CHARACTERISTICS OF CHAIRMAN STATEMENT AND FINANCIAL PERFORMANCE: EVIDENCE FROM AN EMERGING ECONOMY

JYOTI DEVI MAHADEO

DEPARTMENT OF MANAGEMENT

FACULTY OF LAW AND MANAGEMENT

UNIVERSITY OF MAURITIUS

ABSTRACT

This paper analyses the chairman statements of companies listed on the Stock Exchange of Mauritius. It is an accepted fact that those who prepare corporate annual reports have important motivations to manoeuvre the content of these reports, or at least control the impression they convey (Beattie and Jones, 2002). Three characteristics are considered, namely the length of the statements, the number of sections and the presence of pictures or graphs accompanying the statements. No significant relationship was found between the financial performance of those firms and these characteristics.

INTRODUCTION

It is an accepted fact that those who prepare corporate annual reports have important motivations to manoeuvre the content of these reports, or at least control the impression they convey (Beattie and Jones, 2002). Most codes of Corporate Governance have taken into account Cadbury's (1992) recommendation of having a CEO/Chairman split and many studies have revealed that companies of both the developed and emerging nations have adopted this particular requirement. However, even today, the 'Chairman Statement' in the corporate annual report is classified as narrative accounting. Hence, is still considered a voluntary disclosure. There are no formal guiding principles as to what should go into the statement, consequently it is often theorized that top management could be embellishing the qualitative explanation in the chairman statement in an attempt to make a positive impression on shareholders and other readers of the annual report.

Consequently, this study is an endeavour to investigate how companies listed on the Stock Exchange of Mauritius disclose their chairman statement so as to study the effect it has on bottom line reporting. In particular, the study explores whether there is a significant difference between profitable and non- profitable (financial performance) of listed companies with the characteristics of the chairman statement in the corporate annual report.

The study relies on disclosure made in annual reports of the companies under investigation. Independent sample *t*-tests will be carried out to examine whether there is any significant difference, among companies which tend to be more graphical and provide more detailed statement while reporting bottom line performance. It was found that the financial performance of the firm did not have any significant impact on the characteristics of the chairman statement of the listed companies being studied. A thematic analysis of the statements was also performed. The findings of this investigation are expected to add to the present literature on the subject which is already scarce in the non-western context and contribute to policy implementation in emerging nations.

The general aims of the study are to investigate the association of listed companies' financial performance with the features of chairman statement disclosure in the corporate annual report. Particularly, this study intends to answer the following research questions:

a) Whether there is a significant difference between improved revenue and waning revenue of firms with regards to the length/sections of chairman statement and the presence of graphical/picture in the chairman statement?

b) Whether there is a significant difference between profitable and non-profitable firms with regards to the length/sections of the chairman statement and the presence of graphical/picture in the chairman statement?

The paper is structured as follows; the next chapter will review the literature and firm up the objectives to be investigated. The third section describes the methods which will be used in this study. The fourth section presents the findings followed by an analysis of the results. The final section deals with the conclusion and implications of the study.

LITERATURE REVIEW

Agency theory shapes the relations among the various stakeholders to the firm as being laden with conflicting interests (Jensen and Meckling, 1976; Fama and Jensen, 1983). For example, managers can endeavour to cover up a waning firm performance in their annual reports, with the view of benefitting higher compensation (Watts and Zimmerman, 1990). Osma and Guillamon-Soarin (2009) studied the relationship between corporate governance and impression management. Their study hypothesised that sound governance principles will reduce attempt towards impression management. Their results confirmed that firms which were doing well in terms of corporate governance checks impression management.

One of the earliest definitions of impression management dates back to Goffman (1959) who describes impression management as the way in which the manager project impressions of themselves on their audiences. Impression management assists the basic psychological human necessity of self-presentation (Schlenker, 1980). Impression management is an attempt to present a more positive portrait of the company's performance than is merited (Beattie and Jones, 2002). The first part of annual reports consist of messages from the Chairman, CEO and Board members and these are considered as narrative accounting and for this reason, not regulated. The latter sections, which make up the financial statements, are specifically regulated by accounting laws and regulations. It is critical to examine the information in the initial sections of annual reports as they contain important information which potential investors use to make decisions. Very often this information is relied on in preference to data in the financial sections of the report (Barlett and Chandler, 1997; Canniffe, 2003; Henderson, 2004).

The recorded use and importance of the narratives, pictures and graphs enclosed in the front sections of annual reports make them vulnerable to manipulation (Lee, 1994). Impression management is an important thread of financial disclosure and will be studied here. Companies are realising the potential of use of annual reports other than for meeting the statutory requirements. They are excellent vehicles for marketing the company too (Clarke, 1997) and are specially packaged by professional designers to sell their corporate image (Lee, 1994). Corporate annual reports are used in public relations as well (Beattie et al, 2008). The medium for 'impression management' are usually President's letters, Chairman's reports, Management Discussion and Analyses, Operating and Financial Review, Auditors' Reports, Financial Statement Footnotes, Interim Reports, Prospectuses, Press Releases and Environmental Disclosures (Merkl - Davies and Brennan, 2007).

Staton et al (2004) undertook an experimentation to establish the impact of impression management with sophisticated and unsophisticated users of accounts. They did not find any significant difference. On the other hand, Godfrey et *al* (2003) looked into the association of earnings and impression management in financial report surrounding chief executives officers (CEO) changes. The study evinced that the year of CEO change showed downward earnings management and unfavourable impression management of key financial variables graphs. In addition, the study notes that there is an upward earning management and positive impression management in a year post CEO change. Skinner (1994) examines voluntarily reporting by 93 NASDAQ firms during 1981 – 1990. The most important outcomes of this study indicate two findings: corporate management readily engage in earnings management when their company are performing well with the view of impressing the market; and they also do so corporate management to shun more unfavourable impact from the actual declaration of quarterly performance.

Narratives

Jones (1996) and Courtis (2002) pointed out the importance of narratives in the contemporary annual reports and their role as complement to the financial statements. Henderson (2004) claimed that narratives in corporate annual reports are more important than the financial figures and, that potential investors were more likely to read this section of the report. The authors have witnessed an increase in reliance by ordinary investors on narratives, hence there is even more pressure to ensure transparency for the sake of unsophisticated users (Rutherford, 2003, Beattie and Jones, 2002).

The Chairman Statement is a conventional narrative found in most annual reports. According to Barlett and Chandler (1997) it is attracting an even wider readership as it is an important part of the corporate annual report. This was confirmed by other authors such as Courtis (1986), Jones (1988) and Subramanian et al (1993). Substantial amount of research has been undertaken in the past to examine the Chairman Statement or its counterpart (Clatworthy and Jones, 2001, Courtis, 1998, Courtis, 1986, Subramanian et al., 1993). Clatworthy and Jones (2006) looked into the objects of poorly performing companies who engaged in impression management. They found that companies doing poorly tend to concentrate on the future rather than reporting on the past.

Manipulation of narratives has taken several forms, for example, increase in reading complexity and decrease in intelligibility of text (Rutherford, 2003). Another often used manipulation occurs during the fine-tuning of directness of narratives. The concept of directness relates to positioning of information or topics of importance within a narrative statement. The study of Jameson (2000) looks into a variety of possibilities to report on structure, which could be considered as direct or indirect. Directness is about revealing the overall main point at the start of the statement while indirectness is the subtle placing of details and sub-points initially, then developing to the main point close and towards the end (Jameson, 2000). She remarked that companies with mixed returns were less direct than those with positive returns. She also contends that if readers are provided with the same set of information, alteration of the structure of a narrative through directness and the beginning of various themes will allow diverse stories to be told the annual report readers. The strategic positioning of information with the Chairman's statement will not be identified by the readers as a means to draw their attention from the poor performance of the company. The writer hence is concealing the message of poor performance in a very subtle manner. On the other hand, Wills (2008) undertook a laboratory experiment and found that impression management did not influence company performance.

The study of Clatworthy and Jones (2006) was an investigation of the effect of financial performance on the textual characteristics of the chairman statement among 100 very profitable and unprofitable UK listed companies. Their results point to the fact that the chairman statement is in fact subjected to impression management methods as the firms' manager tendency to relate themselves to company financial results is connected to the underlying financial performance. The evidence from their investigation also indicates that unprofitable or less profitable companies concentrate more on the future than on past performance.

Graphs and Pictures

The utilization and extent of graph distortion differ by country (Penrose, 2008). No conclusive evidence could be drawn from the investigations other than recurrent graphical distortion. Moreover, it is worthy to note that emerging nations and continents such as South America, African continent, the Middle-East and India were overlooked in those studied (Penrose, 2008).

The utilization of graphs has been reported as an important means of communicating accounting information in the accounting sphere (Holmes, 1984). The literature acknowledges that graphs are used in two essentially different ways, namely to study data and to present information to an audience. The classic study of Paivio (1974) stipulates that human capacity to bring to mind visual patterns is more enhanced to memory for text or numerical tabulations, graphs are also most apt to be retained. They are also recognized to be predominantly useful emphasize tendency (Wright, 1995).

Impression management also makes use of graphs and pictures; and can take place in three possible fashion: 1) through management decision to use (or not to use) graphs on an annual basis; 2) graphical manipulation technique can be applied to pass on the message and 3) the use of graph features to enhance the message of management in an unmerited way (Beattie and Jones, 1992). Recently, the utilization of graphs has become widespread (Beattie et al, 2008). Graphs are powerful means of communication (Beattie and Jones, 2002) which have been termed double edged sword by the authors. Graphs improve communication but can also be manipulated and they attract the user's interest easily and necessitate spatial intelligence (Beattie and Jones, 2002). It is very easily retrievable in this format for the accounts' user (Leivian, 1980). Past research performed by Beattie and Jones (1999) has identified four major kinds of graph manoeuvring in corporate annual reports: these are selectivity, presentational enhancement, orientation distortion and measurement distortion.

In their study, Johnson et al (1980) studied 50 annual reports from the US Fortune 500 companies. Taken together, these firms comprised 423 graphs over the time period 1977 – 1978. Their main observation was that in 42% of the annual reports at least one graph was not put together while 29.5% was not accurately composed. Parameters were set by Taylor and Anderson (1986) for the accountant to put together graphs for their annual reports. They proposed that it was important for graphs to be coherent with the financial data so that users are not misleading in any way. Moreover, it is also to ascertain that auditing standards are not violated, for example, the percentage change in the basic financial data should be reflected by a corresponding change in the graphs. If the latter condition is not met, distortion occurs.

In their investigation, Beattie and Jones (1992) found that: graphs and pictures were very extensively used by 'well performing' companies. Measurement distortion was important; and the consequence of measurement distortion depicts the company's performance positively. Influence the impression management through key financial variables graphs in CEO change situation among Australian companies. The study concludes that the boards with a higher proportion of independent directors able to constrain impression management among companies with a new CEO in selecting and reporting several important financial graph.

Arunachalam (2002) confirmed that decision making options could be influenced by manipulated graphs when mixed with numerical information. However, there appears to be very little amount of conclusive evidence to date which could provide a clear indication in general whether impression management is effective or not (Stanton et *al*, 2004). Their study also did not provide any evidence whether individual or combined forms of impression management will have an influence on decision makers. Misunderstanding of information in graphs can possibly be related to two reasons, either lack of comprehension of graphical principles by designers of graphs or a calculated attempt by designers or management to handle the perceived image of a company's financial performance. Beattie and Jones (1999) contend that their findings are in harmony with the view that financial graphs are utilized to bring legitimacy to a company. They summed up that graphs are a vital visual device that can be employed to influence users' perceptions. Graphs are subject to impression management to improve perceptions of managerial performance. Graphic designers of annual reports can have power over the perception of the data in a graph through the cautious selection of graph type, scale, emphasis, size (Penrose, 2008).

As discussed previously, many types of impression management have been identified as occurring in corporate annual reports including manipulation of directness of narratives (Jameson, 2000) and graph measurement distortion (Courtis, 2004). Prior research has mostly concentrated on the occurrence of impression management rather than on its effects on decision makers. This study looks into the length, number of sections of the Chairman's statement and the presence of graphs and pictures within the chairman statements; and their ultimate influence if any on the financial performance of companies.

METHOD

The study involves all the 39 companies listed on the Stock Exchange of Mauritius as at 31st December 2009. Annual reports were collected manually or downloaded from the company website when accessible. Corporate annual reports were scrutinised for the variables to be studied. Annual reports are deemed adequate and significant means of communication to report on financial and non financial performance of companies (Hooks et *al*, 2002). It is the most critical means for companies to disseminate information to shareholders and other readers of annual reports.

An in-depth analysis was then performed on each company's chairman statement and the chosen features of the chairman statement were monitored. The financial statements of each company were also appraised based on their net income and revenue. Two performance indicators were established and used: 1) revenue in 2009 and 2008, two groups were set with one as a listed company with recorded increase in revenue and one with a decrease in revenue. 2) The other indicator was the net income for the year 2009, two groups were again determined, with one group showing a net loss and an additional one for net profit. The financial indicators were the independent variables for the study on hand.

The features of the chairman statement comprised of 1) number of pages, 2) number of sections making up the statement, and 3) picture of the chairman and graphs were used as dependent variables for the study. Also the position (independence) of chairperson was also captured. The table below provides a summary of the independent and dependent variables taken on for this study.

Table A: Explanation of Variables

Dependent Variables

Number of pages

Number of pages for the chairman statement in the annual report of the listed company

Number of sections

Number of sections for the chairman statement in the annual report of listed company. Usually, the section includes the overview, financial performance, dividend, prospect and gratitude.

Pictures and graphics

Very often the chairman statement comes with an attachment of his/her picture and graphic on company activities. If the company has both picture and graphic, it was allocated with value '1' and if it has only one of them or does not have both of the elements, it was allocated with value '0'

Independent Variables

Increase/decreased of revenue (0809)

Comparing the revenue earned by listed company in 2008 and 2009. It then classified into two groups: (i) increased revenue and be assigned with the value '1'; and (ii) decreased revenue shall be assigned with value'2'.

Net Income for the year (ProfitLoss09)

The profitability level of construction company is 2009. Two groups were obtained: (i) net profit shall be assigned with value '1'; and (ii) net loss shall be assigned with value '2'.

The examination of the association between the above dependent and independent variables was determined by employing independent sample *t-test.* This investigation is aimed to determine whether there is a significant mean difference between the two groups of independent variables towards the dependent variables. For this study, the analysis was performed twice: 1) on the increase or decrease in revenue and 2) net profit or net loss. These tests are supposed to present an appreciation as to whether the two financial performance indicators used for this study results in different features of the chairman statement. Descriptive and frequency analysis have been performed in addition to the independent sample *t-tests.* The statistical analysis were done using SPSS version 11.5. With the view of deepening the investigation a thematic analysis of the chairman statement characteristics was performed too.

FINDINGS

On the whole, the analysis demonstrated that chairman of the board usually disclosed his/her statement together with a picture, graphs and other graphical representations of the company. A descriptive analysis was performed and it was found that the maximum number of pages in the chairman statement was 10 and the minimum was 0. This indicates that some annual reports did not have a Chairman Statement at all. It is interesting to note that in some annual reports, the report was made on behalf of the Board or a joint CEO/Chairman statement which was signed off by both the Chairman and CEO.

It was also determined that the mean for the number of pages in the Chairman Statement was 2.28 while the mean for the sections was 6.44. The two financial performance indicators showed that on average, both revenue and net income have increased. The table below condenses the descriptive analysis findings:

TABLE A1: Statistics

Variables	Pages in Chairman Statement	Sections in Chairman Statement	Pictures in Statement	Revenue for the year 0809	Profit or Loss for the year 09
N =39					
Mean	2.28	6.44	.74	1.36	1.21
Median	2.00	7.00	1.00	1.00	1.00
Mode	2	8	1	1	1
Minimum	0	0	0	1	1
Maximum	10	14	1	2	2

A frequency analysis was undertaken and it was revealed that in terms of page, 16 companies (41.0%) have released 2 pages in their chairman statements. Next, were 12 companies (30.8%) which made available single page chairman statement. Only one company (2.6%) had a chairman statement of 10 pages and one company (2.6%) did not have a statement at all, hence any section. 8 companies (20.7%) have 8 subsections in the annual reports, followed by 7 companies (17.9%) which have 3 subsections in their statements. Moreover, there are 5 (12.8%) and 6 (15.4%) companies with 6 and 7 subsections respectively.

A qualitative analysis was also undertaken, and upon scrutiny it was determined that the sections of the chairman statements typically included the following concepts: namely, an overview of the firm's activities, the financial performance, a section on Corporate Governance and Corporate Social Responsibility, the future prospects for the company, appreciation and acknowledgement part to management, employees and shareholders.

Table B: Results of Frequency Analysis

Pages in chairman statements	Frequency	Percentage
0	1	2.6
1	12	30.8
2	16	41.0
3	5	12.8
4	2	5.1
6	2	5.1
10	1	2.6

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Table B1: Results of Frequency Analysis

Sections of chairman statements	Frequency	Percentage
0	1	2.6
1	1	2.6
3	7	17.9
4	1	2.6
5	3	7.7
6	5	12.8
7	6	15.4
8	8	20.5
9	4	10.3
11	1	2.6
13	1	2.6
14	1	2.6

Table B2: Results of Frequency Analysis

Revenue 0908		
Increased	25	64.1%
Decreased	14	35.9%
ProfitLoss 09		
Profitable	31	79.5%
Not Profitable	8	20.5%

The reality is that the chairman statement is not an obligatory financial requirement, hence, it has been noted that companies describe it by various names and companies have included varying information. A clear lack of consistency has been noted throughout. For example financial performance has been termed financial highlight, group results, and financial review. Prospects has been branded company outlook, moving ahead, challenges ahead, year or years ahead. Overview was categorised in two: internal and external. For the external overview, the term used was industry trend and an account of activities in the different sectors was performed. Economic outlook or the Mauritian Economy and Development were also seen to be reported in a few annual reports by means of Main Economic Indicators. In most statements, the global financial crisis which has hit the world in 2008 has been mentioned, to explain the state of things within the companies. On the other hand, for internal view the designation used has been operating background, corporate development, portfolio review. Then again, for the corporate governance section, some transactions such as directorship, board mechanism and other board activities. The only section where there was consistency was under the CSR banner. This could be due to the fact that contribution towards CSR (for listed companies) is a compulsory activity in Mauritius.

A closer analysis indicated that 10 companies (25.6%) did not have any pictures or graphs attached to the chairman statement while 29 companies (74.4%) had a picture of the chairperson or graphs depicting the activities of the company. Moreover, it was found that only one company did not have a split between the CEO/Chairman as required by the Code. It was also found that no explanation was provided in the company's annual report as to why the chairman and CEO was the same person. On the other hand, 38 companies (97.4%) have thus complied with this requirement of the code.

TABLE C: FREQUENCY ANALYSIS

Graphics/pictures	**Frequency**	**Percentage**
No pictures	10	25.6
Pictures	29	74.4
No split CEO/Chairman	1	2.6
Split CEO/Chairman	38	97.4
Status of Chairman		
ED	1	2.6
NED	29	74.4

INED	9	23

Table C presents the details of the frequency analysis. A contrast in revenue reveals that 25 companies (64.1%) showed an increase in revenue while 14 companies (35.9%) indicated a drop in revenue. Finally, 31 (79.5%) companies experienced a profit in the year ending 2009 and 8 (20.5%) companies faced a loss in 2009.

Two independent sample *t*- tests were ultimately performed to determine if there was any significant mean difference between financially performing and non performing listed companies in connection with the chairman statement characteristics. The first section of the analysis investigates the impact of increase/decrease in revenue in 2009 weighed up to 2008 with regards to the following characteristics: number of pages, sections and graphs/pictures.

The independent sample *t*-tests revealed that there was no significant difference between these two categories of listed companies in connection with features measured. The results are consistent with the findings of Staton et *al* (2004) and Wills (2008), however, they are in contradiction with the findings of Godfrey et al (2000) who found that company which were performing well were also disclosing more in terms of statement length and graphic presentation. Particulars of the independent sample *t*-test are found in tables D and E.

The subsequent step was to investigate for any significant mean difference between profitable and non profitable listed companies in 2009. Here again, no significant difference was found between the two types of companies towards the features of chairman statements' characteristics being studied. The study of Clatworthy and Jones (2006) also showed no significant mean difference in the companies with the two level of profit towards number of pages and sections in the chairman statements

Table D: Independent Sample *t*-test (Revenue)

	Revenue 0809	N	Mean	Std Deviation	*t-value*	Sig (two-tailed)
No. of pages	Increased	25	2.40	1.414	0.544	0.899
	Decreased	14	2.07	2.369		
Sections	Increased	25	6.88	2.698	0.487	0.217
	Decreased	14	5.64	3.365		
Graphics/Pictures	Increased	25	0.76	0.436	0.555	0.761
	Decreased	14	0.71	0.469		

Table E: Independent Sample *t*-test (Profitability)

	ProfitLoss09	N	Mean	Std deviation	*t-value*	Sig (two – tailed)
No. of pages	Profitable	31	2.10	1.375	-1.282	0.208
	Not profitable	8	3.00	2.928		
Sections	Profitable	31	6.16	2.818	-1.140	0.261
	Not profitable	8	7.50	3.505		
Graphs/Pictures	Profitable	31	0.77	0.425	0.847	0.402
	Not profitable	8	0.63	0.518		

CONCLUSIONS AND IMPLICATIONS

The investigation examines 39 companies listed on the Mauritian Stock Exchange and concludes that there is no statistical significant evidence that companies doing well financially and those not doing well are influenced by characteristics of chairman statements. The results shed doubt over the result of impression management. The findings coincide with those of Mather et *al* (1998) who did not show any relationship between performance and the presence of graphs/pictures. Wills (2008) performed a laboratory experiment and found that impression management did not affect company performance. Clatworthy and Jones (2006) observed that news reported in the Chairman statement is in a way consistent with impression management. It is also important to take note that the utilisation of impression management may be merely customary and unconscious (Leary and Kowalski, 1990).

This research has made an attempt to contribute to existing knowledge in the area of impression management by determining the impact of three features of the chairman statement on the financial performance of firms. Other studies or experiments have focussed on the 'how' or 'why' of impression management. This investigation does not provide any conclusive evidence but the main findings coincide with those of Wills (2008) and Stanton et al (2004). As in the case of most research, this investigation has its inherent limitations. Only three characteristics were measured, that is the length of the statement, the number of sections within the statement and accompanying graphs and pictures. Further studies could examine the effect of other features on financial performance to determine any impact.

Though no significant relationship was found, it is not possible to ascertain the impact of impression management. Still, the findings of the present study conclude that it would be important to regulate the narrative sections of the annual report. This is in line with recommendations made by Beattie et *al* (2008). The responsibilities and duties of auditors and directors should be made clearer in this area (Beattie and Jones, 1992). Research to direct corporate auditors in their assessment of narrative part of annual reports is practically non-existent. Since graphs are expected to be used as a tool to report factual financial data, one would assume that principles and standards to guide their use will rapidly come out in addition to those made earlier by Taylor and Anderson (1986). Conversely, the literature (Penrose, 2008) illustrates that this has not been the case until now. There, are plenty of opportunities which are present for research in current practices for the forthcoming future.

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