ISSN: 2688-9323

Annual Report Inquiry Letter Supervision and Financing Constraints Literature Review

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Abstract

As a non-penalty supervision method, the stock exchange inquiry letter can discover the company's problems and improve the quality of information disclosure of listed companies. At the same time, listed companies were publicly inquired by the exchange to send a risk warning signal to the capital market. Based on the relevant domestic and foreign literature, this paper sorts out the theoretical research related to the annual report inquiry letter supervision and financing constraints, and reviews the research status, and further combines the domestic and foreign research results to look forward to the future research direction.

Keywords

Inquiry Letter Supervision; Financing Constraints; Information Disclosure.

1. Research Status of Annual Report Inquiry and Supervision

The exchange's inquiry letter supervision mainly focuses on matters that may cause major risks to the company. It issues related inquiry letters to listed companies and requires the company to respond within a specified time. Some inquiry letters require professional third-party organizations to provide opinions. If there are still problems with the company's reply letter, the exchange will conduct multiple inquiries until the company's information disclosure problem is resolved. As one of the important means of non-punitive supervision (Chen Yunsen et al., 2018) [1], the annual report inquiry letter of the exchange has attracted the attention of academia. The current research on the annual report inquiry letter mainly focuses on its influencing factors and economic consequences.

1.1. Influencing Factors

Which companies are more likely to receive the annual report inquiry letter? M&A and restructuring transactions with a high degree of information asymmetry and poor report information disclosure are more likely to receive an inquiry letter (Li Xiaoxi et al., 2019) [2]. Liu Bai and Lu Jiarui (2019) [3] found that the higher the degree of accrued earnings management of a company, the greater the probability of receiving an inquiry letter. Cassell et al. (2013) [4] found that companies with poor profitability, high business complexity, hiring small-scale auditing companies, and weak corporate governance are more likely to receive annual report inquiries. In addition, according to the regulatory capture hypothesis, if companies face securities enforcement by regulatory agencies due to violations of regulations, politically-related companies will entrust government officials representing their interests to "plead" with regulatory agencies to obtain "leniency." , Thereby reducing the possibility of securities enforcement by regulatory agencies. However, inconsistent with the regulatory capture hypothesis is that political connections will increase the likelihood of companies receiving annual report inquiry letters (Yu Minggui and Bian Shihui, 2020) [5].

ISSN: 2688-9323

1.2. Economic Consequences

The economic consequences of the issuance of the inquiry letter. First of all, what market perception do investors have on the annual report inquiry letter? Johnston and Petacchi research found that the annual report inquiry letter can help reduce the risk of the company's stock buying and selling spreads. The market response of the annual report inquiry letter was significantly negative (Guo Fei and Zhou Yongtong, 2018) [6], the annual report inquiry letter will reduce the performance forecast deviation of the receiving company (Xia Yidan and Chen Jieyu, 2020) [7] , With the ability to suppress earnings management (Chen Yunsen et al., 2019) [8], improve audit quality (Chen Yunsen et al., 2018) [1], improve the quality of performance forecasts (Li Xiaoxi et al., 2019) [2] and prevent the risk of stock price collapse (Zhang Junsheng et al. , 2018) [9] and other governance functions. The annual report inquiry letter can increase the company's earnings response coefficient (Johnston and Petacchi, 2017)[10], indicating that the annual report inquiry letter has improved the company's financing reporting environment and has received positive market responses from investors. It can be seen that the annual report inquiry letter supplements the disclosure of key information in the annual report to investors, enhances investors' ability to interpret the company's annual report information, and helps information users make investment decisions (Zhao Libin and Fu Xiangfei, etc., 2020) [11]. Second, the annual report inquiry letter has a "spillover effect" on the information disclosure of companies in the same industry. Brown et al. used mandatory annual report risk information disclosure as an experimental environment. The study found that when companies in the same industry receive annual report inquiry letters related to risk information disclosure, other companies in the same industry will improve the level of risk information disclosure in their annual reports in the next fiscal year. Finally, the annual report inquiry letter helps to alleviate the degree of information asymmetry between the company's management and investors.

2. Status of Research on Financing Constraints

There are many influencing factors of financial constraints. Domestic scholars have studied the influencing factors of corporate financing constraints relatively late, but they are roughly the same as the conclusions reached by foreign scholars. The influencing factors of financial constraints are mainly divided into macro factors and micro factors.

Macro factors include external financial development and institutional environment. In terms of financial development, improving the development level of external financial intermediaries and financial markets will effectively alleviate corporate financial constraints (Zhang Fan, 2015) [12]. Wang Fengrong and Mu Qingyu (2019) [13] found that the development of small and medium banks has eased the financing constraints of small and medium enterprises, which is regulated by the heterogeneity of government intervention. In addition, some scholars have found that the development of shadow banking and the Internet can also help alleviate the financing constraints of SMEs (Li Quan et al., 2018) [14]. In terms of the institutional environment, the "inter-enterprise relationship" has a more significant effect on alleviating financing constraints than the "government-enterprise relationship". So far, scholars have paid attention to what role the informal system plays in the survival and development of Chinese enterprises and how to play a role. Especially in the context of the imperfect development of China's financial market, companies generally face financing constraints, and corporate relationship transactions are common, in-depth analysis of the strength of the company's relationship with suppliers based on supply chain connections, and the debt financing and financing constraints on companies Whether there is a significant impact and a specific impact mechanism can further provide theoretical basis and practical guidance for alleviating the financing constraints of SMEs.

Micro-factors include information disclosure, accounting conservatism, agency costs, internal control, etc. The micro level is mainly explained from the perspective of information asymmetry between the enterprise and the outside world. Information asymmetry is the internal cause that affects corporate financing constraints, and the quality of information disclosure is the key to alleviating corporate financing constraints. Effective and reliable accounting information can significantly reduce the level of financing constraints. At the same time, companies with good investment opportunities hope to be understood by investors. They will obtain a large number of investors by providing high-quality accounting information, thereby reducing the degree of financing constraints of the company. The degree of information asymmetry between different investors will decrease with the improvement of the quality of accounting information, so the financing cost caused by adverse selection will also decrease; at the same time, the improvement of the quality of accounting information can reduce the information gap between managers and shareholders. The occurrence of symmetrical situation enables the fund provider to understand the company's operation and capital status, and the financing cost brought by the risk premium will also be reduced as a result. There is a significant negative correlation between accounting conservatism and financial constraints. The average age of executives can promote the relationship between them, while the proportion of male executives has a negative moderating effect. Management ability has a moderating effect on the relationship between the company's internal control and financing constraints, that is, companies with higher management capabilities, internal control can more ease the degree of financing constraints (Li Li and Zhang Di, 2019) [15].

3. Research on the Impact of Annual Report Inquiry Letter Supervision on Financing Constraints

Under the guidance of "innovating regulatory methods and improving regulatory mechanisms," government agencies, in addition to compulsory legislative supervision, also clearly emphasized that self-regulatory organizations should strengthen their review of the capital market in order to realize the self-discipline and self-management of listed companies. Existing studies have mainly focused on the impact of regulatory penalties on corporate financing. After a listed company is penalized for violations, the value of its claims will change. The bad news released by the Securities Regulatory Commission's penalty announcement will increase the information cost of banks and the risk of default, forcing the bank's debt financing capacity of violating companies to significantly decline. Zhu Peihua (2020) [16] researched from the perspective of reputation and found that the penalties imposed by regulatory agencies damage the company's reputation and significantly reduce the company's financial scale. However, there are few studies on the impact of self-regulatory measures on financing behavior. Sun Xuejiao et al. (2019) [17] took the self-regulatory measure of tax credit rating as the research object and found that tax credit rating can reduce information asymmetry and improve corporate reputation. To affect the company’s financing status. After the disclosure of the tax credit rating results, the level of financing constraints and the cost of credit capital for high-rated companies have been significantly reduced.

Under the inquiry letter system, the quality and timeliness of corporate information disclosure has been greatly improved, which has largely regulated the information disclosure of listed companies. Investors can obtain the content of the inquiry letter through formal channels such as the official media of the exchange to reduce the impact of information asymmetry. Investors will use the information released in the inquiry letter and its response letter to make choices when making stock buying and selling decisions to reduce the drawbacks of collecting information through abnormal channels, which will help guide investors to develop from shortterm speculative thinking to long-term investment philosophy. The capital market brings a new atmosphere.

The inquiry letter system has a negative penalty effect. After the company's letter of receipt announcement was disclosed, this negative incident sent bad news to the market, prompting investors to have the motivation and space to dig out more negative information generated during the company's operations. Damage the company's reputation. The SFC inquiry letter announcement has a risk warning effect. The receipt of inquiry letters by listed companies often means that the company has improper disclosure or financial statement defects. Investors speculate that the listed company may operate or hide "bad news" to reduce the impact on the company's finances. The reliance of the report and the expectation that the uncertainty of the company's future development will increase and the stock volatility will increase, requiring the company to increase financial costs as a risk compensation, which will further worsen the company's financial constraints.

4. Literature Review and Future Prospects

The research results of the existing literature show that the stock exchange inquiry letter has a better identification effect, can find the risks in mergers and acquisitions and reorganization, and can also find problems in the aspects of earnings management, financial violations, and internal control. The type, content, characteristics of the inquiry letter and the company's internal and external environment will all have an impact on the market response of the incident. The company's market response when receiving the inquiry letter and responding to the inquiry letter is not necessarily the same, but existing studies have shown that The inquiry letter can cause the company's stock price to fluctuate. Some scholars have conducted research on the relationship between the inquiry letter and the audit, and found that the behavior of auditors is also affected by the inquiry letter. In addition, the inquiry letter also has an impact on the company's performance forecast, earnings management, executive replacement, etc., and it is also inextricably linked to the company's financing.

The stock exchange inquiry letter has been proved to be a good regulatory measure, which can not only identify and discover the problems of listed companies, but also affect the listed companies and prompt them to improve information transparency. Judging from the existing research results, the research objects are mostly concentrated on financial report inquiries, and there is also a small amount of literature on restructuring inquiries, but the inquiries involving other content have not been studied in depth. Inquiry letters are part of the non-punitive regulatory measures of the stock exchange. The Shenzhen Stock Exchange also has letters of concern and other types of letters, which are rarely studied by scholars. Therefore, this subject has a larger research space in the future.

Acknowledgments

This work was financially supported by Anhui University of Finance and Economics and Tongling College jointly cultivate scientific research and innovation fund (2020tlxylhy2).

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