

The impact of IFRS adoption on the value relevance of accounting information in Saudi Arabia



What the authors look at:

- The impact of the adopting IFRS accounting standards in Saudi Arabia

What do they do?

- Examine value relevance of accounting earnings and book values before, at the time of, and after the adoption of IFRS (adoption year = 2016)

What do they find?

- Earnings and book values are value-relevant before and after the adoption of IFRS
- Increase in value-relevance of book values after adoption
- Large firms, profitable firms and Big 4 clients have more value-relevant accounting

IFRS adoption in Saudi Arabia

Background

- IFRS accounting standards adopted widely throughout world from 2005
- Adoption provides a natural 'quasi-experimental' setting as the year of adoption financial statements include restated amounts for the prior year (ie both local GAAP and IFRS are reported)
- This allows measurement of performance for adoption year using both original local GAAP and new IFRS


Why look at value-relevance?

- Value-relevance of aggregate book value and earnings is a natural place to look for the impact of IFRS adoption given the paramount role of equity valuation in the IFRS conceptual framework
- Earnings and book value can be viewed as summary descriptors of value

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Prior research

- IFRS adoption has been widely studied
- This is good! It's clearly considered important

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[P Clarkson](#), [JD Hanna](#), [CD Richardson](#)... - *Journal of Contemporary ...*, 2011 - Elsevier
In this study, we investigate the **impact of IFRS adoption** in Europe and Australia on the relevance of book value and earnings for equity valuation. Using a sample of 3488 firms that initially adopted International Financial Reporting Standards (IFRS) in 2005, we are able to ...
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The impact of IFRS adoption on value relevance of earnings and book value of equity: the case of emerging markets in African and Asian regions
[S Chebaane](#), [HB Othman](#) - *Procedia-Social and Behavioral Sciences*, 2014 - Elsevier
The purpose of this study is to examine the effect of mandatory adoption of International Financial Reporting Standards on the **value relevance** of earnings and the book value of equity. The evidence derived from the study suggested that despite the strength in the ...
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[C Isaboke](#), [Y Chen](#) - *International Journal of Accounting & Information ...*, 2019 - emerald.com

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Lots of prior research

- Challenge: how to contribute something to ensure interest beyond the 'country of focus'?
- Consider what makes Saudi Arabia different from other environments, and **try to build that into your predictions / tests**

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Potential differentiating items

- The financial reporting regime
- Local GAAP similarity to IFRS
- Socio-economic context
- Industry composition of market (especially combined with accounting rule differences) [*it would be helpful to see the industry composition of your sample*]
- Culture
- Did any of these change around the adoption of IFRS?

These factors will help inform us about the extent to which IFRS adoption might 'matter', and explain variation in the change in value-relevance around adoption

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Methodology

- 'Standard' linear functional form

$$P_{it} = a_0 + b_1 BVPS_{it} + b_2 EPS_{it} + e_{it}$$

- Coefficients b_1 and b_2 test V-R of book value and earnings, R^2 shows combined V-R

$$\begin{aligned} P_{it} &= b_0 + b_1 DV_{IFRS} + b_2 EPS_{it}^{IFRS\&Saudi\ GAAP} + b_3 BVPS_{it}^{IFRS\&Saudi\ GAAP} \\ &+ b_4 EPS_{it}^{IFRS\&Saudi\ GAAP} * DV_{IFRS} + b_5 BVPS_{it}^{IFRS\&Saudi\ GAAP} * DV_{IFRS} + e_{it} \end{aligned}$$

- Tests for changes in the the relative value relevance of accounting information in the pre & post periods

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Results

Table 3

Regression results

Panel A: Pre- and post-IFRS value relevance of accounting information: H1 and H2

$$P_{it} = a_0 + b_1 BVPS_{it} + b_2 EPS_{it} + e_{it}$$

Accounting standards	Year	No.	EPS	BVPS	Adj. R ²	Combined Adj. R ²
Saudi GAAP	2015	110	5.493	0.195	44.70%	41.5%
			(25.756)**	(0.333)	45.071**	
IFRS	2016	110	5.01	0.323	37.10%	{78.540}**
			(15.448)**	(0.765)	33.116**	
IFRS	2017	110	5.423	0.78	49.20%	50.8%
			(12.705)**	(4.582)*	53.713**	
IFRS	2018	110	6.728	0.849	52.70%	{114.265}***
			(40.650)**	(13.871)**	61.748**	

Coefficient on book value is low compared with other countries – worth examining?

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Results

$$P_{it} = b_0 + b_1 DV_{IFRS} + b_2 EPS_{it}^{IFRS \& Saudi GAAP} + b_3 BVPS_{it}^{IFRS \& Saudi GAAP} + b_4 EPS_{it}^{IFRS \& Saudi GAAP} * DV_{IFRS} + b_5 BVPS_{it}^{IFRS \& Saudi GAAP} * DV_{IFRS} + e_{it}$$

Accounting standards	Year	N	EPS*DV IFRS	BVPS*DV IFRS	Adj. R ²	Max. VIF
IFRS and Saudi GAAP	2015-2018	440	0.692 (0.39)	0.551 (.013)*	45.70% {124.098}**	1.466

Wald Chi-Square test and F-test value are in (.) and {.} respectively *and ** indicate a significance at the 0.05 and 0.01 level respectively

Change in coefficient on book value is statistically significant – again, worth investigating

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Other considerations

- Early adopters?
- Descriptive statistics show extreme values for some accounting variables; what happens if you winsorize?
- Scaling is on a per share basis - are results robust to alternative scaling methodologies?

Good luck with the paper!