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Fair value accounting and market reaction: evidence from Romanian listed companies

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Abstract

The quality of the accounting information is determined by its capacity to capture the reality regarding the financial position and performance of the company by confronting the interested parts. On the stock exchange, the quality of the accounting information seen from the credibility point of view can be evaluated through the influence of the results in the financial statements on the market value of the company. The objective of this study is to estimate and test the existence of an influence of the accounting information on the market value, based on the multiple linear regressions. The analyzed sample contains 64 BSE listed companies, between 2010 and 2011, for which data has been collected from the annual and interim financial statements. The results of the study show that the accounting information in the interim financial statements have a greater influence on the *market value* compared to the information in the annual financial statements.

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1. Introduction

According to the *agency theory*, the company is regarded to as a sum of contracts agreed by *agents* (managers) and *principals* (shareholders). Principals to represent their interests and to obtain future economic benefits mandate agents. These benefits are determined by the financial position and performance of the company, reflected by the information provided by the financial statements. Accounting information is useful to all stakeholders for them to make decisions. Elaborating and providing accounting information is meant to regulate the power relation between the two parts, the agents and the principals. On a stock exchange, investors (as principals) are interested in the

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financial position and performance of the company, reflected by the information in the annual statements. Investors need such information in order to make strategic decisions regarding the share acquisition or sale, with direct impact on the stock exchange price or capitalization.

The article aims at analyzing and estimating the influence of the accounting information represented by a series of financial indicators from the statements on the decisions of investors on a stock exchange, with direct impact on the share price. The study has been carried out on a sample of 64 Bucharest Stock Exchange (BSE) listed companies, between 2010 and 2011. The results of the research have emphasized the existence of a significant influence of the indicators regarding the financial position and performance of the company on the company market value, estimated upon the share prices.

2. Literature review and hypothesis development

The usefulness of the accounting information and its influence on the users' decisions result from its qualitative characteristics. According to the *Conceptual Framework* of the International Accounting Standards Board (IASB), the main qualitative characteristics of the accounting information aim to have *relevance* for its main users, and also to express the *faithful representation*, obtained from the correct use of the *fair value accounting* principles. The fulfillment of the requirements from the International Financial Reporting Standard (IFRS) accounting referential proposed by the IASB leads to the improvement of the accounting information quality due to a better display of the financial position and performance.

2.1. Qualitative characteristics of accounting information

In the accounting doctrine, criteria that allow to define the concept of accounting information quality are not identical, their selection and hierarchy being different (Minu, 2002; Domnişoru *et al.*, 2006). The Anglo-Saxon conceptual frameworks (USA, IASB, The United Kingdom) see the quality of the accounting information as a basic element. To this respect, the set objective of the accounting information is represented by the support of users' economic decision making. As for users, some conceptual frameworks favor the shareholders, considering them to be the main accounting information users, while the set objective of other conceptual frameworks (like the one of IASB) is to provide information to a wide range of users (shareholders, creditors, employees, banks, the state, the public etc.). The usefulness of the accounting information is determined by the fulfillment of all qualitative characteristics, according to the proportions in a certain situation. As some characteristics might be complementary, independent or even divergent, practical situations might emphasize a characteristic to the prejudice of other (Minu, 2002; Domnişoru *et al.*, 2006).

Starting from the *Conceptual Framework* proposed by the IASB, van Beest and Braam (2006) establish a qualitative characteristics hierarchy: relevance, reliability/ faithful representation and understandability are considered main characteristics, and the comparability is put in the background. The qualitative characteristics of the accounting information are accompanied by a series of limits. These limits are to provide an appropriate display, which will not lead to the loss of information relevance due to the delay in their display, and also to a loss of their credibility due to a faster delay. Therewith, finding a balance between the qualitative characteristics of the accounting information must also take into consideration the cost-benefit ratio.

In the Romanian accounting framework, the issue of defining the accounting information quality is based on the texts that had been issued by legislators between 1990 and 2012. During the first stage, a reform was made which aimed at creating the Romanian accounting law, followed by the stage of harmonization with the European Directives and the IAS/IFRS, and nowadays the standards applied both to small and BSE listed companies take the qualitative features in the *General Framework* of IASB.

2.2. Faithful image and its relevance on the stock exchange

The *true and fair view* concept is assigned to the Anglo-Saxon accounting practice and culture. Lee (1981) assumes that the application of *true and fair view* leads to the report of the financial statements prepared according to the generally accepted accounting principles. To this regard, one must use as much as possible accurate information and make as much as possible reasonable estimations, which can lead to an objective display regarding the financial position and performance, with no significant errors, distortions, manipulations or omissions (Lee,

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