Impact of International Financial Reporting Standards on Stock Price Synchronicity and Cost of Capital in the Asian Countries

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ABSTRACT

International Accounting Standard Board (IASB) has issued International Financial Reporting Standards (IFRS) for better comparability and use of financial statements around the world. Most of the countries have already started adopting IFRS which are of high quality. Several studies have provided evidence suggesting financial statements under IFRS are more informative, relevant and transparent than those made under national accounting standards in the respective countries. Stock synchronicity and Cost of Capital are important issues to be studied after the adoption of a new standard i.e. IFRS. Synchronicity of Stock Price is found to be closely related to economic development and stock market stability in a country. It determines the relative amount of firm-level and market-wide information that is embedded to the stock prices. After adoption of IFRS there is a rise in corporate disclosures which makes stock prices more informative. IFRS adoption also leads to a decrease in the cost of equity capital by removing the existing information asymmetry, both between companies and investors. Most of the literature till date has findings and implications of IFRS in terms of European countries, especially for the period 1990-2005 as European countries had an early start. Here we are interested to see the impacts of adopting the standards on Asian countries which have recently begun to make IFRS mandatory in their financial reporting but there is little empirical evidence available.

The present study examines whether adoption of IFRS reduces Stock price Synchronicity and Cost of equity Capital for firms in Asia. The sample consists of firms from four Asian Countries, namely China, Hong Kong, Israel and Philippines, where IFRS has been made mandatory. Data for Six years covering the period from 2006-2012 has been taken for analysis. Two empirical models (Stock Price synchronicity and IFRS) & (Cost of equity capital and IFRS), and other firm specific control variables were analysed using both univariate and multivariate techniques. Different types of panel data estimates were used and compared so as to interpret the results with the best suited parameters for different data sets for different countries. The empirical results for the first objective supports the argument for all the four countries (China, Hong Kong, Philippines and Israel) that IFRS adoption improves information environment by incorporating the firm-specific information into stock prices by which stock price synchronicity reduces. For the second objective, the results vary for different countries. The firms in Hong Kong and Philippines get benefit from the reduction in their cost of equity capital after adopting IFRS, but for firms in China and Israel cost of equity capital increased. The finding indicates that the firm-specific characteristics play a crucial role in their intrinsic motivation for reporting under IFRS, thereby enjoying the benefits.

The study contributes to the understanding of economic and informational consequences of adopting IFRS across Asian countries. Another contribution of the research is to ascertain whether IFRS adoption affected sectors within each country or across countries differently. The findings would be important not only to countries that have already adopted IFRS, but also to countries that are in the process of adopting the standard. The outcomes will have important implications for the regulators, practitioners, academicians and auditors, as well as end-users of financial statements.

A limitation to the finding of this thesis is that the impact of the movement to IFRSs in the Asian context needs a longer period to be effectively evaluated as important countries such as India, Japan and Singapore are yet in the process of convergence or making IFRS mandatory, to truly reflect the difference in IFRSs impact on different sets of accounting environments.

Keywords: International Financial Reporting Standards, Stock Price Synchronicity, R^2; Firm-specific return variation; Informativeness of stock prices, Cost of equity capital, Panel data

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