

The Effect of Financial Statement Disclosure on Changes in Stock Prices: Empirical Evidence of Colombo Stock Exchange

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Abstract

Share price of stock change according to the information given in the market. Financial statement is one of the most important factors which publish the financial and nonfinancial information regarding the organization. Major components of the financial statements are income statement, yearend balance sheet, cash flow statement, equity statement and notes. Financial statement disclosures provide most important information regarding the organizations to the stockholders. Information generated by the financial statement disclosure helps internal users to make a management decision regarding organizational activities. And also the information helps to external paritiesfor their investment decisions. Financial statements provide financial and non-financial information which helps to stockholders to make and analysis on organization's activities. Information disclosure helps to reduce the risk in decision making because of information provides a better understanding on analysis the data.

The main objective of this study is to examine the effect of financial statement disclosure on stock price movement with special reference to Colombo Stock Market. The study attempts investigate the existence of abnormal return of share prices around the period of the financial statement disclosure by using event study methodology. The data collected form secondary sources.

The behavior of share price movement will be evaluated by using daily share price of registered companies in Colombo Stock Exchange. The selected sample for the study is 20 S & P companies registered under Colombo Stock Market. Share prices of 20 S & P companies are analyzed and market model is applied to estimate the expected return and then relate with actual share prices to estimate the abnormal return within the event window.

Results show a significant difference between share price before and after the financial statement disclosure. Share prices are changing due to the information provided by the financial statement. Based on financial figures shown in the financial statement will impact on share prices movements. Research study data explain the positive relationship between financial statement disclosure and share price movement. Finally, results show that the financial statement disclosure effecting on the share price.

Key Words: financial statement disclosure, share prices, standard and poor (S & P), Colombo stock exchange (CSE).

Introduction

The main objective of financial statements is to provide the information regarding financial position and changes in financial position which are more useful for users in making the economic decisions. The financial statements provide the information in relating to the company financial position, operating results, company cash flows and equity changes details. Based on the information disclosure by the company will create the levels of valuation regarding the company shares. Due to the demand and the supply of the share trading will have decided the share price and also the results generate by the financial statements will give the influence to the shareholders in order to increase or decrease their level interest on the share investment.

Thus, the aim of this study to investigate the relationship among the share price disclosure and the share prices changes. And also identify the level of indicators which information generated by the financial statements. The investigation will help to the investors on their investment decision making on the companies registered in Colombo Stock Exchange in Sri Lanka.

Statement of the Research Problem

Accounting information usually in the form of financial statements is communicated to the external users. Main purpose of the accounting information is assisting the users in making sound financial decisions. Information disclosure of the organization may help to the investors on their financial decision. Information disclosures by the financial statement will impact to share price movement in the market. Therefore, the financial statements disclosures and the information disclosures by the financial statements are important to investors to make their investment decision.

Research Question

The main purpose of this research is to examine the impact of financial statements disclosure on the fluctuation of share prices. To examine the changes of share price, financial statements disclosure has been investigated through the financial statement disclosure date. Therefore, this research aims to address the following research question by adopting the event study methodology.

- What is the response of share prices on the disclosure of financial statements among the selected companies?

Research Objective

The major objective of the study is to identify the relationship between share price changes in relating to the financial statements disclosure. The specific objective of the study is;

- To examine the effect of financial statement disclosure of share price movement with the empirical evidence from Colombo Stock Exchange

Significance of the Study

Using the results of the share prices investigation give the understating to the investors regarding the share prices fluctuation based on the information shared by the organization. Based on the information available in the market implicate the share price of the market because of information creates the demand on the stocks. ShukaiiriNoriMousa (2015) explain on his study that the financial statement announcements and the effect of that information on investors behavior, and its contributions to the investors either current or anticipated to perform and build their investment strategies and contributions to the academic fields by providing a new perspective in finding out the efficiency of selected sample, academic fields will be able to gain better understanding in the interaction between the information content and efficiency of markets.

Literature Review

Financial disclosure (corporate disclosure) practices are an important mechanism in the functioning of an efficient capital market because they provide investors and potential investors with useful and reliable information regarding the operations and processes of a company and its management,GuilhermeKirchet *al* (2012).

Based on the theoretical framework of financial reporting information that is useful, relevant, reliable, and understandable, AbolfazlGhadiriMoghaddamet *al* (2014).

Firms with a high level of information disclosure have a higher association between accounting earnings (EPS) and stock market price than the firms with low levels of information disclosure, positively significant relationship between book value and stock prices. Furthermore, we found that positively significant association between earnings per share and stock price. Hwei Cheng Wang and Hsain-Jane Chang (2008).

More issues in accounting need judgment and decision making. Decision related to voluntary disclosure by management or using voluntary disclosure by investors and analysis are as an example of these decisions, there is positive and significance relationship between voluntary disclosure and stock price, asset return rate, earning per share, firm size, gold price and exchange rate impact controlled. AbolfazlGhadiriMoghaddamet *al* (2014).

According to the stock prices responsiveness to new information, we can describe that process as very slowly because of the existence of abnormal return during the days following the event. There is a delay stock prices response to new information which is seemed by the existence of abnormal return during the period surround the event: this is certain that publishing financial statements has an information content but the process of generating abnormal return certain the daily of adjusting prices to that event and the under action response. ShukaiiriNoriMousa (2015).

Conceptual Framework

Financial statements give all relevance information for external users. For the research purpose the main three indicators which are reflecting to the share price has been selected. Share price before disclosure the financial statement indicates as the independent variable and share price after disclosure the financial statement indicate as the dependent variable. Financial statements disclosure date differentiates the before and after share prices.

The model of the research can be explained as follows;

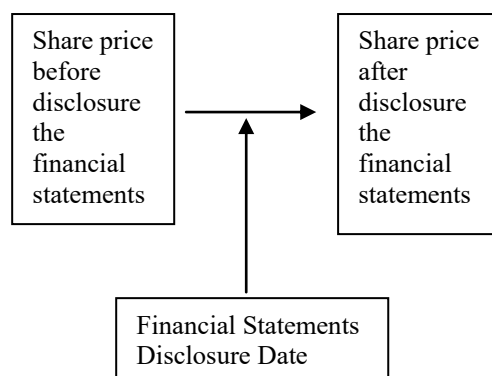


Figure1. Conceptual Framework

For the purpose of analysis this study uses the event study to identify the share price and the variance between real share price and expected share price to estimate the abnormal return with effect to financial statement publication date. Paired sample t-test used to test to hypothesis to measure the difference between abnormal return before and after the financial statement disclosure date.

Hypothesis

In order to find the relationship between financial statement disclosure and the share price, the following hypothesis is formed.

$$H0: \mu (A) = \mu (B)$$

$$H1: \mu (A) \neq \mu (B)$$

$\mu (A)$: Mean value of share price after financial statement disclosure

$\mu (B)$: Mean value of share price before financial statement disclosure

In the same manner the hypothesis we can explain the following way of consider;

H0: There is no difference between share return after financial statement disclosure and the share return before financial statement disclosure.

H1: There is a difference between share return after financial statement disclosure and the share return before financial statement disclosure.

Table 1. Operationalization of Variables

Concept	Indicator	Measure	Reference
Independent Variable	Share price before disclosure the financial statements	Average share price measure before disclosure the financial statements	ShukairiNoriMou sa, (2015),
Dependent Variable	Share price before disclosure the	Average share price measure after	ShukairiNoriMou sa, (2015),

	financial statements	disclosure the financial statements	
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Methodology

The main objective of this study to investigate the relationship among the share price changes due to the financial statement disclosure of listed companies in CSE. For the purpose of finding data was collected by secondary data from the company's annual reports which have been registered in Colombo Stock Exchange and share price changes in stock market.

Sample Selection

There are 20 Standard and Poor companies (S & P) in CSE. These 20 companies are the top companies out of 295 companies those registered under Colombo Stock Exchange. All listed companies which are registered in CSE consider as the proposed population of the research study. Sample of the population will be selected as S & P 20. Five years' data collected for data analysis (2012 to 2016) in each company. 19 Companies were analyzed in the study. One company has acquired by the holding company. Therefore, the relevance past data were not found.

Method of Data Collection and Evaluation

Data is collected before 10 days from the date of financial statement disclosure and 10 days after the financial statement disclosure. One month of average share price calculated for to analysis the abnormal return.

The collected data was analyzed by using the SPSS software (version 16.0) and tool will be analyzing with related analyzes charts will be used to interpret the significance changes in share price. The paired sample t-test used to interpret the relationship among the selected variables.

Data Analysis

The selected sample for the data analysis is S & P 20 companies in stock market. Distilleries Company of Sri Lanka PLC not considered for the analysis. Because of lack of the information due to their recent merge in company.

Table 1 shows the average share price for S & P Companies involved in the study sample before and after the event. (10 days before and 10 days after the financial statement disclosure for five years' average data used for analysis and expected return calculated by using 30 days' average share return for each year in each organization for five years).

Table 2. Total Average Abnormal Return

Serial	Days before \ after	Average Return	Abnormal
1	-10	-0.7934	
2	-9	-0.8660	
3	-8	-1.0734	
4	-7	-0.2723	
5	-6	0.0749	
6	-5	-1.4744	
7	-4	-1.4166	
8	-3	-0.9387	
9	-2	-0.2787	
10	-1	0.7065	
11	0	-5.2276	
12	1	-0.0839	
13	2	-0.1629	
14	3	0.0791	
15	4	1.8928	
16	5	2.3149	
17	6	2.5149	
18	7	1.1907	
19	8	4.2855	
20	9	2.9749	
21	10	3.9518	

Results of the Table 2 indicate the positive average abnormal return after financial statement disclosure. After fourth day of financial statement disclosure shows the positive and slightly increasing average abnormal return. Following diagram shows price changes clearly.

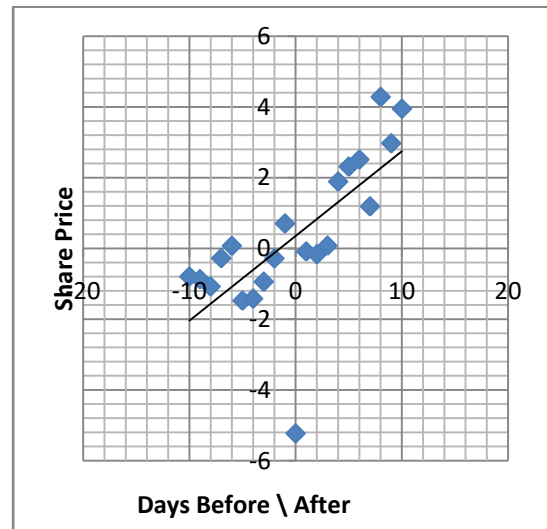


Figure 2. Total Average Abnormal Return

Following figure explain the summary of share price in each S & P companies for five years with compare to the financial statement disclose date.

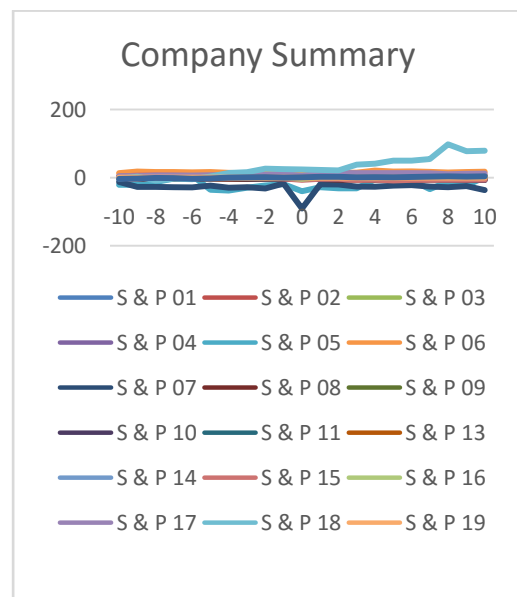


Figure 3. All Average Abnormal Return in S & P Companies

Paired Sample t-test

Table 2 shows the statistical evidences of mean difference of share price before and after the financial statement disclosure.

Table 3. Paired Sample t-test

Paired Samples Statistics					
	Mean	N	Std. Deviation	Std. Error Mean	
Share Price Before	.6332	10	.68645	.21707	
Share Price After	1.8958	10	1.61990	.51226	
Paired Samples Test					
Mean	Std. Deviation	Std. Error Mean	t	df	
-2.52905	2.03060	.64213	-3.939	9	
95% Confidence Interval of the Difference			Sig. (2-tailed)		
Upper	Lower				
-3.98166	-1.07645		0.03		

Mean difference between share price before and after the financial statement disclosure is -2.52905. Since the p value is 0.003, there was a significant average difference between share price before and after the financial statement disclosure. ($t_9 = -3.939$, $p < 0.05$). on average share prices before the financial statement disclosure were 2.52905 lower than the share price after the financial statement disclosure. (95% CI [-3.98166, -1.07645]).

Table 4. Decision Table

H0	H1	P value	Decision	Conclusion
$\mu_A = \mu_B$	$\mu_A \neq \mu_B$	0.003	Reject H0	There is a significant difference between share price before and after the financial statement disclosure

Conclusion

Results show the significant difference between share price before and after the financial statement disclosure. Figure of total average abnormal return shows that there

is a positive impact of financial statement disclosures on share price movements. Shareholders use the financial statement publications as a main source to get the information regarding financial performance of the organizations. With the financial results show in the financial statements, shareholders tend to sell or purchase shares in the particular organizations. Share price will be changed due to the demand and supply of the share in the stock market. Based on the sample results show the positive results of price change after financial statement disclosure. Share prices depend on the results shown in financial statement. Higher performance information in the financial statement tends to increase the share price in the particular organization and lower performance information in the financial statement tends to decrease the share price in the particular organization. Finally, results show that the financial statement disclosure effecting on the share price.

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