The Impact of Accounting Information on Value Relevance in Pre and Post Adoption - IAS: Perspective from Pakistan
(Effect of Pre and Post Adoption of International Accounting Standard in Cross Industries of PSX)

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Abstract

The study is an attempt to examine the impact of accounting information on value relevance with book value as per share (BVPS) and earnings as per share (EPS) and in the period of pre and post adoption IAS (International accounting standards). On the basis of IAS with value relevance of EPS and BVPS, the investors can make decisions of investments. To determine the impact of IAS on the value relevance ability of disclosure practices of accounting information where seven sectors of PSX listed as non-financial companies data were collected from 2000 to 2017. Further, it is divided into two segments to maintain firstly as 2000-2004 for pre adoption and 2005-2009 for post adoption to examine the IAS effect. Secondly, the overall effect of IAS also examined from 2000 to 2017. In this particular study, a pooled least square analysis is used to explore the effect of IAS. Finally, it is concluded that the selected accounting information have more value relevant to market value per share. This study will provide an assistance and guideline to investors to take the investment decisions and enhance the need of adoption of IAS in a more dynamic perspective in Pakistan.

Keywords: IAS, Earning Per Share, Book Value, PSX, Pool, IASB, IFRS.

Introduction:

True and fair view of financial statements is like a foundation for all stakeholders of business to build a story. The users of financial

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statements rely analysis if it contains right information. Every country has its own financial culture, accounting policies and procedures, but due to globalization and increasing trend of international mergers and acquisition. The diversity creates a problem of diverse statements. International accounting standard board has taken the responsibility to share this problem. IASB plays a vital role in harmonization of standards statements. The adoption of IAS is burning issue from last few decades. The board of IAS (international accounting standards) is committed to establish IAS and international accounting policies in the best interest of the general public. The single collection of higher quality accounting standards at global required to make transparent, reliable and comparable information which can be used for general purpose (IASB 2002).The board of IAS (International accounting standards) provide ease to difficulties, interpretation and publications of financial statement and standardize of companies to users of accounting information. The cost of business and financial statements analysis is shrinked because of IAS (Houseton and reinstein 2001). The investors at international call can comparison to financial information at global competition for making investment at foreign. For importing FDI in Pakistan, the corporate sectors in Pakistan comply with international accounting standards. The securities and exchange commission of Pakistan (SECP) has powers with regard to implementation of IFRS under section 234 of company's ordinance 1984. Institute of Charted Accountants of Pakistan recommends the standards and SECP issues notifications about it. Pakistan is following the IAS from very early times. The ICAP council adopted IAS since 1970. These accounting statements are prepared as to approve the standards of accounting as practiced in Pakistan and the requirement of Companies Ordinance 1984. The established accounting practice standards comprise of such IAS as per notification as the provision of Companies Ordinance 1984. The directives as per issuances by the SECP (Securities and Exchange Commission of Pakistan) differ with the requirement of these standards. The requirement of Companies' Ordinance 1984 or the requirements of the directives are being used to set precedent. In the technical release of Accounting are used establish additional guidelines. Companies' Ordinance 1984 explains the presentation and discloses requirements and SBP explains the recognition and measurement requirement. ICAP has developed a due process of analytical review of IFRS which is conducted by various committees. Exposure draft is distributed to the members of corporate sector and consultation is conducted with stakeholders and then recommendations it made. The notable progress has been made by Pakistan to fill the gap between IAS and local requirements. There was a compliance gap between IFRS and Companies Ordinance 1984, so the 4th schedule of Companies Ordinance 1984 established by SECP on 5th July, 2005, after which gap is eliminated however still there is a gap between IFRS and Companies Ordinance 1984 and SECP directives.IAS 39 is conflicting with GAP. Prudential regulation issued by SBP, the rules relating financial and corporate sectors. The ICAP have view of that the entities of public interest should provide confirmation to practice with the IFRS which are being used to generate high quality financial information. The relevant information are comparable, transparent and consistent and thus meet the needs of stakeholders from early times, ICAP followed the adoption approach of IAS-IFRS without changing. However this approach involves difficulties and is affected by the time of adoption and implementation. Due to the adoption of IFRS cross country comparison of financial statements can be become possible. Due to this international market can become more efficient. The less cost of capital of firm and reliability on financial statements by users (investors, creditors, and shareholders) is due to the transparency and improved quality statements. Though the adoption of IFRS is to present the fair view of statements but it has significant impact on firms. Adopting IAS required higher disclosure which is linked with high firm value (Karamanou and Nishiotis 2005). By adopting IAS management becomes more as accountable IAS requires true and superior information which result in getting better financing conditions, (Sumontier and Raffoiner 1998).The IAS has bright picture that the other partner of the firm can evaluate the potential risk and window of mergers and acquisition is required. Comparison of competitors can be made if they adopted the IAS. In this study the impact of IAS on firms is evaluated. In 1974 the ICAP became the member of IASB and recommended to follow the IAS from 1986. However, due to changes made by the ICAP for local needs these could not get prominence. When in 2005 European Union announced to follow the IAS then SECP issued notification to follow these standards.

Theoretical Framework

The financial and economic Information is relevant to value. The number in accounting to be related with firm value. The value of firms can be increased through reliability and trust of the financial information. The financial information not to be relevant, financial reports reflected inability to reliable. It's meant that financial reports are being unable to meet its primary objective (Baisland, 2009). These information are useful for stakeholders for upcoming decision making. Therefore, the information is value relevant. The value relevance and its construct are explained by much way. Barth et al. (2001) explored that the numbers in accounting and value at market of equity are relevant. In accordance with Francis and Schipper (1999), four approaches of relevant to value of financial and economic information as under:

1. The fundamental view of value relevance of financial information.
2. The prediction view of value relevance of financial information.
3. The information view of value relevance of financial information.
4. The measurement of value relevance of financial information.

According to fundamental view of analysis ensured natural corporate value of equity at market. This is happened due to fairly information priced at efficient market and rapidly adjusted in value of equity. The rapid adjustment in an efficient market will reflect fundamental value of shares as compared to market price at equal. Moreover, the financial information is cause to change in equity price increase or decrease as well as fundamental value. The difference at fundamental value and market value will have implication for trading strategies. The buying and selling strategies are the basic premise of accounting information. The information under in not efficient market can have monopolistic access to attain best profits as compared to others who cannot have information (Bauman, (1996). The value relevance of financial information and its interpretation is the main concern of fundamental researchers. The value relevance is considered to evaluate the firm and its returns in next year. The financial statements are used to forcast the inherent value originated from value theories. The information value theories are considered to forcast of profit and cash flows. The profit and cash flows are value relevant in comparison of present and upcoming year (Fancis and Schipper, 1999). The accounting information is value relevant. This information is being used to price equity for investors as documented by Fancis and Schipper (1999). Fancis and Schipper (1999) proposed and examined that there exist reactions of capital market against the full disclosure practice of accounting information. The information is value relevant after announcement of profit rate. These announcements are important to decrease or increase expectations of investor to make up or down in equity market. This change is happened due demand and supply shift in trading pattern. The trading pattern based upon financial information. The value relevance of financial information estimated in term of behavior of market with reference to availability of information and its disclosure practice. The availability of information and its disclosure practice are considered as value relevance as compared to old information which is obsolete. The old information are irrelevant while decision making (Barth et al. 2001). The price of share and return of share are used to estimate the market trend and fashion. The selection of two variables is due to type of question and hypothesis being raised from research. The price based studies are used to examine the value relevance that affected to firm at a particular date. The return based studies are used to examine the value relevance that accounting numbers have capability of control.

Literature Review

The IAS (International Accounting Standards) was established in 1966. It was requested and forwarded by AICPA (American Institute of Certified Public Accountant), ICAEW (Institute of Chartered Accountant of England and Wales) and CICA (Canadian Institute of Chartered Accountant) to establish a study group ISG (International Study Group). The AISG (Accountants International Study Group) was formed in 1967. The AISG published regularly papers on accountancy practice since 1967. The purpose to establish IAS is creation of similarity and elimination of difference that curtailing investment opportunities among countries at international level. However, IAS plays a key role to enhance value of firms and investment behavior. The IAS are developed at agreed conceptual framework to make a consistency for reliance of financial reports quality. It will help to investor trust and confidence to make decision and operation in equity market. The information floated at market without biasness will have trust and confidence on the financial information statements and operations at equity market. The IAS is responsible to provide detailed information to the users of financial information statements. The reports are prepared according to IAS code which required detailed and certain information.

The IAS are set of regulation where effective comparison makes easy to decision of investment within cross national or global economy. The IAS code of conduct prescribed that statements must be prepared according to applicable IAS and verified by Auditors. There may not be a guarantee of a good investment with audit report but lends a credibility to reporting. Beke (2011) has conducted study to examine the role of IAS (International Accounting Standards) in management of business. The IFRS adoption had an impact on turning down the income of business managers. The global management researchers are suggested to use these measure and methods with impact on management function practicaly. Alkali, Y.M. and Lode, A.N., (2016) explored that IFRS adoption has implication for value relevance and relationship of assets and liabilities with stock price. It is found a significant difference of value relevance. The value relevance between asset and liabilities prepared and disclosed under the IFRS. The value relevance increase based is due to adoption of IFRS at Nigeria as an emerging market Petreski (2005) explored a research the impact of IAS (International Accounting Standards) on value of firms. It also summarized that the role of adoption IAS and its impact on value of firms are positive, multiple and noteworthy. The adoption at varying process is accompanies with many obstacles. The IAS compiled accountancy practice more reliable image for the business. It also contributes for a high rate to value of firms. Gerrit Zalm (2008) presented before the economic and monetary affairs Parliament committee of Europe do accounting standards matter? They recognized the impact to introduce the IFRS standards is high on quality of earning and management of earning. They found that the pervasiveness of earnings management did not decline after introduction of IFRS. Luez and Verveechia (2000) conducted a research that by the adoption of IAS, the cost of capital of firms can be reduced. Elshandidy (2014) described that the relevance of accounting information at equity market of China. The convergence of IFRS (International Financial Reporting Standards) with Accounting Standards of China is more relevance to value. According to bushman and Piotroski (2006) due to adoption of IAS the asset allocation efficiency can be evaluated. The importance of reporting at international market can have better understanding regarding relevance of accounting information at emerging markets. The emerging markets provided different findings on the relevance of accounting information. (Kargin, 2013 and Chebaane & Othman, 2014). The relevance of accounting information of local standard of accounting and establishment of new reporting standards for accountancy practices varied at different countries. (Umoren & Enang, 2015, Abubakar et al and 2017; Ahmadi, 2017). Dontoh et al. (2012) provided that value relevance is a primary paradigm of research in accounting. The accounting literature of several researchers suggested about the data of accounting may lost their value relevance. The change happened due to shift in capital-intensive economy to service oriented economy. The accounting information is less relevant to assess a fundamental value. The researches provided only a base for temporal decline. The temporal declines in the implication of accounting information are less relevant to earnings, book value, dividends, and cash flow on the valuation of equity prices. Akarim, et al. (2012) supported the relevance theory and revealed that a significant association of equity returns and its earnings. Jermakowiez et al (2007) suggested that mandatory adopter at first time can increases a market liquidity and value after adoption of ISR mandatory. Karamount and Nishiotis (2005) explored that greater disclosure under IAS or reduce the cost of capital. Karunarathne and Rajapakse studied that EPS is most relevant variable. Bhatt and Sumangala (2012) explored in their research that EPS has major impact on market value of equity. Melissa (2013) found the association of price of share, earnings of share and book value of share. The earnings of share and book value of shares are concerned with share values. No doubt book value found a less significant. Ayzer and Cema (2013) explored the relevant value of accounting Information, using the Ohlson (1995) model and found the book values and earnings are value relevant to explain the equity prices. The book values have the greater power of explanation rather than earnings. Abiodun (2012) declared that the information contained in income statement is more relevant than balance sheet information. The researchers included in this literature provide sufficient support for value relevance but still there are many contradictions. So keeping all facts in mind, we are studying the relevant value of EPS and BVPS the perspective of Pakistan. There is no enough research in this area in Pakistan.

Data and Methodology

The study has two variables one is dependent variable which is Market price of share and two independent variables naming as earning as per share and book value as per share. A market value of share is taken after three months of financial year to examine the impact. Book is calculated by total common stock holders equity divides the outstanding number of shares. Earnings as per share are obtained to divide the available net income to common equity holders to total outstanding number of shares. Data of companies from different sectors is taken from 2000 to 2017 from PSX. Two sets are made of this data. From 2000 to 2004 pre-adoption period and from 2005 to 2009 post adoption period. An overall test is also conducted from 2000 to 2017. The model which is basically derived from the Ohlson (1995) conceptual framework, as under

$$MVPS_t = \alpha_t + \beta_1 (EPS) + \beta_2 (BVPS) + \mu t$$

Where, In Particularly, the Ohlson (1995) Model is as *MVPS* is the value per share at market, *EPS* is the earnings per share of and *BVPS* is the book value as per share of listed firms of PSX.

Fixed Effects Model

It indicated that intercepts differ as compared to different cross sections of the firms with a constant slope. It is used to control over the correlation of regressors, unobserved effect and ε_{it} constant term to a group within a model of regression where fixed effect model is as under:

$$Y = \alpha + \beta X + \mu \text{ -----------------------(1)}$$

$i = 1, 2, \ldots, N$ and $t = 1, 2, \ldots, T$

There is presence of fixed effects, then β and α_i can be consistently estimated within group of estimators to attain from Ordinary Least Square OLS equation.

$$\bar{Y} = \frac{1}{T}\sum_1^T \acute{Y} \ : \bar{X} = \sum_1^T \acute{Y} \quad \text{and} \quad = \frac{1}{T}\sum_1^T \mu \text{------------------(2)}$$

So,

$$Y = \alpha + \beta X + \mu \text{ --(3)}$$

It can be subtracted this equation from equation as under:

$$(Y - \bar{Y}) = \beta(X - \bar{X}) + (\mu - \ddot{u}) \quad \text{------------------------(4)}$$

$$\bar{Y} = (\beta\bar{X} + \ddot{u}) \qquad \text{for } t = 1, \ldots\ldots\ldots, T$$

A pool ordinary least square can be used to transform the model for estimation of β in a natural phenomenon. Within the group, it can also be used to minimize any time-invariant variable in equation.

α is considered as fixed constant where β estimator is known as β*wg*.

$$\beta_{wg} = [\textstyle\sum_1^N \sum_1^T (X_{it} - \bar{X}_{it})(X_{it} - \bar{X}_{it})]^{-1} [\sum_1^N \sum_1^T (X_{it} - \bar{X}_{it})(X_{it} - \bar{X}_{it})] \text{ -(5)}$$

The fixed effect estimators are as under:

$$\bar{\lambda}_i = \bar{Y} - \bar{X}_t \overline{\beta wg_{it}} \text{---(6)}$$

In the fixed effect model the error term can be related to individual effect and unrelated within group means of the regressors

Random Effect Model:

The random effects are OLS with a random constant term where a specific effect can be visualized with the outcome of a random factor. A static random effect is as under:

$$Y_{it} = \beta X_{it} + \mu_{it} \text{---(7)}$$

$$\mu_{it} = \lambda_i + \mu_{it} \text{---(8)}$$

The μ_{it} is an identical distribution and independent:

$$(-E(\lambda_i) = E(\mu_{it}) = 0$$

$$(-E(\lambda_i \mu_{it}) = 0$$

$$-E(\lambda_i, \lambda_j) = \begin{Bmatrix} \delta^2 & i = j \\ 0 & i \neq j \end{Bmatrix}$$

$$-E(\mu_{it}, \mu_{js}) = \begin{Bmatrix} \delta^2 & i = j, i = j \\ 0 & i \neq j, i \neq j \end{Bmatrix}$$

$$-E(\lambda_i, X_{it}) = (\mu_{it}, X_{it}) = 0 \text{ -------------------(9)}$$

The Generalized Least Square of β estimator showed that the random estimator where the β_{GLS} is consistent.

Empirical Results

The results of descriptive statistics show that the market value of share prices of companies averagely are 53.62, book value per share 10.21 and earnings per share 8.2. These amounts can vary 90.59, 4.57 and 23.71 respectively for market value per share, book value per share and earnings per share. These figures are on average basis for overall period for all sectors of PSX.

Table 1:Descriptive Statistics

	MVPS	BVPS	EPS
Mean	53.62	10.21	8.199
Std. Dev.	90.59	4.567	23.71
Observations	400	400	400
Cross Sections	40	40	40

Correlation explains the degree of association between variables. In our study there is 61% relationship between earnings per share and market

value per share.
Table 2:Correlation Matrix

	MVPS	EPS	BVPS
MVPS	1		
EPS	0.60*	1	
BVPS	-0.02	-0.060	1

*Significant at p<0.01
It is strong and significant positive relationship between earnings per share and market value per share. The association between book value per share and market value per share is -0.024. It means that there is very weak and negative relationship between book value per share and market value per share.

Pre-Adoption IAS Period (2000-2004)
Common Effect Model
These are the results of panel regression common effect model. According to the results earnings per share significantly determine the market value per share. Results explain that one percent change in earnings per share brings a 325% change in market value per share. The book value per share does not significantly determine the market value per share. According to the coefficient of book value per share, the 1% change in book value per share brings a 67% change in market value per share. Common effect model under panel regression analysis elaborate the average results of all sections for whole time period. According to the results, we can say that earnings per share are value relevant during pre adoption period.

Table 3

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	9.134	5.570	1.639	0.102
BVPS	0.670	0.439	1.527	0.128
EPS	3.250*	0.186	17.394	0.000
R-squared				0.605
Adjusted R-squared				0.601
S.E. of regression				39.734
F-statistic				151.459
Prob (F-statistic)				0.000

*Significant at p<0.01
But R^2 is a factor by which we can determine the overall value relevance.

The R^2 of common effect model for pre-adoption period is 0.61 which means selected accounting information is 61% is value relevant of market value per share during pre-adoption period.

Redundant Fixed Effects Tests

To identify the application of fixed effect model we have to apply the redundant fixed effect tests. Here we apply the mentioned test. The significant value of cross section chi-square shows that fixed effect test should be applied. So according to the interpretations of this test we applied the fixed effect model.

Table 4

Effects Test	Statistic	d.f.	Prob.
Cross-section F	8.821695	-39,158	0.000
Cross-section Chi-square	231.2194	39	0.000

Fixed Effect Model

We have applied fixed effect model on time period from 2000-2004. Again the earnings per share significantly positively value relevant of market value per share with a coefficient of 1.26 which means 1% change in earnings per share brings a 125% change in market value per share.

Table 5

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	25.656	3.712368	6.911157	0.20345
BVPS	0.132	0.277373	0.478219	0.6332
EPS	1.255	0.218939	5.733166	0
Fixed Effects (Period)				
2000—C				-10.6555
2001—C				-13.8206
2002—C				1.509602
2003—C				8.765061
2004—C				14.20143

*Significant at $p<0.01$

But the book value per share still insignificant value relevant of market value per share with a coefficient of 0.1326. The selected accounting information is more relevant of market value per share in 2005 with highest coefficient of 14.20.

Correlated Random Effect- Hausman Test

After the application of fixed effect model, we should examine either the random effect model is applicable or not. For this confirmation we apply correlated random effect Hausman test. According to the results of Hausman test where the probabilities of period random and cross section random are insignificant. So we should not apply the random effect model.

Table 6

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	0	2	1
Period random	0	2	1
Cross-section and period random	0	2	1

Post Adoption IAS Period (2005-2009)

According to the results of panel regression under post adoption period the earnings per share is positively significantly value relevant of market value per share. The coefficient of earnings per share is 2.011. Again in this period book value per share is not significantly value relevant of market value per share.

Table 7

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	294.5523	464.5152	0.634107	0.5267
BVPS	-24.2956	46.39279	-0.52369	0.6011
EPS	2.010878	0.216321	9.295796	0
R-squared				0.806771
Adjusted R-squared				0.779733
F-statistic				43.58876
Prob(F-statistic)				0

*Significant at $p<0.01$

Again it has negative coefficient -24.29. But the strength of R^2 increased during adoption period. Its value now is 0.81. The overall fitness of the model is also significant.

Overall IAS Adoption Period (2000-2017)

At the end we applied pooled least square regression for an overall period from 2000-2017. The results of individual variables are same as of pre and post adoption period. The earnings per share in this period are positively significantly value relevant but the book value per share is not significant value relevant of market value per share. The value of R^2 is 0.70 and overall model is also fit with highly significant F statistics.

Table 8

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	31.77	8.995	3.532	0.1505
BVPS	0.266	0.790	0.336	0.7365
EPS	2.333	0.152	15.325	0
R-squared				0.702066
Adjusted R-squared				0.688902
F-statistic				117.6159
Prob(F-statistic)				0

*Significant at p<0.0

Conclusion

We conducted the study to determine the value relevance of earnings per share and book value per share of market value per share under IAS adoption and IAS not adoption. No much research is done with reference to Pakistan under this scenario. We applied pooled regression analysis for pre, post and overall period. On the basis of the results of our study we conclude that the earnings per share are value relevant accounting information in pre and post adoption period. The determination of value relevance during post adoption period is more than pre adoption period. So as per our results we recommend that investment decisions can be taken on the basis of information provided in annual reports of companies. The adoption of IAS will reduce the asymmetry of information and earning mismanagement due to full disclosure accountancy practice. The regulatory bodies should consider that the adoption of IAS is beneficial so they should accept standards continuously as issued by IASB.

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