IFRS Adoption and Liquidity Ratios ofthe Conglomerate Sector of Nigeria

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Abstract

This study provides an empirical analysis of the effects of IFRS adoption on the liquidity ratios of the companies listed in the conglomerate sector of the Nigerian Stock Exchange. The study compared the key liquidity ratios computed under the Pre-IFRS (2008-2011) and the Post-IFRS (2013-2016) period of eight (8) years. The means of secondary data extracted from the financial statements of the companies as contained in the FACT book of Nigerian Stock Exchange were compared and ANOVA table was used to test the level of significance. Findings from the study revealed that though the liquidity ratios of the conglomerate sector has changed over the years, the changes do not seem to come to be as a result of the adoption of IFRS. This implies that the adoption of IFRS does not have significant effects on the liquidity ratios of the conglomerate sector of Nigeria. The study however, recommends that investors need to pay close attention to the liquidity position/status of firms but caution should be taken as the liquidity shouldn't be too high since a company with too much cash and heavily-weighted in short term securities is unlikely to be highly profitable.

Keywords: IFRS, Liquidity, Conglomerate Sector, Pre-IFRS, Post-IFRS

Introduction

The requisite and viability for an even global financial reporting structure has for numerous years been a concern. Some elements supporting the adoption of IFRS includes: Incessant integration of world economy; Improved interdependence of the international financial markets; Nonappearance of barriers of capital movements across national borders; Increased kinesis of capital across national boundaries; Multiple listing by companies in capital markets within and outside the home jurisdiction; and constant demand by stakeholders for excellence information and better disclosures (Izedonmi, 2011).

Like other parts of the world, the fast growth of Nigeria in the global business gave rise to the need to adopt a universally accepted accounting standard thereby necessitating the regulators and operators of Nigeria's financial system to take steps in ensuring migration to the IFRS reporting framework. As a result of this, 1st

January, 2012 was approved by the Nigerian Federal Executive Council as the effective date for convergence of accounting standards in Nigeria with International Financial Reporting Standards.

Studies carried out on the effects of IFRS adoption has focused on several variables. (Abdul-Baki, Uthman&Sanni 2014, Yahaya, Yusuf & Dania, 2015, Okpala 2012, Umoren&Enang2015, Ibiamke and Ateboh-Briggs 2014, Nengzih2015, Erin, Oduwole, Olojede&Arumona 2018). Although, there had been a number of studies on financial ratios, very few have specifically focused on liquidity ratios thereby creating a gap that this work intends to fill. Also, several studies have focused on different sectors listed on the Nigerian stock Exchange, in fact, there had been numerous studies on the financial sector but very little have been done concerning the conglomerate sector of Nigeria, hence the motivation of the study to analyze the effect of IFRS adoption on liquidity of the conglomerate sector of Nigeria using liquidity ratios, to find out if there is a significant difference between liquidity ratios computed under Pre-IFRS as against those computed under IFRS and to identify in particular if the adoption has brought about an increase or a decrease in the liquidity position of the selected companies.

Hypotheses Formulation

The purpose of this study is to investigate the impacts of the adoption of IFRS on liquidity ratios, more specifically to test whether the adoption has brought about an increase/decrease in the liquidity of firms in Nigeria and also to test the level of significance of the change. The study thus hypothesized that:

H1: There is significant difference between Current Ratios before and after the adoption of IFRS

H2: IFRS adoption significantly affects the Quick Ratios of firms in Nigeria

H3: The adoption of IFRS has yielded a significant effect on Cash Ratios of firms in Nigeria

Liquidity and Liquidity Ratios

Liquidity is a measure of degree to which a person or organization has cash to meet its maturing financial commitments/obligations. It can also mean the ability of current assets to meet current liabilities in a timely and cost effective manner/way. An organisation is said to be liquid if it can quickly convert its investment portfolio to cash with minimal or no loss in value.

Liquidity Ratios are a set of financial ratios used in measuring the viability of an organisation in paying off its current debts. That is, liquidity ratios are financial metrics employed to determine an organisation/a debtor's ability to meet its immediate (current) liabilities as they fall due.

Liquidity ratios measure a firm's ability to pay operating expenses and other short-term or current liabilities. Because current liabilities, which are debts that must be paid or obligations that must be fulfilled, within 1 year, are paid out of current assets, which are received as cash and cash equivalents. Liquidity ratios are calculated majorly based on current assets and current liabilities.

The Conglomerate Sector

A conglomerate is so named because it combines several unrelated enterprises/corporations under a single corporate structure/business name. Conglomerates are multinational companies that combine different lines of businesses which could range from manufacturing to agriculture, from consumer goods to hotel or even from real estate to automobile. Conglomerates have the ability to increase their stock value as it permits them to raise more money and take out loan to buy more companies. People in turn find it secure to invest in conglomerates as they can easily diversify which can help reduce their investment risks.

Empirical Findings

Akinleye (2016) investigated the relationship between IFRS adoption and performance of 10 randomly selected money deposit banks in Nigeria and the result revealed IFRS adoption has a statistically significant impact on liquidity ratio, current ratio and investment ratio.

Terzi, Oktem&Sen (2013) in a study carried out on Turkey's listed manufacturing companies, found out that financial statements prepared under local GAAP and IFRS showed a level of significant difference as current ratios, liquidity ratios and profitability ratios increased in value as a result of the transition. Callao, Jarne, &Lainez (2007) related financial ratios with accounting figures for IBEX-35 companies in Spain and found out that, total liabilities, long-term liabilities, cash equivalents and shareholders' equity showed that there is statistically significant difference between financial statements prepared under local GAAP and those prepared under IFRS.

With a sample of 60 companies, Ibiamke and Ateboh-Briggs (2014) examined the impact of IFRS adoption of key financial ratios and found a negative statistically insignificant relationship

Though a mixed result was gotten for the cost of capital, Daske, Hail, Leuz and Verdi (2008) posits that firms which adopt IFRS in the year it became mandatory experience large increases in market liquidity.

Punda (2011) examined IFRS effects on key financial ratios of UK listed companies and found out a substantial change in the KPIS of the companies post IFRS adoption as operating profit margin increased by 10.8%, return on investment by 11.4% and return on equity by 27%. However, current ratio and price to earnings ratios showed not much significant change.

Tanko (2012) tested the impact of IFRS adoption on profitability, growth, leverage and liquidity performance applying multiple logit regression and t-test analysis, he found that variability of earnings decreased, this suggested that there exists low erraticism in earnings in the IFRS adoption period. On the issue of timely loss recognition, the study found large negative net income to be positive which indicates that IFRS firms recognise losses more often. The study recognised that accounting quality improved after IFRS, firms exhibit higher values on profitability measure in the area of earnings per share.

Lantto&Sahlstrom (2009) evaluated the economic consequences of IFRS adoption in Finland by calculating ratios from a sample of 91 firms listed on Helsinki Stock Exchange and found out that there is an increase in profitability ratios but a decrease in liquidity ratios and the PE ratio in the period following the adoption of IFRS.

Ibe 2013 investigated liquidity management on the profitability of banks in Nigeria using a sample of three randomly selected banks and the result revealed that the Nigerian banking sector is faced with a great problem of liquidity management.

In 2014, Kurawa&Abubakar investigated the impact of liquidity on banks' profitability in Nigeria using five banks selected through systematic random sampling technique and found out that there is no significant impact between liquidity and profitability among Nigerian Banks.

Theoretical Framework

Capital Needs Theory

Capital needs theory suggests that firms that have growth prospects in the capital market strive for outward sponsorship prospects from the capital market (Core, 2001). They do this by allotting more shares or by borrowing from outward sources. External financing entails some form of competition among companies in order to acquire corporate capital in the best effective way possible. The competition for external financing in one way or the other requires companies seeking finance to know the kind of information they disclose. That is, it is only reasonable that such companies will want to disclose information that will make the providers of the finance have confidence in them. For example, companies seeking external finance will choose to disclose higher financial ratios so that the providers will be assured of their repayment/returns on their investment/transactions. This theory suggests that companies will be more willing to adopt IFRS if it will increase their liquidity and the information about which they will be very much willing to disclose to the public.

Signalling Theory

It has been argued that the most successful companies distinguish themselves so as to obtain capital in best conditions. According to the theory of political costs, firms with great proceeds will issue more information to validate their performance. Therefore, companies which upon transition to IFRS realize positive effects will be very willing to disclose more information in order to prove that their worse performance under the former accounting standards was due to the poor quality of accounting rules and not bad management.

This research is based on signaling theory as it is believed that firms will be willing to disclose information that will make their performance look attractive. That is, the conglomerate sector under study will be willing to disclose information that will make their liquidity level attractive to creditors and suppliers.

Research Methods

This research investigates the impact of IFRS on the liquidity ratios of the firms listed in the conglomerate sector of Nigeria. This was done by comparing the means of liquidity ratios computed under Pre-IFRS with those computed under IFRS for four years' period under each regime, from 2008 to 2011 under Pre-IFRS regime and four year period from 2013 to 2016 under IFRS regime. The population under study is 6 companies listed in the conglomerate sector of Nigeria with only four companiesas the sample size due to the fact that two of the companies (SCOA and John Holt) do not possess the data needed for this research work.

A panel data research design was used to carry out the study of IFRS adoption on liquidity ratios ofthe sampled population as this research design allows for data to be collected at a particular point in time anddata for quoted companies in Nigeria are kept annually. So, the data for this study were collected over a period of eight years (2008-2011 and 2013-2016).

Table 1: Measurement of Variables

Variables	Description	Formula
Dependent	Current Ratios Quick Ratio Cash Ratio	Current Assets ÷ Current Liabs Current Assets – Inventories ÷ Current Liabs Cash and Cash Equivalents ÷ Current Liabs
Independent Variables	IFRS: Dummy Variable	0 for Pre-IFRS Period 1 for Post-IFRS Period
Control Variables	Leverage Firm Size	Total Liabs ÷ Total Assets Natural Logarithm of Total Assets

DATA Analysis and Results

This section presents the analysed result of the data collected from different companies listed under the conglomerate sector of the Nigerian Stock Exchange to test the impact of IFRS adoption on liquidity of the firms.

Independent Variable: IFRS

Dependent Variables: Current Ratio, Quick Ratio and Cash Ratio

Control Variables: Firm Size and Leverage

Results and Discussion

Report

IFRS		CURRENT RATIO	QUICK RATIO	CASH RATIO	FIRM SIZE	LEVERAGE
POSTIFRS	Mean	4.52175	2.85075	.71450	71.21825	2.37600
	N	4	4	4	4	4
	Std. Deviation	.605172	.379182	.310830	.251573	.264660
	Median	4.66150	2.76400	.67750	71.27050	2.38250
	Range	1.346	.895	.703	.598	.581
	Variance	.366	.144	.097	.063	.070
PREIFRS	Mean	4.37000	2.83525	.96350	68.51425	2.12550
	N	4	4	4	4	4
	Std. Deviation	.401016	.397952	.190631	.558281	.149029
	Median	4.43250	2.83950	.93550	68.52550	2.09750
	Range	.825	.720	.387	1.222	.355
	Variance	.161	.158	.036	.312	.022
Total	Mean	4.44588	2.84300	.83900	69.86625	2.25075
	N	8	8	8	8	8
	Std. Deviation	.482138	.359943	.273305	1.499911	.239721
	Median	4.55300	2.76400	.81250	69.99050	2.17600
	Range	1.346	.914	.785	3.573	.684
	Variance	.232	.130	.075	2.250	.057

Source: SPSS

The result shows that there had been an increase in the liquidity of the firms under study. This can be seen in the differences shown in the figures above comparing the mean values of the pre and post IFRS periods. Except for the Cash Ratio which dropped from .96350 to .71450, Current Ratio rose from 4.37000 to 4.52175, Quick Ratio rose from 2.83525 to 2.85075 and even the Control Variables (Firm Size and Leverage) increased from 68.51425 to 71.21825 and from 2.12550 to 2.37600 respectively. This implies that the firms though are aware of the need to be liquid at all times so as to meet their immediate debts/liabilities, they are not holding so much cash and cash equivalents, these cash are rather held in a portfolio of assets that can be easily sold/converted into cash which is expected to increase the profitability of the firms.

ANOVA Table

			Sum of Squares	df	Mean Square	F	Sig.
CURRENT RATIO * IFRS	Between Groups	(Combined)	.046	1	.046	.175	.690
	Within Groups		1.581	6	.264		
	Total		1.627	7			
QUICK RATIO * IFRS	Between Groups	(Combined)	.000	1	.000	.003	.957
	Within Groups		.906	6	.151		
	Total		.907	7			
CASH RATIO * IFRS	Between Groups	(Combined)	.124	1	.124	1.865	.221
	Within Groups		.399	6	.066		
	Total		.523	7			
FIRM SIZE * IFRS	Between Groups	(Combined)	14.623	1	14.623	77.998	.000
	Within Groups		1.125	6	.187		
	Total		15.748	7			
LEVERAGE * IFRS	Between Groups	(Combined)	.126	1	.126	2.721	.150
	Within Groups		.277	6	.046		
	Total		.402	7			

Source: SPSS

Testing Hypothesis 1

H1: There is significant difference between Current Ratios before and after the adoption of IFRS

At a significance level of .690 (69%) which is greater than 5% at 95% confidence interval, it can be deduced that the firms' Current Ratio though had increased from what it used to be is not significant. Therefore, the alternative hypothesis is rejected and the null hypothesis accepted.

Testing Hypothesis 2

H2: IFRS adoption significantly affects the Quick Ratios of firms in Nigeria

The result showed that Quick Ratio has a positive but insignificant relationship with IFRS. It has a significance level of 96%which is greater than 5% at 95% confidence interval. The study therefore accepts the null hypothesis and rejects the alternative hypothesis.

Testing Hypothesis 3

H3: The adoption of IFRS has yielded a significant effect on Cash Ratios of firms in Nigeria

Also, the study rejects the alternative hypothesis of IFRS having a significant effect on Cash Ratios of firms as the result of the ANOVA table showed a level of significance of 22% which is greater than 5% at 95% confidence interval. In fact, it should be noted here that IFRS has a negative effect on Cash Ratio of firms as its mean value reduced under IFRS from what it was before the adoption.

Discussion of Results

The insignificant relationship found between liquidity ratios measured by Current Ratio, Quick Ratio, also Cash Ratio of firms listed under the conglomerate sector of the Nigerian Stock Exchange and International Financial Reporting Standards (IFRS) represented by dummy variables (0 &1) is consistent with the studies of Ibiamke and Ateboh-Briggs (2014) and Punda (2011) which claimed IFRS adoption does not significantly affect firms' liquidity, among other financial ratios in Nigeria.

Conclusion and Recommendation

While studies like those of Terzi, Oktem&Sen (2013), Callao,Jarne, &Lainez (2007), Lantto&Sahlstrom (2009), Blanchette et al (2011) have shown statistically significant difference in the financial ratios calculated under IFRS regime and those calculated under GAAP, this study however has shown a statistically insignificant relationship between IFRS and liquidity ratios of firms in Nigeria.

The study recommends that recommends that investors need to pay close attention to the liquidity position/status of firms but caution should be taken as the liquidity shouldn't be too high since a company with too much cash and heavily-weighted in short term securities is unlikely to be highly profitable.

Also, the conglomerate sector should be considered as an investment opportunity for it is opened to a large streams of income as the business combined are numerous and it is believed that even if one of the businesses is not doing so well, other lines of businesses should cover to the failing one. Hence, investors and creditors will be assured of returns on their investment/repayment.

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