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INTERNATIONAL FINANCIAL REPORTING STANDARDS' ADOPTION AND VALUE RELEVANCE OF ACCOUNTING INFORMATION: A BRIEF LITERATURE REVIEW

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Abstract

This study provides a brief literature on the value relevance of accounting information with IFRS application. High quality accounting standards are required for the purpose of building investor confidence, which in turn reduces cost of capital, improves liquidity and contributes to the efficiency of capital markets. There is a growing literature that links value relevance of accounting information with new accounting standards from different country around the world, but financial reporting standards and requirements differ between countries, which create inconsistencies results among researchers. The aim of this paper is to review empirical studies on this nature and summarizing results. Furthermore, documented whether results are indistinguishable in emerging and matured financial markets. The review considered various studies published between 1999 and 2015 and found IFRS adoption has significant influence on the quality of accounting information but financial reporting standards and requirements differ between countries which create inconsistencies results. More empirical evidence is needed in emerging financial markets as compared to matured financial markets.

Keywords: IFRS, Adoption, Accounting Information, Value Relevance, Literature Review

INTRODUCTION

Accounting literature on value relevance research began in early of 1960 with seminar work of Ball and Brown (1968) who extensively examined relevance of accounting information in order to assess usefulness of accounting information to equity investors. This line of research investigated under capital market based accounting research represents simultaneous testing of relevance and reliability of accounting information (Pervan, I and Bartulovic, 2013).The literature on the value relevance studies is vast and has been studied in many perspectives. For example, seminal work of Miller and Modigliani in 1966 considered as the first study investigated relationship between accounting figures and other financial parameters; they also investigated market values of equity which include cost of capital based in electric utility industry. Value relevance studies also tested whether mandatory or voluntary adoption of IFRS improved quality accounting information.

International Financial Reporting Standards (IFRS) is a set of principle –based issued and established by International Accounting Standards Board (IASB) and generally accepted by different countries around the world to ensure comparability and transparency in accounting practice (Desoky, A and Mousa, G. (2014).The establishment of such standards by IASB aimed at achieving harmonization and promotion of accounting practices to ensure consistency in reporting format across countries which should minimize cost of processing accounting information to investors and improving efficiency of capital markets (Wen et al ,2011).Recently around the world more than 120 countries and reporting jurisdictions required domestic listed companies to prepare their financial statements in accordance with IFRS (Mousa and Desoky (2014).The adoption and implementation of IFRS has been one of the most important events in accounting history of different countries around the world which induce significant changes in the accounting practices (Kousenidis, D.V., et al, 2010).However, changes are found to vary among countries and reported to be more serious in countries that had a code-law accounting system like European counties (Ball et al., 2000).Before implementation of IFRS, existed accounting system affected by severe government and legalistic influences which is in contrast with a common-law accounting system countries like North America (Kousenidis, D.V., et al, 2010). In a common law accounting system there is a proper description of IFRS and accounting is mainly affected by the market practitioners (Ball et al., 2000).With growing adoption and implementation of IFRS by different countries around the world, many researchers aimed to find out empirically whether the new accounting standards has improved relevance of accounting information reported to the users. This review paper presents existing empirical literature tested impact of IFRS adoption on the value relevance of accounting information. In addition, documented whether empirical results differ in matured and emerging financial markets. This review covered a number of empirical studies done by different researchers from different countries around the world and published between 1999 and 2015.Approximately 50 academic empirical articles discussed were primarily selected from well reputable journals, but also comment has been made on important empirical results from other journals.

The following section discuss definition key concepts used in this review and section 3 presenting existing empirical studies tested whether voluntary or mandatory adoption of IFRS improved value relevance of accounting information.

Definition of Key Concepts

This section gives definition of key concepts, which includes meaning of accounting information nature of value relevance research and an overview of IFRS.

Accounting information

Accounting information considered as the best media of communication between company and various stakeholders of the company which assist them in evaluating and knowing performance of organizations (Callao et al, 2007). To facilitate the communicative role of the accounting information which is published in the financial statement, it is required to posses some qualitative characteristics which makes it relevant for decision making by different users particularly investors (Gaston et al, 2010). The decision of investors are said to be qualitative and informed, when published accounting information are of high quality. Also different users of accounting information utilize accounting information to evaluate economic value of companies with the assumption that there is relationship exist between accounting numbers and the market values of companies (Clarkson et al.2011).According to William (1968) accounting information defined as any information obtained from the accounting system of a particular firm and can be shown in a special report, a financial statements or verbal statement. But, for the purpose of this review, accounting information defined as the quantitative written information presented in complete or partial financial statements including balance sheet or profit and loss account or cash flow statement either quarterly or annually (Oyerinde, 2009).

Value Relevance Research

Area of study aimed in examines association between accounting numbers and pricing of financial assets is called value relevance research ((Varun, D, 2014).Research on this area aimed in measuring whether accounting numbers presented in financial statements has ability to capture or summarize information that brought significant influence on market share price or stock returns (Beisland, 2009).According to Franscie and Schipper, (1999) relevance is measured if there is statistical association exist between accounting information and market stock price (stock returns).Value relevance studies classified into three categories by Holthausen and Watts (2001).The first category named as relative association studies, which examine whether there is statistical association exist between stock prices and accounting numbers. Through this category, concept of value relevance is measured by using regression analysis, and for the accounting information with high value of R-squared is considered as more relevant than the others (Oyerinde, A.A. and Olugbenga, A, 2014).Second category is incremental association studies which basically investigated usefulness of accounting information in influencing market values (market returns) given other specified variables (Holthausen and Watts,2001; Oyerinde, A.A. and Olugbenga, A, 2014; Mohamed, Y.A. and Lode, N.A. 2015).By using this category, accounting variable is measured to be relevant by using estimated coefficient from the regression, if the estimated value of coefficient found to be statistical significantly different from zero accounting variable would be considered to be more relevant. For example, a study of Venkatachalan (1996) cited in Oyerinde, A.A. and Olugbenga, A. (2014), investigated incremental association of fair values by using off balance sheet items. In addition, Khanna, M. (2014) investigated incremental association of earnings and book value on market values. Lastly, third category is called marginal information studies, where event study methodology adopted for the purpose of determine whether release of accounting information related with the changes in the value of stock prices. Accounting information would be considered to relevant if the stock prices reacted due to the release of such information. A study of Bayezid, A., and Chowdhury, T.A. (2010) and Menike M. and Wang Man (2013) employed event study methodology for the purpose of investigating reactions of stock price due to the release of annual financial statements.

International Financial Reporting Standards (IFRS)

The term IFRS abbreviated for International Financial Reporting Standards (IFRS) which is considered as a set of principle –based issued and established by International Accounting Standards Board (IASB) and generally accepted by different countries around the world (Desoky, A and Mousa, G. 2014).However former IASs were issued by IASC which is considered as previous IASB (Azeem, M., and Kouser, R. (2011). In accounting history of different countries around the world IFRS adoption considered as the most important events which induce significant changes in the accounting practices (Kousenidis, D.V., et al, 2010). IFRS adoption improved comparability and transparency of financial accounting information disclosed in financial statements and these are two of the four key qualitative characteristics of financial statements that make financial information more useful to the users (Callao et al, 2007).

Before IFRS implementation, existed accounting system affected by severe government and legalistic influences which is in contrast with a common-law accounting system (Kousenidis, D.V., et al, 2010).Evidence provided in the international accounting literature reveals that impact of IFRS adoption involve three elements including the accounting information presented in financial statements, harmonization of accounting practices and efficiency of markets (Callao et al, 2007). For example, Barth (2008) argued that adoption of IFRS improved the function of global capital markets by providing high quality accounting information to investors. Even before IFRS became mandatory to different counties around the world, many firms have voluntarily switched to IFRS and the effects of voluntarily adoption has been identified by different researchers including Dumontier and Raffournier (1998); Cuijpers and Buijink (2005); El-Gazzar et al., (1999) and Lang et al. (2003). Dumontier and Raffournier (1998) examined motivations of Swiss listed companies to voluntarily adoption of IAS. Based on their findings, firms which comply with IAS are found to be larger; more internationally diversified, and also have less capital intensive and have more diffuse ownership. The findings of Cuijpers and Buijink (2005) used a sample of European companies and found no evidence reported for non-local GAAP adopters which lower cost of capital.

EMPIRICAL STUDIES TESTED IMPACT OF IFRS ADOPTION ON THE VALUE RELEVANCE OF ACCOUNTING INFORMATION.

Many empirical studies have investigated whether mandatory or voluntary adoption of IFRS improved value relevance of accounting information or not. This section presents empirical studies based on this nature from matured and emerging financial markets.

The Effects of IFRS Adoption on the Value Relevance of Accounting Information in Matured Financial Markets

This section is designed to presents empirical studies tested the impact of IFRS's adoption on the value relevance of accounting information in developed countries where financial market are well matured. Numerous empirical studies tested whether adoption of IFRS improved relevance of accounting information. For example, Jermakowicz, Kinsey and Wulf (2007) investigated whether adoption of IFRS brought challenges and benefits on the value relevance of earnings and book values of DAX-30 companies listed at NYSE. The analysis of their study based on the annual data which covered a period between 1995 and 2004 and found out that value relevance of earnings and book value significantly increased. The result of Jermakowicz, Kinsey and Wulf (2007) is consistent with Suadiye (2012); Agostino M. et al. (2011); Jermakowicz (2004).Based on their findings, after IFRS adoption value relevance of earnings and book values improved. Similarly, study of Clarkson, Douglas, Richardson and Thompson (2009) investigated whether adoption of IFRS in Europe and Australia has significant impact on the value relevance of book value and earnings by using traditional linear pricing models. Their results reported value relevance of book value and earnings measured under IFRS enhanced comparability and have the same explanatory with local GAAP, inconsistent results reported by Devalle, Onali and Magarini (2010) as value relevance of earnings increased after IFRS adoption in German, United Kingdom and France and book values had increased only in UK and decreased in all analyzed countries.

Also, empirical work of Filip and Raffournier (2010) in Romania and Hellström (2006) in Czech reported an increased on earnings after IFRS regime. However, other empirical studies of Bartov *et al.* (2005), Paananen and Lin (2009), Karampinis and Hevas (2011) report a decreased on the value relevance of both book value of equity and earnings in the period of implementing IFRS, consistent with the study of Ahmed and Goodwin (2006).Another study in Turkey by Bilgic and Ibis (2013) analyses whether adoption of IFRS increased value relevance or not and reported accounting information to be more relevant during the period covered for the study and after the introduction new financial accounting reporting standards. In addition, new accounting standards reported to increase relevance of book values but value relevance of earnings decreased, consistent with Kargin (2013). In Contrast to Bilgic and Ibis (2013); Kargin (2013) a study of Turel (2009) reveals that IFRS implementation in Turkey increased value relevance of earnings but no improvement on the value relevance of book value in post IFRS period.

On the other hand, application of IFRS in Spain does not improved relevance of financial reporting to local stock market operators (Callao et al.2007),similar result reported by Clarkson, Hanna, Richardson and Thompson (2011); Tsalavoutas, Andrea and Evans (2009) In addition, another empirical findings of Gordon et al. (2010)found that, value relevance of earning is not significantly higher under IFRS, consistent with Niskanen et al. (2000) and Morais, A and Curto, J.D (2008).Their results show that, IFRS adoption does not increased relevance of earnings as compared to change in local GAAP earnings. Equally, studies of Schiebel (2006); Hung and Subramanyam (2007) also reported that local German GAAP improved value relevance of accounting information than adoption and implementation of IFRS. Another study done by Gaston et al. (2010) also revealed that IFRS adoption negatively influence value relevance of financial reporting in UK and Spain, although effect is reported to be significant in Spain.

The empirical results of different studies presented in this section are from developed countries where financial market is well matured. Overall empirical results observed that, both book values and earnings improved after IFRS adoption, though in some of studies in US, Spain and German by Gordon et al. (2010); Callao et al. (2007); Hung and Subramanyam (2007) Gaston et al. (2010) reported otherwise and these results are mixed and do not lead to any firm conclusions.

The Effects of IFRS Adoption on the Value Relevance of Accounting Information in Emerging Financial Markets

This section presents empirical results of studies assessed impact of IFRS adoption on the value relevance of accounting information in emerging financial market. More of recent empirical research show some interest in matured financial market where emerging financial markets has been somewhat neglected. Nevertheless, the number of these studies examine in emerging markets is limited. Empirical studies concentrating in China, Nigeria, Iran, Malaysia and United Arab Emirates show mixed results regarding the impact of adopting new accounting standards on the value relevance of accounting information. For example in United Arab Emirates, findings of Alali and Foote (2012) reported earnings per share and book value per share under IFRS are positively and significantly related to market share price per share; the same results reported on the relation between earnings and cumulative returns. However, empirical studies of, Zhu, Zhao, Sun (2009); Wang (2009) suggested otherwise as they found that after the implementation of the new accounting standards, no significant increased on the value relevance of earnings. Similarly, previous work of Khanagha (2011) and Khanagha et al (2011) reported that IFRS application in United Arab Emirates and Iran respectively decreases quality of accounting information. Also introduction of new financial reporting standards in Malaysia bring no effect on the value relevance of earnings, only book value reported to be relevant during IFRS application by Kadri et al (2011).

In China, Wen, Q et al. (2012) also investigate whether 2007 IFRS converged has improved quality of accounting information for investors. The findings their study found earnings per share relative to book value of equity is a stronger explanatory variable of market return in both during the pre- and post IFRS convergence periods. Their results also suggest that in the post IFRS convergence period reliance of investors on accounting information from the income statement information for investment decisions increased. Consistently with previous work of Bao and Chow (1999), Sami and Zhou (2004) and Liu and Liu (2007) as they reported increased on the value relevance of accounting information by using IFRS. However, empirical findings of Haw *et al.* (1999); Eccher and Healy (2000) and Lin and Chen (2005) suggest otherwise as they find that earnings reported in China GAAP are more value relevant to A-share. This study highlight the weakness of IFRS compared to China GAAP which contradicts with Xue, Zhao, Xiao, Cheng (2008).Another study conducted in China by Liu *et al*., (2011) examined the reaction of investors to reporting using the IFRS-converged standards by using a sample of companies issuing A-shares. Based on their findings, immediately after the IFRS convergence financial information becomes more value relevant with the need for less earnings management.

In Nigeria, Adebimpe and Ekwere, R. (2015) empirically examines whether mandatory adoption of IFRS has improved value relevance of accounting information of listed commercial banks in Nigeria stock exchange. The study covered a period of 2010 and 2011 (as pre-adoption period) and 2012 and 2013 (as post-adoption period) and reported that equity value and earnings of banks determined under IFRS are relatively value relevant to market share prices than under Nigerian SAS (old accounting standards).They also found earnings per share to be incrementally value relevant during the period of post-IFRS and book value per share is incrementally less value relevant during the post-IFRS period. Consistent with recent work of Yusuf, A.M and Asma, L.N.(2015) which discussed conceptually concerning adoption of International Financial Reporting Standards (IFRS) by Nigerian financial institutions. They concludes that with the mandatory adoptions of financial reporting under IFRS by all listed financial institutions, the accounting disclosures become more value relevant among Nigerian financial institutions. Another study conducted by Muhibudeen, L. (2015) in Nigeria concluded that following adoption of IFRS in Nigeria improved value relevance of earnings and book value. These studies highlight the weakness of NGAAP compared to IFRS similar to the study of Umoren and Enang (2015).Contrary to the results from Adebimpe and Ekwere, R. (2015); Umoren and Enang (2015); Yusuf, A.M and Asma, L.N. (2015); Zayyad, B, Ahmad and Mubaraq, S. (2014).

In Bahrain, Desoky and Mousa (2014) empirically tested impact of mandatory adoption of IFRS on the value relevance of financial information of 40 listed companies in Bahrain Bourse relative to price and returns models consistent to Alali and Foote (2012).Findings of their study show a slight difference in the value relevance of accounting information after the adoption of IFRS by using returns model. However, in the price model, the findings show some improvement in the value relevance of accounting information after the adoption of IFRS.

In summary, most of empirical findings reported in emerging financial markets are generally consistent with those findings reported in mature financial markets, however some inconsistencies results are evidenced in the number of few studies and warrant further investigation on this area of research.

DISCUSSION OF EMPIRICAL RESULTS

Mandatory or voluntary adoption of IFRS induce significant changes in the accounting practices of different countries around the world (Kousenidis, D.V., et al, 2010),however, the changes are found to vary among countries(Ball et al., 2000). With growing adoption and implementation of IFRS by different countries around the world, many researchers empirically tested whether new accounting standards has improved relevance of accounting information, but financial reporting standards and requirements differ between countries, which creates inconsistencies results among researchers. The literature reveals that, number of empirical studies concentrating in China, Malaysia and Nigeria (in emerging financial market) reported improvement on quality of accounting information after IFRS convergence (Bao and Chow,1999; Sami and Zhou,2004; Chunhui *et al.* (2011); Liu and Liu,2007; Wen,Q et al.,2012; Adebimpe and R. E. Ekwere. (2015). However, other studies such Khanagha (2011); Khanagha et al (2011); Lin and Chen (2005); Eccher and Healy (2000) report decrease. Similarly, no evidenced revealed on the improvement of value relevance of accounting information after IFRS adoption by Zhu, Zhao, Sun 2009; Wang, (2009); Tsalavouts, Andre and Evans (2009).Some of empirical findings reported in emerging financial markets are generally consistent with those findings reported in mature financial markets (Jermakowicz, Kinsey and Wulf (2007); Suadiye (2012); Agostino M. et al. (2011; Filip and Raffournier (2010) and Hellström (2006); Sami and Zhou, 2004; Liu and Liu, 2007; Wen, Q et al., 2012; Adebimpe and R. E. Ekwere. (2015), however some inconsistencies results are evidenced in the number of few studies and warrant further investigation on this area of research. The literature also revealed that, several reasons may lead to such inconsistency including difference in economic and political system between countries, historical background and general context of the country where the studies are carried out could influence the findings, and also rules and regulation of a country also may lead findings to differ. In relation to this, a study of Eccher and Healy (2000) concluded that accounting information determine under IFRS found to be not useful than that prepared under China GAAP. Contrary to Eccher and Healy (2000), findings of Peng *et al.* (2008) suggest improvement on the value relevance of accounting information prepared under IFRS. Improvement in the understanding through different training facilities offered increased in awareness and understanding and efforts made by the government accelerate the findings of these two studies to differ. Similarly, Bae and Jeong (2007) reported value relevance of earnings and book value of Korean firms is lower as compared to the US firms, this is due to the weak governance of Korean stock market by the government. Based on the reviewed published articles used in this study, the early studies on this nature observed to have been conducted in 1999 and 2000 in emerging and matured financial markets. For example, the first studies examined about the effects of IFRS adoption on the value relevance of accounting information was conducted in Finland and China by Niskanen et al. (2000); Bao and Chow, (1999); Haw et al. (1999); Eccher and Healy, (2000).However, after 2000 the number of publication about IFRS adoption and its impact on the value relevance of accounting information has increased in emerging and matured financial markets. Table below (Table 1) shows summary of existing empirical studies discussed in this review from different countries.

Table 1: Summary of Empirical Studies reviewed in this Study

S/No	Country	No. of studies	Name of Author (s)
1	Finland	1	Niskanen et al (2000)
2.	German	5	Bartov et al. (2005); Schiebel (2006); Hung and Subramanyam (2007); Jermakowicz, Kinsey and Wulf (2007); Sellhorn and Skaife (2008)
3.	Australia	2	Ahmed and Goodwin (2006);Clarkson,et al.(2009)
4.	Belgium	1	Jermakowicz (2004)
5.	Czech	1	Hellstrom (2006)
6.	Spain	3	Callao et al. (2007); Gastón et al. (2010); Gordon et al. (2010)
7.	United Kingdom	3	Sellhorn and Skaife (2008): Gastón et al. (2010); Gordon et al. (2010)
8.	France	1	Sellhorn and Skaife (2008)
9.	Europe	2	Meulen (2008); Ferrer et al. (2008)
10	Portugal	1	Morais,A and Curto,J.D (2008)
11.	Turkey	2	Turel (2009); Kargin (2013)
12.	Greece	3	Tsalavoutas et al (2009); Karampinis and Hevas (2011);Bilgic and Ibis (2013)
13.	Romania	1	Filip and Raffournier (2010)
14.	China	12	Jing,G and Lu Miyao (2015); Wen,Q et al.(2012); Liu *et al*., (2011); Zhu, Zhao, Sun (2009); Wang (2009); Xue, Zhao, Xiao, Cheng (2008); Liu and Liu (2007); Lin and Chen (2005); Sami and Zhou (2004); Eccher and Healy (2000); Haw *et al.* (1999); Bao and Chow (1999)
15.	Nigeria	6	Zayyad, B, Ahmad and Mubaraq, S. (2014); Adebimpe and Ekwere,R.(2015); MuhibudeeN,L.(2015);Yahaya,Onyabe,J and Usman,S (2015); Umoren and Enang (2015); Yusuf,A.M and Asma,L.N.(2015);
16.	United Arab Emirates	2	Khanagha (2011);Alali and Foote (2012)
17.	Pakistan	1	Azeem,M and Kouser (2012)
18.	Bahrain	1	Desoky,A.M., and Mousa,G.A. (2014)
19.	Iran	1	Khanagha,J, Mohamad, Hassan, and Sori,Z.(2011)
20.	Malaysia	1	Kadri,M. et al (2009)

CONCLUDING REMARKS

Value relevance is another line of research that throws some light on the quality of accounting information after IFRS adoption. This line of research assumes that if there is a greater significant relationship between accounting information (for example, earnings and book value) and stock returns (stock prices), the financial reporting quality also will be higher. Researchers in this area argue that higher quality of accounting information results from applying accounting standards that require recognition of amounts that are intended to faithfully represent a firm's underlying economics, and high quality accounting standards are required for the purpose of building investor confidence, which in turn reduces cost of capital, improves liquidity and contributes to the efficiency of capital markets. There have been numerous studies tested whether IFRS adoption has significant influence on the quality of accounting information in emerging and mature financial markets but financial reporting standards and requirements differ between countries which create inconsistencies results among researchers. Other reasons which may lead to such inconsistency including difference in economic and political system between countries, historical background and general context of the country where the studies are carried out could influence the findings, and also rules and regulation of a country also may lead findings to differ. There is also little literature in emerging financial markets as compared to mature financial markets.

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