Impact of International Financial Reporting Standard adoption on the Financial Performance of Nigerian Manufacturing Firms

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Abstract

The adoption of International Financial Reporting Standards (IFRS) has been achieved based on the prior expectation that IFRS improves the quality of reporting and ensures uniformity of reporting across the globe (Ball, 2016). The purpose of the study is to examine the Impact of International Financial Reporting Standards (IFRS) on the financial performance of the manufacturing sector. This research work covers a period of 14 years Pre IFRS (2006 -2012) and post IFRS (2013-2019). The sample size for this study is ten (10) Manufacturing Companies listed on the Nigerian Stock Exchange. The study adopted Ordinary Least Squares (Gauss-Newton/Marquardt steps) Model and Wald Test Coefficient Restrictions Model as the main analytical tools to test the formulated hypotheses. The study revealed that a weak and insignificant relationship exist between the Nigerian Manufacturing Firms' Revenue, Profit, Total Assets, and Total Liabilities, and the Nigerian Manufacturing Firms' Earnings per Share, Return on Assets, and Return on Equity before the adoption of IFRS. Based on the findings, this study recommends that investors should consider the values of earnings, book values of equity, and cash flow from operations in the annual reports of firms prepared in accordance with IFRS before making any investment decision. Finally, the study recommends that management, external auditors and regulators should work together to ensure total compliance by Nigerian Manufacturing Firms in order to achieve IFRS objectives, since enforcement is a necessary tool for ensuring compliance.

Keywords: IFRS, Quality of Financial Reporting, Revenue, Profit, Total Assets, Total Liabilities

INTRODUCTION

The adoption of International Financial Reporting Standards (IFRS) has been achieved based on the prior expectation that IFRS improves the quality of reporting and ensures uniformity of reporting across the globe (Ball, 2016). On that premise, international bodies such as IMF and the World Bank have persistently recommended that developing countries adopt IFRS, yet the majority of African counties have neither followed the adoption route nor the convergence pathway. For the few that have adopted IFRS, there have been doubts about their effective implementation. IFRS is now acceptable in many countries and there is a huge increase in the number of companies across the globe moving to IFRS reporting, to make sure that their financials are comparable for investors and capital markets. IFRS has an objective to develop in the public interest, a single set of high quality, understandable, enforceable and globally accepted financial reporting standards based upon clearly articulated principles. This standards has high quality, transparent and comparable information in financial statements and other financial reporting to help investors, other participants in the world's capital markets and other users of financial information make economic decisions. In this context, 'international accounting standards' means standards (International Accounting Standards and International Financial Reporting Standards) issued by the IASB and interpretations issued by the IFRS Interpretations Committee (and its predecessor, the Standing Interpretations Committee) that have been endorsed by the EU. Different researchers have written on IFRS adoption different sector but more have written on the banking sector few on manufacturing sector at large and most of the works focuses on the earnings management, value relevance, timely loss, price earnings ratios, and dividend yield focusing on different countries like Ghana, South Africa etc. This research focuses on the impact of International Financial Reporting Standard (IFRS) adoption on the financial performance of Nigerian manufacturing firms using Revenue, Profit , Total asset and total liabilities as independent variables and dependent on Earnings per share, Return on assets and Return on equity. Given the foregoing, this study therefore seeks to examine the impact of IFRS adoption of the financial performance of Nigerian manufacturing firms and the hypothesis underlying the research are stated thus:

H_{01}: IFRS adoption has no significant effect on Earnings per share of the Nigerian manufacturing Firm.

H_{02}: IFRS adoption has no significant effect on Return on Asset of the Nigerian manufacturing Firms.

LITERATURE REVIEW

Conceptual Clarifications

International Financial Reporting Standard in Developing Countries

International Financial Reporting Standards (IFRS) set common rules so that financial statements can be consistent, transparent, and comparable around the world. IFRS are issued by the International Accounting Standards Board (IASB). They specify how companies must maintain and report their accounts, defining types of transactions, and other events with financial impact. IFRS were established to create a common accounting language so that businesses and their financial statements can be consistent and reliable from company to company and country to country. Others key takeaway of IFRS include: International Financial Reporting Standards (IFRS) were established to bring consistency to accounting standards and practices, regardless of the company or the country. Also, they are issued by the Accounting Standards Board (IASB) and address record keeping, account reporting and other aspects of financial reporting; and IFRS benefit companies and individuals alike in fostering greater corporate transparency.

Concept of Revenue

Revenue, in simple words, is the amount that a firm receives from the sale of the output. According to Prof. Dooley," The Revenue of a firm is its sales receipts or income''. Revenue refers to the amount received by a firm from the sale of a given quantity of a commodity in the market. Revenue is a very important concept in economic analysis. It is directly influenced by sales level, i.e., as sales increases, revenue also increases. In a firm, revenue is of three types: Total Revenue, Average Revenue and Marginal Revenue.

Total Revenue

This is simple. The Total Revenue of a firm is the amount received from the sale of the output. Therefore, the total revenue depends on the price per unit of output and the number of units sold.

Average Revenue

Average Revenue, as the name suggests, is the revenue that a firm earns per unit of output sold. Therefore, you can get the average revenue when you divide the total revenue with the total units sold.

Marginal Revenue

Marginal Revenue is the amount of money that a firm receives from the sale of an additional unit. In other words, it is the additional revenue that a firm receives when an additional unit is sold.

Concept of Profit

The concept of profit entails several different meanings. Profit may mean the compensation received by a firm for its managerial function. It is called normal profit which is a minimum sum essential to induce the firm to remain in business. Profit may be looked upon as a reward for true entrepreneurial function. It is the reward earned by the entrepreneur for bearing the risk. It is termed as supernormal profit analysis.

Total Assets

Total Assets, most commonly used in the context of a corporation, is defined as the assets owned by the entity that has an economic value whose benefits can be derived in the future. Assets are recorded in the balance sheet of the firm.
Assets are further classified into liquid assets and illiquid assets, depending on their liquidity. A liquid asset is that asset that can be easily converted into cash or readily sold for cash; otherwise, it is called an illiquid asset.

Total Liabilities

Total liabilities are the combined debts and obligations that an individual or company owes to outside parties. All assets of a company are either owned by the entity and classified as equity or are subject to future obligations and recorded as a liability. A company's total liabilities are generally split up into three categories: short-term, long-term, and other liabilities. Total liabilities are calculated by summing all short-term and long-term liabilities, along with any off-balance sheet liabilities that corporations may incur.

Short-term liabilities

Short-term, or current liabilities, are liabilities that are due within one year or less. They can include payroll expenses, rent, and accounts payable (AP), money owed by a company to its customers.
Because payment is due within a year, investors and analysts are keen to ascertain that a company has enough cash on its books to cover its short-term liabilities.

Long-term liabilities

Long-term liabilities, or noncurrent liabilities, are debts and other non-debt financial obligations with a maturity beyond one year. They can include debentures, loans, deferred tax liabilities, and pension obligations. Less liquidity is required to pay for long-term liabilities as these obligations are due over a longer timeframe. Investors and analysts generally expect them to be settled with assets derived from future earnings or financing transactions. One year is generally enough time to turn inventory into cash. When something in financial statements is referred to as “other” it typically means that it is unusual, does not fit into major categories and is considered to be relatively minor. In the case of liabilities, the “other” tag can refer to things like intercompany borrowings and sales taxes.
Investors can discover what a company’s other liabilities are by checking out the footnotes in its financial statements.

Empirical Review

Odoemelam, Okafor and Ofoegbu (2019) examine the effect of IFRS adoption on the earnings value relevance of quoted Nigerian firms. Using a sample of 101 firms (1212 firms’ year observation) that are quoted on or before 2006, and have adopted IFRS from 2006 to 2017, we can investigate earnings value relevance. As the principal objective of the inquiry, we introduce a cross-product term, equal to the product of earnings per share (EPS) and IFRS dummy variable, into the basic Ohlson model. The paper uses the Fixed Effect Model as the appropriate estimator for analysis of the data. The estimated coefficient on the cross-product term is statistically significant and positive. The results suggest that the adoption of IFRS in Nigeria leads to higher earnings value relevance. IFRS, as a principle-based, allows managers to use their discretion in the specific treatment of financial items. In doing so, they may bias earnings. Elosiuba and Okoye (2018) examined the effect of the IFRS adoption on the reported performance of Nigerian banks listed on the Nigerian Stock Exchange. Eight (8) out of the fourteen (14) quoted banks were selected for the study. The four indices of performance employed in the study are profitability using the return on equity, liquidity using total deposit to total loan, loan grants and then market value measured by price earnings ratio for the period (2011 and 2012). 2011 represented GAAP era while 2012 stands for IFRS adoption. A comparability index for the banks was computed using the Excel Spreadsheet for each of the banks on each variable. Then the One Sample Test was employed for the analyses. The mean was used to answer the research question while the t-statistics tested the hypotheses. The results showed that mean values for profitability, liquidity and market value are greater in the GAAP era (2011) than in the IFRS period (2012), while loan grant was higher for the IFRS period (2012). The t-tested indicated the fact that none of the variables had significant effect. Thus, the study concluded that IFRS adopted does not have significant effect on bank performance reported in 2011 and 2012.

Okafor, Ogbuehi and Anene (2017) examined the impact of IFRS Adoption and the Value Relevance of Accounting Information in Nigeria: An Empirical Study The objective of this article is to determine the effect of International Financial Reporting Standards (IFRS) adoption on value relevance of accounting information in Nigeria. The study therefore empirically analyzed the effect of IFRS adoption on value relevance of book value, earnings per share, and cash flow from operations in Nigerian firms - evidence from consumer firm’ssector. The ex-post facto research design was used. The population is made up of 25 consumer firms listed in Nigerian Stock Exchange. A sample size of 12 firms selected on the basis of availability of data among other considerations was used. The study covers a period of eight years (2008-2015). Secondary data collected from annual reports of firms and database of Capital Assets (http://www.capitalassets.com.ng/) were used. Multiple regression analysis was used in analyzing the data with the aid of Statistical Package for Social Sciences (SPSS) Version 22. The findings revealed that IFRS adoption has an incremental effect on the value relevance of book value, earnings per share, and cash flow from operations, with earnings per share showing the highest increment. Based on the findings, the researchers recommended that investors should consider the values of earnings, book values of equity, and cash flow from operations in the annual reports of firms prepared in accordance with IFRS before making any investment decision. However, more emphasis should be laid on earnings. Agir (2017) investigates the effect of IFRS adoption on value relevance of accounting information of listed Deposit Money Banks in Nigeria. The study adopts the ex-post facto research design. Data used for the study was sourced from the annual published accounts of selected Deposit Money Banks under investigation from 2008– 2015. Descriptive statistics and regression analysis were used in analyzing the data. Findings from the analysis revealed that there is no significant impact of post IFRS earnings per share and book value per share on the share price of deposit money banks in Nigeria while post IFRS volume of shares issued significantly affect the share price of Deposit Money Banks in Nigeria. It was also found that value relevance of financial information of Pre and post IFRS adoption in Nigerian DMBs differs significantly. The study recommended that management, external auditors and regulators should work together to ensure total compliance by Nigerian DMBs in order to achieve IFRS objectives, since enforcement is a necessary tool for ensuring compliance.

Adewale and Ibukun (2017), examined the impact of IFRSs on the quality of financial statements of banks in Nigeria with emphasis on the comparability, relevancy and clarity of objectives of Nigerian banks. A case study approach was used to arrive at conclusion drawn from the study. This involves a survey of both internal and external stakeholders using a questionnaire. Data obtained were analysed using the Chi- Square technique. Results show that there is a significant relationship between IFRS adoption and the comparability objectives of Nigerian banks as X2 -calculated of 14.96 is greater than the X2 -critical/ table value of 5.99 at 0.05 LOS. It was further discovered that IFRS adoption has a substantial influenced on the relevancy quality as X2-calculated of 14.0 is greater than the X2-critical/ table value of 5.99 at 0.05 LOS. It was also found that IFRS adoption has significantly influence the clarity objectives of Nigerian banks as X2-calculated of 25.4 is greater than the X2-critical/ table value of 5.99 at 0.05 LOS. It was concluded that IFRS adoption has significant impact on quality of financial statements of banks in Nigeria. It is recommended that the adoption of IFRS in preparation and disclosure of financial statement should be enforced. Auditors should declare if the accounts comply with the requirements of the standards. Shehu (2015) researched on adoption of international financial reporting standards and earnings quality in listed deposit money banks in Nigeria. He investigates firm’s attributes from the perspective of structure, monitoring, performance elements and the quality of earnings of listed deposit money banks in Nigeria. The study adopted correlational research design with balanced panel data of 14 banks as sample of the study, using multiple regression as a tool of analysis. The result reveals that firm’s attributes (leverage, profitability, liquidity,bank size and bank growth)have a significant influence on earnings quality of listed deposit money banks in Nigeria after the adoption of IFRS, while the pre-period shows that the selected firm’s attributes have no significant impact on earnings quality. It is therefore concluded that the adoption of IFRS is right and timely. The study therefore recommended that regulatory body should embarked upon enlightenment campaigns on the potential impacts of adopting IFRS in Nigeria. It also point out that government should support the Nigeria’s adoption of IFRS especially in the area of enforcement to compliance as a matter of urgency to enable full attainment of the country’s economic potential.

Matthew (2015) examined the impact of International Financial Reporting Standards (IFRS) adoption on financial reporting practice in the Nigerian banking sector.At the centre of the plethora of corporate scandals that have plagued corporate entities are fraudulent financial reporting practices. Against this backdrop, proponents of the International Financial Reporting Standards (IFRS) have more strongly argued for the internationalization of the adoption of the standards, as a panacea for curbing or mitigating these financial reporting infractions. Ranging from increased comparability to better decision making, the importance of IFRS cannot be over emphasised. It is to this end that this study evaluates the impact of IFRS on Financial Reporting Practices with focus on the Nigerian Banking Sector. The specific objective of this paper is to determine whether the quantitative differences in the financial reports prepared by Nigerian listed banks under NGAAP and IAS/IFRS are statistically significant or not. Secondary data were employed in this study. These data were gleaned from the annual reports of fourteen Nigerian listed banks. One hypothesis was developed and tested at five (5) per cent level of significance. Findings revealed that the quantitative differences in the financial reports prepared under NGAAP and IAS/IFRS are statistically significant. The study therefore concludes that IFRS have impacted on financial reporting in the Nigerian Banking sector. The study recommended that the Financial Reporting Council in conjunction with various professional bodies should place more premium on continuing professional education and training. As much as possible, the professional accountancy bodies should align their continuing professional education requirements with IFAC guidelines.

Theoretical Framework

Agency Theory

This view is based on the idea that in a modern corporation, there is separation of ownership (principal) and management (agent), and this leads to costs associated with resolving conflict between the owners and the agents (Berle & Means, 1932; Jensen & Meckling, 1976; Eisenhardt, 1989). The fundamental premise of agency theory is that the managers act out of self-interest and are self-centered, thereby giving less attention to shareholder interests. For example, the managers may be more interested in consuming perquisites like luxurious offices, company cars and other benefits, since the cost is borne by the owners. The Agency theory is the theory underpinning this research work as it explains how to best organize relationship in which one party determines the work while another party does the work. In this relationship, the principal hires an agent to do the work or to perform a task the principal is unable to do.

Social Responsibility Theory

Social responsibility theory implies that decision makers recognize some obligation to protect and improve welfare of society as a whole along with their own interest. The effect is to enhance quality of life in the broadest possible way, however such quality should be defined by society. Taking cognizance of social responsibility theory it is not disputable that governance is business, moreover now that democracy is globally accepted as the best system of governance. It is seen as the government of the people by the people and for the people run by elected representatives. Anywhere democracy is in practices there is always a quest for development of the congregating communities and those in charge of governance must ensure transparency and accountability in the discharge of the duties, by presenting financial reports that comply with international best practice.

Stakeholder Theory

Stakeholder theory is an extension of the agency view, which expects board of directors to take care of the interests of shareholders. However, this narrow focus on shareholders has undergone a change and boards are now expected to take into account the interests of many different stakeholder groups, including interest groups linked to social, environmental and ethical considerations (Freeman, 1984; Donaldson & Preston, 1995; Freeman, Wicks & Parmar 2004). This shift in the role of the boards has led to the development of stakeholder theory.

METHODOLOGY

The study adopted a time series expo facto research design. Time series expo factor research design is a method of research that can truly test hypotheses concerning cause-and-effect relationships, as well as combines the theoretical consideration with empirical observation. Consequently, this is "an after-the event" research. It involves carrying out research on something that has occurred. It is a systematic empirical study in which the researcher does not have direct control over independent variable because they have already occurred or they cannot be manipulated. Besides, multiple-method strategy was adopted for this study so as to reduce the possibility of personal bias by not depending on only one method or response from only one firm or sector. Adopting this approach enhances the authenticity of the study. The study is designed to cover only secondary information from annual financial reports of some manufacturing firms listed on the Nigerian Stock Exchange. This research work studied the Financial Performance of Nigerian Manufacturing Firms before and after the adoption of International Financial Reporting Standard Adoption in 2013. That is, attention was focused on seven years pre- IFRS adoption and seven years post- IFRS adoption. The population of this study consists of all manufacturing companies listed in the Nigeria stock from 2006 to 2019. The study population is 134 Manufacturing Companies listed on the Nigerian Stock Exchange. These periods are considered long enough for the variables to form a pattern in combination with economic activities of the industries. The periods of the study also envelops economic activities before, during, and after the Nigerian economic recession.

The Convenience Sampling Technique was utilized in this study to determine the sample size. The sample size for this study is ten (10) Manufacturing Companies listed on the Nigerian Stock Exchange. The companies are selected based on the following reasons; i. The companies are among the twenty top manufacturing firms in Nigeria; ii. The availability of the firms' financial reports iii. and because of the firms' full compliance of IFRS. They include; Nigerian Breweries Plc, Nestle Nigeria Plc, Dangote Group Plc, PZ Cussons Nigeria Plc, UAC Nigeria Plc, Unilever Nigeria Plc, DUFIL Prima Plc, Guinness Nigeria Plc, Flourmills Nigeria Plc; and Lafarge Cement Ltd. This study employed secondary source of data collection. This research study adopted a quarterly data from 2006 to 2019, and data were obtained from the annual reports and accounts of the sample companies and Nigerian Stock Exchange Fact Book in order to achieve the objectives of the study. This is due to the fact that corporate annual reports of listed companies were available and easy to access. Data collection involves gathering of relevant and important data used for conducting a particular research work. It is the basis for acquiring data.The data collected were gathered, sorted, and analyzed with the use of Eviews, version 10.

Procedure for Data Analysis and Model Specification

In order to investigate the relationship that exists between the target variable and explanatory variables; this study adopted the following procedures.
Before conducting the co-integration test, variables must be found stationary individually or if both variables are non-stationary, they must be co-integrated. Therefore, individual variables both dependents and independents variables must be subjected to the unit root test. The Augmented Dickey-Fuller (ADF) test was used to identify the presence or otherwise of a unit root in the series. A mathematical model was developed based on the proxies specified for the dependent variable and independent variables. Dependent variable (Financial Performance) was proxied by Earnings per Share (EPS), Return on Assets (ROA)and the independent variable (IFRS Adoption) was proxied by Revenue, Profit, Total Assets, and Total Liabilities. Besides, the study adopted Uwalomwa and Olamide model that used in their study in 2017. However, the models for this study are stated below;

Model 1: IFRS Adoption (Revenue, Profit, Total Assets, and Total Liabilities) and Earnings per Share (EPS)

EPS = $\beta_{01} + \beta_2\text{Rev} + \beta_3\text{Prof} + \beta_4\text{TA} + \beta_5\text{TL} + \varepsilon_1$ ---------------------(1)
Where:
Eps = Earnings per Share
Rev = is the Revenue Generated by the Manufacturing Firms
Pro = is the Profit declared by the Manufacturing Firms
TA = is the Total Assets of the Manufacturing Firms
TL = is the Total Liabilities of the Manufacturing Firms

β_{01} is the intercept of the regression model of Earnings per Share and IFRS Adoption variables.

β_1, β_2, $\beta_{3,}$ β_4, $\square_{54}$are rates of change of the IFRS Adoption variables with respect to EPS

$\square_1$ =is the error term associated with the model of the IFRS Adoption variables with respect to EPS

Model 2: IFRS Adoption (Revenue, Profit, Total Assets, and Total Liabilities) and Return on Asset (ROA)

ROA = $\square_{02} + {}_1\text{Rev} + {}_2\text{Prof} + {}_3\text{TA} + {}_4\text{TL} + {}_2$ ---------------------(2)
Where:
ROA = Return on asset
Rev = is the Revenue Generated by the Manufacturing Firms
Pro = is the Profit declared by the Manufacturing Firms
TA = is the Total Assets of the Manufacturing Firms
TL = is the Total Liabilities of the Manufacturing Firms

$\square_{02}$ is the intercept of the regression model of Return on Asset and IFRS Adoption variables.

$\square_1$, $\square_2$, ${}_{3,}$ *and* $\square_{44}$are rates of change of the IFRS Adoption variables with respect to ROA

□₂ =is the error term associated with the model of the IFRS Adoption variables with respect to ROA

RESULT AND DISCUSSION

Table 3: Descriptive Statistics

	EPS	ROA	REVENUE	PROFIT	TA	TL
Mean	5.245545	43.74367	284.7148	25.80993	323.9312	196.5463
Median	5.724805	43.17525	248.1016	24.15835	287.7730	171.3532
Maximum	7.554240	56.37675	558.7179	42.53378	650.3554	354.7344
Minimum	2.497750	25.45776	124.3582	11.37118	141.7311	99.43252
Std. Dev.	1.154991	7.918636	149.9709	9.405326	161.9341	86.46639
Skewness	-0.745861	-0.619939	0.610016	0.464832	0.605089	0.604309
Kurtosis	2.717029	2.905884	1.918238	1.887392	2.026312	1.942084
Jarque-Bera	5.379054	3.607700	6.203604	4.905070	5.629397	6.019871
Probability	0.067913	0.164664	0.044968	0.086075	0.059923	0.049295
Sum	293.7505	2449.645	15944.03	1445.356	18140.15	11006.59
Sum Sq. Dev.	73.37024	3448.764	1237020.	4865.308	1442247.	411204.0
Observations	56	56	56	56	56	56

Source: Author's compilation using E-views 10

Table 3 above shows the descriptive statistics of the data collected for the study. The descriptive statistics show the trend and comprehensive evidence about the variables. The Mean tells us about the average values of the set of variables. The Nigerian Manufacturing Firms' Total Assets (TA) has the highest average value of ₦323.93 billion, while the Nigerian Manufacturing Firms' Earnings per share (EPS) has the lowest value of ₦5.25 billion. The Median tells us about the middle values for each of the variables. The Nigerian Manufacturing Firms' Total Asset (TA) also has the highest Median value of ₦287.77 billion, while the Nigerian Manufacturing Firms' Earnings per share (EPS) also has the lowest Median value of ₦5.72 billion. The Maximum and the Minimum tell us about the highest and the lowest figures for each of the variables. Nigerian Manufacturing Firms' EPS has the values ranges from 2.50 to 7.55; Nigerian Manufacturing Firms' ROA has the values ranges from 25.46 to 56.38; Nigerian Manufacturing Firms' Revenue has the values ranges from 124.36 to 558.72; Nigerian Manufacturing Firms' Profit has the values ranges from 11.37 to 42.53; Nigerian Manufacturing Firms' Total Assets (TA) has the values ranges from 141.73 to 650.36, and Nigerian Manufacturing Firms' Total Liabilities (TL) has the values ranges from 99.43 to 354.73.5

5. SUMMARY, CONCLUSION AND RECOMMENDATIONS

The aim of this research was to examine the impact of IFRS Adoption on the financial performance of manufacturing firms in Nigeria. There has been a considerable debate as to whether IFRS is better than NGAAP. Better understanding of IFRS is essential to resolving the debate. Public discussion and academic research have not settled the matter. As a result, this study was initiated to further a better understanding of IFRS and its impact on corporate financial reporting components in relation to Nigeria's generally accepted accounting principles (NGAAP). Findings of this study support the view that differences between IFRS and NGAAP are not significant, thus, supporting proponents of adoption of IFRS in Nigeria. The research examined whether key indicators of financial performance post-IFRS are significantly different from pre-IFRS period. The first factor examined was earnings per share followed by return on asset, and finally return on equity.Based on the above, the following recommendations were proffered:

i. Based on the findings, this study recommends that investors should consider the values of earnings, book values of equity, and cash flow from operations in the annual reports of firms prepared in accordance with IFRS before making any investment decision.

ii. Finally, the study recommends that management, external auditors and regulators should work together to ensure total compliance by Nigerian Manufacturing Firms in order to achieve IFRS objectives, since enforcement is a necessary tool for ensuring compliance.

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