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AN EMPIRICAL ASSESSMENT OF CORPORATE TRANSPARENCY IN ZIMBABWE

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CHAPTER 1

BACKGROUND TO THE STUDY

1.1 Introduction

Transparency is increasingly a more topical, broadly relevant, but also more under-researched enterprise. The recent financial crises and corporate scandals in Asia, Europe, and America have highlighted the welfare consequences of corporate transparency, and linked this relatively narrow problem to the broader context of transparency in governance (Vishwanath and Kaufmann, 1999). Transparency, responsible corporate disclosure, and effective corporate governance, have thus given rise to concern and public debate in the UK and on the international scene. Greater transparency is argued to improve the economy through better resource allocation, enhanced efficiency, and increased growth prospects. In recent years, qualitative information and narrative statements have assumed increasing importance in financial disclosure (Rutherford, 2003). This development can be seen from a technical perspective as a response to increasing awareness that traditional systems of accounting measurement and disclosure cannot, by themselves, provide a sufficiently rich data set to satisfy stakeholders' needs for information about, for example, board and management processes, ownership structure, corporate strategy, business risk and social performance. It can also be viewed from a wider perspective as a 'political' response to decreasing public confidence in the accounting numbers that are the output of traditional systems (Labelle, 2002).

The King Report on Corporate Governance in South Africa II (2001) defines transparency as the ease with which an outsider is able to make meaningful analysis of a company's actions, its economic fundamentals and the non-financial aspects pertinent to that business. It states that transparency is a measure of how good management is at making necessary information available in a candid, accurate, and timely manner. Corporate disclosure thus becomes

the principal means by which companies become transparent. Disclosure has long been recognised as the essence of corporate accountability. In the absence of full, timely, and accurate disclosure, market participants will have difficulty comparing the financial performance of different firms and may make investment decisions based on inferences about the information that is not provided. Emerging empirical research suggests that where financial liberalisation takes place in an environment where transparency is absent, financial crisis is more likely (Vishwanath and Kaufmann, 1999). Thus, the trend towards greater transparency has been given substantially greater impetus by the succession of corporate scandals in the United States and Europe, and the wave of financial crises in Russia, Asia, and Brazil.

Zimbabwe has experienced an unprecedented financial crisis in recent months, largely because of the abuse of power by dominant corporate officials, regulatory arbitraging, speculative trading by financial institutions, and poor risk management (Chikura, 2004). These practices have been argued to reflect poor accounting and disclosure standards, combined with weak board and management oversight. Further, they are symptomatic of a lack of effective corporate governance and transparency in Zimbabwe's financial markets and individual companies. However, there have been concerted efforts to enhance corporate governance in recent years in Zimbabwe, partly encouraged by international social and economic developments (Tsumba, 2001). The Institute of Directors of Zimbabwe (IODZ) has spearheaded the campaign to adopt principles popularised in the Combined Code of the UK, and the King Report of South Africa. The IODZ is dedicated to improving the expertise, status and professionalism of managers and directors of Zimbabwean companies through training and education. It also seeks to curb fraud and corruption. IODZ has set up a special purpose committee that prepares and disseminates guidelines on corporate governance, while certain prominent members of the institute, such as Anglo American, and Delta Corporation, have developed their own in-house corporate governance manuals. The current governor of the Reserve Bank of

Zimbabwe undertook in his maiden Monetary Policy statement to foster corporate governance as a vehicle for financial and economic development in Zimbabwe (Gono, 2003).

Zimbabwe has been chosen as the focus of this study for several reasons. First, despite boasting the second largest stock exchange in Africa, after South Africa, very little is known about the Zimbabwean business environment. As a result, the corporate reporting practices in Zimbabwe remain relatively less well understood. Second, Zimbabwe is one of a few emerging economies to adopt the standards of the International Accounting Standards Committee (IASC) as national accounting standards, therefore it is expected that the reporting practices of Zimbabwean companies are internationally comparable. Third, corporate transparency is of particular importance to Zimbabwe because the prevailing economic and political conditions in the country present ethical dilemmas for company directors.

Zimbabwe faces several challenges to good corporate governance practice, particularly corporate transparency (Magaisa, 2004a). The global coalition against corruption, Transparency International, rates Zimbabwe one of the most corrupt countries in the world. In Zimbabwe, as in most African countries, corruption permeates both the public and private sectors, thus the monitoring position and independence of auditors and non-executive directors, for example, becomes compromised. Lack of transparency increases the scope for corruption by creating information asymmetries between regulators and regulated entities, and the corruption vitiates public regulation as a means of mitigating the information failures (UNECA, 2002). It therefore becomes very difficult, but ever more important, to promote transparency and good governance in such an environment (Magaisa, 2004a). The second challenge is presented by the legal and judicial systems. Many authors argue that the *raison d'etre* of corporate governance, in any country, is to protect the interests of shareholders, and the interests of other investors through the contractual relations with the company.

However, the recent agrarian reforms through farm invasions have generally been construed as a disregard of property rights laws by the Zimbabwean government (for example; Bloch, 2004; Robertson, 2003; Magaisa, 2004; OECD, 2004). It may be argued that this portrays a judicial system that is tolerant of crime offenders, lacks monitoring and enforcement, therefore does not promote accountability. From a corporate perspective therefore, the legal system is seen as being weak in enforcing rules and regulations, thus shareholder and creditor rights are compromised. The protection of investor rights is particularly important in an economy where there is a risk that a small group of people endowed with political and economic power may abuse such power if left unchecked (Vishwanath and Kaufman, 1999). Finally, the political instability in Zimbabwe has meant that regulation and enforcement is selective. Business leaders are expected to tow the political line if they are to succeed (Bloch, 2004a). Consequently, any business practices or information that may be construed as promoting the cause of the opposition political party is withheld, further compromising corporate transparency.

1.2 Objectives

The main objective of this study is to assess the transparency of Zimbabwean businesses. The second objective is to explain the variability in the transparency of the sample companies in terms of four corporate governance, and three company-specific attributes. Transparency is conceptualised in this study as the disclosure of corporate information on three broad categories; ownership structure and investor rights, financial information, and board and management structure and process, using the annual report as the information dissemination medium.

1.3 Potential Contributions

There has been extensive research into the transparency practices at both firm

and country levels. However, most of this research has been mainly focused on the United States, the United Kingdom, and other developed economies [1]. Although considerable research has been undertaken in emerging markets in recent years, the focus has been on Asian economies, thus findings of these studies may not be applicable to African economies due to different cultural and political environments. Examining the transparency of Zimbabwean businesses will provide valuable contribution to a debate that is becoming increasingly global. This research is expected to have many other potential benefits. First, the results will be of interest to corporate regulators such as the Government, the Reserve Bank of Zimbabwe, and the Zimbabwe Stock Exchange. For example, results showing that Zimbabwean businesses have low levels of transparency[2] may lead to tighter regulation. Regulation aimed at making businesses more transparent will have benefits to ordinary investors who rely on company management's corporate governance and financial disclosures and may aid the development of the economy as a whole. Second, the audit profession may be interested in the research results because evidence that businesses are not transparent may suggest that auditors need to be more vigilant. Third, the findings may have implications for company management who seek to attract external investment. Finally, although Zimbabwe boasts the second largest, and second oldest stock exchange in Africa (after South Africa), very little academic research has been done on it[3], thus this research will enrich the literature on the corporate reporting practices and transparency levels of African economies, and add to the body of knowledge.

1.4 Summary of Results

In respect to the first objective, results lead to the conclusion that Zimbabwean publicly listed companies have low levels of transparency. The results provide support for the argument that companies in emerging economies are opaque.

1 For example, Malone, Fries and Jones, 1993; Schadewitz, 1994; Raffournier, 1995; Lang and Lundholm, 1996)

2 As shown by Owusu-Ansah in his 1998 case study on the adequacy of corporate mandatory disclosure practices in Zimbabwe

Although quite low, the mean score of 52% is comparable to the transparency scores of other emerging economies (for example; Malaysia, India, Brazil, Poland, South Africa, and the Czech Republic). In order to fulfil the second objective, hypotheses are developed in Chapter 3 and results of the tests presented in Chapter 5. Overall, the results indicate that the variability in the transparency scores can best be explained in terms of a company's ownership structure and the number of non-executive directors on the audit committee. Of these predictor variables, audit committee composition appears the most critical explanatory variable. These results are consistent with agency theory and comparable to studies by Chau and Gray (2002) for Hong Kong and Singapore, Pham et al (2004) and Haniffa and Cooke (2002) for Malaysia, and Williams (2003) in Singapore.

1.5 Project Overview

The remainder of this dissertation is organized as follows. Chapter 2 gives a brief overview of the Zimbabwean economic and legal environment, with a particular emphasis on the accounting and disclosure regulatory framework. This is followed by chapter 3, in which the hypotheses of the study are developed, based on established theory and prior studies. The chapter reviews relevant literature with a view to identify the gaps to be filled by this study, and the theories and themes used in extant disclosure literature to enable the development of testable hypotheses. Seven hypotheses are developed. These hypotheses seek to establish the strength and direction of relationships between certain variables and the transparency of the sample companies. These variables are split into corporate governance variables, and company-specific attributes. The corporate governance variables are ownership concentration, audit committee composition, cross-directorships, and foreign ownership, while company-specific characteristics are company size, profitability, and leverage.

Chapter 4 outlines the research methods and methodology used in the study.

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3 The only published studies on this market known to the present researcher is that of price-earnings ratio research by Oppong (1993), and mandatory disclosure by Owusu-Ansah (1998),

The chapter begins by describing the data used in the study, and the methods by which the data was collected. Next, an explanation is given on how transparency is measured in this study, and finally, an explanation of, and justification for, the statistical techniques employed for hypothesis testing is given. In chapter 5, the findings, analysis, and discussion of the results of the statistical analyses are presented. First, a descriptive analysis of the data is made in order to establish measures of central tendency and dispersion. Second, bivariate analyses are performed to establish the strength of relationships among the variables. An Ordinary Least Squares regression model is then applied to the data to establish the predictive power of selected variables on transparency and detailed analysis of results presented.

The concluding chapter provides conclusions to be drawn from this study, as well as outlining its limitations. An attempt is made to outline the policy implications for Zimbabwean businesses from the conclusions drawn.

CHAPTER 2

THE ZIMBABWEAN BUSINESS OPERATING ENVIRONMENT

2.1 Introduction

This chapter aims to put the study into context by giving a brief overview of the legal and economic operating environment for Zimbabwean business, with particular emphasis on the accounting and disclosure regulatory framework. Section 2.3 outlines the economic framework, while section 2.4 analyses the Zimbabwe regulatory framework. This section is subdivided into the three subsections of shareholders' rights, corporate disclosure regulation, and board composition and ownership structure.

2.2 Political Origin

Among the multitude of potential causes of transparency level differences, perhaps the initial cause is an organisation's country of origin (Ang and Ciccone, 2000). Certain pressures originating from the governance structures may induce an organisation to disclose information, and these pressures can come from the legal, economic, and accounting environments. The former British colony of Southern Rhodesia became the independent Republic of Zimbabwe on 18th April 1980 after a prolonged war of liberation. Zimbabwe, which is twice the size of the United Kingdom in square miles, is situated in the south of the African continent. It is a completely landlocked country, bounded on the north by Zambia, east by Mozambique, south by South Africa, and west by Botswana.

2.3 Economic Framework

Zimbabwe's economy has traditionally been broadly based and highly diverse. In 2002, industry accounted for twenty-five percent of GDP, agriculture sixteen

percent, and the service sector the remaining fifty-nine percent (OECD, 2004). Despite the extensive diversification of the economy and agriculture's relatively small contribution to GDP, the latter remains the cornerstone of the economy. Much of the industrial development has occurred in response to the requirements of the agricultural and mining industries, in terms of both input supply and processing of output (Price Waterhouse, 1995). In addition, out of those employed in 1999, sixty percent of the Zimbabwean workforce were working in agriculture, forestry, and fishing. Substantial road, rail, and telecommunications networks support the Zimbabwean infrastructure. Mining, primarily gold, is also a major activity. Zimbabwe boasts the second largest bourse in Africa (after the Johannesburg Stock Exchange) with well-developed banking and financial service sectors and possesses one of the best-educated work forces on the African continent.

While Zimbabwe has long ranked as one of Africa's most industrially diversified economies, this position has eroded considerably. Its macroeconomic environment has deteriorated sharply over the six years to 2003. At the close of the year, interest rates surged to 900% and inflation was pegged at more than 600%.The high and growing inflation contributed to a rapid depreciation of the exchange rate. The "real" exchange rate was set at about Z$8 000 to the US dollar in the parallel market. Although many public companies, especially in the finance industry, reported huge profits in the 2003 financial year, most small companies collapsed. There appears to be general consensus among economic analysts that the structural adjustment policies of the 1990s, combined with lack of support for the agrarian reforms of 2000, greatly contributed to putting the economy on a steep path of decline (OECD, 2004). The decline has been exacerbated by the resultant brain drain as Zimbabwe's young professionals emigrate *en masse*. In 2003, per capita GDP is estimated to have declined by nearly 14%.

The current economic crisis in Zimbabwe presents challenges to corporate

governance in general, and transparency in particular. For example, economic analysts agree that the recent turmoil in the banking sector was due to a "complete disregard of all principles of corporate governance" by the directors of these institutions (Bloch, 2004b). In other instances, directors and senior management of financial institutions are accused of investing depositors' funds in speculative and unacceptably high-risk foreign currency investments. One economist blames the financial crises of 2003/2004 on "an intentionally myopic oblivion to corruption" in the country (Bloch, 2004b). However, the June 2004 Government Monetary Statement and Fiscal Policy Review indicates positive developments in corporate governance and other areas, for example, tax policy, public finance management, and financial sector guidelines.

2.4 Regulatory Framework

The legal environment holds a foremost position in corporate governance. Shleifer and Vishny (1997) argue that legal protection is essential if outside investors are to provide financing to corporations. Important functions of the legal system include holding managers to their duty of loyalty to shareholders, providing voting privileges for important corporate matters, preventing management self-dealing, and protecting creditors.

The legal system governing business enterprises in Zimbabwe originated from that which was operating in the Cape Province of South Africa in 1891; which was in itself based on Roman-Dutch law, borrowing from English Common Law where necessary (Owusu-Ansah, 1998a). Consequently, the present law in Zimbabwe consists much of English commercial, company, and insolvency laws. In many cases, the persuasive authority of English and South African judicial precedents has strengthened the legislative framework. Two acts substantively govern corporate activity in Zimbabwe, the Companies Act 1952 (Chapter 24:03) and the Zimbabwe Stock Exchange Act (Chapter 24:18). The Companies Act regulates the pre-incorporation, incorporation, operations and duties of a company and its directors, while the Stock Exchange Act provides the legal basis for the establishment of the Exchange and governs its operation. The

Companies Act also deals with the rights and obligations of directors and shareholders.

2.4.1 Shareholders' Rights

The primary rights of a shareholder are the right to a dividend when declared and the right to vote in company meetings. However, there are two types of shareholders in Zimbabwe: owners of preference shares and owners of ordinary shares (Nkala and Nyapadi, 1995). Ordinary shares grant the owner the right to vote at shareholders assemblies while preference shares give the holder the right to a fixed dividend but without the right to vote. In practice, however, preference shares are rare. The memorandum and the articles of association may authorise revisions of the rights attached to any class of shares, subject to the consent of their holders. However, section 91 of the Companies Act protects the rights of dissenting shareholders. It grants holders of fifteen percent of preference shares who do not consent to or vote in favour of the revision, the right to apply to the court to have the variation cancelled. The variation in rights is not effective until the court has ruled. Shareholders have several means of redress in case their rights have been violated. A shareholder who is not satisfied that the board of directors or the management is working towards the best interest of the company may apply to the registrar of companies to request a board of inquiry. Alternatively, if there are at least a hundred dissatisfied shareholders, or if the dissenting party represent at least five percent of the issued share capital of the company, they may apply directly to the Minister of Justice for such an inquiry. An aggrieved shareholder may also approach the court directly if his statutory rights are allegedly violated or, subject to a provision in the articles of association, make use of the arbitration courts.

In general, there are no material restrictions on the ability of an investor to launch a hostile take over bid, except for foreign investors. There is no written takeover code in Zimbabwe to date, nor a comprehensive set of rules governing

the substantial acquisition of shares. Nevertheless, ZSE follows the guidelines of the City Code in London and those of the Securities Exchange in South Africa. In addition, ZSE has issued some directives aimed at protection of minority shareholders. These directives include a provision that any person or body corporate that acquires thirty five percent or more of the share capital of a listed company must make an offer for the outstanding shares. The Companies Act guarantees minority shareholders the right to participate and vote in company meetings and shareholder ballots. The Company Law sets forth, subject to any restrictions attached to any class of shares, the one share one vote principle at annual or special shareholders' meetings. The Law authorises by-laws to limit the number of votes of each class of shareholders. Shareholders, representing five percent of the paid-up capital also have the power to call an extraordinary meeting. Shareholders are not required to attend meetings in order to vote. They may cast vote by using a proxy form or postal vote and are entitled to appoint another person as proxy.

2.4.2 Disclosure Regulation

As a former British colony, Zimbabwe adapted UK-based accounting systems on gaining independence, thus follows a disclosure-based regime. The Companies Act (Chapter 24:03) is the main statute governing corporate reporting in Zimbabwe, and this was modelled on the UK’s 1948 Companies Act (Owusu-Ansah, 1998). Although there is no securities exchange commission in Zimbabwe to date, companies, both public and private, must file a prospectus with the registrar of companies upon incorporation. The prospectus should include basic information on the company and its directors, including their term of appointment, ownership interests and remuneration, as well as basic details concerning the company’s accountants, lawyers, and bankers. Information must also be provided on all material contracts and current litigation.

The Companies Act requires companies registered under it to keep accounting records that sufficiently and accurately explain their financial position and performance. Specifically, every company is required to keep, in the English language, proper books of accounts regarding its assets and liabilities, sales and purchases, all sums received and expended and the matters in respect of which the receipts and expenditures took place (s.140 (1)). The Act also lays down general provisions as to the content and form of the accounts (s.142). These fall into four broad categories; profit and loss provisions, balance sheet provisions, comparative figures, and additional provisions for holding companies. Holding companies are required, with certain exceptions, to prepare group accounts, along with company profit and loss account and balance sheet (s.144). Certain provisions of the Act require specific disclosures to be made, for example with reference to directors' emoluments (s.184) and loans to directors (s.185). Although a cash flow statement is not required under the Act, it is stipulated under the adopted IAS 7 and is thus prepared on a consolidated basis as well. Besides the requirements to publish a balance sheet and a profit and loss account, there is also a legal obligation on companies to include a director's report in their published annual report and accounts (s.147). The report should discuss the performance of the company during the financial year under review, and identify the major issues the company had to deal with, and those expected in the future. In addition, the Act requires the directors should report the amounts proposed or paid in terms of dividend and directors' remuneration.

The financial statements, which must be prepared on a regular basis in accordance with the disclosure requirements prescribed in the Seventh Schedule to the Act, must also give a true and fair view of the operations and the state of affairs of the reporting company. Every company registered in Zimbabwe is legally required to appoint an independent external auditor. In practice, the big five audit companies audit the majority of major Zimbabwean companies. Private companies are, however, exempt under certain circumstances. The auditor is required to make a report to members of the company on the financial statements examined by him (s.153). In the report, he

should express an opinion on whether the accounts have been drawn up in accordance with the provisions of both the Companies Act and International Accounting Standards, and show a true and fair view of the state of the company's affairs at the balance sheet date and the companies' operations for the year under review. The auditor's report should be attached to the company's financial statements, signed by at least two directors and sent to all persons entitled to receive notices of the company's AGM fourteen days before the date of the next meeting (s.146). Audited annual financial statements are required to be filed with the Registrar of Companies where they will be available for public inspection.

The Companies Act however, stipulates only the basic minimum requirements, thus disclosure rules are supplemented by the pronouncements of the professional accountancy body, the Institute of Chartered Accountants in Zimbabwe (ICAZ), which has the primary responsibility for the establishment, adoption and publication of accounting standards (Chamisa, 2000). The procedure in establishing Zimbabwe Accounting Standards is to scrutinise IASC exposure drafts and completed standards for suitability to the socio-economic environment. On adoption, a guideline may be issued pointing out any local conflicts between legislation and the new standards. Following adoption, the government incorporates any new disclosure into the Companies Act and a note is taken of any future legislative amendments necessary to make the legislation and standards fully compatible. Although in most cases the International Accounting Standards are adopted in their entirety, there are a few exceptions. For example, small companies are not required to comply with IAS 7: Cash Flow Statements.

Public listed companies are also required to comply with the Zimbabwe Stock Exchange's listing rules on disclosure. The listing rules require that annual published accounts disclose certain information in addition to that required by the Companies Act. For example, companies' annual financial statements must disclose details of securities listed for purposes of employee share schemes (s.

8.51(g)), the aggregate of the direct and indirect interests of the directors in the share capital of the listed company, distinguishing between beneficial and non-beneficial interests (s.8.52 (d)) and the percentage of each class of listed shares held by public and non-public shareholders. In addition, the Zimbabwe Stock Exchange requires that companies fully disclose, in the notes to the accounts, all borrowings, including off balance sheet borrowings (s.8.52 (b)). Further, listed companies are required to disclose in their annual reports the identity of shareholders behind nominee companies, their cost of sales, information on the markets where the company is selling its products, segment reporting, and full disclosure of relationships with other companies. The country having recently been designated a hyperinflationary country; companies are required to use inflation accounting for the preparation of their reports. In addition to audited annual financial statements, listed companies should publish half-yearly interim reports and provisional annual financial statements (s.8.44). However, there is no legal requirement for interim accounts to be audited.

Listed companies are obliged to report any relevant, material information necessary to enable present and potential investors to appraise their financial position and performance. Consequently, Section 8.52(a) of the listing requirements stipulates that companies are required to comment on the extent of their compliance, or non compliance, with the Code of Corporate Practices and Conduct as set out in the King Report (South Africa) or the Combined Code on Corporate Governance (United Kingdom). This statement should be sufficiently detailed to enable its shareholders and potential investors to evaluate how the principles have been applied. Other than the mandatory disclosures on the composition and compensation of the board of directors, their ownership interests, and terms of appointment which are required to be disclosed in the company's prospectus upon incorporation, corporate governance disclosures are largely voluntary in Zimbabwe. For example, there are no provisions in either the Companies Act or the Stock Exchange Act regarding the disclosure of substantial shareholders who own more than a specific percentage of the share capital of the company. Similarly, the Stock Exchange Act does not contain rules

regarding the substantial acquisition of shares, or concerning the disclosure of ownership of shareholders when they pass certain thresholds, as is the case in modern stock exchanges. Additionally, discussion of risk management is not compulsory in annual reports, though strongly encouraged by the accounting profession.

The ICAZ monitors corporate reporting compliance in Zimbabwe. Like the US Securities and Exchange Commission, the ICAZ employs a review method in monitoring and enforcing compliance with statutory and regulatory disclosure requirements (Owusu-Ansah, 1998).

2.4.3 Board Composition and Ownership Structure

Zimbabwean companies are governed by a single tier board structure. The board of directors is the ultimate body governing the corporation and is responsible for ensuring that the company operates within its articles of association, in compliance with the Companies Act and common law, and in accordance with resolutions passed at shareholders meetings and at meetings of directors. Directors must demonstrate duties of loyalty, care, skill and attendance. They have a fiduciary relationship to the company and some obligations towards the shareholders. They must observe the utmost good faith in their dealings with the company, exercise their powers for its benefit and not their own, and ensure that they avoid conflicts of interests between themselves and the company.

The Companies Act requires every company to have at least two directors, at least one of which must be residing in Zimbabwe (s.169), although most companies have six or seven. Directors may appoint alternates subject to board approval. The Companies Act imposes a duty on directors, through the company's articles of association, to hold a specified share qualification (s.172). Directors can hold any other office inside or outside the company, other than the office of auditor of the company, in conjunction with their office of director for a

term as determined by the board of directors. Where such director acts in a professional capacity for the company he is entitled to remuneration for professional services. There is no distinction of duties between executive and non-executive directors and no legal definition of an independent director, although in practice a non-executive director is understood to be fulfilling such a role. Usually the managing directors, as well as the marketing and finance directors, are the executive directors, although it depends on the management structure adopted by the company in question. Directors can set up committees of the board and delegate its powers to them but there are no legal requirements for inclusion of specific committees. However, in practice, both listed and unlisted companies have board committees such as audit, remuneration, investment, general purpose and technical committees, depending on the nature and scope of their activities.

While data on the structure of ownership of listed companies is scant, preliminary research (Magaisa, 2004) indicates that a major shareholder, or small group of shareholders, dominates the typical Zimbabwean company. In practice, corporate groups dominate the Zimbabwean economy, with often-complex cross-holdings and cross-directorships between the companies comprising the corporate group. Institutional shareholders are courted to provide the much-needed cash resources, thus institutions such as Old Mutual, Anglo American Corporation, First Mutual Life Assurance Society, NSSA, and several pension funds own some 70% of the listed shares.

2.5 Conclusion

This chapter has placed the study into context by outlining the economic and regulatory environment for Zimbabwean businesses. Overall, Zimbabwean company law is very similar to UK company law due to the colonial and, until recently, economic ties between the two countries. The adoption of International Accounting Standards, and the presence and active participation of the big five

audit companies, in Zimbabwe greatly enhances the accounting and corporate disclosure environment in Zimbabwe.

CHAPTER 3

LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

3.1 Introduction

The chapter reviews relevant literature with a view to identify the gaps to be filled by this study, and the theories and themes used in extant disclosure literature to enable the development of testable hypotheses. Seven hypotheses are developed. These hypotheses seek to establish the strength and direction of relationships between certain variables and the transparency of the sample companies. These variables are split into corporate governance variables, and company-specific attributes. The corporate governance variables are ownership concentration, audit committee composition, cross-directorships, and foreign ownership, while company-specific characteristics are company size, profitability, and leverage.

3.2 Prior Studies

One objective of this study is to determine how both corporate governance mechanisms and company-specific attributes affect a company's transparency behaviour. Empirical research on corporate disclosure and transparency has a long history, dating back to work by Cerf (1961). Healy and Palepu (2001) give a comprehensive analysis of empirical disclosure literature. In their view current research has been on three broad areas; disclosure regulation (for example, Leftwich, 1980; Watts and Zimmerman, 1986; and Beaver, 1998); auditors and other information intermediaries (for example, Dodd *et al,* 1984; 1986; Dopuch *et al,* 1986, 1987; Lang and Ludholm, 1993, and Barth and Hutton, 2000); and

the determinants and corporate consequences of corporate disclosure (for example Watts and Zimmerman, 1983; Healy and Palepu, 1993,1995). In the last category, several company characteristics have been found to have an impact on disclosure (Eng and Mak, 2003). Characteristics found to have a significant impact include; in Singhvi and Desai (1971) listing status and earnings margin; Chow and Wong-Boren (1987) firm size, financial leverage and proportion of assets in place; Meek et al. (1995) firm size, international listing status, leverage and country of incorporation.

The framework for linking disclosure to corporate governance is provided in Williamson (1985). Recent empirical work on the association between disclosure and corporate governance has focused on the determinants of voluntary disclosure. A variety of corporate governance mechanisms affecting disclosure have been identified in the literature. These include ownership structure (for example Craswell and Taylor, 1992; McKinnon and Dalimunthe, 1993; Hossain, Tan and Adams, 1994; Raffournier, 1995; Bushee and Noe, 2001), the proportion or existence of independent directors (for example Forker, 1992; Malone, Fries and Jones, 1993, Chen and Jaggi, 2000), the appointment of non-executive director as chairman, (for example Forker, 1992), and the existence of an audit committee (Forker, 1992). A summary of various relevant studies is provided at the end of this chapter, in table 1.

Although there have been several studies on the determinants of corporate transparency, further research is warranted by the generally ambiguous and inconsistent results. Wallace and Naser (1995) attribute the inconsistencies to the lack of uniformity in the statistical designs employed, and the differing nature of the explanatory variables employed. Owusu-Ansah (1998) suggests the inconsistencies could also be due to the differing socio-economic environments of the countries investigated. Although countries may broadly be classified as either developed or emerging, each country is unique in its own right. Findings of studies on the development of capital markets have provided evidence supporting the significant role of culture and legal systems on the development

of corporate ownership, corporate capital structure, and capital markets (for example; La Porta et al, 1997; La Porta et al. 1998). Therefore, the findings of studies in the US, UK and Asian markets may not be applicable to African economies due to different cultural, legal, and political environments.

This study seeks to fill a gap in literature by examining corporate transparency, and the relationship between corporate governance variables, and company specific attributes, and corporate transparency in the African economy of Zimbabwe. Little is known of the transparency levels of Zimbabwean businesses. In 1998, Owusu-Ansah carried out an empirical investigation on the adequacy of corporate mandatory disclosure practices on emerging markets, with the Zimbabwe Stock Exchange as his case study. His findings indicate that mandatory disclosure in Zimbabwean businesses is largely adequate and associated with such company characteristics as company size (market capitalisation/assets), mutlinationality, company age, and profitability and the corporate governance mechanism of ownership concentration. However, the Zimbabwean economy has gone through a great deal of turmoil since 1998, therefore it would be interesting to find out whether the economic decline of the past five years will have had any significant impact on the transparency of businesses. While Owusu-Ansah focused on mandatory disclosure, the scorecard used in this study comprises thirty-three percent mandatory and sixty-seven percent voluntary disclosure items.

Moreover, this study will add a new dimension to the literature by using different proxies for various variables investigated in previous studies. For example, the commonly used proxy for the ownership concentration variable is the proportion of shares held by the top ten or twenty shareholders. This study will use the presence of a controlling shareholder as a proxy for the variable. It is a more appropriate measurement in this study because controlling shareholders are a common phenomenon in Zimbabwean businesses and therefore, their potential impact on corporate transparency may be significant. Secondly, the impact of

the audit committee variable is investigated in several studies, but given the dummy variable of one for existence, and nil for non-existence. As all the companies in this study's sample have an audit committee, the more suitable proxy of proportion of non-executive directors on the committee is adopted. Finally, this will be the second study, to the researcher's knowledge, to empirically investigate the impact of cross-directorships on the transparency of businesses. The only other study to investigate this found a non-significant relationship in Malaysian companies (Haniffa and Cooke, 2002).

3.3 Theoretical Framework

Transparency, and disclosure, as topics span several literatures, including accounting, finance, economics, political economy, sociology, psychology, and corporate governance, thus inevitably take on features of those literatures (Verrecchia, 2001). Academic writers disagree on what, if any, the theory of disclosure is. According to Verrecchia (2001), there is no comprehensive or unifying theory of disclosure. He views the disclosure literature as "an eclectic commingling of highly idiosyncratic (and highly stylised), economics-based models, each of which attempting to examine some small piece of the overall disclosure puzzle". Dye (2001), on the other hand, posits that while there is no received theory on mandatory disclosure, there is a theory of voluntary disclosures, and several empirical studies have corroborated this by relying on several theories to develop hypotheses and interpret study results.

Dye (2001) argues that the theory of voluntary disclosure is a special case of game theory, with the following as its central premise; any entity contemplating making a disclosure will disclose information that is favourable to the entity, and will not disclose unfavourable information. This mirrors Ross' (1979) signalling theory, which argues that companies with good news are more likely to disclose more information. This theory therefore assumes that better performing companies would have better levels of disclosure than poorly performing companies. However, it has been argued that a company with a less

satisfactory performance might be tempted to improve the quality of its narrative statements in order to down play and justify the poor financial position (Labelle, 2002), thus enhancing transparency.

Theorists and researchers often invoke agency theory as a justification for disclosure. Jensen and Meckling (1976) define the agency relationship as a contract under which one or more persons (the principal(s)) engages another person (the agent) to perform some service on their behalf, which involves delegating some decision-making authority to the agent. The agency problem arises from conflicting interests between principal and agent and the resulting information asymmetry, thus increasing the potential for the principal to be exploited in such a relationship. Jensen and Meckling (1976) have suggested several ways that seek to align the interests of agents and principals, thereby mitigating the agency problem. Firstly, the principal can expend resources to monitor the activities of the agent through measuring, observing, and controlling the agent's behaviour, for example, through audits. Certain aspects of monitoring may also be imposed by legislative practices. Non-compliance with regulations must be disclosed and explained, and the attention brought by these statements of non-compliance represents an additional source of monitoring. Secondly, the principal can set up appropriate incentives for the agent to limit excessive behaviour, for example through share options as a form of executive compensation. Finally, the agent can undertake bonding activities either to ensure the principal that he will not jeopardise his interests or will compensate him for any loss sustained by him as a result thereof. Disclosure is widely viewed as one such bonding activity. However, whether agency theory adequately explains the disclosure policies of organisations is open to debate and, as demonstrated in the hypotheses development and results section of this paper, empirical evidence varies.

Proponents of the free market theory argue that if the above measures fail to achieve the desired behaviour of corporate managers, several other means

derived from market discipline (for example; the market for corporate control and information intermediaries) can control these problems. Free market economy theorists view information as a public good and argue that the market forces of demand and supply will interact to provide the desired level of corporate disclosure (Passmore, 1953). Corporate finance theory predicts that shareholders endogenously optimise disclosure policy, corporate governance, and management incentives in order to maximise firm value. This choice involves trading off the reduction in the information asymmetry component of the cost of capital that results from increased disclosure quality against the costs of reduced incentives, litigation costs (Skinner, 1994), and proprietary costs (Verrecchia, 1983). The optimal amount of corporate information would thus be supplied at the level the costs equal the benefits of supplying the information. According to this theory, companies will supply information based on the covenants contained in private lending contracts and the stewardship of managers to the owners of the company. The achievement of this perfectly credible optimum level of disclosure has been disputed however. Opponents of this theory argue that it is too costly to eliminate all manipulation, thus managers will add some bias to disclosure at a low personal cost (Watts and Zimmerman, 1986). Shleifer and Vishny (1997), on the other hand, argue that while the optimal disclosure policy allows some managerial manipulation, corporate governance structures will constrain the manager to follow the optimal policy.

The proprietary costs theory holds that companies' decisions to be transparent are influenced by concern that such transparency will damage their competitive position in product markets (for example, Verrecchia, 1983; Darrough and Stoughton, 1990; Darrough, 1993; Gigler, 1994). However, the incentive not to disclose appears to be sensitive to the nature of the competition, in particular whether companies face existing competitors or merely the threat of entry. The proprietary cost theory has been criticised for assuming no conflict of interest between managers and shareholders. As a result, it assumes that voluntary disclosure will always be credible. Hayes and Lundolhm (1996) argue that

proprietary costs induce companies to provide disaggregated data only when they have similarly performing business segments. Companies with widely varying performance across business segments have incentives to conceal these differences from competitors. There has, however, been relatively little empirical support for the proprietary cost theory (Healy and Palepu, 2001).

Other theorists argue that the “lemons” problem arising from information differences and conflicting incentives between entrepreneurs and savers in capital markets creates an incentive for managers to provide voluntary disclosure to reduce the cost of capital. Thus, the cost of capital theory holds that when disclosure is imperfect, investors bear risks in forecasting the future payoffs from their investment (Barry and Brown, 1984). If this risk is non-diversifiable, investors will demand an incremental return for bearing the information risk. As a result, companies with high levels of disclosure, and hence low information risk, are likely to have a lower cost of capital than the companies with low disclosure levels and high information risk. Some empirical evidence has corroborated this theory (for example; Botosan, 1997; Piotroski, 1999; Choi, 1973; Elliot and Jacobson, 1994).

Finally, several researchers have suggested that the disclosure practices of companies are affected by the legal origin of the country in which they operate. Prior evidence suggests that corporate reporting is more transparent in countries with a common law (vs. civil law) legal tradition (Jaggi and Low, 2000). The economics literature offers at least two reasons why common law countries provide stronger protection of outside investors’ rights (for example, Beck et al. 2002). First, legal traditions differ in the priority given to the rights of individuals’ vis-à-vis the state. Under this theory, the decentralised nature of the English common law evolved to generally protect property rights of individuals. Second, legal traditions may differ in their ability to adapt quickly to changing circumstances and minimise gaps between contracting needs and the legal systems’ capabilities.

3.4 Hypotheses Development

The overall level of transparency is probably a function of several components. One potential component is related to the corporate governance structures, for example ownership structure. Another possibility is that transparency is related to company-specific characteristics, such as size and gearing. The second objective of this study is to explain the variability Zimbabwean companies' transparency levels in terms of both corporate governance variables and company-specific attributes. A combination of corporate governance and company characteristics has been chosen for analysis in this study. The selected corporate governance attributes are ownership concentration, cross directorships, audit committee and foreign ownership. Company characteristics chosen are company size, leverage, and profitability. Attributes have been selected based on the availability of data on them, their ability to facilitate classification of the sample companies into sub-samples without ambiguity, and their relevance to the socio-economic environment of Zimbabwe.

In theory, the impact of internal governance mechanisms on corporate transparency may be complementary or substitutive (Ho & Wong, 2001). If it is complementary, agency theory predicts that a greater extent of transparency is expected since the adoption of more governance mechanisms will strengthen the internal control of companies and provide an "intensive monitoring package" for a firm to reduce opportunistic behaviours and information asymmetry (Leftwich *et al;* 1981; Welker, 1995). On the other hand, if the relationship is substitutive, companies will not provide more disclosures for more governance mechanisms since one corporate governance mechanism may substitute another. If information asymmetry in a company can be reduced because of the existing "internal monitoring packages", the need for additional governance devices is reduced. In spite of this theoretical ambiguity, Hill (1999) suggests that it is desirable to have a system of overlapping checks and balances. Therefore, the hypotheses about the effect of internal governance mechanisms

in this study are mainly predictions of a positive association.

3.4.1 Corporate Governance Variables

I. *Ownership Concentration*

According to positive agency theory, a wider dispersion of share ownership is associated with extensive transparency. The separation of ownership and control generates agency costs resulting from conflicting interests between management and owners (Jensen & Meckling, 1976; Fama & Jensen, 1983). Because agency costs tend to be higher for companies with dispersed share ownership, shareholders press for more information disclosure for monitoring purposes. This is consistent with Francis *et al;* (2002) who argue that less 'outsider' ownership results in less information asymmetry between 'insider' and 'outsider' shareholders, therefore ownership concentration reduces the need for strong corporate governance and transparency.

Many authors argue that the *raison d'etre* of corporate governance, in any country, is to protect the interests of shareholders because the interests of other investors can adequately be protected through the contractual relations with the company. However, outside the United States of America and the United Kingdom, the corporation with widely dispersed ownership is not the rule, but the exception (La Porta *et al*, 1999). What prevail are corporations with large block holders who directly control managers. The use of pyramids and other devices to increase dominant shareholders' control over corporate resources may constitute a functional alternative to improved corporate governance and better protection of minority shareholders' rights in terms of its allowing corporate insiders to gain access to extra-firm sources of investment finance (Oman, 2001). There is, therefore, a contrary view to the explanation offered by agency theory. Zeckhauser and Pound (1990) argue that dispersed individual shareholders are not a formidable influence on corporate outcomes, including disclosure policies and practices, even if the net benefits are great enough to provide significant incentives to become informed. Their argument implies that

where there is diffuse share ownership, individual public shareholders do not have the same bargaining power vis-à-vis the company to access internal information. Similarly, McColgan (2001) posits that ordinary atomistic shareholders may not have the time, skill, or interest to monitor managerial activities. Since they own a small proportion of the total shares, there may be a free-rider problem where it is not in their best interests to monitor management while others also derive the benefits. The existence of a large block investor may thus overcome this problem, as they have a greater financial incentive to monitor management. However, devices to separate corporate ownership rights from the control of corporate resources may serve to facilitate and camouflage self-dealing and related rent seeking behaviour.

Interestingly, empirical evidence is also contradictory. McKinnon and Dalimunthe (1993), and Mitchell et al. (1995), both find weak support for the hypothesis that increased ownership concentration decreases the disclosure of segment information, while Owusu-Ansah (1998) found a statistically significant positive relationship between concentrated ownership and the extent of mandatory disclosure in Zimbabwean companies. Haniffa & Cooke (2002), on the other hand, found a significant negative relationship between ownership concentration and voluntary disclosure, as did Ho & Wong (2001) in Hong Kong companies, implying that companies choose to disclose less, perhaps to avoid losing control. Following agency theory it is hypothesised that:

H1 Companies with a greater concentration of shareholding are likely to have lower levels of transparency

II. Audit Committees and Independent Directors

Regulators and corporate governance experts consider the audit committee as the entity that is at the core of the corporate reporting process (Mangena and Tauringana, 2004). The Cadbury Code (1992) recommended that all companies

should establish audit committees, and the Smith Report (2003) provided detailed guidance on the role and responsibilities of the audit committee. These responsibilities include monitoring the integrity of the company's financial statements and reviewing internal control systems. Agency theory predicts the setting up of audit committees as a means of attenuating agency costs. Forker (1992) argued that the existence of audit committees may improve internal control and thus regarded it as an effective monitoring device for improving disclosure quality. Since audit committees are largely made up of non-executive directors, it is expected that this reduces the scope that management perceive for acting opportunistically and improves transparency.

Fama and Jensen (1983) argued that effective corporate boards would be composed largely of outside independent directors holding managerial positions in other companies. Monitoring of corporate boards by non-executive directors suggests that corporate boards will become more responsive to investors, and inclusion of non-executive directors on board committees will improve the company's compliance with the disclosure requirements which in turn will enhance the comprehensiveness of disclosures and thus enhance transparency (Forker, 1992). Empirical evidence appears to lend support to this theory. For example; Ajinkya *et al.* (2003), Balachandran & Bliss (2004), Chen & Jaggi, (2000), and Ho & Wong (2001) all found a significant positive relationship between the proportion of outside directors and corporate disclosure. However, in their investigation of corporate financial disclosure in the oil and gas industry in the United States, Malone et al. (1993) did not find a significant relationship between the proportion of outside directors and the extent of financial disclosure. This may be explained in terms of the industry-specificity of their study. Further, Forker (1992) found a positive but weak relationship between the disclosure of the audit committee and the quality of share option disclosure for U.K companies. To the extent that audit committees are designed to align managers' interest with those of shareholders, it would be expected that:

H2 Companies with a higher proportion of non-executive directors on the audit

committee are more likely to have higher levels of transparency

III. *Cross Directorships*

Cross-directorships refer to a situation where directors (executive and/or non-executive) sit on more than one board. Several studies have documented that these board interlocks have important implications on the governance function as they are related to independence of directors in a unitary, versus compound, board. For example, Davis (1996) argues that cross directorships put companies at a competitive disadvantage and, in the case of executive directors, their existence on more than one board will make them less independent as they will be more sympathetic with others in similar positions. Those against interlocks argue that they are devices for intercorporate collusion (Pfeffer & Salancik, 1978), bank control over corporate decision-making (Kotz, 1978), and for the aggregation and advancement of the collective interests of the corporate elite (Useem, 1984). Proponents of cross directorships argue that when a director sits on more than one board, the company's preference for confidentiality and restriction on disclosure of information is deterred (Haniffa & Cooke, 2002). It has also been argued that the 'individualistic' nature of companies will no longer hold because information will be shared among the companies through their directors (Gray, 1988). Consequently, companies will now become transparent and the preservation of information will be less. In their study of culture, corporate governance and disclosure in Malaysia, however, Haniffa and Cooke (2002) did not find cross-directorships to have a significant effect on corporate disclosure. Cross directorships are a common phenomenon in Zimbabwean companies, the aggregate result being the creation of an interlocking directorate linking many of the large companies into a single network based on shared board members. Following agency theory, it is hypothesised;

H3 Companies whose executive directors sit on other boards are likely to have higher levels of transparency

IV. Foreign Ownership

Strategic management scholars argue that internationalisation increases the complexity and uncertainty of a firm's business operations. Stakeholders are then likely to place greater pressure on the firm to ensure it implements effective monitoring mechanisms. For example, the performance, behaviour, and consequences of the operations of multi national corporations and their local affiliates are frequently monitored by political pressure groups and international government agencies (Meek et al. 1995). Thus, foreign investors are more likely to require full compliance with all statutory and regulatory requirements of the host countries for their affiliates. Secondly, technology transfers, including accounting and disclosure practices often accompany foreign direct investments (Owusu-Ansah, 1998). Consequently, affiliates are likely to have more sophisticated financial reporting systems that facilitate greater disclosure in their annual reports than other non-affiliated companies. Empirical studies have produced mixed results. While evidence of a positive correlation is found in studies by Ahmed and Nicholls (1994), Haniffa and Cooke, (2002), Jaggi and Low (2000), and Owusu-Ansah, (1998), Meek et al. (1995) finds no significant correlation. Based on empirical evidence, this study predicts a positive correlation and hypothesises:

H4 Companies with some foreign ownership are more likely to have higher levels of transparency

3.4.2 Company Characteristics

There has been extensive empirical work relating company-specific characteristics to the extent of corporate disclosure based on a number of

theoretical arguments, which include agency, signalling, capital cost, and game theories. Three variables viz. size, leverage, and profitability that have been tested in previous studies are included in this study.

V. Company Size

Economic theory, intuition, and empirical evidence suggest that the size of a company is positively related to transparency. Leftwich et al. (1981), and Ball and Foster (1982), maintain that firm size is a comprehensive variable that can proxy for a number of corporate attributes, such as competitive advantage, information production costs, and political costs. Thus, many reasons have been advanced in the literature in an attempt to justify this relationship on *a priori* grounds. For example, Buzby (1975) argues that disclosure puts small companies in competitive disadvantage with their large counterparts in the industry. Thus, the opportunity cost of corporate disclosure may be higher than for the larger companies. Watts and Zimmerman (1986), and Cahan (1992), put forward political visibility as another potential reason for expecting a positive relationship between firm size and disclosure. Likewise, Firth (1979) suggests that firms that are more visible in the "public eye" are likely to voluntarily disclose information to enhance their public image and corporate reputation. Thirdly, it has been established that increased disclosure reduces a company's cost of capital (Choi, 1973; Elliot and Jacobson, 1994) and, since large companies rely more heavily on securities markets for financing of their operations, it follows that they would disclose more extensively than smaller companies. Fourth, empirical evidence confirms the hypothesised positive relationship between company size and corporate transparency (Cerf, 1961; Singhvi and Desai, 1971; Inchausti, 1997, Owusu-Ansah, 1998). As noted by Foster (1986), "the variable most consistently reported as significant in studies examining differences across firms in their disclosure policy is firm size". Finally, in the agency theory literature, Jensen and Meckling contend that agency costs increase with the amount of outside capital. Agency theory thus predicts that larger firms will disclose more information to alleviate the potential for wealth transfers from

suppliers of outside capital to managers. Consequently, it is hypothesised:

H5 (a) Companies with a higher turnover are more likely to have higher levels of transparency

H5 (b) Companies with a higher total assets value are more likely to have higher levels of transparency

VI. Leverage

Jensen and Meckling (1976) argue that leverage is related to the magnitude of external agency costs, thus agency costs increase as the proportion of the company's capital contributed by debt holders increases. The existence of debt provides managers with incentives to adopt investment policies that would increase the value of stock while decreasing the value of debt. The potential conflict of interest results in demand for credible corporate reporting to debt holders by managers (Etteredge et al. 1994). Thus, more highly leveraged firms will incur greater monitoring costs and, in an effort to reduce these costs, firms will disclose more information. Empirical evidence of the association between leverage and the extent of transparency is inconclusive however. While Malone et al. (1993) and Chow & Wong-Boren (1987) find a significantly positive correlation; Meek et al. (1995) find a significant, but negative correlation between leverage and corporate disclosure. Yet another set of studies find no significant correlation between the two (for example; Inchausti, 1997; McKinnon and Dalimunthe, 1993; Raffournier, 1995 and Williams, 2002). Despite the inconclusive empirical results, it is hypothesised based on agency theory:

H6 Companies with higher leverage ratios are more likely to have higher levels of transparency

VII. Profit

Signalling theory argues that companies with good news are more likely to disclose more information (Ross, 1979). Thus, it would be expected that managers of profitable companies would be motivated to disclose more information in order to distinguish themselves from the less profitable companies. However, Labelle (2002) argues that the direction of the relationship between firm performance and transparency is not clear. For instance, a company with a less satisfactory performance might be tempted to improve the quality of its narrative statements, in order to down play and justify the poor financial position. Empirical evidence appears to support both positions. For example, while studies by Haniffa and Cooke (2002) and Singhvi and Desai (1971) provide empirical evidence of a positive association between profitability and disclosure, Inchausti (19970, Meek et al. (1995), find no significant correlation between profitability and the level of disclosure in Spanish firms, and the US, UK, and continental European multinational corporations respectively. However, following signalling theory, this study predicts;

H7 Profitable companies are more likely to have higher levels of transparency

3.5 Conclusion

This chapter reviewed relevant literature and developed seven testable hypotheses therefrom. The hypotheses developed state the expected direction of impact of four corporate governance, and three company-specific, variables on transparency. These variables are ownership concentration, audit committee, cross-directorships, foreign ownership, size, leverage, and profitability. Although these variables have been investigated in prior studies, this study adds a new dimension by using different proxies for the ownership concentration and audit committee variables. Further, it investigates the impact of cross-directorships,

which, to the researcher’s knowledge, has been investigated in only one prior study. The following chapter explains the methods employed to collect data and test these hypotheses.

Table 1: Summary of Literature Relating Corporate Governance Variables and Company Attributes to Corporate Disclosure

Researcher(s) and Year	Country and Sample Size	Object of Study	Significant Variables (+/-)	Non-Significant Variables (+/-)
Ahmed & Nicholls (1994)	Bangladesh (1987/88; N=65)	Mandatory Disclosure	Family members on the board (-), size of audit firm (+), multinational company influence (+), company size (assets & sales)(+)	Leverage (+)
Ajinkya et al (2003)	United States (N=1033 btn 1997 and 2000)	Voluntary Management Forecasts	Institutional ownership (+), proportion of outside directors (+), ownership concentration (-)	
Balachandran & Bliss (2004)	Malaysia (2001; N=200)	Voluntary Disclosure	Proportion of independent directors on the board (+), independent directors on the audit committe (+),role duality (-), company size (market capitalisation)(-)	Big 5 auditor (-)
Buzby (1975)	United States (1970/71; N=88)	Extent Disclosure (Generalist view)	Company size (assets),	Listing status (+)
Cerf (1961)	United States (N=145)		Number of shareholders (+), company size (assets) (+), listing status (+), profitability (+)	
Chau & Gray (2002)	Hong Kong & Singapore (1997; N=122)	Voluntary Disclosure	Ownership diffusion (+), Family ownership (-)	Company size (+), leverage (+), audit firm (+), profitability (-), industry (+)
Chen & Jaggi (2000)	Hong Kong (N= 87 between 1993 and 1994)	Mandatory Disclosure	Proportion of outside directors (+), family ownership (-)	

Table 1: Summary of Literature Relating Corporate Governance Variables and Company Attributes to Corporate Disclosure (continued)

Researcher(s) and Year	Country and Sample Size	Object of Study	Significant Variables (+/-)	Non-Significant Variables (+/-)
Chow & Wong-Boren (1987)	Mexico (1982; N=52)	Extent Voluntary Disclosure	Company size (market capitalisation) (+) leverage (+)	Assets in place (-)
Cooke (1992)	Japan (1988; N=35)	Mandatory and Voluntary Disclosure	Company size (assets & shareholders' funds) (+), Industry type (+), listing status (+)	
Craswell & Taylor (1992)	Australia (1984; N=86)	Disclosure of Reserves by Oil and Gas Companies	Auditor type (+), company size (assets) (+)	Ownership diffusion (+), leverage (+), cash flow risk (-)
Eng & Mak (2003)	Singapore (N=158 between 1991 and 1995)	Voluntary Disclosure	Government ownership (+), managerial ownership (-), proportion of outside directors (-), company size (market capitalisation) (+), leverage (-)	
Firer & Williams (2003)	Singapore (2000; N=390)	Intellectual Capital Disclosures	Government ownership (+),concentrated ownership (-), percentage of inside director ownership (-)	
Firth (1979)	United Kingdom (N=180)	Voluntary Disclosure	Listing status (+), company size (assets & turnover) (+)	Auditor type (+)
Forker (1992)	United Kingdom (1987/88; N=182)	Share Option Disclosures	Audit committees (+), big six auditor (-), dominant personality (-), cost of disclosure (-), company size (market capitalisation)	Outside directors (+)
Gelb (2000)	United States (N= 3 219 between 1981 and 1993)	Mandatory and Voluntary Disclosure	Managerial ownership (-)	

Table 1: Summary of Literature Relating Corporate Governance Variables and Company Attributes to Corporate Disclosure (continued)

Researcher(s) and Year	Country and Sample Size	Object of Study	Significant Variables (+/-)	Non-Significant Variables (+/-)
Haniffa & Cooke (2002)	Malaysia (1995; N=167)	Voluntary Disclosure	Ownership diffusion (+), non-executive board chairman (-), family members on the board (-), assets-in-place (+), profitability (+)	Auditor type (+), cross-directorship (-)
Ho & Wong (2001)	Hong Kong (N=98)	Voluntary Disclosure	Audit committee (+), family members on board (-)	Dominant personality (-) proportion of outside directors (-)
Hossain et al (1994)	Malaysia (1991; N=67)	Voluntary Disclosure	Company size (market capitalisation) (+), foreign listing (+), ownership, concentration (-)	Assets-in-place (-), auditor type (+)
Inchausti (1997)	Spain (N=49 between 1989 and 1991)	Mandatory and Voluntary Disclosure	Company size (assets & sales) (+), audit firm (+), cross-listings (+)	Profitability (+), leverage (+), dividend payout (-)
Jaggi & Low (2000)	28 Countries (N=505)	Mandatory and Voluntary Disclosure	Company size (assets) (+), debt ratio (common law countries) (+), debt ratio (code law countries) (-), market capitalisation (+), multi-nationality (+)	
Leung & Horwitz (2004)	Hong Kong (1996; N=376)	Voluntary Segment Disclosure	Proportion of outside directors (+),concentrated board ownership (-)	
Malone et al (1993)	United States (N=125)	Financial Disclosures in the Oil and Gas Industry	Leverage (+), number of shareholders (+), stock exchange listing (+)	Proportion of outside directors (-), auditor type (+)
McKinnon & Dalimunthe (1993)	Australia (1984; N=65)	Voluntary Disclosure of Segment Information	Ownership diffusion (+), company size (number of shareholders) (+)	Minority interest in subsidiaries (+), diversity (+), industry type (+), leverage (+)

Table 1: Summary of Literature Relating Corporate Governance Variables and Company Attributes to Corporate Disclosure (continued)

Researcher(s) and Year	Country and Sample Size	Object of Study	Significant Variables (+/-)	Non-Significant Variables (+/-)
McNally et al. (1982)	New Zealand (1979; N=103)	Voluntary Disclosure	Company size (assets) (+)	Industry type (+.), auditor type (+.)
Meek et al (1995)	US, UK, & Europe (France, Germany, Netherlands) (1989; N=226)	Voluntary Disclosure	Company size (turnover) (+), listing status (+), industry type (+), leverage (-)	Mutlinationality (+), profitability (+)
Mitchell et al (1995)	Australia (1983; N=129)	Voluntary Disclosure of Segment Information	Ownership diffusion (+), leverage (+), company size (market capitalisation) (+), industry type (+)	
Owusu-Ansah (1998)	Zimbabwe (1994; N=49)	Mandatory Disclosure	Company size (market capitalisation/assets) (+), mutlinationality (+), concentrated ownership, company age (+), profitability (+),	Industry type (-) Liquidity (-), audit quality (+)
Patel & Dallas (2002)	United States (N=500)	Voluntary and Mandatory Disclosure	Price-to-book ratio (+), company size (market capitalisation) (+), market risk (-)	
Patel et al (2002)	19 emerging markets (N=354 btn 1998 and 2000)	Voluntary and Mandatory Disclosure	Price-to-book ratios (Asian markets) (+), price-to-book ratios (Brazil, Poland South Africa) (-), concentration of ownership (-)	
Pham et al (2004)	Malaysia (1996 & 2001; N=104)	Mandatory and Voluntary Disclosure	Company size (+), diffusion of ownership (+), diversification (+), profitability (+) auditor type (-), audit committee (-), internal audit (-), family control (+)	Board member ethnicity (+)

Table 1: Summary of Literature Relating Corporate Governance Variables and Company Attributes to Corporate Disclosure (continued)

Researcher(s) and Year	Country and Sample Size	Object of Study	Significant Variables (+/-)	Non-Significant Variables (+/-)
Raffournier (1995)	Switzerland (1991; N=161)	Voluntary Financial Disclosure	Company size (assets) (+), foreign listing (+)	Assets-in-place (-), ownership diffusion (-), Leverage (+), profitability (+), size of audit firm (+)
Rutherford (2003)	United Kingdom (1998; N=419)	Mandatory Narrative Disclosure	Company size (net assets & turnover) (+), gearing (+), organisational complexity (+), performance ratios (-)	
Singhvi & Desai (1971)	United States (N=155 between 1965 and 1966)	Extent Disclosure (Generalist View)	Company size (assets) (+), listing status (+), number of shareholders (+), profitability (+), number of shareholders (+)	
Tai et al. (1990)	Hong Kong (N = 76)	Mandatory Disclosure		Company size (+)
Wallace et al (1994)	Spain (1991; N=50)	Mandatory and Voluntary Disclosure	Company size (assets & turnover) (+), listing status (+), liquidity (-)	
Williams (2002)	Singapore (N=390)	Voluntary Audit Committee Disclosures	Board size (+), proportion of independent directors (+), international affiliation (+), role duality (-)	Inside director ownership (-) , concentrated ownership (+), company size (+), auditor type (+), leverage (-)

CHAPTER 4

RESEARCH METHODOLOGY

4.1 Introduction

This chapter describes and analyses the processes by which empirical evidence on the transparency levels of Zimbabwean companies has been collected and analysed. The chapter begins by describing the data used in the study, and the methods by which the data was collected. Next, an explanation is given on how transparency is measured in the study and, finally, an explanation of, and justification for, the statistical techniques employed for hypothesis testing is given.

4.2 Data Description

The data used in this study is obtained from the annual reports of ZSE listed companies. Due to the relatively small number of companies listed on the market, all the 79 companies were contacted by post for a copy of their audited annual reports for the financial year ending in 2003. After a poor response to the first request, a second letter was sent to several stockbrokers, with a remarkably favourable response. Fifty-four annual reports were received, however, to ensure uniformity in the annual disclosure practices of the sample, some companies were eliminated from the sample for one of two reasons. Firstly, Zimbabwean financial institutions are registered under a separate statute from other companies, thus report under a different regulatory framework. From the 54 reports received, 11 fell into this category, leaving 43 companies in the sample. Secondly, companies that are merely listed on the ZSE, but not incorporated under Zimbabwean law, such as Ashanti, Kinross, Pretoria Portland Cement, and Falcon are deemed not to be representative of the general population of Zimbabwean companies, and have thus been eliminated

from the sample. The resulting final sample of 39 companies represents about 71% of the total population of Zimbabwean, non-financial, listed companies as at December 2003. Table 2 summarises the sample design:

Table 2: Summary of Sample Selection Criteria

Description	No. Of listed companies	Proportion of total population (%)
Population		
Companies with equity shares on ZSE as at 31 December 2003	79	100.00
Less:		
Companies registered under the Banking Act	20	25.00
Companies not incorporated in Zimbabwe	4	5.00
	55	70.00
Respondents		
Total	54	98.00
Less:		
Companies registered under the Banking Act	11	20.00
Companies not incorporated in Zimbabwe	4	7.00
	39	71.00

The corporate annual report has been chosen as the main data source as it is generally considered the most important source of corporate information Zimbabwe. The annual report is commonly regarded as the key accountability mechanism (Lamond, 1995). It is an official, regulated, and reasonably, accurate vehicle of disseminating both financial and non-financial information about an organisation. The annual reports are examined for possible information attributes, based on a transparency scorecard derived from Standard and Poor's Transparency and Disclosure score system which addresses disclosure patterns along a broad spectrum of factors that affect corporate governance practices (Patel & Dallas, 2002). A binary scheme was used to denote the existence of an

information attribute, coded ‘1’ to denote existence and ‘0’ to indicate non-existence. A score was then computed for each company, as a ratio of the absolute possible transparency score. In order to minimise the subjectivity inherent in the scoring procedure, 10 annual reports were randomly drawn form the sample and independently scored by a classmate. The resulting scores from this sample were not found to be significantly different from the results obtained by the present researcher.

4.3 Transparency Measurement

Transparency has been defined as a process by which information about existing conditions, decisions and actions is made accessible, visible and understandable (Pham et al, 2004). Similarly, Pownall and Schipper (1999) state that a standard requiring transparency mandates financial statements that reveal the events, transactions, judgements, and estimates underlying the numbers and their implication. However, while transparency is an intuitively appealing concept, there is little consensus about its measurement. For example, transparency has previously been measured broadly as a combination of ten factors, including adoption of international accounting standards (CLSA, 2001) and, narrowly as timeliness in incorporating economic income, particularly negative economic or bad news, into accounting profit (Ball et al, 2000). In this study, transparency is being assessed in terms of the sample companies’ disclosure of ninety possible corporate governance and financial items in their annual reports and accounts for the 2003 financial year. Corporate governance and financial information have been chosen because of their documented link with transparency.

Corporate governance has been defined as the means of protecting minority shareholders from expropriation by managers or inside shareholders (Mitton, 2002). The governance role is concerned with giving overall direction to the

enterprise, with overseeing and controlling the executive actions of management, and with satisfying legitimate expectations of accountability and regulation by interests beyond corporate boundaries (Tricker, 1984). The corporate governance system specifies the terms of the equity contract between management and the shareholders. They ensure corporate conformance with investors' and society's interests and expectations by limiting the abuse of power, the siphoning-off of assets, the moral hazard and the significant waste of corporate-controlled resources (so-called "agency problems") that the self-serving behaviour of managers and other corporate insiders can be expected to impose on society and investors (Shleifer and Vishny, 1997). Management is given great discretion to run the business of the corporation, while shareholders receive the residual income resulting from the corporation's operations, thus giving them the incentive to monitor management's performance.

The relationship between good corporate governance and transparency should thus be apparent. Corporate governance at its core involves the monitoring of the corporation's performance and the monitor's capacity to respond to poor performance – the ability to observe and the ability to act (Gilson, 2000). Transparency goes directly to the equity market's ability to observe a corporation's performance. Most information concerning a corporation's performance is uniquely available from the corporation. Financial accounting information is the product of corporate accounting and external reporting systems that measure and routinely disclose audited, quantitative data concerning the financial position and performance of publicly held firms. Audited balance sheets, income statements, and cash-flow statements, along with supporting disclosures, form the foundation of the firm-specific information set available to investors and regulators (Bushman and Smith, 2003). Financial accounting systems thus provide direct input to corporate control mechanisms by contributing to the information contained in share prices. Without effective disclosure of financial performance, existing equity investors cannot evaluate

management's past performance, and prospective investors cannot forecast the corporation's future cash flow. Equity investment requires good corporate governance, and good corporate governance requires the capacity to make credible disclosure of financial results. In the absence of effective financial disclosure, a country's capacity to support equity markets and, in turn, important kinds of industry, is compromised.

Effective corporate governance also requires a second form of transparency – ownership transparency. Just as shareholders can suffer from poor corporate performance they also can suffer from a controlling shareholder's divergence of earnings or opportunities to itself (Gilson, 2000). For this reason, it is also important that companies disclose the identity of shareholders who own significant amounts of shares. Arguably, disclosure alone is insufficient to police self dealing by controlling shareholders. However, as a rapidly growing empirical literature demonstrates, effective substantive protection of minority shareholders is also critical to effective corporate governance and a successful equity market, but knowledge of whether the potential exists is a necessary first step.

4.4 The Transparency Scorecard

One of the major limitations of studies on corporate transparency is the difficulty in measuring the extent of disclosure. Researchers use several proxies for this variable, including management forecasts (for example, Miller and Piotroski, 2000), metrics based on some analysts' database (for example, Lang and Ludholm, 1993; Healy et al: 1999), and self-constructed measures (for example, Owusu-Ansah, 1998; Haniffa and Cooke, 2002; Pham *et al*., 2004). However, Healy and Palepu (2001) maintain that each approach has its limitations. They posit that the use of management forecasts yields the advantage that they can be precisely measured and the timing of the disclosure is typically known. It is therefore possible to assess whether the forecast preceded or lagged particular

changes in variables, enabling researchers to conduct more powerful tests .The limitation, however, is that the accuracy of management forecasts can only be verified *ex post* by outside investors through actual earnings realizations. It is more difficult to *ex post* verify the accuracy of many other types of voluntary disclosure however, for example board processes. Therefore, research using management forecasts as the metric for disclosure is likely to increase the power of the tests, but the findings may not generalize to other forms of disclosure. Healy and Palepu (2001) postulate that studies with self-constructed measures of disclosure face a different set of problems. They argue that because the authors have developed their own proxy, there is increased confidence that the measure truly captures what it is intended. However, to the extent that construction of the metric involves judgment on the part of the researchers, the findings may be difficult to replicate.

Professional analysts have been argued to be one of the most important groups making assessments of the financial future of companies, thus are considered a good source of data to measure transparency (e,g, Brian and Rozeff, 1978; Lys and Sohn, 1990). According to Healy and Palepu (2001) analysts' databases provide a more general measure of disclosure. Although it is unclear what biases the analysts may bring to the ratings they are likely to be particularly well qualified to judge companies' corporate disclosure. Consequently, this study uses one such analyst's benchmark to assess corporate transparency in Zimbabwe.

The Standard and Poor Transparency and Disclosure benchmark has been chosen because of its appropriateness to this study. It provides the required link between transparency, corporate governance, and financial information by encompassing three broad categories; ownership structure and investor rights, financial transparency, and board structure and processes (Patel and Dallas, 2002). The methodology, with ninety-eight questions in the three categories and

twelve sub-categories, is designed to balance the range of issues analysed and the tractability of the analysis. Its breadth and flexibility allow it to be applied to any country, thus allows for global comparisons. The Standard and Poor transparency benchmark has been proved transparent and objective. It is well documented and publicly available, thus is easily verifiable.

Out of the ninety-eight questions, eight were removed from this study, as they are not applicable to the Zimbabwean reporting regime. For example, for the most part Zimbabwean accounting standards are wholesale adoptions of International Accounting Standards, therefore it is not necessary for companies to provide accounts in alternate internationally recognised methods and reconcile the two. Thus, the final transparency scorecard has ninety information items, thirty of which are legally mandated by the Zimbabwe Companies Act, the ZSE listing requirements, and accounting standards, while the rest is voluntary. A difficulty arose in handling items thought to be “not applicable” for a particular company. Coding genuinely “non applicable” items as zeros would bias a company’s transparency score downwards, thus these items were removed from the total score of that company. As a result, transparency is assessed using a relative score, which is a ratio of the actual score to the total possible score per sample company.

The scorecard is scored using an unweighted dichotomous scale. This approach assumes that each item of information disclosed is of equal importance in the decision-making process of information users (Chau and Gray, 2002). The use of an unweighted dichotomous scale has been used, and supported, in prior empirical studies (for example; Hossain et al, 1994; Ahmed and Nicholls, 1994; Chen and Jaggi, 2000). Ahmed and Courtis (1999) posit that the approach based on unweighted items has become the norm in annual report studies. The assigning of weights to each information attribute is not employed, as this would introduce a degree of subjectivity to the analysis. Moreover, prior empirical

research indicates both methods are generally interchangeable as they produce the same results (Chow and Wong-Boren, 1987; Marston and Shrives, 1996).

4.5 Hypothesis Testing

Normality tests were carried on the dependent variable and results reported in the next chapter show that the data was taken from a normally distributed population; therefore parametric statistical tests were employed to test the hypotheses developed in Chapter 3. Pearson' product momentum correlations are used to assess the strength of the relationship between the corporate governance, and company specific, attributes and the transparency scores. Although correlations are a useful analytical tool, they are concerned with the covariability of variables, therefore do not prove causality between the variables involved. Correlation analysis does not suggest that variations in the transparency scores are caused by variations in, say, concentrated ownership or vice versa. It is thus used as a suggestive and preparatory tool to give some clues to what the data might yield; to be followed by more sophisticated techniques (Barrow, 2002). Consequently, an ordinary least squares multivariate regression model is developed to ascertain the corporate governance and company-specific attributes that explain, in a conjunctive manner, the transparency levels of the sample companies.

The use of ordinary least squares multiple regression approach is consistent with similar prior studies (for example; Hossain et al, 1994; Ahmed and Nicholls, 1994; Chen and Jaggi, 2000, Owusu-Ansah 1998, Haniffa and Cooke, 2002). Multiple regression analysis enables the investigation of the collective influence of several independent variables on a single dependent variable. In the context of this study, it allows for investigation of the collective influence of both the corporate governance and company-specific variables on the transparency scores. A third reason for using a multiple regression is the influence of each

variable upon the dependent variable is measured, and its significance ascertained. Fourth, it allows the combination of different variables, with differing measurement scales, into one model. Finally, the use of multiple regression analysis does not deny the existence of other factors that might influence transparency; rather, it merely estimates the proportion of the transparency score that can be explained by the identified variables. Thus, the following linear model is assumed to hold for the sample companies:

$$Transcr = \beta_o + \beta_1 Cntrl_i + \beta_2 Audit_i + \beta_3 Xdir_i + \beta_4 FrnOwn_i + \beta_5 Size_i + \beta_6 Levrg_i + \beta_7 Prft_i + e_i$$

Where:

Transcr = the relative observed value of the dependent value (the transparency score) for the $_i$ sample company.
β_o = the intercept to be estimated from the data which is assumed constant across the sample companies
β_1 = the coefficients of the independent variables to be estimated from the data, where $_i$ = 1…7
$Cntrl_i$ = the ownership concentration variable for the $_i$ sample company.
$Audit_i$ = the audit committee variable for the $_i$ sample company
$Xdir_i$ = the cross directorship variable for the $_i$ sample company
$FrnOwn_i$ = the foreign ownership variable for the $_i$ sample company
$Size_i$ =the company size variable for the $_i$ sample company
$Levrg_i$ = the leverage variable for the $_i$ sample company
$Prft_i$ = the profitability variable for the $_i$ sample company
e_i = residual term

The table below summarises the operationalisation of the independent variables in the model:

Table 3: Summary of the Operationalisation of Independent Variables

Independent Variable	**Operationalisation**	**Model Notation**
Corporate Governance Characteristics:		
I. Ownership Concentration	Existence of a controlling shareholder, defined as a single shareholder owning at least 50% of shareholding	$Cntrl_i$
II. Cross-Directorship	Ratio of directors on the board with directorships in other companies to total number of directors	$Xdir_i$
III. Audit Committee Composition	Ratio of non-executive directors on the audit committee	$Audit_i$
IV. Foreign Ownership	Ratio of total shares owned by foreigners to total number of shares issued	$FrnOwn_i$
Corporate Characteristics:		
V. Company Size	i) Log of total assets as at 2003 financial year-end	$Size_i$
	ii) Log of total turnover for the financial year ending in 2003	
VI. Leverage	Debt ratio defined as total debt to total assets	$Levrg_i$
VII. Profitability	Return on equity defined as net income to total owners' equity	$Prft_i$

Natural logarithms were used for the company size proxies of total assets and turnover in order to standardise the data. Natural logarithms have been used in prior studies such as Owusu-Ansah, 1998.

4.6 Summary

This chapter described and analysed the processes by which empirical evidence on the transparency levels of Zimbabwean companies has been collected and analysed. Data from the final sample consisting of 39 ZSE listed companies as at the end of the 2003 financial year will be subjected to statistical tests such as

correlation in order to test the association between seven variables and corporate transparency levels. Ordinary Least Squares multiple regression model was built with the seven variables of ownership concentration, audit committee, cross directorships, foreign ownership, company size, leverage, and profitability in order to test the hypotheses developed in Chapter 3. The results of these tests are presented in the next chapter.

CHAPTER 5

FINDINGS, ANALYSIS AND DISCUSSION

5.1 Introduction

In this chapter the findings, analysis, and discussion of the results of the statistical analyses are presented. First, a descriptive analysis of the data is made in order to establish measures of central tendency and dispersion. Section 5.3 deals with the strength of relationships between the variables, while section 5.4 is concerned with establishing the predictive power of the regression model. A section follows this on model diagnostics to test the reliability of the statistical model. This chapter is expected to develop conclusions regarding the relationship between selected variables and transparency. While correlations examine the extent to which variables are related, regression analysis will determine their predictive power, thereby testing the hypotheses developed.

5.2 Descriptive Statistics

Descriptive statistics are presented in table 4. The transparency scores for the sample companies in the study range from a minimum of 26% to a maximum of 66%, with a mean of 52%. Although quite low, these scores are comparable to the transparency scores of other emerging economies. In their study of transparency and disclosure in 19 emerging markets, Standard and Poor find the mean scores of their sample companies to range from 22% to 55%, with varying means across the countries (Patel et al, 2002). They report South African companies as having the highest mean score of 55%, followed by Asia at 43%, Europe and the Middle East with 36%, and Latin American companies have a mean score of 29%. In comparison therefore, the Zimbabwean

companies in this sample demonstrate relatively high levels of transparency.

Table 4: Descriptive Statistics

	Minimum	***Maximum***	***Mean***	***Std. Deviation***	***Skewness***	***Kurtosis***
TRANSCR	0.29	0.66	0.52	0.07	-0.76	2.836
CNTRL	0.00	1.00	0.38	0.49	0.49	-1.854
XDIR	0.00	1.00	0.29	0.25	0.64	0.172
AUDIT	0.00	1.00	0.73	0.30	-1.02	0.457
ASSETS	1,345.00	293,424.00	52,705.97	77,953.05	2.23	4.069
TNVR	707.00	174,526.00	37,780.67	36,542.54	1.78	4.019
LEV	0.02	0.73	0.32	0.16	0.29	-0.155
PRFT	0.06	3.06	0.60	0.49	3.38	17.056
FRNOWN	0.00	0.77	0.15	0.23	1.39	0.654

The Variables in the table are defined thus:

TRANSCR	Transparency Score	
CNTRL	Ownership Concentration	Existence of a controlling shareholder, defined as a single shareholder owning at least 50% of shareholding
XDIR	Cross-Directorship	Ratio of directors on the board with directorships in other companies to total number of directors
AUDIT	Audit Committee Composition	Ratio of non-executive directors on the audit committee
FRNOWN	Foreign Ownership	Ratio of total shares owned by foreigners to total number of shares issued
ASSETS	Company Size (total assets)	i) Log of total assets as at 2003 financial year-end
TNVR	Company Size (total turnover)	ii) Log of total turnover for the financial year ending in 2003
LEV	Leverage	Debt ratio defined as total debt to total assets
PRFT	Profitability	Return on equity defined as net income to total owners' equity

The frequency distribution tabulated below shows variability in the extent of transparency scores among the sampled companies. About 64% of the companies in the sample disclosed between 25% and 75% of the items in the transparency scorecard, while about 36% disclosed between 50% and 75%. No company's transparency scores fell in either the lower or upper quartiles. This

distribution of scores is similar to the results in the Standard and Poor study. Out of the 354 companies in the sample, about 74% disclosed between 50% and 75% of the items, while 25% disclosed less than 50%, and only one South African company disclosed more than 75% of the items in the scorecard.

Table 5 (a): Frequency Distribution of Transparency scores

Overall Transparency Score (%)	No. Of Companies	Proportion of Sample (%)
75 and above	0	0.00
Between 50 and 75	25	64.10
Between 25 and 50	14	35.90
Less than 25	0	0.00
	39	**100.00**

When the transparency scores are disaggregated into the three categories of; ownership structure, financial transparency, and board structure, an interesting pattern emerges. Ninety-five percent of the companies disclose at least 50% of the financial transparency items, while 74% disclose more than 50% of the ownership structure items, and only 10% disclose at least half of the board structure items. Again, the same pattern is found in the Standard and Poor study, where Patel et al (2001) state that the principal similarity across the regions is that disclosure of financial information is consistently higher than that of ownership, or board, structure. The financial transparency scores range from a minimum of 41% to a maximum 79%, with a mean of 36%. It may be argued that these relatively higher scores result from the regulation of financial disclosures, whereas ownership and board structure disclosures are largely voluntary. For example, there are no provisions in the Zimbabwean Companies Act regarding the disclosure of substantial shareholders who own more than a specific percentage of the share capital of the company, no stipulation on the number of non-executive directors, and details of executive compensation are only required to be disclosed in a company’s prospectus upon flotation.

Table 5 (b): Frequency Distribution of Disaggregated Transparency Scores

Transparency Score Quartiles (%)	Financial Transparency and Information (%)	Ownership Structure and Investor Rights (%)	Board Process and Structure (%)
75 and above	5.10	0.00	0.00
Between 50 and 75	89.80	74.4	10.30
Between 25and 50	5.10	23.00	84.60
Less than 25	0.00	2.60	5.10
	100.00	**100.00**	**100.00**

Although higher than the other two categories, the financial transparency scores in this study are lower than those reported by Owusu-Ansah (1998) for his 1994 Zimbabwean sample. He found that the sample companies disclosed between 63% and 85%. One explanation for this apparent reduction in financial transparency may be that companies disclose less in times of economic crises. However, this contradicts with the findings of a longitudinal study of Malaysian transparency before and after the Asian financial crises by Pham et al (2004). They find that levels of transparency significantly increased because companies improved their corporate governance in response to the crisis. Another possible explanation for the difference may be the role that management discretion plays in companies' disclosure practices. One might argue that Owusu-Ansah found higher levels of disclosure in his sample because his disclosure index is based on mandatory disclosure requirements. Thus, as this study focuses on both mandatory and voluntary disclosure, the reduction may be construed to mean the managers of the sample companies exercised considerable discretion regarding what was disclosed in the 2003 annual reports. Finally, it may be that compliance levels have reduced between 1998 and 2003 due to less stringent enforcement efforts by the regulatory authorities as investor protection and property right laws are documented to have become almost non-existent in Zimbabwe in the past four years (for example, Magaisa, 2004; Bloch, 2004; Robertson, 2003)

The least transparency scores are found in the board structure category, with a mean score of 40%. The results indicate a particular weakness in the disclosure of processes. For example, none of the companies in the samples disclosed the procedures for board appointments, decisions on performance related executive compensation, or procedures for proposals at shareholders' meetings. Interestingly, when Standard and Poor carried out a similar study on British, Japanese, and American companies, they found similar results (Patel and Dallas, 2001).

5.3 Correlation Analysis

As mentioned in Chapter 4, correlation analysis seeks to assess the strength of the relationship between variables. It is generally argued that highly correlated variables should not be included in the same regression model. However, the problem lies in determining what constitutions a high correlation coefficient. For some, a high coefficient is anything above ±0.500; for others it is anything around ±0.600 (Eastman, 1984). However, a correlation coefficient less than ±0.0800 is not considered to offer a serious threat to regression results (Farrar and Glauber, 1967 and Judge et al; 1985).

The parametric Pearson product momentum test was employed to assess the strength of the bivariate relationships between the variables. As shown by Table 6 below, the three variables of ownership concentration, audit, and size are significantly correlated with transparency, with the audit variable showing quite a strong relationship, at 0.721 Pearson's correlation coefficient. On the other hand, cross directorships, leverage, profitability, and foreign ownership are clearly not significant. It is interesting that the profitability variable is shown to have a negative, albeit non-significant, relationship with transparency, as this is contrary to theory and several prior studies. However, Owusu-Ansah (1998) also found mixed results for his 1994 Zimbabwean sample, with the Pearson product-momentum correlation test showing a positive association with mandatory

disclosure, while a negative association was found with the Spearman rank-order test. Both correlations were, however, not statistically significant.

Table 6: Pearson's Correlations

	Transcr	Cntrl	Xdir	Audit	LogAss	Logtnvr	Levrg	Prft	FrnOwn
Transcr	1								
Cntrl	-0.345*	1							
Xdir	0.087	0.197	1						
Audit	0.721**	0.037	0.082	1					
LogAss	0.370*	0.180	0.276*	0.416**	1				
Logtnvr	0.364*	0.207	0.127	0.427**	0.784**	1			
Levrg	-0.111	0.178	-0.132	-0.002	0.110	0.259	1		
Prft	-0.067	-0.056	-0.112	-0.001	-0.022	0.245	0.560**	1	
FrnOwn	-0.140	0.262	-0.139	-0.231	0.029	0.089	0.248	0.170	1

* Correlation is significant at the 0.05 level (1-tailed).
** Correlation is significant at the 0.01 level (1-tailed).

As a preliminary approach to detecting the presence of multicollinearity, the correlation matrix is scanned for high correlation coefficients between independent variables. Except for log total assets and log total turnover, no other independent variables possess a correlation coefficient greater than ±0.600. The two are highly correlated because they are both proxies for the same variable, company size. Field (2000) states that high levels of collinearity will increase the probability of a type II error, that is, a good predictor may be found non-significant and rejected from the model. Secondly, it limits the multiple regression coefficients, and makes it difficult to assess the individual importance of a predictor. Thus, two multiple regression models are run, each with only one of the company size variables.

This collinearity detection procedure is commonly used in empirical studies, however, it has been criticised for missing more subtle forms of multicollinearity. Thus, further collinearity diagnostics are analysed in section 5.5.

5.4 Multiple Regression Analysis

A multiple regression model was employed to establish the predictive power of the variables in this study, and test the hypotheses developed in Chapter 3. The variables used as predictors in this study have been selected using both past research and substantive theoretical importance. Because of the high multicollinearity between the two proxies for the company size variable, *LogAss* and *Logtnvr*, two different regression models were run, first with *Logtnvr*, then with *LogAss.* A third regression Model C, was run using the stepwise regression method in order to confirm the predictive power of the variables identified as significant by Models A and B. However, because this model gave the same results as A and B, its results will not be reported on.

5.4.1 Model A

Model A is a simple ordinary least squares regression model, regressing transparency scores against ownership concentration, audit committee, cross-directorships, foreign ownership, size, leverage, and profitability. This model used the natural logarithm of turnover (*LogTnvr)* as a proxy for the company size variable. This variable needed to be transformed as it exhibited positive skewness. The results of this regression analysis are presented in table 7. The *F*-statistic of 11.799 indicates that the model is highly significant. Overall, the independent variables selected in this study explain about 67% of the variation in the dependent variable (*Transcr)*. Of the seven variables examined, two corporate governance variables of *Cntrl* and *Audit* are found to have a significant effect on transparency. The *t* statistics of the remaining variables are not significant at the 5% level, indicating a negligible effect on the transparency practices of Zimbabwean listed companies.

Table 7: Model A Regression Results

Source	SS	df	MS	*F*	Sig.

Model residual total						
	0.125	7	0.018		11.799	0.000
	0.047	31	0.002			
	0.172	38				

Variable	*Coefficient*	*Std Error*	*t-value*	*Sig.*	*95% Confidence Interval*		*Tolerance*	*VIF*
(Constant)	0.329	0.056	5.93	0.000	0.216	0.443		
Cntrl	-0.479	0.014	-4.566	0.000	-0.093	-0.036	0.799	1.251
Audit	0.695	0.024	6.361	0.000	0.105	0.204	0.738	1.355
Xdir	0.108	0.027	1.082	0.288	-0.026	0.084	0.887	1.127
FrnOwn	0.174	0.031	1.653	0.108	-0.012	0.113	0.793	1.261
LogSize	0.177	0.006	1.56	0.129	-0.003	0.023	0.685	1.459
Levrg	-0.019	0.052	-0.157	0.876	-0.115	0.099	0.614	1.629
Prft	-0.144	0.016	-1.222	0.231	-0.052	0.013	0.638	1.569
Mean VIF								**1.379**
Number of observations			39					
R Square			0.727					
Adjusted R Square			0.665					

5.4.2 Model B

This model uses the log of total assets (*LogAss*) as a proxy for company size, and regresses transparency (*Transcr*) against all the selected variables. The regression results are presented in table 8 below.
The explanatory power of the model is very similar to that of Model A, with a significant *F* statistic of 11.174, and an adjusted R Square statistic of 0.652. Consistent with the results from Model A above, the existence of a controlling shareholder, and the proportion of non-executive directors on the audit committee, are found to be significant predictors of the transparency practices of Zimbabwe Exchange listed companies. Thus, it can be inferred that company size has the same effect on a company's transparency level, however it is measured.

Table 8: Model B Regression Results

Source			SS	df	MS		F	Sig.
Model residual total			0.123 0.049 0.172	7 31 38	0.018 0.002		11.174	0.000
Variable	*Coefficient*	*Std Error*	*t-value*	*Sig.*	*95% Confidence Interval*		*Tolerance*	*VIF*
(Constant)	0.364	0.047	7.676	0.000	0.267	0.461		
Cntrl	-0.463	0.014	-4.357	0.000	-0.092	-0.033	0.812	1.231
Audit	0.721	0.024	6.558	0.000	0.111	0.210	0.757	1.321
Xdir	0.097	0.028	0.929	0.360	-0.032	0.084	0.833	1.200
FrnOwn	0.179	0.031	1.662	0.107	-0.012	0.116	0.791	1.265
LogSize	0.121	0.005	1.070	0.293	-0.005	0.017	0.720	1.388
Levrg	-0.016	0.054	-1.300	0.898	-0.117	0.103	0.609	1.642
Prft	-0.1	0.016	-0.844	0.405	-0.047	0.019	0.650	1.539
Mean VIF								**1.369**
Number of observations			39					
R Square			0.716					
Adjusted *R* Square			0.652					

Overall, the results of the two models show that, of the seven variables examined in this study, ownership concentration and audit committee composition are found to have a statistically significant impact on transparency levels. The most significant variable is the percentage of non-executive directors on the audit committee, implying that this corporate governance mechanism has a significant complementary impact on transparency. Ownership concentration has a significantly negative *t* statistic, thus plays a substitutive role. These results lend support to agency theory and substantiate the first and second hypotheses of this study. Variables found not to have a significant association with the sample companies' transparency scores are: cross-directorships, foreign ownership, leverage, and profitability. Consequently, hypotheses H3, H4, H5 (a), H5 (b), H6 and H7 have been rejected at the 0.05 significance level. The results for each variable are discussed in detail in the following sections. As the results of both regression models are similar, the analysis of results will be based on the statistics from Model A.

5.5 Discussion of Results

The existence of a controlling shareholder is clearly a major explanatory variable of transparency in Zimbabwean companies. The *t* statistic is negative and significant at the 0.05 confidence level. This implies that devices to separate corporate ownership rights from the control of corporate resources may serve to facilitate and camouflage self-dealing and related rent seeking behaviour in Zimbabwe thus, do not constitute a functional alternative to improved corporate governance and better protection of minority shareholders' rights. Thus, agency theory, which holds that where there is separation of ownership and control shareholders press for more information disclosure for monitoring purposes, is supported and the first hypothesis of this study substantiated. The results of the Independent t-test lend further support to this. The results indicate a significant difference between the mean disclosure practices of companies with controlling shareholders, and those without. Having found no prior studies using the existence of a controlling shareholder as a proxy for ownership concentration comparisons are made with studies that have looked at the association between ownership concentration, *per se*, and disclosure. The negative association is consistent with previous empirical findings in other emerging economies, such as Firer and Williams (2003) for Singapore, Chau and Gray (2002) for Hong Kong and Singapore, Pham et al (2004) and Haniffa and Cooke (2002) for Malaysia. However, this is in contradiction with the results found by Owusu-Ansah (1998), and Hossain et al (1994). In a sample of 49 companies listed on the Zimbabwe Stock Exchange in 1994, Owusu-Ansah (1998) found a significant positive association to exist between ownership concentration and mandatory disclosure. The *t* statistic in his study was significant at the 10% level. It is suggested that this apparent contradiction arises from the differences in objects of study. Because this study is focused on both voluntary and mandatory disclosure practices, Zimbabwean companies with concentrated

ownership may choose to disclose less, perhaps to avoid losing control.

The audit committee variable has been found to be positively associated with transparency scores in both regression models. The *t* statistic of 6.361 indicates strong evidence that the audit committee variable significantly contributes to corporate transparency, thus hypothesis H2 is supported. The β value suggests that a percentage change in the composition of the audit committee will change the transparency score by 0.695. It may be concluded from both these statistics that the composition of the audit committee has the strongest effect of all the variables, on the transparency practices of the Zimbabwean companies in this sample. This implies a high proportion of non-executive directors on Zimbabwean audit committees reduces the scope that management perceive for acting opportunistically and improves transparency, lending support to agency theory. Several studies have found similar results in other emerging economies, for example, Balachandran and Bliss (2004) in Malaysia, and Chen and Jaggi (2000) and Leung and Horwitz (2004) in Hong Kong, and Williams (2002) in Singapore. Eng and Mak (2003), on the other hand, found a negative significant association between the increased presence of outside directors and disclosure in Singaporean firms. This result suggests that Singaporean outside directors may be elected by block holders to represent their interests and thus acquire information directly from the company, rather than through public disclosure. Thus, the external directors tend to play a substitute-monitoring role to disclosure. Audit committees have been found in prior studies to be positively associated with disclosure practice. For example, Ho and Wong (2001) found a significant, positive relationship between audit committees and the voluntary disclosure practices of Hong Kong companies. On the other hand, a previous study by Forker (1992) had only found a weak, and non-significant relationship.

The third corporate governance variable of cross-directorships was found to have a positive association with companies' transparency scores. Although the direction of the relationship was as predicted, the *t* statistic for the regression

coefficient is not significant at the 0.05 confidence level. Therefore, the third hypothesis is rejected. This is consistent with the only other study that has been found to test this hypothesis, Haniffa and Cooke (2002). Although they found a stronger association than in this study, the variable was not found to be a significant predictor of the disclosure behaviour of Malaysian companies. Although not significant, the positive association provides empirical evidence to the theory that when a director sits on more than one board, the company's preference for confidentiality and restriction on information disclosure is deterred, thus the 'individualistic' nature of companies no longer holds as information is shared among the companies through their directors (Gray, 1988).

Both tests of association, and tests of difference, were employed in order to test the hypothesis that companies with substantial foreign ownership are likely to have higher levels of transparency. As predicted, the results of the regression analysis suggest a positive association. Although the *t* statistic is not significant at the 0.05 level, it has a value (1.653) above the critical value for this sample size at the 0.10 confidence level (1.310). Therefore, these results provide weak support for the hypothesis that companies with some foreign ownership are likely to have higher levels of transparency. The Independent t-test for equality of means suggests no significant difference in the disclosure practices of companies with a substantial foreign shareholding (5%), and those that do not, however. The *t* value has a 1-tailed ρ value of 0.237. It can therefore be inferred that the presence of foreign investors has a negligible effect on the transparency levels of Zimbabwean companies. Although not significant at the 5% level, the positive association is consistent with Owusu-Ansah (1998), Ahmed and Nicholls (1994), and Haniffa and Cooke, (2002) who found a positive and significant association between foreign ownership/MNC affiliation and the disclosure practices of companies in Zimbabwe, Bangladesh, and Malaysia respectively. The positive relationship supports the argument that obtaining foreign funds means a greater need for transparency to monitor actions by

management. However, Soh (1996) and Hossain et al (1994) found a negative association.

The hypothesis that the extent of the average company's transparency score associates positively with the mean size of the companies in the sample was rejected. Although the positive association is consistent with agency theory and several other economic theories, the coefficients' *t* statistic was not significant at the 0.05 confidence level. However, the results were similar for both models, suggesting that mean Zimbabwean company transparency levels associate positively with mean corporate size; however size is measured. Although the positive association is consistent with several other empirical studies, the finding of a non-significant relationship is not. As noted by Foster (1986), "the variable most consistently reported as significant in studies examining differences across firms in their disclosure policy is firm size" and this is supported by previous findings reported in literature, such as Buzby (1975), Chow and Wong-Boren (1987), Eng and Mak (2003), Jaggi and Low (2000), McNally et al. (1982), and Wallace et al (1994). Other studies have found similar results to this, however. Williams (2002) found company size not to have a statistically significant association with voluntary audit committee disclosures in Singapore, as did Tai *et* al (1990) in Hong Kong. Contrary to the results in this study, Owusu-Ansah (1998), found positive, statistically significant, correlations for his Zimbabwean sample. The different objects of study may explain these differing results. As Owusu-Ansah's study focused on mandatory disclosure practices, it may be inferred that the management of the sample companies in this study exercised considerable discretion when it comes to voluntary disclosure.

The regression coefficient for the leverage variable shows a negative association with transparency, with a *t* statistic which is not significant at the 5% confidence level. While the results do not support agency theory, or the hypothesis in this study, they are consistent with findings by Williams (2002) and Meek et al (1995). Meek et al (1995) in particular, found a negative, but

statistically significant correlation between leverage and voluntary disclosure practices of sample firms in the UK, the US, and continental Europe. These findings question the implications in agency theory and cast doubt on Jensen and Meckling's (1976) argument that more highly leveraged companies incur greater monitoring costs, thus will disclose more information in an effort to reduce these. Meek et al (1995) argue that agency theory may not offer a good explanation of disclosure, and the company size phenomenon noted above may be related to the costs of information production, proprietary cost, or political cost theories rather than agency costs. However, some empirical research shows significant positive association between leverage and disclosure, for example; Malone et al (1993) for a US sample and Chow and Wong-Boren (1994) for a Mexican sample. It is suggested that these inconclusive results may arise from differences in the definition, and therefore measurement, of the leverage variable. On the other hand, finance theory argues that low-geared companies are low-risk and, following signalling theory, may choose to disclose more to signal this good news. Low leverage, and the consequent low risk, may especially be viewed as good news in a highly volatile economic environment such as Zimbabwe's, and may thus explain the negative correlation between leverage and transparency found in this study. On the other hand, the low *t* statistic indicates the probability that the negative sign may have occurred by chance.

Contrary to expectation, the final corporate attribute of profitability is found to have a negative association with the transparency scores of the sample companies and the *t* statistic is not significant at the 0.05 confidence level, thus hypothesis H7 is rejected. Interestingly, Owusu-Ansah (1998) found mixed results in his 1994 Zimbabwean sample. Out of the four regression models that he ran, only one found profitability to be a significant predictor of companies' mandatory disclosure practices, while it was not significant in the rest. While signalling theory suggests a positive association between disclosure and

profitability, there is an alternative school of thought. Labelle (2002) argues that a company with a less satisfactory performance might be tempted to improve the quality of its narrative statements in order to down play and justify the poor financial position, thus the direction of the association between profitability and transparency would be negative. Empirical evidence appears equally mixed. Cerf (1961), Singhvi and Desai (1971), and Haniffa and Cooke (2002), for example, provide empirical evidence of a positive association. On the other hand, Inchausti (1997), Meek et al. (1995), find no significant correlation between profitability and the level of disclosure in Spanish firms, and the US, UK, and continental European multinational corporations respectively, while Rutherford finds a negative association between performance and disclosure in a UK sample.

5.5 Robustness Checks

Several diagnostic tests were run in order to assess whether the regression model used in this study is a good fit of the observed data and can be generalised to the wider population of Zimbabwean companies. First, the possibility that certain cases might exert undue influence on the model parameters was investigated using standardised residuals and Cook's distance statistic. Cook's distance is a measure of the overall influence of a case on a model and Cook and Weisberg (1982) have suggested that values greater than 1 are cause for concern. It is generally expected that ninety-five percent of cases would have standardised residuals within ±2 (Field, 2000; Barrow, 2002). From the thirty-nine cases in this sample, two (5%) have standardised residuals outside the ±2 limits, and Cook's *D* statistics for these two cases are within the recommended threshold. Further, none of the DFBeta statistics for these two cases has an absolute value greater than 1, showing that they have no undue influence over the regression parameters. Thus from these diagnostics, the regression model appears reliable.

Table 9: Robustness Diagnostics

Case	Standardised Residuals	TRANSCR	Predicted Value	Residual	Cook's *D* Statistic
Cairns Holdings	2.171	0.553	0.469	0.084	0.070
Falcon Gold	-2.059	0.289	0.369	-0.080	0.243

a Dependent Variable: TRANSCR

Second, the regression model assumptions were checked using econometric criterion. The first assumption has been satisfied as all the predictor variables, and the outcome variable of transparency score are quantitative. The non-zero variance assumption is difficult to verify and often taken for granted (Berry, 1993). Similarly, it is assumed to hold in this study. The third assumption of independent errors holds that for any two observations the residual terms should be uncorrelated. The Durbin-Watson statistic tests for this autocorrelation phenomenon and a value close to 2, (2.096 is in this model), is generally accepted to mean the assumption of independent errors is tenable (Field, 2000).

The results of two related procedures for testing the fourth assumption of no perfect multicollinearity, tolerance and variance inflation factor (VIF) are presented in tables 7 and 8 for both regression models, and reproduced below for Model A. Four guidelines are given in statistics literature for detecting multicollinearity using these procedures. First, Myers (1990) and Bowerman and O'Connell, (1990) suggest there is cause for concern when the largest VIF is greater than 10. Second, if the average VIF is substantially greater than 1 then the regression may be biased. Third, tolerance levels below 0.1 indicate a serious problem. Finally, tolerance below 0.2 may indicate a potential problem (Menard, 1995). The results in the table below indicate, based on the four criteria, multicollinearity is not a problem in this study.

Table 10: Multicollinearity Diagnostics

Variable	*Tolerance*	*VIF*
Cntrl	0.799	1.251
Audit	0.738	1.355
Xdir	0.887	1.127
FrnOwn	0.793	1.261
LogSize	0.685	1.459
Levrg	0.614	1.629
Prft	0.638	1.569
Mean VIF		**1.379**

5.6 Summary

The results presented in this chapter suggest that corporate transparency levels of Zimbabwean businesses are weak. Further, the results of the regression models indicate that the variability in the transparency scores can best be explained in terms of a company's ownership structure and the number of non-executive directors on the audit committee. Of these predictor variables, audit committee composition is a very critical explanatory variable as it had a strong regression coefficient. Thus of the seven hypotheses developed in this study, hypotheses 3 to 7 were rejected. Robustness diagnostics indicate that the regression models employed are reliable and the results of this study can thus be generalized to the wider population of all Zimbabwean companies.

CHAPTER 6

CONCLUSIONS, LIMITATIONS, AND POLICY IMPLICATIONS

6.1 Introduction

This chapter contains the summary and overall conclusions that have been drawn from this dissertation. It discusses the limitations of the research

methodology and statistical techniques employed on the data in an attempt to fulfil the two objectives set out in Chapter 1. Further, possible policy implications of the findings of this study are set out in section 6.2, while further areas for research are identified in section 6.3.

6.2 Conclusions and Policy Implications

The objective of this study was twofold: (1) to assess the corporate transparency of Zimbabwean businesses; and (2) empirically explain the variability in the transparency levels of the sample companies in terms of four corporate governance, and three company-specific attributes. The four corporate governance mechanisms in question were ownership concentration, audit committee composition, cross directorships, and foreign ownership. The company-specific attributes of company size, profitability, and leverage were also examined. In respect to the first objective, results lead to the conclusion that Zimbabwean publicly listed companies have low levels of transparency. The results provide support for the argument that companies in emerging economies are opaque. Although quite low, the mean score of 52% is comparable to the transparency scores of other emerging economies. In their study of transparency and disclosure in 19 emerging markets, Standard and Poor find the mean scores of their sample companies to range from 22% to 55%, with varying country means from 29% for Latin America to 55% in South Africa (Patel et al, 2002). However, a disaggregating of the scores of the sample companies on the basis of the three broad categories of financial transparency, board structure, and ownership structure, indicate that low transparency scores are found in the corporate governance categories of board and ownership structure, while financial information disclosures are relatively high.

Although the reported results are based on a sample of 39 public listed companies, the results can be generalised to all other ZSE listed companies and the wider population of all public companies in Zimbabwe. One important policy implication arising from these results relates to the public policy concerning the

need to regulate corporate governance disclosures. Opponents of disclosure regulation suggest that mandatory requirements will lead companies to a ‘box-ticking’ approach and limit the disclosure of useful information to stakeholders. However, while in fully developed capital markets private intermediaries may support non-legal incentives to make accurate disclosure, in capital markets with less fully evolved private institutions such as Zimbabwe, legal mandate may be necessary to allow honest companies credibly to distinguish themselves from dishonest companies (Gilson, 2000).

It must be emphasised, however, that mandatory disclosure is no more effective than a company’s expectation that the rules will be enforced. There is evidence from this study that disclosure regulatory enforcement in Zimbabwe may not be stringent. Although the category of financial transparency yielded the highest score in this study, the mean score was still only 61% despite the high ratio of mandatory to voluntary disclosure items in the category. These results also have implications for the audit profession in Zimbabwe. Although the majority of Zimbabwean companies are audited by the ‘big 5’ auditing firms, the findings suggest that these auditors need to be more independent and vigilant in their audits and opinions in order to ensure compliance with regulations. The policy makers in Zimbabwe appear cognizant of the need for stringent monitoring however. The ZSE has recently reported that plans to set up a monitoring panel that would review all publications by listed companies are at an advanced stage (Dube, 2004). The ZSE chief executive stated that the purpose of this panel would be to ensure that listed companies published correct information and that listed companies were transparent in their conduct.

The second conclusion relates to the statistical results of the multiple regression analysis to test the hypotheses developed in Chapter 3. The results indicate that the variability in the transparency scores can best be explained in terms of a company’s ownership structure and the number of non-executive directors on

the audit committee. Of these predictor variables, audit committee composition is a very critical explanatory variable as it had a strong regression coefficient in both models. These results are consistent with agency theory and comparable to studies by Chau and Gray (2002) for Hong Kong and Singapore, Pham et al (2004) and Haniffa and Cooke (2002) for Malaysia, and Williams (2002) in Singapore. As the diagnostics for the statistical model indicate that it can be generalised, these findings suggest that corporate governance mechanisms play a substantial role in the disclosure policies of Zimbabwean companies. Thus, transparency levels can be improved by making appropriate adjustments to companies' corporate governance structures, namely board of directors and ownership structures. There is therefore scope for policy intervention through the encouragement of shareholder activism and strengthening minority protection to minimise rent-seeking behaviour by block holders, enhancing the governance of institutional investors, and encouraging disclosure of ownership and control to enhance the market for corporate control. The codification of a corporate governance manual that is uniquely Zimbabwean and suitable for the socio-economic environment of Zimbabwean companies may thus provide an alternative to regulation, while achieving similar results. Currently, ZSE listed companies are required to comply with either the King Report of South Africa, or the UK's Combined Code. Companies such as Delta Corporation and Anglo American have devised their own in-house corporate governance manuals.

The findings from this study have implications for company directors. A lack of transparency by a company with a majority of non-executive directors on the board, for example, may be construed by potential investors as a deliberate failing to provide greater transparency when the board has both the incentive and ability to do so. In the long term, stakeholders may lose confidence in the corporate accountability of the company, affecting the reputation of the directors and, consequently, the value of the company. Results indicate that about 88% of the companies in the sample have a majority of non-executive directors on the

audit committees; thus this risk may be aggregated to the Zimbabwean economy as a whole and have negative consequences for investor confidence in the accountability of Zimbabwean companies, thereby affecting the economy's development opportunities.

An interesting result from this study was the lack of support for the hypothesis that company size has a positive impact on transparency levels. This is contrary to theory and several empirical studies (for example; Buzby, 1975; Chow and Wong-Boren, 1987; Eng and Mak, 2003; Jaggi and Low, 2000; and Wallace et al, 1994). This may indicate that company size is not a significant factor in Zimbabwean companies' disclosure policies. However, as an earlier study on ZSE companies found company size to be significantly positively related to mandatory disclosure practices, it may be inferred from this study that larger companies' management exercise considerable discretion in the disclosure of voluntary information. Other variables found not to have a significant association with disclosure are: cross-directorships, foreign ownership, leverage, and profitability.

6.3 Limitations and Further Research

The conclusions drawn from this study should be considered in light of the following potential limitations. First, the use of the transparency scorecard means that this study does not assess the quality of corporate transparency. Thus, it suffers from the conceptual limitation that high levels of transparency are better than low levels. It has been analytically demonstrated that more information is not necessarily better, however. For example, literature on information economics has documented instances where more disclosure is Pareto inferior to less disclosure (for example; Hirshleifer, 1971). High levels of transparency may also lead to information over-load, more so in an emerging economy where a greater proportion of corporate annual report users are

unsophisticated (for example; Jagetia and Nwadike, 1983). As pointed out by Healy and Palepu (2001), experts' ratings are a noisy measure of transparency and consequently, may limit the power of the tests. This is exacerbated by the less formal aspects of corporate governance practices, which are more difficult to measure and may be more sensitive to changes in incentives to disclose. Thus, future research may examine Zimbabwean managers' motives to make corporate governance disclosures.

Second, corporate transparency has been assessed in terms of information disclosed in the corporate annual reports and accounts. Although this may encompass the institutional infrastructures of mandatory disclosure, accounting standards and, to some extent, the audit profession, corporate transparency encompasses the joint output of a multi-faceted system whose components collectively produce, gather, validate, and disseminate information to market participants outside the firm. It is thus a broad concept that is affected by, and should be assessed in terms of, other country-level discretionary factors. Moreover, companies use other disclosure media such as interim reports, prospectuses, and analysts' conferences to disseminate corporate information. The annual report is assumed to serve as a good proxy for other media, however, and Lang and Ludholm (1993) have found corporate annual report disclosures to positively correlate with disclosures provided in these media. Further, the annual report is the major source of official, regulated corporate information in Zimbabwe (Oppong, 1993).

Third, the study is cross-sectional in nature, thus the conclusions drawn relate to the transparency levels of the sample companies for the 2003 financial year. As regulatory environments change in response to local and international pressure, a longitudinal study would provide a more complete picture of the corporate transparency in Zimbabwean businesses. Fourth, the resulting model explained about 67% of the variability in corporate transparency, there is therefore a

possibility of omitted variables from the regression model. Due to data unavailability, some factors that have been found to explain the variability in corporate transparency such as company age and group affiliation have not been examined in this study. The high explanatory power of the model would, however, suggest that most of the significant variables have been captured in the model. Finally, the study is based on a sample of 39 ZSE listed companies. Although the robustness checks on the regression model suggest that the results can be generalised, replication of this study with a larger number of companies in other countries may assist in establishing whether the results reported are supported, and enable global comparison.

Notwithstanding the above limitations however, the present study contributes to extant literature. First, the study provides unique evidence of transparency levels amongst publicly listed companies in Zimbabwe. It extends current literature on Zimbabwean corporate reporting by examining both voluntary and mandatory financial and corporate governance disclosures. Second, this study adds to the literature on companies' corporate transparency practices in economic crises. Third, the explanatory power of the multiple regression model is sufficiently high to warrant an extension of the results to a larger sample size, and other African economies.

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