Chapter 9
Shifting Our Lenses to Behavioral Finance Paradigm:
CEO Inopportune Optimism and Financial, Non-Financial Communications

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ABSTRACT

Recent crisis periods have shown how corporate communication could contribute to organizational performance regarding financial outcomes, reputation concern, etc. The efforts to reduce information asymmetry, deal with agency problems, improve stakeholder engagement have brought it to the fore. Past research on reporting mechanisms has overly focused on its normative structure and manifested ethical or problematic issues. Some research has argued credibility of both reporters and assurance providers of this information. Although some limited research on management control over reporting mechanisms and on some weaknesses of assurance providers' verification statements, this research doesn't explain enough why this manipulative control occurs. Shifting our lenses to behavioral finance paradigm, it's understood that judgmental decision making seems to be exposed to diverse systematical biases and fallacies. Amidst them, inopportune optimism, alias overconfidence, stands for one of the most serious biases.

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INTRODUCTION

"…The illusion that we understand the past fosters overconfidence in our ability to predict the future…" (Kahneman, 2015)

Companies utterly attempt to survive in a global cutthroat competition environment. And, information has actually made a world of difference in early 2000s since accounting/auditing scandals, market collapses have amplified significance of all relevant information, let alone financial information. Unfortunately, companies have discerned that they couldn't ensure their survival in this environment through focusing merely on financial outcomes. Through a battery of ethical, disciplinary, institutional arrangements aimed for reconstructing confidence in financial reporting (FR) functions and toward the goal of sustainable development, companies have to both disclose financial/non-financial data in concordance with global standards and also to ensure this information's credibility for their stakeholders. At the same time, the efforts to reduce information asymmetry through signaling theory, and to improve stakeholder relations have conspicuously brought corporate communication to the fore. Considering signaling theory, information disclosed by companies doesn't seem to decrease definitely. Then, striving to ensure accuracy and credibility of this immense information seems a vital task and this requires first to know what's actually going on in corporate communications.

Past research on financial reporting (FR) and sustainability reporting (SR) has overwhelmingly put emphasis on its normative structure and manifested ethical or problematic issues. Or, research has widely argued credibility of both reporters and assurance providers of this information. Although limited research referring to management control over these reports and to some weaknesses of assurance providers' statements, this research body doesn't explain enough why this control or weaknesses occur. Additionally, the research arguing personal attributes of these actors (e.g., management and responsible reporting staff, assurance providers) is interestingly rare. By the virtue of signaling theory, it is well known that companies as more informed parties could convey this valuable information to stakeholders as less informed parties (Karaman et al., 2020) in order to ameliorate information asymmetry. This theory also discusses that firms could disclose favorable information more in order to communicate positive firm attributes to outside users (Connelly et al., 2011). According to Stiglitz (2000), presence of asymmetry especially gets crucial for two types of information: Information about quality, information about intent. Yet, the latter is not as easy as the former to be detected since this task necessitates to invoke unobservable constituents or behavioral processes. Further, upper echelons approach (Hambrick & Mason, 1984; Hambrick, 2016) which purports that organizational decisions reflect views and tone of top management really helps

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