / US	Empirical evidence concerning the adequacy of disclosure in published corporate annual reports. Precisely, this study examines whether public accountants and security analysts have any consensus about the value of information in published annual reports.	<ul style="list-style-type: none"> Public accountants; Security analysts. 	600 CPAs and 400 CFAs were randomly selected. Of the 1000 questionnaires mailed, 498 replies were received.	<p>Questionnaire, containing 58 information items.</p> <p>A simple t test was used to detect significant differences.</p>	The overall result indicates that accountants generally do not value information for equity investment decisions the same as security analysts do.
Lee & Tweedie (1975a) / UK	To examine whether shareholders use information from financial reports, and whether they understand the statutory regulations and accounting conventions underlying the production of these reports.	<ul style="list-style-type: none"> Private shareholders. 	Questionnaires were sent to 1594 shareholders of one of the largest UK industrial companies, with 374 usable replies. The response rate was around 24%.	Survey (postal questionnaire), and follow up by an interview survey of the shareholders of one of the largest UK industrial companies.	<ol style="list-style-type: none"> Many respondents skim through the annual report (e.g., those with no knowledge of accounting were more interested in the chairman's report); Financial press reports were considered to be the most important of the sources of information other than the annual financial report; The economic prospects of a company were considered to be the most important item of information. <p>The results indicate that shareholders are very interested in information about the future of the company, and that shareholders without any knowledge of accounting seem to prefer to consider an interpretation of the company's results rather than the published statements themselves.</p>

Authors (Year) / Country	Research Objectives	User Group	Sample	Methods	Findings / Results
Lee & Tweedie (1975b) / UK	To provide indicators of private shareholders' level of understanding of the accounting information contained in the company annual financial report; To investigate the nature and the extent of user understanding of company financial reports (e.g., whether shareholders use company annual reports; how they use them; and whether they reasonably understand their content).	<ul style="list-style-type: none"> • Private shareholders. 	A small public company with 1974 ordinary shareholdings. Questionnaires were sent to 1594 shareholders, with 374 replies (24% response rate).	Postal questionnaire survey.	68% of respondents believed that they understood the information, and 59% believed it to be relevant to their investment decisions; the greater the experience, the more relevant the information is believed to be.

Authors (Year) / Country	Research Objectives	User Group	Sample	Methods	Findings / Results
Chenhall & Juchau (1977) / Australia	At the broadest level, identify a range of information (both financial and non-financial) that is regarded as an important input into investor equity transaction decision models. At a second level, empirically test the relative importance and usefulness of information that has been suggested as important ingredients of company reports.	<ul style="list-style-type: none"> • Australian investors. 	From a total population of 1025 investors, 476 valid replies were received. The response rate was 46%.	Mail questionnaire, based on the format of Baker & Haslem's (1973) study.	For the 37 factors analysed, 7 were regarded as having great importance, including expected future increase in share price, listing of the shares on stock exchange, future economic outlook of the company, quality of management, future economic outlook of the industry, expected future growth in EPS, and financial strength of the company. Different investor groups have different information needs.
Benjamin & Stanga (1977) / US	To compare the perceived information needs of two groups who are primary users of external accounting information: bankers and financial analysts.	<ul style="list-style-type: none"> • Bankers. • Financial analysts. 	600 commercial bank loan officers, and 600 chartered financial analysts.	A questionnaire with 79 information items; Chi-square test.	Findings show that differences between the bankers and the analysts do exist. Differences may be the result of fundamental differences in the two types of decisions considered, or could be the result of differences in sophistication levels between the groups surveyed.

Authors (Year) / Country	Research Objectives	User Group	Sample	Methods	Findings / Results
Anderson (1981) / Australia	To investigate the usefulness of annual reports to institutional investors in Australia.	<ul style="list-style-type: none"> Institutional Investors. 	300 institutional investors selected from the share registers of 15 Australian companies. 188 responses were received, with a response rate of 63%.	Mail questionnaire.	<p>Findings show that institutional investors attach most importance to an investment objective of an equal combination of dividend income and capital gains. The desired additional information includes increased disclosure on remuneration, current value of non-current assets, changes in accounting policies, and reasons for and disclosure of off-balance sheet transactions.</p> <p>Institutional investors also desire information on future prospects, company products, divisional performance, the provision of audit reports, and the publication of quarterly reports.</p> <p>They ranked the annual report as the most important source of information, followed by share brokers' advice and company visits.</p> <p>The most widely read sections were balance sheet, profit and loss statement, notes to the accounts, and chairman's address.</p>
McNally et al. (1982) / New Zealand	To examine the 'quality' of discretionary disclosure practices and their association with corporate characteristics in New Zealand.	<p>Two groups of professional users:</p> <ul style="list-style-type: none"> Financial editors; Stock exchange members. 	Questionnaires were sent to 12 financial editors and 175 stock exchange members, with 9 replies from financial editors, and 74 replies from	<p>Questionnaire; 5-point scale.</p> <p>A t test was performed to compare the differences between the financial editors and stockbrokers.</p>	<p>The findings were consistent with earlier US and UK studies.</p> <ol style="list-style-type: none"> Two groups of external users attribute different levels of importance to the disclosure of specific items, few of these differences were statistically significant. There is considerable divergence between the degree of disclosure practised by companies and the level of disclosure perceived by external users to be desirable.

Authors (Year) / Country	Research Objectives	User Group	Sample	Methods	Findings / Results
			stock exchange members.		3. There is a level of agreement among the external users surveyed in three different countries about the relative importance of disclosing certain selected items.
Curtis (1982) / Australia	To report on a recent study into private shareholder response to annual reports of Australian public listed companies.	<ul style="list-style-type: none"> Private shareholders. 	Approximately 2000 usable replies.	Postal questionnaire.	<p>The results show that although annual reports are ranked third to stockbroker advice and newspapers as sources of corporate information, two-thirds claim the report is of some importance and one-quarter of participants would buy it.</p> <p>Readership behaviour reveals that whereas the chairman's review is the most read item, traditional financial statements are more important in influencing equity decision-making. The auditor's report, statistical data and notes to accounts are least read and least important.</p>

Authors (Year) / Country	Research Objectives	User Group	Sample	Methods	Findings / Results
Day (1986) / UK	To examine: 1) the usefulness of all information contained in annual reports and accounts to investment analysts, and their views about possible improvements to the content of and disclosure in published accounts; 2) the forecasting process used by investment analysts.	<ul style="list-style-type: none"> Investment analysts. 	15 firms of stockbrokers nominated a senior analyst or partner who was willing to participate in the study.	Interview.	The results confirm that the annual report is seen by investment analysts as only one source of information. While it is an important document, it is not seen as containing any price sensitive information.
Vergoossen & Amsterdam (1993) / Netherlands	Examine the use and perceived importance of annual reports by investment analysts in the Netherlands.	<ul style="list-style-type: none"> Investment analysts (e.g., Investment adviser, portfolio manager, director of department, etc.) 	506 members of the Dutch Association of Investment Analysts, 215 responses were usable, a response rate of 43% of the questionnaires mailed.	Postal questionnaire survey; 5-point scale.	<p>The findings are consistent with the findings of those in similar studies in the US, UK, and New Zealand.</p> <p>The annual report appears to be a vital, though not sufficient source of information to investment analysts.</p>

Authors (Year) / Country	Research Objectives	User Group	Sample	Methods	Findings / Results
Bartlett & Chandler (1997) / UK	To gauge the extent of ordinary shareholders' reading of the annual report; revisiting and re-testing the Lee & Tweedie (1975-77) approach in a modern day setting.	<ul style="list-style-type: none"> • Private shareholders (i.e., excluding institutional, nominee, director and overseas shareholders). 	Companies were chosen at random from the companies listed in the Times Top 100 in 1994; A random sample of 300 UK private shareholders, with a valid response rate of 25%.	Questionnaire-based research, similar to those asked in the Lee & Tweedie studies, taking into account the subsequent developments in financial reporting.	Results suggest that the annual report is still not widely read. In particular, in the UK, very few shareholders read the then two newer primary statements in the annual report (the cash flow statement and the statement of total recognized gains and losses).
European Financial Reporting Advisory Group (EFRAG) (2009) / 10 European Countries	To determine: <ul style="list-style-type: none"> a) how useful different forms of financial information are to users in their decision-making process; b) what improvements to financial information users require; and c) whether certain assumptions made by the Joint Boards were valid. 	<ul style="list-style-type: none"> • Investors; • Leaders; • Advisors; • Regulators; • Other. 	32 user organisations in 10 countries, 32 different respondents actually took part.	On-line questionnaire.	Majority of users find financial statements and management commentary the most useful sources of financial information as compared to press releases, economic surveys and market information.

Authors (Year) / Country	Research Objectives	User Group	Sample	Methods	Findings / Results
Colmar Brunton (2012) / New Zealand	To understand how key stakeholders perceive the New Zealand Treasury's current fiscal reporting. Specifically, to understand how well fiscal reports meet the information needs of key stakeholders and what needs to change to make better and improved reports	<ul style="list-style-type: none"> • Media; • Industry representatives; • Analysts/ economists; • Political entities; • Academia; • International organisations. 	30 key stakeholders.	Face-to-face in-depth interviews.	Stakeholders' feedback is generally positive about the New Zealand Treasury's openness and willingness to provide timely and detailed information. However, the main concern is the difficulty in finding relevant information.
PricewaterhouseCoopers (PwC) (2014a) / New Zealand	To investigate the needs and opinions of investment professionals on the disclosure of adjusted performance.	<ul style="list-style-type: none"> • Professional investors. 	85 investment professionals around the world.	Interview.	The majority of investment professionals find adjusted performance measures helpful for their analysis. However, there are certain areas where the adjusted performance reporting could be improved. For example, the adjusted performance reporting must be transparent, balanced, and consistent.

Authors (Year) / Country	Research Objectives	User Group	Sample	Methods	Findings / Results
PricewaterhouseCoopers (PwC) (2014b) / New Zealand	To investigate investment professionals' views on accounting policy innovation, and their preference on the presentational format and layout of financial statements.	<ul style="list-style-type: none"> Professional investors. 	85 investment professionals around the world.	Interview.	<p>There is little consensus among investment professionals about any particular preference on the presentational format or delivery method for accounting policies. They don't all agree on how companies should lay out their financial statements, but it is considered to be worth experimenting to find the best approach.</p> <p>Professional investors want accounting policies to be easy to find; they want management to make sure that the disclosures are company-specific with a useful level of detail.</p>
CFA UK (2015)	To examine the importance of the annual report and other forms of company reporting, as well as perspectives on adjustments to IFRS numbers and issues with IFRS accounts.	<ul style="list-style-type: none"> Members of the CFA Society of the UK. 	More than 290 investment professionals.	Survey.	Most respondents (60%) believe that financial reports contain too much irrelevant information; 55% think financial reports omit important information; 47% think the disclosure of risks and uncertainties need to be improved in the annual reports. Overall, most respondents (71%) agree that the quality of financial reporting has improved over the last 10 years.

Appendix 2: Importance of information source to various user groups

Author(s)/ Country	User group	Top Sources of Information		
		First	Second	Third
Baker & Haslem (1973) / UK	Individual investors	Stockbrokers	Advisory services	Newspapers
Lee & Tweedie (1975a) / UK	Private shareholders	Annual reports	Financial press reports	Stockbrokers' reports
Anderson (1981) / Australia	Institutional investors	Annual reports	Visits to company	Share brokers' advice
Day (1986) / UK	Investment analysts	Annual reports		
Vergoossen & Amsterdam (1993) / Netherlands	Investment analysts	Annual reports	Management communication	Interim reports
Bartlett & Chandler (1997) / UK	Private shareholders	Financial press reports	Summary of annual financial statements	Interim financial statements
Barker (1998) / UK	Analysts	Direct company contact	Analysts meetings	Results announcements
Gassen & Schwedler (2010) / 22 countries	Professional investors	Annual financial statements	Direct personal management contact	Notes to financial statements
Martinez Conesa & Ortiz Martinez (2004) / Spain	Financial analysis	Consolidated financial statements	Contact with directors	Annual reports
EFRAG (2009) / 10 European countries	Professional investors, lenders, and related advisors	Financial statements	Management commentary	Economic survey
CFA UK (2015)	Investment professionals	Annual reports	Databases (Bloomberg, etc.)	Sell-side research reports

Appendix 3: Questionnaire

XRB project - Survey

Financial Reports of New Zealand Capital Market Entities: An XRB survey of users' information needs

This questionnaire is part of a research project commissioned by the External Reporting Board (XRB) to identify the information needs of the key users of statutory published general purpose financial reports (GPFR)**, hereafter referred to as financial reports, of for-profit entities operating in the New Zealand domestic capital market.

This survey should take about 15-20 minutes to complete. Response to the survey is voluntary and all information you do provide will remain strictly confidential. Individual responses will be known only to the researchers. Completion and submission of the questionnaire implies consent. You have the right to decline to answer any particular question.

Your responses would be more useful if you would take the opportunity to provide comments and explanations that would support your responses.

This project has been evaluated by peer review and judged to be low risk. Consequently, it has not been reviewed by one of the University's Human Ethics Committees. The researcher(s) named below are responsible for the ethical conduct of this research. If you have any concerns about the conduct of this research that you wish to raise with someone other than the researchers, please contact Professor Brian Finch, Director, Research Ethics, telephone 06 356 9099, extn 86015, email humanethics@massey.ac.nz We hope you will take the time to complete this questionnaire.

Regardless of whether you choose to participate, please let us know if you would like to be notified when the report is published. You can contact us by email at: F.Laswad@massey.ac.nz Thank you for helping us with this research. Your feedback will assist in developing reporting frameworks and standards that address users' needs in New Zealand and internationally.

Sincerely,

Professor Fawzi Laswad Head of School, School of Accountancy Private Bag 11-222, Massey University Palmerston North New Zealand, 4442 Email: F.Laswad@massey.ac.nz Direct Dial +64 6 951 6064

** GPFR means financial reports that are intended to meet the needs of users who are not in a position to require an entity to prepare reports tailored to their particular information needs.

Financial Information in Corporate Financial Reports

Q1 Use of financial reports

Do you use the information in corporate financial reports in your decisions relating to investments and/or corporate performance?

- Yes
 No, please explain reasons _____

If No, please explain reasons Is Selected, Then Skip to Q7

Q2 Types of decisions for which you use financial reports

For what types of decisions do you use corporate financial reports? Please allocate 100% among the various types of decisions you undertake to indicate their approximate level of importance.

_____ Equity investment

_____ Debt investment

_____ Lending or extension of credit

_____ To monitor/assess performance of those responsible for governance

_____ To monitor/assess performance of those responsible for management

_____ Others, please specify as many categories as you see relevant and indicate their importance

Q3 The usefulness of components of financial statements

The items below comprise a full set of financial statements. Please rate the usefulness of each item to you in making decisions. Please use the scale 1 to 5, where 5 is the most useful. Please support your responses by providing reasons in the space below each item.

	1 (Least useful)	2	3	4	5 (Most useful)	N/A or do not know
• Statement of financial position (balance sheet)	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
• Statement of profit or loss and other comprehensive income	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
• Statement of changes in equity	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
• Statement of cash flows	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
• Notes to the financial statements	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

Q4 Information in financial statements that is not useful

Is there any material or information currently included in the financial statements that have no value to you and could be left out? Please explain your response in the space provided.

Yes _____

No _____

Q5 Information not provided in financial statements

Is there any material or information that is currently not included in the financial statements that you would find useful? Please explain in the space provided.

Yes _____

No _____

Q6 Improving information provided in financial statements

Do you have any other suggestions for improving financial statements? Please use the space below to explain any suggestions you may have.

Q7 Sources of information

We would like to gain insights into the key sources of information which you use in making decisions. Please allocate 100% among the various sources of information to indicate their importance. Please use the space below to explain your reasons.

- _____ Corporate financial statements
- _____ Management commentary and analysis including directors' reports
- _____ The press, media and other on-line sources
- _____ Advisors and analysts reports
- _____ Others, please indicate the other sources and their weightings

Other Information in Financial Reports

Q8 Interest in supplementary information

Do you use or require any supplementary information that is not included in current corporate financial reports?

- Yes
- No

If No Is Selected, Then Skip to Background information:

Q9 Usefulness of supplementary information

Please indicate the level of usefulness to you, of supplementary information in financial reports, using the scale 1 to 5, where 1 indicates very low usefulness and 5 indicates very high usefulness. Please support your views with comments in the spaces provided.

	1 (Least useful))	2	3	4	5 (Most useful))	N/A or do not know
• Information about the entity's business	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
• Narratives that explain the entity's performance and financial position.	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
• Information on business strategies, and prospects for future financial years.	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
• Summary financial information	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
• Others, (please specify)	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

Background information:

Q10 Your job title

Q11 Your knowledge, skills and experience

How would you describe your level of your knowledge, skills, and experience in reading, understanding and analysing financial statements? Please use the scale where 0 indicates none and 5 very high.

_____ Knowledge and Skills

_____ Experience

Q12 User group

Please indicate which of the following financial information user groups best describes you or the institution you work for. Please select as many categories as appropriate.

- Individual Equity investor
- Institutional Equity investor
- Individual Debt investor
- Institutional Debt investor
- Other creditor
- Intermediary/advisor to investors
- Financial market/prudential regulator
- other, please specify _____

Q13 Domestic or international market activity

Please indicate whether your interest is in entities which operate domestically; operate internationally; or operate in both domestic and international markets

- Domestic
- International
- Both domestic and international

Thank you for your participation.

If you would like to be notified when the results of this survey are published, please provide the following information:

Name:

Email address:

Second email address (optional):

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