

## Chapter 5

# Value Relevance of Accounting Information in the Emerging Chinese Stock Market (Re Visited)

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### ABSTRACT

*Value relevance of accounting information is a very important issue – not just from the perspective of Foreign Direct Investment and the reliability and relevance of financial and accounting information for investors – whether institutional or individual, but also in matters of Corporate Social Responsibility and financial reporting. This being of crucial importance given the need to enhance the quality and presentation of financial information, the need for comparability and consistency as a means of enhancing the relevance and reliability of financial information. This issue of reconciliation of discrepancies hence constitutes a matter in need of urgent redress in capital markets.*

### INTRODUCTION

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vidual, but also in matters of Corporate Social Responsibility and financial reporting. This being of crucial importance given the need to enhance the quality and presentation of financial information, the need for comparability and consistency as a means of enhancing the relevance and reliability of financial information. This issue of reconciliation of discrepancies hence constitutes a matter in need of urgent redress in capital markets.

As highlighted in Enron (IFRS:2014):

*Enron's accounting was misleading to users and that specifically, the accounting risks for Enron were too high to be considered acceptable or presented fairly. To make them acceptable, adjustments would have been necessary to the reported estimates. Accounting risks should have been reduced to an acceptable level (as suggested by ISA 540) so that the reported numbers were more reliable.*

This chapter seeks to contribute to the gap in the literature on the value relevance of accounting information in China. In so doing it investigates the relevance and reliability of results derived in this study, their applicability to current market developments – as well as recent fluctuations and volatility in the financial markets.

Conclusions derived from previous study undertaken by Chen et al, (2001). Is Accounting Information Value-Relevant in the Emerging Chinese Stock Market? Journal of International Accounting, Auditing & Taxation 10 (2001) 1–22 are as follows:

## **Conclusions of the Study**

1. Using a sample of all available observations in the Shanghai and Shenzhen Stock Exchanges from 1991 to 1998, the authors obtain evidence of value-relevance of accounting information in China based on a return and a price model. The results provide evidence that accounting information is value-relevant in the Chinese market according to both the pooled cross-section and time-series regressions or the year-by-year regressions. The evidence is consistent between the return model and the price model.
2. Authors examine whether value-relevance changes in a predictable manner with respect to four factors including positive versus negative earnings, firm size, earnings persistence, and percentage of public share holdings. Overall, the results support the conclusion that value-relevance in China changes in a predictable manner. Chen et al find that while accounting earnings are value-relevant for companies reporting positive earnings, there is no value-relevance evidence for companies reporting losses.

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