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The Fundamental Determinants of Systematic Risk and Financial Transparency in the DFM General Index

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Abstract

This research study examines the association between firm's fundamental financial information and systematic risk in the DFM General Index. The methodology utilizes a stepwise regression analysis to identify the financial ratios that are associated with firm's beta significantly. The data are obtained from ReutersP@P Financial database for the firms included in DFM General Index which are classified into three categories: Banking, Insurance and non-financial firms. The results indicate that the fundamental determinants of systematic risk in the banking sector are (a) Assets/Equity (b) Book Value Per Share. The fundamental determinants of systematic risk in the insurance sector are (a) Book Value Per Share, (b) Cash Operating/Assets, (c) Cash Operating/Fixed Assets Purchased, (d) Earnings Before Interest, Tax, Depreciation / Assets, (e) Total Liability/Equity. The fundamental determinants of systematic risk in the non-financial sector are (a) Book Value Per Share, (b) Cash Flow/Book Value Per Share, (c) Earnings Before Interest, Tax, Depreciation Per Share, (d) Total Liability/Total Assets (e) Sales/Receivables, (f) Sales/Total Assets. In terms of the association with systematic risk, it was also found out that the financial reports of the DFM Index are not quite transparent to shareholders which offers little help control and manage firm's systematic risk. This study has an intrinsic value in three ways (1) the study is a practical attempt to create a link between financial reporting and the control and management of systematic risk in the DFM General Index, (2) the study identifies the most significant financial information to be published in firm's financial reports in order to control and manage systematic risk, (3) the study shows the methodology to be followed to create an informative link between financial reporting and systematic risk. This study has also certain policy-level implication regarding the scope of transparency that it shows what is to be considered a compulsory financial information to be included in financial reporting.

Keywords: Beta, Financial Transparency, DFM general index

JEL Classification: P34, G30

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