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MANDATORY ADOPTION OF INTERNATIONAL FINANCIAL REPORTING STANDARDS AND VALUE RELEVANCE OF ACCOUNTING INFORMATION IN THE NIGERIAN FINANCIAL FIRMS

Muhammad Mustapha Bagudo

Department of Accounting

Ahmadu Bello University Zaria

mmbagudo@yahoo.com/+2348036057525

Nasiru Yunusa

Department of Accounting

Ahmadu Bello University Zaria

nasiruyunusa80@yahoo.com/+2348060335408

Aisha Oyiza Otori

Department of Accounting

Ahmadu Bello University Zaria

aishah22bulb@yahoo.com/+2348060335408

Abstract

Prior to mandatory adoption of International Financial Reporting Standards (IFRS), the Nigerian Statement of Accounting Standard (SAS) was considered of low quality and inadequate to address the financial reporting needs of companies in Nigeria. Nigeria adopted IFRS to overcome the weaknesses of SAS and improve the information contents of financial reports in Nigeria. This study compares the information contents of Book Value per Share (BVPS) and Earnings per Share (EPS) under SAS and IFRS to determine the impact of IFRS adoption on the value relevance of accounting information in the Nigerian financial industry using Ohlson (1995) model. Data is collected from 52 companies for the period 2010-2013. The overall result shows that the adoption of IFRS has improve the value relevance of accounting of

accounting information in the Nigerian financial industry. The coefficients of BVPS and the EPS and the combined value relevance of accounting information measured by adjusted R-square are higher under IFRS than under the Nigerian SAS. The study recommends future research in the non-financial firms and other proxies of accounting quality such as earnings management for better understanding of the impact of IFRS in Nigeria. Future research should also examine the long-term effect of IFRS adoption in Nigeria.

Key words: IFRS, SAS, value relevance of Accounting Information

1. Introduction

The most widely used accounting standard in the World is the International Financial Reporting Standard (IFRS) issued by International Accounting Standard Board (IASB). Over 120 countries permit the use of IFRS around the World. Nigeria joined the leagues of countries that mandatorily adopted IFRS in 2012. All publicly listed companies are required to use IFRS beginning January 1, 2012. Prior to mandatory adoption of IFRS, the Nigerian Statement of Accounting Standard (SAS) was considered of low quality and inadequate to address the financial reporting needs of companies in Nigeria (World Bank, 2004, 2011). According to World Bank (2011) many disclosure requirements and standards relevant to Nigeria such as financial instruments and standard on Agriculture are missing in the Nigerian SAS.

Nigeria adopted IFRS to overcome the weaknesses of SAS and improve the quality of financial reporting. Prior literatures on the other hand argue that adoption of high-quality standard in form of IFRS does not necessarily improve the quality of financial reporting (Doukakis, 2010; Hellstrom, 2006). Literatures from jurisdictions that adopted IFRS provide mixed result. Adoption of IFRS in some countries improve the value relevance of accounting information (Iatridis & Rouvolis, 2010; Chunhui Liu, Yao, Hu, & Liu, 2011; Suadiye, 2012; Uyar, 2013) while in other countries adoption of IFRS decreases the value relevance of accounting information (Dobija & Klimczak, 2010; Gastón, García, Jarne, & Láinez Gadea, 2010).

Even though prior literature have examined the value relevance of mandatory adoption of IFRS in many jurisdictions, very little is known on the value relevance of mandatory adoption of IFRS in Africa (Ames, 2013; Prather-Kinsey, 2006). Adoption of IFRS is a global phenomenon as the objective of IASB is to develop high-quality standard and promote the use of the standard around the World (IFRS Foundation, 2013). Therefore, there is the need to receive feedback

from all over the World. A careful examination of the prior literature in Nigeria has revealed that most of the studies on value relevance have been conducted before the adoption of IFRS in Nigeria (Abiodun, 2012; Enofe, Asiriwa, & Ashafoke, 2014; Olugbenga & Atanda, 2014; Titilayo, 2011). The study conducted after the adoption of IFRS by Uthman and Abdul-baki (2014) is a perception study.

The study therefore examines empirically the impact of IFRS mandatory adoption on the value relevance of book value of equity and earnings in the Nigerian financial industry. The study hypothesized that there is no significant differences in the value relevance of book value of equity and earnings under IFRS and the Nigerian SAS. The study will add to academic literature on the value relevance of IFRS in Africa being the continent with the lowest number of countries that adopted IFRS (PwC, 2013).

The remaining part of the paper consists of four sections. Section two provides for the literature review and hypotheses development. Section three discusses the methodology. Section four presents the result and section five provides for summary and conclusions.

2. Literature Review

Literature on the value relevance of IFRS can be divided into two periods: Voluntary adoption period and the mandatory adoption period. Most of the earlier studies on voluntary basis compare the value relevance of IFRS accounting numbers with domestic GAAP accounting numbers and the findings from these studies are mixed. Niskanen, Kinnunen, and Kasanen (2000) examine the value relevance of accounting numbers of 18 companies in Finland between 1984 and 1992. Using stock return model, the study finds earnings and earnings reconciliations under IFRS to be value relevant. Bartov, Goldberg, Stephen, and Kim (2005) find earnings under IFRS and US GAAP to be more value relevant than under German GAAP when they examine the relationship between stocks return and earnings across 417 sample companies in Germany for the period 1998-2000.

In another study, Jermakowicz, Prather-Kinsey, and Wulf (2007) also find increase in value relevance of IFRS earnings in Germany between 1995-2004. Barth, Landsman, and Lang (2008) also find value relevance of earnings and equity to be higher for companies that adopted IFRS compared to those that used domestic standard across 327 companies in 21 countries around the World. On the other hand, some earlier studies find decrease in value relevance when IFRS is compared with domestic standard. Lapointe-Antunes, Cormier, Magnan, and Gay-Angers (2006) find the value relevance of earnings and equity for 90 sample firms

using Swiss GAAP to be higher than those using IAS/US GAAP. Schiebel (2007) also find accounting numbers under German GAAP to be more value relevant than IFRS accounting numbers in explaining market capitalization in Germany.

Other literature on voluntary adoption of IFRS reported mixed results on the value relevance of earnings and equity under IFRS. Harris and Muller (1999) find IFRS earnings and equity to be more closely related to share prices using price model but when using return model, US GAAP accounting numbers are more closely related to return. Hung and Subramanyam (2007) find the coefficient of earnings is higher under the domestic GAAP and the adjustment for earnings were not value relevant but IFRS adjustments to equity were value relevant.

Another stream of literatures examines the value relevance of IFRS during mandatory adoption in Europe. Substantial number of these literatures compares the value relevance of accounting information under domestic GAAP and IFRS in the year prior to mandatory adoption because of provisions of IFRS 1, which requires accounting information prepared under local GAAP to be restated under IFRS for comparison. Schadewitz and Vieru (2007) find IFRS earnings adjustment to be value relevant but no evidence to show IFRS equity adjustments are value relevant in Finland across 46 companies. Gjerde, Knivsflå, and Sættem (2008) find little increase in the value relevance of accounting information after mandatory adoption of IFRS in Norway.

Goodwin, Ahmed, and Heaney (2008) also find no increase in relative and incremental value relevance of earnings and equity after the adoption of IFRS in Australia. Clarkson, Hanna, Richardson, and Thompson (2011) also did not observe any change in value relevance across 3,488 firms either in the code law or common law countries in Europe and Australia. Horton and Serafeim (2010) on the other hand find the valuation coefficient of earnings under IFRS is greater than the valuation coefficient of earnings under domestic GAAP but the valuation coefficient of equity is not value relevant. Jarva and Lantto (2012) also find IFRS earnings to provide greater information content in predicting future cash flows but find book values of assets and liabilities of no greater value relevance than they were under Finnish GAAP.

Again, other studies on mandatory adoption of IFRS examined the value relevance of IFRS in the year of adoption and the findings from most these studies shows increase in value relevance of accounting information. Tsalavoutas and Dionysiou (2014) find accounting information to be value relevant in Greece after IFRS adoption and the value relevance of earnings is higher for companies with higher level of compliance with mandatory disclosure requirements of IFRS.

Aubert and Grudnitski (2011) find variation in the level of value relevance across 15 countries in Europe but the accounting numbers in one-third of the countries studied are value relevant.

Prior literatures have also examined the value relevance of mandatory adoption of IFRS by comparing accounting numbers in pre and post IFRS adoption periods. The findings from these studies also produce mixed result. Several studies reported increase in value relevance of earnings and equity (Agostino, Drago, & Silipo, 2010; Aharony, Barniv, & Falk, 2010; Dimitropoulos, Asteriou, Kousenidis, & Leventis, 2013; Iatridis & Rouvolis, 2010; Ismail, Kamarudin, Zijl, & Dunstan, 2013; Kim, 2013; C. Liu, Yao, Hu, & Liu, 2011; Suadiye, 2012; Tsoligkas & Tsalavoutas, 2011; Uyar, 2013). Other studies reported decrease in value relevance of earnings and equity (Ames, 2013; Dobija & Klimczak, 2010; Morais & Curto, 2008; Oliveira, Rodrigues, & Craig, 2010). Other studies find increase in value relevance of only earnings (Chalmers, Clinch, & Godfrey, 2011; Devalle, Onali, & Magarini, 2010) while others find increase in value relevance of only equity (Kadri, Aziz, & Ibrahim, 2009; Tsalavoutas, André, & Evans, 2012).

The Nigerian SAS is derived from IFRS but have not been updated to conform to the provisions of IFRS. As at January 1, 2012 when Nigeria mandatorily adopted IFRS there are 38 issued IFRS but only 50% of the disclosure requirements are contained in the Nigerian SAS (WorldBank, 2011). In addition, differences exist between the two standards in terms of basis of account preparation, components of financial statements, consolidation procedures, accounting for business combination, assets and liabilities treatment, related party transactions and foreign transactions (PwC, 2011).

Many standards relevant to the Nigerian economy such as standard on financial instruments, non-current assets held for sale and discontinue operations, accounting for government grants, borrowing cost and related party transactions are missing in the Nigerian SAS (WorldBank, 2011). Nigeria adopted IFRS being high-quality standard (IFRS Foundation, 2013) and being more superior to Nigerian SAS (WorldBank, 2011). Empirical literature from jurisdiction that mandatorily adopted IFRS provide mixed result on the value relevance of IFRS with majority of the studies reporting increase in value relevance of earnings and equity (Ismail et al., 2013; Jarva & Lantto, 2012; Suadiye, 2012; Türel, 2010; Uyar, 2013). Other studies reported decrease in value relevance (Dobija & Klimczak, 2010; Oliveira et al., 2010).

3. Methodology and Data

The population of the study is the Nigerian Financial industry, which constitute of banks, insurance, and other financial institutions other than Banks and Insurance. As at December 31, 2013 there are 58 firms in the financial sector in Nigeria and they accounted for 30% of all listed companies in Nigeria and 35% of the market capitalization (NSE, 2013). The sample of the study is all the firms in the financial industry but six firms were dropped due to incomplete data. Data is hand collected from the annual reports of the sample firms and the Nigerian Stock Exchange facts book. Share price data is collected from Thomas & Reuters data base. The period of study is 4 years (2010-2013). The period of study is divided in to pre-IFRS (2010-2011) and two years post-IFRS (2012-2013).

The study employs the Ohlson (1995) price model to determine the information content of accounting numbers under IFRS and SAS. The price model examines the information content of the book value of equity and earnings in explaining market values. Prior studies have used the price model extensively in value relevance studies (see Ismail et al., 2013; Jarva & Lantto, 2012; Tsalavoutas et al., 2012; Liu et al., 2011; Clarkson et al., 2011; Türel, 2010; Devalle et al., 2010). The price model used for determining the value relevance is specified below:

$$\begin{aligned}
 PPS_{it}^{SAS} &= a_0 + b_1 BVPS_{it}^{SAS} + b_2 EPS_{it}^{SAS} + b_3 IND + \varepsilon_{it} & \dots\dots\dots i \\
 PPS_{it}^{IFRS} &= a_0 + b_1 BVPS_{it}^{IFRS} + b_2 EPS_{it}^{IFRS} + b_3 IND + \varepsilon_{it} \varepsilon_{it} & \dots\dots\dots ii
 \end{aligned}$$

Where PPS_{it} is the stock price per share of firm i at year t (one month after the release of financial statements under consideration to ensure that the information released is in the public domain for users (Tsalavoutas et al., 2012). $BVPS_{it}$ is the book value per share for firm i at year t (end of the financial year under consideration), and EPS_{it} is the earnings per share for firm i at year t (end of the financial year under consideration). SAS is financial data prepared using Nigerian SAS. IFRS is the financial data prepared using the IFRS. ε_{it} is the error term for firm i at year t . IND_{it} It is measured 1 if the firm belongs to banking, 0 otherwise. It serves as a control variable.

The accounting numbers are based on per share to avoid scale problems as suggested by prior literature (Barth et al., 2008; Hung & Subramanyam, 2007; Tsalavoutas et al., 2012).

4. Results and Discussion

4.1 Descriptive statistics and Correlations

Table 1 below provides descriptive statistics of the variables used in determining the value relevance.

Table 1: Descriptive statistics

		PPS	BVPS	EPS
Mean	Pre-IFRS	2.99	2.35	0.10
	Post-IFRS	3.60	2.85	0.42
	Pre and Post IFRS	3.29	2.60	0.26
Standard deviation	Pre-IFRS	4.49	3.38	0.90
	Post-IFRS	6.01	3.94	0.88
	Pre and Post IFRS	5.30	3.67	0.90
Minimum	Pre-IFRS	0.42	-8.57	-6.61
	Post-IFRS	0.10	-2.17	-0.87
	Pre and Post IFRS	0.10	-8.57	-6.61
Media	Pre-IFRS	0.52	1.12	0.06
	Post-IFRS	0.68	1.10	0.11
	Pre and Post IFRS	0.62	1.11	0.09
Maximum	Pre-IFRS	17.71	12.11	2.70
	Post-IFRS	27.60	16.22	3.64
	Pre and Post IFRS	27.60	16.22	3.64

Source: E-views result for descriptive statistics

The mean value of all the variables is higher in the post-IFRS adoption period suggesting that performance of financial firms in terms of their share prices book value of equity and earnings increases after the mandatory adoption of IFRS.

Table 2 presents the correlation matrix of the variables used in the study

Table 2: Correlation Matrix

Variables	Pre-IFRS			Post-IFRS			Pre and Post IFRS		
	PPS	BVPS	EPS	PPS	BVPS	EPS	PPS	BVPS	EPS
P	1.00	0.56	0.43	1.00	0.80	0.82	1.00	0.71	0.64
BVPS	0.56	1.00	0.08	0.80	1.00	0.87	0.71	1.00	0.50
EPS	0.43	0.08	1.00	0.82	0.87	1.00	0.64	0.50	1.00

Source: E-views result

The correlation between share price and accounting numbers (BVPS and EPS) is higher in the post-IFRS adoption period. For BVPS in the post-IFRS period is 0.80 which is greater than 0.56 in the pre-IFRS period. The EPS in the post-IFRS period of 0.82 is also greater than 0.43 in the pre-IFRS period. This suggests that both equity and earnings are more associated with share price in the post-IFRS period and therefore more value relevant. On the other hand, the bivariate analysis shows a positive relationship between BVPS and EPS in both pre and post-IFRS period.

4.2 Test of Value relevance in Pre and Post-IFRS period

Table 3 presents the results of pre and Post IFRS regression. The result shows that the coefficients of BVPS and EPS are positive and statistically significant. The coefficient of BVPS is significant at 5% in both pre and post-IFRS period while that of earnings is significant at 1% in the pre-IFRS period and 5% in the post-IFRS period. The coefficient of IND is only significant in the pre-IFRS period, indicating that no significant differences in value relevance of accounting information between the banking industry and the insurance industry after the adoption of IFRS.

The adjusted R-squares for pre and post-IFRS period are also statistically significant. The F-statistics are significant at 1% suggesting that the BVPS and EPS in the model explained 54% and 55% of the variation in the share prices for pre and post-IFRS respectively. If a comparison is made between the coefficients of the accounting numbers in a single period, the coefficient of EPS is higher than the coefficient of BVPS, irrespective of the pre or post-IFRS period. This indicates that the market gives more weight to EPS than BVPS in the valuation of share prices. The findings support earlier studies in Nigeria before the mandatory adoption of IFRS that have shown earnings to be more value relevant in determining corporate values in Nigeria (Abiodun, 2012; Olugbenga & Atanda, 2014). The findings also support prior literature in other jurisdictions that have mandatorily adopted IFRS (Tsalavoutas et al., 2012; Uyar, 2013).

Table 3: Regression result for Pre and Post IFRS

	Pre-IFRS	Post -IFRS
Intercept	0.92	0.55
BVPS	0.24**	0.44**
EPS	1.53*	2.72**
IND	4.68**	2.24
R squared	0.56	0.56
Adjusted R square	0.54	0.55
N	104	104

Overall F-statistics	41.63*	42.42*
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Source: E-views result

*, ** represent significant at 1% and 5% respectively

Additionally, Table 3 reveals that the coefficient of book value per share of 0.44 in the post-IFRS period is greater than the coefficient of 0.24 in the pre-IFRS period. This suggests that the value relevance of equity under IFRS is greater than the value relevance of equity under SAS. In addition, the coefficient of EPS of 2.72 under post-IFRS is greater than the coefficient of EPS of 1.53 in the pre-IFRS period suggesting that earnings under IFRS have higher value relevance than earnings under Nigerian SAS.

Similarly, the combined value relevance measured by adjusted R-square of 55% in the post-IFRS period is also greater than the adjusted R-square of 54% in the pre-IFRS period suggesting that the combined value relevance is greater for IFRS accounting numbers than the Nigerian SAS accounting numbers. In general, the BVPS and the EPS are value relevant in both pre and post IFRS period but the value relevance is greater in the post-IFRS period if the two periods are compared. This is consistent with findings from prior literature (Agostino et al., 2010; Dimitropoulos et al., 2013; Karampinis & Hevas, 2009; Paglietti, 2009; Suadiye, 2012; Türel, 2010; Uyar, 2013).

From the result in Table 3, the study therefore rejects the hypothesis that there is no significant difference in the value relevance of book value of equity and earnings under IFRS and the Nigerian SAS. The study therefore finds IFRS equity (BVPS) and earnings (EPS) to be more value relevant in explaining share prices (PPS) in the Nigerian Financial industry than BVPS and EPS under the Nigerian SAS. Additionally, the study finds the combined value relevance of accounting information (BVPS and EPS) under IFRS is greater than that of Nigerian SAS. This is evidenced in the high R-square in the post-IFRS period if compared to pre-IFRS period.

4.3 Further Test and Analysis

To further, identify the contribution of IFRS adoption to the value relevance of accounting information in the Nigerian financial industry, a cross sectional analysis of 2011 financial statements is undertaken. IFRS 1 requires that in the year of mandatory adoption, prior year financial statements should be restated using IFRS for comparative purpose. The study compares the 2011 financial statements prepared under SAS with the 2011 restated under IFRS to bring out the contribution of IFRS to value relevance of accounting information. The economic

and market condition are the same but the accounting standard are different. Table 4 and 5 presents the result of the analysis

Table 4: Correlation Analysis

Variables	2011-SAS			2011-IFRS		
	P	BVPS	EPS	P	BVPS	EPS
P	1.00	0.65	0.28	1.00	0.66	0.31
BVPS	0.65	1.00	-0.06	0.66	1.00	-0.05
EPS	0.28	-0.06	1.00	0.31	-0.05	1.00

Source: E-views result

Table 5: Regression results 2011 SAS and IFRS

	2011-SAS	2011-IFRS
Intercept	0.54	0.52
BVPS	0.57**	0.61**
EPS	1.20**	1.31**
IND	2.30**	2.04
R squared	0.55	0.57
adjusted R ²	0.52	0.54
N	52	52
Overall F-statistics	19.5*	21.53*

Source: E-views result

*, ** represent significant at 1% and 5% respectively

The correlation coefficient of BVPS of 0.66 and EPS of 0.31 under IFRS is greater than the correlation coefficient of 0.65 and 0.28 for BVPS and EPS respectively under SAS. This corroborated the earlier findings that equity and earnings under IFRS are more associated with share prices. This shows that the increase in value relevance can also be associated with IFRS adoption. In addition, the regression results in table 6 shows that the coefficient of BVPS and EPS under IFRS standard is greater than the coefficients under SAS and all the results are significant at 5%. The combined value relevance under IFRS measured by adjusted R-square of 54% is greater than the adjusted R-square of 52% under

SAS. This suggests that the increase in the value relevance can also be associated with change in the accounting standard.

5 Summary and Conclusion

The study examines the impact of IFRS mandatory adoption on the value relevance of book value of equity and earnings in the Nigerian financial industry using Ohlson (1995) model. The accounting numbers (BVPS and EPS) are value relevant in pre and post IFRS period but when the two periods are compared separately, the value relevance in the post-IFRS period is greater than the value relevance in the pre-IFRS period. Comparing 2011 financial statements under SAS and IFRS further enhance the results and the findings supported the superiority of IFRS over Nigerian SAS. The implication of the result is that adoption of IFRS might have improved the value relevance of accounting information in the Nigerian financial sector.

The study therefore concluded that mandatory adoption of IFRS improves the information contents of book value per share and earnings per share in the Nigerian financial industry. The study is subject to some limitations. Firstly, the study adopted Ohlson (1995) model, which assume that market is efficient. Prior literature in Nigeria indicates that market is efficient in a weaker form of efficiency (Ojo & Azeez, 2012) and therefore being less efficient might affect the result. Secondly, the study is for short period of time (2 years pre-IFRS and 2 years post-IFRS) and therefore the impact in the long run might be different. Thirdly, the study cannot be generalized to other sectors (non-financial) of the economy, as the financial sector constitutes only 30% of listed companies in Nigeria.

The study recommends that the regulatory bodies responsible for ensuring compliance with accounting regulation should ensure full compliance with IFRS since mandatory adoption improves the contents of accounting information. Similarly, the study recommends the followings for future research: firstly the effect of IFRS should be examine in the non-financial firms which constitute 70% of firms in the NSE for better understanding of the impact of IFRS in Nigeria. Secondly, other forms of accounting quality such as earnings management should be examine to fully examine the effect of IFRS in Nigeria. Thirdly, future research should examine the long-term effect of IFRS adoption in Nigeria.

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