

IFRS adoption and capital flows sensitivity to global uncertainty in Latin America

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Discussion

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High-level summary

■ WHAT

- effect of IFRS adoption on (the volatility of) cross-border capital inflows in Latin America

■ WHY

- impact of country-level IFRS adoption on macro variables is of key practical and academic interest (Ball 2023: “The economic role of an accounting regime is to increase welfare through its effects”)

■ HOW

- regressions of level (and volatility) of cross-border capital inflows on a composite IFRS adoption score (plus market integration and international uncertainty)

Why the paper fits this conference well

- ✓ From the IASB's original call for papers:
„Academics are invited to submit papers on the ... costs and ***benefits of IFRS Accounting Standards***”
- ✓ From this week's IFRS Advisory Council meeting in London:
„Many jurisdictions benefit from IFRS Standards. How do we articulate these benefits to ensure **jurisdictions contribute** to the costs incurred to generate these benefits?”
- ✓ From a keynote speech by Khrystyna Bochkay (University of Miami, Academic Advisor to the IFRS Foundation) at conference at the University of Waterloo in October:
“Academic research should give greater attention to **context**” (paraphrased)

Some thoughts for extending the paper

What is driving what?

audit and enforcement

e.g., Brown, Preiato and Tarca
(2014): AUDIT, ENFORCE

e.g., Christensen et al. (2013)

IFRS adoption (X) → capital flows (Y)

Omitting *enforcement*—an important modifier of the IFRS effect—does not bias β_1 in Eq. 1. But it does conceal important cross-country heterogeneity in the IFRS effect on capital flows.

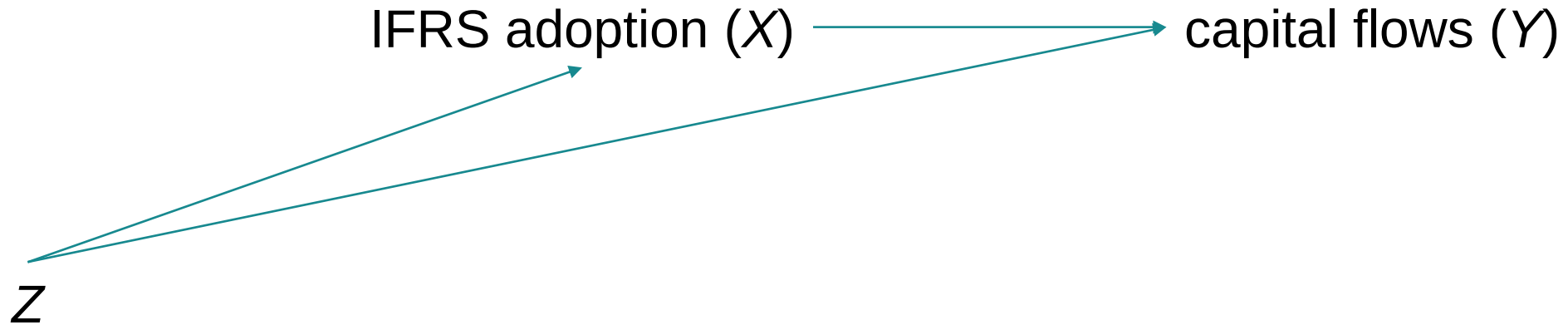
- Table 6 results suggest: “Just adopt IFRS, and capital will flow.”
- More realistically, perhaps: “IFRS is part of a package that includes credible enforcement.”
- Ball (2023): “The economic role of an accounting regime is to increase welfare ... —in conjunction with **complementary institutions**”.

Some thoughts for extending the paper

What is driving what?

A potential confounder Z : **network effects** (Ramanna and Sletten 2014)—the perceived trade benefits from economic ties with other IFRS-adopting countries.

Omitting Z means that what looks like an “IFRS effect” is actually an effect of “IFRS plus being plugged into the IFRS network.”



e.g., Ramanna and Sletten's
(2014) network effects

For example, countries trading more with the EU (the U.S.) should see a greater (lower) effect of IFRS adoption on inbound capital flows.

Some thoughts for extending the paper

Establishing causality ...

- ... seems important here—since standard setters care about what to expect when IFRS is adopted.
- ... is, of course, hard in archival studies. But you might get closer. Consider:
 - a control sample of otherwise similar countries (difference-in-differences)
 - more (institutional) detail about the assumed causal mechanism; e.g., how do the six sample countries differ...
 - ... from each other
 - ... from similar countries adopting IFRS earlier, later, or not at all
 - company-level analyses (as IFRS benefits should differ predictably across companies)

Some thoughts for extending the paper

What is it about *IFRS Adoption* that causes these effects?

type and extent of adoption (70%)

“not adopted (0.00), formal commitment (0.10), early/voluntary/partial adoption (0.20), or mandatory/full adoption (1.00). In the latter case, adoption is further broken down into four domains: public domestic consolidated statements (0.50), separate/individual statements (0.30), foreign firms (0.10), and non-public firms (0.10), each weighted by the extent of requirement (e.g., permitted, required, or not allowed).”

endorsement (30%)

“(i) which IFRS version is adopted (0.40), (ii) whether IFRS has force of law (0.30), (iii) whether there are changes to the original standards (0.20), and (iv) whether standards are translated (0.10). Each receives a grade according to specific classifications.”

*similarity of prior
GAAP to IFRS*
(Bae, Tan and
Welker 2008)

IFRS Adoption Score $\in [0,1]$

~ Ramanna and Sletten's
(2007) „degree of IFRS
harmonization“ ($Adoption_{i,t}$)

IFRS_Adopt $\in \{0,1\}$

IFRS_Commit $\in \{0,1\}$

IFRS_Mand $\in \{0,1\}$

...

IFRS_Transl $\in \{0,1\}$

Minor points

- You standardize capital flows by GDP.
 - Could your effects be driven by shifts in the denominator?
 - Would it be better control for GDP in the regression?
- Modeling time-varying volatility of capital inflows using a GARCH(1,1) process, after filtering out predictable components with a SARIMA model. That makes very clever use of your limited data!
 - But: Everything hinges on GARCH(1,1) being a reasonable description of volatility dynamics. If capital flows have jumps or structural breaks, GARCH is a blunt instrument.

Points in conference discussion

- Ulf Brüggemann: Is capital flow data quality constant over the analysis period? Is it affected by IFRS adoption itself?
- Ann Jorissen: Does the World Bank mandate countries to make certain institutional changes along with IFRS adoption?
- Seema Jamil-O'Neill: Explore differences in endorsement

Concluding remarks

- Valuable focus on six Latin American countries that are often underrepresented.
- Citing Ball (2023) again: „the partial correlations and average effects that occupy the archival literature can provide poor, misleading, or even meaningless proxies for welfare effects”
 - A single average effect across countries is a bit like asking how far the “average animal” can fly.
 - Enforcement quality and IFRS network integration may both drive capital flows and shape the IFRS effect—and could be explicitly modeled.
 - *IFRS adoption* variable aggregates several distinct dimensions that could be explored separately.
- Strong starting point—exploring (sources of) heterogeneity within the 6 and comparing to other regions would make it even more insightful for standard setters and policymakers.



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Good luck with the paper!

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