

# Parliamentary Briefing



## The value of narrative reporting

### ACCA

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Globally, we support our 122,000 members and 325,000 students throughout their careers, providing services through a network of 80 offices and centres around the world. We use our expertise and experience in areas such as tax and finance to work with governments, donor agencies and professional bodies to develop the global accountancy profession and to advance the public interest. By promoting our global standards, and supporting our members wherever they work, we aim to meet the current and future needs of international business.

### What is narrative reporting and why is it important?

Narrative reporting is an increasingly important feature of corporate reports, providing an opportunity for directors to set out a clear and balanced analysis of the strategic position and direction of their business. Good narrative reporting is a means by which companies can achieve transparent and open communication with their shareholders.

Voluntary narratives are defined as those parts of the annual report not mandated by Companies Act requirements and not reported on a part of the audit or report. Such disclosure narratives include, among other things, the chairman's statement, the chief executive's review, social and environmental reports, and risk disclosures. Some of these are mandatory, for example, the directors' report, while other elements, such as sustainability reporting are not.

There has been a marked growth in many types of voluntary and narrative reporting in recent years, but the actual usefulness of this surfeit of narrative in annual reports, who reads it, and whether it is material to fund allocation decisions made by investors, is unclear. And if it is not useful or material, what are the implications for those preparing annual reports?

ACCA's research, prepared by the University of Northumbria and the University of Newcastle sought to investigate:

- The real, if any, contribution these reports made to companies
- Whether the reports impacted upon decision-makers or investment analysts' stock recommendation

## Summary of key findings

The findings show that analysts are dismissive of anything other than directly value relevant numerical data. Specific findings include:

- Analysts are generally sceptical about all voluntary narrative reporting and are dismissive of large sections of it as irrelevant. Indeed, they are dismissive of anything other than directly value-relevant numerical data.
- There is a general belief that narrative reporting is not immediately applicable nor helpful in the primary tasks of the sell-side (to construct forecast models and produce written reports for the buy-side).
- Chief executive's statements are considered more useful than the chairman's statements because they are more likely to contain information on future strategies. Indeed, the content of the chairman's statement was generally dismissed as irrelevant to investment decisions or to forecasting figures.
- Risk disclosure is thought of as too general in nature to be useful.
- Corporate governance reporting (mandatory under listing rules under UK 'comply or explain' practice) is usually unread because governance in UK banking was generally trusted by the analysts.
- Social and environmental reporting was universally considered irrelevant and incapable of influencing a financial forecast. It is rarely read by analysts.
- There is the view that no narrative reporting is capable of informing, amending or challenging a financial forecast.

## Implications of the research

- The research poses many challenges to preparers of annual reports who have presided over the massive increase in the narrative reporting. It appears that there is a need to reconsider how to make narrative reporting relevant and material to investors.
- It questions the value of narrative content, if any, to analysts.
- It raises the question of what, if anything, can be done to change the view that no narrative reporting is capable of informing, amending or challenging a financial forecaster.
- The research also poses the question whether we need to break up the annual reporting system or whether we should just continue as we are.

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