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Impact of the Application of International Accounting Standards to Attract Foreing Investment in Developing Countries

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ABSTRACT:

International accounting Standards (IAS) has been accepted in countries mainly because it is widely believed that those standards enhance transparency in the preparation of financial statements. Consequently, increased transparency should lead to enhanced Foreign Direct Investments (FDI). The purpose of this paper was to ascertain the impact of IAS on FDI as it affects the Developing countries economy. Using data from secondary and primary sources, the results from the regression analysis showed that there is a positive but not significant relationship between FDI inflow and IAS adoption. It was found that the longer a country uses IAS, the higher the FDI. Furthermore, the perception of the business managers and preparers of financial statements towards FDI could signal their willingness to adopt IAS. The study recommends that the accounting council of Developing countries (FRCN) should monitor compliance with the requirements of the accounting standards as this might help organizations in the long run to secure FDIs.

INTRODUCTION:

Adopted International Accounting Standards (IAS) in September, 2015 but the implementation started with Public Limited Liability Companies in 2015. The IASs are standards set by the International Accounting Standards Board (IASB) which is the international body responsible for monitoring the preparation of financial statements worldwide. Before the advent of IAS, most countries had their own national accounting standards which were issued by national accounting bodies [1].

For instance, the Developing countries Accounting Standards Board (NASB) was responsible for developing and issuing standards known as Statements of Accounting Standards (SAS) up to 2012 in Developing countries. This adoption is expected to improve corporate transparency especially in financial terms which in turn should lead to increase in Foreign Direct Investment (FDI). That the preparation of financial statements in accordance with IAS increased transparency in the statements thus, boosting the investment potential of the country. This means that adopting IAS will give investors more confidence in the financial statements since they have been prepared according to international standards. The term foreign direct investment arises as a result of removed hindrances across country borders and enhanced trade between countries. Reference propounded that FDI arises as a result of OLI, an acronym that stands for Ownership, Location and Internalization. The motives underlying FDI include: market, resource, efficiency, and strategic asset seeking. This research seeks to test whether the adoption of IAS has increased foreigner's interest in investing into the companies in Developing countries. Specifically, this study ascertained whether the number of foreign investors has increased since IAS adoption. This is important because one of the purposes of adopting IAS among others is to increase the level of economic activity between and among countries. This study ascertained whether and to what extent IAS adoption affects the rate of FDI. Also, this study examined whether there is a change in the level of acceptability of FDI between companies that have adopted IAS and those that have not [2].

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LITERATURE REVIEW:

According to DeFond, M., Hu, X., Hung, M., & Li, S. (2011), Proponents of IAS argue that mandating a uniform set of accounting standards improves financial statement comparability that in turn attracts greater cross-border investment. We test this assertion by examining changes in foreign mutual fund investment in firms following mandatory IAS adoption in the European Union in 2005. We measure improved comparability as a credible increase in uniformity, defined as a large increase in the number of industry peers using the same accounting standards in countries with credible implementation. Consistent with this assertion, we find that foreign mutual fund ownership increases when mandatory IAS adoption leads to improved comparability.

According to Zeghal, D., & Mhedhbi, K. (2006), purpose of this study is to identify the factors that could explain the adoption of international accounting standards by developing countries. The following factors have been selected: economic growth, education level, the degree of external economic openness, cultural membership in a group of countries, and the existence of a capital market. Our results indicate that developing countries with the highest literacy rates, that have capital markets, and that have an Anglo-American culture are the most likely to adopt international accounting standards.

According to Al-Shammari, B., Brown, P., & Tarca, A. (2008), This study investigates the extent of compliance with international accounting standards (IASs) by companies in the Gulf Co-Operation Council (GCC) member states (Bahrain, Oman, Kuwait, Qatar, Saudi Arabia, and the United Arab Emirates). Based on a sample of 137 companies (436 company-years) we find that compliance increased over time, from 68% in 1996 to 82% in 2002. Despite strong economic and cultural ties between the GCC states, there was significant between-country variation in compliance and among companies based on size, leverage, internationality, and industry.

The study provides evidence of de jure but not de facto harmonization in the region. Noncompliance reflected some ineffectiveness in the functions of external auditors and enforcement bodies, which may be of interest to countries that have adopted IASs recently. According to Covrig, V. M., Defond, M. L., & Hung, M. (2007), test the assertion that a consequence of voluntarily adopting International Accounting Standards (IAS) is the enhanced ability to attract foreign capital. Using a unique database that reports firm-level holdings of over 25,000 mutual funds from around the world, our multivariate tests find that average foreign mutual fund ownership is significantly higher among IAS adopters.

We also find that IAS adopters in poorer information environments and with lower visibility have higher levels of foreign investment, consistent with firms using IAS adoption to provide more information and/or information in a more familiar form to foreign investors. Taken together, our findings are consistent with voluntary IAS adoption reducing home bias among foreign investors and thereby improving capital allocation efficiency.

METHODOLOGY

This study used both secondary and primary data. Primary data was collected from managers and preparers of financial statements in companies that have adopted IAS and the secondary data was obtained from the World Development Indicators. One sample t-test was used to test the primary data and was analyzed using descriptive analysis whereas secondary data was analyzed using correlation and regression [4].

The population for the survey includes companies that have adopted IAS in the preparation of financial statements. The sample size of this study includes twenty companies in Developing countries that have adopted IAS. Fifty (50) copies of questionnaire were administered to managers and preparers of financial statements in the selected companies. The study was conducted Lagos and Ogun States.

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DATA PRESENTATION AND ANALYSIS

There were forty-six (46) responses and the responses were graded using the Five Likert Scale. The response to the first question has a mean of 2.87 and a standard deviation of 1.392. This shows that the average respondent agreed that there were Foreign Direct Investors in their organizations before IAS adoption in Developing countries. The response to the second question has a mean of 1.93 and a standard deviation of 1.063. The mean shows that the average respondents did not necessarily agree that since Developing countries adopted IAS, there has been an increase in foreign interest. The response to the third question has a mean of 2.61 and a standard deviation of 1.437 and this shows that the average respondents agreed that new interest by foreigners will be embraced [5]. The responses to the fourth question had a mean of 2.63 and a standard deviation of 1.511. which shows that the average respondents agreed that more foreigners should invest directly in Developing countries. The responses to the fifth question had a mean of 2.63 and a standard deviation of 1.511. This shows that the average respondents agreed that there should be government incentives towards increased FDI in Developing countries companies.

The responses to the sixth question had a mean of 2.70 and a standard deviation of 1.504 which shows that the average respondents agreed that FDI will bring about economic development in Developing countries [6]. The responses to the seventh question had a mean of 2.57 and a standard deviation of 1.559. This shows that the average respondents agreed that there should be more FDI than portfolio investment. It was also discovered that the longer a country uses IAS, the higher the FDI because 0.0416 shows a positive relationship although weak. Also, as natural resources increase, FDI inflow increases, this is because there is a positive relationship between natural resources and FDI inflow (0.9217). There is a strong relationship between natural resources and FDI inflow. The higher the GDP of a country, the higher the FDI inflow in that country, there is a positive relationship between the GDP and IAS inflow (0.6888).

The relationship between them is strong. The relationship between institutions and FDI inflow is a positive one. This means that the higher the institutions, the higher the FDI inflow into a country. These institutions have a strong relationship with FDI inflow [7]. The results from the regression analysis show that FDI inflow and IAS adoption have a non significant relationship because the regression between them gives a value above 0.5 (ie>0.5). This means that IAS adoption has an impact on FDI inflow but the impact is not significant. The results of One-Sample Test have a calculated T value of 11.808, with a degree of freedom of 45 and 0.05 significance level because of its 2-tailed nature. The test has a p-value of .000 which is less than the significance level of 0.05. Alternatively, we got a tabulated value of 1.684 which is less than the calculated value at 0.05 level of significance. Hence, companies in Developing countries are willing to accept FDI [8].

CONCLUSION

This research was carried out with the main purpose of finding out the impact of International Accounting Standards (IAS) adoption on Foreign Direct Investment (FDI). The finding from the field survey shows that the companies that have very good reputation globally have had a good level of FDI inflow before IAS adoption. In some other companies however, the adoption of IAS was the beginning of FDI inflow in the company. Based on the study, the managers and the preparers of financial statements used for this study would welcome FDIs if such opportunity opens up and the government is expected to provide incentives towards improvement of FDI inflow. The company's managers believe that FDI inflow would bring about economic development in Developing countries. From the primary data, it was observed that companies want more of FDI than portfolio investment in their companies. In West Africa, Developing countries has the highest rate of FDI along with Ghana. Countries such as Sierra Leone have very low inflow of FDI. Only nine, out of the sixteen West African countries have adopted IAS. From the above analysis and presentation, several conclusions were drawn. The researchers found that IAS adoption does not impact FDI inflow into a country. However, other factors such as institutions, natural resources and Gross Domestic Product (GDP) among others impact the inflow of FDI significantly. Also, it was found that companies in Developing countries are open to the idea of FDI inflow. Finally, the fact that IAS adoption does not impact FDI does not mean that the adoption of IAS is not important in any Nation; IAS adoption affects several variables that were not the topic for this research.

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