



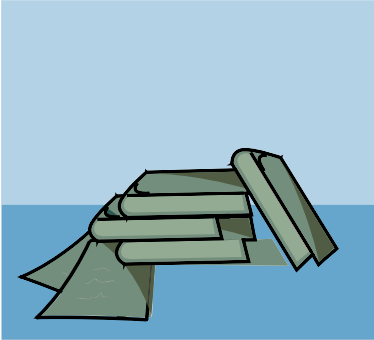
# *Information and its Sources*





## *Introduction*

A lot of people think that the most expensive merchandise is oil or gold, but it is proved that information is the most expensive merchandise available. Thus, the most important step an investor should take before investing in the stock market is to search for and ask about the information available on the company he is interested in investing in to try to understand its potential future performance. For example, the investor should have some knowledge on several factors critical to his decision in investing in this company like the expectations for the risk level in the company's stock and its growth level.



## *Types of Information*

It is a fact that financial markets change rapidly. This is a result of the instant market interaction with the sudden periodical and daily information and news whether their source was the media, the government or the companies themselves. Information and news can be divided into two independent categories each one has its own characteristics.

## *Partial Information (Corporate Information)*

Partial information, as the name suggests, focuses on specific news that are related to the developments in local companies such as issuing and publishing quarterly reports, annual

reports and detailed press releases. Although such news could leave relatively large-scale effects on the financial markets especially if the information is associated with a leading industrial company. However, the effect of partial information is usually limited to the targeted company and might reach its primary competitors in the sector.



## *Overall Information (Information on Macroeconomics)*

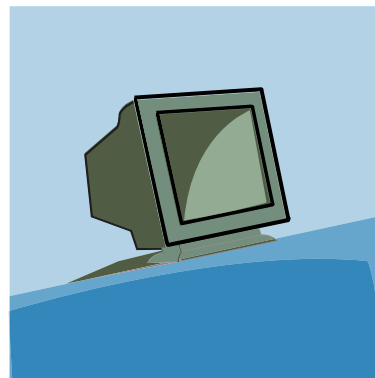
Overall information focuses on what is related to the macroeconomics that exceeds the level of production units and establishments. Information on the underlying sectors of the overall economy falls under the same catego-

ry as well. When overall information such as changes occurring in the GDP, inflation rate and government spending is released, it often affects the entire local market and it may reach to international markets as well. For example, a report referring to a large increase in the government spending rate might have a positive effect on the market. It will lead most of the investors to believe that the levels of public demand will improve and growth levels will help the benefiting companies to increase their capital, thus, contributing to higher demand for factors of production and utilizing more of them.

International economic and political instability is another example for the effect of overall information on financial markets. International financial markets have become largely interdependent, which makes it possible for the political and economic developments in any country or region to leave their influence on all international markets.

### *Information Sources*

Information may come in different forms. It might come as statistics, graphs or statements and media reports. The ways of pre-



senting it also differ greatly. It might come out as printed material or recorded CDs, audio and video broadcasts or available on the internet. Information can be obtained free of charge, usually, or charged. Whatever the information was, the sources to get it can be categorized as the following:

### *The Company's Source*

The report on the quarterly and annual preliminary financial statements, released by the company, is a good starting point to know the company. The regulations and rules issued by the Capital Market Authority require the companies listed on the market to provide the CMA with their annual and initial financial statements and publish

them immediately after being approved by the company's board. This will give it credibility and transparency. Financial statements contain detailed information on the company's current financial position.

CMA has issued a comprehensive booklet on "Reading Financial Statements" to help the investor to have a clear picture of the company's financial position.



Companies also publish annual reports in which they review the productive, administrative, investment and financial achievements in the past fiscal year. They give indicators of future plans and financial difficulties they may encounter.

Such information can be reached, in addition to the press releases and other related corporate news, by visiting the company's headquarter, logging on to its website (if it has one) or the "Tadawul" website.

### *Other Sources*

In addition to the information provided to investors by the companies about their business which usually aims to draw a bright picture of the company, there is a various range of external sources that can be described as more comprehensive. A good example can be newspapers, financial satellite channels, specialized investment websites and newsletters. All of them can give the investor a broad idea on corporate stocks and the industry in which the company operates in addition to the macroeconomics.



Many consulting and financial intermediary companies have specialized websites that offer the service of emails providing investors with accurate and in-depth information that commensurate with their needs whether the information and reports are derived from official reports and data on the national economy, the stock prices or the material news on the companies the investor owns in his portfolio.

## *How to Use Information Wisely*

Unfortunately, it is not enough to have the information on time to be a successful investor. The most vital factor is the credibility and accuracy of the information, the investor's ability to study and interpret it, what it means to his portfolio, what he should do when he has all the information and whether he should buy, sell or do nothing.

Although gaining profits is not guaranteed at all when it comes to investment, the investor can develop his investment strategy to reach his financial goals if his investment decisions

were made based on reliable sources not rumors or assumptions that do not represent a dependable approach to achieve goals.

## *The Power of News*

News headlines can have a huge impact on the market. Markets rapidly interact with daily news whether it was new information related to the microeconomics like local companies' developments or changes in the macroeconomics. It is agreed that the market is affected by the news, but the most important thing is what this information means, especially to the individual investor.

Undoubtedly, an investor's goals determine the way he reacts to the received news. If we assume that an investor has short-term goals, and intends to buy a house for example, the increase in the stock price of a company he invested in due to released data about its profits may encourage him to sell some of his shares and buy the house. On the other hand, if he has long-term goals, he might consider increasing his investments in the company.



## *Rumors and Speculation*

There are sound procedures an investor should adopt to develop his investment strategy. There are also some practices that should be completely avoided such as spreading rumors, trading according to it and speculating rather than investing.

### *Rumors*

The Capital Market Law (CML) prohibits anyone from, whether directly or indirectly, deliberately spreading incorrect data about a particular company which may have a negative or a positive effect on the share price of this company shares.

If a person leaks explicit criticism of the company and has prior knowledge that the basis for such criticism is untrue, then he is in breach of the Law because the value of the company's share price may decrease as a result of this improper conduct. Similarly, it is not legal that corporate executives keep quiet and do not give any material information about their companies while knowing the importance of such information in an attempt to cause a change in the stock price.

*Why is it so important to prevent rumors from affecting the market?*

The answer can be summarized in the following three reasons:

1. Rumors lead to generating unfair profits for those who benefit from spreading them.
2. Rumors lead to unfair losses among the victims who were deceived.
3. Rumors may lead to exaggerated buying and selling prices for shares which can affect the whole market reflected by "Tadawul" index (TASI).



## Speculation

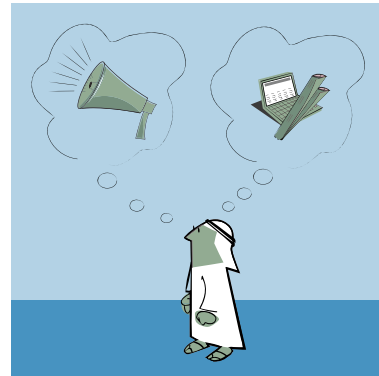
Speculation is somehow similar to gambling if it was based on rumors or weak information. It is a fact that trading on the stock market involves risks, but there are ways to manage these risks. The most important of which is to make the investment decision based on reliable information.

On the other hand, a speculative behavior means having a stock without a reasonable reason except for anticipating a future increase in its value. Although a speculation's risk and damage in general is not as that of rumors because speculation does not usually affect a large segment of traders in the market, but it is still a harmful behavior for some stockholders who embrace it as a basic tool in their investments.

## Rumors Vs. Research

Investors who want to eliminate rumors and rely on accurate and credible information face difficulty in distinguishing between the two. There are several ways an investor can use to draw a distinction between true information and other false information that can

be harmful. In addition, the investor can ask some questions when he hears some hard-to-believe news or he has doubts about them. Some of these questions can be:



1. What is the main source of this information?
2. What is the level of experience of the person, or the newsletter that released that information?
3. What would the person gain if he disclosed this information?
4. Is it possible to get more evidence and proof from a reliable source to support the inaccurate information acquired?
5. Did the provider of the information ask the investor not to disclose it?

If the answer to the last question was yes,

then the information acquired is unfortunately not true. It may also come under the name of Irregular Information.

### *Researching the Company Invested in*

Each investor, before making the decision to invest in a company, should make an effort in learning about the company he is investing in. Examining financial statements is, without question, the most important step in knowing a company. Moreover, knowing the company's products, services, executive and senior management is equally important as well as its growth potential.

There are signs that show that the investor is aware of the status of the company he is investing in. For example, the investor should ask if the company belongs to a sector that is always affected by international economic and political changes, and whether the demand for its products is increasing or decreasing? Are there any upcoming changes in the management's team or strategies?

Clearly, the investor needs to follow all the above-mentioned matters. Perhaps the most suitable and available sources to get this information are the company's annual report and prospectus. These two reflect the company's vision and objectives, its investment and production strategies outline, as well as a detailed presentation of its financial statements.

### *Annual Reports*

Annual reports are an important source for highlighting the company's performance and operations in general during the past year. Whilst quarterly financial statements give a detailed explanation for the company's financial performance to date, the annual report illustrates more in-depth details regarding the company and its philosophy in running its business.

Under the Capital Market Law, joint stock companies are obligated to inform the shareholders of the developments in the company's general performance. As the name suggests, the annual report, is published once a year. It should be available to all investors without any costs, and you do not have to be a share-

holder or owner in the company to have access to the annual reports of joint stock companies.

A company's annual report, with its rich content of information, can influence the investor's decision to invest in the company or not. A copy of the annual report can be obtained from brokerage firms, the company itself, or its website on the internet.



### *Reading the Annual Report*

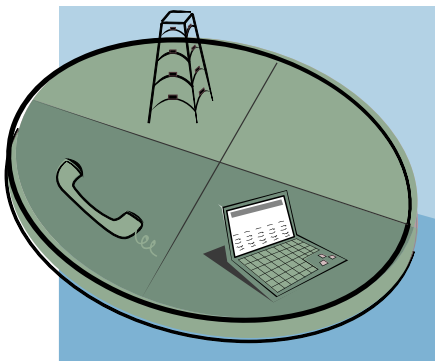
Unlike financial statements which only include figures, an annual report contains several chapters that have texts and illustrations explaining the company's business. The texts written in the report aim, in some parts, at explaining the figures mentioned in the financial statements which reveal the performance

level of the company.

Note that the message conveyed in the written texts of the annual report may differ from the one communicated by the figures of the financial statements. For example, a company may include, in its financial statement report, achieving an increase in its profits during the past year, and this is of course good news about the company. However, the investor might find, by reading the general text of the annual report or in some footnotes at the end of the report, that this increase was a result of non-operating profits such as: selling a land owned by the company or selling shares of another company which was cofounded by the company he invested in. This might not be repeated next year. Thus, one of the benefits of reading the annual report is to know whether the text is compatible with the stated financial figures and make sure that they both offer a clear exact image of the company's performance and its future prospects.

### *Annual Report Contents*

The annual report provides detailed information on the company's business and performance as well as future performance pre-



dictions. The report usually begins with the chairman's statement that summarizes the

most prominent achievements in the preceding year. After that, it includes general future expectations for the company in the upcoming year.

The annual report contains the following sections:

- An introduction that describes the company's general philosophy in running its business.
- An overview or detailed reports on each part of the company's operations.
- A glimpse of the financial aspects of the company. It includes net income and sales, stocks profit, and the market value of the company.

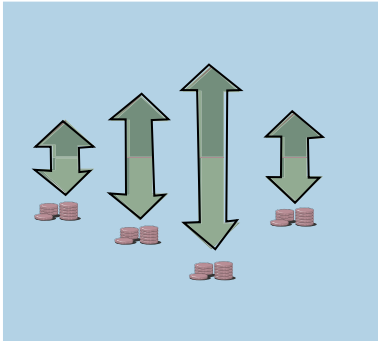
- A balance sheet that indicates the company's assets, liabilities and shareholder's equity at the end of the year in comparison to the previous year.
- An income statement that shows the company's profitability including last year's expenses and revenues compared to previous years.
- A cash flow statement that explains the cash flows from and into the company during the year compared to previous years.

#### *The Annual Report's Introduction*

One of the golden rules in investments is to avoid investing in a company the business of which is not fully known to the investor or he does not have any idea about the sector it operates in. The best place to look for these aspects is the introduction of the annual report.

The introduction is often extensive rather than being an introductory insight on the company's performance in the past year. The introduction gives a historical glimpse of the company, its basic business, and then a general outline on the company's structure. For

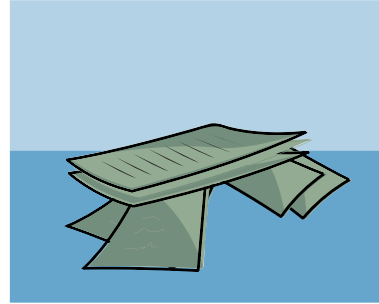
example, the report refers to the size of the company and its activities, and whether a variety of other establishments come under the same corporate name, or whether it is composed of a limited business that does not go beyond one or two production units.



The report also explains the business strategy of the company, or what is sometimes called the company's vision, that answers the following:

- How ambitious are the company goals?
- Does the company have any plans to achieve its goals?
- Which business does the company engage in and commit to?

The answers to these questions can be found in the introduction while the other chapters of the report include all the supporting evidence.



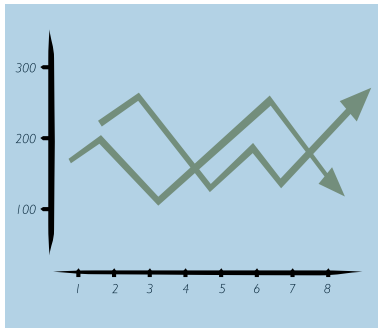
### *Chairman's Statement*

The chairman's statement is a message from the highest power in the company often sent to its investors. In this part of the report, the chairman gives some evidence in examples and numbers to prove what was mentioned at the beginning. In the opening of the statement, the chairman focuses on the strengths of the company and his quest to assist investors in understanding and interpreting the figures included. He will, for example, explain the reasons behind the increase and decrease in past year's revenue compared to the previous two years. The chairman will explain in his statement the direction in which the company will go on based on its vision or he would detail the goals and objectives that are going to be achieved. For example, the chairman indicates whether the company is going to

change its business strategy, expand its main business circle, concentrate on one of its other sub-businesses or make a huge investment; all these issues are usually highlighted by the chairman. It is a norm that the chairman is the one who takes full responsibility if the company could not achieve these goals.

### What Should be Taken into Account in the Chairman's Statement

The investor should take into account, and pay attention to what the chairman has to say regarding the expected challenges and competition, or the threats the company may face. He should also identify the strategy prepared to face such risks, and will these risks lead the chairman to adopt more conservative vision or expectations next year?



## Financial Indicators

The annual report's section on financial indicators shows the figures that reflect and highlight the strengths of the company's performance. For example, if a company had a big rise in sales last year which led to hitting a record level in net profits, then all this information would be documented and highlighted in this section of the annual report. Examples of the information that can be gathered by reading the section on financial indicators include: increase in earnings per share, increase in the company's market value as a result of the increase in the shares value or the decrease in the operating expenses and so on.

If the company had a bad fiscal year, the investor probably would not find any indication to that in the financial indexes chapter in the annual report. The investor should not expect the company to release any negative information on the figures of the financial operations in the section on financial indicators. If the investor is trying to identify the vulnerabilities in last year's financial performance, he has to rely on self-skills in reading the financial indicators or

in considering the figures and graphs that illustrate the company's performance in the past five or ten years.

## *Overview on the Company's Activities*

It is difficult to describe all the operations of a huge company to explain how it runs its operations and the reasons behind choosing these approaches in management in just a few pages of the annual report. Nevertheless, the investor might find some of this in the overview on the company's businesses section.

In this section of the report, the company describes its business operations and procedures in detail which some might regard as boring sometimes. For example, when reading the annual report of an industrial company, this section will explain the manufacturing steps the product goes through, how they affect the operating expenses, especially by mentioning the nature of the material used in manufacturing, and the issues related to supply and demand for the material or the final product.

The investor who has a previous good knowledge on the sector that the company belongs

to, will definitely benefit from the information mentioned in this section. However, when he is not aware of the company's business mechanisms, then the section of the annual report discussing on the overview of the company's businesses along with its new topics will make him curious to look for more to have a good idea on the company's business.

## *Prospectuses*

### *1. Securities Offering Prospectus*

A prospectus is an official document required by the CMA for offering securities. The CMA does not allow the initial public offering (IPO) of any security unless this prospectus is presented and fulfilled all the requirements and conditions set by the Listing Rules. The prospectus includes an adequate description of the company issuing these securities and those going to be offered as well as a detailed description of the company's financial position or any other information required by the CMA.

Since the prospectus is a legal document, it has the highest levels of transparency. Issuing companies tend, by regulatory controls, to state all the information and facts

that ensure that there is no uncertainty for those investing in the company in its IPO.

The Capital Market Authority (CMA) reviews the prospectus before approving it to make sure that all the necessary information is there, and to indicate all the expected risks in the security to be issued, which can be adequate for the investor to make an investment decision. Civil responsibilities, (the victim's right to compensation) resulting from the lack of accuracy of the data mentioned in the prospectus or the omission of some information that should be stated, are usually bared by the company issuing the securities and its senior executives, board members and the financial advisor, who all have been identified in the prospectus.

Reading the prospectus a joint stock company prepares when going public might not be interesting, but it definitely gives the investor a lot of information on the company's goals, plans and financial position. The most important part when reading this document is that the investor can differentiate between all the information mentioned in all prospectuses

and those discussing the quality aspects of the company itself.

When looking at the company's aspects of quality, the investor should concentrate on the section where there is a description of its business and the kinds of products or services it offers in addition to the expected risk factors as well as an analysis of the competitive advantages in its markets.

The investor should also examine the future strategic goals of the company and its plans to reach these goals. After having a look at the data, he can decide how suitable is the company's business scope for his investment goals. He can also form his own vision on the company's potential to achieve its goals. When discussing the risks that might encounter the company, the investor should know the kind of operating risks, especially the ones related to sales in the market it operates in, and whether the nature of this market helps it in reaching its goal.

We should not forget the risks related to the



sector in which the company operates. One of the common questions in this area is when the investor asks if the company can have secure raw materials for its products at competitive prices, and the availability of these raw materials. He would also ask about the level of competitiveness among the companies within the same sector.

One of the things that an investor should be extra cautious about is that all the data written in the prospectus are expectations and predictions that are based on certain hypotheses. There is nothing that can guarantee that all or some of these predictions will happen, even if the company reached the expected level of sales and profitability.

The investor should check the financial risks related to the company which come under the section on the financial statements in the prospectus. He can calculate the company's significant accounting percentages to have an idea about the level of these risks. The fourth awareness booklet published by the CMA "Reading Financial Statements" can help in calculating such risks.

## 2. *Investment Funds' Prospectuses*

Financial markets' commissions or authorities require the issuers of investment funds to have special prospectuses for each investment fund accordingly. They are not allowed to receive the investors' money until the CMA approves their prospectuses. The prospectus should explain the necessary information regarding the level of risks related to the investment products in which the fund invests in. It discloses the investment products of the fund and whether it invests in stocks, bonds, money, commodities, or a combination of them all. It also explains the fund's policy and goals, and whether it maintains its capital or allows the possibilities of exposing the capital to the profit and loss risks.



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