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EVALUATION OF THE ROLE OF ACCOUNTING INFORMATION ON THE NIGERIAN STOCK MARKET GROWTH

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Abstract
This paper evaluates the role of accounting numbers in the Nigerian Stock market growth by analyzing changes in share prices of firms listed on the Nigerian Stock Exchange to accounting earnings and net book value. The method of estimating the information content of accounting information is Ordinary Least Squared. The study finds that there is a significant relationship between accounting numbers and share prices of companies list on the Nigerian Stock Exchange. The paper advocates for more efficient accounting system that will bring about the required reliable accounting data and information which will in turn increase investors' confidence in the Nigerian stock market.
Key Words: Stock Market, Accounting Information, Earnings and Accounting System.

1. INTRODUCTION

The role of accounting numbers is critical to stock market growth because financial reporting and disclosure is a vital channel of communication with investors and other stakeholders (Meyer, 2007). They allow a firm to tell its investors and the wider market about its performance. This explains why accounting has been globally highlighted as a major driver of stock market growth.

There is no doubt that capital market provides signals on current situations and future expectations. Strong domestic capital market helps ensure the efficient and sustainable funding of large-scale and long term projects. However, capital market (of which the stock market is a subset) cannot function effectively unless a number of elements are in place. One of such elements is accounting earnings which is the most widely used accounting information (Beisland, 2009).

Therefore, reliable accounting information can be described as an essential pre-requisite for stock market growth. Based on the "engine of economic growth" potential of the stock market, developed nations do not toy with their stock markets and relevance of financial reporting. That the United States of America stock market is very successful can in part be ascribed to the willingness of investors to invest more capital since they receive higher quality financial information than is available in any other place in the world (Turner, 2001). The Investors require information about the stock market to assist them take informed investment decisions. One of the ways this information is received is through published financial statements or accounting information released through other sources. Adequate accounting information is essential for efficient functioning of capital markets and by extension, the economic growth of any nation. The reason for this is that accounting data have impact on behaviour. It can influence, pacify, and instigate actions and reactions (Morgenstern, 1963, Iyoha, 2005). A study in UK and US found that analysts used Earnings per Share (EPS) as the main basis for valuing shares (Dimsdale and Prevezer, 1994). The development of stock market can therefore be thought of to be dependent on the integrity of financial reporting process. Little accounting information would generate little confidence and hence, low investment. This invariably could affect the economic growth of the country.

The timeliness, relevance, understandability, completeness of accounting information of a company will hence be of essence in increasing the investors' confidence to commit their funds. This would no doubt lead to the viability of the stock market. Considering the role of accounting information in stock market growth, the study objective is to determine whether there is any relationship between accounting information and stock prices of companies listed on the Nigerian Stock Exchange. It may not be an overstatement to say that Nigerian Stock Exchange will not function well without relevant and reliable accounting information (Umoren, Oyerinde and Nwobu, 2009). Deficiency in Nigerian Stock Exchange will affect Nigerian economy because capital market is the engine of economic growth (Okeke, 2004). Hence, the study as to whether the market prices of stock listed in the Nigerian Stock Exchange reflect accounting information is not only important to investors but also crucial to Nigerian economic growth.

In the light of this, the rest of the paper is divided into four sections as follows: related literature, methodology, discussion of result and conclusion and recommendation.

2. REVIEW OF RELATED LITERATURE

The importance of financial accounting information in stock market growth can best be appreciated by examining how well accounting information numbers such as earnings impact on stock prices. Research indicates that earning is a factor that is "priced" in the securities market (Blume and Husic, 1973). The share price impact appears to subsume both the earnings yield and size effects upon abnormal security returns. The research also indicates that share price has a strong cross-sectional association with security returns. Covill (1998) investigates relationship between changes in earnings per share and the performance of the market. He employs linear correlation coefficient and infers that changes in average earnings per share over five years might be a good predictor of average changes in stock prices over the next five years. Salmi, Virtanen, Yli-Olli and Kallunki (1997) claim there is a clear relationship between the firm's accounting and stock-market variables. Ariff, Loh and Chew (1997) also report relationship between earnings and share prices. Their results show that unexpected earnings changes are significantly associated with share price changes. It is pertinent to note that most of these studies were carried out in the developed countries.

Generally, investors are not in a situation to directly assess the performance of companies in which they intend to invest. They usually depend on financial reports prepared by the management of such organizations. Financial report is one of the best sources of accounting information about a company. Financial reporting is an essential part of disclosure and helps the investor to discover investment opportunities. Thus, the primary purpose of financial statements is to provide information concerning the financial situation of a company, its operational results, any changes of control in the company and cash flow. Hendricks, (1976) also asserts that the main reason for which accounting information is generated is to facilitate decision making. However, for financial reporting to be effective, among other requirements, it should be relevant, complete and reliable. These qualitative characteristics require that the information must not be unfair nor has predisposition of favouring one party over the others. Accounting information should give a decision maker the capacity to predict future actions. It should also increase the knowledge of the users to identify similarities and differences in information.

One of the most important components and widely used figures of financial report by the users of accounting information in general and investors in particular is earnings. Earnings, which is also called 'net income' is an indicator of the profitability of the company. Earnings is the accounting information most analyzed and forecast by security analysts because it is oriented towards the interest of shareholders who are the important users of financial statement (Brow, 1994, cited in Deegan, 2004). Investors use accounting earnings to price stock because it is thought that the level of earnings and changes in earnings indicate relevant information about a company's current and future ability to engender economic value that other investors will recognize and price aptly (Hawkins, 1998). With other data, earnings can be very valuable in appraising management's past performance and predicting future earnings and cash flow potential. Earnings-per-share (EPS) has become the single accounting number that is reported most often in media and receives by far the most attention by investors and creditors.

Lang and Lundholm (1996) as cited in Deegan show that firms with more accounting informative policies have a larger analyst following and more accurate analyst earnings forecasts. Germon and Meek (2001) state that those who have funds to invest or lend may decide where to place their resources based on the financial accounting information reports. They state further that importance of stock markets as a source of external finance is growing around the world and stock market development has become a top priority of many countries. Turner (2001:1) advances that:

> *The reason the U.S. capital markets are so successful is simply that people are willing to invest more capital here because they perceive higher quality financial information than is available in any other place in the world. And with that higher quality information, they are able to make more informed and better reasoned decisions on how to allocate their capital. The result is higher returns for investors, lower cost of capital for market participants, and greater availability of capital in the deepest, most liquid markets.*

According to Harteneck (1997) as cited in Izedonmi (2006), countries where "doubts exist as to the quality, consistency or transparency of their rules, a price must be paid for the shortcomings namely lower market values for their shares and /or higher interest rates for their financing."

3. METHODOLOGY

The relationship between accounting numbers and stock market growth was examined using secondary data of 68 companies that have the required data and were listed on the Nigerian Stock Exchange from 2002 to 2008. This period is of interest because of growth in the Nigerian stock market at the time. This section further discusses model specification and model estimation technique.

3.1 Description of the Models

In order to give empirical support to this work, an observation of the investors' reactions to accounting information was carried out to establish correlation between accounting information and share prices. Proxies for accounting information are Earnings per Share and Net Book per Share. Established on ideas of Ohlson (1989) and Edwards and Bell (1961), a model was developed.

Model

The Relationship between Share Prices, Earnings per Share, Net Book per Share

$LDSP_{it} = \beta_0 + \beta_1 VRE_{it} + \beta_2 VRBV_{it} + e_{it}$

for i =1,2..., N cross-section units and periods t = 1,2....T

Where:

LDSP: Last Day price per share
VRE : Earnings per Share
VRBV = Book Value per Share
t: Time dimension
i: individual firm

LDSP is the dependent variable; β_0, β_1, $\beta 2$, are regression coefficients with unknown values; *VRE* and $_{VRBV}$ are the independent variables and e is a random error component.

APriori Expectation is such that $\beta_{>0\,(i=1\text{-}3)}$.

3.2 Model Estimation Technique

In an attempt to estimate the model above, the Ordinary Least Squares Estimation technique was used in running the regression, Stata/SE10 package was employed.

Table 1: Results and Data Analysis showing Relationship between the Variables

Dependent Variable: LDSP		
Estimator	OLS	
Variable	Coef	Prob
VRE	.1073168* (8.99)	0.000
VRBV	-.00004 (-0.05)	0.963
Cons	10.34729* (5.85)	0.000
``R^2	0.1602	
Adj R^2	0.1564	
Prob. F	0.0000*	

Note: * significant at the 1% level
Numbers in parentheses are t- values
LDSP = Last trading day share price; VRE = Earnings per Share;
VRBV = Net Book Value
LDSP are stated in naira while VRD and VRBV are

Source: Results of Stata/SE10 Analysis

4. DISCUSSION OF RESULTS

Table 4.1 shows the results of all applied variables in the analysis of the model. The table presents the results of Ordinary Least Square (OLS) which is Stock Market Reaction to Accounting Earnings and Net Book Value in Equity Valuation. In this model, earnings (VRE) are highly significant at 1% level in explaining share price. The output of OLS indicates that VRE has a larger beta coefficient, absolute terms than Net book value (VRBV). Beta value measures the degree to which each of the explanatory variables affects the dependent variables. Using OLS, the coefficient of VRE is 0.107. It means that a unit change in earnings will lead to approximately 11 kobo change in share price. In order words, 1 kobo change in earnings will lead to approximately 11 kobo change in share price. This is because share prices are stated in Naira while earnings are stated in kobo.

Moreover, the R-squared and adjusted R- squared are high. They are 16% and 15.6% respectively. Accounting number is typically deemed to be value relevant if its estimated regression coefficient is significantly different from zero (Holthausen and Watts, 2001).

The result of Net book value beta coefficient is -.00004 which is not significant. The reason for the insignificance of VRBV could be that the share price does not reflect the actual situation for the firm. Another reason could be that most investors still depend on the earnings performance rather than the Net Book Value. Besides, there may be other factors affecting a firm's performance other than the variables used in the study.

F statistics is 0.000 which is highly significant. F statistics is a measure of joint significance of all explanatory variables of the model used. This may provide support for the proposition that: first, there is a positive relationship between earnings, book value and stock market in the Nigerian Stock Exchange (NSE). Second, earnings have great information content (comparable to net book value). Our results are consistent with the findings of the previous studies such as Pourheydari, Aflatooni and Nikbakhat (2008) and Beisland, (2009) among others. Based on this analysis, we conclude that there is significant relationship between accounting information and stock market growth.

5. CONCLUSION AND RECOMMENDATION

This paper has discussed the link between two key features- accounting information and Nigerian stock market growth. The link between accounting information and stock market is usually demonstrated through the aggregate markets reaction to accounting information.

Therefore, it can be inferred that sustainable development of the Nigerian stock market can be boosted through reliable accounting information. Without confidence in accounting information, investors will not invest adequately in the Nigerian Stock Exchange.

It therefore becomes imperative that policy makers begin to think of alternative techniques of stimulating economic growth via vibrant stock market. As a result, the study advocates for greater commitment and more efficient accounting system that will bring about the required reliable accounting information which will in turn increase investors' confidence in Nigerian stock market.

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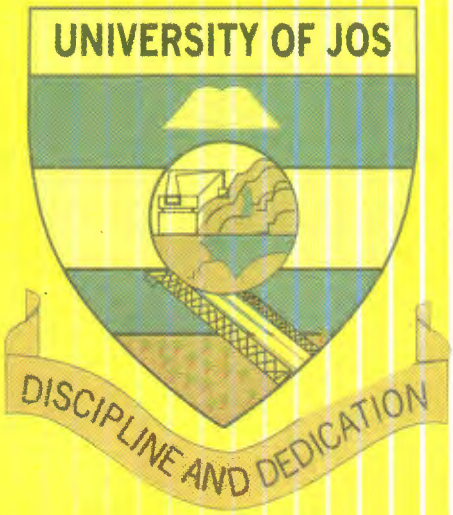

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