AKURASI Jurnal Studi Akuntansi dan Keuangan
p-ISSN : 2720-9067
e-ISSN : 2685-1059
Program Studi Magister Akuntansi
Fakultas Ekonomi dan Bisnis
Universitas Mataram

EXPLORING THE ROLE OF KEY AUDIT MATTERS DISCLOSURE IN MITIGATING INVESTMENT RISK

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INFORMASI ARTIKEL

Article history:
Dikirim tanggal:19/03/2025
Revisi pertama tanggal: 26/04/2025
Diterima tanggal: 24/05/2025
Tersedia online tanggal: 18/06/2025

ABSTRAK

Penelitian ini mengkaji dampak pengungkapan Key Audit Matters (KAM) terhadap risiko investasi dalam konteks transparansi audit Indonesia yang terus berkembang. Penelitian ini dilatarbelakangi oleh implementasi SA701 yang mewajibkan pengungkapan KAM dalam laporan audit. Tujuan penelitian ini adalah untuk menyelidiki bagaimana berbagai aspek pengungkapan KAM memengaruhi persepsi risiko investor. Dengan menggunakan pendekatan kuantitatif, kami menganalisis data lebih dari 700.000 data terkait saham dan 1.358 observasi pada seluruh perusahaan yang terdaftar di Bursa Efek Indonesia (BEI) periode 2022-2023. Hasil analisis regresi menunjukkan bahwa pengungkapan KAM yang mendalam (KAM2) secara signifikan mengurangi risiko investasi, sementara jumlah KAM yang diungkapkan (KAM1) dan informasi moneter (KAM3) tidak menunjukkan efek signifikan. Temuan ini menegaskan pentingnya pengungkapan audit yang kontekstual dan komprehensif dalam mengurangi asimetri informasi. Penelitian ini memberikan kontribusi literatur dengan menekankan peran transparansi audit di pasar berkembang serta menyajikan rekomendasi praktis bagi regulator untuk meningkatkan standar pelaporan KAM.

Kata Kunci: SA701, KAM, risiko investasi, laporan auditor independen, IDX

ABSTRACT

This study examines the impact of Key Audit Matters (KAM) disclosures on investment risk in the context of Indonesia's evolving audit transparency landscape. The research is motivated by the implementation of SA701, which requires KAM disclosures in audit reports. The purpose of this study is to investigate how different aspects of KAM disclosures influence investor perceptions of risk. Using a quantitative approach, we analyze data from more than 700,000 stock data points and 1,358 firm-year observations of companies listed on the Indonesia Stock Exchange (IDX) from 2022 to 2023. Regression analysis reveals that detailed KAM disclosures (KAM2) significantly reduce investment risk, while the number of KAM disclosed (KAM1) and monetary information (KAM3) show no significant effect. These findings highlight the importance of contextual and thorough audit disclosures in reducing information asymmetry. The study contributes to the literature by emphasizing the role of audit transparency in emerging markets and provides practical recommendations for regulators to enhance KAM reporting standards.

Keywords: SA701, KAM, investment risk, IDX, audit report

1. Introduction

The implementation of *Standard Audit 701 (SA 701)*—the Indonesian adoption of *International Standard on Auditing (ISA) 701*—which focuses on the disclosure of Key Audit Matters (KAM) in auditor reports, is a significant development in enhancing audit quality and transparency in financial reporting. This standard aims to improve communication between auditors and stakeholders, thereby fostering greater accountability and trust in financial statements. The implementation of SA 701 in Indonesia became effective on January 1, 2022, marking a significant shift in the country's audit reporting practices. The introduction of this standard aims to enhance the clarity and usefulness of audit opinions by requiring the disclosure of KAM, a change that is expected to influence investor decision-making and improve the overall audit process in the country. The communication of KAM provides investors with insights into the critical aspects of a company's financial health, which can influence their investment decisions. Research indicates that the disclosure of KAM can significantly impact the quality of financial information, thereby enhancing investor confidence in the reported financial statements (Gold & Heilmann, 2019; Matta & Feghali, 2021; Yue, 2022).

Investment risk encompasses the potential for loss or unfavorable outcomes in financial investments, arising from various uncertainties impacting asset valuations. It can be segmented into several categories, including market risk, liquidity risk, credit risk, and operational risk, each presenting unique challenges to investors. Understanding these risks is paramount because inadequate management can lead to severe repercussions for individual investors, financial institutions, and the broader economy, as emphasized by Pfeiferová & Kuchařová (2020). Moreover, risk assessments are vital in investment performance, revealing how systematic monitoring and strategic planning can mitigate adverse effects while enhancing competitiveness (Wulandari, 2021). The complexity and volatility inherent in financial markets indicate that effective risk management strategies, such as portfolio optimization and adherence to informed decision-making frameworks, are crucial for preserving capital and achieving desired returns (Syahyono, 2018).

The role of audits in managing investment risk is pivotal, as they enhance the reliability of financial reporting and foster investor confidence. Auditors evaluate the financial health of companies, thereby ensuring stakeholders have accurate information to make informed investment decisions. This is especially critical in contexts plagued by high uncertainty, where investment managers' strategies could lead to substantial risks without oversight. Effective auditing helps manage investment risk by balancing risk tolerance with expected returns, facilitating improved decision-making within investment portfolios (Khakhanaev, 2019). Furthermore, continuous improvement in risk reporting and internal controls can significantly mitigate financial risks faced by organizations, reinforcing the need for stringent audit processes (Li, 2015). Ultimately, robust audits contribute to a sustainable investment environment by ensuring integrity and transparency, thereby encouraging long-term economic stability and growth amidst inherent uncertainties (Ren & Du, 2020).

The disclosure of KAM in audit reports has become an essential feature of modern auditing practices, with the aim of enhancing transparency and providing greater insights into financial reporting risks. However, despite the growing body of literature on KAM

disclosures, several gaps remain in our understanding of how these disclosures influence investment decision-making and risk mitigation, particularly in emerging markets such as Indonesia. The relevance of KAM is underscored by its potential to direct the attention of users to significant issues encountered during the audit process, which can ultimately influence their decision-making (Sirois et al., 2018). Research indicates that the introduction of KAM in auditor reports has a profound impact on the audit process and the judgments made by auditors. For instance, the inclusion of KAM has been shown to enhance the informational value of audit reports, as they provide insights into the most critical areas of concern identified during the audit (Asbahr & Ruhnke, 2019). This is particularly pertinent in the context of Indonesia, where the quality of audits has been scrutinized.

Existing research has largely focused on the descriptive characteristics of KAM disclosures, including factors influencing their extent and content. Studies by Shao (2020) and Genç & Erdem (2021) provide valuable insights into the determinants of KAM disclosures, such as firm size, auditor characteristics, and audit opinions. Similarly, Segal (2019) highlights the perceived challenges of KAM implementation, raising questions about the actual value these disclosures provide to investors. Despite these contributions, there remains a significant gap in understanding how KAM disclosures specifically impact investment risk, especially in developing markets with distinct regulatory environments and corporate governance structures, such as Indonesia.

Moreover, while prior research, such as the work by Al-mulla & Bradbury (2021) and Yue (2022), has explored the role of KAM disclosures in shaping market behavior and stock price fluctuations, these studies tend to focus on more developed markets like New Zealand and China. There is a lack of empirical evidence from Indonesia, a country with a growing capital market but distinct challenges in corporate governance and financial reporting practices. The Indonesian context, particularly in terms of audit committee influence, the regulatory environment, and the interaction between auditors and investors, presents unique dynamics that have yet to be explored in relation to KAM disclosures.

The literature also lacks a detailed examination of the investment risk mitigation potential of KAM disclosures. While Matta & Feghali (2021) and Kend & Nguyen (2022) show that KAM disclosures can enhance transparency and reduce the expectation gap, their impact on investment risk—measured in terms of stock volatility, risk premiums, or investor sentiment—has not been systematically investigated. Moreover, there is insufficient evidence on whether the specific content of KAM disclosures (e.g., the complexity of the issues disclosed or the tone used) affects investor behavior and, consequently, mitigates risk. The nuanced role of KAM in reducing information asymmetry and enhancing investor confidence in financial statements, especially during periods of economic uncertainty or crisis, remains underexplored.

This research aims to fill these gaps by investigating the relationship between KAM disclosures and investment risk mitigation in Indonesia. By focusing on the impact of KAM disclosures on stock volatility, investor sentiment, and the perception of audit quality, this study will contribute to the literature by providing new insights into the effectiveness of KAM disclosures in emerging market contexts. Additionally, this research will explore how firm-specific factors (such as governance structures and financial health)

influence the extent to which KAM disclosures reduce perceived investment risk, offering a more comprehensive understanding of the value of KAM disclosures in mitigating risk.

Thus, while the literature provides broad insights into the role of KAM disclosures in mitigating investment risks, there is a substantial gap in research focusing on Indonesia. A more in-depth exploration of how KAM disclosures operate within Indonesia's regulatory framework, the behavioral patterns of its investors, and the role of audit committees in these processes is essential for a comprehensive understanding of how KAM can contribute to risk mitigation in emerging markets like Indonesia. This research gap offers an opportunity to extend the existing body of knowledge on KAM disclosures and their potential to promote financial stability and investor confidence in Indonesia.

This paper is organized as follows: the introduction identifies the research gap and the need for studies focusing on Indonesia. The following sections review the literature on KAM disclosures, their impact on investment risk, and the theoretical framework. The methodology outlines the empirical approach to assessing KAM's role in the Indonesian market. The results section presents key findings, and the conclusion summarizes these findings, discusses their implications, and suggests avenues for future research.

2. Literature Review and Hypothesis Development

Key Audit Matters (KAM) are defined as areas of significant risk of material misstatement in financial reports that auditors identify in their audit reports. Grounded in information asymmetry theory (Akerlof, 1970) and signaling theory (Spence, 1973), the inclusion of KAM addresses market inefficiencies by reducing information gaps between auditors and stakeholders. The inclusion of KAM is posited to enhance the transparency of corporate disclosures and ultimately mitigate investment risk. This review examines the existing literature regarding KAM in the context of Indonesia, focusing on how they influence investor behavior and corporate governance.

The accuracy and completeness of financial disclosures are critical for investors in assessing investment quality (Adil et al., 2021; Al-Hadrami et al., 2020). Information asymmetry theory explains how deficient disclosures distort investor judgment, leading to suboptimal capital allocation (Sen, 2020). This lack of transparency hampers effective evaluation and alters investors' incentives to engage with certain markets, including foreign investments. Consequently, a strong disclosure regime, including KAM, can enhance the quality and reliability of reported financial information. KAM acts as signals that counteract this asymmetry, aligning with signaling theory by providing verifiable, auditor-endorsed insights into material risks. Moreover, research indicates that the quality of disclosures can significantly impact investment efficiency. Zhang's study reveals that high-quality disclosure inhibits inefficient investment behaviors by providing a clearer picture of a company's actual performance and risks (Zhang, 2020). Such insights into performance dynamics are crucial for stakeholders, particularly in developing market contexts like Indonesia.

Corporate governance structures play an instrumental role in risk disclosure practices. Research by Maani et al. establishes that the characteristics of audit committees, particularly their independence and experience, strongly influence voluntary corporate risk disclosures (Maani et al., 2024). This supports the assertion that robust corporate

governance contributes to more detailed and effective KAM disclosures, thereby reducing information asymmetry between investors and firms. In the Indonesian context, where governance mechanisms have historically been under scrutiny, the establishment and enforcement of stringent auditing practices, including KAM disclosures, become particularly relevant. Mukhibad et al. (2020) also shed light on how governance mechanisms affect risk disclosures in Islamic banks in Indonesia, suggesting that corporate governance is pivotal in determining the extent of risk information disseminated to investors. As such, KAM disclosure can reflect a firm's governance quality and its commitment to transparency, potentially enhancing investor trust and mitigating perceived investment risks.

Recent studies have begun to evaluate the specific implications of KAM disclosures within the Indonesian auditing framework. Sania & Ali (2024) highlight several factors influencing KAM disclosures, such as the size of the auditing firm and the characteristics of the audited companies. Their findings indicate that as firms increase audit fees, there typically corresponds to an increase in KAM disclosures, suggesting that higher investment in audit quality leads to better disclosure practices. Additionally, Yulianto (2025) provides preliminary evidence linking KAM disclosures and audit report lag, suggesting that timely and comprehensive disclosures may impact regulatory compliance and investor perceptions in Indonesia. The role of KAM in influencing investor behavior has also received attention, as evidenced by the work of Yue, which investigates the effect of KAM disclosures on stock price volatility (Abdullatif et al, 2023). This implies that KAM disclosures could have a direct impact on firm valuation and investor decision-making processes, reinforcing the argument that effective risk communication can mitigate uncertainties associated with investments.

In the context of investment risk, KAM disclosures can mitigate perceived risks by providing a more accurate representation of a company's financial health, highlighting areas of concern that could affect future earnings or company performance. This reduces the "unknown" elements for investors and enables them to assess potential risks with greater certainty. KAM, by clearly identifying material risks and areas of uncertainty in the audit process, helps investors gauge the level of potential exposure to financial misstatements, which could affect investment returns.

The number of KAM disclosed and the level of detail provided in the paragraphs are crucial to the quality of this risk communication. Research has shown that more comprehensive KAM disclosures are associated with lower levels of information asymmetry, which in turn reduces market volatility and risk. For instance, Zhang (2020) argues that clear and detailed disclosures help eliminate uncertainties that investors may have regarding a company's operations or financial status. The disclosure of monetary information related to KAM could further enhance this effect, as it provides specific financial data on the risks being discussed. This type of detailed information allows investors to make more informed decisions, potentially leading to a decrease in stock price volatility, which is often seen as an indicator of investment risk (Longyuan et al., 2022; Mathew, 2011; Segal, 2019).

Moreover, the presence of KAM disclosures can influence the way investors perceive the risk of material misstatement and its impact on the company's financial stability. The

transparency offered by KAM disclosures makes investors more aware of the risks involved in investing in a particular company, allowing them to make more accurate assessments of the company's risk profile. As a result, investors are less likely to be surprised by adverse financial outcomes, and therefore, are less likely to view the investment as risky (Baatwah et al., 2022; Brouwer et al., 2016; Genç & Erdem, 2021; Nguyen & Kend, 2021).

In Indonesia, where financial reporting and auditing standards continue to evolve, the impact of KAM (Key Audit Matters) disclosures may be particularly significant. Emerging markets like Indonesia tend to have less stringent regulatory frameworks and more volatile markets, making detailed audit disclosures especially beneficial for investors in mitigating risk. The study by Sania & Ali (2024) underscores the role of KAM disclosures in Indonesian audits, demonstrating that firms investing more in audit quality tend to provide more detailed KAM disclosures. This finding supports the notion that the extent of KAM disclosure can serve as a critical tool in reducing investment risk by enhancing transparency and providing investors with a clearer understanding of potential financial risks. Based on this reasoning, the main hypothesis is there is a negative association between KAM disclosures and investment risk.

3. Research Method

This study employs a quantitative research design aimed at investigating the relationship between Key Audit Matters (KAM) disclosures and investment risk for firms listed on the Indonesia Stock Exchange (IDX) during the 2022-2023 period. This period aligns with the initial implementation of SA 701 in Indonesia. Crucially, this research examines the entire population of Indonesian publicly listed firms across all market sectors, thereby eliminating sampling gaps and providing definitive baseline data for future studies. The primary focus of the research is to examine whether the level and quality of KAM disclosures have any significant impact on reducing investment risk. Given the increasing reliance on transparency in corporate governance and reporting, it is essential to assess how KAM disclosures, which highlight critical audit matters and significant risks in a company's financial statements, might influence the risk perception of investors. The research utilizes a cross-sectional approach, meaning that the data is gathered from companies at a single point in time over two years (2022-2023). This study uses the ordinary least square (OLS) regression method to test the research hypothesis. This approach allows for an in-depth analysis of the relationship between KAM disclosures and investment risk within a specific timeframe, capturing how these disclosures might influence investors' behavior, perceptions, and decision-making in the short term.

The population for this study consists of all firms listed on the Indonesia Stock Exchange (IDX) during the years 2022 and 2023. In total, there are 951 companies on the exchange during this period. To select the sample, purposive sampling was applied, which is a non-probability sampling technique where the researcher selects specific cases that meet predefined criteria relevant to the research objectives. The criteria for purposive sampling in this study are as follows:

1. Availability of audit reports for 2022 and 2023
2. Availability of stock data for 2022 and 2023
3. Completeness of stock data (stock price available for minimum 6-month data)
4. Average annual stock price is more than 55 (to ensure sufficient stock price variability).

Table 1. Sampling Selection

No	Criteria	Number of Sample Excluded	Remaining Sample
1.	Total population (951 firms for two years)	-	1,902
2.	Excluded due to no audit report for 2022 or/and 2023	238	1,664
3.	Excluded due to no stock data for 2022 or 2023	77	1,587
4.	Excluded due to incomplete stock data for 2022 and 2023	93	1,494
5.	Excluded due to stock price outside range (IDR 50-55)	136	1,358
	Final Observation		1,358

After applying these criteria, the final sample consists of 1,358 firm-year observations. These companies are deemed to meet the requirements for examining the relationship between KAM disclosures and investment risk, providing a robust dataset for the study.

To obtain the necessary data for this research, the author relied on secondary sources, specifically focusing on audit reports published by companies listed on the Indonesia Stock Exchange (IDX). The research utilized the annual financial statements of these companies, which include independent auditor reports. These reports were accessed through the IDX website, providing detailed information on the KAM disclosed in the audit reports.

A total of 1,664 audit reports were analyzed for the years 2022 and 2023. These reports provided insights into the KAM disclosures, including the number of KAM disclosed, the number of paragraphs devoted to each KAM, and any monetary information included in the reports. Each of these elements serves as a proxy for the level of transparency and the quality of risk disclosures. In addition to the audit reports, the study required stock price data to assess the investment risk. The stock price data, covering the same period (2022-2023), was sourced from Google Finance. Over 700,000 stock data points were collected, which were then used to calculate the standard deviation of stock returns, a key measure of investment risk in this study. This large volume of stock data allowed for a robust analysis of how stock price volatility correlates with KAM disclosures.

Table 2. Variable Measurement

Variable Type	Variable	Definition/Measurement	Referenced from
Independent Variable	Key Audit Matters (KAM1, KAM2, KAM3)	Measured by three proxies: 1. Number of KAM disclosed 2. Number of paragraphs dedicated to KAM in the audit report 3. Monetary information disclosed within KAM	*Developed for this study*
Dependent Variable	Investment Risk (RISK)	Measured by the standard deviation of daily stock returns, reflecting the variability in stock prices and uncertainty in the company's future performance.	Originally Markowitz (1952) from (Jogiyanto, 2017)
Control Variables	Audit Opinion (AUOP)	Dummy variable: 1 if the company has a clean audit opinion, 0 otherwise.	(Siagian, 2023); (Alverina & Hadiprajitno, 2022)
	Big 4 Auditor (BIG4)	Dummy variable: 1 if the company is audited by a Big 4 firm, 0 otherwise.	(Alverina & Hadiprajitno, 2022); (Putri & Nursiam, 2021)
	Volume Trading (TVOL)	Measured by the natural logarithm of the daily average of trading volume of the company's stock.	(Septyadi & Bwarleling, 2020); (Setyawan, 2010)

This study uses the multiple linear regression method to test the research hypothesis. The following is a regression model that will be applied to regression analysis:

$$RISK_i = \alpha_0 + \beta_1 KAM1_{i,j} + \beta_2 KAM2_{i,j} + \beta_3 KAM3_{i,j} + \beta_4 AUOP_{i,j} + \beta_5 BIG4_{i,j} + \beta_6 TVOL_{i,j} + \varepsilon_i$$

Where,

$RISK_{i,t}$: Standard deviation of the daily stock returns for firm *i* in fiscal year *t*;
α_0 : Constant;
β_{1-6} : Slope coefficients for each independent/control variable;
$KAM1_{i,t}$: Number of KAM disclosed by the auditor for firm *i* in fiscal year *t*;
$KAM2_{i,t}$: Number of paragraphs dedicated to discussing KAM in the audit report for firm *i* in fiscal year *t*;
$KAM3_{i,t}$: Dummy variable (1 if monetary figures are disclosed in KAM, 0 otherwise);
$AUOP_{i,t}$: Control variable (1 if the audit opinion is unqualified, 0 otherwise);
$BIG4_{i,t}$: Control variable (1 if audited by a Big 4 firm, 0 otherwise);
$TVOL_{i,t}$: Control variable, natural logarithm of the average daily trading volume;
$\varepsilon_{i,t}$: Error term capturing other unobserved factors.

In addition to the primary analysis, this study conducts robustness checks to address potential endogeneity issues and validate the model's reliability. Following Wooldridge

(2013) methodological recommendations, the first robustness test involves re-estimating the model by systematically excluding control variables. Furthermore, the trading volume variable is re-specified using the natural logarithm of the sum of shares traded (instead of average volume) as an alternative proxy. To strengthen the robustness of findings, investment risk is measured using both daily and weekly stock return data, ensuring the results are not sensitive to temporal aggregation biases.

4. Results and Discussions

This research investigates how different aspects of KAM disclosures, such as the number of KAM disclosed, the length of KAM-related paragraphs, and the inclusion of monetary information, influence the perception of investment risk. Additionally, the section explores the role of control variables, including audit opinion, the type of auditor (Big 4), and volume trading, in shaping investor decisions. By examining the relationships between these variables, the study seeks to provide insights into how KAM disclosures may reduce information asymmetry and enhance transparency, thereby helping investors make more informed decisions and mitigating potential risks in the market. The results are interpreted in relation to the existing literature, providing a deeper understanding of how KAM disclosures can influence corporate governance and investment outcomes.

The descriptive statistics presented in Table 3 provide an overview of the variables included in the study, which focuses on the relationship between KAM disclosures and investment risk. The table presents the mean, minimum, maximum, and standard deviation of the continuous variables, as well as the distribution of dummy variables.

Starting with the investment risk (RISK), the mean value is relatively low at 0.0324, indicating that the typical company in the sample shows a moderate level of variability in stock returns. The minimum value (0.005) suggests that some companies have very low stock return variability, while the maximum value (0.086) shows a small number of companies experiencing higher stock return volatility. The standard deviation (0.0151) indicates that there is relatively low variability in the RISK variable across the sample, suggesting that most companies in the sample exhibit similar levels of investment risk.

Table 3. Descriptive Statistics

Variable	N	Minimum	Maximum	Mean	Std. Deviation
RISK	1358	0.005	0.086	0.0324	0.0151
KAM1	1358	0	6	1.32	0.668
KAM2	1358	0	10	2.23	1.231
TVOL	1358	6.559	22.21	14.593	2.807

Dummy Var.	N	0	1
KAM3	1358	234 (17.2%)	1124 (82.8%)
AUOP	1358	11 (0.8%)	1347 (99.2%)
BIG4	1358	964 (71.0%)	394 (29.0%)

Regarding KAM, the three proxies reveal different patterns. The first proxy, KAM1 (the number of KAM disclosed), has a mean of 1.32 indicating most firms report 1–2

KAM suggesting room for enhanced transparency. The standard deviation of 0.668 indicates moderate variability suggesting reasonable consistency in disclosure quantity across firms reflecting divergent auditor practices—while some provide minimal compliance, others offer detailed discussions. The second proxy, KAM2 (the number of paragraphs dedicated to KAM in the audit report), has a higher mean of 2.23 and a more considerable range, from 0 to 10. The higher standard deviation of 1.231 suggests that the length of the KAM-related disclosures varies more widely across companies, reflecting divergent auditor practices—while some provide minimal compliance, others offer detailed discussions. The third proxy, KAM3 (monetary information within KAM disclosures), is represented by a dummy variable in the table. The percentage of companies that disclose monetary information within KAM is 82.8%, indicating that the majority of firms provide some form of monetary information in their KAM disclosures.

For the control variables, Audit Opinion (AUOP) shows that almost all companies in the sample (99.2%) received a clean audit opinion, as indicated by the dummy variable distribution. This suggests a relatively low occurrence of audit qualifications within the sample. Similarly, Big 4 Auditor (BIG4) also demonstrates that the majority of companies in the sample (71.0%) are audited by one of the Big 4 firms, which is consistent with the global trend where large and established companies tend to be audited by major international audit firms. Volume Trading (TVOL), which measures the natural logarithm of daily average trading volume, has a mean value of 14.593 with a standard deviation of 2.807, showing substantial variation in stock trading volumes across companies. The minimum value of 6.559 and the maximum of 22.21 further highlight the diversity in trading activity.

The descriptive statistics provide a clear explanation that while most companies disclose a relatively small number of KAM, there is notable diversity in the depth and content of the KAM disclosures. Additionally, the variables related to investment risk and trading volume display substantial variability, reinforcing the need for further analysis to understand the underlying factors affecting these outcomes.

The correlation analysis in Table 4 provides important insights into the relationships between the research variables. The results show that Investment Risk (RISK) exhibits a weak and negative correlation with the number of Key Audit Matters disclosed (KAM1), which suggests that as the number of KAM disclosed increases, there may be a slight decrease in the perceived investment risk. This finding supports the notion that more detailed KAM disclosures could potentially enhance transparency and reduce uncertainty for investors. However, the correlation is weak (-0.02), indicating that the relationship is minimal.

Further examination of KAM2 (the number of paragraphs dedicated to KAM) reveals a weak to moderate with KAM3 (the monetary information disclosed within KAM), with a correlation coefficient of 0.212, significant at the 0.01 level. This implies that firms that dedicate more paragraphs to KAM are also more likely to include monetary information, indicating a stronger emphasis on providing detailed financial risk disclosures. The correlation between RISK and KAM2 is negative and statistically significant at the 0.01 level (-0.099), which suggests that more detailed KAM disclosures in the form of additional paragraphs could potentially be associated with lower perceived investment risk.

This finding aligns with prior research indicating that transparent and comprehensive disclosure helps reduce information asymmetry, thereby reducing the perception of risk.

Table 4. Correlation Matrix

	RISK	KAM1	KAM2	KAM3	AUOP	BIG4	TVOL	VIF
RISK	1							-
KAM1	-0.02	1						1.067
KAM2	-.099**	.185**	1					1.087
KAM3	-.02	.171**	.212**	1				1.081
AUOP	-.042	-.055*	.05	.024	1			1.010
BIG4	-.316**	.009	.100**	.085**	.04	1		1.016
TVOL	.152**	.086**	-.019	.094**	-.041	.003	1	1.018

Notes: *Correlation is significant at the 0.10 level; **Correlation is significant at the 0.05 level; ***Correlation is significant at the 0.01 level.

The correlation analysis shows that the control variables, AUOP (Audit Opinion), BIG4 (Audit Firm), and TVOL (Volume of Trading), exhibit varying relationships with the primary variables. AUOP has a weak negative correlation with both KAM1 and KAM2, indicating that clean audit opinions are not strongly associated with the level of KAM disclosures. BIG4 shows a significant negative correlation with RISK, suggesting that companies audited by Big 4 firms tend to have lower perceived investment risk. Meanwhile, TVOL shows a moderate positive correlation with RISK, implying that higher trading volumes are associated with increased market uncertainty or risk. The Variance Inflation Factor (VIF) values, all of which are below the threshold of 10, suggest that multicollinearity is not a concern in the model, ensuring that the results from further regression analyses are robust and reliable.

In summary, these correlation results highlight important associations between the variables, particularly the relationships between KAM disclosures, audit opinions, and investment risk. These findings suggest that KAM disclosures and the quality of audit opinions can serve as useful tools in reducing investment risk and enhancing transparency in financial reporting. However, the weak correlation between KAM disclosures and RISK suggests that other factors not captured by this analysis may also play significant roles in influencing investment risk.

To test the hypotheses, we use multiple linear regression to analyze the association among variables. The multiple linear regression analysis underwent rigorous diagnostic testing to validate adherence to classical assumptions. The model satisfied all critical requirements: (1) heteroskedasticity was assessed using the glejser test, confirming constant error variance; (2) normality of residuals was verified via Kolmogorov-Smirnov and Q-Q plot analysis; (3) autocorrelation was ruled out through Durbin-Watson testing, and (4) multicollinearity checks revealed variance inflation factors (VIFs) consistently below the threshold of 10. With all assumptions met, the baseline regression model is statistically robust and fit for inference.

The regression results presented in Table 5 indicate the relationships between the independent variables (KAM1, KAM2, KAM3) and the dependent variable (RISK), along

with the control variables (AUOP, BIG4, TVOL). The Adjusted R-squared value of 0.125 suggests that the model explains only about 12.5% of the variation in investment risk, implying that other factors not included in the model may contribute to the variability in RISK.

KAM1, which represents the number of KAM disclosures, does not have a statistically significant relationship with RISK (t = -0.816, p = 0.415). This suggests that the mere disclosure of KAM in the audit report, in terms of their count, does not meaningfully impact the perceived investment risk, implying that investors may not rely heavily on the number of disclosures as an indicator of risk. KAM2, which refers to the number of paragraphs dedicated to KAM in the audit report, shows a significant negative relationship with RISK (β = -0.001, t = -2.358, p = 0.019). This finding suggests that a higher number of paragraphs allocated to KAM can decrease the perceived investment risk. The detailed explanation of the audit process and the emphasis on specific risks within the company might reduce uncertainty among investors, potentially making the company appear less risky. KAM3, which measures the monetary information disclosed within KAM, does not have a significant effect on RISK (t = 0.371, p = 0.710). This indicates that the financial details shared in KAM, such as the monetary implications of identified risks, do not significantly alter the perceived investment risk, suggesting that investors may not place significant weight on these disclosures when assessing risk.

Table 5. Regression Results

Variables	Coefficients		
	β	**t**	**p-value**
Constant	0.029***	5.963	0.000
KAM1	0.000	-0.816	0.415
KAM2	-0.001**	-2.358	0.019
KAM3	0.000	0.371	0.710
AUOP	-0.004	-0.865	0.387
BIG4	-0.010***	-12.120	0.000
TVOL	0.001***	5.903	0.000
Adjusted R-Squared	0.125		
Durbin-Watson	1.911		
Prob > F	0.000		

The Prob > F value of 0.000 indicates that the overall regression model is statistically significant at the 1% significance level. In other words, at least one of the independent variables in the model has a significant relationship with the dependent variable (RISK). Despite the relatively low Adjusted R-squared, this result from the F-test shows that the regression model can be used to predict investment risk, as the independent variables included in the model significantly contribute to explaining the dependent variable.

Regarding the control variables, AUOP (audit opinion) is not significant (t = -0.865, p = 0.387), suggesting that a clean audit opinion does not significantly affect investment risk. BIG4 (audit firm) shows a significant negative relationship with RISK (β = -0.010, t = -12.120, p = 0.000), indicating that companies audited by Big 4 firms tend to exhibit lower

investment risk. Lastly, TVOL (trading volume) has a significant positive relationship with RISK (β = 0.001, t = 5.903, p = 0.000), suggesting that higher trading volumes are associated with increased market uncertainty and risk.

Table 6 presents the robustness test results, which were conducted by modifying the primary research model through three distinct approaches. Model 1 represents the baseline specification used in the main analysis. Model 2 substitutes the original trading volume (TVOL) control variable with the natural logarithm of the sum of shares traded rather than the average. Model 3 excludes all control variables to assess the standalone effect of KAM disclosures, while Model 4 replaces the daily return standard deviation (the primary investment risk proxy) with a weekly standard deviation measure. The results confirm that KAM2 (paragraph-based disclosure depth) continues to show a statistically significant negative association with investment risk across all specifications ($p < 0.01$), regardless of whether the risk is measured using daily or weekly standard deviations. This consistency persists even after adjusting control variables, though the Adjusted R^2 declines markedly in Models 3–4 (from 0.125 to 0.002–0.008), indicating that the control variables collectively explain a substantial portion of investment risk variability. Notably, neither KAM1 (count of KAM items) nor KAM3 (monetary disclosures) shows significant effects in any model, reinforcing the primacy of disclosure *quality* over quantity.

Table 6. Robustness Test Results

Variable	β (KAM1)	β (KAM2)	β (KAM3)	Adjusted R^2
Model 1	0.000	-0.001**	0.000	0.125
Model 2	0.000	-0.001**	0.000	0.121
Model 3	-0.000	-0.001**	0.000	0.008
Model 4	0.003	-0.003**	0.001	0.002

In summary, while KAM2 (the number of paragraphs dedicated to KAM) has a statistically significant negative impact on investment risk, both KAM1 (the number of KAM disclosures) and KAM3 (monetary information in KAM) do not show a meaningful effect. These findings suggest that the level of detail and context in which KAM are presented (such as the number of paragraphs) plays a more crucial role in influencing investment risk perceptions than the simple presence of KAM or financial figures disclosed within them.

The results show that KAM2 (the number of paragraphs dedicated to KAM in the audit report) has a statistically significant negative impact on investment risk (RISK) at the 5% significance level. Specifically, the coefficient for KAM2 is -0.001, and it is significant at the 0.019 level. This suggests that an increase in the detailed disclosure of KAM in the audit report is associated with a reduction in investment risk. The findings of this study align with prior research emphasizing the importance of KAM disclosures in reducing investment risk. Matta & Feghali (2021) demonstrated that KAM disclosures enhance the understanding of audited financial statements, helping investors make more informed decisions and thereby reducing the audit expectation gap. Similarly, Al-mulla & Bradbury (2021) highlighted the value relevance of KAM, revealing that the detailed disclosure of financial reporting risks aids investors in assessing the underlying uncertainties, thus

lowering perceived investment risk. Gold & Heilmann (2019) further support this view, noting that increased transparency from KAM disclosures improves the quality of financial information, directly influencing investor behavior by fostering greater confidence and reducing market uncertainty. Additionally, Kend & Nguyen (2022) found that during times of crisis, such as the COVID-19 pandemic, KAM disclosures provided crucial information that helped mitigate risks and improved investor trust in audit reports. Together, these studies underscore the significance of comprehensive KAM disclosures in enhancing transparency, fostering investor confidence, and ultimately reducing the risks associated with investment decisions.

In contrast, KAM1 (the number of KAM disclosed) and KAM3 (the monetary information disclosed within KAM) do not appear to significantly influence investment risk, with p-values of 0.415 and 0.710, respectively, both exceeding conventional significance thresholds (0.10, 0.05, and 0.01). This suggests that the mere presence of KAM, as well as the inclusion of monetary details within these disclosures, may not have a sufficient impact on mitigating investment risk from the perspective of investors. One possible explanation for these results is that while KAM disclosures enhance transparency by providing additional insights into audit risks, they may not address the more significant and complex concerns that investors typically consider when assessing risks, such as long-term market volatility, industry-specific challenges, or broader macroeconomic factors.

Moreover, KAM often focuses on past or current audit risks, rather than future uncertainties, which may leave investors seeking more forward-looking information that directly addresses potential financial volatility or external shocks, such as economic recessions or political instability. In addition, the monetary details in KAM (KAM3) may not be viewed as particularly valuable to investors if they do not offer specific insights into the potential financial impact of disclosed risks, or if the context around these figures does not adequately explain the severity or likelihood of the risks materializing. This could lead to the conclusion that the impact of KAM disclosures on investment risk may depend not only on their quantity and content but also on the clarity and relevance of the information provided within them.

In sum, while KAM disclosures are beneficial in increasing transparency, their ability to directly reduce investment risk may be limited if the disclosures do not sufficiently address the broader, more complex factors influencing investor decision-making. Further research could explore the interaction between KAM disclosures and other risk indicators to better understand how investors perceive and react to different types of financial and non-financial risks. This research investigates how different aspects of KAM disclosures, such as the number of KAM disclosed, the length of KAM-related paragraphs, and the inclusion of monetary information, influence the perception of investment risk. Additionally, the section explores the role of control variables, including audit opinion, the type of auditor (Big 4), and volume trading, in shaping investor decisions. By examining the relationships between these variables, the study seeks to provide insights into how KAM disclosures may reduce information asymmetry and enhance transparency, thereby helping investors make more informed decisions and mitigating potential risks in the market. The results are interpreted in relation to the existing literature, providing a deeper

understanding of how KAM disclosures can influence corporate governance and investment outcomes.

5. Conclusion, Implications, and Limitations

This study investigates the relationship between Key Audit Matters (KAM) disclosures and investment risk. The results show that the number of paragraphs dedicated to KAM in the audit report, which reflects the detailed disclosure of KAM, is significantly associated with a reduction in investment risk, supporting the notion that increased transparency in audit reporting helps mitigate uncertainty and perceived risk among investors. However, the number of KAM disclosed and monetary disclosure does not exhibit a significant relationship with investment risk, suggesting that the mere presence of KAM or their monetary details may not be enough to impact investors' perceptions of risk.

These findings contribute to the literature on audit transparency and risk perception, emphasizing that the depth and clarity of audit disclosures are critical factors in reducing perceived investment risk. The results also highlight the complexities of the relationship between audit reporting and investor behavior, suggesting that other factors, such as firm characteristics and market activity, should be considered when evaluating the effectiveness of audit disclosures.

Despite providing valuable insights, this study has several limitations that should be acknowledged. First, the analysis focuses on a specific set of companies within a certain timeframe, which may limit the generalizability of the findings to other markets or periods. The study uses data from Indonesian companies listed on the IDX, and the results might differ in other countries with different regulatory environments or market conditions. Second, while this study controls for several variables, other potential confounding factors, such as corporate governance practices, macroeconomic conditions, and industry-specific risks, could further influence the relationship between audit disclosures and investment risk. Future research could address these limitations by expanding the sample size, considering different market contexts, and incorporating additional variables that could affect the relationship between audit disclosures and investment risk.

Based on the limitations and findings of this study, several directions for future research can be suggested. First, future studies could extend the analysis by incorporating a larger and more diverse sample of companies from different countries or regions, which would provide a more comprehensive understanding of how audit disclosures influence investment risk across various regulatory environments. Second, additional research could examine the role of other forms of audit transparency, such as the quality of the auditor’s opinion or the extent of financial statement restatements, in influencing investor behavior and market outcomes. Finally, future research could investigate the potential moderating effects of corporate governance, firm performance, or market conditions on the relationship between audit disclosures and investment risk, providing further insights into the contextual factors that influence investor decision-making. By exploring these areas, future research can contribute to a more nuanced understanding of the role of audit reporting in reducing investment uncertainty and enhancing market stability.

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