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JAROSŁAW PAWŁOWSKI\*

Nicolaus Copernicus University in Toruń

## THE USEFULNESS OF FINANCIAL REPORTING FOR FINANCIAL INSTRUMENTS IN THE DECISION-MAKING PROCESSES OF INDIVIDUAL INVESTORS

**Keywords:** financial reporting, individual investors, financial instruments.

**J E L Classification:** G11.

**Abstract:** This study focuses on the issue of usefulness of financial reporting for financial instruments in the decision-making processes of individual investors. Dynamic development of financial instruments, identified difficulties in application and analysis of the rules of accounting for financial instruments, as well as the importance of individual investors on the financial market were the major reasons to deal with this issue. The main purpose of this study is an assessment of usefulness of reporting data concerning financial instruments in the decision-making processes of individual investors in Poland. To achieve the specified goal, the following research methods have been used: descriptive, comparative, subject literature review, third party research analysis and analysis of selected results of individual research. A significant part of the study concerns the analysis of the results of a survey conducted in a group of 408 individual investors in Poland.

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\* Contact information: [jpawlowski@umk.pl](mailto:jpawlowski@umk.pl), Department of Finance Management, Faculty of Economic Sciences and Management, Nicolaus Copernicus University in Toruń, Gagarina 13a, 87-100 Toruń, Poland, phone: +48 56 611 46 34; ORCID ID: <https://orcid.org/0000-0002-5021-8871>.

## ■■■ INTRODUCTION

Individual investors constitute the basic group of participants of contemporary financial markets (Kaniel, Saar & Titman, 2008, pp. 23–24). They are important group for standards accounting setters (Brazel, Jones, Thayer & Warne, 2015, p. 1374). In their decision-making processes, they often use reporting data, therefore financial reporting is a major source of information. As a result of the rapid development of financial instruments, a growth in the value and volume of their trade is noticeable. An increasing number of entities is involved in transactions where subjects are financial instruments. Nonetheless, growing complexity of current financial instruments, in particular derivatives, causes difficulties for business entities in preparing appropriate information, while investors face problems related with proper analysis of provided information. Considering that, this study gives an insight into the issue of usefulness of financial reporting for financial instruments in the decision-making processes of individual investors. The main purpose of this study is an assessment of usefulness of reporting data concerning financial instruments in the decision-making processes of individual investors. To achieve the specified goal, the following research methods have been used: descriptive, comparative, subject literature review, third party research analysis and analysis of selected results of individual research.

### **THE RESEARCH METHODOLOGY AND THE COURSE OF THE RESEARCH PROCESS**

This paper aims at analysing the usefulness of financial reporting for financial instruments from the point of view of individual investors.

The major purpose of the study is the assessment of usefulness of reporting data concerning financial instruments in the decision-making processes of individual investors in Poland.

To achieve the assumed goal, the following research methods have been used: descriptive, comparative, subject literature review, third party research analysis and analysis of selected results of individual research. The essential part of this study is the presentation and comments to the individual survey conducted in a group of individual investors in Poland.

### FINANCIAL STATEMENT VS. DECISION-MAKING PROCESSES OF INVESTORS

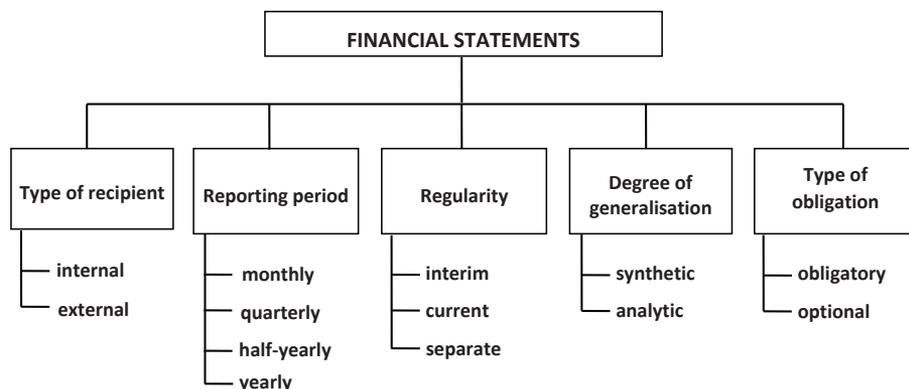
A financial statement is usually considered the primary source of financial information used in economic analyses. In this regard, reporting data are the grounds for many business decisions, which is the reason why entities are widely interested in this type of data (Sierpińska & Jachna, 2004, pp. 47–48).

The term of financial statement refers to a set of data concerning the property and financial position as well as financial results achieved in a specified period of activity of a given unit. Proper data are prepared and presented according to particular accepted rules and formulas of description and presentation (Krzywda, 2003, p. 37).

The basic type of financial statement is a separate financial statement. However, due to the ongoing social and economic transformations, an increase in the scale and complexity of commercial, organisational and capital relations between business entities can be observed. As a result, capital groups emerge and develop, which entails the growth of importance of consolidated financial statements (Ignatowski, 2012, p. 22).

A number of various financial statements can be distinguished, considering e.g. different legal requirements, expectations of recipients, business specificity or purpose of information. Thus, the current catalogue of financial statements contains a relatively wide selection of types. A number of classifications can be distinguished (Wędzki, 2014, p. 17), some of which are presented in diagram 1.

**Diagram 1.** Classification of financial statements based on selected criteria



Source: individual work based on: (Kamiński, 2015, pp. 14–15).

Currently it is accepted that the major purpose of financial statements is to provide information concerning the property and financial position, financial results achieved and cash flows of a business unit, that are useful for a wide group of users in making their business decisions. A set of statement data is presented in an ordered manner, according to an agreed statement structure (Świdarska, 2010, p. 15). In the context of the Polish legal regulations on accounting, financial statements comprise (Accounting Act, Art. 45 paragraph 2):

- balance sheet,
- profit and loss account,
- additional information.

For business entities whose yearly financial statements are subject to mandatory review of a statutory auditor, it is necessary to provide two additional documents (pursuant to Art. 45 paragraph 3 of the Accounting Act):

- cash flow statement,
- statement of changes in equity.

However, according to the international accounting regulations, a complete set of financial statements comprises (IAS 1, Art. 10):

- a statement of financial position as at the end of the period,
- a statement of profit or loss and other comprehensive income for the period,
- a statement of changes in equity for the period,
- a statement of cash flows for the period,
- notes, comprising a summary of significant accounting policies and other explanatory information,
- a statement of financial position with reference to the preceding comparative period<sup>1</sup>.

It must be noted that IAS 1 gives a proposed terminology regarding particular financial statement components, and entities may use other titles (IAS 1, Art. 10).

Financial statements, according to their purpose, are drawn up to meet the informative needs of a wide and diversified group of recipients (Gos, 2006, p. 7). However, in the recent years the focus on investors has become more distinct in financial reporting. It is evidenced by the observed changes in the international accounting regulations, attempting to adjust the purpose and scope of

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<sup>1</sup> In certain situations, an entity shall attach the statement of financial position as at the beginning of the preceding period.

disclosed information to the relevant expectations of investors (Burlaud & Colasse, 2011, p. 32).

### INDIVIDUAL INVESTORS ON FINANCIAL MARKETS

Investors are the major category of participants on the world financial markets. The essential goal of their activity is to achieve economic benefits. Investors are often generally referred to as buyers of financial instruments, intending to resell them to gain profit. Consequently, they constitute a community that is diversified in many aspects (Cichorska, 2015, p. 15). In particular, they differ in terms of the volume of kept resources, investment goals and strategies, degree of knowledge in undertaking and management of investments, as well as the impact on the financial market (Czyżycki, 2016, p. 14). In this regard, various methods of classification of investors are distinguished, based on different criteria. Some of them are presented in table 1.

**Table 1.** Selected classifications of investors on the financial market

Classification criterion	Type of investor
Subject of legal relationship	Natural person
	Legal entity
Form of organisation	Individual
	Institutional
Place of residence / registered office	Domestic
	Foreign
Turnover	Wholesale
	Retail
Knowledge of decision-making techniques	Amateur
	Professional
Eagerness for risk	Conservative
	Moderate
	Aggressive
Attitude to investments	Investing on own account
	Dealer

Source: (Cichorska, 2015, p. 16).

Considering the goal of this study, further considerations will focus on the informative needs of individual investors. The major characteristics of this group of investors is making investment decisions personally. They also act on their own account and not professionally. Mostly these are households and small entities having relatively small capitals. It is pointed out that their basic motive to undertake investments is to protect the held assets against the loss of value in time (Czyżycki, 2016, p. 14).

The investment activity of this group of investors is clearly diversified. A number of factors is identified that may promote the willingness to take decisions, or may restrict it. They include: availability of information on a given market, cost of acquisition of relevant information, properties, investment knowledge and experience, age, gender, personal attributes, socialisation behaviour, capitals owned, level of transaction costs (Yang, 2013, pp. 303–304).

The literature of the subject does not provide a uniform definition individual investor. They are usually defined as natural persons investing their savings in various assets (Dziawgo, 2004). This explanation has been assumed for the purposes of this study and the described research.

### **REVIEW OF SELECTED THIRD-PARTY RESEARCH RESULTS**

In view of the rapid growth of financial markets, the problem of use and usefulness of financial reporting in the decision-making processes of individual investors is an interesting and important subject of study. It is confirmed by the recent attempts to analyse this subject.

The issue of the using of financial reporting by individual investors in Poland was the research subject of M. Adamczyk. In 2011–2012, he carried out a survey on a group of 339 non-professional investors. He determined that approximately 75% of the respondents use financial reporting information in investment decisions. Balance sheet and profit and loss account were the most frequently used components of the financial statements in this group of respondents (Adamczyk, 2017, pp. 9–12).

Another studies in this field was the analysis of usefulness of data included in financial statements in the decision-making processes of individual investors, made by J. Błażyńska. The survey was conducted in a group of 334 respondents in 2013.

The analysis of the results indicates that most of the surveyed found useful information in financial statements (95%), but only a small group claimed that all information was useful (8%). Over a half of survey participants came to a conclusion that most of the data were useful (59%). A large part of surveyed investors indicated that only certain information was useful (28%). The remaining group reported lack of usefulness of this type of data (5%) (Błażyńska, 2015, pp. 219–221).

Other research in the described field was the survey conducted by D. Dziawgo in 2009 and 2010 among 416 individual investors. It comprised an assessment of adaptation of the scope of information provided by companies to the informative needs of the investors. The results lead to a conclusion that only a small group of survey participants (18%) was satisfied with the scope of presented information. Much more frequently the surveyed reported only sufficient adjustment of provided information to their needs (46%). Relatively large percentage of investors indicated poor adjustment of this type of data (28%) (Dziawgo, 2011, pp. 225–227).

### **INDIVIDUAL INVESTORS IN POLAND – PRESENTATION OF AUTHOR'S RESEARCH RESULTS**

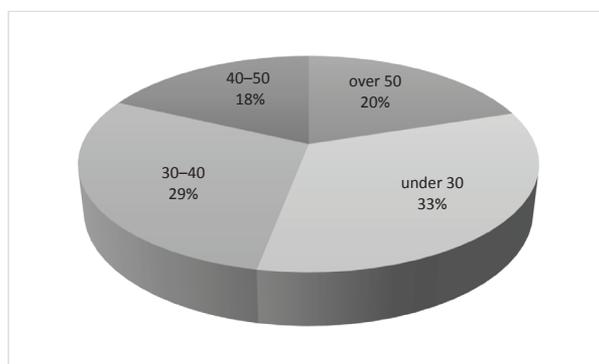
In order to fulfil the goal of this study, selected outcomes of the author's survey on usefulness of the reporting data concerning financial instruments in the opinion of individual investors will be used. The said survey was conducted at the author's request in 2015 by the Polish Association of Individual Investors (Stowarzyszenie Inwestorów Indywidualnych, SII). It encompassed a group of 408 individual investors from Poland. The research tool was an online survey questionnaire published on the website of the Association.

The characteristic of the surveyed group of respondents started with determining their age. Considering the age of the them, there is a noticeable differs. That's why, the following age categories have been distinguished:

- a) under 30,
- b) at least 30, but less than 40,
- c) at least 40, but less than 50,
- d) over 50.

The obtained results are presented in figure 1.

**Figure 1.** Division of the surveyed group of individual investors in terms of age (%)

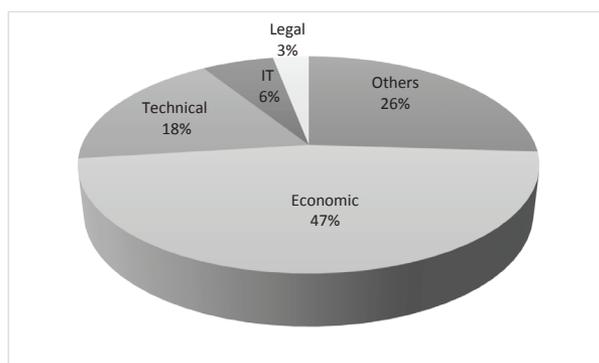


Source: individual study.

The youngest investors, under 30 years of age were the largest group of respondents. Their participation in analysed group was approx. 33%. Respondents from 30 to 40 were the second largest age group. Their portion in this community reaching approx. 29%. Investors over 50 and aged 40 to 50 were the next groups, with the percentage of 20% and 18%, respectively.

The surveyed group of individual investors is also diversified in terms of kind of education. Taking into account this characteristic the following categories have been distinguished: economic, technical, IT, legal and others. The obtained results are presented in figure 2.

**Figure 2.** Division of the surveyed group of individual investors in terms of type of education (%)

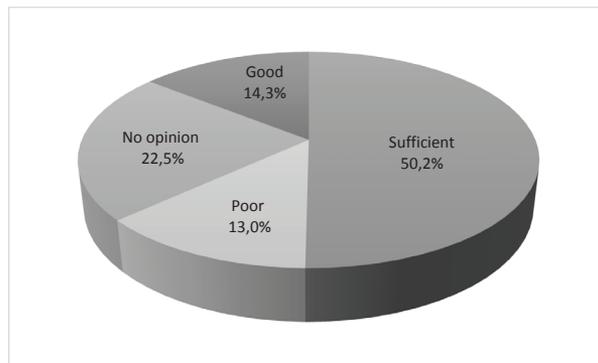


Source: individual study.

The vast majority of respondents have an economic education (47%). The next the directions of education of the surveyed investors were: technical (18%), IT (6%), legal (3%). Moreover, others types of education were indicated relatively often (26%).

The analysis started with a question concerning the usefulness of reporting data regarding financial instruments in the decision-making processes of individual investors. The outcomes are presented in figure 3.

**Figure 3.** Percentage of replies to the question: "What is your opinion on the usefulness of financial reporting data regarding financial instruments in their current form in the context of investment decisions?" (%) – group of individual investors (N=408)

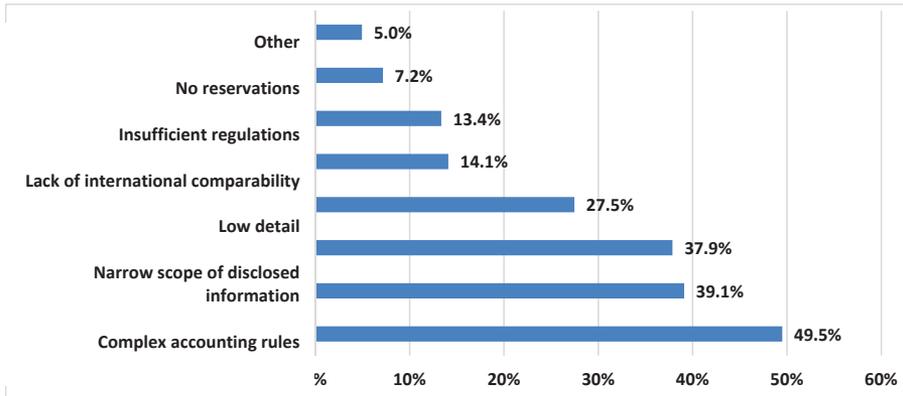


Source: individual study.

The analysis of the results indicates that almost half of the surveyed claimed that the usefulness of the said information was only sufficient (50.2%). Relatively small groups of respondents indicated that the usefulness of these data was good (14.3%) or poor (13.0%). Quite frequently survey participants couldn't provide a clear opinion on this issue (22.5%).

The following stage of the research was an attempt to determine the reasons behind the poor opinion of individual investors on the reporting data regarding financial instruments. On the basis of their answers, a list of comments reported by the survey participants has been prepared. It is presented in figure 4.

**Figure 4.** Percentage of replies to the question: “What factors, in your opinion, decrease the usefulness of information regarding financial instruments presented in financial statements?” (%) – group of individual investors (N=404)



\* In the analysed question respondents could choose more than one answer. The total amount of indications in the analysed field was 782.

Source: individual study.

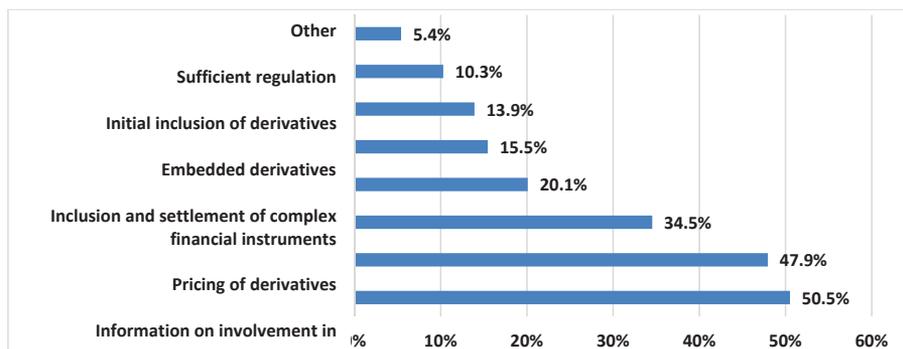
The presented assessment of usefulness of reporting information regarding financial instruments, made by the surveyed investors, caused that a significant group contributed to determining the reasons of the described situation (N=404, 99.0%). The most frequently indicated negative factor was poor transparency of presentation (49.5%). Other most frequent comments concerned:

- complex accounting rules (39.1%),
- narrow scope of disclosed information (37.9%),
- low detail of the data (27.5%).

Survey participants quite frequently indicated the lack of international comparability of this type of information (14.1%) and also insufficient regulation of financial reporting for financial instruments (13.4%). Additionally, it must be pointed out that a small group of respondents referred to causes other than those mentioned in the question (5.0%). These mainly included the concerns of the possibility of data manipulation by entities and delayed disclosure of relevant information.

Another question concerned the areas of accounting for financial instruments that in the opinion of the surveyed individual investors needed particular regulation. The answers given to this question are presented in figure 5.

**Figure 5.** Percentage of replies to the question: "Which areas of financial instruments accounting need particular regulations?" (%) – group of individual investors (N=388)



\* In the analysed question respondents could choose more than one answer. The total amount of indications in the analysed field was 769.

Source: individual study.

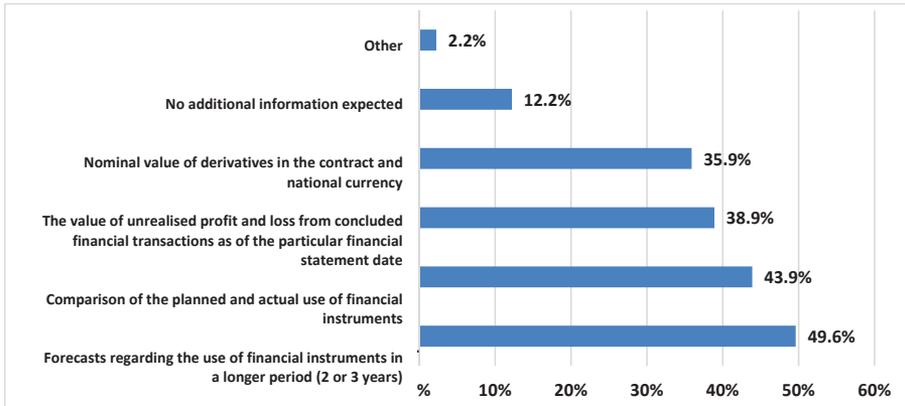
The analysis of the results leads to a conclusion that survey participants mainly identified problems concerning the exposure to the risk related with financial instruments (50.5%) and the presentation of information regarding the involvement in derivatives (47.9%). Another area that required changes in the opinion of some respondents, was pricing of derivatives (34.5%). Additionally, the answers quite often indicated the need to formulate particular rules regarding:

- the inclusion and settlement of complex derivatives (20.1%),
- embedded derivatives (15.5%),
- initial inclusion of derivatives (13.9%).

The respondents also mentioned other issues, not included in the answers (5.1%). These included: sensitivity of financial instruments pricing to the changes of market factors, pricing based on fair value, effect of government decisions. A small group of surveyed investors claimed that the valid regulations on financial instruments accounting were sufficient (10.3%).

Another area of analysis were the expectations of the investors regarding disclosure of additional information concerning financial instruments. Many of the surveyed individual investors mentioned the necessity to provide such information. The outcomes are presented in figure 6.

**Figure 6.** Percentage of replies to the question: "What additional information concerning financial instruments should be disclosed by the companies?" (%) – group of individual investors (N=401)



\* In the analysed question respondents could choose more than one answer. The total amount of indications in the analysed field was 733.

Source: individual study.

The data presented in the diagram above indicate that the expectations concerning the disclosure of forecasts regarding the use of financial instruments in a longer period (2 or 3 years) were the most frequent response of the survey participants (49.6%). A relatively large group of respondents mentioned the need to provide comparisons of the planned and actual use of financial instruments (43.9%). Another expectations of the surveyed investors concerned the disclosure of:

- a) the value of unrealised profit and loss from concluded financial transactions as of the particular financial statement date (38.9%),
- b) nominal value of derivatives in the contract and national currency (35.9%).

The majority of the answers referred to the disclosure of these types of information. A few participants mentioned other expectations (2.2%). Nonetheless, a group of respondents claimed that no additional reporting information regarding financial instruments were required (12.2%).

## ■■■ CONCLUSIONS

The analysis of the results of the survey concerning the usefulness of reporting data regarding financial instruments in the decision-making processes of individual investors leads to a number of conclusions.

In general, most of the survey participants claimed that the usefulness of the analysed information was merely sufficient (50.2%). Quite often respondents could not provide a clear assessment (22.5%).

A large group of the surveyed investors had reservations concerning the information presented in this scope. The major factors decreasing the usefulness of data concerning financial instruments included:

- poor transparency of presentation (49.5%),
- complex accounting rules (39.1%),
- narrow scope of disclosed information (37.9%).

It has also been determined that the surveyed investors emphasised the necessity to introduce changes in accounting for financial instruments. In particular, their comments concerned the following issues:

- exposure to risk related with financial instruments (50.5%),
- presentation of information regarding the involvement in derivatives (47.9%),
- pricing of derivatives (34.5%).

Additionally, a number of the surveyed investors presented their expectations concerning the disclosure of additional information regarding financial instruments. Most frequently they claimed that companies should provide:

- forecasts on using financial instruments in a longer period (2 or 3 years) (49.6%),
- comparisons of planned and actual use of financial instruments (43.9%),
- the data concerning the value of unrealised profit and loss from concluded financial transactions as of the particular financial statement date (38.9%).

That said, it can be noticed that financial reporting, being the primary source of information for investors, is also quite often used to provide data regarding financial instruments. The scale and complexity of rules concerning the accounting for financial instruments causes that reporting information presented in this scope is characterised by a highly complicated form. Consequently, it is difficult to use for investors, which is evidenced by the outcomes of the con-

ducted survey. These results confirm the necessity to introduce a number of modifications in this field, allowing to adjust the rules of financial reporting for financial instruments to the informative needs of individual investors.

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