Accounting and Business Research
Publication details, including instructions for authors and subscription information:
http://www.tandfonline.com/loi/rabr20

Discussion of 'How can business reporting be improved? A research perspective'

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Published online: 28 Feb 2012.

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In responding to the thoughts of the experts I need to explain my viewpoint, which is that of an interested observer who has an important stake in the outcome of the debate. As vice-chairman of Barclays Global Investors I approach the issues as a large scale institutional investor which, because of its quantitative investment approach, has a critical interest in the origin and meaning of the reported numbers. In a wider context, in various capacities at the Financial Reporting Council, the Investment Management Association and the Association of British Insurers, I take the broader investing industry point of view. And finally, I am the only non-expert to be invited to speak at this conference, so please interpret my thoughts in that context.

One major point to make at outset is that it is generally very difficult to get institutional investment practitioners to take an interest. They all know that financial reporting is really important, but are reluctant to get engaged as they find themselves down in the weeds a lot quicker than they want to be, and spending much more time than they would like, on very dry debate. Against that background, I would comment that the 'invisible hand' works extraordinarily well. The market does work better than any individual. There is no obvious free lunch available from any manifest deficiencies in financial reporting.

Having made this point, I want to cover three main topics, as follows:

1. OFR and the business review.
2. IFRS.
3. Sustainability.

1. The Operating and Financial Review

Why is this so important? It plays into the discussion about disclosure at this conference.

I agree with comments that we are a very long way from modelling the economic effects of corporate disclosures on the cost of capital. Just look at the IFRS disclosures that we have had in the UK this year. Much new information is going out into the market place, but for the vast majority of companies, what happened to their share prices? Absolutely nothing. Disclosure will obviously affect the cost of capital; it is just not clear that the information is feeding through very quickly.

I would also agree with the view that it is a question not of 'if you disclose', but 'when you disclose'. The worst corporate frauds have been disclosed when the company concerned runs out of cash – like, for example, Barings. So it is a question of when you tell the market, rather than if – critical information will feed through over time.

As the paper suggests, corporate disclosure is a continuous process, and as an investor I understand it that way. As an investor, I realise that I am being 'managed' by company directors. Surprisingly, I like it! I do not like the feeling that I am being manipulated, but I do like to have my expectations properly managed.

That is where the idea of disclosure being a continuous process comes in. The Operating and Financial Review sets out a road map. It establishes a strategy for the company, sets out the targets that the management have chosen to pursue, and subsequently reports progress against those self-selected targets. That plays into the paper's ideas about marginal cost and marginal benefit, and addresses the Government agenda to which it referred. The ideas of what you actually disclose, who makes the decisions around disclosure and so on, are extremely important. They are governance issues.

2. IFRS

I stated at the outset that the 'invisible hand' worked well, but I think that practitioners are really struggling with the development of IFRS at the moment. It feels as if we have come into the cinema when the movie has been running for a couple of hours, with only an hour to go. Is it possible to understand or even re-write the plot at this point? I struggle with 'fair valuing' everything. It seems that we are actually trying to value a company, and to end up with the financial statements which sum to its market capitalisation. But we are already

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valuing the company through the market and not through the financial statements. There is a fallacy here.

So practitioners need to engage with the IASB and have some sensible discussions, but it is hard to know how to do that without getting sucked into the mire. I am greatly in favour of the investor view the paper suggested about how we are trying to view earnings. How we feed that through into the way that standards develop is not at all clear.

Just as an aside, I find it slightly ironic that a number of the academics addressing the conference are based in the US and are heavy influences on IASB. But IFRS is being implemented in the rest of the world and not in the US. The whole convergence project needs to be reviewed.

3. Sustainability

I would agree with a number of the papers on this. Although people are talking about it, I do not think this risk is being seriously addressed by corporates and investors. The big issue is that we deal in price; sustainability is mis-priced; and I do not see it being adequately tackled in our system.

My conclusion is that this is vital work. This has been an important conference. We need to take things in the right direction, but I have concerns as to whether we have the institutions to enable us to do so.