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Influence of Corporate Information Transparency on Foreign Institutional Investors' Shareholding Behavior: Evidence from Public Listed Companies in China

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Abstract: In 2003, China implemented the Qualified Foreign Institutional Investor (QFII) system, which has garnered considerable interest from international institutional investors in the mainland market. As global investors, QFIIs depend significantly on precise, thorough information to bolster their investing criteria. Consequently, the transparency of corporate information becomes a crucial factor for QFIIs, as they prioritize well-disclosed information in their investment strategies. However, due to the relatively late development of the Chinese market, an imbalanced structure of listed companies, and information asymmetry, the information disclosure of listed companies has been subject to certain degrees of distortion. This can hinder the effectiveness of the QFII system. Therefore, to better facilitate the development of China's securities market and to help QFIIs fully realize their advanced value investment strategies, this paper aims to study the impact of corporate information transparency on the stockholding behavior of foreign institutional investors. This paper begins by reviewing the literature on the factors influencing institutional investor holdings, corporate transparency, and the characteristics of foreign institutional investors' stockholding. It then defines the concepts of corporate information transparency and foreign institutional investors, analyzes the current state of information transparency in Chinese listed companies, and examines the development of the QFII system in China. The theoretical framework explores the mechanisms through which corporate information transparency influences the stockholding behavior of foreign institutional investors. In the empirical analysis, the paper plans to measure the information transparency of listed companies from three perspectives: earnings quality, information ratings by the Shenzhen Stock Exchange, and the number of analyst followings, to investigate how corporate information transparency influences QFII stockholding behavior.

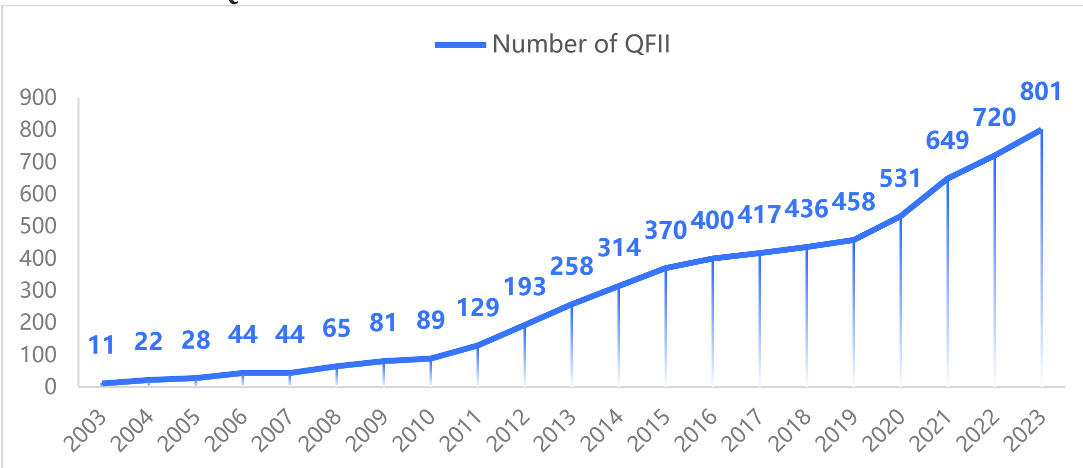
Keywords: *Corporate Information Transparency, Foreign Institutional Investors' Shareholding Behavior, QFII.*

1. Introduction and Background

In response to the requirements of rapid economic growth, the coexistence of a weakened securities market, and the need to open China's capital account, the Qualified Foreign Institutional Investor (QFII) program was implemented in 2003 as a transitional measure in China's capital markets. It aimed to allow foreign institutional investors to participate in the domestic market. In July 2003, the Union Bank of Switzerland completed the first foreign investment in A-shares through the QFII program, signifying the official participation of QFII in China's securities market. Over the past 20 years, China's QFII system has undergone various stages of development, from its introduction and improvement to maturity, gradually emerging as one of the most important institutional arrangements in the Chinese capital market. As time passed, the QFII program gained popularity thanks to favorable policies and the bullish market conditions in China. By 2011, QFII accounted for 1.07 percent of the A-share market, with total assets reaching 265.5 billion yuan. In July 2012, the China Securities Regulatory Commission (CSRC) introduced new regulations that expanded the investment scope for QFII and raised the ownership limit from 20 percent to 30 percent. Subsequently, in January 2019, the State Administration of Foreign Exchange (SAFE) increased the QFII investment quota to $300 billion. In September 2019, the quota restrictions were eliminated, allowing QFII investors to operate without single-investment quotas and approvals. As of December 2021, a total of 670 institutions outside mainland China have obtained QFII qualifications, with QFII holdings amounting to 284 billion yuan.[1] As shown in Figure 1, as of 2023, the number of QFII has reached 801. It is important to note that the primary objective of the QFII program was to mitigate the impact of capital flows on the domestic market and promote efficient resource allocation. However, for the program to effectively achieve these goals, it is imperative to provide QFII investors with comprehensive and transparent company information to facilitate informed decision-making and investments.

[1] https://www.news.cn/fortune/2022-08/25/c_1128944897.htm

Figure 1: The number of QFII from 2003 to 2023



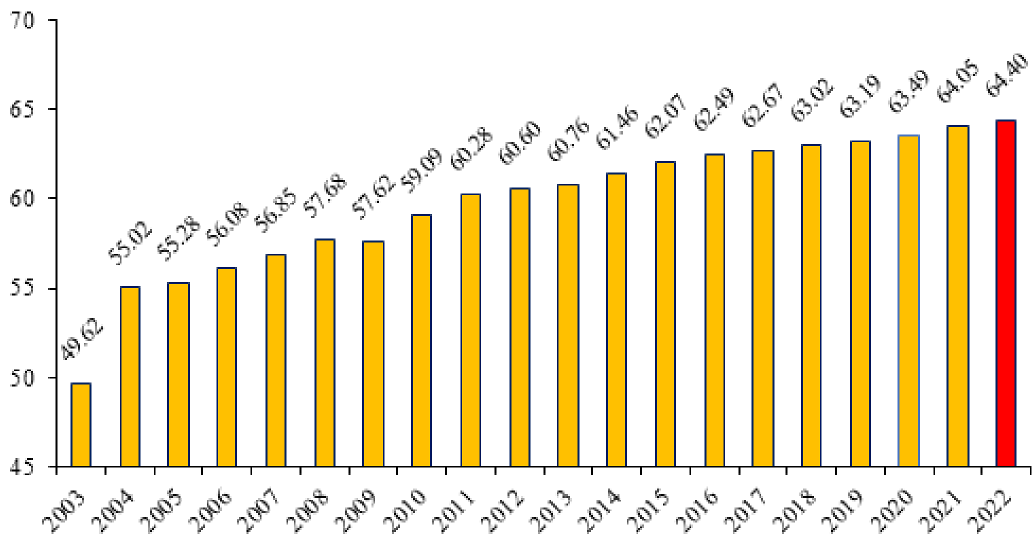
Information disclosure bridges the gap between listed companies and the capital market. With the increasing number of institutional investors, including QFII, in the Chinese market, there is a growing demand for higher-quality information disclosure. These investors have evolved from passive recipients of disclosed information to actively participating in corporate governance. Therefore, the transparency of company information has become increasingly significant.

The market has developed rapidly in the 32 years since China's securities market was established. To regulate market behavior, China has successively promulgated laws and regulations such as the "Company Law" (1993), "Securities Law" (1998), "Interim Measures for the Administration of Stock Issuance and Trading" (1993), and "Corporate Governance Guidelines for Listed Companies" (2002). These legal frameworks have regulated corporate governance and corporate activities related to capital markets. Compliance with these regulatory arrangements is reflected externally through the financial information enterprises disclose. While improving corporate governance in China, these institutional arrangements can also be considered macro-level regulatory norms for information disclosure by listed companies, which is crucial for enhancing corporate information transparency.

Following the initial PricewaterhouseCoopers' opacity index survey, Kurtzman Group (2004) and the Milken Institute (2006 and 2008) conducted surveys evaluating opacity indices in various countries. These subsequent surveys expanded to include most developing countries and measured fundamental changes in these economies. These surveys revealed two important situations regarding China's overall transparency; over time, China's overall information environment has gradually improved. Between 2004 and 2009, China's opacity index decreased from 50 percent to 42 percent, and this improvement was primarily attributed to improvements in China's regulatory and legal environment and the implementation of specific audit requirements. Second, despite China's improved overall information environment, the 2009 survey results showed that China ranked 38th out of 48 countries regarding information transparency. Specifically focusing on accounting and financial reporting transparency, it can be observed that between 2004 and 2009, China made significant progress in the opacity score for "accounting and financial disclosure," decreasing from 56 percent to 40 percent. This improvement resulted from the overall global trend of increasing transparency over the past decade. Second, despite the decrease in the opacity index, China's 40 percent accounting opacity index in 2009 still ranked it the fourth-worst country among the 48 surveyed regarding accounting opacity. The three countries ranking below China were Colombia, Saudi Arabia, and Nigeria. In comparison, other major emerging economies had accounting opacity scores of 26 percent for Russia, 29 percent for India, and 36 percent for Brazil, while the opacity score for Hong Kong was as low as 1 percent (Piotroski and Wong, 2012) .

Since 2004, the Research Institute of Corporate Governance at Nankai University has constructed the Corporate Governance Index for Chinese Listed Companies based on the evaluation results of publicly disclosed information of listed companies, drawing upon relevant research findings. Among the components of this index is the Information Disclosure Index for Chinese listed companies; as illustrated in Figure 2, from 2004 to 2022, the level of corporate governance in Chinese listed companies has steadily increased, with an overall improvement of 29.8 percent. This outcome indicates that the governance structure of Chinese listed companies has been largely established, and the current phase involves refining governance mechanisms and gradually enhancing governance effectiveness.

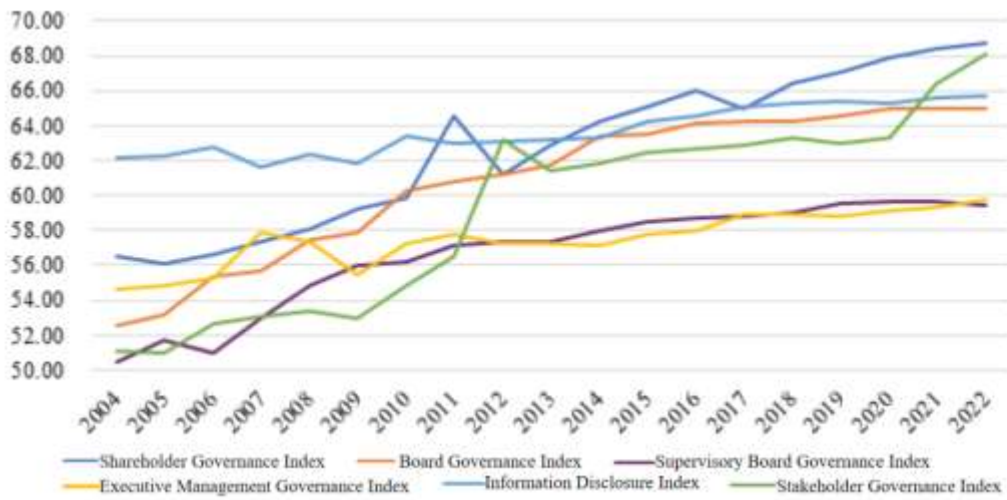
Figure 2: Trend of Corporate Governance Index from 2003 to 2022



Based on a 20-year evaluation spanning a cumulative sample of 46,982 companies, it is evident that the overall standard of corporate governance among listed entities has steadily advanced. Following the setback triggered by the 2008 financial crisis, the average corporate governance index of listed companies has shown a consistent annual increase, reaching a new pinnacle of 64.40 in 2022, marking a substantial 14.78-point surge from 49.62 in 2003. Over the past decade, privately held listed companies have outpaced their state-owned counterparts. State-owned listed firms must further incorporate market mechanisms, elevate their economic governance proficiency, and refine the distinctive modern Chinese corporate framework.

However, as depicted in Figure 3, the Information Disclosure Index has shown relatively slow growth compared to the other six sub-indices. In 2022, the mean disclosure index for Chinese listed companies stood at 65.74, marking a 0.14-point ascent from the previous year. Assessing the three disclosure sub-indices, the authenticity average stood at 65.37, relevance at 65.44, and timeliness at 67.08. Authenticity witnessed a 0.15-point upsurge, primarily driven by the heightened compliance costs from the December 2020 release of delisting regulations. This resulted in a reduction of 152 companies with non-standard audit opinions and an 8.79 percent decline in companies with anomalous profit margins. Relevance experienced a 0.25-point increase, chiefly attributable to a 69.78 percent surge in companies disclosing research and development investment information and an 11.04 percent rise in asset and liability composition disclosures. Conversely, timeliness registered a 0.07-point decline, largely due to adverse economic conditions, manifesting in a 20 percent increase in delayed annual reports from loss-making companies and a 2.37-fold surge in companies penalized for significant delays.

Figure 3: Trends of the six major sub-indices of corporate governance from 2004 to 2022



In summary, while China's information environment has improved over the years, the overall transparency, i.e., the level of information disclosure by Chinese listed companies, remains a cause for concern. Issues such as information distortion and insufficient regulatory enforcement continue to be the main challenges faced by the quality of information disclosure in China.

From existing literature on QFII research, scholars have delved into issues related to the QFII system (Bekaert & Harvey, 2001; Zeng, 2009), QFII shareholding and corporate governance (Gillan & Starks, 2003; Hartzell & Starks, 2003; Almazan, 2005; Luong, 2017; Lel, 2019), company performance (Sun & Lin, 2006; Ye, 2009; Tang & Song, 2010; Wang, Fang & Liu, 2013; Zeng & Zhu, 2019), and relationships with securities markets (Sun & Lin, 2006; Schuppli & Bohl, 2009; Rao, Xu, Mei & Liu, 2013; Sun, Pan & Li, 2017). The conclusions drawn from these studies are thorough and mature, reflecting the increasing attention given to QFII from external stakeholders and underscoring its growing role in driving capital market development.

In the realm of research exploring the relationship between corporate transparency and institutional investors, considerable discussions have taken place within the academic community. Prior studies show that when making global asset allocation decisions, foreign institutional investors consider the degree of corporate transparency shaped by country-level disclosure requirements and firm-level financial reporting choices (Aggarwal et al., 2005; Leuz et al., 2009). Domestically, scholars argue that the current information disclosure practices of listed companies in China fall short of meeting the requirements of institutional investors. Institutional investors necessitate comprehensive, timely, and reliable company information for their analyses and investments (Jiang 2004; Pan & Xin, 2004). Furthermore, scholars have identified that the proportion of institutional investors' holdings tends to increase with improved information transparency (Jiang, 2004; Hong & Fang, 2005; Lu, 2006; Gao, He & Huang, 2006). In international research, empirical studies have indicated that within the internal environment, foreign institutional investors are inclined to invest in companies characterized by high-quality accounting information, high information transparency, and robust corporate governance (Leuz et al., 2009; Bae & Goyal, 2010). Some scholars believe that the more transparent a company's information is, the higher the proportion of institutional investors holding its shares (Healy et al., 1999; Bushee & Noe, 2000). Aggarwal et al. (2005) found in her study of institutional investors in the United States that they tend to prefer holding stocks of listed companies with higher transparency levels. Manogna (2021) surveyed the Indian market, examining how corporations improve their transparency and corporate governance structure to attract foreign institutional investments.

In China's domestic research landscape, more research needs to explore the impact of corporate information transparency on QFII holding behaviors. Xin (2014) studied the investment style of QFIIs from multiple perspectives, including corporate liquidity, fundamental information, and historical operational performance. The research found that QFIIs tend to hold stocks of listed companies with high transparency, high profitability, and low financial risk. Li (2018) found that QFII holdings significantly improve the quality of information disclosure by companies. Moreover, QFIIs can further enhance the quality of information disclosure by already well-governed companies by increasing the number of analysts tracking the company and by linking executive compensation to performance sensitivity. Zhao et. al. (2024) discovered a positive correlation between the proportion of independent institutional investors and the quality of information disclosure by listed companies. Interestingly, they found that as the proportion of non-independent institutional investors holding shares increases, the quality of information disclosure by listed companies tends to deteriorate. Zhou and Wang (2013) conducted a study indicating that foreign shareholders positively influence the quality of accounting information.

In domestic research, there needs to be more comparative analysis on the impact of corporate transparency on QFII shareholding behavior. When investing, QFIIs require access to complete and reliable market information. Only in markets with high transparency and where company information is fully disclosed can QFIIs effectively leverage their rich experience, advanced concepts, and mature technologies to inform investment. To summarize, scholars from both domestic and international contexts have conducted extensive research on the relationship and mutual influence between corporate transparency and institutional investors. This body of research confirms that institutional investors, characterized as more professional and rational, rely heavily on a wealth of objective company data, including annual reports and securities analyst data when conducting market analyses. Additionally, it affirms that enhancing corporate information transparency encourages institutional investors to amplify their investments. However, the existing literature often concentrates on comprehensive studies of institutional investors, with limited dedicated analysis specifically for QFII. Recognizing the significant differences between QFII and other types of investment institutions, it is inappropriate to make sweeping generalizations. QFII, as a globally recognized investment institution, adheres to the principle of value growth. Moreover, due to regional distinctions, QFII is less susceptible to the country's policies where the invested enterprises are located. From the perspective of QFII, there is a compelling need for a distinct study (Wei, 2021).

This article seeks to draw inspiration from foreign literature and, within the institutional framework of China, examine the influence of corporate information transparency on QFII investment behavior.

2. Literature Review

Influencing Factors of Institutional Investor Shareholding: Over the past few decades, foreign securities markets' rapid growth and maturation have created an optimal investment environment for institutional investors. As of 2003, statistics reveal that the assets of institutional investors in developed countries, primarily the United States and the United Kingdom, have surpassed their respective GDP. In mature markets, institutional investors from developed countries account for over 70% of the market share. Consequently, foreign scholars have conducted extensive and mature research on institutional investors, examining the preferences and influencing factors affecting institutional investor shareholdings.

Foreign scholars have identified key characteristics that attract institutional investors, such as companies with robust profitability (Badrinath et. al, 1989), low stock price volatility, and a lengthy listing period (Gompers & Metrick, 2001). Additionally, research on fund shareholding has shown that funds exhibit distinct preferences, favoring stocks of listed companies with high-quality information disclosure and strong liquidity (Falkenstein, 1996). Empirical studies have further analyzed characteristics of fund shareholding, considering factors like stock quality, company size, establishment duration, stock liquidity, and earnings quality, all of which vary based on the distinctive features of different institutional investors (Del Guercio, 1996). Besides these characteristics, institutional investors' preferences are also influenced by a company's reputation, which favors reputable companies with high dividend payments and attention to forecasted earnings standard deviation (Eakins et. al, 1998).

While foreign research has extensively explored institutional investor preferences and influencing factors, the domestic landscape in China, with the introduction of the QFII system in 2003, is still evolving. Domestic scholars have primarily focused on examining the influencing factors of fund shareholding, finding significant impacts from characteristics such as earnings per share, net assets, stock volatility, stock price, stock turnover rate, company profitability, and internal governance (Wang & Xiao, 2005; Hu & Wu, 2004; Hu et al., 2024; Song et al., 2013). Notably, domestic scholars have also highlighted institutional investors' preference for stocks with high information transparency, emphasizing that institutional investors tend to favor companies with transparent information and selectively avoid companies with characteristics such as high risk, complex management structures, and high insider ownership ratios.

Shareholding Preference of Foreign Institutional Investors: Since introducing the QFII system in China in 2003, marking the allowance of overseas investors to engage in the stock market under certain conditions, QFII has evolved into an indispensable participant in the Chinese market. With several increases in QFII investment quotas, the growing number of QFII participants and the substantial funds they bring have made them integral players in the domestic market. QFII, as a foreign institutional investor in the Chinese context, possesses a lengthy investment history and diverse investment methods, with activities spanning global financial markets. Consequently, the investment preferences of QFII have garnered attention from scholars both domestically and internationally. Existing literature reveals two primary approaches in foreign research on QFII.

The first approach empirically tests QFII investment preferences using data from foreign institutional investors in specific financial markets. Scholars examine factors influencing foreign institutional investor shareholdings by analyzing data on their holdings in a particular financial market during a specific time frame. For example, studies on the Japanese market found that foreign institutional investors tend to favor companies with high market capitalization, low financial leverage, and high accounting quality (Kang, Stulz, 1997). Similarly, research on the Swedish stock market suggests that foreign investors are interested in internationally recognized, large-scale companies, showing reluctance to invest in companies where the largest shareholder holds absolute controlling power (Dahlquist et al., 2003). Comparative studies between different markets, such as Japan and Korea, have also yielded similar conclusions, with foreign investors showing a preference for stocks with larger market capitalization and lower book-to-market ratios (Ko et al., 2007).

The second approach primarily focuses on studying the investment preferences of institutional investors from developed countries (e.g., the United States) in foreign markets. This type of research emphasizes the impact of the external environment in foreign markets on investor protection (mainly legal protection) and the influence of corporate information disclosure quality on foreign investor investments. Scholars have found that due to information asymmetry, foreign investors prefer to invest in locally headquartered companies (Coval, Moskowitz, 1999).

In comparison, since the introduction of the Qualified Foreign Institutional Investor (QFII) system in China, domestic research has primarily focused on the impact of the QFII system on the Chinese market, comparing the QFII system domestically and internationally and addressing potential challenges posed by QFII. Additionally, studies on QFII investment preferences within the domestic academic community have mostly relied on qualitative analyses. These studies have found that QFII-held stocks exhibit stable performance, strong profitability, and the ability of QFII to adjust based on economic and industry cycles, showcasing remarkable industry insights (Sun and Lin, 2006). Liu, Bredin and Cao (2020) investigate the dynamic investment preference of QFIIs. The results indicate that total QFIIs prefer more recognized firms with low liability levels, large size, high turnover ability, and state-owned.

Existing studies on foreign institutional investors' investment preference, the home bias hypothesis argues that foreign investors have less local knowledge than domestic investors (Kang & Stulz, 1997; Huang & Shi, 2013; Liu et al., 2020; Roque & Cortez, 2014; Zhou et al., 2019; Ferreira et al., 2017). To overcome this issue, foreign institutional investors prefer to invest in firms with a more transparent information environment (Chou et al., 2014), a good corporate governance structure (Chung & Zhang, 2011; Miletkov et al., 2014; McCahery et al., 2016), firms located in countries with stronger investor protection (Aggarwal et al., 2005), or with higher levels of social trust (Jin et al., 2016). Besides, foreign investors will choose a concentrated investment strategy to reduce information processing costs (Kang & Stulz, 1997; Fedenia et al., 2013; Liu et al., 2020).

Empirical studies on Corporate Information Transparency: Corporate information transparency encompasses mandatory disclosures stipulated by regulations and voluntary disclosures by the company. A comprehensive analysis of these aspects is essential to accurately reflect the company's transparency. Research on corporate transparency has been a focal point in the study of corporate governance, primarily examining the factors influencing information transparency and the economic consequences of corporate disclosures.

International research studies have focused on both external and internal factors. At the national level, scholars have found that cultural factors such as national hierarchies and risk tolerance (Gray & Vint, 1995), legal systems (Jaggi, Low, 2000; Hope, 2003), and foreign trade (Khanna, Palepu, et al., 2004) influence corporate disclosures. In studies comparing accounting information across different countries, it has been observed that in common law countries, the resolution of accounting information asymmetry through open and timely disclosures is key to the robustness of accounting information compared to civil law countries (Ball, Kothari, et al., 2000). Ball et al. (2016) found that the accounting policy environment impacts the quality of information transparency.

At the corporate level, empirical studies have revealed that companies disclose information around six months before issuing stock (Lang & Lundholm, 2000) and focus on revealing management earnings forecasts during mergers and acquisitions (Brennan, 1999). Characteristics such as corporate governance structures and disclosure motivations have also been identified as influencing transparency. Armstrong et al. (2018) suggest that companies can moderately adjust their information transparency, with factors such as financial leverage, whether the company is listed overseas (Hossain, Perera, et al., 1995), and the nature of shareholders (Chen & Jaggi, 2000) affecting corporate disclosures.

In Chinese domestic research, Chinese scholars have primarily focused on the impact of internal corporate governance on information transparency. Studies have found that the quality of voluntary disclosures is influenced by factors such as the ownership concentration of the top ten shareholders, the presence of institutional investors among shareholders (Cui, 2018), CEO duality (Cui, 2018), whether the company issues H shares (Wang & Jiang, 2004), earnings performance (Fan et al., 2014), and the effectiveness of the board of directors (Sun & Zhu, 2014). They also assert that changes in regulatory policies affect the quality of corporate disclosures (Li & Liu, 2018). The potential avenues for improving transparency in listed companies through capital market openness are influenced by external judicial efficiency and optimization of internal corporate governance (Kassi, Li & Dong, 2023). Based on the implementation of the investor field research system by the Shenzhen Stock Exchange, Lin & Ding (2024) found that institutional investor field research improves the financial information quality of listed companies in the current and subsequent years, with higher research convenience enhancing this effect.

Furthermore, studies on the disclosure levels of companies with different ownership structures reveal that state-owned enterprises have better disclosure quality than non-state-owned enterprises. Still, foreign-controlled companies have higher disclosure levels than state-owned enterprises. Among the domestic market, foreign-controlled companies exhibit the highest level of information disclosure (Zhang et al., 2016). In summary, Chinese scholars have predominantly used earnings quality to study and analyze the voluntary information disclosures of listed companies and have yet to explore corporate transparency comprehensively.

Earnings Quality and Foreign Institutional Investors' Shareholding: The quality of a company's earnings is closely related to information asymmetry in the market. Earnings quality is one indicator for assessing corporate information transparency and disclosure quality. Research has shown that if the bid-ask spread is used to measure the degree of information asymmetry among investors, companies ranked in the bottom third for information disclosure quality have bid-ask spreads approximately 50 percent higher than those ranked in the top third (Welker, 1995). This suggests that the poorer the quality of information disclosure under corporate management's manipulation, the lower the information transparency. Therefore, the quality of earnings, as an aspect affecting disclosure quality, can also lead to information asymmetry driven by insider trading, a point supported by many scholars. For instance, Dye (1988) analyzed both internal and external demands for earnings management and concluded that information asymmetry between managers and investors perpetuates earnings management behavior.

Moreover, earnings management exacerbates information asymmetry (Richardson, 1997). Improving the quality of information disclosure can reduce the likelihood of mispricing by investors (Bushman et al., 2004). Studies by Ascioglu (2012) and Bhattacharya et al. (2012) have also explored the relationship between accrual earnings and information asymmetry.

Using data from the Chinese stock market, Zhang (2024) found that lower earnings quality is also associated with higher degrees of information asymmetry in China. With the development of the PI indicator to measure the probability of informed trading, some scholars have incorporated informed trading into their research. Brown and Hillegeist (2007) argued that companies with higher information disclosure quality attract more uninformed traders, reducing the probability of informed trading. Jayaraman (2008), using the PIN indicator to measure informed trading and corporate earnings volatility and cash volatility to measure earnings quality, found that when earnings volatility exceeds cash flow volatility, there is more informed trading, leading to higher information asymmetry. Some scholars have studied the mechanisms behind this relationship. Kim and Verrecchia (1994) discovered that experienced investors have a greater information advantage over companies with poorer earnings quality, exacerbating market information asymmetry. Brown and Hillegeist (2007) believed that higher information disclosure quality could deter investors from actively acquiring private information and reduce the likelihood of informed traders using private information, thereby decreasing information asymmetry. Bhattacharya et al. (2012) found that companies with low earnings quality face higher adverse selection risks and more pronounced information asymmetry, with uninformed traders at a greater disadvantage. Bhattacharya et al. (2012) found that both bid-ask spreads and the PIN indicator negatively correlate with accrual quality, impacting the cost of equity capital. When accrual quality declines, information risk rises, and the cost of equity capital increases. Scholars generally agree on the relationship between earnings quality and market information asymmetry. Regardless of the proxies used or the focus on mechanisms, the consensus is that lower earnings quality increases investor information asymmetry. Thus, higher earnings quality correlates with greater corporate information transparency.

Considering the above analysis, combined with the definition of corporate information transparency, scholars include information about listed companies accessible to external users, such as annual reports and mandatory and voluntary disclosures reflecting company characteristics (Bushman et al., 2004). The most direct basis for QFIIs to judge a company's profitability is the financial condition reflected in the company's public financial statements. High-quality financial reporting indicates good information disclosure quality. In asymmetric information markets, Biddle et al. (2009) posited that accounting information plays a role in reducing information asymmetry, as asymmetric information in the securities market allows company managers or external investors to profit more from selling or buying stocks. However, company managers' comprehensive and effective disclosure of internal information prevents external investors from paying more than the stock's value. Based on the principal-agent problem, effective oversight mechanisms can avoid agency issues, and Biddle demonstrated that high-quality accounting information forms such an effective oversight mechanism.

Their research shows that improving the quality of accounting information disclosure effectively reduces information asymmetry between companies and external investors, alleviates principal-agent problems, reduces investor oversight costs, and enhances investment efficiency. Companies with high-quality earnings typically exhibit characteristics such as consistent and robust accounting policies, appropriate levels of corporate debt, and predictable future earnings. As earnings quality, serving as a channel of information that satisfies both corporate self-interest and the interests of stakeholders centered around investors, increases, its impact on corporate management and investment analysis also grows. Li, Wang, Wu, and Zhou (2021) investigated the influence of QFIIs on internal control quality in China. Their study sheds light on how foreign institutional investors can impact internal control quality, closely related to earnings quality. This suggests that the presence of QFIIs may affect the overall quality of financial reporting in a given market. Overall, these studies underscore the significance of earnings quality in attracting and retaining foreign institutional investors. By enhancing transparency, monitoring earnings management practices, and improving internal control quality, companies can potentially increase their appeal to foreign investors and strengthen their position in the global market (Al-Duais et al., 2022; Lee, 2021; Li et al., 2021). Hence, this study proposes the following proposition:

P1: The higher the company's earnings quality, i.e., the higher the quality of the financial statements and the greater the corporate information transparency, the higher the proportion of foreign institutional investor holdings.

Disclosure Score and Foreign Institutional Investors' Shareholding: In the Chinese mainland market, the

Shenzhen Stock Exchange and the Shanghai Stock Exchange have been rating the information disclosure of all listed companies on their exchanges since 2002, according to the "Listed Company Information Disclosure Evaluation Method." The stock exchanges assess the quality of listed companies' information disclosure from various angles, checking if the disclosure is timely, accurately reflects the company's operational status, is comprehensive and complies with relevant laws and regulations. They also integrate the company's daily operations and trading behaviors for a thorough evaluation, categorizing the quality of information disclosure into grades: fail, pass, good, and excellent. The results of the information disclosure ratings are then published on the Shenzhen Stock Exchange website for market reference, further encouraging listed companies to value transparency and improve their information disclosure quality. The rating by the Shenzhen Stock Exchange has evolved from a general description to a specific grading, distinguishing companies with "excellent" information transparency from those with "fail" quality disclosure.
According to Healy, Hutton, and Palepu et al. (2001), the higher a company's information transparency, the more it can attract institutional investors' attention, leading to more investors willing to invest in it. Therefore, the investment of QFIIs in the mainland market is no exception, and this study proposes:
P2: The higher the company's information disclosure rating, i.e., the greater the corporate information transparency, the higher the proportion of foreign institutional investor holdings.

Analyst Following and Foreign Institutional Investors' Shareholding: Analysts serve as vital information intermediaries in capital markets, deeply engaged in the collection, processing, and dissemination of information. Analysts provide professional earnings forecasts and investment recommendation reports by thoroughly investigating companies' private information, reflecting the intrinsic value of securities to the capital markets. This process helps mitigate information asymmetry and enhances transparency.

Lang et al. (2012), through a study of FAF's historical data from 1985-1989, derived the relationship between company researchers and information disclosure. Their findings indicate that researchers tend to follow companies with comprehensive information disclosure. As a result, their forecasts for these companies are more accurate, and the discrepancies among different researchers' earnings forecasts are smaller. This implies a complementary relationship between the number of analysts and the transparency of a company's information. Better information transparency attracts more analysts, reduces information asymmetry between company management and investors, and lowers the information risk, thereby reducing the risk premium required by investors and increasing the value of the listed company. Jegadeesh and Kim (2006) found that analysts possess more professional analysis capabilities regarding listed companies, enabling them to make more accurate judgments about company information, thus enhancing the depth and quantity of information available to investors. Roychowdhury (2010) concluded that increased analyst attention and tracking can improve internal competition within company management, expanding the breadth and depth of information available to investors. Lang and Lundholm (2000) defined the transparency of a listed company's information environment by the number of analysts tracking the company and the accuracy of earnings forecasts. The accuracy of analysts' earnings forecasts is measured by the absolute difference between the median EPS forecast for the year and the actual EPS, then subtracting this value from the company's stock price. A larger value indicates lower forecast accuracy and lower information transparency.

Bai et al. (2009) examined the impact of company information disclosure policies on the quantity and quality of analyst forecasts, finding that greater transparency leads to more analysts following the company, more accurate earnings forecasts, and smaller discrepancies. Li (2012) used information disclosure evaluation indicators from the Shenzhen Stock Exchange to measure company transparency, discovering that higher transparency attracts more analyst attention. However, more is needed to improve company transparency significantly. Zhou and Wang (2013) posited that analysts can accurately interpret and transmit information released by company spokespeople, thereby enhancing company transparency. Li et al. (2018) found that QFII holdings significantly improve the quality of corporate information disclosure by attracting more analyst attention and increasing earnings sensitivity. The effect is more pronounced when the internal corporate governance and audit quality are higher.

As early as 1990, O'Brien and Bhushan found in their study of institutional investors that companies tracked by more analysts attract more institutional investment. Relevant studies in the U.S. market have also confirmed this view, with Roulstone (2015) and Kepler et al. (2024) presenting mixed evidence on the relationship between components of transparency (such as voluntary information disclosure) and analyst tracking and liquidity. Besides company-initiated disclosures, standardized accounting principles, and auditor choices, information from intermediary institutions likely affects transparency. Analysts collect and aggregate information from public and private channels to evaluate company value, enhancing overall market transparency (Brennan & Subrahmanyam, 1995; Lang & Lundholm, 2000; Lang et al., 2012). Further research found that analysts, as an external governance mechanism reducing information asymmetry, can lower a company's earnings management (Yu, 2008; Knyazeva et al., 2015) and enhance transparency (Lang et al., 2012).

Domestic scholars have also proven that analysts' presence reduces information asymmetry in the capital market (Xu et al., 2010). Thus, for QFIIs, apart from publicly available annual reports for information, they often rely on analyst reports to gather data on company growth and development. The level of analyst attention to a company also reflects its information transparency to some extent. Based on this, this study proposes:
P3: The greater the number of analysts tracking a company, i.e., the higher the corporate information transparency, the higher the proportion of foreign institutional investor holdings.

3. Research Methodology

The sample for this study consists of Chinese A-share listed companies from 2013 to 2023. Data for this study were sourced from the CSMAR, Choice, and Ruisi databases. Additionally, information such as the rating of listed companies on the Shenzhen Stock Exchange was obtained from the Shenzhen Stock Exchange website and manually collected and organized.

Variable Setting: The variable setting is shown in Table 1.

Table 1: Variable setting

Variable type	Name	Symbol	Description
Dependent variable	QFII's shareholding	QHP	The proportion of shares held by foreign institutional investors
Independent variable	Earnings Quality	DD	Using a model adjusted by Francis et al. (2005) based on the Dechow and Dichev (2002) model
	Disclosure Score	DSCORE	The disclosure score issued by the Shenzhen Stock Exchange for companies listed on its exchange
	Analyst Following	ANALYST	The count of analysts forecasting the annual earnings of the company from the disclosure date of the previous year's annual report to the disclosure date of the current year's annual report
Control Variable	Stock Turnover Rate	TUR	Annual Trading Volume / Annual Total Number of Outstanding Shares
	Company Size	SIZE	Natural Logarithm of Total Assets at Year-End
	Leverage Ratio	LEV	Total Liabilities / Total Assets
	Book-to-Market Ratio	BP	Book Value of Equity / Market Value of Equity
	Revenue Growth Rate	GROW	(Current Year Operating Revenue - Previous Year Operating Revenue) / Previous Year Operating Revenue

Model: This study examines the impact of information transparency on the holdings of foreign institutional investors. Following and referencing the model proposed by Bushee (2001), various measures of information transparency are utilized to investigate its effect on foreign institutional investor holdings.

$$QHP_t = a_0 + a_1 TRANSPARENCY_t + a_2 TUR_t + a_3 SIZE_t + a_4 LEV_t + a_5 BP_t + a_6 GROW_t + INDUSTRY + YEAR + e_t$$

In the regression model, TRANSPARENCY represents the measure of information transparency, which includes the previously mentioned indicators of earnings quality (DD), Shenzhen Stock Exchange rating (DSCORE), and analyst coverage (ANALYST).

Descriptive Statistical Analysis: Descriptive statistical analysis will be applied in this study. Observations of key variables in the sample, maximum, minimum, median, mean, skewness, kurtosis, and standard deviation, are all applied in descriptive statistical analysis. Descriptive statistical analysis can analyze whether the sample data is normally distributed and provide descriptive analysis for subsequent analysis.

Correlation Analysis: This study should conduct a Pearson correlation analysis on the model to preliminarily verify the hypothesis. If the correlation coefficients are all within 0.5, it can be assumed that there is no serious multicollinearity. However, if the coefficients are relatively high, a tolerance and variance inflation factor (VIF) analysis should be performed to assess whether the model has multicollinearity issues. In the VIF test, if the VIF values are less than 10 and their tolerance (1/VIF) values are greater than 0.4, it can be concluded that including control variables does not cause serious multicollinearity. Otherwise, multicollinearity is present.

Robustness Test: To verify the robustness of the conclusions, this study plans to use the Heckman two-step method to address data missingness and endogeneity issues. The Heckman two-step method, also known as the Heckman correction, is a statistical technique used to correct for sample selection bias. This method is often applied in econometrics when the sample is not randomly selected, leading to biased estimates. If the coefficient of the IMR (lambda) is statistically significant, it indicates the presence of sample selection bias. This means the selection process affects the outcome variable, and the Heckman correction is necessary. If lambda is insignificant, it suggests that sample selection bias may not be a concern, and ordinary least squares (OLS) regression might suffice.

Endogeneity Analysis: This study plans to use the GMM model to solve the endogeneity of independent variables, lag variables' timing, and individuals' specificity.

4. Conclusion

The research objectives of this paper are to examine the impact of corporate information transparency (earnings quality, disclosure score, analyst following) on QFII's shareholding behavior of publicly listed companies in China. The expected outcome of this paper is that the higher the company's information transparency, the greater the number of shares held by foreign institutional investors. This paper delves into the relationship between QFII shareholding behavior and corporate information transparency, specifically focusing on analyzing QFII to fill the gap in previous research regarding the relationship between corporate information transparency and institutional investors' investment behavior. Thus, this paper's findings will inform regulatory policies and promote corporate governance. Understanding the impact of transparency on foreign shareholding can guide regulators in making more informed decisions on disclosure requirements and investor protection, thereby enhancing market transparency and attractiveness. Findings may encourage companies to improve governance and disclosure practices, as increased transparency could attract more QFII investments, boosting their international competitiveness and market image.

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