FACULTY OF ECONOMICS
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THESIS

Disclosure of Accounting Information and Stock Return Volatility in Indonesia

Firms listed in Indonesia Stock Exchange Period January 2004 – June 2006

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ABSTRACT

Recent studies have shown the existence of a relationship between the disclosure of accounting information and economic effects. The disclosure of value-relevant accounting information reduces the information asymmetry on the market and, consequently, the risk of investors making mistakes in their decisions, which fosters the attraction of foreign capital. This paper has the purpose of investigating if there is a relationship between level of accounting information disclosure and the volatility of stock returns of Indonesian firms. The hypothesis tested is that firms with higher levels of disclosure present lower volatility of stock returns. The research design involves a sample including 30 firms listed on the Indonesia stock exchange (IDX) from January 2004 until June 2006 (30 months). The samples are selected by using purposive sampling method. Cross-firm linear regression SPSS version 14 is used for analyzing the samples. The results can conclude that higher level of accounting information disclosure posses shares with lower stock return volatility.

Key words: Indonesian stock market, stock returns, disclosure, accounting, volatility, cross-firm linear regression.

CHAPTER I

INTRODUCTION

1.1 Problem Background

Corporate disclosure is critical for the functioning of an efficient capital market. Firms provide disclosure through regulated financial reports, including the financial statements, footnotes, management discussion and analysis, and other regulatory filings. In addition, some firms engage in voluntary communication, such as management forecasts, analysts' presentations and conference calls, press releases, internet sites, and other corporate reports. Finally, there are disclosures about firms by information intermediaries, such as financial analysts, industry experts, and the financial press.

Recent research has demonstrated the existence of a relationship between the disclosure of value-relevant accounting information and economic effects. These effects can be perceived on various levels, such as the accuracy of earnings forecasts made by market analysts (Hope, 2003), the increase of stock liquidity, the reduction of capital costs, and the increase of firm monitoring by market analysts (Healy and Palepu, 2001; Botosan and Plumlee, 2002), the impact on bid-ask spreads of traded securities (Greenstein and Sami, in Medeiros and Quinteiro 2004), as well as the effect on the mobility of international capital (Young and Guenther, 2003).

As a developing country, Indonesia needs investments to foster its economic growth. The stock market is one of the sources of funds available to firms when they need long-term financing. However, well defined regulations with respect to taxation, minority shareholder protection as well as sound corporate governance mechanisms are necessary for stock market development, providing higher transparency and permitting a better control of corporate events. Besides the level of market development, a potential barrier to capital movements, according to Young and Guenther (2003), is the cost for the investor to become well informed. Lower disclosure levels imply higher information costs, which changes the risk return relationship of an investment option. The timely disclosure of high-quality accounting information reduces the risk of investors incurring losses in their transactions, which increases the international capital mobility (Bushman and Smith, 2001).

1.2 Problem Definition

This research tries to examine the following problem:

Is there any relationship between the level of disclosure of accounting information and stock return volatility?

1.3 Research Purpose and Contribution

The purpose of this research is to examine whether there are relationship between accounting information disclosure and return on stock, especially on firms listed in Indonesia Stock Exchange. The result of this research is expected to contribution into: (1) literary of accounting information and disclosure, to help others in having researches with related topics (2) the literature of auditing; internal and external auditor, (3) it can be used as guidance for external auditors in order to make them sure about the firm's condition then it can help them to make their opinion objectively, (4) as guidance to predict the return on stock factors.

CHAPTER V

CONCLUSION

This research investigates the effect of level of accounting information disclosure on stock return volatility in Indonesia (firms listed in Indonesian Stock Exchange). The empirical results obtained demonstrate that the level of disclosure of accounting information has a significant and negative effect upon stock's market risk, measured by stock return volatility (standard deviation) of Indonesian listed firms, which confirms the predetermined hypothesis.

The upshot strongly suggest that higher levels of disclosure of accounting information produce a reduction of the market's perception of the risk associated to stocks, which lowers the risk versus return relationship of marketed securities. The result confirms for Indonesian accounting and stock market environment the beneficial effects of accounting disclosure documented in previous empirical studies. (Young and Guenther, 2002; Bushman and Smith, 2001)

Finally, there are several points that can be generated from this result, (1) firms' decision to increase their disclosure of accounting information level is correct, since it can reduce the stakeholder's risk of investment. (2) Investors and creditors should be more confidence to invest their money into high level of accounting information disclosure firms. (3) Given the firms' resistance to disclose pointed out in the chapter II, this result might contribute to the clarification of the advantages of disclosing accounting information by firms and to decrease the resistance to disclose. The evidence presented in this research suggests that accounting information disclosure may be useful to both investor and firms.

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