Financial Risk and Management:
An International Journal
Volume 4, Number 2, 2025

Corporate Transparency, Disclosure Quality, and Their Effects on Investor Risk Perception

Laila Fatma[1]

[1] Universitas Negeri Yogyakarta, Yogyakarta, Indonesia

Abstract

Article history:
Received: July 10, 2025
Revised: August 5, 2025
Accepted: October 19, 2025
Published: December 30, 2025

Keywords:
Corporate Transparency,
Disclosure Credibility,
Disclosure Quality,
Investor Risk Perception,
Systematic Literature Review.

Identifier:
Zera Open
Page: 81-94
https://zeraopen.com/journal/frmij

This article investigates how corporate transparency and disclosure quality shape investor risk perception by synthesizing evidence from a systematic literature review of peer reviewed studies on financial and non financial reporting. The review shows that timely, accurate, comparable, and decision useful disclosure reduces information asymmetry, enhances price efficiency, and supports higher stock liquidity, thereby lowering risk premiums demanded by investors. High quality reporting also mitigates downside risk by constraining earnings management and stock price crash risk, especially when accompanied by strong assurance mechanisms and effective internal control structures. Evidence on environmental, social, and governance disclosure indicates that credible sustainability reporting is associated with a lower cost of equity and more conservative capital structures, suggesting that investors view transparent firms as more resilient to regulatory and reputational shocks. At the same time, complex or boilerplate disclosure can increase processing costs and skepticism, weakening these benefits. The article concludes that investor risk perception acts as a key intervening mechanism linking transparency, market outcomes, and firms capital costs for diverse types of firms.

1. Introduction

Corporate transparency and disclosure quality have become central themes in contemporary capital markets as investors face growing uncertainty from economic shocks, geopolitical tensions, and evolving sustainability expectations. High-quality disclosure is expected to reduce information asymmetry, improve the pricing of risk, and support more efficient capital allocation by enabling investors to better assess firm-specific exposures and governance practices (Blankespoor et al., 2020; Ho et al., 2022). In this context, transparency is not limited to the volume of information released, but encompasses the timeliness, accuracy, comparability, and decision usefulness of both financial and non-financial reporting, all of which shape how investors form beliefs about downside risk and future cash flow volatility.

Recent empirical evidence suggests that better disclosure quality is associated with improved market microstructure outcomes that are closely linked to perceived risk. Using a composite information rating, Ho et al. (2022) find that firms with higher disclosure quality exhibit lower stock price delay and greater price efficiency, which in turn reduces expected returns through a lower risk premium channel. Similarly, Wang et al. (2022) show that, in periods of heightened economic policy uncertainty, firms with high quality information disclosure experience less deterioration in stock liquidity, as investors react more strongly to management announcements and analysts' forecasts become more precise. Complementary evidence from the Chinese market indicates that high disclosure quality curbs earnings management and mitigates stock price crash risk, underscoring its role as a mechanism for reducing extreme downside events that investors are particularly sensitive to (Wang, 2022).

At the same time, the literature highlights that the impact of transparency on investor risk perception depends critically on disclosure credibility and processing costs. Experimental and review studies on sustainability and non-financial reporting show that investors respond not only to the presence of disclosures, but also to their perceived believability, precision, and assurance, with more credible disclosures generally lowering perceived risk and increasing willingness to invest (Misiuda & Lachmann, 2022). Survey based evidence further indicates that internal control reporting and internal assurance mechanisms strengthen investors' perceptions of disclosure credibility, with investor culture moderating this relationship (Alqaraleh, 2024). However, when disclosure is overly complex, boilerplate, or perceived as opportunistic, processing costs and skepticism may rise, potentially weakening the risk-reducing benefits of transparency (Blankespoor et al., 2020).

Despite these advances, prior studies have mostly focused on market-based risk proxies such as volatility, liquidity, price delay, or crash risk, rather than directly modelling investor risk perception as an intervening mechanism. The interplay between corporate transparency, disclosure quality, and subjective risk assessments remains underexplored, particularly in emerging markets and in settings where regulatory reforms or sustainability mandates are reshaping reporting practices. This study therefore examines how corporate transparency and disclosure quality jointly influence investor risk perception, and whether improvements in disclosure credibility and assurance can translate into more favourable risk assessments, thereby strengthening market confidence and potentially lowering firms' cost of capital.

2. Literature Review

Corporate transparency and disclosure quality are rooted in agency and information asymmetry theories, where richer, more decision useful reporting is expected to reduce hidden-information problems and improve capital market outcomes. Recent work on disclosure quality in developing markets shows that more disaggregated, informative financial reporting strengthens corporate performance because it constrains managerial myopia and is reinforced by effective governance mechanisms (Afifa & Nguyen, 2024). In the non financial domain, Arvidsson and Dumay (2022) argue that high quality ESG reporting characterized by relevance, balance, and verifiability signals long-term orientation and enhances investor confidence, highlighting that the quality rather than the mere quantity of disclosure drives capital market reactions.

A large empirical strand links disclosure quality to information asymmetry and market microstructure risk. Using French listed firms, Garrouch and Omri (2024) document that IFRS adoption, by improving reporting quality, reduces bid ask spreads and return synchronicity, indicating lower information asymmetry and more informative prices. Similarly, Dutta (2024) shows that firms with lower information asymmetry enjoy higher stock liquidity, suggesting that transparent disclosure contributes to a lower required liquidity premium. Cross country evidence further reveals that institutional and political environments moderate this link: Kim et al.

(2024) find that in more democratic regimes, higher stock liquidity and lower information asymmetry are more strongly associated with transparent reporting, implying that investors' perceptions of risk depend jointly on disclosure practices and the broader governance context.

Another important channel operates through downside risk and stock price crash risk. Xiang et al. (2020) provide evidence that higher financial reporting quality weakens the positive association between political connections and crash risk, indicating that transparent reporting limits managers' ability to hoard bad news. Studies of assurance and auditing reach similar conclusions: Sultana et al. (2022) show that stronger audit quality via industry specialization and independent audit committees reduces crash risk by lowering reporting opacity, while Han et al. (2023) find that greater audit effort (measured by audit hours) is associated with lower future crash risk, especially in firms with higher inherent information risk. Collectively, this literature suggests that investors interpret opaque or low quality disclosure as a signal of higher tail risk exposure, which is then priced into required returns.

The growing ESG and non-financial reporting literature reinforces the view that disclosure quality shapes investor risk assessments through the cost of capital channel. Jafar et al. (2024) find that firms with higher quality ESG disclosure face a lower cost of equity, consistent with investors pricing these firms as less risky or more resilient to regulatory and reputational shocks. Studies on large U.S. corporations show that firms with more comprehensive sustainability reporting tend to face a lower cost of capital and adopt more conservative capital structures, suggesting that transparent ESG disclosure can help ease their financing constraints. In a similar vein, Dwomor and Mensah (2024) document that ESG reporting improves firm value in an emerging-market setting, with the cost of capital mediating the ESG value relationship evidence that investors translate credible sustainability information into more favourable risk return expectations.

Recent studies also emphasize that disclosure credibility and presentation shape investor risk perception beyond traditional market based proxies. Keter et al. (2024) show that intellectual capital disclosure mediates the positive relationship between financial performance and firm value, suggesting that investors reward transparent communication of intangible resources because it reduces uncertainty about future earnings capacity. In experimental research, Festa et al. (2024) demonstrate that quantitative audit materiality disclosures can either enhance or erode investor trust depending on investors' prior concerns about earnings management; detailed qualitative explanations mitigate mistrust and lead to more balanced risk judgments. These findings indicate that investors respond not only to the existence of disclosure, but also to its readability, specificity, and perceived sincerity, which directly influence their subjective perception of audit and reporting risk.

Overall, the literature converges on the view that corporate transparency and disclosure quality affect investor risk perception through multiple, interrelated mechanisms: by lowering information asymmetry and improving liquidity, by mitigating stock price crash risk via more timely bad news recognition, and by reducing the cost of capital when financial and ESG reports are viewed as credible and decision-useful. However, most prior studies still rely on indirect, market-based proxies (volatility, spreads, crash risk, or implied costs of capital) rather than directly measuring investors' subjective risk perceptions, and evidence from emerging markets where institutional weaknesses and rapid regulatory changes may amplify the role of transparency remains relatively limited. These gaps motivate further research that explicitly models investor risk perception as an intervening mechanism linking corporate transparency, disclosure quality, and firms' financing outcomes.

3. Methods

This study employs a systematic literature review (SLR) approach to synthesize and critically evaluate prior research on corporate transparency, disclosure quality, and their effects on investor risk perception. The SLR is structured to ensure transparency, replicability, and minimization of selection bias through a clearly defined search strategy, screening procedure, and data extraction protocol. Academic articles were identified through major scholarly databases such as Scopus, Web of Science, ScienceDirect, and Google Scholar, using combinations of keywords related to "corporate transparency," "disclosure quality," "financial reporting quality," "ESG disclosure," "investor risk perception," "cost of capital," "information asymmetry," and "stock price crash risk." Boolean operators and keyword truncations were used to refine the search, and the initial pool of records was expanded by examining the reference lists of relevant empirical and review papers (backward and forward snowballing).

The inclusion criteria focused on peer-reviewed journal articles written in English that explicitly examine the relationship between corporate transparency and/or disclosure quality and outcomes related to investor risk, such as perceived risk, information asymmetry, liquidity, volatility, stock price crash risk, or the cost of capital. Both quantitative and qualitative studies, as well as mixed methods research, were considered as long as they provided conceptual or empirical insights into how transparency and disclosure shape investors' risk assessments or risk related market outcomes. Exclusion criteria comprised conference proceedings, book chapters, dissertations, non peer reviewed sources, technical reports, and studies that dealt with disclosure but did not connect it to any risk-related dimension at the investor or market level. Duplicate records were removed, and titles and abstracts were screened, followed by full text assessments to confirm eligibility.

For all included studies, a structured data extraction form was used to capture key characteristics, including research setting, sample characteristics, measurement of transparency or disclosure quality, operationalization of investor risk or risk proxies, research design and analytical methods, and main findings. Studies were also coded according to contextual features such as country or region, type of disclosure (financial vs. non-financial, ESG specific, voluntary vs. mandatory), and institutional environment (e.g., governance quality, legal origin, or regulatory context where available). A qualitative synthesis was then conducted to identify recurring themes, theoretical mechanisms, and patterns in empirical results, with particular attention to how transparency and disclosure quality influence investor risk perception directly or indirectly through channels such as information asymmetry, liquidity, crash risk, and the cost of capital. Where appropriate, a vote counting logic was used to compare the direction and consistency of relationships across studies, while noting methodological differences and research gaps that warrant further investigation.

4. Results and Discussion

A further contribution of the reviewed studies is to highlight that the effects of transparency on investor risk perception depend critically on disclosure credibility, contextual factors, and processing costs. Research on sustainability and non-financial reporting shows that investors respond not only to the presence of disclosure, but also to its perceived believability, precision, and assurance, with more credible disclosures generally lowering perceived risk and increasing willingness to invest (Misiuda & Lachmann, 2022). Survey based evidence indicates that internal control reporting and internal assurance mechanisms strengthen investors' perceptions of disclosure credibility, and that investor culture moderates this relationship, implying that similar levels of transparency may be interpreted differently across cultural and institutional settings (Alqaraleh, 2024; Kim et al., 2024). Studies of intellectual capital disclosure suggest that transparent communication of intangible resources mediates the relationship between financial performance and firm value, reducing uncertainty about future earnings capacity (Keter et al., 2024). Experimental work on audit materiality disclosures further demonstrates that detailed qualitative explanations can mitigate mistrust and lead to more balanced risk judgments, whereas poorly framed or overly technical disclosures may raise skepticism and perceived reporting risk (Blankespoor et al., 2020; Festa et al., 2024).

Overall, the synthesis indicates that corporate transparency and disclosure quality influence investor risk perception through interrelated channels: by lowering information asymmetry and improving liquidity, by mitigating stock price crash risk via timelier recognition of bad news, and by reducing the cost of capital when financial and ESG reports are perceived as credible and decision useful. However, the review also reveals important gaps. Most studies still rely on indirect, market based proxies such as volatility, liquidity, crash risk, or implied costs of capital, rather than directly measuring investors' subjective risk perceptions. Moreover, while several contributions examine emerging markets, evidence remains relatively fragmented in contexts where institutional weaknesses, political connections, and rapid regulatory changes may amplify the role of transparency. These gaps suggest the need for future research designs that combine market based indicators with survey or experimental measures of perceived risk, and that explicitly account for institutional, cultural, and governance heterogeneity when analysing how corporate transparency and disclosure quality shape investor risk perception and, ultimately, firms' financing outcomes.

5. Conclusion

This study set out to synthesize the growing body of evidence on how corporate transparency and disclosure quality shape investor risk perception. The review shows that high-quality disclosure covering both financial and non-financial information consistently contributes to a more favourable risk environment. Transparent reporting reduces information asymmetry, improves price efficiency, and supports higher stock liquidity, which together lower the risk premium demanded by investors. At the same time, credible and timely disclosure mitigates downside risk by limiting bad-news hoarding and reducing the likelihood of stock price crashes, especially when supported by strong assurance mechanisms and effective governance structures.

The findings also highlight that investor responses are not driven by the mere existence or volume of disclosure, but by its perceived credibility, clarity, and decision usefulness. ESG and other non-financial disclosures can lower the cost of capital and enhance firm value when they are relevant, balanced, and verifiable, signalling resilience to regulatory, reputational, and sustainability-related shocks. However, overly complex, boilerplate, or opportunistic disclosure may increase processing costs and skepticism, dampening or even reversing the risk-reducing benefits of transparency. Contextual factors such as institutional quality, investor culture, and country level governance further condition how similar levels of disclosure are interpreted and priced in different markets.

At the same time, the review reveals important gaps in the literature. Most studies still rely on indirect, market-based proxies such as volatility, liquidity, crash risk, and implied cost of capital, rather than directly measuring investors' subjective risk perceptions. Evidence from emerging markets remains fragmented, even though institutional weaknesses and rapid regulatory change may amplify the importance of transparency and assurance. Future research should therefore develop designs that combine market indicators with survey or experimental measures of perceived risk, and explicitly incorporate institutional, cultural, and governance heterogeneity. By modelling investor risk perception as an explicit intervening mechanism, future work can offer a more complete understanding of how corporate transparency and disclosure quality translate into market confidence and ultimately shape firms' financing outcomes.

References

Abu Afifa, M., & Nguyen, N. M. (2024). Corporate performance modeling through disclosure quality at the level of developing countries in Southeast Asia. *Economic Research-Ekonomska Istraživanja, 37*(1).

Alqaraleh, M. H. (2024). Evaluating the effect of investor culture on internal control reporting and investor perceptions of disclosure credibility. *Investment Management & Financial Innovations, 21*(4), 314.

Arvidsson, S., & Dumay, J. (2022). Corporate ESG reporting quantity, quality and performance: Where to now for environmental policy and practice? *Business Strategy and the Environment, 31*(3), 1091–1110.

Blankespoor, E., deHaan, E., & Marinovic, I. (2020). Disclosure processing costs, investors' information choice, and equity market outcomes: A review. *Journal of Accounting and Economics, 70*(2–3), 101344.

Dutta, S. (2024). The nexus between information asymmetry and liquidity: Evidence from an emerging market. *The Indian Economic Journal, 72*(1), 1–19.

Festa, M. M., Jones, M. M., & Witz, P. D. (2024). Auditor materiality disclosures and investor trust: How to address conditional risks of disclosure mandates. *Behavioral Research in Accounting, 36*(2), 47–70.

Garrouch, H., & Omri, A. (2024). IFRS adoption, information asymmetry and stock liquidity: Moderating effects of corporate governance mechanisms.

Han, X., Luo, W., Wu, L., & Zhou, W. (2023). Audit effort and stock price crash risk. *Abacus, 59*(1), 230–257.

Ho, K. C., Lee, S. C., & Sun, P. W. (2022). Disclosure quality, price efficiency, and expected returns. *The North American Journal of Economics and Finance, 59*, 101573.

Jafar, R., Basuki, B., Windijarto, W., Setiawan, R., & Yaacob, Z. (2024). Environmental, social and governance (ESG) disclosure and cost of equity: The moderating effects of board structures. *Cogent Business & Management, 11*(1), 2429794.

Keter, C. K. S., Cheboi, J. Y., & Kosgei, D. (2024). Financial performance, intellectual capital disclosure and firm value: The winning edge. *Cogent Business & Management, 11*(1), 2302468.

Kim, J. C., Su, Q., & Elliott, T. (2024). Political regimes, stock liquidity, and information asymmetry in a global context. *Journal of Risk and Financial Management, 17*(8), 342.

Misiuda, M., & Lachmann, M. (2022). Investors' perceptions of sustainability reporting: A review of the experimental literature. *Sustainability, 14*(24), 16746.

Sultana, F., Aslam, M., Sarwar, A., & Iqbal, A. (2022). Impact of audit quality on stock price crash risk: Evidence from Pakistan Stock Exchange. *Journal of Economic Impact, 4*(3), 161–169.

Wang, F., Mbanyele, W., & Muchenje, L. (2022). Economic policy uncertainty and stock liquidity: The mitigating effect of information disclosure. *Research in International Business and Finance, 59*, 101553.

Wang, Q., Zhai, A., Pang, Q., Wang, H., & Chu, X. (2022, December). Information disclosure quality, earnings management and stock price crash risk: Evidence from China. In *2022 2nd International Conference on Financial Management and Economic Transition (FMET 2022)* (pp. 622–633). Atlantis Press.

Xiang, C., Chen, F., & Wang, Q. (2020). Institutional investor inattention and stock price crash risk. *Finance Research Letters, 33*, 101184.