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A Theoretical Review of The Impact of Accounting Information on Capital Markets in Nigeria

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ABSTRACT

The study focused on the impact of accounting information on capital markets in Nigeria. Accounting information is very important, especially, when sourcing for funds for possible expansion. With the use of secondary data, the study adopted library and theoretical literature survey approach and quotient research analysis. Extant literature was reviewed and the result shows that accounting information impacts greatly on capital markets in Nigeria through the participants and instruments. And that without the accounting information capital market participants will not respond as well. This research work also noted the strategic role accounting information provides for users of the information in making accurate decisions and in understanding their business properly. The qualitative characteristics of accounting information have a major influence in economic decision making process to owners, managers and creditors/customers. Transparency in financial reporting enables investors, creditors and contributors in the market to assess the company's financial condition. In other words, transparent financial information can help companies achieve good investment opportunities and improve the supervisory role of managers by reducing information asymmetry. Achieving this goal requires that the information has the necessary quality and transparency. Therefore, capital markets can function better through consistent practice and availability of accounting information in Nigeria. It is also noted that financing opportunities and providers of funds needs accounting information to ensure financial security. This study also advised policy makers and *monitoring agents to ensure complete compliance to set standards in the preparation and reporting of financial reports in Nigeria.*

***Keywords**: Accounting information, Financial reports, Transparency, Capital, Capital market.*

INTRODUCTION

In the business environment, accounting information is key to the growth and sustenance of any business corporation. Information regarding the accounting figures or finances is of great interest to both the corporation and other stakeholders. The accounting figures reported by a firm are one of the most important information resources for investors' decisions concerning stock prices (Breton & Taffler, 1995). Through the information gotten monthly, quarterly or yearly, actions or responses are shaped positively or negatively. Basically, every business corporation needs funding for possible growth and expansion. One major source of getting these funds is through the capital market. The capital market will only respond in accordance to the accounting information provided by the corporation. Therefore, a good report will certainly receive a positive respond. This paper is structured accordingly as follows: the above section is the first section called the *introduction*. This will be followed by section two, *accounting information, concepts and practice*. The third section focuses on *capital markets, capital market participants and instruments,* followed by review of *theories and prior studies on the impact of accounting information on capital market in Nigeria*, and will be concluded in the fifth chapter with *conclusion and recommendation*

ACCOUNTING INFORMATION

In general, accounting is concerned with the process of measuring and communicating business information to satisfy the information needs of the users of such information. The importance of accounting information in the business environment is far reaching, in that, both external and internal decisions are directed in accordance to the outcome of the accounting information. For instance, within the firm, internal accounting information could be used to make decisions concerning the evaluation of projects and profitability. Meanwhile, external accounting information or financial reporting is a practice that goes beyond the boundaries of the reporting firm and is directed towards helping stakeholders in making decisions regarding their relationship with the firm (Spohr, 2005). Accounting information involves standard practices and principles to give stakeholders an accurate depiction of a firm's finances, including revenues, expenses, profits/ losses, capital and cash flows as a formal record that provides an in-depth insight into the financial information of the firm upon which relevant decisions could be made. The overall aim of accounting information is to direct decisions for possible actions or reactions concerning the firm.

Financial accounting is the aspect of recording and categorizing business transactions. Thus, data is generated historically, meaning it's from the past activities, and it must be prepared in conformity with external regulations as provided in IFRS and IAS.

The concept of International accounting is simply the specialty within the entire discipline that is focused on using specific accounting standards that are as relevant in balancing the books of a company over-sea. Financial statements are prepared according to agreed upon guidelines so as to achieve the objectives of the report. These objectives of financial reporting as stated in the Financial Accounting Standards Board (FASB), statement of financial accounting concepts No 1, are to provide information that;

1. Is useful to existing and potential investors and creditors and other users in making rational investment, credit and similar decisions.
2. Helps existing and potential investors and creditors and other users to assess the amounts, timing and uncertainty of prospective net cash inflows to the enterprise.
3. Identify the economic resources of an enterprise, the claims to those resources and the effects that transactions, events and circumstances have on those resources.

These objectives could only be achieved when the preparers of such accounting information adhere to the Generally Accepted Accounting Principles (GAAP). It is often presented through the statement of financial position, statement of profit or loss account and other comprehensive income, statement of cash flow, statement of equity and notes to the accounts.

TYPES OF FINANCIAL REPORTS

1. Income statement: otherwise called statement of profit or loss account and other comprehensive income is one of the financial statements of a company and shows the company's revenues and expenses during a particular period.
2. Statement of financial position: A statement of financial position is another name for the balance sheet. It displays the assets of a company and their sources of financing, debt and equity.
   The statement of financial position displays the financial health of a company at a specific point in time. Whereas, the income statement reports the financial performance of a company over the course of a period, usually a year. Investors and creditors will use the statement of financial position to determine how efficiently a company is using its resources and how efficiently is it being financed.
3. Statement of cash flows: A cash flow statement summarizes the amount of cash and cash equivalents entering and leaving a company
4. Statement of changes in equity: A statement of change in equity (also referred to as statement of retained earnings) is a business' financial statement that measures the changes in owners' equity throughout a specific accounting period. It covers the following elements: Net profit or loss, Dividend payments.
5. Notes to the accounts: Notes to the financial statements disclose the detailed assumptions made by accountants when preparing a company's: income statement, balance sheet, statement of changes of financial position or statement of retained earnings. The notes are essential to fully understanding these documents.

These statements must be complete and show that the accounts are true and fair in order to give the users a sense of direction.

The result of processing an accounting data is called Accounting Information. The accounting process shows useful books of records, files, vouchers, and such other data relating to processing the accounting data in order to have useful financial information (Abdullahi, 2014). When quantitative values are attached to economic activities of the past, present and future, it gives a better understanding of the business. This will guide suppliers, creditors and investors while choosing options for investment and supply of materials/funds to the business. Furthermore, the qualitative characteristics of accounting information enhance investment and investor decision, and aid the actualization of operational goals and increased performance. Thus, for capital markets to function properly the aspect of accounting information which enhances financing options must be properly managed (Okoh & Uzoka, 2012). It is often said that the quality of decision depends on the quality of information contained in the financial statement presented by the management (Umar, 2018). According to Amidu et al., (2011) accounting information is a representation of critical tools for recording, analyzing, evaluating and monitoring the financial status of the business and also prepare documents needed for tax purposes, giving information to support other functions of the business by providing an understanding of the present financial situation of the enterprise to aid economic and strategic decision making. For business to grow and succeed, proper accounting system needs to be maintained. The failure or success, Ankrah et al. (2015) depends on keeping accurate and timely accounting information to give a clear financial image of the business. That is why it is necessary to have a good body of professional accountants or an accountant to use methods to ensure that accounting policies could be fallowed and implemented regularly (Pavtar, 2017). Studies indicated that accounting information can be used as a measure of the probability of alternative course of action and performance and to evaluate the response of the capital market participants in terms of liquidity, leverage, profitability and activity from which the firm's performance could be improved (Abusomwan et al., 2016). The study, therefore, highlights how accounting information can have great impact on capital markets in Nigeria.

ACCOUNTING INFORMATION: CONCEPT AND PRACTICE

Accounting information is information gotten from accounting data. The process of generating such financial information to the organization is called the Accounting Information System (AIS) (Mia, 1993). The modern AIS is the use of computer in processing the accounting data while the traditional AIS mainly uses biro and paper. The modern AIS have greater potentials to influence enterprise performance (Haitham et al., 2019). It also enhances the qualitative characteristics of accounting information in terms accuracy and timeliness. According to Hosain (2019) AIS uses Information and Communication Technology (ICT) tools to assist the organization in performing its monetary and economic functions. Emeka, (2012) defined AIS as a system that collects, stores, and process financial and accounting data to help managers of the organization make plans, direct, control, and evaluate decisions and performances of the organization. It is used to record and process the financial transactions of the business, combining the methods of control, and accounting technology to track transactions, provide internal and external reporting data, financial statement and trend analysis (Urquia et al., 2011). AIS is a system that processes data and information to provide users with the information needed for accurate and timely decision making (Lallo & Selamat, 2014). This system must be capable and reliable for analyzing and monitoring the financial status of the organization, preparations of document for tax reasons, provision of information need to support other functions of the organization, like production, marketing, human resource management, and strategic planning (Harash, et al., 2014).

According to a study conducted by Perez et al. (2011), to test the impact of AIS on performance measure in terms of responses in from the capital market participants, the result showed a very significant positive relationship between capital market reactions and accounting information for a better performance measure. The usefulness of accounting information in business is well known, whether in the public or private sector, capital markets and capital market participants requires accounting information to make financial decisions. As acknowledged by Saira et al. (2010) organizations need AIS to improve organizational efficiency and increase their ability to compete with others and also have a better management commitment. The functions of AIS is to assign quantitative values of the past, present and future economic events. This is in line with the requirement of the International Accounting Standard Board (IASB), for the preparation of financial statements, framework in paragraph 26, information is relevant and useful when it is capable to influence the economic decisions of users to aid them evaluate the past, present, and future events or confirming or correcting pervious evaluations (Lawani et al., 2005). Paragraph 47 of the Financial Accounting Statement Board (FASB) says that in order to be relevant, accounting information must be capable of making a difference in a decision by helping users to form predictions concerning the results of the past, present and future events or to confirm or make correct expectations. The major benefits of AIS are seen from its impact on the decision making process, quality of accounting information, performance evaluation, internal controls and enhancing business transactions (Sajady et al., 2008). This is true in that the success of every business is borne out of a well informed decision and according to Onah (2011) fundamental accounting information provides business owners and managers with basic skills in book-keeping, purchasing, supplying, bargaining, determining labour costs, simple budget planning and keeping of accurate receipts and payments and having knowledge of prudent financial and working capital management which other stakeholders can rely upon for decision making. Again, a study conducted by Muhindo et al. (2014) showed positive signs between accounting information and profitability level of firms.

THE CAPITAL MARKET

Capital markets are used to sell different financial instruments, including equities and debt securities. These markets are divided into two categories; primary and secondary markets. When a company publicly sells new stocks and bonds for the first time, it does so in the primary capital market. This market is also called the new issues market. In many cases, the new issue takes the form of an initial public offering (IPO). While a secondary market is any financial market where investors buy and sell securities such as stocks or bonds, which have already been issued by a company. There are about 526 listed capital market operators in Nigeria (SEC, 2019). The best-known capital markets include the stock market and the bond markets. The Nigerian capital market is principally a market for long-term investments where corporate equities and long-term debt securities are issued and traded. It is a market that is regulated by the Securities and Exchange Commission (SEC), which is the apex regulatory body of the Nigerian Capital Market.

BENEFITS OF CAPITAL MARKET

One of the most significant benefits of capital markets is its potential to reduce unemployment. By providing businesses with the necessary capital to expand their operations, capital markets allow businesses to create new job opportunities for the workforce.

Capital markets can also increase tax revenues for the government.

Capital markets also play a vital role in boosting foreign exchange reserves. As businesses expand through capital markets, they tend to attract foreign investment, leading to an influx of foreign exchange into the economy.

Capital markets can stimulate overall economic growth by promoting entrepreneurship and innovation. Access to capital markets enables entrepreneurs to raise funds and invest in new ideas, technologies, and businesses, creating a more dynamic and competitive business environment that foster innovation.

PARTICIPANTS OF THE CAPITAL MARKET

The three main participants of the capital markets are savers (also known as investors), borrowers, and stockholders. The term capital market includes the stock market, bond market, and related markets. The term is frequently used with reference to banks and banking in both a narrow and broad sense.

Capital market, as it is known, is that segment of the financial market that deals with the effective channeling of medium to long-term funds from the surplus to the deficit unit. The process of transfer of funds is done through instruments, which are documents (or certificates), showing evidence of investments.

INSTRUMENTS OF CAPITAL MARKET

The instruments traded (media of exchange) in the capital market are:

1. **Debt Instruments**

A debt instrument is used by either companies or governments to generate funds for capital-intensive projects. It be can obtained either through the primary or secondary market. The relationship in this form of instrument ownership is that of a borrower – creditor and thus, does not necessarily imply ownership in the business of the borrower. The contract is for a specific duration and interest is paid at specified periods as stated in the trust deed (contract agreement). The principal sum invested, is therefore repaid at the expiration of the contract period with interest either paid quarterly, semi-annually or annually. The interest stated in the trust deed may be either fixed or flexible. The tenure of this category ranges from 3 to 25 years. Investment in this instrument is, most times, risk-free and therefore yields lower returns when compared to other instruments traded in the capital market. Investors in this category get top priority in the event of liquidation of a company.

When the instrument is issued by:

The Federal Government, it is called a Sovereign Bond;

A state government it is called a State Bond;

A local government, it is called a Municipal Bond; and

A corporate body (Company), it is called a Debenture, Industrial Loan or Corporate Bond

2. **Equities**

This instrument, also called Common Stock, is issued by companies only and can also be obtained either in the primary market or the secondary market. Investment in this form of business translates to ownership of the business as the contract stands in perpetuity unless sold to another investor in the secondary market. The investor therefore possesses certain rights and privileges (such as to vote and hold position) in the company. Whereas the investor in debts may be entitled to interest which must be paid, the equity holder receives dividends which may or may not be declared.

The risk factor in this instrument is high and thus yields a higher return (when successful). Holders of this instrument however rank bottom on the scale of preference in the event of liquidation of a company as they are considered owners of the company.

3. **Preference Shares**

This instrument is issued by corporate bodies and the investors rank second (after bond holders) on the scale of preference when a company goes under. The instrument possesses the characteristics of equity in the sense that when the authorized share capital and paid up capital are being calculated, they are added to equity capital to arrive at the total. Preference shares can also be treated as a debt instrument as they do not confer voting rights on its holders and have a dividend payment that is structured like interest (coupon) paid for bonds issues.

Preference shares may be:

Irredeemable, convertible: in this case, upon maturity of the instrument, the principal sum being returned to the investor is converted to equities even though dividends (interest) had earlier been paid.

Irredeemable, non-convertible: here, the holder can only sell his holding in the secondary market as the contract will always be rolled over upon maturity. The instrument will also not be converted to equities.

Redeemable: here the principal sum is repaid at the end of a specified period. In this case it is treated strictly as a debt instrument.

It is also worthy of note that interest may be cumulative, flexible or fixed depending on the agreement in the Trust Deed. A Trust Deed is a document that states the terms of a contract. It is held in trust by the Trustee.

4. **Derivatives**

These are instruments that derive from other securities, which are referred to as underlying assets (as the derivative is derived from them). The price, riskiness and function of the derivative depend on the underlying assets since whatever affects the underlying asset must affect the derivative. The derivative might be an asset, index or even situation. Derivatives are mostly common in developed economies.

Some examples of derivatives are; Mortgage-Backed Securities (MBS), Asset-Backed Securities (ABS), Futures, Options, Swaps, Rights, and Exchange Traded Funds or commodities.

Of all the stated derivatives, the common one in Nigeria is Rights where by the holder of an existing security gets the opportunity to acquire additional quantity to his holding in an allocated ratio.

THEORETICAL FRAMEWORK

The study first based on the Technology Acceptance Model as propounded by Davis (1986). Technology Acceptance Model is related to the Theory of Analytic Action, which involves the supposed acceptability of tools and changes that occurs in the system that operators must accept. The modern information system is technology driven and until workers in this setting accept to use these technologies, proper accounting information is still a mirage. The various means technology can be used to enhance corporations, especially, in storing as well as communicating accounting information are evidenced in the aspect of spotting document for further review launched in the capital market, processing larger volume of transactions identifying business trends and having a preliminary understanding through the information disseminated for quick and economic decision making.

Again, is the Knowledge Based Theory by Penrose (1959). This theory is of the opinion that knowledge is a resource and that accounting/business knowledge is a strategic asset of the enterprise since it can make the business have a competitive advantage involving tacit and explicit knowledge of the business enterprises. The knowledge-based theory of the firm considers knowledge as the most strategically significant resource of a firm. The three aspects of this theory states that, knowledge is personal, procedural, and propositional (Barney, 1997). It recognized the multiple stages knowledge passes and revolves in a firm such as business policies, employees/personnel management, documents and documentation, accounting processes, products and services which are of great importance (Okafor, 2019). The knowledge of the firm will form the basis of the accounting information. The technical know-how of business is capable to improve performance competitiveness and growth in the long run. So Technology Acceptance Model and Knowledge Based Theory in business can have great impact on the functioning of capital markets. The American Institute of Certified Public Accountants (AICPA) recognized technology as imperative to business enterprise and accountants. Therefore, this research acknowledged the Knowledge Based Theory as the knowledge of the firm which forms the accounting information that may direct reactions of the capital market on the basis of

Technology Acceptance Model.

The capital market theories and pricing models included in the study are Portfolio Theory, the Efficient Market Hypothesis, the Capital Asset Pricing Model, the Arbitrage Pricing Theory, Options Theory and the Black Scholes and the Option Pricing Model.

The functioning of a capital market follows the theory of the circular flow of money. This is the basis of the study and can be made possible through the interactions of the firm, the market and the market participants based on the accounting information provided by the firm. For example, a firm needs money for business operations and usually borrows it from households or individuals. In the capital market, the money from individual investors or households is invested in a firm's shares or bonds.

PRIOR STUDIES

Most African countries' capital markets are underdeveloped, but countries that introduced reforms aimed at developing their capital markets have been growing at a higher rate and sustainable levels (Kolapo & Adavamola 2012). The study indicated that South Africa, a country with the largest and most developed capital market in Africa by way of capitalization and trading volume, has been having a steady growth since 2000. Empirical studies have affirmed the positive relationship between accounting information and capital market activities. The significance of accounting information for company valuation is analyzed in value relevance studies. Value relevance research is based on the idea that accounting information is useful for determining company value in the case that its cross sectional variation corresponds with the cross sectional variation in stock prices or stock returns. Barth et al. (2001) proposes that Value relevance research examines the association between accounting amounts and equity market values.

Ben-Nasr and Abdullah (2016) examined the relationship between stock price information content and labor investment efficiency. The results of their research showed that stock information content has a significant positive relationship with investment efficiency. Omokhudu & Ibadin (2015) examined the value relationship of accounting information content and reported that income, dividends and cash flow were statistically significantly related to share price.

Ahmadi and Bouri (2018) in studying the content of financial information showed that income and book value are significantly related to the value of the company as well as the value of the company's shares. Mofidabadi et al. (2019) designed a mixed model of financial decisions for the development of Iranian financial markets. The results showed that each of the mixes of financial decisions of the government, companies and households has a significant impact on the development of the Iranian capital market.

CONCLUSION AND RECOMMENDATIONS

The study focused on the impact of accounting information on capital markets in Nigeria. Accounting information is seen to be of great importance to growing any business, especially, when sourcing for funds for possible expansion. With the use of secondary data, the study adopted library and theoretical literature survey approach and quotient research analysis. Literature reviewed shows that accounting information impacts greatly on capital markets in Nigeria through the participants and instruments. And that without the accounting information capital market participants will not respond as well. This research work also noted the strategic role accounting information provides for users of the information in making accurate decisions and in understanding their business properly. The qualitative characteristics of accounting information have a major influence in economic decision making process to owners, managers and creditors/customers. Therefore, capital markets can function better through consistent practice and availability of accounting information in Nigeria. It is also noted that financing opportunities and providers of funds needs accounting information to ensure financial security. This study therefore, recommend that policy makers and monitoring agents should ensure complete compliance to set standards in the preparation and reporting of financial reports by firms in Nigeria.

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