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CONVERGENCE OF ACCOUNTING STANDARDS: IMPLICATIONS TO THE NIGERIAN ECONOMY

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ABSTRACT

The study sought to empirically determine the effect of the disclosures and presentation of accounting information in line with International Financial Reporting Standards on the Nigerian economy. It investigated whether IFRS adoption suits the Nigerian economy in terms of Foreign Direct Investment, and market capitalization. In order to capture the macro-economy as a whole, control variables were introduced into the models which were inflation, corruption, human capital development and monetary policy rate. The granger causality test and multiple regression analyses were used to analyse the data. The findings reveal that IFRS adoption had a significant positive effect on FDI. Market capitalization however, was not affected by IFRS adoption. The study concludes that IFRS adoption significantly affects the Nigerian economy though this effect is dependent on other economic factors as outlined in the control variables. It is therefore recommended that a hybrid form of accounting standard (IFRSs and SASs) is adopted to fit the Nigerian environment.

Keywords: International Financial Reporting Standards [IFRS]; Foreign Direct Investment [FDI]; Market Capitalisation.

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Introduction

Corporate organizations have sought ways of improving transparency by disclosing relevant and reliable information in financial reports. Accurate, relevant and reliable disclosures are seen as means of enhancing corporate image, reducing cost of capital, and improving marketability of shares. High-quality accounting information no doubt, facilitates the acquisition of short and long term fund and also enables management to properly account for the resources put in their care. Thus, it acts as a significant spur to the growth and development of money and capital markets, which are fundamental to the smooth running of any economy. The increasing growth in international trade, cross border financial transactions and investments which unavoidably involves the preparation and presentation of useful accounting reports across various national borders, has brought about the adoption of IFRS by both the developed and developing countries (Armstrong, Barth, Jagolinzer, & Riedl, 2007). Recently, 123 countries have either required or permitted the use of International Financial Reporting Standards (IFRS) in their jurisdictions, indicating that the acceptance of IFRS has been growing substantially (IASPlus, 2010). It appears that the global convergence of national accounting standards and International Accounting Standards (IAS, superseded by IFRS) has been successfully achieved (IASB, 2007).

As a result of this rapid diffusion of IFRS, it is expected that countries adopting IFRS would have higher degree of transparency and comparability of financial reporting, would decrease asymmetric information and at the end would attract more investment and foster higher international trade. Barone and Mcleay (2013) supported this stating that accounting regulators and their agencies work to a remit of setting standards that will govern the corporate financial information essential to the efficient functioning of an economy. In accounting terms, this objective is seen as the provision of 'credible, transparent, comparable, and unbiased' financial statements. Nevertheless, preparing and auditing information to such standards is costly, and for that reason new accounting rules and regulations are expected from standard setting agencies only when the improvement in quality and the consequent economic impact justify the cost of preparation and dissemination (FASB, 2013).

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The transition to IAS/IFRS has meant fundamental changes for many companies and economies alike. IAS/IFRS conversion has not been viewed simply as an accounting exercise, but as a change in national GAAP (generally accepted accounting principles) and in whole basis of financial reporting. IAS/IFRS information has affected the perception of firm's business performance, and firms have been enabled to produce IAS/IFRS financial statements that allow them to adopt a global financial reporting language as well as to be evaluated in a global marketplace (PricewaterhouseCoopers, 2004).

The Federal Executive Council on July 28, 2010 outlined a roadmap for the adoption of the International Financial Reporting Standards (IFRS) in Nigeria in view of the country's aim to become one of the fastest growing economies by the year 2020.On June 3, 2011, the Financial Reporting Council of Nigeria Act, 2011 (the "FRC Act") established the Financial Reporting Council of Nigeria ("FRC") and repealed the Nigerian Accounting Standards Board Act No. 22 of 2003 ("NASB Act") which had established the NASB (Akindele 2012). An important difference between IFRS and Nigeria GAAP is that IFRS place much greater reliance on the use of fair value and reported measures of earnings (Jones & Higgins, 2006). However, it is important to note that the primary objective of financial reporting based on IFRS is to provide high quality financial reporting information concerning economic entities, primarily financial in nature, useful for economic decision making (FASB, 2008). Providing high quality financial reporting information is important because it will positively influence capital providers and other stakeholders in making investment, credit and similar resources allocation decision enhancing overall market efficiency (IASB, 2007).

Okoye and Akenbor (2014) opined that it is expedient for Nigeria to adopt a global standard because many Nigerian companies have securities of foreign companies. Hence, IFRS will result to a better decision about the flow of economic capital. A number of researchers have also identified the benefit IFRS is deemed to produce. According to Mary, Okoye and Adediran (2013) the adoption of IFRS in Nigeria will open opportunities for a larger finance transformation for firm and upturn the centralization of economies of scale. The Financial Reporting Council of Nigeria mandated public companies to adopt IFRS in 2012, Public sector organizations 2013 and SMEs 2014. This makes five years in which financial reports have been prepared in adherence with IFRS.

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The study seeks to provide empirical evidence as to whether these years of IFRS adoption have spelt improvement or decline in the Nigerian developing economy at large especially since IFRS was not prepared considering our legal environment. One of the major reasons for adopting IFRS in developing economies is to attract investments from foreign countries and foster economic growth (Lin, 2012). Lasmin (2011) stated that Botswana, Haiti, Nepal, Panama, Papua New Guinea, Tajikistan, and Venezuela are among countries that substantially adopt IFRS have not able to obtain desirable economic benefits from the adoption. However, there is no clear evidence suggesting that IFRS adoption has significantly increased foreign investments in Nigeria, although there is some evidence suggesting that IFRS adoption has reduced home bias among foreign investors and improved capital allocation efficiency in developed economies. This creates an inclination to know whether Nigeria's economy benefits from the adoption of IFRS in terms of higher value of foreign direct investment and market capitalization.

The study proposes these hypotheses in their null forms. They are:

Ho_1: The adoption of IFRS has no significant effect on Foreign Direct Investment in Nigeria.

Ho_2: The adoption of IFRS does not significantly affect Market Capitalization in Nigeria.

Review of Related Literature

2.0 Conceptual Review

2.1.1 International Financial Reporting Standards [IFRS]

International Accounting Standards Board (2007) defined International Financial Reporting Standards (IFRS) as a single set of high-quality, understandable and enforceable accounting standards that require high quality, transparent and comparable information in financial statements and other financial reporting to help participants in the world's capital markets and other users make economic decisions. On the history of IFRS and convergence, The International Accounting Standards Committee was established in 1973 by professional accounting bodies of Australia, Mexico, France, Ireland, Japan, the Netherlands, Canada, the UK, Germany and the US.

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The objectives of the IASC stated in its Constitution (2000) are: to develop in the public interest, a single set of high-quality, understandable and enforceable accounting standards that require high quality, transparent and comparable information in financial statements and other financial reporting to help participants in the world's capital markets and other users make economic decisions; to promote the use and rigorous application of those standards; to bring about convergence of national accounting standards and International Accounting Standards to high quality solutions (IASB, 2007). IFRS draw upon the Conceptual Framework that has been adopted by the IASB from the IASC. The framework is most importantly used as a guide to the IASB in developing IFRS. The framework provides a set of concepts for the development of IFRS and should be seen as a frame of reference for IASB members when deliberating these standards. Furthermore, the framework is valued for maintaining consistency in IFRS, since each promulgated standard is based on the Conceptual Framework. Besides, the framework serves as reference point to preparers and auditors of financial statements in resolving accounting issues where standards are lacking.

Van-Tendeloo and Vanstraelen (2005) point out four advantages resulting from IFRS adoption. *First*, such adoption will trigger greater investors' ability to make informed financial decisions, eliminating confusion that arises from the existence of different ways to measure status and financial performance in different countries, leading to reduced risk for investors and lower cost of capital for companies. *Second*, it will lead to reduced costs related to preparation of financial information according to several sets of standards. *Third*, it will lead to greater incentives for international investment. *Fourth*, it will allow a more effective allocation of financial resources worldwide. Despite the advantages usually associated with convergence to IFRS, the effect of adopting this set of standards is still a matter of debate (Hail, Leuz, & Wysocki, 2010). Onafalujo, Ekeh and Akinlabi (2011) also stated that IFRS is a global agenda to foster common benchmark in financial information across international borders with the aim of generating greater momentum for economic development.

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According to IMF (2004), Foreign Direct Investment (FDI) occurs when there is an investment in a business organization by an investor from a foreign country. Foreign companies engaged in foreign direct investment are normally exposed to business environment and systems that are different from their home country. It is important that these foreign companies are aware of the country differences for the purpose of establishing or maintaining an efficient global operation. Accounting standards compliance and harmonization constitute an important issue as a company can find it difficult to follow different accounting standards for the same business structure in different countries. Adetula and Owolabi (2014) posit that IFRS was adopted in Nigeria to improve corporate transparency especially in financial terms which in turn should lead to increase in Foreign Direct Investment (FDI).

Proponents of the IFRS argue that IFRS is capital – market oriented and thus is more relevant to capital markets and investors than other local accounting standards. They justify that by referring to several arguments such that reporting under the IFRS is less costly for investors to compare firms across markets and countries, facilitates cross-border investments, and enhances capital market integration (Covrig, Defond, & Hung, 2007). Roberts, Weetman and Gordon (2002) stated that standards pronounced by the IASB have positively affected the efficiency of global capital market, and this fact is admitted by International Organization of Securities Commissions (IOSCO) that in May 2000 IOSCO recommended its members to use IFRS as a basis to prepare financial statements. Biddle and Hillary (2006) found that high quality accounting information reduced the investment-cash flow sensitivity in market-based economies (strong investor protection) but not in bank-based or creditor-dominated economies.

2.1.2 Inflation Rate

Inflation rate had generally been on the increase in Nigeria even when there is small volume of money in the circulation, which in a way affects interest rate, the increase or decrease in exchange rate affects the demand for money. The demand for money affects the economy negatively especially when it is cash outflow.

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2.1.3 Human Capital Development

Thus, human capital is regarded at the macro level as a key factor of production in the economy-wide production function. From a microeconomic perspective, education increases the probability of being employed in the labour market and improves earnings capacity (ADB, 2010). The World Bank (2010) specifies that Nigeria has found it difficult to grow her economy in her quest to become a knowledge-based economy because of the challenges faced in the national educational system.

2.1.4 Corruption

Corruption is a disease, which eats into the cultural, political and economic growth of any country and as well destroys the functioning of various organs of the government (Okoye & Gbegi, 2013). It is one of the greatest challenges of the contemporary world which undermines good government, fundamentally distorts public policy, leads to the misallocation of resources harms the private sector development and as well hurts the poor (Transparency International, 2014). Corruption leads to the depletion of our national wealth. Corruption also reduces economic growth, enhances inequalities and reduces the government's capacity to respond to people's needs. In Nigeria, corruption is one of the reasons for many unresolved problems that have critically hobbled and reduce development (Ayobolu, 2006). It also remains a long-term major political and economic growth challenge for Nigeria (Sachs, 2007). Abiodem (2007) in World Bank studies rated corruption as accounting for up to 15% of the Gross Domestic Product of Nigeria.

2.2 Theoretical Perspective

The study is anchored on the enterprise theory. Suojanen (1954)'s enterprise or social theory sees the large listed corporation as an institution with social responsibilities. Companies' actions affect many different stakeholders such as stockholders, creditors, customers, employees, the government as a taxing and regulatory authority and the public at large (Hendriksen &Van Breda, 1992). Financial reports according to the enterprise theory are to be prepared from the perspective of the enterprise as a social institution. This study on IFRS implications on the economy views financial reporting as socially and economically inclined.

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2.3 Review of Empirical Literature

Daske, Hail, Leuz and Verdi (2008) examined the economic effects of IFRS adoption for both voluntary and mandated adopters. They found that the adoption of IFRS creates unassailable economic gains in countries with uncompromising regulation over financial reporting. These benefits include an enhancement in the stock's market value, an increase in market liquidity, and a lower cost of capital. Okpala (2012) found that IFRS implementation will promote FDI inflows and economic growth after analyzing responses from 123 structured questionnaires.

Zeghal and Mhedhbi (2012) analyzed the consequences of using international accounting standards for the development of capital markets located in emerging capital markets and found that the development of the emerging capital markets is positively and significantly associated with the use of international accounting standards.

Zaidi and Huerta (2014) used ordinary least square and two stage least square regression to analyze the relationship between the adoption of IFRS and economic performance on 51 countries that adopted IFRS and 51 countries that have not yet adopted IFRS. They found that IFRS adoption lifts the economic growth rate of the country and countries that adopted IFRS gain much more economic benefits when there is a high level of enforcement.

Ozcan (2016) investigated whether the adoption of IFRS fosters countries' economic growth. Findings revealed that IFRS adoption has significantly increased countries' economic growth. The adoption of IFRS is not the sole factor affecting countries' economic growth rate. Other factors such as education policy, human capital, geographical factors, and political structure also influence the economic development rate. The study is a meaningful contribution to accounting literature on accounting standards in developing countries and fills the gap of empirical investigation of the effect of IFRS adoption on the Nigerian economy in aggregate terms.

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Design and Methodology

This study used *ex-post facto* design. The study was carried out using secondary data obtained from 2016 CBN statistical bulletin, Federal Inland Revenue Service reports and World Bank Database. Corruption Indices was extracted from Corruption Perceptions Index Transparency International. 10% level of significance was adopted to give increased probability of results for the low number of years of time series. The Ordinary Least Squares (OLS) multiple regression approach was used to analyse the secondary data used in testing the hypotheses.

Model specification

The study used an ordinary least square (OLS) estimation which is defined as:

$Y = f(IFRS, INF, HCD, COR)$

$Y_1 = \beta_0 + \beta_1 IFRSi + \beta_2 INFi + \beta_3 HCDi + \varepsilon i$……..1

$Y_2 = \beta_0 + \beta_1 IFRSi + \beta_2 INFi + \beta_3 HCDi + \varepsilon i$……..2

Where:

Y_1 - Market Capitalisation
Y_2 - FDI

Data Analysis and Results

Table 1: Least Squares Result for Market Capitalisation

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-7.24E+13	5.89E+13	-1.229197	0.3066
IFRS_ADOPTION	-1.47E+12	2.34E+12	-0.629021	0.5740
INFLATION	-1.97E+12	9.82E+11	-2.007153	0.1384
MPR	-4.36E+11	7.65E+11	-0.570218	0.6084
HDI	9.05E+13	1.18E+14	0.769419	0.4977
CORRUPTION	2.48E+12	1.69E+12	1.463914	0.2394
GCE	3.992681	8.952983	0.445961	0.6858

R-squared	0.901690	Mean dependent var	1.23E+13
Adjusted R-squared	0.705071	S.D. dependent var	4.63E+12
S.E. of regression	2.51E+12	Akaike info criterion	60.13823
Sum squared resid	1.89E+25	Schwarz criterion	60.35004
Log likelihood	-293.6912	Hannan-Quinn criter.	59.90588
F-statistic	4.585963	Durbin-Watson stat	1.567113
Prob(F-statistic)	0.119506		

Source: E-Views 9

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The table above revealed the effect of IFRS adoption on market capitalization. The t statistic (-0.629) had probability value of 0.5740. This is greater than the probability value adopted for the study (0.1) and implies an insignificant negative effect of IFRS adoption on market capitalization. The coefficient of determination (R^2) implies that a very huge proportion of 90.1 % of the variation in Market Capitalization is explained by all the explanatory variables under consideration. The adjusted R^2 (0.70), Akaike info criterion (60.13) and Schwarz criterion (60.35) further confirmed the position of our R^2, which adjudged the model as a "best goodness of fit". The Durbin Watson result of 1.56, within the context of sample size used for this research clearly shown the non-existence of autocorrelation. The implication being that the model has been correctly specified.

Decision Rule:
The result of F statistic shows that all the regression coefficients is not statistically significant at 10% level of significance for the years under consideration. Hence we accept the null hypothesis that the adoption of IFRS does not significantly affect Market Capitalization in Nigeria.

Table 2: Least Squares Result for FDI

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	64.25116	11.88432	5.406381	0.0124
IFRS_ADOPTION	1.101463	0.471802	2.934588	0.0517
INFLATION	0.257390	0.198026	1.299779	0.2845
MPR	0.203927	0.154271	1.321874	0.2780
HDI	-125.9877	23.73573	-5.307934	0.0131
CORRUPTION	-0.384712	0.341238	-1.127400	0.3416
GCE	6.19E-12	1.81E-12	3.426458	0.0416

R-squared	0.961325	Mean dependent var	2.360000
Adjusted R-squared	0.883976	S.D. dependent var	1.487877
S.E. of regression	0.506806	Akaike info criterion	1.674649
Sum squared resid	0.770556	Schwarz criterion	1.886458
Log likelihood	-1.373243	Hannan-Quinn criter.	1.442294
F-statistic	12.42833	Durbin-Watson stat	1.284005
Prob(F-statistic)	0.031752		

Source: E-Views 9

The table above revealed the effect of IFRS adoption on Foreign Direct Investment. The model controlled for certain macro-economic factors. IFRS adoption had coefficient of 1.101463. It can be interpreted that as the adoption of IFRS increases by one percent (1%), FDI increases by 1.1% of GDP. The t statistic (2.934) had probability value of 0.0517. This is

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lower than the probability value adopted for the study (0.1). This implies a significant positive effect of IFRS adoption on FDI. Government capital expenditure had a positive coefficient and are each significant at 1 percent. GDP, inflation, monetary policy rate and corruption are statistically insignificant. Human Development Index is significant at 10 percent but with an unexpected negative coefficient. The coefficient of determination (R square) implies that a very huge proportion of 96.1 % of the variation in Foreign Direct Investment is explained by all the explanatory variables under consideration. The adjusted R square (0.88) further confirmed the position of our R square, which adjudged the model as a "best goodness of fit". The Durbin Watson result of 1.28, within the context of sample size used for this research clearly shown the non-existence of autocorrelation. The implication being that the model has been correctly specified.

Decision Rule:
Accept null hypothesis if p value of F is greater than 0.1, otherwise, reject. The result of F statistic shows that all the regression coefficients is statistically significant at 10% level of significance for the years under consideration. Hence we accept the hypothesis that IFRS adoption significantly affects FDI.

Discussion of Findings

The results showed that the adoption of IFRS increased foreign direct investment in Nigeria for the period of study. IFRS adoption helps IFRS-users from other countries to understand financial information which in turn reduces information asymmetries and costs between users of financial statements in different countries. This could imply that adopting IFRS brought in harmonization with international standards and made international investors more familiar with reporting as they do not need a Nigerian-based qualified accountant to explain information presented in reports from the scratch. The results support IFRS adoption having an important effect on reducing information costs and investor uncertainty. This encourages FDI as revealed in the study. This is consistent with Okpala (2012), Ozcan (2016) and Akpomi and Nnadi (2017). They found that IFRS adoption will promote FDI inflows and economic growth. Adetula et al (2014) however found no significant effect.

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Conclusion and Recommendations

This study investigated the suitability of IFRS adoption to the Nigerian economy in terms of FDI and market capitalization. In order to capture the macro-economy as a whole, control variables were introduced into the models which were inflation, corruption, human capital development and monetary policy rate. Foreign Direct Investment was found to be benefit from IFRS adoption. This was attributed to the motivation of direct investors to invest since there is less information asymmetry as standards in Nigeria and certain foreign countries have same reporting patterns which are guided by IFRS. International Trade (net exports) was found to reduce significantly with IFRS adoption. The study however takes into cognizance other economic factors as represented by control variables that make Nigeria an import-dependent economy and thus reduces exports.

Based on this finding, the study recommends that regulatory agencies should take measures to ensure that institutions adopt IFRS to increase FDI. Though the capital market is not affected, IFRS adoption is necessary to ensure uniformity of presentation of information of listed companies. Also, IFRS might not be optimum given Nigeria's peculiar environment since IFRS were established based on international environments. A hybrid form (IFRSs and SASs) is thus recommended.

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