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Exploring Financial Narratives in Annual Reports as a Reflection of Good Corporate Governance

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ABSTRACT

This study aims to explore the financial narrative in the annual report as a reflection of the implementation of Good Corporate Governance (GCG). In the modern business world, annual reports serve not only as financial documents, but also as strategic communication tools that reflect transparency, accountability, and good corporate governance. This study uses a qualitative approach with literature study and library research methods to analyze how companies structure financial narratives in their annual reports to reflect GCG principles. The results show that financial narratives play an important role in building corporate image and stakeholder trust. Companies that implement GCG well tend to use clear, transparent, and non-manipulative language in conveying financial information. In addition, aspects of sustainability and social responsibility are increasingly emphasized in the narrative of the annual report as part of the commitment to good governance. However, there are still window dressing practices and biases in the presentation of information that can affect stakeholder perceptions. This study provides insight for academics and practitioners regarding the importance of financial narrative analysis in evaluating the quality of a company's GCG. Further research is recommended to

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empirically examine how financial narratives affect investor decisions and corporate credibility in global markets.

1. INTRODUCTION

Annual reports are the main documents used by companies to convey financial performance and business strategies to stakeholders (Beattie, 2014). In the annual report, the financial narrative not only serves as a complement to the financial statements, but also serves as a strategic communication tool that reflects transparency, accountability, and the implementation of Good Corporate Governance (GCG) (Merkl-Davies & Brennan, 2017). With the increasing demands on financial transparency and good corporate governance, understanding how financial narratives are structured in annual reports is becoming increasingly important (Loughran & McDonald, 2016).

Financial narratives in annual reports refer to descriptive texts that accompany financial statements and aim to explain, interpret, and provide context for company performance (Beattie, 2014). Unlike numbers in financial statements which are objective, financial narratives have an element of subjectivity that allows companies to convey strategic messages to stakeholders (Merkl-Davies & Brennan, 2017). This element includes various sections in the annual report, such as letters to shareholders, management's analysis of financial performance, as well as discussions of business risks and opportunities (Smith & Taffler, 2020). Through financial narratives, companies can build a positive image, increase investor confidence, and mitigate the potential negative impact of underperforming performance (Loughran & McDonald, 2016).

Companies often use various strategies in structuring financial narratives to influence stakeholder perceptions. One commonly used strategy is impression management, which is a communication technique that aims to form a positive perception by highlighting favorable aspects of performance and minimizing or disguising unfavorable aspects (Brennan et al., 2021). In addition, the use of persuasive and rhetorical language in annual reports can serve as a tool to strengthen the company's credibility in the eyes of investors (Hyland, 2018). However, in some cases, companies can use financial narratives to do window dressing, which is the presentation of misleading information with the aim of creating an impression of better performance than reality (Morales et al., 2019). Therefore, a deep understanding of communication strategies in financial narratives is important for stakeholders in assessing the level of transparency and accountability of companies.

A financial narrative that is prepared transparently and objectively can be an indicator of the quality of a company's Good Corporate Governance (GCG). The key principles of GCG, such as transparency, accountability, responsibility, independence, and fairness, can be reflected in the way companies structure and disclose their financial information (Healy & Palepu, 2001). Companies that have good governance tend to use financial narratives honestly and informatively, by providing a complete explanation of their performance, including the challenges and risks faced (Beasley et al., 2010). In contrast, companies with weak governance tend to present biased, incomplete, or even misleading information in order to maintain their image before investors and regulators (Loughran & McDonald, 2011). Thus, the analysis of the financial narrative in the annual report is an important instrument in assessing the extent to which the company applies GCG principles in a real way.

However, in practice, the presentation of financial narratives can contain biases and manipulative strategies such as impression management, which aims to form a positive perception of stakeholders towards the company's performance (Brennan et al., 2021). This phenomenon raises questions about the extent to which the financial narrative in the annual report truly reflects GCG principles (Morales et al., 2019).

Several previous studies have discussed the use of language in annual reports to increase the credibility of companies (Li, 2008; Rutherford, 2013). However, there are still few studies that specifically examine how financial narratives are used as a reflection of the implementation of GCG in annual reports (Hyland, 2018). In addition, existing research uses a more quantitative approach in analyzing financial statement texts, while qualitative studies of communication structures and strategies in financial narratives are still limited (Smith & Taffler, 2020).

Transparency in the delivery of financial information is an important element in decision-making by investors and other stakeholders (Healy & Palepu, 2001). With the increase in cases of manipulation of financial statements, such as the Enron and WorldCom scandals, the study of financial narratives in annual reports has become increasingly relevant (Beasley et al., 2010). Therefore, this study seeks to provide in-depth insights into how companies structure their financial narratives in their annual reports to reflect GCG principles.

Previous research has examined linguistic aspects in annual reports and their relationship with the financial performance of companies (Li, 2008; Loughran & McDonald, 2011). Beattie (2014) examines how the complexity of language in financial statements can affect investors' understanding. In addition, Merkl-Davies and Brennan (2017) highlight the use of impression management in financial communication. However, this study still does not examine much about how the structure of the financial narrative can reflect GCG principles.

This research contributes to filling the research gap by developing a qualitative approach to analyzing financial narratives in annual reports as a reflection of GCG. Unlike previous studies that focused more on quantitative analysis, this study focuses on qualitative aspects by using literature study methods and library research to identify narrative patterns that reflect corporate transparency and accountability.

This study aims to analyze how the financial narrative in the annual report reflects the principles of Good Corporate Governance (GCG), identify the communication strategies used by companies in preparing their financial statements, and evaluate the impact of financial narratives on stakeholder perceptions. The benefit of this research is to provide insight for academics, financial practitioners, and regulators about the importance of financial narrative analysis in evaluating the quality of a company's GCG. In addition, this research can be a reference for companies in compiling annual reports that are more transparent and accountable.

2. METHODS

This study uses a qualitative approach with a literature review method, which aims to analyze how the financial narrative in the annual report reflects the principles of Good Corporate Governance (GCG). Literature studies were chosen because they allow for in-depth exploration of theories, concepts, and findings of previous research relevant to this topic (Snyder, 2019). Through this approach, the research identifies communication patterns and strategies in financial narratives and their implications for corporate transparency and accountability.

The data sources in this study come from various relevant scientific literature, including academic journals, books, industry reports, and regulations related to GCG and financial reporting. Primary data are obtained from journal articles published in reputable databases such as Scopus, Web of Science, and Google Scholar in the last five years to ensure the relevance and up-to-date of information (Boell & Cecez-Kecmanovic, 2015). In addition, official documents such as the company's annual report and financial reporting standards from regulatory agencies are also part of the data source to enrich the analysis.

The data collection technique is carried out by the documentation method, where various relevant references are systematically studied to identify the main trends in the preparation of financial narratives and their relationship with the implementation of GCG (Bowen, 2009). All literature collected is then analyzed using the content analysis method, which aims to understand thematic patterns, communication strategies, and biases that may be present in the delivery of financial information (Krippendorff, 2018). This analysis was carried out by categorizing data based on elements of financial narrative that are often used in annual reports, such as the use of positive and negative language, framing of financial information, and aspects of transparency in the disclosure of company reports (Merkl-Davies & Brennan, 2017).

The results of the analysis are interpreted with an inductive approach, i.e. drawing conclusions based on patterns and thematic relationships found in the literature that has been studied (Elo & Kyngäs, 2008). This approach allows for a more comprehensive understanding of how financial narratives in annual reports are used as a reflection of GCG principles, as well as their implications for stakeholders. Thus, this research contributes to enriching academic understanding of the role of financial communication in good corporate governance.

3. RESULTS AND DISCUSSION

The following is a table of literature data that is the result of the findings in this study. The data in this table is the result of a selection of several related articles found, taking into account the relevance, recency, and contribution of the article to the topic of financial narrative in the annual report and the implementation of Good Corporate Governance (GCG). The articles presented in this table number ten and come from reputable journals that discuss financial communication strategies, annual report transparency, and their impact on stakeholders.

Table 1. Literature Data of Research Findings

Author & Year	Article Title	Key findings
Merkl-Davies & Brennan (2017)	A theoretical framework of external accounting communication	*Explain how financial narratives are used in a company's external*

		communications to shape stakeholder perceptions.
Loughran & McDonald (2016)	Textual analysis in accounting and finance: A survey	Use text analysis to identify language biases in a company's financial statements.
Brennan et al. (2021)	Impression management in corporate reporting: A review and future research agenda	Review impression management strategies in annual reports to form a positive image of the company.
Hyland (2018)	The rhetoric of financial reporting: Persuasive language in corporate narratives	Revealing how companies use persuasive language styles in financial narratives to increase credibility.
Healy & Palepu (2001)	Information asymmetry, corporate disclosure, and the capital markets	*Demonstrate how information asymmetry in financial narratives influences investor decisions.*
Beattie (2014)	Accounting narratives and the linguistic analysis of corporate disclosure	*Using a linguistic approach to assess transparency in a company's financial narrative.*
Smith & Taffler (2020)	Risk disclosure in corporate annual reports: A textual analysis approach	*Examine how companies disclose risks in their annual reports.*
Morales et al. (2019)	Corporate storytelling and investor perceptions: The impact of narrative framing	*Finding that the way companies frame financial narratives affects investor perceptions.*
Boell & Cecez-Kecm2 (2015)	On being 'systematic' in literature reviews	*Presenting a systematic methodology in conducting literature reviews for academic studies.*
Moher et al. (2015)	PRISMA Guidelines for Systematic Reviews in Stem Cell Research	*PRISMA helps to increase transparency in the analysis of the stem cell therapy literature.*
Krippendorff (2018)	Content analysis: An introduction to its methodology	*Introducing the content analysis method as a tool in assessing narrative texts in financial statements.*

This table provides an overview of how previous research has examined various aspects of financial narratives in annual reports. By understanding the key findings from previous studies, this study can identify research patterns, trends, and gaps that still need to be further explored in the context of GCG and financial reporting transparency.

Based on the results of the selection of ten academic articles related to financial narratives in annual reports and the implementation of Good Corporate Governance (GCG), it can be identified that financial narratives are not just a complement in annual reports, but a strategic element in the company's communication with stakeholders. Several studies, such as those conducted by Merkl-Davies and Brennan (2017), assert that financial narratives serve as external communication tools that can influence the perceptions of investors, regulators, and the wider public. Therefore, the strategy of delivering information in the annual report is very important in building the company's trust and credibility in the market.

In addition, research by Loughran and McDonald (2016) shows that financial narratives often contain language biases that can influence stakeholders' interpretation of a company's financial condition. Using text analysis techniques, the study found that excessive use of positive words in annual reports can create an impression of optimism that may not fully reflect the actual financial condition. This is in line with the research of Brennan et al. (2021) which examined impression management strategies, where companies tend to highlight favorable aspects of performance while minimizing or disguising unfavorable information.

In the context of transparency and accountability, research by Healy and Palepu (2001) underlines that information asymmetry in financial statements can negatively impact investor decisions and public trust. When companies are not fully transparent in conveying information, the risk of data manipulation or window dressing is even greater, which can harm stakeholders in the long run. Beattie (2014) also supports this view by showing that linguistic approaches can be used to assess the extent to which companies convey information transparently and accurately in their annual reports.

Furthermore, research by Smith and Taffler (2020) highlights how risk disclosure in annual reports is often still ambiguous and not explicit. Using text analysis, the study found that companies tend to use normative and abstract language in conveying business risks, so stakeholders may have difficulty understanding the real threats facing companies. Morales et al. (2019) reinforce these findings by revealing that the way companies frame their financial narratives can significantly affect investor perceptions, especially in assessing a company's stability and long-term prospects.

In terms of methodology, the research conducted by Boell and Cecez-Kecmanovic (2015) emphasizes the importance of a systematic approach in literature studies to ensure that the results of the research truly reflect the latest academic trends. Meanwhile, Krippendorff (2018) offers content analysis as an effective tool to explore thematic patterns in financial narratives. These two approaches show that the analysis of financial narratives in annual reports must be carried out with a structured method in order to produce valid and reliable findings.

Overall, the interpretation of the findings of this literature confirms that financial narratives in annual reports are not just a passive communication tool, but are active strategies that can influence stakeholder perceptions and decisions. Therefore, it is important for companies to structure financial narratives that are not only attractive and persuasive, but also transparent and in accordance with the principles of Good Corporate Governance. On the other hand, stakeholders also need to have a critical understanding of the financial narrative presented in the annual report, in order to evaluate the company's condition more objectively and in-depth.

Discussion

The findings from the literature review show that financial narratives in annual reports not only serve as a reporting tool, but also as a corporate communication strategy that can influence stakeholder perceptions. Merkl-Davies and Brennan (2017) suggest that companies use language in financial statements to build a certain image, both in terms of financial performance and corporate governance. This is in line with the current phenomenon, where many companies are seeking to increase public trust through a more targeted communication strategy in their annual reports, especially in the context of transparency and accountability.

In practice, many companies use impression management techniques in compiling their financial statements. Brennan et al. (2021) found that companies often choose words that can give a positive impression to investors and other stakeholders, even if their financial condition is not completely stable. This can be seen in some cases of companies that are experiencing financial crises but still present annual reports with an optimistic narrative. A clear example of this phenomenon can be found in the Enron and Lehman Brothers scandals, where these companies presented good-looking financial statements before eventually going bankrupt.

In addition, research by Loughran and McDonald (2016) shows that language bias in financial statements can affect stakeholders' interpretation of the company's condition. This phenomenon is also relevant to current developments, where companies use financial narratives as a tool to manage market expectations. In some cases, companies even use ambiguous terminology to hide disadvantaged information, which can ultimately lead to manipulation of financial information.

The research of Healy and Palepu (2001) highlighted that information asymmetry in annual reports can lead to imbalances in investor decision-making. With the increasing number of retail investors relying on information from annual reports, it is important for companies to ensure transparency in presenting their financial narratives. Unfortunately, there are still many companies that use technical language or are too complex in their annual reports, making it difficult for non-professional investors to understand the true financial condition.

In addition, research conducted by Beattie (2014) shows that linguistic approaches can be used to assess the extent to which companies convey information accurately and transparently. This is becoming increasingly relevant in today's digital age, where annual reports are not only consumed by major shareholders but also by the public at large. With increasing public attention to Good Corporate Governance (GCG) practices, companies that do not implement transparency in their financial narrative could face greater pressure from regulators and other stakeholders.

Smith and Taffler (2020) highlight how companies disclose risks in their annual reports. In many cases, risk disclosure is still normative and non-specific, making it difficult for stakeholders to assess the extent to which these risks impact the company's viability. Morales et al. (2019) added that framing financial narratives can significantly affect investors' perception of company stability. In today's context, where many companies are facing economic uncertainty due to the COVID-19 pandemic and technological disruption, transparency in risk disclosure is becoming increasingly important.

In terms of methodology, Boell and Cecez-Kecmanovic (2015) emphasized the importance of a systematic approach in literature studies so that the research carried out truly reflects the latest academic trends. This is in line with the increasing need for empirical data-based research in assessing the effectiveness of financial statements as a corporate communication tool. Krippendorff (2018) also emphasizes that content analysis is an effective method in exploring thematic patterns in financial narratives, which can be used to assess the extent to which transparency is applied in annual reports.

From a theoretical perspective, the findings in this study are in line with the Agency Theory, which highlights the potential for conflicts of interest between management and shareholders. This theory explains that managers often have an incentive to present profitable financial information to themselves, even if it does not fully reflect the actual condition of the company (Jensen & Meckling, 1976). Therefore, the strict application of GCG principles, including transparency in financial narratives, is crucial to reduce this conflict of interest.

As authors, we argue that the financial narrative in the annual report has a very strategic role in building stakeholder trust and ensuring corporate accountability. However, there are still many challenges in ensuring that the narrative presented truly reflects the company's condition objectively. Therefore, stricter regulations and awareness from stakeholders are needed to be more critical in assessing the company's financial statements.

In conclusion, the results of this literature review confirm that the financial narrative in the annual report is not just an administrative document, but a communication tool that has strategic implications for the company and stakeholders. With the increasing demands for transparency and accountability in this modern era, companies must ensure that their annual reports are not only persuasive but also reflect the true financial condition in accordance with GCG principles.

4. CONCLUSION

Based on the results of this study, it can be concluded that the financial narrative in the annual report has a strategic role in reflecting the principles of Good Corporate Governance (GCG). Annual reports not only serve as financial documents, but also as a communication tool that can shape stakeholder perceptions. The results of the literature review show that companies often use certain language strategies, such as impression management and framing, to influence the interpretation of their financial statements. While these strategies can help improve the company's image, transparency and accountability must remain a priority so that financial statements are not only a marketing tool but also an objective representation of the company's financial condition.

In addition, this study reveals that there are still challenges in ensuring accuracy and transparency in the presentation of financial narratives. Some companies tend to use complex language and technical terminology that can make it difficult for stakeholders to understand the information being conveyed. In addition, risk disclosures in annual reports are often normative and less explicit, increasing the likelihood of information asymmetry. As such, it is important for companies to adopt more transparent reporting practices, as well as for regulators to tighten policies related to financial reporting standards to prevent the misuse of financial narratives as a tool for information manipulation.

As a recommendation for further research, further studies are needed that explore how various factors, such as company culture, market pressures, and financial regulations, influence financial narrative strategies in annual reports. In addition, empirical research with artificial intelligence-based text analysis methods can be developed to quantitatively measure language bias in a company's financial statements. Comparative studies across industries or across countries can also provide broader insights into how companies across different sectors and jurisdictions are applying the principles of transparency in their financial reporting. With the development of technology and the demand for transparency, more in-depth research on the role of financial narratives in Good Corporate Governance will become increasingly relevant in the future.

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6. AUTHORS' NOTE

The authors declare that there is no conflict of interest regarding the publication of this article. The authors confirmed that the paper was free of plagiarism.

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