



Key Audit Matter Disclosures and Retail Investors in Emerging Markets: A Review of the Evidence

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Abstract

Since 2016 auditors of listed companies in most jurisdictions have been required to describe the key audit matters (KAMs) they dealt with during the audit. The reform was justified largely by its expected value to investors, and it has now been adopted across many emerging markets where individuals, and not institutions, do much of the trading. This review asks what is known about whether KAM disclosures change how retail investors read and use annual reports in those markets. It brings together three bodies of evidence: archival studies of market reactions to expanded audit reports, experiments on non-professional investors, and descriptive studies of KAM reporting in emerging economies. The archival work, mostly from the United Kingdom and France, finds little or no price or volume response. Experiments show that KAMs can shift where readers look and how they judge a company, but that non-professional readers process them with difficulty. Evidence from emerging markets is growing and concentrates on what auditors disclose and on audit quality; direct evidence on retail readers is almost absent. The review sets out why the developed-market findings may not transfer, and what studies would be needed to answer the question properly.

Keywords: Key audit matters, ISA 701, Expanded audit report, Retail investors, Emerging markets, Annual reports

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1. Introduction

For most of the last century the audit report was a pass or fail document. A reader learned that the auditor had given an unqualified opinion and nothing about what the audit had involved. ISA 701 changed that. For periods ending on or after 15 December 2016, auditors of listed entities applying international standards must communicate the matters that were of most significance in the audit, explain why, and say how each was addressed (IAASB, 2015). The United Kingdom had introduced a similar requirement in 2013, and the United States followed with critical audit matters under AS 3101 (PCAOB, 2017).

The stated purpose was to make the report more informative for its users. Within a few years the requirement had been taken up across emerging markets, among them China, India, Thailand, Malaysia,

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South Africa, Brazil and Jordan. In several of these markets individual investors account for a large share of trading, annual reports are long and often published in a second language, and analyst coverage is thin. If KAMs help anyone, one might expect them to help retail investors there. Whether they do is the question this review addresses.

The question cannot be answered directly, because studies of retail investors in emerging markets reading KAMs are very few. What can be done is to assemble the evidence that bears on it and to be clear about how far each part reaches.

2. Scope and Approach

This is a narrative review. It covers peer-reviewed studies of expanded audit reports published since the first proposals in 2013, grouped by method: archival studies of market and reporting outcomes, experimental studies of readers, and descriptive studies set in emerging economies. A recent survey of the whole literature ([Minutti-Meza, 2021](#)) served as the starting point. Studies of auditor liability are mentioned only where they bear on what auditors choose to write. No new data were collected, and no quantitative synthesis was attempted.

3. What KAM Reporting Was Meant to Do

A KAM section is expected to work in two ways. It may carry new information, telling the reader something about the company's accounts that could not be learned elsewhere. Or it may direct attention, pointing a reader with limited time to the handful of areas that deserve it. The distinction matters for retail investors. Professional analysts already know where the judgement in a set of accounts lies. An individual reading a two-hundred-page annual report may not, and for that reader a signpost could be worth more than a disclosure. Research on individual investors shows that they respond to disclosures that are clear and concise and hold back from those that are not ([Lawrence, 2013](#)), and that annual reports have been growing harder to read for a long time ([Li, 2008](#)).

4. Evidence on Investor Response

Table 1 summarises the studies most often cited on the question. They fall into three groups.

4.1. Market-level studies

The archival evidence is the most consistent. Studies of the United Kingdom's 2013 reform found no significant change in abnormal returns or trading volume around the release of expanded reports ([Gutiérrez et al., 2018](#)), and a later study traced the absence of a reaction to the fact that most of the risks described had already been disclosed by the company or were otherwise known ([Lennox et al., 2023](#)). French justifications of assessments, a forerunner of KAMs in place since 2003, produced no market response either ([Bédard et al., 2019](#)). There is some evidence of a benefit on the preparer's side, with reporting quality improving after the United Kingdom change at no significant extra audit cost ([Reid et al., 2019](#)). These studies measure the aggregate market. They cannot separate retail from institutional investors, and they come from markets where institutions dominate.

4.2. Experiments with non-professional investors

Experiments get closer to the individual reader. The earliest and best known found that non-professional investors shown a critical audit matter paragraph about a fair value estimate were more likely to change their investment decision than those shown a standard report, and more likely than those given the same information in a management footnote ([Christensen et al., 2014](#)). The auditor's voice, in other words, carried weight of its own. Later work complicates the picture. German non-professionals had trouble making use of KAM content that investment professionals handled readily ([Köhler et al., 2020](#)), and participants in a later experiment valued KAMs chiefly as a signal about a less well-known auditor ([Moroney et al., 2021](#)). A disclosure that flags measurement uncertainty can also act as a forewarning, lowering the confidence readers place in the flagged number ([Kachelmeier et al., 2020](#)).

Table 1: Selected studies on how users respond to key or critical audit matter disclosures			
Study	Setting and method	Readers studied	Main finding
Christensen <i>et al.</i> (2014)	United States; experiment	Non-professional investors	A critical audit matter paragraph made readers more likely to stop considering the company as an investment
Sirois <i>et al.</i> (2018)	Eye-tracking experiment	Participants reading financial statements	KAMs direct attention to the related disclosures; with several KAMs, less attention goes to the rest of the statements
Gutiérrez <i>et al.</i> (2018)	United Kingdom; archival	Equity market as a whole	No significant change in market reaction, audit fees or audit quality after adoption
Bédard <i>et al.</i> (2019)	France; archival	Equity market as a whole	No market reaction to justifications of assessments; the disclosures appear largely symbolic
Köhler <i>et al.</i> (2020)	Germany; experiment	Investment professionals and non-professionals	KAM content affected professionals' judgements; non-professionals had difficulty processing it
Moroney <i>et al.</i> (2021)	Experiment	Non-professional investors	KAMs raised the perceived value and credibility of the audit mainly when the auditor was not a Big 4 firm
Lennox <i>et al.</i> (2023)	United Kingdom; archival	Equity market as a whole	Risk disclosures were not incrementally informative, largely because investors already knew of the risks

4.3. Attention and processing

The eye-tracking study by Sirois *et al.* (2018) speaks most directly to the signpost idea. Readers given KAMs reached the related notes faster and spent more time on them. When the report contained several KAMs, however, they spent less time on the remainder of the financial statements. Attention is finite, and directing it has a cost. For a retail reader this cuts both ways: the KAM section may be the most efficient route into the accounts, and it may also become a substitute for reading them.

5. The Emerging-Market Setting

Research set in emerging markets has grown quickly since adoption, but it has asked different questions from the one posed here.

5.1. What has been studied

Most studies describe what auditors report and test for effects on audit quality. Work on Thailand, one of the earliest adopters, examined whether KAM reporting changed audit quality (Kitiwong and Sarapaivanich, 2020). A study of Jordan documented a small number of KAMs per report, heavy concentration on a few standard topics and little variation from year to year (Abdullatif and Al-Rahahleh, 2020). Analysis of Chinese reports linked the way KAMs are described to measures of audit quality (Zeng *et al.*, 2021). A European comparison found that the number of KAMs varies with client complexity, auditor and the precision of accounting standards (Pinto and Morais, 2019), a result that suggests institutional setting shapes disclosure everywhere. None of these studies observes an individual investor reading a report.

5.2. Why the developed-market findings may not transfer

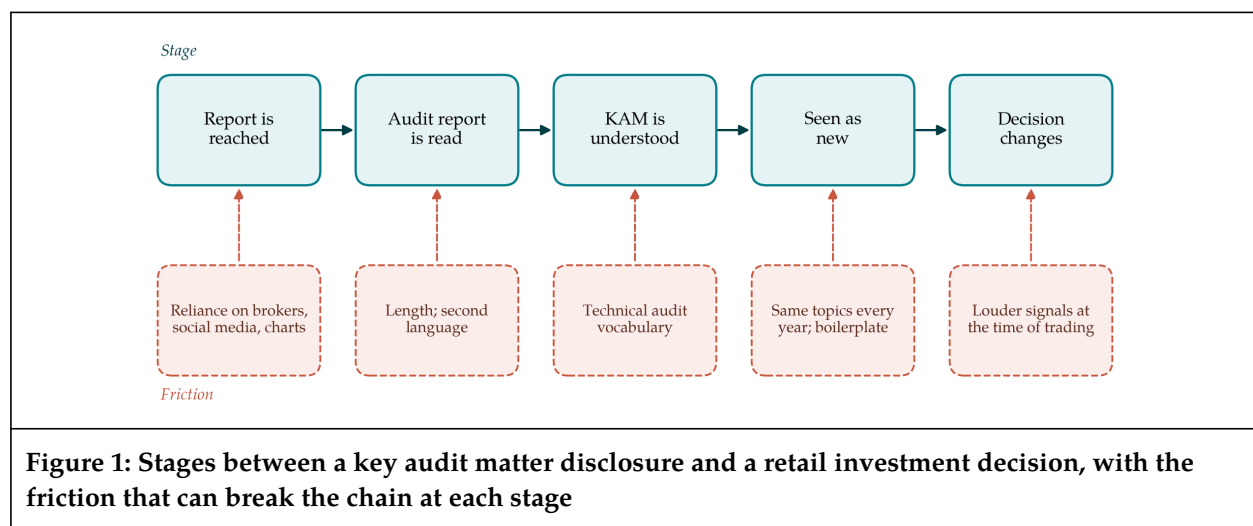
There are reasons to think the answer could differ in emerging markets, in either direction. On one side, the conditions that made KAMs uninformative in the United Kingdom are weaker. Where analyst coverage is sparse and company disclosure less complete, the auditor's account may contain more that is new. Where retail investors hold and trade a large share of the market, a clear signpost has more readers to help.

On the other side, several frictions stand between a KAM and a retail decision, and each may be stronger. Figure 1 sets them out as stages. The report must be reached, which depends on whether individuals consult annual reports at all or rely on brokers, social media and price charts. It must be read, often in a language that is not the reader's first. It must be understood, and KAM sections are written in the technical vocabulary of auditing. It must be believed to say something new, which is doubtful if the same few topics recur in every report. And it must compete with louder signals at the moment of decision. Where ownership is concentrated and litigation risk for auditors is low, there is also less pressure to write anything other than boilerplate. The liability experiments from the United States ([Brasel et al., 2016](#); [Gimbar et al., 2016](#)) show that auditors' incentives respond to legal exposure, and that exposure differs sharply between jurisdictions.

6. Gaps and a Research Agenda

Three gaps stand out. The first is the absence of experiments with real retail investors in emerging markets. Most experimental participants have been students or online panel members in developed economies. Replicating the established designs with brokerage clients in, say, India, Thailand or Brazil, in the local language, would show quickly whether the basic effects hold.

The second is the lack of evidence on use. Brokerage records, report download logs and survey data could establish how many individual investors open an annual report, how many reach the audit report, and how long they spend there. Without that, tests of comprehension answer a question about a reader who may barely exist.



The third concerns content. Archival work in emerging markets could exploit variation in KAM specificity, asking whether entity-specific descriptions are followed by different retail trading patterns from generic ones, in markets where retail order flow can be identified. Staggered adoption dates across countries and company groups offer natural comparisons that the first-mover markets did not.

7. Conclusion

On present evidence it is not possible to say that key audit matter disclosures change how retail investors in emerging markets read annual reports. Market-level studies from developed economies find little response. Experiments show that individual readers can be moved by KAMs and can also be confused by

them. Studies in emerging markets describe the disclosures without observing their readers. The setting gives grounds for expecting both more benefit and more friction than elsewhere. The honest summary is that the reform was introduced for the benefit of a reader about whom, in these markets, very little is yet known.

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