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RISK MANAGEMENT DISCLOSURE BY FINANCIAL LISTED COMPANIES IN VIETNAM

Nguyen Huu Cuong

Danang University of Economics - The University of Danang

Email: cuonghien@due.edu.vn

Vo Hoang Tung

Asia Dragon Audit and Appraisal Firm

Email: vohoangtung1992@gmail.com

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To the best of our knowledge, there have been no studies to assess the level of risk management disclosure (RMD) by listed companies in the financial sector in Vietnam. This research evaluates the level of mandatory and discretionary disclosure of risk management in financial statements of Vietnamese financial listed firms. Using the content analysis method, this study has revealed that the level of information disclosure on risk management by those firms is relatively low. The regression analyses demonstrate that RMD level is affected by firm size, solvency, leverage and independent directors.

Key words: *disclosure, risk management, risk management disclosure, factor analysis.*

1. Introduction

Globalization has posed a challenge to the field of risk management in the financial sector. Enterprises in general and financial firms in particular always want to expand their business, so the risk also increases proportionally with the expansion. In addition, financial institutions are facing increased risk because they are funding higher-risk projects. In this context, investors, shareholders and other stakeholders have the right and desire to know all the information about risk and risk management of the business to make the relevant decisions. Meanwhile, research on RMD by enterprises in Vietnam is scarce. Therefore, the assessment of the

level of RMD and its associated factors will be meaningful not only to financial reporting preparers, information users, but also for state management agencies. To fill the gap of RMD, this study has focused on assessing the level of RMD on financial statements of financial listed firms in Vietnam for three years (from 2014 to 2016) and the factors affecting the disclosure level. Deriving from the findings, this study proposes some policy and management implications with the expectation that the stock market will have financial reports with high levels of disclosure compliance, which are more meaningful to users and contributing to promoting transparency in financial market.

2. Theoretical framework and research method

2.1. Theoretical framework

Although there are almost non-existing in-depth studies examining RMD by enterprises, the kind of information disclosure is part of the financial reporting disclosure. Prior research recognises that financial reporting disclosure is influenced by many factors and is explained by different theories.

Agency theory was developed by Jensen and Meckling in 1976 when investigating the relationship between the principals (owners) and the agents (manager) of the firm (see Jensen & Meckling, 1976). Both sides in this relationship want to maximize their interests; So, they tend to seek personal gain. Larger firms will often face more risk, so they may disclose more information on risk management in order to give shareholders confidence in their ability to cope with risk, then reducing agency cost. In addition, high risk firms lead to high information asymmetry between managers and investors (Deumes & Knechel, 2008), and risk reporting can reduce the agency cost. as well as the information asymmetry between managers and shareholders (Watts & Zimmerman, 1983).

Signalling theory, developed by Spence (see Spence, 1973), suggests that information asymmetry between insiders and investors will cause adverse selection for investors. This theory provides an explanation for the behaviour of managers as they demonstrate their ability to identify, measure, and manage risk through the release of more risk information, to differentiate themselves from other managers (Elshandidy, Fraser, & Hussainey, 2013).

Political theory, proposed by Watts and Zimmerman (see Watts & Zimmerman, 1978), argues that state management agencies make decisions that are relevant to the firms' interests based on their information disclosure. Large firms often have the incentive

to improve investor confidence by providing higher quality disclosure of risk management to reduce political sensitivity (Hassan, 2009).

Proprietary cost theory, developed by Watner and later developed by Verrecchia, has been used as a theoretical framework for much of the later disclosure literature (see Watner, 1982; Verrecchia, 1983). This theory suggests that the cost will arise when there is a decline in cash flow in the future due to the firm's disclosure. Proprietary cost theory is the basis for explaining that RMD by firms may not be useful to users because managers find that the disclosing more information will not bring more benefits than the potential costs of disclosure (Amran et al., 2009). In addition, according to Healy and Palepu (2001), highly profitable firms may not want to disclose their proprietary information to competitors, since such information can undermine those firms' competitive position.

Information economics theory is based on three classic studies, including Akerlof (1970), Spence (1973), and Rothschild and Stiglitz (1976). This theory implies that when engaging in business transactions or potential transactions there may be one party with an informational advantage over the others. Managers do not make the same decision with the disclosure extent because there are differences when considering trade-offs between costs and benefits. Firms will only provide additional information if they find that the benefits of disclosure exceed the costs associated with the disclosure. Nguyen Huu Cuong (2017) compared the commonality of the framework theories commonly used in information disclosure research and identified that information economy theory is most appropriate to explain the variations in the level of information disclosure in the firms' financial reporting.

2.2. Research Method

2.2.1. Hypothesis Development

Hypothesis one (H1) - Firm Size

Kolmatsui, Legenzova, and Seilius (2016) applied-mixed methods to assess the difference between risk and RMD at Nasdaq OMX Baltic and Euronext Brussels and identified its associate factors. They found that firm size has influence on RMD. Similarly, Linsley and Shrives (2006) have also applied a content analysis approach to examine risk disclosure in the annual report of the UK non-financial firms in 2000 and also documented the influence of firm size on risk disclosure.

Consistent with agency theory and signal theory, as well as empirical findings from previous studies, it is hypothesised that:

H1-Firm size has positive influence on RMD.

Hypothesis two (H2) - Firm Leverage

High-debt firms often have higher levels of risk because when the firms have a growing number of creditors, managers will provide more information on risk management as a way to show creditors the ability to cope with risk, thereby turning risk into managers' opportunities. This is consistent with agency theory, signal theory and some empirical evidence from prior studies. For example, Khelif and Hussainey (2016) investigated the relationship between risk disclosure and company characteristics, by using meta - analysis, and concluded that financial leverage was related to risk reporting.

On the other hand, the high debt ratio means the risk that enterprises are facing is also high. These risks can affect the ability of companies to attract investment, but benefit competitors so that managers have temptation to withhold information about the risks; therefore, reducing the level of risk management disclosure (see, for example, Jia, Munro & Buckby, 2016).

Consistent with agency theory and signal theory, as well as empirical findings from previous studies, it is hypothesised that:

H2 - Firm leverage has influence on RMD.

Hypothesis three (H3) - Firm Profitability

Managers of well - performing firms tend to disclose more information on risk management in order to show shareholders the ability to manage and cope with risks that affect their profitability. Investors can also appreciate the firms' risk management capacities when they perceive that the high profitability of firms is due to the ability to manage business risks. Regarding empirical evidence, Samanta and Dugal (2016) evaluated the nature and characteristics of risk reporting as required by banks in India by examining the 2012-2013 annual reports of 38 banks and showed that net profit is correlated with the level of information disclosure.

Consistent with agency theory and signal theory, as well as empirical findings from previous studies, it is hypothesised that:

H3 - Firm profitability has positive influence on RMD.

Hypothesis four (H4) - Firm Liquidity

Disclosing more information on risk management when the firm's solvency is low will solve the information asymmetry problems between managers (the agents) and shareholders (the principals). Shareholders will know the management policies to deal with the risks from which to increase trust, reduce the agency cost. Investors will be more secure when investing in enterprises when they understand the firm's management policies in general and risk management in particular. Prior research has found that liquidity has a negative effect on the level of risk disclosure (see, for example, Elzahar & Hussainey, 2012). This negative influence is also can explain by the information economics theory, providing that the firm pursues to provide more information to enjoy more benefit.

Consistent with agency theory and information economics theory, as well as empirical findings from previous studies, it is hypothesised that:

H4 - Firm liquidity has negative influence on RMD.

Hypothesis five (H5) - Auditor

In order to maintain a reputation and avoid the cost of reputation losses, large auditing firms have the advantage of being able to require higher levels of disclosure. Therefore, the firms are audited by independent auditing companies with high prestige tend to provide more information. Kolmatsui, Legenzova, and Seilius (2016) also found that the presence of auditing firms was an important factor influencing the disclosure of risk and vulnerability of companies. This impact is also confirmed in Achmad et al. (2017)'s research on the voluntary disclosure (including risk disclosure) by Indonesian firms.

Consistent with agency theory and empirical findings from previous studies, it is hypothesised that:

H5 - Firms audited by Big - 4 auditor has higher level of RMD.

Hypothesis six (H6) - Independence of Board of Directors

The higher the number of independent board members, the more likely they are to release more information about risk management as the result of the independent members' supervision. The board independence may have an impact on disclosure level in the same direction as the independent shareholders' effect. Agency theory implies that the ownership structure influences the level of supervision, and that affects the level of disclosure. This may explain why the degree of shareholder independence can affect the level of risk disclosure. Previous studies have shown that shareholder independence has a negative impact on the level of RMD (Jia, Munro & Buckby, 2016). Independence

of board members is measured by the proportion of non-executive directors, and the chairman duality (i.e. whether or not the chairman is also the chief executive officer).

Consistent with agency theory and empirical findings from previous studies, it is hypothesised that:

H6a - Firms with a higher percentage of independent directors has higher level of RMD.

H6b - Firms without the duality of chairman has higher level of RMD.

2.2.2. Research Design

Research Model

This study was conducted to evaluate the risk management practices by measuring the level of RMD, and identify the associated factors. The level of disclosure is measured by the content analysis method based on the checklist of risk management disclosure items; The influencing factors are identified by analysing two regression models with the alternatives of the two related independent variables: mandatory risk management disclosure (MRMD) (refer to Equation 1) and discretionary risk management disclosure (DRMD) (refer to Equation 2).

Equation 1:

$$\text{MRMD}_{it} = \beta_0 + \beta_1 \text{SIZE}_{it} + \beta_2 \text{LEVERAGE}_{it} + \beta_3 \text{PROFITABILITY}_{it} + \beta_4 \text{SOLVENCY}_{it} + \beta_5 \text{AUDITOR}_{it} + \beta_6 \text{INDEPENDENCE}_{it} + \beta_7 \text{DUALITY}_{it} + \varepsilon_{it}$$

Equation 2:

$$\text{DRMD}_{it} = \beta_0 + \beta_1 \text{SIZE}_{it} + \beta_2 \text{LEVERAGE}_{it} + \beta_3 \text{PROFITABILITY}_{it} + \beta_4 \text{SOLVENCY}_{it} + \beta_5 \text{AUDITOR}_{it} + \beta_6 \text{INDEPENDENCE}_{it} + \beta_7 \text{DUALITY}_{it} + \varepsilon_{it}$$

The influence of factors on the RDM level was verified through three regression models including ordinary least square (OLS), fixed effects model (FEM), and random effects model (REM). Based on the

regression analyses the three models, this study performed the Hausman test to confirm which model was more appropriate to explain the variations in RMD by financial listed firms in Vietnam. Finally, this study also carried out a statistically significant exclusion from the most appropriate model and performed a re-estimation of the model to determine the optimal regression equation for the effect of factors to the level of RMD.

Measurement of Risk Disclosure Management (MRMDit and DRMDit)

The risk management of listed firms in Vietnam has not been specifically defined. Circular 155/2015/TT-BTC requires public companies to provide information on risks in annual reports but the information provided is very general and very limited. Meanwhile, financial institutions must disclose the financial risk management policies of *credit, liquidity, interest rates, exchange rates, securities, and commodity prices* (State Bank of Vietnam, 2007, 2014). This mandatory requirement on RMD is the basis for establishing the checklist to measure the level of mandatory RMD (MRMDit). Specifically, disclosure of each of the six risk management policies was measured on three aspects: *risk identification, risk management, and data presentation*. Thus, the total number of indexes for evaluating the level of mandatory RMD is 18.

The level of discretionary RMD (DRMDit) is determined based on the different levels of detail for both *risk identification and data presentation* of related disclosure of risk management policies. In particular, discretionary RMD about risk identification is determined on the basis of differences in *identifying the way in which the risk arises and assessing the impact of the risk*; The data related to each of the risk management policies is determined on the basis of differences in data disclosure, data comparison, and data

sensitivity analysis. Thus, the total number of indexes to evaluate the discretionary RMD is 30.

Based on information disclosed on financial statements provided by each firm, the level of RMD disclosure is determined as follow.

$$MRMD \text{ (or DRMD)}_i = \sum_{j=1}^{n_i} \frac{d_{ji}}{n_i}$$

Where

MRMD_i and DRMD_i are indices of mandatory and discretionary RMD of firm i ($0 \leq MRMD_i$ and $DRMD_i \leq 1$), and are the dependent variables in *Equation 1* and *Equation 2*.

n_i is the maximum number of disclosure items that are subject to be disclosed after excluding the number of not applicable items, i.e. items are explicitly not relevant to firm i.

d_{ji} is assigned a value of "1" if the item j is published on the annual financial report of DN i and "0" if not published

Measurement of independent variables:

+ SIZE_{it}: is the size of firm i at the end of the financial year t, which is measured as the base 10 logarithm of total assets at the end of the year;

+ LEVERAGE_{it}: is the debt ratio of firm i at the end of the financial year t, which is measured as the base 10 logarithm of liabilities to equity at the end of the year;

+ PROFITABILITY_{it}: is the profitability of firm i at the end of the financial year t, which is measured as the ratio of profit after tax to equity at the end of the year;

+ SOLVENCY_{it}: is the solvency of firm i at the end of the financial year t, which is measured as the base 10 logarithm of the ratio of current assets to current debt at the end of the year;

+ AUDITOR_{it}: is the auditor audits the financial statements of firm i for financial year t, which is

assigned the value of "1" if it is a Big 4 auditor, and "0" otherwise;

+ INDEPENDENCE_{it}: is the percentage of non-executive members of the board of directors of firm *i* as at the date of the financial statements for the year *t*, which is measured as the ratio of total non-executive members to the total number of members at the end of the year.

+ DUALITY_{it}: is the duality of the chairman of the Board and CEO of firm *i* as at the date of the financial statements for the year *t*, which is assigned the value of "1" if the chairman is separated from CEO, and "0" otherwise.

Data and sample: The data in the study is the time series data collected from the annual financial report of 38 listed firms in the financial sector in Vietnam for the three years from 2014 to 2016 (corresponding to 114 observations).

3. Research Findings and Discussion

3.1. Research findings

Risk management disclosure by financial listed firms in Vietnam

Table 1 shows that the level of MRDM on average risk of 38 CTNYs in the research sample is 72.86%, indicating that there are still many mandatory disclosure items on risk management. published (27, 14%). It is notable that the discretionary information on average risk management of these enterprises is lower, reaching only 46.21% - that is, the average is still 53.79% of the arbitration disclosure arbitration has not been announced.

Table 1: Risk management disclosure by Vietnamese financial listed firms (from 2014 to 2016)

	N	Min	Max	Mean	Std. Deviation
Mandatory risk management disclosure (MRMD)	114	0,00	1,00	0,7286	0,2461
Discretionary risk management disclosure (DRMD)	114	0,00	0,80	0,4621	0,1654

Source: Summary from the authors' calculation on RMD using the self-constructed checklist.

Factors affecting the level of RMD

On the basis of the Hausman test, the REM model was considered most suitable for the study (both equations, with $p < 0.05$). Based on the estimation results using the three regression models (OLS, FEM, and REM) with the dependent variable being the alternative of MRMD and DRMD, all redundant variables (not statistically significant) are eliminated. Then, the optimal REM model is estimated with the remaining variables. The results of this estimation show the effect of the factors on the level of RMD as follows.

For MRMD, the influential factors of MRMD level are firm size, solvency, and independence of the board of directors. The results of REM model estimation (Table 2) show that the level of MRMD is positively influenced by the firm size ($\beta = 0,0842$), the proportion of non-executive directors ($\beta = 0,4702$), and is negatively affected by solvency ($\beta = -0,11734$). The combination of these three factors explains 17.35% of the change in the level of MRMD of Vietnamese financial listed firms in the period from 2014 to 2016 (adjusted $R^2 = 17,35$).

For DRMD, the influential factors are firm size, leverage, solvency, and independence of the board of directors. The results of REM model estimation (Table 3) show that the level DRMD is influenced positively by the size of enterprises ($\beta = 0,0613$) and the proportion of non-executive directors ($\beta = 0,3593$), but is negatively affected by the debt ratio ($\beta = -0,1084$) and solvency ($\beta = -0,2348$). The combination of these four factors explains 30.39% change in DRMD of

Table 2: Regression result for the optimal REM with MRMD

$MRMD_{it} = \beta_0 + \beta_1 xSIZE_{it} + \beta_2 xSOLVENCY_{it} + \beta_3 xINDEPENDENCE_{it} + \varepsilon_{it}$			
Variables	Unstandardized β	z-stat	p-value
(Constant)	-0,6551	-2,32	0,020
SIZE	0,0842	3,91	<0,001
SOLVENCY	-0,1734	-3,99	<0,001
INDEPENDENCE	0,4702	3,62	<0,001
Adjusted R^2	0,1735		
Wald-stat	77,12		<0,0001

Source: Summary from the authors' regression analyses

Vietnamese financial listed firms in the period from 2014 to 2016 (adjusted $R^2 = 30,39$). RMD of financial listed firms. This can be explained by the fact that firms with large assets, and many

Table 3: Regression result for the optimal REM with DRMD

$DRMD_{it} = \beta_0 + \beta_1 xSIZE_{it} + \beta_2 xLEVERAGE_{it} + \beta_3 xSOLVENCY_{it} + \beta_4 xINDEPENDENCE_{it} + \varepsilon_{it}$			
Variables	Unstandardized β	z-stat	p-value
(Constant)	-0,5130	-2,13	0,033
SIZE	0,0613	3,15	0,002
LEVERAGE	-0,1084	-3,41	0,001
SOLVENCY	-0,2348	-5,36	<0,001
INDEPENDENCE	0,3593	3,69	<0,001
Adjusted R^2	0,3039		
Wald-stat	60,22		<0,0001

Source: Summary from the authors' regression analyses

3.2. Discussion of research findings

The regression results of the random effects (REM) show that the firm size has a positive effect on the level of both mandatory and discretionary

shareholders are under more pressure on providing information in general and RMD in particular for the stakeholders, especially investors. This result is consistent with agency theory, signal theory and evi-

dence from prior studies, such as Linsley and Shrives (2006).

Firm leverage has no impact on the level of MRMD, but they have a negative impact on the level of DRMD. This can be explained by the fact that firms with high debt-to-equity ratios have more interest from stakeholders (investors, owners, banks, etc.) that can make them more cautious in providing detailed information on risk management. This result is consistent with the theory of information economics and evidence from prior studies, such as Jia, Munro, and Buckby (2016).

Firm profitability has no impact on the level of RMD of financial listed firms. The results are not consistent with previous studies, such as Samanta and Dugal (2016). This may be due to the fact that in Vietnam, the disclosure of risk management is not yet focused, and therefore financial firms with high or low profitability do not consider RMD as a way to create good signal to improve their reputation, thereby attracting investors.

Firm solvency has a negative effect on both MRMD and DRMD of the financial listed firms. This result can be explained by the fact that, during the period of low liquidity, the firm tends to provide more information with an attempt to show its potential advantages to investors and creditors to attract the inflows of capital. This is in line with economic information theory. In addition, as the lower the solvency, the higher the risk of a business, the more likely it is that firms will disclose more information on risk management in order to address the asymmetric information between managers and investors; thereby reducing the agency cost. This is consistent with agency theory. The negative effect of firm solvency is consistent with previous studies, such as Elzahar and Hussainey (2012).

Auditing firms have no impact on the level of RMD of the financial listed firms. This finding, unlike the study by Kolmatsui, Legenzova, and Seilius (2016), has proved the positive impact of independent auditors on the level of information disclosure. This may be because there is no clear difference in terms of audit quality between a Big-4 auditor and non-Big 4 auditor in Vietnam when engaging in auditing for firms in this industry.

The proportion of non-executive directors has a positive impact on the level of both mandatory and discretionary RMD of the financial listed firms. In contrast, the duality of the chairman does not show any effects. This result is consistent with previous studies, such as Jia, Munro, and Buckby (2016).

4. Conclusion and implications.

4.1. Conclusion

The research provides evidence that the level of information disclosure on risk management of firms in financial sector is low. Specifically, the average level of mandatory disclosure of risk management is only 72.86%, while the level of discretionary disclosure is even lower, only 46.21%. The disclosure of risk management is influenced by firm size, solvency, and the proportion of non-executive directors. In addition, mandatory disclosure of risk management is also affected by the debt ratio.

Although this research has evaluated the disclosure of financial institutions in the securities market in Vietnam for 3 years from 2014 to 2016 and have verified some influencing factors, this study has certain limitations. The first limitation is the scope of the study (time and scope of the sample). The second limitation is not really researched the level of information on risk management in the annual report (rather than annual financial statements). The third limitation is that the factors tested in this model are modest. Future studies

may be able to conduct a review of the level of risk management for companies in other sectors and on the annual report to test the impact of other factors.

4.2. Research Implication

With more detailed regulations and coverage of information disclosure in the spirit of full disclosure of international accounting standards, regulatory authorities (the Ministry of Finance, the State Securities Commission, and the Stock Exchange) should consider applying these standards in a roadmap to improve the level of RMD of the financial listed firms in particular and listed firms in Vietnam in general. This is becoming increasingly urgent when the International Financial Reporting Standards (IFRS 9), which replaced many of the new IFRSs, has replaced the previous International Accounting Standards (IAS 39).

In addition, regulatory authorities should study and consider the application of high-quality standards and good practice principles from the developed countries for Vietnam. It then complements and completes corporate governance regulations for listed firms as well as regulations on disclosure of risk management to improve transparency in financial activities of financial listed firms in particular and in the financial market in general.

With a lower level of discretionary disclosure on risk management compared to that of mandatory one, it is necessary to have more incentive and guidance mechanism to make firms more focus on quality of disclosure, restrict the situation that firms may withhold many useful information but still not required to be disclosed. The regulators should launch an information channel to publicly recognise firms complying with disclosure requirements and voluntarily providing more information on risk management in parallel with warning those having lower level of disclosure. The implementation of such initiative could replicate good practice in information disclosure

resulting the improvement in transparency of Vietnam's stock market.

The percentage of non-executive directors is a factor contributing to improving the level of RMD. At present, Circular 95/2017/TT-BTC (Ministry of Finance, 2017) has regulations on this issue and sanctions if enterprises do not comply; However, authorities should communicate broadly about the role of board of director members' independence in order to raise awareness rather than responding to requests for rates.

Finally, the regulators should offer regularly training programs for business leaders, especially the board members, so that they are aware of the importance and benefits of RMD as well as disadvantage of withholding such information. Regulators should also respond to questions from enterprises in a timely manner.

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Summary

Theo hiểu biết của chúng tôi, đến thời điểm hiện nay vẫn chưa có nghiên cứu nào đánh giá mức độ công bố thông tin (CBTT) về quản lý rủi

ro (QLRR) của các công ty niêm yết (CTNY) thuộc ngành tài chính ở Việt Nam. Nghiên cứu này đánh giá mức độ CBTT bắt buộc và tùy ý về QLRR trong các báo cáo tài chính (BCTC) của các CTNY thuộc ngành tài chính ở Việt Nam. Vận dụng phương pháp phân tích nội dung, nghiên cứu này đã ghi nhận được mức độ CBTT về QLRR bởi các đơn vị này còn tương đối thấp. Kết quả phân tích hồi quy cũng chứng tỏ rằng mức độ CBTT về QLRR bị ảnh hưởng bởi quy mô DN, khả năng thanh toán, tỷ suất nợ và tỷ lệ thành viên hội đồng quản trị không tham gia điều hành.

NGUYEN HUU CUONG

1. Personal Profile:

- Name: Nguyen Huu Cuong
- Date of birth: 8th October 1976
- Title: Dr
- Workplace: Faculty of Accounting, Danang University of Economics
- Position: Head of Accounting Division

2. Major research directions:

Financial reporting, Integrated reporting, Information disclosure.

3. Publications the author has published his works:

- + Journal of Economics & Development
- + Economics Studies
- + Accounting and Auditing Review
- + Review of Finance
- + Journal of Economic Development
- + Corporate Ownership & Control