



# THE IMPACT OF IFRS ADOPTION ON EARNING MANAGEMENT AND MARKET VALUE: A COMPARISON STUDY OF SAUDI LISTED COMPANIES (2012-2022)

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## ABSTRACT

*This study examined the impact of International Financial Reporting Standards (IFRS) adoption on earnings management and market values of Saudi companies listed on the Saudi Stock Exchange (Tadawul). The study used descriptive statistics, correlation analysis, and comparative analysis of sampled companies five years before IFRS adoption and five years after (2012 up to 2022) to estimate the results.*

*The study population is non-financial companies listed on the Saudi stock exchange market. A sample of 188 companies was selected from 270 non-financial listed companies, representing 70%. The study revealed that there are still contradictory results concerning the relationship between accounting rules and the level of earnings management. The result implies that IFRS have created an environment that mitigates earnings management practices in favor of better quality of performance. It also supports the prediction of the accrual model that earnings management incentives are stronger under local accounting standards than under IFRS, acting as a moderator for*

*reducing earnings management among global companies. These results deny the concerns that had been raised by some market participants suggesting that IFRS would lead to increased earnings management.*

**Keywords:** IFRS Adoption, Earning Management, Market Value, and Saudi listed companies.

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## 1. Introduction

### 1.1 Background of the Study:

The profit and market value of a business have more attention among investors, practitioners, regulators, and other users of companies' financial reports. For this, the companies give a lot of attention to follow-up and managing their market value and earnings.

The International Financial Reporting Standards (IFRS) have been widely adopted by countries around the world, including Saudi Arabia. The adoption of IFRS expects to improve the quality of financial reporting and increase comparability across companies. However, there are also concerns that IFRS adoption may lead to increased earning management and a decrease in market value.

Daske and Gebhardt (2006) concluded, "IFRS has increased the quality of financial reporting. They also found that there is a positive relationship between transparency, firm size, independent board membership, and public subsidiaries. It has been pointed out that the implementation of IFRS and corporate governance has a positive impact on the transparency of financial statements and disclosure. They have also found out that among the firms that implement IFRS, there is a strong relationship between liquidity and level of disclosure in the banking sector".

Byard et al. (2010) found that analysts' absolute forecast errors and forecast dispersion decrease only for those mandatory IFRS adopters located in countries with both strong enforcement regimes and domestic accounting standards that differ significantly from IFRS. Furthermore, for mandatory adopters located in countries with both weak enforcement regimes and domestic accounting standards that differ significantly from IFRS, they found that forecast

errors and dispersion decrease more for firms with stronger incentives for transparent financial reporting. These results highlight the important roles of enforcement regimes and firm-level reporting incentives in determining the impact of mandatory IFRS adoption.

DeFond (2011) reported that “Proponents of IFRS argue that mandating a uniform set of accounting standards improves financial statement comparability that in turn attracts greater cross-border investment. He argued that foreign mutual fund ownership increases as mandatory IFRS adoption leads to improved comparability. He also found that that mandatory IFRS adoption results in a greater increase in foreign investment among companies in countries with strong implementation credibility”.

Hellman (2011) stated, “The adoption of International standards in Sweden originated from a need to ensure a satisfactory development of accounting practices in multinational firms. He reported that empirical research suggests that the quality of the international accounting standards is high and that IFRS adoption is associated with capital market-related economic benefits, including increases in the stock’s market value, increases in market liquidity, and a lower cost of capital. He noticed that the widespread adoption of IFRS might not lead to adequate and consistent changes in local accounting practice because the legally enforceable versions of IFRS may not fully correspond to IFRS as issued IASB and because the existence and functioning of enforcement institutions may vary across jurisdictions. In addition, he noticed that within a certain country, firms’ incentives to report informative profit numbers to capital providers will vary due to firm-specific factors and the institutional environment. He has also shown that the empirical results display material increases in net profit and balance sheet numbers in connection with the hard adoption of IFRS. He concluded that although Sweden is classified as a country with a very high quality of its legal system and enforcement in general, the Swedish adoption of IFRS during 1991- 2004 was in fact soft”.

In their study of the impact of IFRS adoption in China, He et al. (2011) surveyed many relevant studies and reported that there are mixed results regarding the impacts of IFRS adoption. They found that while some researchers reported an overall increase in foreign investments in countries that have mandated the use of IFRS, other researchers reported that the adoption of IFRS failed to improve the quality of financial reporting in some countries. In addition, He et al. (2011) found that there could be some unintended consequences of mandatory IFRS adoption. They indicated that the move towards Fair Value Accounting would improve transparency but it would be beneficial only when the fair value could be known or if it could be measured efficiently which is not the case in China as the information on the fair

value of many assets may not be available. Consequently, with the absence of active markets for nonfinancial assets, earnings may be managed to avoid reporting losses, especially in regions with weaker enforcement institutions.

Hail et al. (2010) considered many empirical studies related to the adoption of IFRS in many countries around the world. They found that companies who voluntarily adopted IFRS have in general witnessed positive capital market impacts. They caution however that such results may not be surprising since companies would not choose to adopt IFRS unless they are going to gain benefits. Some studies surveyed by Hail et al. (2010) indicate that mandatory adoption of IFRS in Europe has led to an increase in market liquidity, a decrease in the cost of capital, and an increase in the integration of capital markets although the magnitude of these effects varies from one country to another. Regarding the fair value debate, Hail et al. (2010) have stated that, “While fair value accounting is in many ways conceptually appealing, it is often difficult to implement and could be incompatible with the current legal, institutional, and political environment in the United States. In addition, Hail et al. (2010) reported that countries have different circumstances and that not all countries and firms benefit from the adoption of IFRS. In addition, they found that it is not certain that benefits are based solely on adopting new accounting standards. Moreover, they reported that the impact is more apparent in countries with strong enforcement and whose GAAP is highly different from IFRS. According to Hail et al. (2010) adoption of IFRS could improve the chances of trade between countries but may have the undesirable effect of disclosing some proprietary information to competitors. As reported by Hail et al. (2010), reporting discretion may be minimized with the adoption of IFRS compared to many local GAAP. Hail et al. (2010) conclude by stating that benefits from the adoption of IFRS in the United States are based on the utilization of what they call the “IFRS Network” which has grown significantly worldwide in addition to the benefits of comparability.

On the other hand, different studies also have been conducted in Saudi Arabia reflect the local experience about earning management. For example, Alghamdi (2012) and Habbash and Alghamdi (2015) examined earning management in Saudi companies and reported that the four main incentives for Saudi managers to manage earnings are to increase the amount of remuneration to report a reasonable profit and avoid loss, to obtain a bank loan and to increase share price. Al-Thuneibat et al. (2016) reported that the effect of corporate governance on earnings management is statistically insignificant. They concluded that there is a big question mark on the effectiveness of corporate governance in Saudi Arabia. They also revealed that there is a high degree of compliance with corporate governance requirements, but there is no

significant effect on earnings management. In the same context, Alshetwi (2016) found that audit committee members' multiple directorships have statistically insignificant relationship in reduction the level of earnings management in 98 Saudi nonfinancial listed companies. However, Habbash (2019) found that board size and independence are negatively associated with earnings management at significant levels. In the same line, Baatour et al. (2017) provided evidence that earnings management practices increase with the number of multiple directorships. They stated that multiple directorships have a positive and significant effect on real earnings management in the Kingdom of Saudi Arabia. However, they found no significant impact of multiple directorships on accrual-based earnings management. Alsultan (2017) concluded that Big 4 firms have a role in curbing earnings management only in income-decreasing activities. However, Habbash and Alghamdi(2016) indicated that only auditor opinion indicates earnings management practice, they advocate that auditors are powerless in front of managerial opportunistic activities.

Riadh (2021) attempted to examine the relationship between corporate social responsibility (CSR) disclosure and earnings management practices in the context of Saudi Arabia after mandatory IFRS adoption. It is carried out on an unbalanced panel of 277 observations over the period 2017–2019. For this purpose, CSR disclosure is measured by Bloomberg ESG scores, while the residuals from the modified Jones model are considered for earnings management. As control variables, we have retained the firm performance, market-to book ratio, firm size, financial leverage, board independence, ownership concentration, managerial ownership, and lagged discretionary accruals. Using the system GMM estimator in the dynamic panel, the results show a positive association between CSR disclosure and earnings management practices, thus supporting the perspective of agency theory. Managers engage in socially responsible activities beforehand to conceal their wrongdoing and convince stakeholders that the organization is transparent. They probably use ethical codes as a tool to achieve their own goals rather than the firm's goals. Our contribution is the use of recent data (2017–2019) taking into account the mandatory adoption of IFRS in Saudi Arabia. Additionally, this study is one of the first studies to address CSR disclosure and earnings management practices using GMM system estimates.

Alsuhaibani (2012) expected the impacts of the IFRS on Saudi businesses with a particular emphasis on the telecommunication business. He predicted that the role of the Saudi Organization for Certified Public Accountants (SOCPA) would be impacted by IFRS. He is expected that SOCPA after the adoption of IFRS will act as a facilitator and trainer. The Saudi

SOCPA exam should be redesigned. The curriculum of accounting programs in Saudi Universities should be revised accordingly. In addition, he is expected that the adoption of IFRS would have some negative impact, especially in the short term. This impact includes the cost of migration to the IFRS, consultation, redesigning the IT systems, retraining of accountants and auditors, and raising awareness among all stakeholders. Another cost element is the need to adjust earlier financial reports based on IFRS in order for decision-makers to compare the current year's financial reports with those of previous years. These officials believe that these costs are justified by the positive outcomes of the adoption.

Hashed and Almaqtarib (2021) assessed the influence of corporate governance mechanisms and IFRS adoption on compliance with IFRS, earning management, and financial reporting quality (FRQ). A sample comprises 102 Saudi listed firms for the period spanning from 2014 up to 2019 was used. The study used descriptive statistics, correlation analysis and multivariate analysis to estimate the results. The results reveal that while board size, board meeting and foreign ownership had negative effects on compliance with IFRS, board and audit committee independence exhibited a positive effect. Further, the results demonstrate that there was a sign of earning management under IFRS when a performance magnitude was used. The results also indicate that board and audit committee size, audit committee meeting, and managerial ownership had significant negative effects on financial reporting quality however, board and audit committee independence showed a significant positive effect. Importantly, the results found that financial reports quality (FRQ) under IFRS was better than Saudi GAAP.

The researchers concluded that increased foreign direct investment and enhanced quality reporting, transparency, and comparability are key benefits the country will enjoy from adopting IFRS.

### **1.2 Statement of the Problem:**

The countries enjoy a number of benefits from adopting IFRS like the quality of reporting, transparency, and comparability. The standards and laws governing the accounting profession require public joint stock companies to announce their financial results in accordance with the requirements of International Financial Reporting Standards (IFRS) and generally accepted principles approved in the country.

“Saudi Organization for Certified Public Accountants (SOCPA)” is the body responsible for developing accounting standards in Saudi Arabia. SOCPA has released a project in 2013 to shift to IFRS. SOCPA has approved a plan by which listed firms other than financial institutions would be mandated to follow SOCPA's new standards, which will be IFRS with some modifications. SOCPA approved an IFRS convergence Plan, called the “SOCPA Project

for Transition to International Accounting & Auditing Standards”. Under this plan, financial institutions are required to comply with IFRS as per SAMA requirements. All listed firms are required to comply with IFRS beginning in 2017, and other remaining firms are mandated to comply with IFRS by 2018. IFRS in Saudi Arabia are similar to the standards issued by the IASB with possible modifications in three respects: adding more disclosure requirements, removing optional treatments; and amending the requirements that contradict Shariah or local law, taking into consideration the level of technical and professional preparedness in the Kingdom” [Hashed and Almaqtarib (2021)].

Since 2017 all Saudi companies listed on the financial market (Tadawul) are required to adopt IFRS, this may prevent these companies from falling in earning management practices and conversely may enhance their market value. The adoption of IFRS performs important improvements to financial reporting considering its quality. Moreover, the implementation of the new accounting standards upon financial reports can influence the confidence that shareholders have in these reports and conversely the market value of listed firms.

The current study examines the effect of adopting international financial reporting standards by Saudi-listed companies on earning management and corresponding market value. The study compares earning management and market value of listed entities five years before and after the adoption of IFRS.

### **1.3 Questions of the Study:**

The purpose of this study is to detect if earning management and market value have increased or decreased in the five years after Saudi Arabia switched to IFRS compared with the five years before the adoption. This study searches for answers to the following questions:

1. Do the companies listed on the Saudi Arabia Stock Exchanges practice any type of earning management to influence the disclosed information?
2. Is there an effect of earning management on the market value of companies listed on the Saudi Arabia Stock Exchanges?
3. What is the impact of IFRS adoption on the earning management for the companies acting in Saudi Arabia’s financial market?
4. What is the impact of IFRS adoption on the market value of the companies acting in Saudi Arabia’s financial market ?

### **1.4 Objectives of the Study:**

The objective of this study is to investigate the impact of IFRS adoption on earning management and market value of Saudi listed companies. These objectives are:

1. Finding out the extent to which companies registered in the Saudi Stock Exchange practice earning management process to influence the published information.
2. The effectiveness of earnings management on market value of the companies listed on the Saudi Stock Exchange.
3. Knowing the impact of adopting international financial reporting standards (IFRS) on earning management for companies operating in the Saudi financial market.
4. Knowing the impact of adopting international financial reporting standards (IFRS) on the market value of companies operating in the Saudi financial market.

### **1.5 Importance of the Study:**

The practical significance of this study is the service it provides to policy-makers, stock market regulators, and academics. The research also makes a new contribution to IFRS compliance, earning management, financial reporting quality, and market capitalization literature. The unique contribution of this study is that it attempts to investigate this issue in the context of an emerging economy and newly adopted IFRS in Saudi Arabia, which has its own characteristics as a country. The study also provides evidence by investigating the earning management and the market value according to the two sets of accounting standards; IFRS and Saudi GAAP.

### **1.6 Variables and Hypotheses Development:**

The variables of this research are of three kinds:

#### **1.6.1 Independent Variable: IFRS Adoption:**

The International Financial Reporting Standards (IFRS) have been widely adopted by countries around the world, including Saudi Arabia. The adoption of IFRS is expected to improve the quality of financial reporting and increase comparability across companies. However, there are also concerns that IFRS adoption may lead to increased earning management and a decrease in market value.

In the Kingdom of Saudi Arabia, all listed firms are required to comply with IFRS beginning in 2017, and other remaining firms are mandated to comply with IFRS by 2018. This study tries to examine the relationship between the adoption of IFRS by Saudian companies and the market value of its stocks.

#### **1.6.2 Dependent Variable: the Market Value:**

The market value represents the price that the investor is willing to pay for the company's assets. It is measured by multiplying the closing price of the share at the end of the year by the number of shares traded (Cohen, et al., 2008).

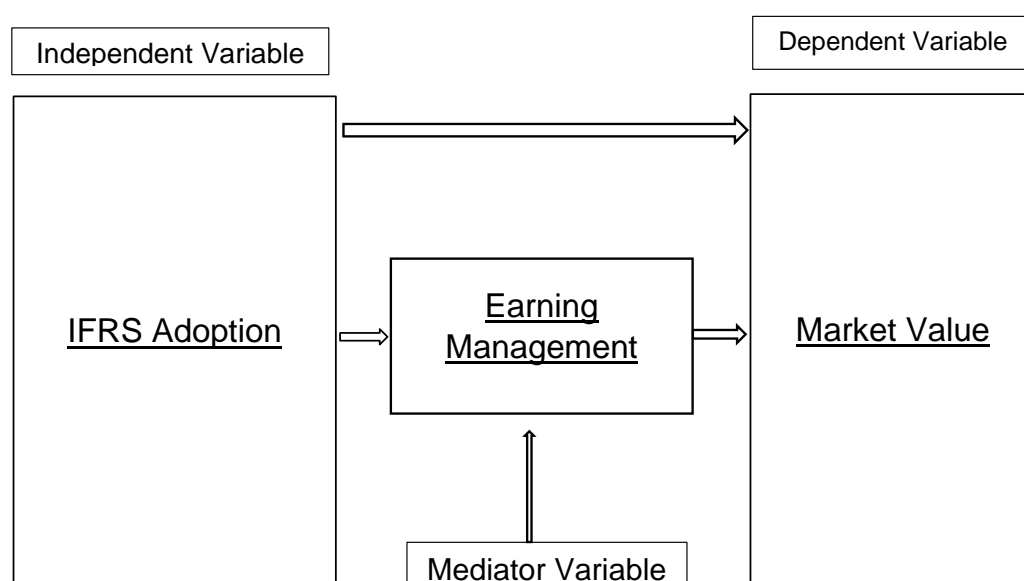
Furthermore, the market value considered as a measure of the efficiency of the company's performance in the financial market. It measures by dividing the closing price of the share at the end of the year by the book value of the share, as the book value of the share represents the equity divided by the number of subscribed shares.

### 1.6.3 Mediator Variable: Earning Management:

There is an agreement among the accountants that the profit of the economic units announced in the financial statements considers one of the most important information for all stakeholders, especially those dealing in the capital markets. Earnings management bases on adapting the accounting methods and estimates in order to influence the published profit numbers through the flexibility available in the use of various accounting policy alternatives such as the accounting policies alternatives related to depreciation. The emergence of earnings management came due to the wrong application of the principle of accrual, as the basis of accrual, according to the principle of matching, requires determining the timing of recognition of revenues, expenses, and expenditures.

The adoption of IFRS performs important improvements to financial reporting considering its quality. Moreover, the implementation of the new accounting standards upon financial reports can influence the confidence that shareholders have in these reports and conversely the market value of listed firms. This study mediates Earning Management (EM) in examining the relationship between IFRS adoption and the market value of companies listed on the Saudi stock exchange.

Relationship between the variables of the study:



## **1.7 Hypotheses Development:**

The previous studies investigated the relationship between IFRS adoption and earning management practices, while the current research contributes to the literature by providing further evidence on the association between IFRS adoption and earning management in the case of Saudi companies. It uses the modern dataset and extends the relationship in two ways: first by mediating earning management on association between IFRS adoption and market value as newly built relation. Second, test the direct relationship between IFRS adoption and the market value.

### **1.7.1 The relationship between IFRS adoption and Earning Management:**

The hypothesis investigates this relation is:

H1: Companies registered in the Saudi market do not exercise earnings management to influence published information.

H2: There is no significant relationship between applying international financial reporting standards (IFRS) and earning management for companies registered in the Saudi Stock Exchange.

### **1.7.2 The relationship between IFRS adoption and Market Value:**

The hypothesis investigates this relation is:

H1: There is no correlation between the adoption of international financial reporting standards (IFRS) and the market value of companies operating in the Saudi financial market.

H2: The market value of Saudi-listed companies in the five years following the adoption of IFRS did not differ compared with the previous five years.

## **2. Literature Review and the Previous Studies:**

### **2.1 IFRS Adoption: Concept and Background:**

According to Adhana (2020) defined International Financial Reporting Standards (IFRS) as set of uniform accounting standards which is used by the companies, accountants, auditors, investors, regulators & tax authorities etc. of different nations for preparing books of the accounts or Annual Financial Statements. In other words, IFRS is rules, which have uniform accounting language, followed worldwide. IFRS are widely recognized to produce information that is accurate, comprehensive, comparable, and available in a timely manner and serves the largest base of investors with the lowest possible risks. It is a set of general rules issued by a committee or a specialized body (IASB) that determines the accounting policies and treatments

for the economic unit's various transactions and financial events to provide reliable, objective, and comparable information (Hashed & Almaqtari, 2021). The importance of international standards in preparing financial reports while maintaining stability and transparency throughout the financial world. This allows companies and individual investors to make informed financial decisions because they are able to see exactly what is going on with the company in which they wish to invest (Alsuhaibani, 2012).

From the foregoing, it appears to the researcher, IFRS issued by a specialized professional committee (IASB) in order to standardize accounting practices between companies and different countries. IFRS aims to standardize entities' financial reporting through a single set of high-quality accounting standards as well as provide clear information with greater disclosure. It seeks to provide high-quality accounting standards that result in transparent, credible, and comparable accounting information.

Choi et al., (2013) concluded that the implementation of the IFRS leads to various benefits, both at the local and international level, as well as on the micro level (company) or the macro level (national economy). It increases the quality of accounting information by improving the quality of accounting disclosure, and the ability of investors to make a sound investment decision. It revitalizes the financial market by reducing the cost and nature of loans and attracting more financing institutions and foreign creditors and lenders.

Accordingly, the information contain in the financial statements prepared in accordance with the IFRS is of good quality and suitable to be used in managerial decisions, which will have a positive impact on market value and raise the level of performance.

Despite the forgoing benefits of applying the IFRS, Adhana (2020) noted a number of obstacles or challenges facing a country when applying these standards: lack of guidelines, increased costs of its implementation, confusion or ambiguity in understanding some standards, which leads to difficulties in applying them, and the stickiness of investors and users of financial statements to application of local standards and unwillingness to change to apply international financial reporting standards.

Since 2017 all Saudi companies listed on the financial market (Tadawul) are required to adopt IFRS, this may prevent these companies from falling in earning management practices and conversely may enhance their market value. IFRS in Saudi Arabia are similar to the standards issued by the IASB with possible modifications in three respects: adding more disclosure requirements, removing discretionary treatments; and amending the requirements

that contradict Shariah or local law, taking into consideration the level of technical and professional preparedness in the Kingdom” [Hashed and Almaqtarib (2021)].

It is important to recognize that the change in the Saudi Accounting Standards during the second phase was not an ordinary change. Rather, it was a convergence change with International Financial Reporting Standards. IFRS is generally regarded as more market-friendly and is considered more informative than mandatory GAAP because it requires better disclosures. The benefits of mandatory IFRS adoption for developing financial markets have significant production impacts in terms of improved reporting quality. In the context of Saudi Arabia, mandatory IFRS and convergence from Saudi Accounting Standards have unique impacts on both accounting quality and market efficiency that are different from non-regulation adoption countries. Thus, this paper empirically investigates the impacts of such a convergence switch on earnings management and market value in Saudi Arabia for the period of 2012 to 2022.

## **2.2 Earnings Management: Definition and Techniques:**

Earnings management has taken multiple definitions, so there is no single definition for it. According to (Healy & Wahlen, 1999), earning management occurs when managers use their judgments in financial reports and in organizing transactions for misleading stakeholders about the true financial performance of the company or to influence contractual decisions that depend on reported accounting information. It also, may occurs as a result of the desire of the preparers of the financial statements to bring about continuous improvement in the operational performance, to increase the financial statements continuously, and to bring about long-term growth in the value of the company. It may appears because of the existence of some incentives among managers, such as incentives for long-term contracts, bonus contracts, organizational motives, and capital market motives.

The researcher believes that earnings management is the legal and illegal actions and practices used by management when preparing financial reports, with the aim of affecting profits.

The application of IFRS comes to limit earning management by reducing the use of some accounting alternatives or accounting options in front of management, and thus reducing opportunistic opportunities (Barth et al., 2008), improving accounting disclosure, increasing the transparency of financial reports, attracting and diversifying investors, and increasing comparability (Ball et al., 2012), which leads to an increase in the quality of financial reports, and the appropriateness of accounting information for the investment decisions that are taken.

Strakova, (2021) stated three motives for earnings management, first; Contract motives: this appears when accounting data is used as a basis for reliance on them in organizing some contractual relations with others, such as lending contracts. Secondly, motives related to the firm's position in the financial market: There is no doubt that the accounting information of the financial statements published for the establishments in the financial market constitutes an important and useful source for investors and analysts to rely on in making their decisions. This creates an incentive for managers to manipulate profits in an attempt to influence the evaluation of the share price in line with the expectations of these analysts. Thirdly, organizational motives: These motives are related to what the management may do in terms of profit manipulation or circumvention of decisions or regulatory controls issued by some official and supervisory bodies regulating performance with this arrangement; This may prompt some managers to positively affect profits for the purpose of circumventing these systems and showing their establishment in a way that achieves the required financial solvency.

Furthermore, Strakova (2021) summarized the technique use in earning management; prefers most common method, accrual accounting procedures, income smoothing, and exaggerating the recognition of book losses.

The researcher thinks that there are multi ways to exercise earning management, some like: Changing the method of depreciation of fixed assets, changing the default life of fixed assets in the process of calculating their depreciation ratio, changing the percentage of scrap value estimation used in calculating the depreciation of fixed assets, changing the principles used in calculating the provision for doubtful accounts in relation to customer accounts and loans, changing the basis for calculating collateral liability provisions, and estimating the percentage of decline in the value of assets that occurred over time.

It is important to note that there is a plurality of opinions about whether earnings management is considered good or bad practices, and the saying here is due to what companies do during the process of managing their earnings. The researcher agrees that the earning management process, if the purpose is to mislead, deceive and cheat, then it is an unethical practice and the law must impose penalties on it.

The most popular model uses in measuring earning management is the modified Jones Model. This model developed by Dechow, et al. (1995) to Jones (1991) model to avoid any effect resulting from manipulation of revenues that lead to biased estimates in calculating non-discretionary accruals. The modified Jones model bases on three assumptions: First, all changes in deferred sales during the study period result from the earning management process. Second,

entering the volume of change in accounts receivable as a controlling factor for the level of non-discretionary accruals after deducting them from the volume of change in the company's revenues. Third, the change in property and equipment represents a controlling factor for the level of depreciation of assets.

### 2.3 Market Value: Measurement and Importance:

The Cambridge Dictionary defines the market value as “the price at which something can be sold, at a particular time in a particular place”

(<https://dictionary.cambridge.org/dictionary/english/market-value>).

The market value can be regard as the value of the company or the assets it owns based on the evaluation of the financial market, and this is often does by multiplying the company's share price offered for trading by the number of shares of the company that treated in the stock market.

The market value can be measuring in the forms of mathematical ratios that give the management insight into what the company’s investors think of the company, both at present and in the future. These measures are:

- Earnings per Share (EPS): allocating a portion of a company’s profit to every individual share of stock. A higher EPS denotes higher profitability.
- Book Value per Share: dividing the company’s equity by the total number of outstanding shares.
- Market Value per Share: considering the market value of a company divided by the total number of outstanding shares.
- Market/Book Ratio: compares a company’s market value to its book value. It calculate by dividing the market value per share by the book value per share.
- Price-Earnings (P/E) Ratio: The P/E ratio is the current price of the stock divided by the earnings per share.

### 2.4 The Gaps in Literature:

construct	Prior accomplishments	Literature gap	Potential contribution
Daske & Gebhardt (2006) - Byard et al. (2010) - Hellman (2011) - Alghamdi (2012) - Habbash &	Motives and reasons behind the practice of earnings management	The relationship between IFRS adoption and Market Value	providing further evidence on the association between IFRS adoption and (MV)

Alghamdi (2015).			
Alshetwi (2016) - Alsuhaiyani (2012)	The methods adopted by the different firms to practice earnings management	Relation between earning management and market value	providing additional evidence on the relation between market value and earnings management practices in the context of developing country; namely Saudi Arabia after mandatory IFRS adoption.
Habbash & Alghamdi (2016) - Alsultan (2017)).	The accounting and statistical methods and models used to detect the earnings management practices	Submitting valuable findings to the listed companies in developing countries.	Improving accounting reports quality in Kingdom of Saudi Arabia can create value for the companies.
Daske (2006) - DeFond (2011) - Baatour et al. (2017) - Habbash (2019) – Bokhuwa & Obied (2020) - Hashed & Almaqtarib (2021)	The impact of applying IFRS on earnings management practice	Using mediators in examining the impact of IFRS adoption.	Mediating Earning Management the relation between IFRS adoption and Market Value.

**Source: designed by the researchers from the literature review (2024)**

### 3. Methodological Framework:

This study attempts to examine the impact of International Financial Reporting Standards (IFRS) adoption on earnings management and market values of Saudi companies listed on the Saudi Stock Exchange (Tadawul). The study used descriptive statistics, correlation analysis, and comparative analysis of sampled companies five years before IFRS adoption and five years after (2012 up to 2022) to estimate the results.

The study population is non-financial companies listed on the Saudi stock exchange market. A sample of 188 companies was selected from 270 non-financial listed companies, representing 70%. The companies selected in studied sample are those:

- The company must be listed on the Saudi Stock Exchange during the study period (2012 - 2022).
- The company must continue to operate during this period.
- It must not be merged or suspended from issuing during the period of study.
- It must have all the necessary data to measure the study variables.

The annual financial statements of these companies were obtained based on the financial information and ratios that are calculated annually and published on the Saudi Stock Exchange website.

In light of the methodologies used in previous studies to measure or study the relationship between the adoption of international financial reporting standards and the company's market value and measuring earnings management, and in light of the objectives of the study, a model was developed for this study that explains the relationship between the adoption of international standards and the company's value by mediating earnings management.

for which the financial statements are available. Also, the data of these companies is relatively more completed than others. The study covers the years 2012-2022, which consists of some years before the IFRS adoption, the year of IFRS adoption, and some years after the IFRS adoption for the comparison sake.

Earning management measured by using a modified version of the Jones model, which is widely used in the literature. Market value will be measured using market capitalization. The study will use statistical techniques to analyze the data and test for any significant differences between the groups of companies. The raw data is mainly from the data provided by a company that provides detailed and general company information for all Saudi non-financial stock exchange listed companies. Another source based on the financial statements of these companies, that found in different databases or the company's official websites. Further, the study segregates non-financial companies into three segments: high market value companies and low market value companies. The rule is segregated with the lowest 33.33% of the market value of all non-financial companies in Saudi Arabia. The rule for high market value companies is companies above the 66.6 percent level of the market value of all traces. The analysis includes

all non-financial listed companies for which financial statement information is reported in the respective period of interest.

#### **4. Empirical Analysis and Results:**

Data for Saudi non-financial companies are obtained for the period 2012-2022. The year 2014 is the year when, for the first time, the Ministry of Commerce in Saudi Arabia requested all Saudi companies to prepare their financial statements as per International Financial Reporting Standards. As of 2016, all Saudi companies except the listed banking sector were required to prepare financial statements as per IFRS. To examine the impact of IFRS, the sample consists of non-financial companies, as the regulatory reporting requirements for banks are significantly different.

For the earnings management analysis, this study calculates discretionary levels; the reference model uses residual income calculated following and accrual levels following. Then, discretionary core earnings are forecasted as opposed to the actual value of the operating results. The paper utilizes a log-linear model with firm and score effects to estimate genuine and discretionary components of residual income, total assets, and cost of equity capital. The sample consists of 188 company-year observations with financial data available for the non-financial company-year observations. Market valuation analysis, profitability, and investment measures are used to perform the hypotheses testing, and revenues performed sample selection estimates and accounting estimates of market value to test the study hypotheses. The paper adds other important variables to recognize the parent's role in detecting significant changes due to IFRS adoption. The study tested the Multiple test to detect differences between early and late IFRS adopters.

Management can use the discretion available in the accounting standards to manage reported earnings. Earnings management aims to satisfy a broad range of objectives, including a market-oriented approach. Companies take advantage of the discretion granted to them under accounting principles to manipulate accounting figures to achieve malicious purposes such as manipulating stock prices and producing overstated figures for their performance in a market where poor performance may result in takeovers, mergers, collapse, and a decline in stock price. Earnings management refers to one of two different types of behavior as a result of unwelcome noise, not to the deliberate use of judgments and estimates that are better than judgment. Companies have some room to manage earnings before adopting any formal standards. Also,

formal standards give more room for managers to manage earnings and demonstrate in some studies that companies tend to manage earnings using formal standards that are less predictable.

Based on evidence from companies in the market, it was shown that firms increased when the company had a large stock market. Earnings management leads companies to use standards to facilitate accounting statement manipulations. Also, certain standards are found to provide managers with the most discretion. Companies are likely to be firms using local standards. Data detects that contracts with companies because standards are vague and lack important issues. Agency mimicking also suggests that users will manage earnings and will imitate managers who have adopted the classification analyst. Based on the failed studies of the standard associated with earnings management and the failed debates, there are still contradictory results concerning the relationship between accounting rules and the level of earnings management.

#### **4.1 Comparison of Earning Management Before and After IFRS Adoption:**

The results showed that discretionary accruals decreased after IFRS adoption due to statistically significant values. This result is consistent with a multitude of studies that were conducted in various contexts of emerging economies. It reflects the accounting standard setters' rhetoric and the main motivation for adopting IFRS, which is to improve the transparency and the quality of financial reporting and reduce earnings management approaches.

The result implies that IFRS have created an environment that mitigates earnings management practices in favor of better quality of performance. It also supports the prediction of the accrual model that earnings management incentives are stronger under local accounting standards than under IFRS, acting as a moderator for reducing earnings management among global companies. Furthermore, these results deny the concerns that had been raised by some market participants suggesting that IFRS would lead to increased earnings management. They confirm that the introduction of cross-border reporting standards likely prompts improved earnings quality, all else being equal, by limiting efforts to use accruals to mislead constituents.

**Table (1): EM before and after IFRS adoption**

Period	Independent variables	Dependent Variable	Co-relation R	R <sup>2</sup>	B	t-test	p-value	F	p-value
Before Adoption	Local Standards	EM	0.659	0.655	0.975	4.323	0.000	18.604	0.000
After Adoption	IFRS	EM	0.18	0.032	0.497	2.252	0.001	2.063	0.000

Source: Calculated by researchers according to field data (2024).

The adoption of International Financial Reporting Standards (IFRS) by Saudi listed companies has significantly influenced the practices of earning management, leading to observable changes in financial reporting behaviors before and after its implementation.

#### 4.2 Impact of IFRS Adoption on Market Value:

The adoption of International Financial Reporting Standards (IFRS) has significantly influenced the market value of Saudi listed companies, as it enhances transparency and comparability in financial reporting.

**Table (2): co-relation between IFRS adoption and market value**

Co-relation R			0.565		
R <sup>2</sup>			0.319		
Adjusted R <sup>2</sup>			0.299		
F			15.328		
Variable	$\beta$	Std. Error	Beta	t	Sig. t
Constant	0.097	0.937		0.104	0.918
IFRS Adoption	0.819	0.126	0.566	6.524	0.000

Source: Calculated by researchers according to field data (2024).

The adoption of International Financial Reporting Standards (IFRS) has significantly influenced the market value of Saudi listed companies between 2012 and 2022, revealing critical insights into the relationship between financial reporting practices and investor perceptions.

The analysis of trends in market value for Saudi listed companies from 2012 to 2022 reveals significant fluctuations influenced by various economic factors, regulatory changes, and global market dynamics.

The total market value of Saudi companies listed on the stock exchange during the period 2012-2022 ranged from a minimum of 201.16 billion riyals in 2012 to a maximum of 1.786 trillion in 2014. In the last year of the study, from 2018 to 2022, the value of market capitalization exceeded one trillion riyals, and the market value of Saudi listed companies decreased in both of the two years at the end of the research. The calculated averages of the total amount in two different cases of using the average of each of the minimum, the maximum, and the amount of market value of Saudi listed companies ranged from 841.785 billion riyals for the total amount of the average of market value of Saudi listed companies, using successively from 2016-2022, riyals 3.564, 5.252, and 6.389 trillion for the averages of the maximum, the minimum, and the values of market value of Saudi joint stock companies.

**Table (3): Trend in Market Value during (2012-2022)**

Variable	N	Mean	Std. Deviation	Minimum (Billion SAR)	Maximum (Billion SAR)
Market Value	188	841.785	0.953	201.16	1,786
Market Value	Top 50	517.753	0.244	222.770	812.735

**Source: Calculated by researchers according to field data (2024).**

Concerning the calculation of 50 companies with the highest market values, the market value ranged between 222.770 billion riyals in 2012 and 812.735 billion corresponding to the year 2014. The trend of the largest market value of the Saudi 50 companies differs from the trend of total market value, as the trend of the market value of the 50 largest companies in the stock exchange moved upwards over the years of the study in general, which reflects the stability and strength of the market, while the total market value's general trend tended to fluctuate. During the last two years of the research, which are 2021-2022, the market value of the 50 largest companies in the stock exchange decreased, and in 2022, the market value increased compared to 2021, taking the market value of Saudi listed companies to approximately one trillion riyals.

#### **4.3 Factors Influencing Market Value:**

The market value of funds listed in the Saudi financial market is influenced by many factors. Considering these variables in the model could increase the percentage of variations resulting from the independent variables. Therefore, the numbers from previous studies are used to determine the possible variables to derive our suggestions. These factors can be classified as internal, external, and foreign companies. The suggested model could be:  $M.V = F$  (profits, dividends, stability, efficiency of business management, current assets, free market, type of business, quality of real estate, foreign investments in the Kingdom, restricted zones for the adoption of contributions, quality, and disclosure of financial reports, corporate governance, and some services such as trial, audit, and legal advisory offered.

#### **5. Discussion and Implications:**

The analysis of the results reveals significant trends regarding the relationship between IFRS adoption and both earnings management practices and market value among Saudi listed companies during the period from 2012 to 2022.

The analysis of the impact of IFRS adoption on earning management and market value among Saudi listed companies from 2012 to 2022 reveals significant trends and implications for financial reporting practices.

The study is expected to provide insights into the impact of IFRS adoption on earning management and market value of Saudi listed companies. The results of the study will contribute to the literature on IFRS adoption and its impact on financial reporting and market value.

The research results show that Saudi Arabia also becomes increasingly market-oriented, as recognized or measured. The earnings management based on IFRS is less concerning. Discretionary accruals significantly decreased after the adoption of IFRS. The research results meaningfully illuminate the broader economic implications of increasing the convergence of accounting measurement and recognition principles.

The researcher expects some solutions for these challenges, some like; Stakeholders should put in place adequate resources to support the sustainable implementation of IFRS, qualifications be needed to local accountants to be aware of IFRS, and additional disclosure requirements have to be added to some standards, mainly to reflect Sharia' or local laws.

## 6. Conclusion and Future Research Directions:

**Recommendations for Future Research:** Few areas of potential future research were noticed during the research process. These include:

a. Longitudinal studies that compare earnings management and market value before, during, and after IFRS adoption to show a complete picture of the short- and long-term impacts of IFRS in Saudi Arabia. To the best of the researcher's knowledge, most of the previous studies had a one-year period of adoption.

b. Since it was evidenced earlier that IFRS changes the way of fair value accounting, the research suggests investigating the change in the level and the quality of earnings management after the adoption. This can be achieved by breaking down earnings using a specific model. Earnings can be proxied by actual accruals and changes in the actual accruals that relate to the three components of earnings, which are investment, financing, and operations, before and after the adoption.

Future research on the impact of IFRS adoption should explore various dimensions, such as the long-term effects on earnings management practices and market valuations in different sectors beyond those currently studied.

To further advance the understanding of the implications of IFRS adoption on earnings management and market value, future research should explore various dimensions such as industry-specific impacts, regional variances in implementation, and the role of corporate governance mechanisms.

Future research on the impact of IFRS adoption should explore various dimensions such as the long-term effects on earning management practices, the influence on different sectors within the Saudi market, and potential regional comparisons to better understand the overall implications on market value.

Future research on the impact of IFRS adoption on earnings management and market value should explore several key areas to enhance understanding and provide deeper insights.

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