



Determinants of corporate disclosures: An empirical test of political economy theory

 W.A.N. Priyadarshanie^{1*}
Siti Khalidah Md Yusoff²

 S. M. Ferdous Azam³

^{1,2,3}Graduate School of Management,
Management & Science University,
Malaysia.

¹Email: nadeesha@msu.ac.lk

²Email: khalidah@msu.edu.my

³Email: dferdous@msu.edu.my

Licensed:

This work is licensed under a Creative
Commons Attribution 4.0 License.

Keywords:

Colombo stock exchange

Corporate disclosures

Political economy theory

Structural equation modelling.

JEL Classification:

M41.

Received: 5 June 2023

Revised: 27 September 2023

Accepted: 16 October 2023

Published: 19 October 2023

(* Corresponding Author)

Abstract

The principle objective of this study was to employ political economy theory in order to examine the determinants that impact the corporate disclosure of listed companies in Sri Lanka. Data was gathered from 122 companies over a period of eight years, from 2012 to 2019. Corporate disclosures of Sri Lankan listed corporations were analysed using Partial Least Square Structural Equation Modelling (PLS-SEM). Determinants of corporate disclosures have been examined in light of political economy theory, namely legitimacy, isomorphic effects, and stakeholder power. The amount of corporate disclosure was quantified using an unweighted index in this research. This study found that legitimacy, isomorphic influences, and stakeholder power are positively associated with the level of corporate disclosure. Findings suggest that managers use corporate disclosures as a strategy to legitimize themselves, manage stakeholder power, and cope with isomorphic influences. This is the first research so far to utilize the PLS-SEM to identify the determinants of corporate disclosures. Considering emerging economies across the globe, the findings of the study provide valuable insights for companies to understand how political economy theory affects the level of corporate disclosures.

Funding: This study received no specific financial support.

Institutional Review Board Statement: Not applicable.

Transparency: The authors confirm that the manuscript is an honest, accurate, and transparent account of the study; that no vital features of the study have been omitted; and that any discrepancies from the study as planned have been explained. This study followed all ethical practices during writing.

Data Availability Statement: The corresponding author may provide study data upon reasonable request.

Competing Interests: The authors declare that they have no competing interests.

Authors' Contributions: Study conception and design, data collection, analysis and interpretation of results, draft manuscript preparation and supervised the project, W.A.N.P., S.K.M.Y., and S.M.F.A. All authors have read and agreed to the published version of the manuscript.

1. Introduction

The importance of understanding the relationship between political economy theory and corporate disclosures has grown in recent years. Financial statements, corporate governance documents, sustainability reports, and other publicly available documents are all examples of corporate disclosures (Liu & Wang, 2018). Companies may choose whether or not to reveal much of the information they provide since most of it consists of voluntary information items for which there are no standards governing their disclosure. Yet, theories of corporate disclosure argue that companies might benefit from voluntary disclosure of information for the sake of fostering investor trust through transparency and integrity (Healy & Palepu, 2001). While there are studies that have looked at the various parts of corporate disclosures, such as environmental information (Matta, Akhter, & Malarvizhi, 2019), CSR information (O'dwyer, 2002), social and environmental information (Cormier & Gordon, 2001), voluntary disclosures (Watson, 2011), and so on, a review of the literature shows that there remains potential for enhancement in the corporate disclosure studies. Additionally, research undertaken in developing nations, particularly those with an emerging capital market, such as the Colombo Stock Exchange (CSE), which has a low level of disclosures, is also limited. This disparity in disclosure levels

is indicative of the importance of addressing corporate disclosures in the context of developing nations, given their ability to affect the number of corporate disclosures. Because of the vast disparities in economic, cultural, political, and social elements between the two markets, the findings of research undertaken in developed capital markets cannot be deemed relevant to developing capital markets (De Zoysa & Rudkin, 2010).

This research aims to bridge a gap by exploring the factors influencing corporate disclosures in Sri Lanka, an emerging country. Previous studies have identified predictors of corporate disclosures using various theories, including Agency Theory (Al-Razeeen & Karbhari, 2004; Healy & Palepu, 2001), Signalling Theory (Campbell, Lettau, Malkiel, & Xu, 2001), needs of capital theory, and regulatory theory (Johansen & Plenborg, 2018). However, the application of political economy theory to understanding the determinants of corporate disclosures remains underexplored. Consequently, this article seeks to investigate the drivers of corporate disclosures through the lens of political economy theory.

Corporate annual reports are viewed as multifaceted documents with political, economic, and social dimensions. They serve as tools for establishing, upholding, and legitimizing economic and political arrangements that align with a company's private interests (Guthrie & Parker, 1990). By adopting political economy theory, researchers can consider broader factors that influence what firms choose to disclose (Deegan, 2014).

Stakeholder theory, legitimacy theory, and institutional theory are all sub-theories of political economy theory that are not often examined together. Previous research has typically focused on one particular sub-theory (Fernando & Lawrence, 2014). These theories have been used to explain managers' incentives for providing non-financial disclosures, but they may also apply to voluntary financial disclosures. In recent years, some researchers have integrated these three theoretical frameworks (Amran & Haniffa, 2011; Naser & Hassan, 2013; Setyorini & Ishak, 2012). While legitimacy theory has been the most commonly employed theory in social and environmental accounting literature, Ji and Deegan (2013) note that institutional theory is gaining relevance in the field. This comprehensive approach involving all sub-theories of political economy theory offers a deeper understanding of corporate disclosure behaviour, which may not be achievable through a single theory alone (Fernando & Lawrence, 2014).

This research contributes novel insights into corporate disclosure practices. It provides empirical evidence regarding the determinants of corporate disclosures in Sri Lanka, filling a gap in the literature on corporate disclosure practices. Additionally, it addresses the scarcity of research on corporate disclosures in developing economies (Barako, Hancock, & Izan, 2006; Betah, 2013; Bhayani, 2012; Hau & Danh, 2017), which consistently indicates lower disclosure levels compared to developed nations. Secondly, this study establishes that legitimacy, stakeholder power, and isomorphic influence impact corporate reporting practices in the context of developing countries. It examines the explanatory factors of corporate disclosures and offers theoretical support for institutional theory, stakeholder theory, and legitimacy theory from a developing country perspective. Furthermore, unlike previous research that often focuses on a single type of corporate disclosure, this study explores all forms of corporate disclosure. Lastly, it contributes to the limited empirical investigations of political economy theory's explanatory power by utilizing PLS-SEM analysis to dissect the factors affecting public disclosures by corporations. Firms, investors, and other interested parties can benefit from this knowledge of the link between politics and corporate disclosures. Given the rising demand for transparency and accountability, the result suggested that policymakers, regulatory authorities, and professional organisations should consider establishing a universally accepted framework for corporate reporting, especially for non-financial information. These results can guide business leaders towards more effective corporate reporting practices by outlining best practices in disclosure.

The remainder of this research is structured as follows: Part two of this paper examines the current state of corporate disclosure in Sri Lanka. The literature review and hypothesis development are presented in the third section. Section 4 explains how the research was conducted. The findings are summarised in Section 5, and then further examined in Section 6.

2. Corporate Disclosure Practices in Sri Lanka

Sri Lanka is renowned for its open economy and free capital market. However, in the historical context of accounting practices in Sri Lanka, Perera (1975) asserts that there was no tradition of publicly disseminated financial reporting. A small group of investors primarily used accounting reports prior to independence. This scenario underwent a significant transformation in the early 1970s. During this period, the ownership structure of businesses became more complex, and new financial institutions emerged. Simultaneously, accounting statements began to play an increasingly crucial role as a source of information for decision-making.

The landscape of accounting practices in Sri Lanka experienced substantial changes with the establishment of the Sri Lanka Institute of Chartered Accountants (CA Sri Lanka) in 1959. The Colombo Stock Exchange (CSE) also contributed to improved disclosure practices by releasing additional information on its disclosure policy. Companies listed on the stock exchange are obligated to adhere to the listing rules, and the Securities and Exchange Commission (SEC) enforces various regulations that require both direct and indirect disclosures. Both the Companies Act and the CSE's listing regulations mandate certain disclosure

practices. To further improve the country's reporting mechanisms, CA Sri Lanka has adopted and revised a number of accounting and auditing standards on an ongoing basis. A significant milestone in corporate financial reporting in Sri Lanka occurred in 2012 when CA Sri Lanka introduced Sri Lanka Financial Reporting Standards (SLFRS) and Sri Lanka Accounting Standards (LKAS) to align with International Financial Reporting Standards (IFRS). Furthermore, to promote the adoption of Integrated Reporting, CA Sri Lanka has collaborated with the International Integrated Reporting Council (IIRC) to provide expertise and insights in this area within Sri Lanka.

Various media are used to disseminate business information, including annual reports, newsletters, webcasts, and publications at conferences, meetings, and seminars (Modugu, 2018). The annual report is considered the most significant official disclosure medium (Hope, 2003). However, a survey by Deloitte (2019) found that annual reports have grown longer over time, with an average of 172 pages in 2019 compared to 164 in 2018. In 2006, the average corporate report was approximately 85 pages long. In recent years, there has been a noticeable increase in the average length of corporate reports, with the current average report being over 50% longer than in 2006. Additionally, there is significant variation in the amount of information disclosed in the annual reports of different companies (KPMG International, 2016).

Hence, the objective of this research is to identify the factors influencing the level of disclosure in the annual reports of Sri Lankan listed companies. This study is grounded in political economy theory, which serves as the foundation for selecting the determinants to be investigated.

3. Political Economy Theory and Hypothesis Development

Political economy encompasses the intricate web of societal, political, and economic structures that define human existence. Political economy theory asserts that because of the deep interconnections between society, politics, and economics, any examination of economic matters must consider the broader political, social, and institutional context within which economic activities take place. Corporate annual reports are viewed as multifaceted documents with social, political, and economic dimensions. They play a crucial role in shaping, sustaining, and legitimizing economic and political systems, institutions, and ideological constructs that serve the interests of the company (Guthrie & Parker, 1990). Integrating political economy into research allows scholars to contemplate the broader factors that influence an organization's operations and its decisions regarding what information to disclose (Deegan, 2014).

These theories are commonly referred to as open-system theories in the literature (Deegan, 2014). Gray, Owen, and Adams (1996) propose that adopting a systems-oriented perspective of organizations and society allows us to emphasize the importance of information and disclosure in the interactions among organizations, individuals, groups, and the state. The systemic perspective claims that an entity is subject to influence of, and also exerts influence upon, the society within which it operates. These theories are frequently used to analyse managerial decisions regarding corporate disclosures encompassing both voluntary and mandatory disclosures, as well as financial and non-financial information. Several researchers have recently applied these three theoretical perspectives in their studies of corporate disclosures.

3.1. Legitimacy Motives and Corporate Disclosure

Legitimacy theory underscores the idea that organizations aim to maintain the perception that they operate in line with societal norms and boundaries. Organisations strive for external legitimacy (Deegan, 2014). Legitimacy theory highlights the importance of organisations demonstrating their commitment to the welfare of the general public. Noncompliance with social norms can result in various sanctions for an organisation, such as legal restrictions, resource limitations, and reduced product demand. Organisational survival is contingent on legitimacy. Organisations will implement strategies to maintain resource supplies. O'dwyer (2002) found that disclosing corporate social responsibility information can be a part of this legitimacy-building process. Legitimacy theory can also be used to explain the disclosure of corporate environmental information (O' Donovan, 2002). Corporate legitimacy can be assessed through various factors like the age of the company, the size of the company, profitability, and media coverage. This study regards profitability and firm size as indicators of corporate legitimacy. Profitability is a commonly used factor in literature to explain corporate disclosure (Naser & Hassan, 2013). The influence of profitability on CSR disclosures can be seen as either positive or negative according to legitimacy theory (Neu, Warsame, & Pedwell, 1998). Companies with a considerable amount of profit tend to convey optimistic messages to their stakeholders through corporate information. However, certain companies are disclosing comprehensive information despite incurring losses, with the aim of elucidating the reasons behind their setbacks and outlining their strategies for rectification. Research studies examining the relationship between corporate disclosures and profitability have produced inconsistent results. Mirza, Muneeb, and Ashghar (2017) observed a positive correlation between profitability and disclosures, whereas the findings of the study conducted by Reverte (2009) shows an insignificant association between the two variables. This study employs ROA as a measure of profitability.

Several studies have investigated the correlation between corporate reporting and company size, including those conducted by Naser and Hassan (2013), Othman, Thani, and Ghani (2009), and Tagesson,

Blank, Broberg, and Collin (2009). Larger corporations face heightened public scrutiny and are more vulnerable to negative reactions due to their prominent visibility. Consequently, these larger companies tend to provide more extensive information in their reports as a means of fostering public trust. Tagesson et al. (2009) employed employee count as a metric for determining firm size. Naser and Hassan (2013), Othman et al. (2009), and Hossain and Hammami (2009) employed total assets as a measure of firm size. Dyduch and Krasodomska (2017) regard total sales as a metric for determining a company's size. In this study, the value of total assets has been employed to measure firm size.

H₁: There is a relationship between legitimacy and corporate disclosures of listed companies in Sri Lanka.

3.2. Isomorphic Influences and Corporate Disclosure

According to Institutional theory, applications that use similar practices are called isomorphism. Organizational isomorphism refers to the convergence of organizations in similar environments (Dacin, 1997). There are three types of isomorphism: coercive isomorphism, mimetic isomorphism, and normative isomorphism. Depoers and Jerome (2019) found that all three types of isomorphism are associated with explanations for corporate disclosures.

Coercive isomorphism refers to the phenomenon of an organisation altering its practices in response to external pressures from its stakeholders. The field of organizational behaviour is subject to the influence of external factors, including formal or informal pressure exerted by other organisations, as well as societal cultural expectations. The pressure exerted in this context can be understood as encompassing elements of coercion, persuasion, or an invitation to engage in communal in communal activities. Chinese firms increase voluntary disclosure practices in response to coercive pressure, as discovered by Qu, Leung, and Cooper (2013). Scott (1995) posits that coercive pressures stem from the legal and contractual framework within which a firm operates. Government shareholding and foreign share ownership are viewed as forms of coercive isomorphism in this context.

Lan, Wang, and Zhang (2013) found a quadratic convex association between state ownership and voluntary disclosure. Persson and Vingren (2017) discovered that state ownership affects sustainability disclosures significantly in Swedish State-Owned Enterprises. However, Hau and Danh (2017) found that government ownership of listed companies in Vietnam was negatively associated with corporate disclosure. Mimetic isomorphism holds that businesses attempt to mimic or enhance the methods used by other businesses, maybe to acquire a competitive edge in terms of legitimacy (Deegan, 2007). Mimetic isomorphism results from uncertainty in the environment, such as regulators not telling companies how to disclose information. Setyorini and Ishak (2012) discovered that when government laws and regulations are ambiguous, firms in Indonesia prefer to follow similar practices or replicate the practices of other enterprises. Furthermore, the study conducted by Pfarrer, Smith, Bartol, and Zhang (2005) revealed that organizations demonstrate a willingness to restate their financial outcomes following the precedent set by their peers within the same industry. The measurement of mimetic impacts is typically conducted through the assessment of industry organisation membership and the qualification of prizes obtained.

Professional and industrial networks establish conventions, shared values, and laws, all of which have normative implications. The term 'group norm' is used to describe the pressure put on individuals by social groups to adopt particular patterns of behaviour in institutional settings. Regarding corporate disclosures, annual report preparers are expected to adhere to the accounting standards, which serve as a type of accounting isomorphism for the organisations that employ them. According to Nyahas, Samson, Munene, Orobia, and Kigongo Kaawaase (2017), a positive correlation exists between normative isomorphic mechanisms and voluntary disclosures. As a result, this research hypothesizes that:

H₂: There is a relationship between isomorphic influences and corporate disclosures of listed companies in Sri Lanka.

3.3. Stakeholder Pressure and Corporate Disclosure

Stakeholder theory describes how businesses communicate with their stakeholders (Deegan, 2014). According to the managerial branch of stakeholder theory, different stakeholder groups' expectations are anticipated to affect the organization's operating and reporting policies (Deegan, 2014). Organizations can manage stakeholder support and acceptance using information disclosure as a key instrument (Gray et al., 1996). Businesses can provide information to the stakeholder groups that have control over the vital resources a business requires to survive. In this case, the level of corporate disclosure that the company agrees to meet the needs of its stakeholders will vary depending on what stakeholders believe is important for the company to achieve its goals. In this study, shareholder power, debtor power, auditor power, and lobby group power were considered stakeholder powers. One measure of shareholder power is shareholder concentration. The strength of the borrower was measured by the value of the loan (debt ratio) and the value of the loan against the asset (debt to asset ratio). The type of industry, whether environmentally sensitive or not, was used to assess lobby group power. The auditor type was defined as whether the auditor belonged to the Big Four or not. Thereby, the following hypotheses have been developed:

H₃: There is a relationship between stakeholder pressure and the level of corporate disclosures by Sri Lankan listed companies.

4. Methodology

4.1. Population and Sample

According to [Sekaran and Bougie \(2018\)](#), the population denotes the complete set of individuals, occurrences, or objects that are important to the researcher's investigation. As of January 2020, the study population included 288 companies traded on the CSE. In this study, a structured sampling design was used to select the sample, as the representativeness of the sample has a significant impact on generalization. Companies listed on the Colombo Stock Exchange represent 20 Global Industry Classification Standards (GICS) industry groups. Therefore, the population can be divided into relevant and significant strata based on industry. Since the sample can be divided into several groups, a proportional stratified random sampling design is adopted. Using the [Krejcie and Morgan \(1970\)](#) sample size selection, the sample size is 165 companies. However, due to a lack of data, we collected data from 122 companies between 2012 and 2019.

4.2. Index Development

This study used an unweighted method to construct the index, following previous researchers ([Mohamad, Salleh, & Chek, 2013](#)). Researchers assessed companies' disclosure levels using a self-constructed index based on the GRI guidelines, a checklist of voluntary disclosure developed by [Hamrouni, Miloudi, and Benkraiem \(2015\)](#), and guidelines for the South Asian Federation of Accountants (SAFA) Annual Report Awards. There are 131 items in nine categories in the index. Each item was scored (1) if disclosed in the annual reports and (0) if otherwise ([Nyahas et al., 2017](#)). It was assumed that all items were equally important. After tallying up all of the points for disclosure, a total score was determined for each firm, with a maximum possible score of 131 for disclosure. After that the disclosure scores were converted into percentages by dividing the overall disclosure score of each corporation by the highest score that was attainable. Calculating the disclosure index using this methodology has been done in a number of previous studies ([Mohamad et al., 2013](#); [Nyahas et al., 2017](#)).

4.3. Data Analysis Process

Structural Equation Model is used for the data analysis to achieve research objectives. The use of PLS SEM in accounting is relatively new. The use of PLS-SEM in this study has several justifications. Utilizing the latent construct measurement is the primary justification for using PLS-SEM. Other factors include the presence of constructs that can be formatively measured in the model and the complexity of the structural model, which includes numerous constructs and indicators. Additionally, data was not distributed normally, which is not supported by Covariance-Based Structural Equation Modelling (CB-SEM).

5. Data Analysis

Collected data were entered into SPSS 20 for statistical analysis prior to PLS-SEM analysis. SMART PLS 3 was used for hypothesis testing. Hypothetical models were evaluated on a hierarchical basis using a two-step approach ([Chin, 1998](#); [Henseler, Ringle, & Sinkovics, 2009](#)). First of all, the measurement model is evaluated by looking at the reliability and validity of the measurement items. The structural model was then evaluated using multiple regression techniques.

This study comprises two distinct types of constructs, namely formative constructs and reflective constructs. Formative constructs are conceptualised as indicators that contribute to the formation of latent variables, with the directional arrow pointing from the indicators toward the construct. In contrast, reflective constructs acknowledge the influence of latent variables on observed indicators, whereby the indicators are reflective of changes in the latent variables, and the direction of the arrow is from the construct to the indicators.

Presence of formative constructs among the constructs is one justification for employing PLS-SEM in this investigation.

[Figure 1](#) depicts the structural equation model for determinants of corporate disclosures. There were three independent variables, i.e., legitimacy, isomorphic influence, and stakeholder power, in the model. There were two dimensions of legitimacy, i.e., profitability and size of the firm. Return on Assets (ROA) was used to measure profitability, while total assets were the measure of firm size. Coercive power, mimetic power, and normative power were the three dimensions of isomorphic influences. Foreign shareholding and government shareholding were used to measure coercive power. Number of industrial associations, and the number of awards won were measures of mimetic power. Managing director's membership in a professional accounting body was considered normative power. Ownership concentration was used to measure shareholder power. Debt ratio and the debt-to-asset ratio were the indicators of debt power. Whether the industry to which the company belongs is environmentally sensitive or not was considered an industry type, and it is used to measure the lobby group's power. Auditor power was measured by testing whether the firm belonged to the big four audit firms or not. The level of disclosure, which was measured by an index, was the dependent variable in the model.

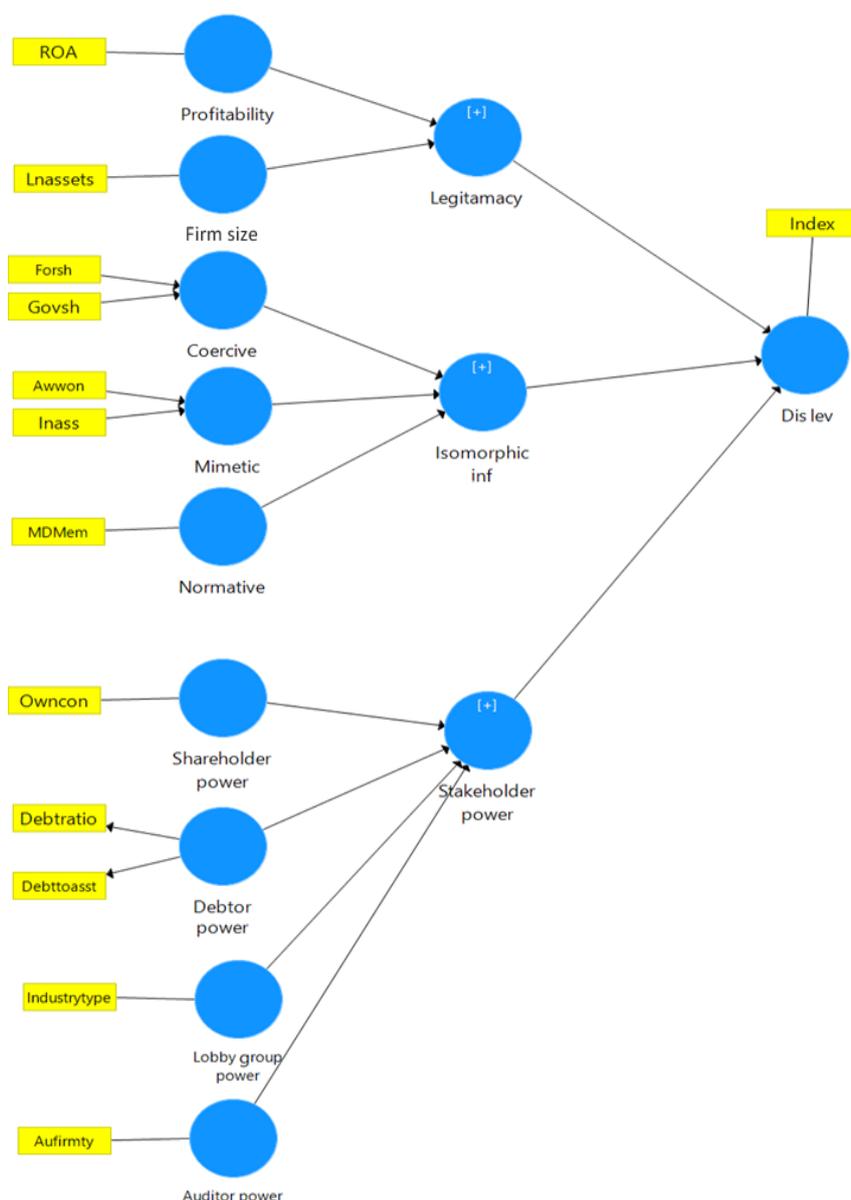


Figure 1. Structural equation model of determinants of corporate disclosures.

The model utilised in this study comprises two layers of constructs, specifically Hierarchical Component Models (HCM), as the constructs have been operationalized at elevated levels of abstraction. Higher-order components (HOCs) encapsulate second-order abstractions. Low-order constructs (LOCs) are capable of capturing sub-dimensions that belong to higher-order domains, such as the first degree. The present study employs a model that comprises reflective-formative and formative-formative relationships. According to Hair Jr., Hult, Ringle, and Sarstedt (2016), there are various concerns to contemplate when utilising the repeated indicator technique for creating formative-formative and reflective-formative models. A two-stage methodology was employed, integrating the repeated indicator approach with latent scores. In the initial phase, the repeated indicator approach was employed to acquire the scores of the latent variables of LOCs. The LOC scores are employed as manifest variables in the second step of the HOC measurement model.

5.1. Evaluation of Measurement Model – First Order Constructs

Figure 2 presents the first-order constructs in the measurement model. The proposed measurement model has been evaluated in terms of reliability and validity (Hair Jr. et al., 2016). Following other researchers (Awn & Azam, 2020; Kartadjudena & Rodgers, 2019), the measurement model was evaluated using the following criteria: convergent validity (using indicator reliability and Average Variance Extracted (AVE)), internal consistency (using Cronbach's alpha and composite reliability), and discriminant validity (Fornell and Larcker and Heterotrait-Monotrait ratio (HTMT)). Table 1 presents the statistical results of the evaluation of reflective constructs.

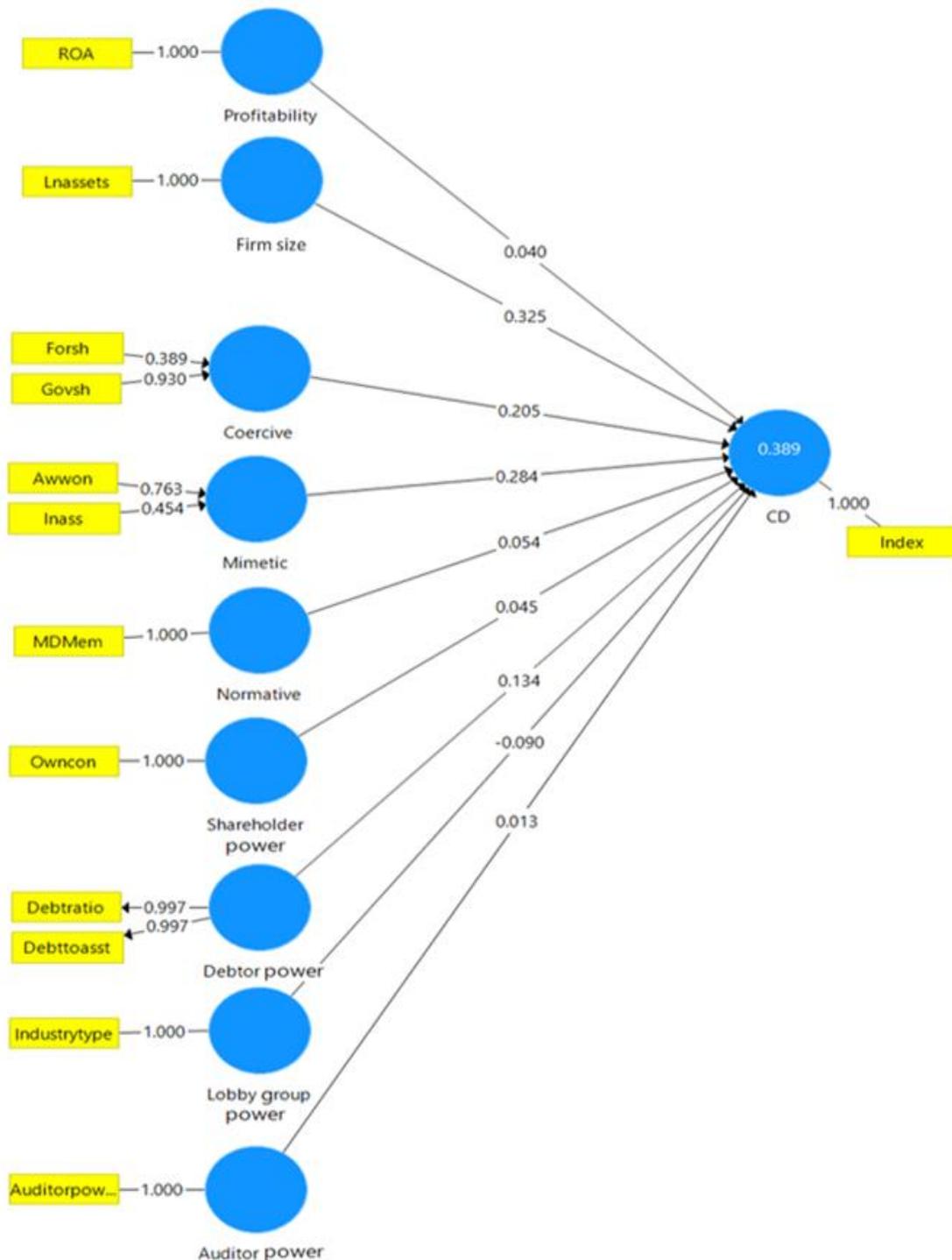


Figure 2. First order constructs.

To evaluate the convergent validity of reflective constructs, researchers consider the outer loadings of the indicators and AVE. The rule of thumb is that outer loading should be 0.70 or higher (Hair Jr. et al., 2016). However, outer loading values greater than 0.4 are acceptable (Churchill, 1979; Hulland, 1999). All variables had outer loads greater than 0.7.

The AVE is defined as the mean of the squares of the outer loads of the indicator of the construct. It must be 0.50 or higher to determine convergent validity (Hair Jr. et al., 2016). The results show the AVE of the debtor power (0.994) indicates measures greater than 0.5, which explains more than half of the variance in the indicators. For internal consistency to be considered adequate, composite reliability and Cronbach's alpha coefficients must be 0.70 or higher (Hair Jr. et al., 2016). The values satisfy the standard criteria recommended for evaluating measurement models.

Table 1 Evaluation of reflective constructs.

Latent variable	Measures	Loadings	Cronbach's alpha	CR	AVE
Debtor power	Debt ratio	0.997	0.994	0.997	0.994
	Debt to asset	0.997			

The Fornell-Larcker criterion and HTMT ratio can be used to examine discriminant validity. The results of the Fornell and Larcker criteria are presented in the Table 2.

Table 2. Fornell and Larcker criterion.

Indicator	Auditor power	CD	Debtor power	Firm size	Lobby group power	Normative	Profitability	Shareholder power
Auditor power	1							
CD	0.09	1						
Debtor power	-0.148	0.259	0.997					
Firm size	0.223	0.517	0.316	1				
Lobby group power	0.165	-0.079	0.023	0.03	1			
Normative	0.088	0.063	0.271	0.127	0.227	1		
Profitability	0.201	0.067	0.037	0.037	0.05	-0.031	1	
Shareholder power	0.073	-0.052	-0.044	-0.175	-0.088	-0.11	-0.014	1

According to Fornell-Larcker criteria, the square root of each construct's AVE should be greater than its highest correlation with another construct (Hair Jr. et al., 2016). The Fornell-Larcker statistics in Table 2 show that the diagonal values representing the square root of the AVE are larger than the off-diagonal elements in the respective lines, indicating shared correlations among the constructs. Thus, the model satisfies the heuristic requirements of the Fornell and Larcker model.

The results of the HTMT are presented in Table 3.

Table 3. HTMT.

Indicator	Auditor power	CD	Debtor power	Firm size	Lobby group power	Normative	Profitability	Shareholder power
Auditor power								
CD	0.09							
Debtor power	0.149	0.26						
Firm size	0.223	0.517	0.317					
Lobby group power	0.165	0.079	0.023	0.03				
Normative	0.088	0.063	0.272	0.127	0.227			
Profitability	0.201	0.067	0.037	0.037	0.05	0.031		
Shareholder power	0.073	0.052	0.044	0.175	0.088	0.11	0.014	

HTMT value is also utilized to measure the discriminant validity. According to the HTMT rule, if the correlation between two constructs is close to 1, there is no discriminant validity between the constructs. However, a more conservative threshold value of 0.85 is suggested by Hair Jr. et al. (2016). Based on the findings presented in Table 3, it can be observed that all HTMT values are below the threshold value of 0.85. This suggests that all measures successfully pass the discriminant validity test.

The evaluation of formative constructs in measurement models involves the assessment of their multicollinearity with the indicators. The authors employed the Variance Inflation Factor (VIF) to account for multicollinearity and evaluated the significance of the outer weights to validate the formative constructs. The VIF value ranges from 1 upward. Typically, a VIF value exceeding 5 is indicative of a substantial degree of correlation and is cause for concern.

Table 4. Evaluation of formative constructs.

Latent variable	Measures	VIF	Weights	T statistic	P value
Coercive	Forsh	1.001	0.389	4.66	0.000
	Govsh	1.001	0.930	25.66	0.000
Mimetic	Awwon	1.102	0.763	16.03	0.000
	Inass	1.102	0.454	7.44	0.000

Table 4 presents the statistical results of VIF and significance of outer weights. The findings show that the outer weights of indicators within the formative construct exhibit statistical significance at a level of 1%. Furthermore, the VIF values for these weights range from 1 to 1.102, suggesting that the indicators are not affected by multicollinearity and can be regarded as independent variables.

After evaluating the first-order constructs for reliability and validity, second-order models were built. Second-order constructs are represented by the factor scores of their associated first-order constructs. Figure 3 depicts the second-order model.

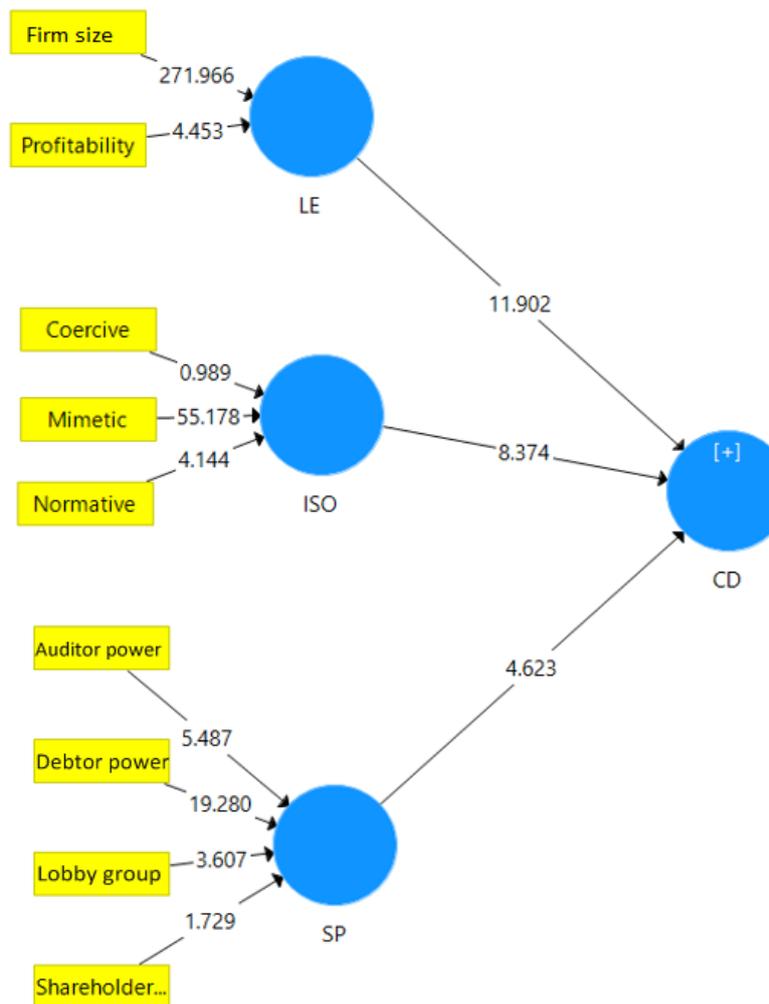


Figure 3. Second order model.

5.2. Evaluation of Measurement Model – Second Order Constructs

The relationship between second-order constructs and their indicators is formative. Thereby, VIF value and the significance of outer weights were selected to validate the model. Table 5 presents the results of the validation measures for the second-order model. VIF values are notably below the threshold value of 5. This suggests that the issue of collinearity among the dimensions is not a significant concern for the present study.

According to Hair Jr. et al. (2016), the second measure for evaluating a formative model is the statistical significance of the outer weights associated with the formative items. Table 5 presents the statistical data pertaining to the outer weights. It is noteworthy that, with the exception of profitability and shareholder power, all other dimensions exhibit statistical significance. Consequently, the model eliminated considerations of profitability and shareholder influence and was developed again.

Table 5. Validation measures of the second order model.

Construct	Dimensions	VIF	Outer weights	T-value	P value	Significance (P< 0.05)
Legitimacy	Firm size	1.01	0.99	425.49	0.00	Yes
	Profitability	1.01	0.01	0.88	0.38	No
Isomorphic influences	Coercive	1.02	0.63	8.01	0.00	Yes
	Mimetic	1.1	0.74	11.29	0.00	Yes
	Normative	1.11	0.31	4.03	0.00	Yes
Stakeholder power	Auditor power	1.05	0.49	4.9	0.00	Yes
	Debtor power	1.02	0.89	14.43	0.00	Yes
	Shareholder power	1.02	0.21	1.53	0.13	No
	Lobby group power	1.04	0.28	2.33	0.00	Yes

5.3. Amended Measurement Model - Second Order Constructs

Figure 4 presents the amended measurement model after removing propitability and shareholder influence.

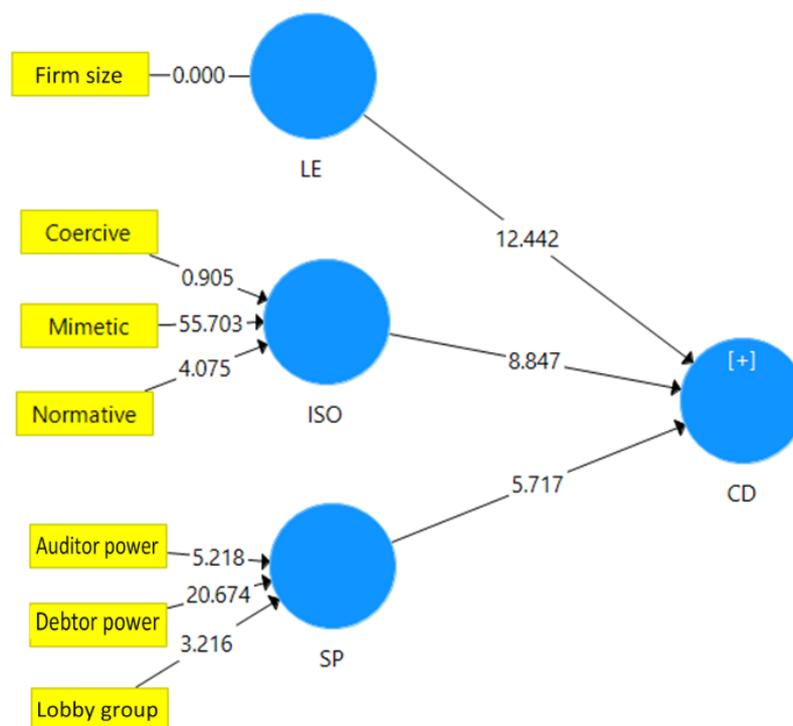


Figure 4. Amended second order model.

Table 6 presents the results of the validation measures (VIF and significance of outer weights) of the amended second-order model.

Table 6. Validation measures of the second order model (Amended).

Construct	Dimensions	VIF	Outer weights	T-value	P value	Significance (P< 0.05)
Legitimacy	Firm size	1	1	425.49	0.00	Yes
Isomorphic influences	Coercive	1.02	0.63	8.01	0.00	Yes
	Mimetic	1.1	0.74	11.49	0.00	Yes
	Normative	1.11	0.31	3.99	0.00	Yes
Stakeholder power	Auditor power	1.05	0.47	4.7	0.00	Yes
	Debtor power	1.02	0.91	17.38	0.00	Yes
	Lobby group power	1.03	0.29	2.43	0.02	Yes

In the amended model, the statistics for the outer weights are statistically significant. Finally, to summarize, the statistical analysis of the PLS path model indicates that the 09 dimensions, which are comprised of 12 sub-items as indicators, are appropriate for representing the 03 second-order constructs.

5.4. Structural Model

After establishing a reliable and validated measurement or outer model, the subsequent step involves estimating the assumed causal linear relationships among the exogenous and endogenous latent variables.

Figure 5 presents the structural model of the analysis.

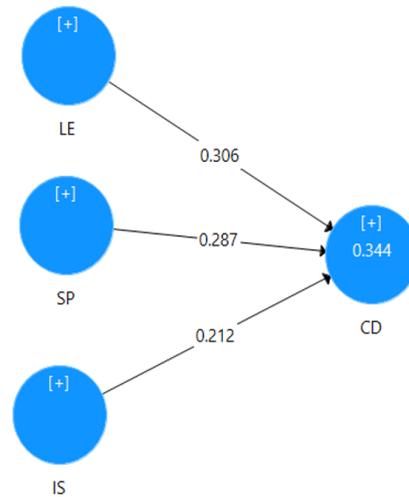


Figure 5. Structural model.

Table 7 presents the results of path analysis.

Table 7. Path coefficient.

Path	Coefficient	T statistics	P values
IS -> CD	0.212	7.609	0.000
LE -> CD	0.306	11.25	0.000
SP -> CD	0.287	10.068	0.000

Results indicate that isomorphic influence, legitimacy, and stakeholder power have a significant positive impact on the level of corporate disclosures. Results are in line with previous studies on corporate disclosure. According to the researchers (Nyahas et al., 2017; Qu et al., 2013), stakeholder power and their expectations impact disclosure policies of the firm. Stakeholder theory also argues that the expectations of different stakeholders will impact operating and disclosure policies of the organizations. Isomorphism theory assumes that organizations in similar environmental conditions adopt the same policies. Confirming the theory, the results of this study also found that there is a positive impact of isomorphic influences on the level of corporate disclosures. Findings are in line with the results of other researchers (Nyahas et al., 2017; Persson & Vingren, 2017). According to the proponents of legitimacy theory, businesses actively promote themselves as law-abiding and ethical in an effort to gain public trust. The research supports the notion and demonstrates that credibility has a substantial beneficial effect on the number of disclosures made. Prior research conducted by O’dwyer (2002); O’ Donovan (2002), and Mirza et al. (2017) has similarly demonstrated a positive correlation between corporate legitimacy and the extent of disclosures.

6. Discussion

This study aimed to examine the factors that influence corporate disclosures. The political economy theory posits that corporate disclosures are determined by legitimacy, isomorphic influences, and stakeholder power. The study found that all of these factors have a positive impact on disclosure levels.

Legitimacy theory suggests that organizations disclose information to maintain the perception that they are conforming to societal norms and expectations (Deegan, 2014). Legitimacy was measured using firm size and profitability. Large corporations are more susceptible to negative responses due to their high visibility. Hence, companies aim to mitigate conflicts between management and stakeholders by providing additional information. The study's results support the assertion that profitable companies convey positive messages to their stakeholders. This study's results are consistent with those of previous researchers (Mirza et al., 2017; O’dwyer, 2002; Zhang, 2013).

Depoers and Jerome (2019) suggest that disclosures are linked to all three types of isomorphism. Firms enhance their voluntary disclosure practices in response to coercive pressure, as noted by Qu et al. (2013). Normative influences which are arising from particular institutional practices leads to increase the volume of disclosures. In the Sri Lankan context, CA Sri Lanka has issued accounting standards that listed companies

must comply with when preparing their financial statements. Meanwhile the Integrated Reporting Council also has issued an IR framework to provide guidance on annual report preparation.

Mimetic isomorphism states that organizations strive to imitate the institutional practices of other organizations (Deegan, 2007). The study found a significant positive correlation between isomorphic influences and the extent of corporate disclosures. Prior studies (Nyahas et al., 2017; Persson & Vingren, 2017) have also established a positive correlation between organizational isomorphism and the extent of corporate disclosures.

Stakeholder theory primarily focuses on how firms engage with their stakeholders. The managerial aspect of stakeholder theory suggests that the operating and disclosure policies of an organisation are influenced by the expectations of various stakeholders (Deegan, 2014). Information disclosure is a key strategy for companies to effectively manage stakeholders with varying interests. This study examined the power of shareholders, debtors, auditors, and lobby groups. The study found a positive correlation between stakeholder power and disclosure levels, supporting stakeholder theory. Consistent findings were reported by other scholars as well (Nyahas et al., 2017; Qu et al., 2013).

7. Conclusion

The findings of the study suggests that the disclosure practices of corporations can be elucidated by considering factors such as legitimacy, stakeholder power, and isomorphic influences. The study enhances political economy theory by providing insight into the factors that influence the disclosure of corporate information by companies listed on the CSE. The study's results enhance institutional theory, stakeholder theory, and legitimacy theory by identifying the factors within each theory and elucidating their impact on corporations' decisions to disclose information in their annual reports. This study addresses the lack of empirical research on corporate disclosures in developing countries. This study introduces a novel, structured, and comprehensive disclosure index that enhances the current understanding of corporate disclosures. This index was designed to measure corporate disclosures by categorizing the extent of disclosures made in annual reports into nine categories. The study utilised PLS-SEM to analyse the data, representing a novel approach in the field of accounting. The application of factor analysis in PLS-SEM has potential benefits for corporate disclosure theory. It can aid in identifying the underlying correlation patterns among variables and testing theoretical models by detecting the overall structure of relationships between variables.

Corporate disclosures can serve as a means for managers to legitimise their actions, manage stakeholder power, and deal with isomorphic pressures. This study's findings highlight particular aspects of disclosure enhancements that current practitioners should focus on for learning. The disclosure index clarifies reporting requirements for companies that were previously uncertain about the contents of their annual reports. This disclosure index analysis establishes a benchmark for future practitioners to follow regarding the practicality of disclosing corporate information in annual reports.

This study has significant practical implications for non-financial reporting regulations. CA Sri Lanka, the prominent accounting organisation in Sri Lanka, has initiated the development of regulations for non-financial reporting by forming a dedicated committee. The committee could utilise the study's results to formulate an improved non-financial reporting policy.

The study's results necessitate recommendations. Many companies strive to adhere to the Global Reporting Initiative (GRI) guidelines, which are a voluntary and universal set of guidelines. The applicability of GRI guidance varies across countries, industries, and companies of different sizes. Regulators ought to consider adopting a principle-based approach to non-financial information disclosure guidance, as opposed to relying on rule-based guidelines.

This study is the first to employ PLS-SEM to identify the factors that influence corporate disclosures. The study's use of political economy theory to analyse differences in corporate disclosures does not negate the potential explanatory value of other theories, such as agency theory and positive accounting theory. The study employed content analysis to assess disclosure levels. Content analysis is subjective. The unweighted index was utilised to quantify the data simultaneously. To enhance comprehension of corporate disclosures, it is preferable to assess the quality of the disclosures rather than their quantity. This study assessed solely the data presented in annual reports, which is a primary medium for conveying corporate information and a significant type of corporate documentation in the literature. Alternative communication methods, such as press releases, quarterly reports, and websites, provide timely information.

The study's findings and limitations suggest several potential areas for future research. The quality of disclosures can be evaluated through a weighted index that assigns weights to various aspects of disclosures. Subsequent research should emphasise the calibre, in addition to the quantity, of the disclosures. Alternative media can be a faster and more efficient means of conveying information than traditional annual reports in certain situations. Subsequent studies could encompass these alternative sources along with annual reports.

Apart from political economy theory, researchers may analyse the influence of resource dependency theory, agency theory, and positive accounting theory. They may also assess the effect of corporate culture and institutional settings (such as ownership structure and corporate governance) on corporate disclosures using

the structural equation modelling method, which is a recent trend in accounting research. It has the potential to make a valuable contribution to the literature on corporate reporting.

References

- Al-Razeen, A., & Karbhari, Y. (2004). Interaction between compulsory and voluntary disclosure in Saudi Arabian corporate annual reports. *Managerial Auditing Journal*, 19(3), 351-360. <https://doi.org/10.1108/02686900410524364>
- Amran, A., & Haniffa, R. (2011). Evidence in development of sustainability reporting: A case of a developing country. *Business Strategy and the Environment*, 20(3), 141-156. <https://doi.org/10.1002/bse.672>
- Awn, A. M., & Azam, S. F. (2020). The determinants of investment in Islamic Sukuk: A study of Libyan investors. *International Journal of Business Society*, 4(3), 9-19.
- Barako, D. G., Hancock, P., & Izan, H. (2006). Factors influencing voluntary corporate disclosure by Kenyan companies. *Corporate Governance: An International Review*, 14(2), 107-125. <https://doi.org/10.1111/j.1467-8683.2006.00491.x>
- Betah, T. (2013). An investigation into determinants of corporate disclosure & transparency of listed companies in Zimbabwe during financial crisis (2007-2008). *International Journal of Scientific & Technology Research*, 2(1), 19-25.
- Bhayani, S. (2012). *Association between firm-specific characteristics and corporate disclosure: The case of India*. Paper presented at the International Conference on Business, Economics, Management and Behavioral Sciences (ICBEMBS'2012) Jan. 7-8, 2012 Dubai.
- Campbell, J. Y., Lettau, M., Malkiel, B. G., & Xu, Y. (2001). Have individual stocks become more volatile? An empirical exploration of idiosyncratic risk. *The Journal of Finance*, 56(1), 1-43. <https://doi.org/10.1111/0022-1082.00318>
- Chin, W. W. (1998). The partial least squares approach to structural equation modeling. *Modern Methods for Business Research*, 295(2), 295-336.
- Churchill, G. (1979). A paradigm for developing better measures of marketing constructs. *Journal of Marketing Research*, 16, 64-73. <http://dx.doi.org/10.2307/3150876>
- Cormier, D., & Gordon, I. M. (2001). An examination of social and environmental reporting strategies. *Accounting, Auditing & Accountability Journal*, 14(5), 587-617. <https://doi.org/10.1108/eum0000000006264>
- Dacin, M. T. (1997). Isomorphism in context: The power and prescription of institutional norms. *Academy of Management Journal*, 40(1), 46-81. <https://doi.org/10.5465/257020>
- De Zoysa, A., & Rudkin, K. (2010). An investigation of perceptions of company annual report users in Sri Lanka. *International Journal of Emerging Markets*, 5(2), 183-202. <https://doi.org/10.1108/17468801011031810>
- Deegan, C. (2007). Organisational legitimacy as a motive for sustainability reporting. *Sustainability Accounting and Accountability*, 127-149. <https://doi.org/10.4324/noe0415384889.ch7>
- Deegan, C. (2014). *Financial accounting theory*. London: McGraw-Hill.
- Deloitte. (2019). *Annual report insights: Surveying FTSE reporting*. Retrieved from <https://www2.deloitte.com/uk/en/pages/audit/articles/annual-report-insights.html>
- Depoers, F., & Jerome, T. (2019). Coercive, normative, and mimetic isomorphism as drivers of corporate tax disclosure: The case of the tax reconciliation. *Journal of Applied Accounting Research*, 21(1), 90-105.
- Dyduch, J., & Krasodomska, J. (2017). Determinants of corporate social responsibility disclosure: An empirical study of polish listed companies. *Sustainability*, 9(11), 1-24. <https://doi.org/10.3390/su9111934>
- Fernando, S., & Lawrence, S. (2014). A theoretical framework for CSR practices: Integrating legitimacy theory, stakeholder theory and institutional theory. *Journal of Theoretical Accounting Research*, 10(1), 149-178.
- Gray, R., Owen, D., & Adams, C. (1996). *Accounting and accountability: Changes and challenges in corporate social and environmental reporting*. London: Prentice-Hall.
- Guthrie, J., & Parker, L. D. (1990). Corporate social disclosure practice: A comparative international analysis. *Advances in Public Interest Accounting*, 3, 159-175.
- Hair Jr., J. F., Hult, G. T. M., Ringle, C., & Sarstedt, M. (2016). *A primer on partial least squares structural equation modeling (PLS-SEM)*. Thousand Oaks, CA: Sage Publications.
- Hamrouni, A., Miloudi, A., & Benkraiem, R. (2015). Signaling firm performance through corporate voluntary disclosure. *Journal of Applied Business Research*, 31(2), 609-620. <https://doi.org/10.19030/jabr.v31i2.9157>
- Hau, L. L., & Danh, L. C. (2017). Determinants of corporate disclosure in financial statements: Evidence from Vietnamese listed firms. *International Journal of Advanced Engineering, Management and Science*, 3(5), 474 - 480. <https://doi.org/10.24001/ijaems.3.5.11>
- Healy, P. M., & Palepu, K. G. (2001). Information asymmetry, corporate disclosure, and the capital markets: A review of the empirical disclosure literature. *Journal of Accounting and Economics*, 31(1-3), 405-440. [https://doi.org/10.1016/s0165-4101\(01\)00018-0](https://doi.org/10.1016/s0165-4101(01)00018-0)
- Henseler, J., Ringle, C., & Sinkovics, R. (2009). The use of partial least squares path modeling in international marketing. *Advance in International Marketing*, 20, 277-319. [https://doi.org/10.1108/s1474-7979\(2009\)0000020014](https://doi.org/10.1108/s1474-7979(2009)0000020014)
- Hope, O. K. (2003). Disclosure practices, enforcement of accounting standards, and analysts' forecast accuracy: An international study. *Journal of Accounting Research*, 41(2), 235-272. <https://doi.org/10.1111/1475-679x.00102>
- Hossain, M., & Hammami, H. (2009). Voluntary disclosure in the annual reports of an emerging country: The case of Qatar. *Advances in Accounting*, 25(2), 255-265. <https://doi.org/10.1016/j.adiac.2009.08.002>
- Hulland, J. (1999). Use of partial least squares (PLS) in strategic management research: A review of four recent studies. *Strategic Management Journal*, 20, 195-204. [https://doi.org/10.1002/\(SICI\)1097-0266\(199902\)20:2<195::AID-SMJ13>3.0.CO;2-7](https://doi.org/10.1002/(SICI)1097-0266(199902)20:2<195::AID-SMJ13>3.0.CO;2-7)
- Ji, S., & Deegan, C. (2013). *The origin, use and contribution of legitimacy theory to social and environmental accounting research, working paper*. Melbourne: School of Accounting, RMIT University.
- Johansen, T. R., & Plenborg, T. (2018). Company responses to demands for annual report changes. *Accounting, Auditing & Accountability Journal*, 31(6), 1593-1617. <https://doi.org/10.1108/aaaj-02-2016-2419>

- Kartadjuma, E., & Rodgers, W. (2019). Executive compensation, sustainability, climate, environmental concerns, and company financial performance: Evidence from Indonesian commercial banks. *Sustainability*, 11(6), 1-21. <https://doi.org/10.3390/su11061673>
- KPMG International. (2016). *Room for improvement: The KPMG survey of business reporting (2nd ed.)*. Retrieved from <https://www.integratedreporting.org/wp-content/uploads/2016/06/room-for-improvement-survey-of-business-reporting.pdf>
- Krejcie, R. V., & Morgan, D. W. (1970). Determining sample size for research activities. *Educational and Psychological Measurement*, 30(3), 607-610. <https://doi.org/10.1177/001316447003000308>
- Lan, Y., Wang, L., & Zhang, X. (2013). Determinants and features of voluntary disclosure in the Chinese stock market. *China Journal of Accounting Research*, 6(4), 265-285. <https://doi.org/10.1016/j.cjar.2013.04.001>
- Liu, Z., & Wang, X. (2018). How to regulate individuals' privacy boundaries on social network sites: A cross-cultural comparison. *Information & Management*, 55(8), 1005-1023. <https://doi.org/10.1016/j.im.2018.05.006>
- Matta, R., Akhter, J., & Malarvizhi, P. (2019). Managers' perception on factors impacting environmental disclosure. *Journal of Management*, 6(2), 219-229. <https://doi.org/10.34218/jom.6.2.2019.025>
- Mirza, H. H., Muneeb, K. F., & Ashghar, M. J. K. (2017). Determinants of voluntary disclosure in non-financial listed companies of Pakistan. *South Asian Journal of Banking and Social Sciences*, 1-10.
- Modugu, K. P. (2018). Corporate disclosure: A synthesis of literature. *International Journal of Accounting and Financial Reporting*, 8(3), 1-28. <https://doi.org/10.5296/ijaf.v8i3.11773>
- Mohamad, Z., Salleh, H. M., & Chek, I. T. (2013). Stakeholder influence on the quality of non-financial information disclosure in five Malaysian sectors. *International Journal of Arts and Commerce*, 2(10), 93-102.
- Naser, K., & Hassan, Y. (2013). Determinants of corporate social responsibility reporting: Evidence from an emerging economy. *Journal of Contemporary Issues in Business Research*, 2(3), 56-74.
- Neu, D., Warsame, H., & Pedwell, K. (1998). Managing public impressions: Environmental disclosures in annual reports. *Accounting, Organizations and Society*, 23(3), 265-282. [https://doi.org/10.1016/s0361-3682\(97\)00008-1](https://doi.org/10.1016/s0361-3682(97)00008-1)
- Nyahas, I., Samson, Munene, J. C., Orobia, L., & Kigongo Kaawaase, T. (2017). Isomorphic influences and voluntary disclosure: The mediating role of organizational culture. *Cogent Business & Management*, 4(1), 1351144. <https://doi.org/10.1080/23311975.2017.1351144>
- O' Donovan, G. (2002). Environmental disclosures in the annual report, extending the applicability and predictive power of legitimacy theory. *Accounting, Auditing and Accountability Journal*, 15(3), 344-371.
- O'dwyer, B. (2002). Managerial perceptions of corporate social disclosure: An Irish story. *Accounting, Auditing & Accountability Journal*, 15(3), 406-436. <https://doi.org/10.1108/09513570210435898>
- Othman, R., Thani, A. M., & Ghani, E. K. (2009). Determinants of Islamic social reporting among top Shariah-approved companies in Bursa Malaysia. *Research Journal of International Studies*, 12(12), 4-20.
- Perera, M. (1975). Accounting and its environment in Sri Lanka. *Abacus*, 11(1), 86-96. <https://doi.org/10.1111/j.1467-6281.1975.tb00045.x>
- Persson, K., & Vingren, T. (2017). *Factors affecting the sustainability disclosures in Swedish State-Owned enterprises as hybrid organizations*. Master Thesis, Kristianstad University.
- Pfarrer, M. D., Smith, K. G., Bartol, D. M., & Zhang, X. (2005). *Coming forward: Institutional influence on voluntary disclosure*. Retrieved from <http://mba.track.edu/mechanism/papers/pages>
- Qu, W., Leung, P., & Cooper, B. (2013). A study of voluntary disclosure of listed Chinese firms—a stakeholder perspective. *Managerial Auditing Journal*, 28(3), 261-294. <https://doi.org/10.1108/02686901311304376>
- Reverte, C. (2009). Determinants of corporate social responsibility disclosure ratings by Spanish listed firms. *Journal of Business Ethics*, 88(2), 351-366. <https://doi.org/10.1007/s10551-008-9968-9>
- Scott, W. R. (1995). *Institutions and organizations*. Thousand Oaks, CA: Sage.
- Sekaran, U., & Bougie, R. (2018). *Research methods for business: A skill-building approach* (6th ed.). Haddington: John Wiley & Sons.
- Setyorini, C. T., & Ishak, Z. (2012). Corporate social and environmental disclosure: A positive accounting theory view point. *International Journal of Business and Social Science*, 3(9), 152-164.
- Tagesson, T., Blank, V., Broberg, P., & Collin, S. O. (2009). What explains the extent and content of social and environmental disclosures on corporate websites: A study of social and environmental reporting in Swedish listed corporations. *Corporate Social Responsibility and Environmental Management*, 16(6), 352-364. <https://doi.org/10.1002/csr.194>
- Watson, T. J. (2011). Ethnography, reality, and truth: The vital need for studies of 'how things work' in organizations and management. *Journal of Management Studies*, 48(1), 202-217. <https://doi.org/10.1111/j.1467-6486.2010.00979.x>
- Zhang, J. (2013). *Determinants of corporate environmental and social disclosure in Chinese listed mining, electricity supply and chemical companies annual reports*. Retrieved from <https://ro.ecu.edu.au/theses/529>