

THE ROLE OF CORPORATE GOVERNANCE ON THE INFORMATIVENESS OF THE DEVELOPING COUNTRIES FINANCIAL STATEMENTS

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ABSTRACT. Corporate governance analysis is vital for understanding corporate dynamics and boosting investor confidence. Its disclosure in financial statements enhances transparency, reduces information asymmetry, and lowers agency costs, thereby increasing firm value and profitability. In Zimbabwe, poor adherence to governance principles affects the informativeness of financial statements. This study explores firm-level governance indicators: board effectiveness, director liability, shareholder rights, transparency, and minority protection and their impact on financial reporting. Using interviews with top management, thematic analysis revealed that effective governance improves financial statement quality. The study recommends mandatory disclosure of governance aspects to foster investor trust, accountability, and company growth despite political and economic challenges.

Keywords: Corporate Governance, Financial statements, Informativeness, firm's level, Zimbabwe

JEL classification: G34; M41

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Introduction

Recently, analysing corporate governance has become crucial for understanding corporate dynamics and gauging investor confidence in management and board decisions. Consequently, corporate governance disclosure is gaining increasing attention from both professionals and academics. Hence, financial reporting now extends beyond financial disclosures to include non-financial information, such as governance practices, in annual reports. Corporate governance disclosure details a company's governance characteristics and activities, providing crucial information to the capital market for evaluating the effectiveness of each firm's governance system. This transparency reduces information asymmetry between internal and external stakeholders, thereby lowering agency costs and enhancing firm value (Durnev & Kim, 2005). Aren *et al.* (2014) revealed that companies with that practise corporate governance benefit from lower costs of capital as a result of lower risk score. As a result of lower risk, the company's profitability increases. There is a dearth of studies that have focused on the role of corporate governance on the informativeness of financial statements in developing countries such as Zimbabwe. It follows therefore, that this study investigates the role of corporate governance in enhancing the financial statements. According to Mappingire (2016), some Zimbabwean companies do not uphold corporate governance principles, and as such, the informativeness of their financial statements provided to stakeholders remains a bone of contention.

According to World Economic Forum (2015), the firm level, good governance, legal systems and financial development are the four determinants of corporate governance. These determinants are key indicators of effective corporate governance systems in individual companies (Matashu, 2016; World Economic Forum, 2015). This paper concentrates on the firm level determinant of effective corporate governance and its role on the informativeness of the financial statements. These determinants include the Board responsibilities and effectiveness of the board, Director liability, shareholders' rights, disclosure and transparency and protection of minority shareholders. An effective corporate governance mechanism ensures the maximisation of shareholders' wealth. Hence, the financial statement's informativeness positively correlates with the stakeholders' wealth maximisation (Nwaobia & Ajayi, 2021). The effective corporate governance mechanisms are expected to play a major role in enhancing the informativeness of financial statements. This study is important because it can influence policymakers, practitioners, and future studies interested in developing countries' corporate governance indicators and the informativeness of their financial statements.

Corporate governance in Zimbabwe

Maune (2017) reiterates that the notion of governance has been known for several years. In addition, the existence of the governance concept is equated to any form of human organisation. Corporate governance focuses on how companies are controlled and directed by those charged with governance. In recent years, corporate governance has become a matter of great concern in the corporation. This is because of scandals and the folding of various companies (Maune, 2017). For instance, corporate governance has attracted much attention in Zimbabwe since the 2008 financial crisis. Zimbabwean companies that have been part of high-profile scandals due to weak and poor corporate governance mechanisms include Air Zimbabwe, Premier Service Medical Aid Society (PSMAS), Zimbabwe Revenue Authority (ZIMRA), National Railways of Zimbabwe (NRZ), National Oil Company of Zimbabwe (NOCZIM), African Renaissance Bank (AFRE), United Merchant Bank (UMB), ENG Capital and Barbican Bank and so on. In 2015, Zimbabwe launched a national code of corporate governance as a measure to curb corruption and fraud. The Companies Act (2006), Amended Zimbabwe Stock Exchange Act (1996), Public Finance Management Act (2009), Public Entities Corporate Governance Act (2018), National Code on Corporate Governance Zimbabwe (NCCGZ) and rules from some professional bodies such as the Institute of Directors of Zimbabwe (IoDZ) have formed part in regulating corporate governance in Zimbabwe. The adoption of the code is voluntary to all entities, and its enforcement is on an 'apply or explain' basis. The code gives companies an opportunity to exercise transparency and accountability to its stake holders (Oxley, 2015).

In order to address corporate failures and operational difficulties comprehensively, the Zimbabwe Leadership Forum (Zimleaf), and the Institute of Directors, Zimbabwe (IoDZ) took the initiative (NCCGZ, 2014). The IoDZ trains Zimbabwean managers and company directors on prestigious competence and professionalism. A special purpose committee established by IoDZ is responsible for creating and distributing corporate governance rules. ZimLeaf oversees, among other things, advocating for policies, evaluating research, and conducting training to ensure adherence to good governance standards. These entities took the lead in developing and implementing a national corporate governance code that applies to all areas of the economy. IoDZ and Zimleaf, however, are only able to promote compliance; they are unable to compel any organisation to adhere to good corporate governance practices. Zimbabwe has high standards of corporate governance from a business perspective, despite concerns that political governance norms may permeate the sector. On the other hand, the Government of Zimbabwe, also established a corporate governance

unit (CGU) that governs how the state-owned entities and parastatals operate through the Public Entities Corporate Governance Act of 2018. The act was established to mitigate the misappropriation of assets and fraudulent activities.

Literature review

Defining corporate governance

According to IoDSA (2016), corporate governance is defined as an exercise of ethical and effective leadership. It is used to govern and manage institutions to achieve exceptional outcomes. Corporate governance shapes the organisation's ethical culture, its performance, effectiveness on controls and legitimacy (IoDSA, 2016). Similarly, Crowther & Seifi (2011) revealed that corporate governance is about creating moral values, trust, ethics and confidence to stakeholders. Thus, good corporate governance requires a multi-faceted approach where internal and external stakeholders are recognised.

In the context of Zimbabwe institutions, according to Hamadziripi & Osode (2021) corporate governance includes processes and structure that help to direct and manage companies. This is influenced by management desire to ensure that companies are in a sound state and are able to attract investors and enhance profitability. Corporate governance is about the division of power to manage the companies. The stakeholders, board of directors and management devise system that ensure transparency and accountability to protect the interest of all stakeholder groups (Maune, 2015). Corporate governance can also be understood as a system that public and private institutions or non-governmental organisations (NGOs) use to direct, control and ensure accountability to its stakeholders (Public Entities Corporate Governance Act, 2018). IoDSA (2016) suggest that corporate governance is about systems, policies and direction. It also ensures that the organisation conform to relevant laws and regulations that govern the industry.

In conclusion, despite extensive discussions among policymakers and scholars, there is still no clear agreement on a single definition of corporate governance or institutional quality. Numerous authors and organisations have proposed a variety of definitions. It can be deduced that the definitions given above are context-dependent and grounded on schools of thought. The following section unpacks the key indicators of effective corporate governance. These include Board responsibilities and effectiveness of the board, Directors' liability, Shareholders' rights, Disclosure and transparency and protection of minority shareholders.

Conceptual framework

This section of the paper analyses effective corporate governance concepts and seeks to establish how these concepts affect the informativeness of the financial statements. The conceptual framework builds on the earlier discussions from the introduction and background sections.

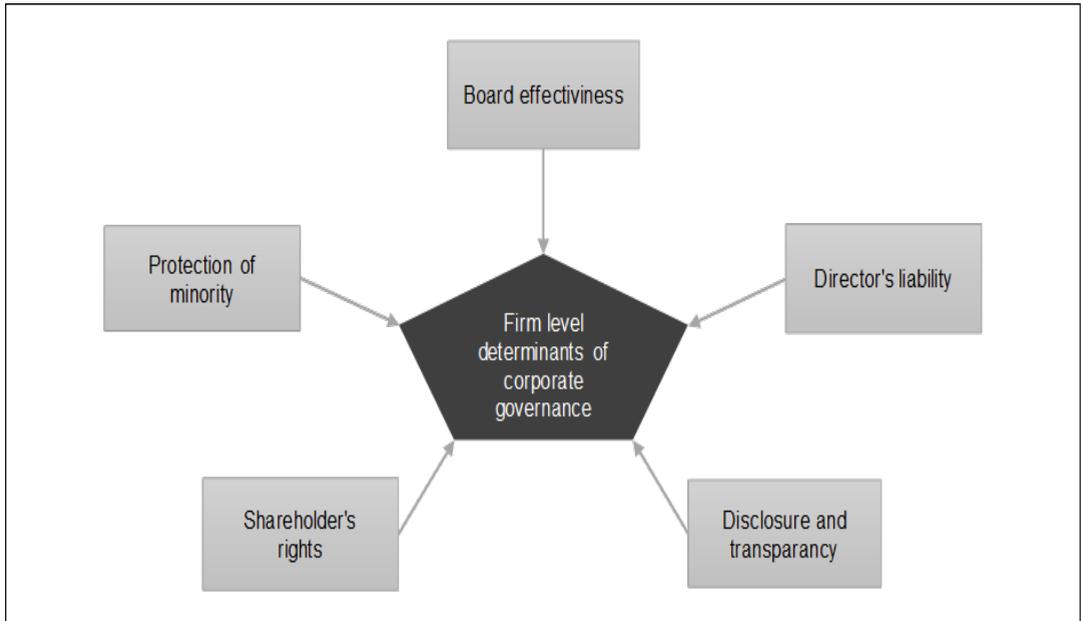


Figure 1: Determinants of effective corporate Governance
Source: Author's compilation

Board effectiveness

The desire to maximise the board effectiveness have been constant and somewhat indefinite in corporate governance objectives in public and private sector (Jafeel *et al.*, 2024). This implies that the board effectiveness is a goal that organisations envy to achieve throughout their existence. Salehi & Hassanzadeh (2024) revealed that an effective board sets out a clear business strategy and vision, it inculcates a culture of accountability and transparency in the organisation. Goyal *et al.* (2024) assert that an effective board provides support to the organisation CEO, communicates inclusively, resolve conflicts amicable

and exercise influence rather than power in the execution of its duties. It can be deduced from the scholarly views that board effectiveness has to do with the performances of board members either individually or collectively when taking up their responsibilities and duties. The effectiveness of the board is measured using the performance indicators such as clear roles and responsibilities defined for each member in the organisation, effective measures to manage risk, the board composition and diversity, availability of processes of learning and improvement, availability of systems to ensure compliance with the laws and regulations and presents committee structures.

However, some scholars are of the view that the board effectiveness can be determined using the organisation's profitability. The perception is that the profitable organisations have effective boards, this view lacks objective as they are many underlining factors that can influence profitability outside the board. Goyal *et al.* (2024) suggest that the board members provide a healthy tone across the organisation by providing expert and independent input when executing their duties. Hence, it is imperative to establish if the effectiveness of the board has a significant implication on the informativeness of the financial statements.

Directors' liability

The term directors' liability refers to the legal responsibility that the directors have on the organisation they are serving. The IoDSA (2016) suggest that directors' duties are set out in the common law and in the Companies Act. The Act stipulates that directors should act in the best interest of the organisation, exercise due care, proficiency and thoroughness when carrying out their organisation duties. The IoDSA (2009) report assert that the directors should provide ethical and effective leadership in which the IoDSA (2016) further revealed that the directors should execute their duties in line with the Companies Act to avoid being subjected to criminality punishment such as fines and disqualification from serving as directors in the future. The directors are liable for recklessly trading where their conduct is deemed to have intentions of defrauding creditors. In addition, the directors of a company may be liable for the loss, or damages caused by the direct or indirect conduct in carrying their duties (Stevens & De Beer, 2016). According to Wandrag (2018) the civil law the directors do not incur personal liability if they are acting on behalf of the company. This implies that the commitment they enter a bind the company. However, they are liable when there in mismanagement. It can be concluded that it is imperative to establish the directors' liability role on the informativeness of the financial statements.

Shareholder Rights

Matashu (2016) avows that shareholders have a right to receive a dividend and also a right to control management through voting. The author further describes these rights as procedural entitlements for shareholders. La Porta *et al.* (1997) established an anti-director rights index, the index measures legal protections for investors. The index has several rights such as the simplicity of polling for the directors, cumulative voting, trading shares during meetings, pre-emptive rights for new securities, minority board representation, grievance mechanisms, and the percentage of votes needed for extraordinary meetings. These shareholder ownership rights and meeting procedures indicates the level of shareholder protection. Standard & Poor (2008) note that shareholder rights are frailer in countries with poor legal systems. Agency theory and property rights theory both affirm shareholders' rights over their investments. Dallas (2004) distinguishes cash flow rights (dividends and sale proceeds) from control rights (voting and meeting participation).

Disclosure and Transparency

Standard & Poor (2008) revealed that disclosure and transparency cover appropriate distribution of information about a company's operations, governance and financial performance. Disclosure and transparency refer to the process of publishing annual financial statements (statement of financial position, and statement of cash flows) and directors' reports (Dallas, 2004). Additionally, Dallas (2004), assert that disclosure and transparency permit the stakeholders to monitor company performance. The stakeholders require reliable information to make informed economic decisions (Standard & Poor, 2008). The failure to adhere to corporate governance principles such as disclosure and transparency in African countries has negatively affected the economic growth (Waweru, 2014). Okeahalam & Akinboade (2003), Okeahalam (2004), and Waweru (2014) argue that improved corporate governance can enhance the market value of African firms, attracting foreign investment and boosting economic growth. Studies by Kaunda & Pelsler (2023) and Leung & Cheng (2013) show a significant relationship between disclosure, transparency, and value of the company, as measured by Tobin's Q and ROA. Standard & Poor (2008) also highlight that inadequate disclosure, and transparency can deter investment, cause share undervaluation, and increase costs. The efficiency market hypothesis (EMH) by Fama (1980) supports the idea that transparency lowers the cost of capital by reflecting available information in share prices. Lack of disclosure and transparency can lead to low economic growth due to perceived investment risks. It is imperative to ascertain the role of the disclosure and transparency determinant on the informativeness of the financial statements.

Protection of minority shareholders' rights

Minority shareholders require protection due to their limited influence on organizational decisions. Matashu (2016) notes that without legal safeguards, minority shareholders risk having their investments expropriated by controlling shareholders. Different ownership structures, such as family, shareholder, or institutional ownership, necessitate this protection (Matashu, 2016). Solomon (2011) highlights that in companies with major shareholders, minority shareholders are often dominated by larger controlling shareholders. To ensure equitable treatment, measures like equal voting rights and meeting attendance for shares of the same class are essential (Wandrag, 2018). Djankov *et al.* (2006) developed an anti-self-dealing index to assess minority shareholder protection. Wandrag (2018), vows that the enforcement of laws against self-dealing in the public and private sectors is vital for defending minority shareholders. The legal system in developing countries is weak and it often fails to protect the rights of the minority groups (Solomon, 2011). Consequently, corporate governance in African economies is hindered by the lack of minority shareholder protection and weak legal frameworks. In light of the above discussions on the protection of minority shareholders' rights, it is imperative to establish the function of corporate governance on the informativeness of the financial statements.

Research Methodology

The study adopted an interpretivist research philosophy, which resulted in a deeper understandings and interpretations of the study phenomenon (Saunders *et al.*, 2012). This approach allowed the study to explore various perspectives on effective corporate governance indicators from different organisational stakeholders. The study's population consisted of 24 top management members, including accountants, financial controllers, human resources managers, audit managers, finance directors, general managers, and corporate affairs executives. These participants were chosen for their knowledge, competence, and relevance to this research topic. Participants from finance and administration departments, responsible for preparing and presenting financial statements, were included due to their expertise. The study used both face-to-face and telephone interviews, reaching a saturation point after 12 interviews with six of the largest Zimbabwean companies, as guided by Snyder (2019). The results were analysed and interpreted using a thematic analysis. According to Clarke & Braun (2013) thematic analysis involves the identification of key themes which are critical in understanding the views, opinions, values and lived experiences of the participants. Through the thematic analysis, the researchers were able to identify themes and patterns from the data collected through conducting interviews. Six steps were followed during

the process and this allowed rigour to enhance credibility and trustworthiness of this paper. The first step involved familiarising with the data collected through interviews and deciding on how to group the codes. Secondly, the initial codes were generated based on the interview results. After establishing the codes based on their similarities, the researchers had to find the themes and group them on three categories, that is, basic, organising and global themes. The fourth step, involved the reviewing the identified themes to ensure they are grouped accordingly and the fifth step, defining and naming of the themes was done and lastly, a comprehensive report was produced. The following section provides the findings of this paper based on the interviews' results.

Discussion of the results

Effective corporate governance has an important role in enhancing the informativeness of financial statements. The paper established that to improve the quality of the financial statements, the following aspects of effective corporate governance should be considered, and these are Board responsibilities and effectiveness of the Board, Directors' liability, Shareholders' rights, disclosure and transparency and protection of minority shareholders. The researcher outlined the disclosure criteria of the firm level determinants of corporate governance as a strategy to enrich the informativeness of the financial statements, benefiting investors and other stakeholders. The table below outlines the firm level determinants of corporate governance and the narratives on what companies should disclose to enhance the informativeness of financial statements.

Table 1: Reporting on corporate governance aspects

Factor	Disclosure Requirements
Board Effectiveness	There is a need to disclose the meetings held per year, board size, board independence, committees, CEO duality and women experiences.
Directors' liability	The companies should disclose how their directors are regulated on self-dealings and any fines they have been ordered to pay by the courts as a result of restitution.
Protection of Minority Shareholders' rights	Companies should disclose the rights of the minority shareholders such as the right to a fair distribution of resources, right of inspection and weighted voting rights.

Factor	Disclosure Requirements
Disclosure and Transparency	Companies should disclose clear and accurate reporting of a company’s policies, structures, and financial status to stakeholders, regulators, and the public. This practice enhances trust and credibility, as it provides a glimpse into how the company operates and its value creation and financial performance.
Shareholders’ rights	Companies should disclose how they are protecting investor investments and the costs they incur to safeguard the rights of the investors.

Source: Author’s Compilation

Discussion of the corporate governance aspects disclosure requirements

This study makes a deduction centred on the findings that effective corporate governance system should report on the aspects tabulated in table 4.1 in its financial statements. The disclosure of the aspects helps stakeholders to have a broader understanding of the significance of corporate governance. The stakeholder gets to appreciate the importance of corporate governance in value creation and its contribution to the overall performance of the organisation, leading to the informativeness of the financial statements. A few frameworks were utilised to identify the most important aspects that companies should report on. Some of the frameworks include the World Economic Forum report (2013; 2015; 2020) and the IoDSA (2016). These frameworks provided the key aspects that companies should include in their corporate annual reports. Furthermore, the study established that the aspects such as board effectiveness, directors’ liability, protection of minority shareholders’ rights, shareholders’ rights and disclosure and transparency enhances the informativeness of the financial statements. The study revealed that the established corporate governance disclosure aspect is relevant to Zimbabwean companies. Thus, Zimbabwean companies are encouraged to adopt them to enhance the informativeness of their financial statements. The following sections discuss the identified aspects in detail.

Disclosure requirements of Board effectiveness

According to Garcia-Torea *et al.* (2016) companies should disclose the following information in relation to the board effectiveness: CEO duality, size and experience of the Board, women experience, board committees, board independence

and meetings held per annum. In Zimbabwe, some companies' financial statements lack the disclosures mentioned by Garcia-Torea *et al.* (2016). It is therefore crucial that these board effectiveness disclosures be reported as they increase investor confidence among other stakeholders. If the board effectiveness disclosure is followed, they will also play a role in the informativeness of financial statements and contribution to the maximisation of shareholders equity.

Directors' liability disclosure requirements

Directors' liabilities can be measured using the costs that the company incurred addressing the breaches of fiduciary and statutory duties (World Bank's Corporate Governance Indicators report, 2015). Thus, the director's liability affects the effectiveness of corporate governance. The research established that directors' liability has a significant role in enhancing the financial statements. Hence, the requirement that it be measured and included in the financial statements. Consequently, this study recommends that companies should disclose all losses or damages linked to the directors' liability because of any breaches. Such disclosures guarantees that the integrity, transparency and accountability principles are upheld in the company thereby enhancing the informativeness of the financial statements.

Disclosure requirements for the protection of minority shareholders' rights

Corporate governance stalwarts advocate that minority shareholders rights must be respected. Companies should report on availability of contractual protection under the shareholders' agreement and the present of a clause which ensures that minority shareholders have weighted voting rights on matters. Moreover, companies should report whether minority shareholders have a right to the sharing of resources and the right of inspection, among others. Thus, these disclosure requirements are in line with the study by Reese & Weisbach (2002).

Protection of shareholders' rights disclosures

It is paramount that companies protect the rights of the shareholders. Thus, this study suggests that the rules and regulations that protect the rights of shareholders should be disclosed in the financial statements. According to Kaufmann *et al.* (2011), the disclosure of shareholders right enhances the investors' confidence. Henceforth, the companies should assess their rules and regulations if they effectively support the rights of shareholders by making an evaluation of the movement in their paper stock market liquidity movement. Weak legal systems and poor corporate governance reduce investor confidence

hence companies should ensure that they build robust systems that protect the shareholders rights. When shareholders are protected from expropriation, the market becomes attractive to investors and they are prepared to pay extra for financial assets (La Porta *et al.*, 1997). Conversely, when companies fail to protect the shareholders the stock market suffer from poor liquidity (Chung *et al.*, 2012). This study recommends that the investors be protected, and their protection be quantified by the total costs suffered to defend the property of investors. This signifies an independent position in decision-making to their stakeholders to entice and retain investors.

Disclosure requirements of the disclosure and transparency determinant

There is a need that companies indicate in their financial statements that disclosure and transparency are important factors in the organisation in line with the corporate governance principles. Companies should report in their financial statements that they practise stakeholder engagement in economic decision-making. The disclosure requirements suggested by this study are based on the studies carried out by the World Bank (2010). The study established that disclosure and transparency can be measured using the compliance indicators such as the stakeholder engagement, audit reports, accessibility of information, third part ratings, sustainability reporting, corporate governance disclosure, and quality and timeliness of financial reporting. These indicators together deliver a broad understanding of how transparent a company runs and communicates with its stakeholders.

The study also revealed that the corporate governance aspects complement each other to facilitate an environment that is conducive for company stability, competitiveness and sustainability. These are the ingredients for enhanced company performance, and it help increase the shareholders' wealth. Measurement and disclosure of human capital have been also identified as effective tool of enhancing corporate governance. Thus, companies should disclose these aspects to promote good corporate governance and boost the confidence of investors and shareholders. The study settles that corporate governance, and functional legal systems can positively contribute to the financial performance of a company.

Conclusion and recommendations

In conclusion, the study settles that the board responsibility and effectiveness, shareholders' rights and minority shareholders' rights protection, disclosure and transparency and directors' liability form the key aspects of corporate governance. This study recommends the abovementioned corporate governance aspects be disclosed in the financial statements of the companies to

enhance the informativeness of financial statements. Ultimately, the study calls for stakeholder (accounting professions and policymakers) engagement to increase the chances of inclusion of the corporate governance aspects in financial statements. In the final analysis, the study established that Zimbabwe has a voluntary code of corporate governance, and some entities feel not indebted follow the code disclosure requirements. This study recommends that the corporate governance aspects be disclosed by companies on their financial statements as a starting point. The benefit of this recommendation is that the companies will recognise company growth through the increased investor confidence, transparency, accountability and legitimacy through stakeholder engagement. Conversely, dares such as political intrusion, economic volatility, and inadequate regulatory enforcement hamper the effectiveness of these governance practices.

Conflict of interest: The author declares no conflict of interest

Informed consent statement: Informed consent was obtained from all subjects involved in the study.

Data availability: The data used to support the research findings are available from the corresponding author upon request.

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