IFRS CONVERGENCE AND EARNINGS FORECASTS: MALAYSIAN IPO COMPANIES

By

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ABSTRACT

The study sheds light on the Malaysian initial public offering (IPO) management earnings forecasts by examining the effect of International Financial Reporting Standards (IFRS) convergence and the forecast errors. It examines whether the convergence of IFRS is a credible signal of improved quality of financial information. Besides, the study also investigates the other factors that influence the forecast errors of the earnings forecasts. A sample of 98 IPO companies that went public during the period 2004-2007 is used. The time frame of this study includes the years 2004 to 2005 (i.e., pre-IFRS convergence) and years 2006 to 2007 (i.e., post-IFRS convergence). Forecast errors as a dependent variable is used to proxy the earnings forecast error and to represent financial disclosure quality.

By examining the forecast errors in two different periods (i.e., pre-IFRS convergence & post-IFRS convergence), the study finds that the forecast errors has increased under the post-IFRS convergence. In addition, the findings reveal the size of the company is significantly negative with the forecast errors. This study has implications on the disclosure regulations of earnings forecasts in the prospectuses in Malaysia and provides evidence regarding disclosure of the earnings forecasts being changed from mandatory to voluntary in Malaysia.

ABSTRAK

Kajian ini menyiasat tentang kesan penggunaan Piawai Kewangan Laporan Antarabangsa (PLKA) terhadap unjuran pendapatan pengurusan iaitu ralat ramalan sama ada ralat ramalan menurun atau meningkat selepas penumpuan PLKA. Kajian ini menyiasat sama ada PLKA merupakan salah satu faktor yang menyumbang kepada kualiti penyata kewangan di Malaysia. Selain itu, kajian ini juga menyiasat faktor-faktor lain yang mempengaruhi ralat ramalan kepada ramalan pendapatan. Sampel kajian ini terdiri daripada 98 buah syarikat-syarikat tawaran awam permulaan yang tersenarai di Bursa Malaysia pada tahun 2004 sehingga 2007. Tempoh masa kajian ini meliputi tahun 2004 hingga 2005 (iaitu, sebelum penggunaan PLKA) dan tahun 2006 hingga 2007 (iaitu, selepas penggunaan PLKA). Ralat ramalan digunakan sebagai pembolehubah bersandar untuk mengukur ralat ramalan pendapatan dan mewakili kualiti penyata kewangan.

Dengan membandingkan ralat ramalan dalam dua tempoh yang berbeza iaitu (iaitu sebelum dan selepas penggunaan PKLA), kajian ini mendapati ralat ramalan meningkat selepas penggunaan PKLA. Tambahan pula, hasil kajian ini mendapati saiz syarikat merupakan faktor yang paling mempengaruhi ralat ramalan dan penting secara statistiknya. Kajian ini memberi implikasi terhadap polisi di Malaysia dalam melaporkan ramalan pendapatan dalam prospektus di Malaysia dan menyediakan bukti tentang perubahan dalam melaporkan ramalan pendapatan daripada wajib kepada sukarela.

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LISTS OF ABBREVIATIONS

AGAAP	Australian GAAP
FRA 1997	Financial Reporting Act 1997
FRF	Financial Reporting Foundation
FRS	Financial Reporting Standards
IAS	International Accounting Standards
IASB	International Accounting Standards Board
IASC	International Accounting Standards Committee
IFRS	International Financial Reporting Standards
IPO	Initial Public Offerings
KLSE	Kuala Lumpur Stock Exchange
MASB	Malaysian Accounting Standards Boards
MFRS	Malaysian Financial Reporting Standards
MIA	Malaysian Institute of Accountant
SC	Securities Commission
SOPs	Standards of Procedures

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The interconnectedness of the capital market across the globe has fuelled the demand for the harmonization of the accounting language. Harmonized accounting language, which is widely postulated in literature will add more value to reporting quality, and at the same time, understandability of financial information across different regulatory settings (Stovall, 2010). The International Accounting Standards Board (IASB) has been at the forefront in the course of accounting standards harmonization. The body previously known as the International Accounting Standards Committee (IASC) is committed to developing a single set of accounting standards that can be applied globally. Interestingly, international organizations, like the United Nations, the International Organization of Securities Commissions, the World Bank and the World Trade Organization have endorsed the International Financial Reporting Standards (IFRS) as a set of global high quality accounting standards (Stovall, 2010).

The adoption of IFRS in many reporting jurisdictions will improve financial reporting transparency and comparability and consequently contribute to the efficient functioning of the global capital market (Firth, Gounopoulus and Pulm, 2013). The IFRS has now become a global trend with many countries in the European Union, Asia, Africa and some other continents converting their local standards to IFRS. The IFRS are principle-based accounting standards. Compared to rule-based accounting standards, principle-

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APPENDIX A

Descriptive statistics for all variables for total samples (2004 to 2007), n=100

Statistics

		FE	IFRS	AGE	SIZE	HORIZON	LEVERAGE	AUDITOR	INDUSTRY
N	Valid	100	100	100	100	100	100	100	100
	Missing	0	0	0	0	0	0	0	0
Mean		2.71408	.33	3.0710	268627.09789	7.66	52.386662	.51	.37
Median		.51500	.00	1.3700	97791.50000	7.00	48.391500	1.00	.00
Std. Deviation		40.223542	.473	4.86114	783468.389923	2.992	24.4587572	.502	.485
Minimum		-85.491	0	.15	35122.735	3	3.8612	0	0
Maximum		238.274	1	33.06	6313792.000	13	100.0089	1	1

IFRS

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	PRE-IFRS (2004 AND 2005)	67	67.0	67.0	67.0
	POST-IFRS(2006 AND 2007)	33	33.0	33.0	100.0
	Total	100	100.0	100.0	

APPENDIX A (cont'd)

AUDITOR

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	NON BIG 4	49	49.0	49.0	49.0
	BIG 4	51	51.0	51.0	100.0
	Total	100	100.0	100.0	

INDUSTRY

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	consumer and industrial products	63	63.0	63.0	63.0
	Trading services, Construction, Properties, Technology, Plantation	37	37.0	37.0	100.0
	Total	100	100.0	100.0	

APPENDIX B

Descriptive statistic for pre-IFRS convergence (2004-2005), n=67

Statistics

		FE	IFRS	AGE	SIZE	HORIZON	LEVERAGE	AUDITOR	INDUSTRY
N	Valid	67	67	67	67	67	67	67	67
	Missing	0	0	0	0	0	0	0	0
Mean		-.44263	.00	2.5991	289446.03382	7.85	49.561181	.51	.27
Median		-3.65000	.00	1.2400	93677.00000	8.00	46.730300	1.00	.00
Std. Deviation		46.977902	.000	3.87941	931453.775917	3.031	23.1604443	.504	.447
Minimum		-85.491	0	.15	35122.735	3	3.8612	0	0
Maximum		238.274	0	21.04	6313792.000	13	100.0089	1	1

IFRS

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	PRE-IFRS (2004 AND 2005)	67	100.0	100.0	100.0

AUDITOR

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	NON BIG4	33	49.3	49.3	49.3
	BIG4	34	50.7	50.7	100.0
	Total	67	100.0	100.0	

APPENDIX B (cont'd)

INDUSTRY

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	consumer and industrial products	49	73.1	73.1	73.1
	Trading services, Construction, Properties, Technology, Plantation	18	26.9	26.9	100.0
	Total	67	100.0	100.0	

APPENDIX C

Descriptive statistic for post-IFRS convergence (2006-2007), n=33

Statistics

		FE	IFRS	AGE	SIZE	HORIZON	LEVERAGE	AUDITOR	INDUSTRY
N	Valid	33	33	33	33	33	33	33	33
	Missing	0	0	0	0	0	0	0	0
Mean		9.12315	1.00	4.0291	226358.34918	7.27	58.123245	.52	.58
Median		5.90300	1.00	1.7100	130435.00000	7.00	54.614400	1.00	1.00
Std. Deviation		19.760524	.000	6.37608	326843.092394	2.918	26.3398348	.508	.502
Minimum		-35.099	1	.19	38383.000	3	16.9867	0	0
Maximum		74.577	1	33.06	1903953.000	13	100.0000	1	1

IFRS

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	POST-IFRS(2006 AND 2007)	33	100.0	100.0	100.0

APPENDIX C (cont'd)

AUDITOR

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	NON BIG4	16	48.5	48.5	48.5
	BIG4	17	51.5	51.5	100.0
	Total	33	100.0	100.0	

INDUSTRY

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	consumer and industrial products	14	42.4	42.4	42.4
	Trading services, Construction, Properties, Technology, Plantation	19	57.6	57.6	100.0
	Total	33	100.0	100.0	

APPENDIX D

Descriptive statistics for variables after remove the outliers

Total sample (2004-2007), n=98

Statistics

		FE	AGE	SIZE	HORIZON	LEVERAGE	AUDITOR	INDUSTRY	IFRS
N	Valid	98	98	98	98	98	98	98	98
	Missing	0	0	0	0	0	0	0	0
Mean		-1.04345	3.0954	272670.92642	7.64	52.779039	.52	.62	.34
Median		.28250	1.3450	97947.00000	7.00	48.967850	1.00	1.00	.00
Std. Deviation		29.723785	4.90786	790979.835479	2.999	24.4601690	.502	.487	.475
Minimum		-85.491	.15	35122.735	3	3.8612	0	0	0
Maximum		93.433	33.06	6313792.000	13	100.0089	1	1	1

Pre-IFRS convergence (2004-2005), n=65

Statistics

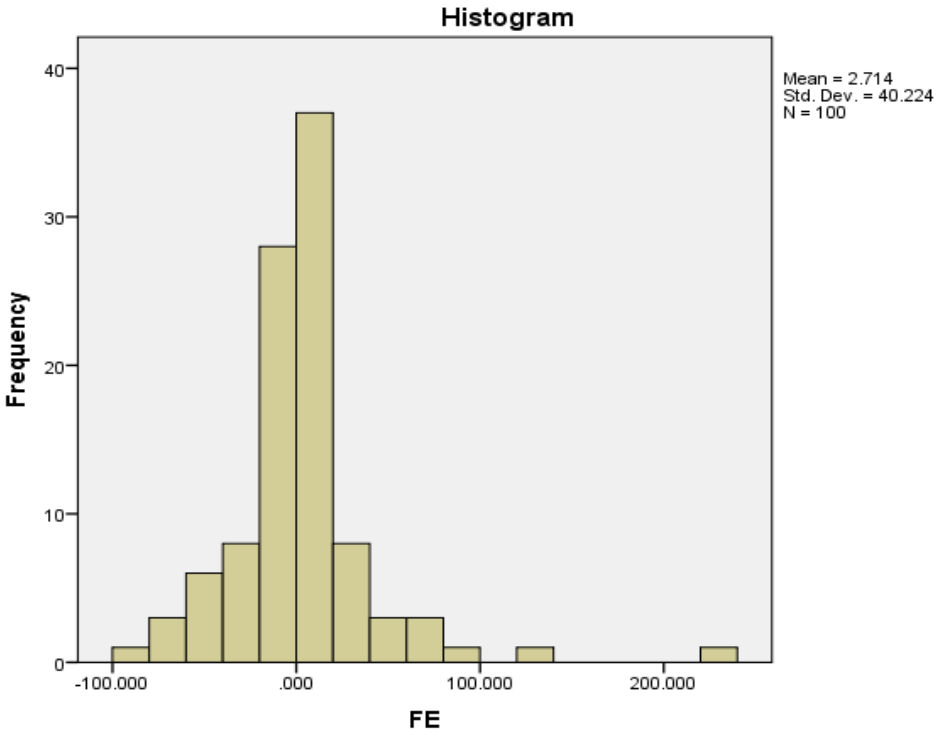
		FE	IFRS	AGE	SIZE	HORIZON	AUDITOR	LEVERAGE	INDUSTRY
N	Valid	65	65	65	65	65	65	65	65
	Missing	33	33	33	33	33	33	33	33
Mean		-6.20495	.00	2.6214	296183.46563	7.83	.52	50.065826	.28
Median		-3.65400	.00	1.1900	94414.00000	8.00	1.00	46.730300	.00
Std. Deviation		32.610863	.000	3.93727	945076.079207	3.044	.503	23.1883960	.451
Minimum		-85.491	0	.15	35122.735	3	0	3.8612	0
Maximum		93.433	0	21.04	6313792.000	13	1	100.0089	1

APPENDIX E

Normality test

Descriptives

			Statistic	Std. Error
FE	Mean		2.71408	4.022354
	95% Confidence Interval for Mean	Lower Bound	-5.26714	
		Upper Bound	10.69530	
	5% Trimmed Mean		-.03214	
	Median		.51500	
	Variance		1617.933	
	Std. Deviation		40.223542	
	Minimum		-85.491	
	Maximum		238.274	
	Range		323.765	
	Interquartile Range		18.757	
	Skewness		2.344	.241
	Kurtosis		12.293	.478



APPENDIX F

Heteroskedasticity

Breusch-Pagan / Cook-Weisberg test for heteroskedasticity
Ho: Constant variance
Variables: fitted values of FE
chi2(1) = 3.62
Prob > chi2 = 0.0571

VIF test

Variable	VIF	1/VIF
IFRS	1.16	0.178563
YEAR	1.17	0.182352
HORIZON	1.19	0.841463
INDUSTRY	1.18	0.845995
AGE	1.14	0.875739
LEVERAGE	1.14	0.880315
AUDITOR	1.12	0.894265
SIZE	1.07	0.934908
Mean VIF	1.03	

APPENDIX G

The Bivariate Pearson correlation between dependent and independent variables

Correlations

		FE	IFRS	AGE	SIZE	HORIZON	LEVERAGE	AUDITOR	INDUSTRY
FE	Pearson Correlation	1	.245*	-.024	-.121	-.071	-.020	.050	.097
	Sig. (2-tailed)		.015	.813	.234	.489	.849	.627	.340
	N	98	98	98	98	98	98	98	98
IFRS	Pearson Correlation	.245*	1	.136	-.042	-.088	.156	-.007	.291**
	Sig. (2-tailed)	.015		.181	.682	.387	.124	.942	.004
	N	98	98	98	98	98	98	98	98
AGE	Pearson Correlation	-.024	.136	1	.075	.284**	-.108	.048	.068
	Sig. (2-tailed)	.813	.181		.465	.005	.292	.639	.505
	N	98	98	98	98	98	98	98	98
SIZE	Pearson Correlation	-.121	-.042	.075	1	-.048	-.122	.190	.133
	Sig. (2-tailed)	.234	.682	.465		.636	.232	.061	.193
	N	98	98	98	98	98	98	98	98
HORIZON	Pearson Correlation	-.071	-.088	.284**	-.048	1	-.210*	-.074	-.133
	Sig. (2-tailed)	.489	.387	.005	.636		.038	.470	.193
	N	98	98	98	98	98	98	98	98
LEVERAGE	Pearson Correlation	-.020	.156	-.108	-.122	-.210*	1	-.192	-.006
	Sig. (2-tailed)	.849	.124	.292	.232	.038		.058	.952
	N	98	98	98	98	98	98	98	98
AUDITOR	Pearson Correlation	.050	-.007	.048	.190	-.074	-.192	1	.200*
	Sig. (2-tailed)	.627	.942	.639	.061	.470	.058		.048
	N	98	98	98	98	98	98	98	98
INDUSTRY	Pearson Correlation	.097	.291**	.068	.133	-.133	-.006	.200*	1
	Sig. (2-tailed)	.340	.004	.505	.193	.193	.952	.048	
	N	98	98	98	98	98	98	98	98

*. Correlation is significant at the 0.05 level (2-tailed). **.Correlation is significant at the 0.01 level (2-tailed)

APPENDIX H

Ordinary Least Square regression analysis for overall samples during period 2004-2007(PanelA)

Panel A (1) - Regression controlling for heteroskedasticity

	Robust					
FE	Coef.	Std. Err.	t	P>t	[95% Conf.	Interval]
IFRS	10.87971	14.45221	0.75	0.454	-17.83653	39.59595
AGE	-.2722865	.4094349	-0.67	0.508	-1.085825	.5412519
HORIZON	-.5380634	.9881346	-0.54	0.587	-2.501466	1.425339
SIZE	-5.02e-06	2.01e-06	-2.49	0.015	-9.02e-06	-1.02e-06
AUDITOR	3.219171	6.125887	0.53	0.601	-8.952836	15.39118
LEVERAGE	-.0938925	.1015118	-0.92	0.357	-.2955942	.1078092
INDUSTRY	1.537956	5.761333	0.27	0.790	-9.90969	12.9856
YEAR	2.069747	6.278306	0.33	0.742	-10.40511	14.54461
_cons	-4145.801	12583.14	-0.33	0.743	-29148.24	20856.63

R-squared = 0.0893 F-Static = 2.21

Panel A (2) - Regression controlling for heteroskedasticity without Year and Industry

	Robust					
FE	Coef.	Std. Err.	t	P>t	[95% Conf.	Interval]
IFRS	15.87954	5.734449	2.77	0.007	4.488762	27.27032
AGE	-.2726505	.4195818	-0.65	0.517	-1.106098	.5607972
HORIZON	-.5383066	.9392115	-0.57	0.568	-2.403935	1.327322
SIZE	-4.92e-06	2.02e-06	-2.44	0.017	-8.93e-06	-9.07e-07
AUDITOR	3.51086	5.958189	0.59	0.557	-8.32435	15.34607
LEVERAGE	-.0972637	.0981634	-0.99	0.324	-.2922533	.0977259
_cons	3.215309	8.83267	0.36	0.717	-14.3297	20.76032

R-squared = 0.0875 F-Static= = 2.96

APPENDIX G

Ordinary Least Square regression analysis for pre-IFRS convergence during period 2004-2005(Panel B)

Panel B(1) - Regression for pre-IFRS

	Robust					
FE	Coef.	Std. Err.	t	P>t	[95% Conf.	Interval]
IFRS	(omitted)					
AGE	-.5361422	.5207235	-1.03	0.308	-1.578873	.5065886
HORIZON	-.9352006	1.336276	-0.70	0.487	-3.611048	1.740647
SIZE	-5.05e-06	2.04e-06	-2.47	0.016	-9.14e-06	-9.57e-07
AUDITOR	7.102965	8.549632	0.83	0.410	-10.01738	24.22331
LEVERAGE	-.1053226	.1621379	-0.65	0.519	-.4299981	.219353
INDUSTRY	-1.212431	7.79777	-0.16	0.877	-16.8272	14.40234
YEAR	1.502613	9.025112	0.17	0.868	-16.56986	19.57509
_cons	-3005.925	18086.5	-0.17	0.869	-39223.51	33211.66

R-squared = 0.0472 F -Static = 1.56

Panel B(2) - Regression for pre-IFRS without year and industry

Robust						
FE	Coef.	Std. Err.	t	P>t	[95% Conf.	Interval]
IFRS	(omitted)					
AGE	-.5714527	.5145517	-1.11	0.271	-1.601068	.4581629
HORIZON	-.8900926	1.244588	-0.72	0.477	-3.380508	1.600323
SIZE	-5.09e-06	1.94e-06	-2.62	0.011	-8.98e-06	-1.21e-06
AUDITOR	7.058407	8.596574	0.82	0.415	-10.1433	24.26011
LEVERAGE	-.1015892	.1623852	-0.63	0.534	-.4265213	.2233429
_cons	5.165769	13.06756	0.40	0.694	-20.98235	31.31389

R-squared = 0.0464 F-Static = 2.04

APPENDIX H

Ordinary Least Square regression analysis for post-IFRS convergence during period 2006-2007(Panel C)

Panel C(1) - Regression for post-IFRS

Robust						
FE	Coef.	Std. Err.	T	P>t	[95% Conf.	Interval]
IFRS	(omitted)					
AGE	-.3373935	.4465059	-0.76	0.457	-1.256989	.5822026
HORIZON	.8033901	.9301612	0.86	0.396	-1.112313	2.719093
SIZE	-9.55e-07	9.05e-06	-0.11	0.917	-.0000196	.0000177
AUDITOR	-7.565755	7.488913	-1.01	0.322	-22.98946	7.857949
LEVERAGE	.0065957	.1490223	0.04	0.965	-.3003214	.3135129
INDUSTRY	10.67941	7.038025	1.52	0.142	-3.815678	25.17449
YEAR	3.735011	8.81282	0.42	0.675	-14.41533	21.88535
_cons	-7492.362	17682.84	-0.42	0.675	-43910.85	28926.13

R-squared = 0.0897 F-Static = 1.28

Panel C(2) - Regression for post-IFRS without year and industry

	Robust					
FE	Coef.	Std. Err.	t	P>t	[95% Conf.	Interval]
AGE	-.3315684	.536601	-0.62	0.542	-1.432583	.7694458
HORIZON	.7281856	.9147724	0.80	0.433	-1.148772	2.605143
SIZE	1.29e-06	9.39e-06	0.14	0.892	-.000018	.0000205
AUDITOR	-3.901334	8.222017	-0.47	0.639	-20.77152	12.96885
LEVERAGE	-.0808019	.1152018	-0.70	0.489	-.3171765	.1555728
_cons	11.57849	12.48833	0.93	0.362	-14.04545	37.20243

R-squared = 0.0246 F-Static = 3.40