Influential factors in the trust relationships existing between financial analysts and corporate managers in Iran

Mehdi ArabSalehi Nasrabadi
University of Wollongong
NOTE

This online version of the thesis may have different page formatting and pagination from the paper copy held in the University of Wollongong Library.

UNIVERSITY OF WOLLONGONG

COPYRIGHT WARNING

You may print or download ONE copy of this document for the purpose of your own research or study. The University does not authorise you to copy, communicate or otherwise make available electronically to any other person any copyright material contained on this site. You are reminded of the following:

Copyright owners are entitled to take legal action against persons who infringe their copyright. A reproduction of material that is protected by copyright may be a copyright infringement. A court may impose penalties and award damages in relation to offences and infringements relating to copyright material. Higher penalties may apply, and higher damages may be awarded, for offences and infringements involving the conversion of material into digital or electronic form.
Influential Factors in the Trust Relationships Existing Between Financial Analysts and Corporate Managers in Iran

A Thesis Submitted in Fulfillment of the Requirements for the Award of the Degree

Doctor of Philosophy

From

University of Wollongong

By

Mehdi ArabSalehi Nasrabadi

School of Accounting and Finance

July 2006
Dedicated to my wife, Badrossadat Amiri, without whose encouragement and support this thesis might never have seen the light of day.
I, Mehdi ArabSalehi, declare that this thesis, submitted in fulfilment of the requirement for the award of Doctor of philosophy, in the Department of Accounting and Finance, University of Wollongong, is wholly my own work unless otherwise referenced or acknowledged. The document has not been submitted for qualifications at any other academic institution.

Mehdi ArabSalehi
TABLE OF CONTENTS

TABLE OF CONTENTS .................................................................................. I

APPENDICES ............................................................................................. VII

LIST OF TABLES ....................................................................................... VII

LIST OF FIGURES ..................................................................................... VII

ACKNOWLEDGMENT ............................................................................... IX

ABSTRACT ................................................................................................. XI

CHAPTER 1. INTRODUCTION ................................................................... 1

1.1. Background .......................................................................................... 1
1.2. Delegated Choice Situations and Trust in Business Relationships ... 3
1.3. The Research Question ........................................................................ 7
1.4. Motivation of This Study ..................................................................... 8
1.5. Trust and Business Relations ............................................................. 9
1.6. Review of Trust Models ..................................................................... 12
1.7. Foundations of Trust Theory in Practice ........................................... 16
1.8. Main Components of the Modified Trust Model ....................... 18
   1.8.1. Trust ............................................................................................... 18
   1.8.2. Antecedent Factors to Trust ......................................................... 19
1.9. Corporate Governance in Iran .......................................................... 21
1.10. Iranian Financial Analysts ................................................................. 25
1.11. Rules and Regulations in the Iranian Business Relationship ...... 26
1.12. Islamic Principles and Business Relationship ............................. 28
1.13. The Relationship Between the Factors in the Iranian Context and
     Trust Theory ....................................................................................... 29
3.3.1. Definition and Types of Companies ................................................. 75
3.3.2. Shareholders ...................................................................................... 76
3.3.3. Shareholder Meetings ........................................................................ 76
3.3.4. The Board of Directors ..................................................................... 78
3.3.5. Statutory Inspectors (Auditors) ........................................................... 79
3.4. Tehran Stock Exchange Rules and Regulations ............................... 80
3.4.1. Quick Disclosure of Information ...................................................... 82
3.5. The History of Modern Accounting and the Auditing Profession in Iran ................................................................................................... 83
3.6. Privatisation in Iran ............................................................................ 84
3.7. Business in Islam ................................................................................... 89
3.8. A Brief Review on Some Islamic Principles and Beliefs ................. 91
3.8.1. Ownership in Islam .......................................................................... 93
3.8.2. Life as a Test ..................................................................................... 94
3.8.3. Justice as a Principle of Islam ........................................................... 96
3.8.4. The Islamic Rule of “LaZarar Wa La zirar” (No Harm to Self or Others) ............................................................................................... 96
3.9. The Role of the Islamic Government ............................................... 97
3.9.1. The Relationship between Islamic Traditions and the Trust Theory 98
3.10. Summary............................................................................................ 101

CHAPTER 4. THEORETICAL FRAMEWORK- TRUST THEORY ....
..................................................................................................................... 102
4.1. Introduction .......................................................................................... 102
4.2. Trust as a Relationship ........................................................................ 104
4.3. Risk as an Essential Element in Trust Relationship ...................... 106
4.4. A Review on Different Perspectives on Trust ................................. 107
4.5. A Conceptual Definition of Trust ...................................................... 110
4.6. The Modified Model of Trust ............................................................ 115
4.6.1. Three Parts of the Modified Trust Model ....................................... 118
4.6.2. Antecedents Factors of Modified Trust Model ............................... 118
4.6.2.1. Dispositional Based Trust ....................................................... 119
4.6.2.2. Institutional Based Trust .......................................................... 121
4.6.2.3. The Relationship Between Islam and Dispositional and 
Institutional Based Trust ....................................................... 124

4.6.3. Trust ......................................................................................... 126

4.6.3.1. Willingness to Depend ......................................................... 126

4.6.3.2. The Relationship Between Islam and Trusting Intention ...... 127

4.6.3.3. Trusting Beliefs ................................................................. 127

4.6.3.3.1. Integrity.............................................................................. 129

4.6.3.3.2. Benevolence..................................................................... 130

4.6.3.3.3. Competence..................................................................... 131

4.6.3.3.4. Predictability.................................................................... 132

4.6.3.3.5. The Relationship between Islam and Trusting Beliefs ...... 133

4.6.4. An Interrelationship Among the Trustworthiness Key Factors ..... 134

4.6.5. Behavioural Intentions ......................................................... 135

4.6.6. The Relationship between the Components of the Trust Model..... 136

4.6.6.1. The Relationship between Dispositional Based Trust and 
Institution Based Trust ............................................................. 136

4.6.6.2. The Relationship between Dispositional Based Trust and 
Trusting Beliefs & Trusting Intention ....................................... 137

4.6.6.3. The Relationship Between Institutional Based Trust and 
Trusting Beliefs & Trusting Intention ....................................... 138

4.6.6.4. The Relationship Between Trusting Beliefs and Trusting 
Intention ............................................................................... 141

4.7. The Summary of the Modified Model ...................................... 141

4.8. Summary ..................................................................................... 144

CHAPTER 5. EMPIRICAL RESEARCH METHOD ......................... 146

5.1. Introduction .............................................................................. 146

5.2. Research strategy ................................................................. 147

5.3. Research Design of Survey .................................................... 150

5.3.1. Establishing the Goals of the Project ................................. 151

5.3.1.1. The Aim of the Research .................................................. 152

5.3.1.2. The Necessary Information in This Research............... 154

5.3.2. Determining the Sample ..................................................... 159

5.3.2.1. Purposive Sampling ......................................................... 161
5.3.3. Choosing Interviewing Methodology ............................................. 162
  5.3.3.1. The Selection of Interviewees .................................................. 164
  5.3.3.2. Selecting Types of Interview ................................................... 167
5.3.4. Constructing the Semi-Structured Interview Schedule .......... 169
5.3.5. Conducting a Pilot Study ........................................................... 170
5.3.6. Conducting the Interview ............................................................ 170
  5.3.6.1. Recording and Transcribing Interviews ................................. 172
5.3.7. Analysis ....................................................................................... 173
  5.3.7.1. Pattern Matching Model ......................................................... 176
        5.3.7.1.1. Conducting Pattern Matching ............................................. 177
5.4. Summary ....................................................................................... 181

CHAPTER 6. DATA GATHERING AND ANALYSIS .................. 182
6.1. Introduction .................................................................................. 182
6.2. Data collection ............................................................................... 184
  6.2.1. Data Collection Process ............................................................ 184
  6.2.2. Financial Analysis in Iran ......................................................... 188
  6.2.3. The Profile of Financial Analysts Interviewees ......................... 189
  6.2.4. Primary Data Collection ............................................................ 191
        6.2.4.1. Antecedent Factors to Trust ............................................... 193
        6.2.4.2. Trusting Beliefs ................................................................. 195
6.3. Data Analysis ................................................................................ 196
  6.3.1. The Analysis the Antecedent Factors to Trust ......................... 196
        6.3.1.1. Financial reports ............................................................... 197
          6.3.1.1.1. Accounting errors ......................................................... 198
          6.3.1.1.2. Accounting system ..................................................... 199
          6.3.1.1.3. Fraud in Financial Reports ........................................... 201
          6.3.1.1.4. The History of Financial Reporting ............................... 203
          6.3.1.1.5. Legal Accounting Manipulation .................................... 203
          6.3.1.1.6. The Quality Appearance of Financial Reports ............... 205
          6.3.1.1.7. The Amount of Adjustments ......................................... 206
        6.3.1.2. Managers .......................................................................... 206
          6.3.1.2.1. The Reputation of Managers ......................................... 207
          6.3.1.2.2. Duration of Association Between Financial Analysts and
Managers .............................................................................................. 208

6.3.1.2.3. Ownership Structure .............................................................. 209
6.3.1.2.4. Managers’ Code of Conduct .................................................. 212
6.3.1.2.5. Management tenure................................................................. 212
6.3.1.3. External Auditing ....................................................................... 213
6.3.1.3.1. Audit firm ................................................................................ 213
6.3.1.3.2. Audit report ............................................................................. 215
6.3.1.4. Rules and Regulations ............................................................... 216
6.3.1.5. Religion .................................................................................... 216
6.3.2. Trusting beliefs ............................................................................. 218
6.3.2.1. Integrity .................................................................................... 219
6.3.2.2. Benevolence .............................................................................. 221
6.3.2.3. Competence .............................................................................. 222
6.3.2.4. Predictability ............................................................................. 223
6.3.3. Interaction Amongst the Key Factors of the Trustworthiness of a
Corporate Manager .............................................................................. 225

6.4. Summary .......................................................................................... 226

CHAPTER 7. CONCLUSION AND SUMMARY .............................................. 228

7.1. Introduction .................................................................................... 228
7.2. Findings .......................................................................................... 228
7.3. Contributions .................................................................................. 229
7.3.1. Adding Trust as an Important Element in Business Relationship .. 230
7.3.2. Providing Empirical Evidence of the Key Factors
Trustworthiness .................................................................................. 231
7.3.3. Providing Empirical Evidence of the Influential Factors on Trust
Relationship Between Financial Analysts and Corporate
Managers .............................................................................................. 232
7.3.4. Proposing a New Model of Trust Relationship Between the
Financial Analysts and Corporate Managers ...................................... 233

7.4. Implications ...................................................................................... 236
7.5. Limitations ........................................................................................ 238
7.6. Suggestion for Further Researches .................................................. 239
7.7. Summary .......................................................................................... 241
List OF TABLES

Table 1-1: Percentage of ownership owned by Large shareholders in TSE
.............................................................................................................. 24
Table 4-1: Trust Referent Characteristic-Based Definition Categories... 114
Table 4-2: Mapping of Literature Trust Definitions Based on CT/ RC... 114
Table 5-1: Relevant Situations for Different Research Strategies........ 150
Table 6-1: Interviewees’ Academic Qualification Background .......... 189
Table 6-2: Interviewees' Experiences in Financial Market................. 190
Table 6-3: Duration of Interview............................................................... 190
Table 6-4: Antecedent Factors to Trust ................................................. 195
Table 6-5: Summary of Antecedent Factors to Trust ......................... 196
Table 6-6: Sub Factors of Financial Reports........................................... 198
Table 6-7: Managers’ Influential Factors in Financial Analysts’.........
Level of Trust in Managers................................................................. 207
Table 6-8: External Auditing Factors ...................................................... 213
Table 6-9: Managers Trustworthiness Characteristics ....................... 219

List OF FIGURES

Figure 2-1: Qualitative Characteristics of Financial Information in Iran. 48
Figure 2-2: Influential Factors in the Qualitative Characteristics of .........
Information ........................................................................................... 54
Figure 4-1: An Interdisciplinary Model of High Level Trust Concepts .. 115
Figure 4-2: Comprehensive Trust Model................................................ 117
Figure 4-3: Comprehensive Modified Trust Model.............................. 119
Figure 4-4: Modified Multidimensional Trust Model......................... 143
Figure 5-1: Process Pattern Matching......................................................... 175
Figure 6-1: Interviewees’ Academic Qualification Background .............. 190
Figure 6-2: Managers Trustworthiness Characteristics from the
                 Financial Analysts’ Perspective .............................................. 219
Figure 7-1: Obtained Trust Model .............................................................. 236
Acknowledgments

I am grateful to almighty Allah who gave me the opportunity to complete this thesis. In completing this thesis, I owe a debt of gratitude and thanks to many individuals and institutions that have supported my aspirations in carrying out the project. While being thankful to all of them, I must register my gratitude to some in particular. First and foremost, I would like to express my deepest appreciation to my supervisors Dr. Kathie Cooper and associate professor Michael McCrae and especially Professor Andrew Worthington who kindly accepted to supervise my thesis and whose comments on drafts of the thesis enabled me to prepare the thesis for submission.

I would like to thank Professor Michael Gafka for his administrative and academic supports during my study at University of Wollongong. I would also like to thank staff of the School of Accounting and Finance; Ms Tina Mak (Professional Officer), Ms Cynthia Nicholson (Executive Assistant to Head of School and Disciplines), and Ms Lena Ivancevic (Administrative Assistant). I would like to thank Dr. Abbas Valadkhani for his effective support.

In Iran, I would like to thank the Iranian financial analysts who kindly gave me an opportunity to interview them. In fact, they provided me with real information which was very important to my thesis. I am also indebted to BouAli Investment Company and its staff especially Dr. Rasoul Saedi (Director of the company) and Mr. Mojtaba Kobari (investment manger of the company) who provided me with office and other necessary facilities. Without their help it was not possible for me to collect data during my short stay in Iran.
Thanks all my friends at the Faculty of Commerce of University of Wollongong especially Ahmad Nasseri at School of Accounting and Finance for his helps and encouragements which motivated me to complete this thesis. In addition, I am thankful to my friend Mohammad Ali Bagherpour from Australian National University whose helps and encouragements enabled me to collect the required material for completion of this thesis. Thanks Mrs. Joan Phillips for her outstanding structural and editorial comments.

Further, I am very grateful to the Ministry of Sciences, Researches and Technology of the Islamic Republic of Iran and the University of Isfahan for their administrative and financial support for my Doctoral program.

Finally, this thesis would not have materialised had it not been for the support and love of my wife. I owe more than I can describe in words. Her tolerance and support of my study has always been much appreciated. Her encouragement and succour is born out in the pages of this thesis, and this is as much hers as it is mine. I would like to record my love and my appreciation for her for taking more family responsibilities, sharing the burden and for making even the pain a pleasure. My two children, Faezeh and Sajjad, also deserve thanks for tolerating an ‘absent father’ engaged in a pursuit of which they understood little, an apology for allowing the thesis to keep me away from them. A deal of indebtedness is also due to my father, mother and my wife’s parents for their kindness, spiritual encouragement and prayers, which were indispensable to the completion of this thesis. I would also thank my brother and sisters and my wife’s family member for their helps during my study.
Abstract

This research explored the role of trust in the relationship between the financial analysts and corporate managers in Tehran Stock Exchange (TSE) by focusing on two important aspects of the trust relationship. These aspects are key trustworthiness factors and the influential factors to perceive these key factors. Financial analysts use financial reports, which are prepared by corporate managers, in their analysis. In this thesis components of trust are distinguished from each other. These components are antecedent factors to trust, trust, and outcome of trust. Trust is considered as the financial analyst’s intention to depend on managers based on their perception of managers’ key characteristics including: integrity, benevolence, competence, and predictability. Antecedent factors to trust are psychological and sociological factors that influence the perception of financial analysts about those key characteristics. These antecedent factors include: related factors to: financial reports, management as well as external auditors, rules and regulations, and religion- Islam. The financial analysts’ trust in corporate managers results in their reliance in the provided financial reports. The level of financial analysts’ reliance on the financial reports is positively associated with the level of their trust in managers. The theoretical model of trust developed by … is modified to apply in Iranian context. Purposive sampling is used to collect the required data. The primary data is gathered from in-depth interviews with 20 financial analysts in Iran. After that, the pattern coding technique proposed by Miles and Huberman (1994) is applied to summarise and analyse the interview data. The pattern matching technique is then used to compare the results of interviews to the theoretical patterns. The main findings of this research are: 1) trust is important in the relationship between the financial analysts and corporate managers, 2) the degree of trust that the financial analysts put in the corporate managers is identified by the corporate managers’ level of trustworthiness, 3) the key factors of trustworthiness of a corporate manager are integrity, benevolence, competence, and predictability in his/her behaviour, 4) a model of trust relationship which explains how financial analysts build their relationships is suggested, 5) the main reason for financial analysts to build the relationship with corporate managers is to get accurate information about the company, especially
inside information. This research contributes to the literature of trust which include: (i) adding trust as an important element in business relationship (ii) providing empirical evidence of the key factors of trustworthiness (iii) providing empirical evidence of the influential factors on the trust relationship between financial analyst and corporate managers (iv) proposing a new model of a trust relationship between the financial analysts and corporate managers. This research has several limitations that limit the findings to be generalised. These include: Firstly, in the selected sample, the relationship between the financial analysts and corporate managers was very specific. This is because: the Iranian financial market, the Iranian financial analysis industry, and the TSE all are in an early stage of development. Secondly, the required data were collected through conducting semi-structured interviews with financial analysts only. It was not possible therefore to directly monitor the actual relationship between financial analysts and corporate managers. As a result of this restriction, the researcher had to accept the statements made by financial analysts and the data analysis had to be limited to the results of these interviews. Thirdly, because the beliefs and attitudes of financial analysts had to be translated from Farsi into English in the process of translation some concepts may not have been conveyed correctly because of the linguistic differences. Fourthly, there is a lack of previous research in this area, especially in the Iranian financial market. The study also suggests some prospective areas for investigation by applying the research proposed model in different business relationships such as the relationship between investors and corporate managers and relationship between investors and financial analysts. The results of these suggested studies may be helpful to build a general model of trust which would be applied in different business relationships.