ERASMUS SCHOOL OF ECONOMICS
ACCOUNTING, AUDITING AND CONTROL

Master thesis:

Conservatism and value relevance

The relationship between conditional conservatism and value relevance of earnings

Student: Fouad Akhloufi

Student number: 323152

Supervisor: Mr. C. van der Spek RA

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FEM 11032 MASTER'S THESIS ACCOUNTING, AUDITING AND CONTROL

THE RELATIONSHIP BETWEEN CONDITIONAL CONSERVATISM AND VALUE RELEVANCE OF EARNINGS

Abstract

The purpose of this study is to examine the relationship between conditional conservatism and value relevance of earnings in the post-IFRS time period. Two countries, France and Germany, have been examined in this master thesis. Value relevance of earnings has increased in France, but not in Germany, after the introduction of IFRS when regressing returns on earnings per share. However, when using a regression of stock prices on earnings per share, both countries show an increase in value relevance of earnings after the introduction of IFRS. Conditional conservatism has declined in the post-IFRS time period in France but not in Germany. The results reveal that there is a negative relationship between conditional conservatism and value relevance of earnings in Germany in the post-IFRS time period. This does not seem to be the case in France. However, the results should be interpreted with care due to the small sample size.

Student: Fouad Akhloufi

Student number: 323152

Email address: fouad_151@hotmail.com

Supervisor: Mr. C. van der Spek RA

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Preface

The master thesis that is lying in front of you is the conclusion of my Master program Accounting, Auditing and Control at the Erasmus University in Rotterdam. It is the end of a very instructive and pleasant studentship.

The writing of this master thesis has gone through ups and downs. However, the process has been eased due to the help of some people. First of all, I would like to thank my supervisor Mr. Cor van der Spek RA. His advice during the process and his critical comments really added value to this master thesis. Without him, this master thesis would not have had the scientific foundation it has now. I would also like to thank him for always responding very quickly and clearly to my questions.

Furthermore I would like to say a word of thanks to the data team of the Erasmus University who have helped me find the data I needed. They were an essential link in completing this master thesis.

Lastly, I would like to thank my parents. Even though they do not have the knowledge to help me with the content of this master thesis, they did contribute to this thesis with their motivational support.

Fouad Akhloufi
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Introduction

The purpose of financial reporting is to give useful information to investors and other stakeholders that they can use in making decisions. To achieve this objective, the financial statements should provide a true and fair view. The financial statements should give a fair view of the result that has been achieved in the financial year and the financial position of the entity. The financial position should not be presented too optimistic nor too pessimistic. However, the use of conservatism undermines the true and fair view of the financial statements. Conservatism can be seen as accountants' tendency to require a higher degree of verification when recognizing good news in comparison with recognizing bad news (Basu 1997). For example, unrealized losses are usually recognized faster in the profit and loss account than unrealized gains. This causes a distortion. Basu (1997) found that earnings respond much more to bad news than to good news. This was proof that conservatism really exists. The use of conservatism could also influence the value relevance of earnings. Value relevance means that accounting information needs to be useful for stakeholders. This master thesis aims to examine the relationship between conditional conservatism and value relevance of earnings. It builds further on the research performed by Balachandran and Mohanram (2011). They empirically examined whether conservatism is the cause of the decline in value relevance in the United States by forming different groups based on their level of conservatism.

This thesis will start with formulating the research question. This will be done in chapter 1. To answer the research question we will first have to know what conservatism and value relevance really mean and how they can be measured. This will be done in chapter 2. Chapter 3 will be a literature review. This chapter will be divided into 3 subcomponents. Chapter 4 will be used to compose hypotheses. These hypotheses will have the same structure as the hypotheses that are used in the paper of Balachandran and Mohanram (2011). The research design will be explained in chapter 5. Models that will be used for the empirical research will be presented and explained in detail. The results will be exposed and explanation about how to interpret these results will be given in chapter 6. In chapter 7 the conclusion will be drawn. Furthermore, opportunities for future research will be given.

Chapter 1: Research question

1.1 Introduction

This chapter will present the research question. Before the research question is presented, explanation about value relevance and why conservatism is used will be given. Furthermore, the two different forms of conservatism will be explained. Subsequently, the relevance and methodology of this thesis are elaborated and finally the research question will be presented.

1.2 Value relevance

Value relevance has been the subject of many research papers since the paper of Ball and Brown (1968). Ball and Brown concluded that firms with earnings increases show abnormal positive returns. The opposite holds for earnings decreases. Nichols and Wahlen (2004) have also examined the value relevance of accounting numbers. They show that not only the sign is important (positive or negative) but also the magnitude of the earnings increase or decrease. They also examined the relationship between annual changes in cash flows from operations and annual stock returns. This relationship appeared to be significant but weaker than the earnings-returns relation.

Prior literature has also shown that value relevance of accounting information has declined over time in the United States. Lev and Zarowin (1999), Francis and Schipper (1999) and Core et al. (2003) all come to this conclusion.

This master thesis will focus only on the value relevance of earnings. Earnings are the most important number of the financial statements (Nichols and Wahlen (2004)). It represents the bottom line accounting measure of firm performance. Shareholders use current earnings to forecast the future value of a firm. Possible future earnings are predicted on the basis of current earnings. Subsequently, shareholders use these expectations about possible future earnings to come up with expectations about future dividends. These future dividends form the basis of current share value. This earnings-dividends-value link shows the major importance of the earnings number to shareholders (Beaver 1998).

1.3 Reasons for conservatism

Even though conservatism causes a distortion, there are several reasons for the use of conservatism (Watts 2003). The first explanation is the so called contracting explanation. Management has more information about the company than the stakeholders. This means that information asymmetry exists. There is a risk that management will overstate profits so that they will earn a higher bonus. Use of conservatism diminishes that risk. Not only does conservatism reduces that risk, it also increases firm value. Since conservatism restraints the opportunistic payments of management to themselves and shareholders there is more firm value that can be shared among all stakeholders. Shareholder litigation is the second explanation for the use of conservatism. Shareholders are more likely to sue a firm when the profits and net assets are overstated than when they are understated. Because of this, management has an incentive to be conservative when reporting values for profits and net assets. Thirdly, tax reasons also play a role in using conservatism. Firms desire a taxable income that is as low as possible so that tax payments are reduced to a minimum. Losses are faster recognized than profits under conservatism. This leads to a delay in the recognition of revenues and an acceleration in the recognition of costs. Ultimately this leads to a postponement of tax payments. The fourth explanation has to do with standard setters and regulators. Standard setters are more criticized when firms overstate net assets than when they are understated. To make sure that they are not faced by political criticism and interference, they develop conservative accounting standards. Conservatism thus helps to reduce political costs.

1.4 Forms of conservatism

There are two different forms of conservatism (Beaver and Ryan 2005). The first one is conditional conservatism. Conditional conservatism is ex post or news dependent. This means that book values are written down when the circumstances ask for it, for example when the value of a building goes down. On the other hand however, book values are not written up in favorable circumstances. This causes the conservative behavior.
The second form of conservatism is unconditional conservatism. This form is ex ante or news independent. This means that the accounting process itself is conservative. More specifically,

aspects of the accounting process determined at the first recognition of assets and liabilities lead to unrecorded goodwill. For example, the immediate expensing of internally developed intangible assets and the use of historical cost accounting. As a consequence, assets are understated and costs are taken immediately.

1.5 Relationship between conservatism and value relevance

More interesting is the relationship between conservatism and the value relevance of earnings. This subject has not been examined frequently in the past. Lev and Zarowin (1999) find in their paper that firms with increasing R&D, which means more unconditional conservatism, show a greater decline in value relevance. However, they do not use a comprehensive measure for conservatism in their paper. On the other hand, Francis and Schipper (1999) conclude that firms that are active in high technology industries do not display a greater decline in value relevance than firms in other industries. Just like Lev and Zarowin (1999) they do not use a comprehensive measure for conservatism. Lev and Zarowin only focus on a specific business activity (R&D) whereas Francis and Schipper (1999) only focus on a specific industry (high technology). This means that it is impossible to draw conclusions about the relationship between conservatism and value relevance.

Balachandran and Mohanram (2011) are the first that empirically tested whether accounting conservatism is responsible for the decline in value relevance in the United States. By making use of comprehensive measures (Beaver and Ryan approach (BR-CONS) and Penman and Zhang approach (C-SCORE)) and by focusing on both level and growth in conservatism they come to the conclusion that unconditional conservatism is not responsible for the decline in value relevance.

Their research only takes companies into account that are active in the United States. This master thesis will discuss the relationship between conditional conservatism and value relevance of earnings in a European setting. A European setting is particularly interesting to investigate because public firms in the European Union are obliged to report their consolidated financial statements according the standards of International Financial Reporting Standards (IFRS) since

the year 2005. IFRS is introduced so that financial statements of companies are more understandable and comparable across different countries. The use of fair value increases under IFRS. This could have a major impact on the level of conservatism. It is most likely that the level of conservatism will decrease under IFRS. Fair value demands symmetric timeliness of earnings. Both losses and benefits are recognized at the same time. Recognition of good news is not postponed. Fair value accounting leads to more recognition of unrealized gains which in turn leads to less conservatism.

1.6 Relevance

This master thesis is especially relevant for standard setters since it examines whether conditional accounting conservatism enhances or deteriorates value relevance of earnings. If the value relevance of earnings is indeed affected negatively by the level and growth of conditional conservatism, standard setters should consider making less conservative accounting standards in the future. On the other hand, when it turns out that value relevance of earnings is not affected negatively by conditional conservatism, this master thesis gives no reason to make less conservative accounting standards.

1.7 Methodology

Somewhat the same models that are applied in the Balachandran and Mohanram paper (2011) will also be applied in this master thesis. However, there are some important differences. First of all, Balachandran and Mohanram (2011) use unconditional measures of conservatism such as BR-CONS and the C-SCORE. This master thesis only focuses on conditional conservatism. Therefore the Basu (1997) measure and the AACF measure are applied. Only conditional conservatism is examined because literature shows (Andre and Filip 2012) that this type of conservatism has declined after the introduction of IFRS. Secondly, there was no change of accounting system in the time frame that Balachandran and Mohanram (2011) have studied. US GAAP was the applicable accounting standard during the entire period of time. This master thesis explicitly looks at two different periods, namely pre-IFRS and post-IFRS. Thirdly, the time frame that will be used in this master thesis will be much shorter than the time frame used in Balachandran and Mohanram (2011). They use a time frame of 30 years. The time frame used

in this thesis is much shorter so that the time period pre-IFRS and post-IFRS are approximately the same.

Just like in Balachandran and Mohanram (2011), groups will be formed. These groups are based on the level of conservatism. The model of Easton and Harris (1991) will be used to measure value relevance of earnings.

1.8 Research question

The following research question will be answered in this master thesis:

What is the relation between conditional conservatism and value relevance of earnings?

1.9 Conclusion

There are different reasons for the use of conservatism. The four most important are: the contracting explanation, shareholder litigation, tax reasons and standard setters and regulators reasons. A clear distinction needs to be made between conditional and unconditional conservatism. The focus of this master thesis is primarily on conditional conservatism. This master thesis is especially relevant for standard setters since it provides insight in whether conditional conservatism deteriorates value relevance of earnings. The methodology that will be used is somewhat the same as the methodology of Balachandran and Mohanram (2011).

Chapter 2: Concepts and measures

2.1 Introduction

This chapter will go deeper into the concepts and measures of conservatism and value relevance. First of all, the development of conservatism throughout the years will be presented. Reasons for conservatism will be explained in detail and measures for conditional and unconditional conservatism will be shown. After that, two different value relevance of earnings measures will be explained.

2.2 Conservatism in the early years

Traditionally conservatism has been explained as "anticipate no profits, but anticipate all losses" (Bliss, 1924). The criticism on conservatism already existed in 1939. Gilman says in his article:

"Conservatism has a tendency which is opposed to the ideal of matching costs with income. Ruled by the doctrine of conservatism, the accountant declines to recognize income until such recognition is clearly warranted but, on the other hand, has a tendency to be generous in recognizing costs, expenses, and losses and including them in the profit and loss statement of one period even though there may be some doubt as to the fairness of such inclusion."

The most important objection against the use of conservatism is that present overstatement of expenses leads to overstatement of future income. The Financial Accounting Standards Board (FASB) also states in SFAC 2 (1980) that conservatism is inconsistent with qualitative characteristics of accounting such as neutrality, representational faithfulness and comparability.

There were also early advocates of conservatism. According to Wilcox and Hassler (1941), there is no conflict between conservatism, which calls for exclusion of doubtful assets and inclusion of liabilities, and consistency. They argue that this conflict disappears upon exploration of the field of business. Their field operation leads them to the conclusion that assets tend to escape and liabilities tend to adhere. To preserve assets and profits and to avoid liabilities and losses work needs to be done against this field of force. This means that less doubtful assets should be excluded in the financial statements or as Wilcox and Hassler say themselves:

"Consistent treatment in financial statements would include both assets and liabilities having a comparable degree of probability, and recognizing of the field of force shows that inclusion of all known liabilities and exclusion of doubtful assets accomplishes this. Understanding of the fundamental consistency in this application of conservatism will assist judgment in specific cases."

2.3 Breakthrough in conservatism literature

The early definition of conservatism seemed to be very broad and needed to be adapted and specified. The real breakthrough in the conservatism literature came with the article of Basu in 1997. Basu redefines conservatism as "capturing accountants´ tendency to require a higher degree of verification for recognizing good news than bad news in financial statements". In other words, there is an asymmetry in the recognition of earnings. Losses are more quickly recognized in the profit and loss account than revenues. Basu gives a clear example of this conservatism in his article. Consider that the economic lifetime of an asset changes. The economic lifetime increases with three years. This means that the depreciation costs that are left are spread over the remaining lifetime thereby reducing the annual depreciation costs and increasing the annual profit over the entire period with the same amount each year. Now consider a situation where the economic lifetime of the asset decreases with three years. In this situation, other than the situation where the lifetime increased, the accountant records an asset impairment which has a huge impact on current income but does not impact future profit. This example clearly shows that losses and gains are treated differently in the financial statements.

What is so special about the article of Basu is that he comes up with a measure of conservatism. He translates conservatism into financial economics terminology. To empirically test whether conservatism really exists, Basu uses returns to measure news. Negative returns represent bad news and positive returns represent good news. He uses a reverse earnings-returns regression to measure conservatism. The details of this measure will be explained later on. Basu concludes that conservatism is really present and that bad news is timelier recognized in the profit and loss account than good news. More specifically, earnings are two to six times more sensitive to negative returns than to positive returns. The other reason that the article of Basu is so influential

in conservatism literature is because he changed the worldview of conservatism. In the old worldview, conservatism was often seen as something negative that standard setters should exterminate. The new worldview, which emerged after Basu (1997), was that conservatism is used by firms to solve one or more problems. Researchers were now interested in finding out what problems were exactly unriddled by the use of conservatism and how the conceptual framework failed to solve these problems.

This is exactly what Watts (2003) did in his paper. He found different explanations for the use of conservatism as already mentioned in short in chapter 1 of this thesis. The first explanation is the contracting explanation. This contracting explanation means that conservatism is used because information asymmetry exists between different parties such as management and stakeholders. Management has more information about the firm than the stakeholders which creates a risk that they will overstate profits. Conservatism prevents this. To reduce agency costs, firms make use of contracts such as debt and management compensation contracts. Three characteristics of accounting measures are explained by contracting: timeliness, verifiability and asymmetrical verifiability. First of all, performance measures in contracts are more effective when they are timely. These measures should reflect the effects of the actions of the manager on firm value. This will encourage managers to do projects that have positive net present value but negative near-term earnings. They will still get rewarded for this project even if they leave the firm in the near future.
Accounting measures cannot always be verified easily and need to be estimated. Therefore, these estimates of accounting measures are not used in contracts. Only accounting measures that can be verified are used in contracts.
More verification is needed for gains than for losses because firms have asymmetric payoffs from the contracts. Creditors are only interested in receiving back their money with interest. They do not receive any additional money even if net assets are at a high level. On the other hand, when net assets are lower than the promised payments creditors receive less money back. Therefore they want to have an assurance that the minimum amount of net assets is bigger than the contracted sum.

Ahmed et al. (2001) examined whether the contracting explanation of conservatism played a role in practice. According to them, contracting reduces dividend policy conflicts. Ahmed et al.

(2001) predict that the greater the dividend conflicts are in a firm, the more conservative the firm will be. They use different proxies to measure the degree of dividend conflicts such as leverage and the ratio of dividends to assets. The conclusion from their paper is that conservatism increases when dividend conflicts increase. Holthausen and Watts (2001) find that conservatism also existed in the pre-litigation period (before 1967) which implies that the contracting mechanism plays a role in explaining conservatism. Ball et al. (2000) examined different countries. They divided the countries in two: common law countries and code law countries. In common law countries firms tend to resolve information asymmetry conflicts among parties with the use of contracts. Information asymmetry conflicts in code law countries are resolved within the firm and without the use of external contracts. Therefore they predict that the level of conservatism in common law countries is higher than in code law countries. This also appears to be the case. Another study of Ball et al. (2002) compared four Asian countries (that have some similarities with common law countries) with the common law countries of their study in 2000. These four Asian countries however had an important difference with the common law countries. There did not rely on contracts but on family and other insider networks when resolving information asymmetry conflicts. Ball et al. (2002) find a higher level of conservatism in the common law countries compared to the Asian countries which supports the contracting explanation.

The second explanation for conservatism is shareholder litigation. This is a relatively new phenomenon. Kothari et al. (1988) find that litigation was rare before 1966. Litigation occurs much more when profits are overstated compared to when they are understated which leads to conservative values for profits. There has been empirical evidence for the shareholder litigation explanation as well. Chung and Wynn (2008) find that there is a negative correlation between managerial legal liability coverage and conditional conservatism. Managerial legal liability coverage means that managers are in some way protected against shareholder litigation. To measure this they used two proxies: directors and officers liability insurance coverage and cash for indemnification. The negative association between managerial legal liability coverage and conditional conservatism implies that the more managers are protected against shareholder litigation the less conservative they are. Basu (1997) has also found evidence for the shareholder litigation explanation. He examined four different periods which are qualified previously by Kothari et al. (1988) as either a high or a low litigation growth period. An increase of

conservatism was found in the high litigation growth periods whereas no increase was found in the low litigation growth periods.

The third explanation is an income tax explanation. Firms want to report a taxable income that is as low as possible and therefore they report conservative values for profits. Shackelford and Shevlin (2001) find that the link between reported accounting income and taxable income provides an incentive to lower accounting income in order to reduce current taxes. Also an increase in taxes could lead to more conservative financial reporting.

The last explanation for conservatism is a regulatory explanation. Since standard setters and regulators do not want to get into the attention of politicians they come with conservative accounting standards. Overvalued assets and overstated income leads to much more attention from the politics than undervalued assets and understated income. This leads to conservative accounting standards.

2.4 Conditional vs. unconditional conservatism

A distinction needs to be made between conditional and unconditional conservatism. This distinction has been made by Beaver and Ryan (2005). Former researchers (Basu 1997, Ball et al. 2000 and Pae et al. 2004) used the terms income statement and balance sheet conservatism. Under conditional conservatism, book values are written down under unfavorable circumstances but are not written up under favorable circumstances. The latter causes the conservative behavior. Conditional conservatism is ex post or news dependent. An example of conservative behavior is impairment accounting for long-lived tangible and intangible assets. This type of conservatism is investigated by Basu (1997).

The definition of unconditional conservatism as stated by Beaver and Ryan (2005) is:

"First, conservatism can be unconditional (or *ex ante* or news independent), meaning that aspects of the accounting process determined at the inception of assets and liabilities yield expected unrecorded goodwill. "

Some examples of unconditional conservatism are the immediate expensing of internally developed intangible assets and accelerated depreciation. Accelerated depreciation means that

assets are faster depreciated than economic depreciation. Since unconditional conservatism already exists at the inception of assets and liabilities it precedes conditional conservatism.

There are different measures for conditional and unconditional conservatism. The Basu measure (Basu 1997) is a measure for conditional conservatism which will be explained in detail in the following section. The BR-CONS is a measure for unconditional conservatism developed by Beaver and Ryan in 2000. It measures the downward bias in book value by using the book-to-market ratio. Bias means that the book-to-market ratio is constantly above or below one. The coefficient in the formula they use then shows the persistent portion of the difference between book value and market value. The lower this coefficient is, the more conservative a firms accounting.

Another unconditional conservatism measure is the C-SCORE developed by Penman and Zhang (2002). This measure focuses on the hidden reserves. The C-SCORE formula divides the hidden reserves by net operating assets. The amount of hidden reserves can be used to identify the level of unconditional conservatism. The more hidden reserves, the more unconditional conservatism there is in a firm. To estimate the amount of hidden reserves Penman and Zhang use different numbers such as the value of the LIFO reserve, the expensing of R&D and advertising expense. The value of the LIFO reserve displays unconditional conservatism because when prices go up the products that you bought last will go out first. This leads to products in your inventory that are bought at a very low price which means that a big profit on those products can be achieved when selling them.

The third unconditional conservatism measure is the negative accruals measure. This measure has been developed by Givoly and Hayn (2000). The level of unconditional conservatism becomes clear by looking at the total cumulative non-operating accruals. These accruals are used to recognize losses immediately and to defer the recognition of gains. This leads to more and more negative accruals after a time.

2.5 Measures for conditional conservatism

2.5.1 Basu measure

The most well known and widely used measure for conditional conservatism is the Basu measure

(Ryan 2006). The formula looks at the relation between earnings and stock returns. Stock returns are used as a proxy for news. Negative unexpected returns indicate bad news and positive unexpected returns indicate good news. It is expected that negative unexpected returns have a stronger relationship with earnings than positive unexpected returns have with earnings. This is in accordance with the conservatism principle which says that losses are immediately recognized in the profit and loss account and gains are not immediately recognized.

$$E_{it} = \alpha_0 + \alpha_1 BN_{it} + \alpha_2 R_{it} + \alpha_3 BN_{it} R_{it} + \varepsilon_{it}$$

Where:

E_{it} is the net income of firm i in year t, scaled by beginning of the period market value;

R_{it} is the market return over 18 months (01.01.N to 30.06.N+1) net of dividends and capital contributions;

BN_{it} is a dummy variable equal to 1 if R_{it} is negative (indicating bad news) and 0 otherwise (indicating good news).

Earnings are the dependent variable in the Basu measure and stock returns are the independent variable. The Basu measure makes us of a dummy variable to make a distinction between negative and positive returns. The dummy variable has a value of 1 if there are negative unexpected returns and a value of 0 if there are positive unexpected returns. The most important coefficient in the Basu measure is a3. This coefficient shows the incremental increase in the relationship between unexpected returns and earnings when returns are negative. If a3 is significantly positive it means that bad news is reflected quicker in earnings than good news. This coefficient thus shows whether conditional conservatism is present or not within a firm. The greater coefficient a3 is, the higher the degree of conservatism. Basu concludes that earnings are

four and a half times more sensitive to negative returns than to positive returns. Basu also used the explanatory power of the model to examine whether conservatism is present. He divided the sample into a "bad news firms" sample and a "good news firms" sample. The explanatory power (R^2) for "bad news firms" was 6,64 % whereas the R^2 for "good news firms" was 2,09 %. The results clearly show that conditional conservatism is present.

Even though the Basu measure has been the most widely used measure for conservatism it has some weaknesses. First of all, it does not provide a firm specific measure of conservatism. Firm specific factors that could play a role are not taken into account. Secondly, Dietrich et al. (2007) have found some econometric errors in the Basu measure. They conclude that there is an upward bias in the Basu measure. According to them, the Basu measure shows that conservatism is present even though in reality there is no conservatism. Thirdly, markets are not perfect. This could lead to mispricing of stocks which means that stock returns do not always correctly reflect underlying economic news. Givoly et al. (2007) have shown that the Basu measure does not work well in time-series research designs. A strength of the Basu measure is its simplicity. It can easily be used on a very large sample since not much data is needed. Only returns and earnings are needed to measure conservatism. Another strength of the Basu measure is that, even though markets are not perfect, it makes a clear distinction between good and bad news. Returns do not always reflect underlying economic news. In most cases however, it does reflect underlying economic news.

2.5.2 Khan and Watts measure

The Basu measure has been improved by Khan and Watts in 2009. They included firm-specific factors in the model of Basu. The firm-specific factors are: size, market-to-book and leverage. These firm-specific factors are related to the investment opportunity set of a firm (IOS). This IOS is again related to the four explanatory reasons for conservatism. The level of conservatism varies with these firm-specific factors. These variables are used to determine the C_SCORE and the G_SCORE. The G_SCORE shows the timeliness of good news and the C_SCORE shows the incremental timeliness of bad news.

$$G\_Score = \beta_3 = \mu_1 + \mu_1 Size_i + \mu_1 M/B_i + \mu_1 Lev_i$$

$$C\_Score = \beta_4 = \lambda_1 + \lambda_2 Size_i + \lambda_3 M/B_i + \lambda_4 Lev_i$$

These scores are then implemented in the Basu measure. This gives the following equation:

$$X_i = \beta_1 + \beta_2 D_i + R_i(\mu_1 + \mu_2 Size_i + \mu_3 M/B_i + \mu_4 Lev_i) + D_i R_i(\lambda_1 + \lambda_2 Size_i + \lambda_3 M/B_i + \lambda_4 Lev_i) + (\delta_1 Size_i + \delta_2 M/B_i + \delta_3 Lev_i + \delta_4 D_i Size_i + \delta_5 D_i M/B_i + \delta_6 D_i Lev_i) + \varepsilon_i$$

The a2 coefficient in the old Basu equation is replaced by the G_SCORE and the a3 coefficient is replaced by the C_SCORE. Size is measured by taking the natural log of market value of equity. Leverage is calculated by taking long term and short debt deflated by market value of equity. The results of Khan and Watts show that firms with high growth options (high market-to-book ratio), small sized firms and firms with more leverage have higher asymmetric earnings timeliness. The higher the C_SCORE, the higher the degree of conservatism within a firm. The measure of Khan and Watts cannot be applied in every country however. The three characteristics are derived from the explanatory reasons that Watts (2003) has described. Therefore their measure cannot be used in countries where the institutional features differ from United States institutional features.

2.5.3 Asymmetrical accrual to cash-flow measure (AACF)

Ball and Shivakumar (2005) have developed a measure that is able to identify conditional conservatism in private companies. The Basu measure uses returns as a proxy for news. Therefore it is only suitable for firms that are operating in the stock market. The AACF measure does not have this problem.

$$ACC_t = \beta_0 + \beta_1 DCFO_t + \beta_2 CFO_t + \beta_3 DCFO_t \times CFO_t + \varepsilon_t$$

where

ACC_t: Accruals measured as Δ inventory + Δ Debtors + Δ other current assets – Δ Creditors – Δ Other current liabilities – Depreciation.

CFO_t: Cash-flow for period t.

$DCFO_t$: Dummy variable that is set to 0 if $CFO_t \geq 0$, and is set to 1 if $CFO_t < 0$.

The AACF measure is derived from the Basu measure and also makes a distinction between good and bad news. Instead of using returns, the AACF measure uses operating cash flow to make the distinction. A dummy variable is used just like in the Basu measure. The AACF measure uses accruals as the dependent variable. The b3 coefficient is the conservatism coefficient. It shows that accruals are more likely when operating cash flow is below zero.

2.6 Value relevance of earnings measures

2.6.1 Easton and Harris model

Earnings are the bottom line accounting measure of firm performance. It shows how a firm has performed over a period of time. The stock return of a company displays how the capital market evaluates firm performance. The relation between accounting numbers and stock returns reveals the economic relevance of financial reporting. A way to measure the value relevance of earnings is by using the model that Easton and Harris (1991) have developed.

$$Ret_{i,t} = \alpha_0 + \alpha_1 \frac{EPS_{i,t}}{P_{i,t-1}} + \alpha_2 \frac{\Delta EPS_{i,t}}{P_{i,t-1}} + \varepsilon_{i,t}$$

Where:

$Ret_{i,t}$ = The annual logarithm of stock returns of firm i at year t

$P_{i.t,}$ = The share price of firm i at year t

$EPS_{i,t}$ = The earnings per share of firm i at year t

ΔEPS_{it} = The difference of earnings per share of firm i between two points in time

This model measures the association between earnings and returns. A high association between earnings and returns means that there is a high value relevance of earnings. Coefficients a1 and a2 in this formula represent the value relevance of earnings. When a1 and a2 are high and significant it means that earnings have high value relevance. The sum of a1 and a2 is called the earnings response coefficient. A major disadvantage of this measure is that it provides little evidence of whether a change in stock returns is caused by the earnings numbers. This is due to the large window that is used in the formula, namely one year. Other information that has become available during the year could have caused the shift in stock price. The window needs to be smaller to make sure that the change in stock price is not caused by other factors. Nichols and Wahlen (2004) have found that there is a very quick response by the capital market to earnings announcements. The new earnings information is, for a large part, incorporated in the stock price immediately on the first day of the earnings announcement.

2.6.2 Perfect foresight measure

Value relevance of earnings can also be measured by using the approach of Francis and Schipper (1999). They focus on the returns that could be earned when someone has perfect foresight of accounting information. A hedge portfolio is formed based on the following formula.

$$R_{j,t} = \gamma_{0,t} + \gamma_{1,t}\Delta EARN_{j,t} + \gamma_{2,t}EARN_{j,t} + \gamma_{j,t}BV_{j,t} + \xi_{j,t}$$

$R_{j,t}$ stands for the market-adjusted return on security j. $\Delta EARN_{j,t}$ is the change in earnings before extraordinary items deflated by the market value of equity and $BV_{j,t}$ is the book value of equity. A long position is taken in the highest 40 percent and a short position in the lowest 40 percent. These hedge returns are then scaled by a perfect foresight returns-based hedge portfolio. This perfect returns-based hedge portfolio is formed by looking at the 15-month market-adjusted returns. When this 15-month market-adjusted return is positive, a long position is taken in the stock. A short position is taken when the 15-month market-adjusted return is negative.

The perfect foresight measure and the Easton and Harris model have the same limitations. They only focus on earnings and do not take other accounting information into account. Furthermore, there has been a significant increase in footnote disclosure through time. Both equations are not able to take into account the effect that the increase in footnote disclosure has on value relevance. Increase in value relevance of earnings could therefore be partially due to an increase in footnote disclosure. Third, there has been an increase in non-information based trading (Dontoh et al. 2004).

2.7 Conclusion

There have been both early supporters as early opponents of conservatism. The opponents say that conservatism goes against the matching principle whereas the advocates emphasize that conservatism is used by firms to solve one or more problems. Three different unconditional measures are explained in this chapter: Beaver and Ryan measure, Penman and Zhang measure and the negative accruals measure. The Basu measure is the most important conditional conservatism measure. The Khan and Watts measure and the AACF measure are derived from the Basu measure. The Easton and Harris model is used to determine value relevance of earnings. The perfect foresight measure is derived from the Easton and Harris model.

3 Literature review

3.1 Introduction

This chapter will elaborate on the literature that has to do with value relevance and conservatism. Firstly, literature that deals with value relevance of earnings under IFRS will be discussed. Subsequently, the conservatism literature will be studied. The focus will be on conservatism after the introduction of IFRS. Finally, literature that deals with the relationship between value relevance and conservatism will be presented.

3.2 Value relevance of earnings under IFRS

Value relevance of accounting information has been a frequently examined topic in the accounting literature. This subject has had especially a lot of attention in the United States. Several researchers come to the conclusion that value relevance of accounting information has deteriorated over time. Lev and Zarowin (1999) conclude that the association between earnings and returns diminishes in the years 1978 until 1996. The same holds for the association between cash flows and returns. Francis and Schipper (1999) and Core et al. (2003) share the conclusion of Lev and Zarowin that value relevance has diminished over time in the United States. Lev and Zarowin search the cause for the decline in value relevance at the increasing R&D expenses of firms. They state that conservative accounting rules, such as expensing R&D, are not able to cope with the changing circumstances. R&D is expensed immediately whereas the benefit of this R&D is recognized in other periods. This distortion leads to lower informativeness of accounting information.

Value relevance of accounting information has been examined in Europe as well. Especially the time period after the mandatory adoption of IFRS is interesting. IFRS has been introduced in 2005 and is more fair value based than most national General Accepted Accounting Principles (GAAP). Therefore there could have been a shift in value relevance after the introduction of IFRS. IFRS is aimed at increasing comparability across countries and increasing transparency. It is therefore expected that the increased comparability and transparency will lead to less information asymmetry which in turn leads to an increase in the relationship between accounting information and market data.

The impact of IFRS on value relevance of accounting information has been examined by Devalle et al. (2010). They expect an increase of value relevance of accounting information after the adoption of IFRS. Furthermore they expect that the relationship between accounting information and market data will be similar across European countries after the adoption of IFRS. The sample includes 3721 firms in five different countries, namely Spain, Germany, France, United Kingdom and Italy. The time period studied is 2002-2007. Value relevance is measured by regressing share price on book value of equity per share and earnings per share. The explanatory power (R^2) is used to determine value relevance. They conclude that the impact of IFRS differs across countries. Across the whole sample there has been an increase of value relevance. The explanatory power of the model before IFRS is 51 percent and after the introduction of IFRS 57,7 percent. The coefficient on book value of equity decreases whereas the coefficient on earnings increases after the introduction of IFRS. This means that the increase of value relevance is due to the increase in value relevance of earnings. However, major differences are observed when looking at countries individually. Italy, Spain and Germany show a decrease in value relevance when the explanatory power is used as a proxy for value relevance. France and the United Kingdom show an increase. If only value relevance of earnings is studied, an increase is seen in France, Germany and the United Kingdom. Value relevance of earnings has decreased in Spain and Italy. The United Kingdom is the only country that shows an increase in value relevance of book value of equity. All the other countries show a decrease.

The impact of IFRS on value relevance has also been studied by Morais and Curto (2009). Just like Devalle et al. (2010), they find an overall increase of value relevance after the introduction of IFRS. They include 6977 European listed firms that are active in 14 different countries in their sample. The investigated countries are: Austria, Denmark, Belgium, Finland, Germany, Greece, Ireland, Italy, France, the Netherlands, Sweden, Spain, Portugal and the United Kingdom. Somewhat the same model that Devalle et al. (2010) have applied is also used by Morais and Curto to determine whether value relevance has increased. The time frame studied is 2000-2005. Their conclusion is that the explanatory power of the model has increased after the adoption of IFRS which means that value relevance has increased. The explanatory power of the model has increased for all countries except for Austria, Ireland, Sweden and the Netherlands. Based on the results of both studies we can say that in general there is an increase in value relevance if value relevance is measured by the explanatory power of the model. Both studies, Morais and Curto

(2009) and Devalle et al. (2010), show that the explanatory power of the model post-IFRS is higher than pre-IFRS across the whole sample. However, there are major differences between countries. France, Germany and the United Kingdom show an increase in value relevance of earnings whereas Italy and Spain show a decrease. There is also some contradiction between the two studies. Where Devalle et al. (2010) find that Italy, Spain and Germany experience a decrease in value relevance when the explanatory power of the model is used; Morais and Curto find an increase in value relevance for these countries. The different time frame used in both studies could be the cause of the difference.

3.3 Conservatism in Europe after the mandatory adoption of IFRS

Balachandran and Mohanram (2011) have studied the level of conservatism throughout the years in the United States. They find that the level of unconditional conservatism has increased. Basu (1997) also finds that conservatism has increased in the United States in the period 1963-1990. In contrast to Balachandran and Mohanram (2011), Basu (1997) examines conditional conservatism.

The level of conservatism has also been examined in Europe. However, research on this topic is scarce. Andre and Filip (2012) have studied the effect of IFRS on the level of conditional conservatism in European countries. They also studied whether institutional and political differences would persist after the introduction of IFRS. They expect that the level of conservatism and the institutional differences would decrease after IFRS. Sixteen countries and 7378 firm-year observations have been examined by Andre and Filip. The time period studied was 2003-2007.

The Basu measure is used to measure conditional conservatism. They used an adapted version of the Basu measure to take into account the effect of IFRS. By using dummy variables they can clearly observe whether IFRS caused a shift in the level of conditional conservatism. Institutional differences were also taken into account in the adapted Basu measure. This changes the formula from:

$$E_{it} = \alpha_0 + \alpha_1 BN_{it} + \alpha_2 R_{it} + \alpha_3 BN_{it} R_{it} + \varepsilon_{it}$$

Into the adapted Basu measure:

$$Y_{it} = \alpha_0 + \alpha_1 BN_{it} + \alpha_2 R_{it} + \alpha_3 BN_{it} R_{it} +$$
$$+ \alpha_4 IFRS_{it} + \alpha_5 IFRS_{it} BN_{it} + \alpha_6 IFRS_{it} R_{it} + \alpha_7 IFRS_{it} BN_{it} R_{it} +$$
$$+ \alpha_8 IF_{it} + \alpha_9 IF_{it} BN_{it} + \alpha_{10} IF_{it} R_{it} + \alpha_{11} IF_{it} BN_{it} R_{it} +$$
$$+ \alpha_{12} IF_{it} IFRS_{it} + \alpha_{13} IF_{it} IFRS_{it} BN_{it} + \alpha_{14} IF_{it} IFRS_{it} R_{it} + \alpha_{15} IF_{it} IFRS_{it} BN_{it} R_{it} + \varepsilon_{it}$$

Where:

IF_{it} is a dummy variable that takes the value 1 if the firm belongs to a specific classification scheme, and 0 otherwise;

The results show that big differences existed between countries prior to the introduction of IFRS when it comes to the level of conditional conservatism. After IFRS however, they find that these differences seem to disappear. Furthermore they find that the overall level of conditional conservatism has decreased after IFRS. Conditional conservatism decreased for France, the Netherlands, Greece, Germany, Spain, Portugal and Switzerland. Conditional conservatism has decreased in code law countries and in countries with a French and German law origin. Furthermore, conservatism decreased in countries with higher perceived levels of governance, debt market dominated countries and less developed equity markets and in countries with high tax book conformity. Lastly, countries where the national standards differed much from IFRS also showed a decrease in conservatism.

3.4 Relationship between conservatism and value relevance

Balachandran and Mohanram (2011) have studied the relationship between conservatism and value relevance in the United States. The object of their study was to examine whether the decrease in value relevance throughout the years is caused by the increase in conservatism. They investigated 30 years (1975-2004) and their sample included 100984 observations. Only unconditional conservatism is taken into account since prior research (Lev and Zarowin (1999)) has identified that this is the type of conservatism that could be the cause of the decline in value relevance. The Beaver and Ryan approach (BR-CONS) and the Penman and Zang approach (C-SCORE) are used to measure unconditional conservatism. They do not only focus on the level of

conservatism but also on growth of conservatism. Their sample is divided into two groups based on the level of conservatism. The sample is also partitioned into two groups based on the growth of conservatism. After dividing the sample in groups, they examine whether there are differences in value relevance between the two groups. Three different measures of value relevance are used in this study: the adjusted R^2 of a regression of stock price per share on earnings per share and book value per share, the adjusted R^2 of a regression of annual stock returns on scaled earnings and changes in earnings (Easton and Harris model) and a perfect foresight measure. Subsequently, a time trend is used for both groups to see how value relevance has changed over time for the different groups. Value relevance (VALREL) is the dependent variable in this equation. The results show that unconditional conservatism is not the cause of the decline in value relevance throughout the years. What is remarkable about the results is that the firms that were in the steady conservatism group showed the greatest decline in value relevance. Firms with increasing conservatism experienced the smallest decline in value relevance.

Balachandran and Mohanram (2011) only focus on the relationship between conservatism and value relevance in the United States. Brown et al. (2006) examine this relationship in an international context and also take the institutional environment into account. Twenty countries are examined in the time period 1993-2004. The Basu measure and the AACF measure are used to measure conditional conservatism. Countries in Asia, Europe, North America and Africa were included in the sample. The following regression is used to measure whether the relationship between conservatism and value relevance depends on the accrual intensity of a country:

$$value\ relevance = \gamma_0 + \gamma_1^* accrual\ index + \gamma_2^* tax + \gamma_3^* C + \gamma_4^* accrual\ index^* C + \gamma_5^* UCC + \eta$$

C stands for conditional conservatism measured by either the Basu measure or the AACF measure. UCC stands for unconditional conservatism. Y4 is the most important coefficient of this regression. This coefficient appeared to be significantly positive when using both measures for conditional conservatism. They conclude that a positive association exists between conditional conservatism and value relevance of earnings in countries with high accrual intensity. This positive association is incremental to the effect of shareholder protection. Conservative accounting makes sure that opportunistic actions of managers are constrained.

Brown et al. (2006) state that: "Conditional conservatism constrains managers' opportunistic actions and such benefits should be stronger for firms with greater latitude or availability in the use of accruals". The relationship between conservatism and value relevance thus depends on the degree of accrual intensity. This could also explain why Balachandran and Mohanram (2011) did not find an association between value relevance and conservatism. They did not focus on variation in accrual intensity.

Kousenidis et al. (2009) have examined the relationship between conservatism and value relevance in a European context. They expected that conservative accounting had a positive effect on value relevance of earnings. The studied time period is 1989-2003 which means that it was before the introduction of IFRS. They subdivided this period into 2 different periods. The first period (1989-1999) is the period before the market crisis and the second period (1999-2003) is the period after the market crisis. The Easton and Harris (1991) model is applied to determine value relevance of earnings. Only Greek firms that are listed on the Athens Stock Exchange are taken into account which leads to a final sample of 127 firms with 1035 year observations. The Basu measure is used to determine conditional conservatism. The final sample is divided into three different groups based on their level of conditional conservatism. The firms with the lowest 30 percent of conditional conservatism are in the first group. Firms with medium conditional conservatism (between 30 and 70 percent) are included in the second group. The last group contains firms with the highest amount (30 percent) of conditional conservatism. They conclude that conditional conservatism is present in Greece. Conditional conservatism has increased in the time period after the market crisis but before that period it does not show a clear pattern. The increase after the market crisis could be due to stricter accounting rules which have been introduced after this crisis. Furthermore, firms could have been afraid of increased shareholder litigation. Value relevance, as measured by the adjusted R^2, has significantly declined over the time period studied. The relationship between conditional conservatism and value relevance of earnings shows a non-linear relationship. Firms in the medium conditional conservatism group appear to have the highest value relevance of earnings. The high conditional conservatism group shows more value relevance of earnings than the low conditional conservatism group. These results are more or less in accordance with the results of Balachandran and Mohanram (2011) who find that firms in the increasing conservatism group show lower decline in value relevance

than firms in the steady conservatism group. Both high conservatism and low conservatism distort the information content of earnings. However, high conservatism appears to do that to a lesser extent than low conservatism.

The only study that takes the effect of IFRS into account is the study of Maganaris et al. (2011). They examined the period between 1999 and 2008. They make a distinction between two sub periods, namely 1999-2004 and 2005-2008. This is done to observe the effect of IFRS.
Three code law countries (France, Germany and Greece) and one common law European country (United Kingdom) are taken into account. Code law countries are characterized by a tax-driven, law-based and stakeholder-oriented system whereas common law countries are characterized by low taxes, shareholder oriented accounting practices and profound corporate governance. They focus primarily on firms in the financial sector since they believe that the financial sector is greatly affected by IFRS. The R^2 of the Easton and Harris (1991) model is applied to measure value relevance. The results show that the R^2 decreases for code law countries after the introduction of IFRS. In the United Kingdom however, an increase of value relevance is seen after the introduction of IFRS. The Basu measure is used to capture conservatism. In accordance with previous research (Andre and Filip 2012), a decline in conservatism is observed in code law countries after the introduction of IFRS. The United Kingdom remarkably shows an increase of conservatism post-IFRS. To examine the relationship between conservatism and value relevance, Maganaris et al. (2011) divide the sample into two groups: a high and a low conservatism group. They choose two groups instead of three groups because of the relatively small sample size, especially in the case of Greece. They conclude that more conditional conservatism leads to less value relevant earnings post-IFRS. This holds for all countries except for Germany. These findings are thus in contradiction with previous findings of Balachandran and Mohanram (2011), Kousenidis et al. (2009) and Brown et al. (2006).

3.5 Conclusion

The literature shows that in general there is an increase in value relevance of earnings after the adoption of IFRS. However, major differences between countries still exist. The level of conservatism in European countries seems to decline and differences in conservatism levels between countries disappear after the introduction of IFRS. The literature shows mixed results

when it comes to the relationship between value relevance and conservatism. Most researchers find that conservatism has a positive association with value relevance. However, the only research that takes the effect of IFRS into account finds that more conservatism leads to less value relevance of earnings. This literature review has formed the basis for the development of the hypotheses which will be presented in the next section.

4 Hypotheses

4.1 Introduction

This chapter is dedicated to the development of the hypotheses. There will be four hypotheses in total. The first two hypotheses are a build up towards the last two which are the most important hypotheses of this master thesis. These last two hypotheses deal with the relationship between conditional conservatism and value relevance of earnings. Explanation will be given about the expectations of each hypothesis.

4.2 Explanation of hypotheses

The first hypothesis deals with the value relevance of earnings after the introduction of IFRS. As already mentioned before, this thesis only focuses on value relevance of earnings because it is the most important number in the financial statements. Two countries will be examined in this master thesis: Germany and France. The literature shows (Devalle et al. 2010) that the value relevance of earnings has increased for Germany after the introduction of IFRS. The coefficient on earnings increased from 0, 3408 pre-IFRS to 0.4521 post IFRS in the price-regression model and is significant at the 1% level. The same holds for France where the explanatory power of the price-regression model even increased from 15% pre-IFRS to 80% post-IFRS. The coefficient on earnings shows a major increase from 0, 3376 to 2, 2489 and is statistically significant at the 1% level. Therefore, the expectation is that value relevance of earnings will increase after the adoption of IFRS for both Germany and France.

Hypothesis 1: Value relevance of earnings is higher after the mandatory adoption of IFRS.

The second hypothesis focuses on the level of conditional conservatism after the introduction of IFRS. The focus is on conditional conservatism since prior literature (Andre and Filip 2012) shows that this type of conservatism decreases after the adoption of IFRS. More specifically, the level of conditional conservatism in Germany declines from 0,422 pre-IFRS to 0,157 post-IFRS and is statistically significant at the 5 percent level. The level of conditional conservatism in France decreases from 0,365 pre-IFRS to 0,148 post-IFRS and is statistically significant at the 1% level. Therefore hypothesis 2 predicts:

Hypothesis 2: The mandatory introduction of IFRS will lead to a decrease in conditional conservatism.

The last two hypotheses will deal with the relationship between conditional conservatism and value relevance of earnings. The main question that will be answered is whether the increase in value relevance of earnings after the introduction of IFRS is driven by the decrease in conditional conservatism. The literature review has shown mixed results about the relationship between conservatism and value relevance. However, the research that comes closest to this master thesis is the paper of Maganaris et al. (2011). This is the only research that takes the effect of IFRS into account. They found that more conditional conservatism leads to less value relevance of earnings after the introduction of IFRS. In contrast with this master thesis, they only include firms in the financial sector in their sample. This master thesis will focus on firms in different sectors. Based on the results of the paper of Maganaris et al. (2011), the following is predicted:

Hypothesis 3: Value relevance of earnings is lower when conditional conservatism is present after the implementation of IFRS.

Hypothesis 4: Firms with low conditional conservatism will show a higher increase in value relevance of earnings than firms with high conditional conservatism after the implementation of IFRS.

4.3 Conclusion

This section has been dedicated to the development of the hypotheses. The expectations are based on the results of prior research. The main hypotheses of this master thesis are hypothesis 3 and 4 which examine the relationship between conditional conservatism and value relevance of earnings. The following chapter will elaborate on how these hypotheses will be tested.

5 Research design

5.1 Introduction

This chapter will show how the different hypotheses will be tested. The research design of the hypotheses will be explained separately for each hypothesis. This is because different models are used to test the hypotheses. Furthermore explanation will be given about why certain models are used. The sample and the limitations of this study will also be presented in this chapter.

5.2 Research design of the hypotheses

Hypothesis 1: Value relevance of earnings is higher after the mandatory adoption of IFRS.

The first hypothesis that deals with the value relevance of earnings after the mandatory adoption of IFRS will be tested by using the Easton and Harris model (1991). This model has been explained in chapter 2: Concepts and measures. The perfect foresight measure will not be used to determine value relevance. Even though the perfect foresight measure takes the perspective of a shareholder, it is impossible for shareholders to use this measure to make profits since foresight is required. A distinction needs to be made between the period before IFRS and the period after the introduction of IFRS to test whether an increase in value relevance of earnings has occurred. The value relevance of earnings in the Easton and Harris model is presented by the coefficients a1 and a2 (earnings response coefficient). These coefficients will be calculated and a comparison between the two periods will be made to determine whether value relevance of earnings has increased. Hypothesis 1 predicts that the earnings response coefficient will be higher in the post-IFRS time period.

Hypothesis 2: The mandatory introduction of IFRS will lead to a decrease in conditional conservatism.

For the second hypothesis, both the Basu measure as well as the AACF measure will be used to determine conditional conservatism. This is done because the Basu measure has some clear weaknesses. To make sure that the results are not driven by errors in the Basu measure, the AACF measure is also used. The measure of Khan and Watts (2009) is not used because they themselves say that their measure cannot be used in countries where the institutional settings

differ from those of the United States. France and Germany have clearly different institutional features than the United States. For example, there is more shareholder protection in the United States and Germany and France are more debt oriented. The focus is on conditional conservatism rather than unconditional conservatism since prior research (Andre and Filip 2012) has shown that the level of conditional conservatism has declined post-IFRS. No studies have been found about the impact of IFRS on unconditional conservatism. Therefore these measures will not be used. To make a distinction between the pre-IFRS time period and the post-IFRS time period, the model of Andre and Filip (2012) will be applied. This model adds dummy variables to the normal Basu measure. This changes the normal Basu measure into:

$$Y_{it} = \alpha_0 + \alpha_1 BN_{it} + \alpha_2 R_{it} + \alpha_3 BN_{it} R_{it} +$$

$$+ \alpha_4 IFRS_{it} + \alpha_5 IFRS_{it} BN_{it} + \alpha_6 IFRS_{it} R_{it} + \alpha_7 IFRS_{it} BN_{it} R_{it} + \varepsilon_{it}$$

Where:

$IFRS_{it}$ is a dummy variable that takes the value 1 if the year is 2005, 2006 or 2007 and 0 otherwise;

The first part of the equation shows the normal Basu measure. The second part takes the effect of IFRS into account. A0 and a1 are intercepts. The same holds for a4 and a5. Coefficient a2 shows how earnings respond to good news (returns above zero) whereas coefficient a6 shows how earnings respond to good news after the introduction of IFRS. The responsiveness of earnings to bad news pre-IFRS is measured by the sum of coefficients a2 and a3 whereas the coefficients a6 and a7 measure the responsiveness of earnings to bad news post-IFRS. The most important coefficients of this model are a3 and a7. When coefficient a7 appears to be lower than coefficient a3, it means that conditional conservatism has declined post-IFRS. The prediction is that coefficient a7 will be lower than coefficient a3.

Hypothesis 3: Value relevance of earnings is lower when conditional conservatism is present after the implementation of IFRS.

To examine the relationship between value relevance of earnings and conditional conservatism, groups will be formed based on the level of conditional conservatism. Prior research has either divided the sample into two groups (Balachandran and Mohanram 2011, Maganaris et al. 2011) or three groups (Kousenidis et al. 2009). Three groups will be formed in this master thesis. Only the extreme conservatism groups are taken into account to test this hypothesis because then a clear difference exists between the levels of conditional conservatism of both groups. The first group exists of firms with the lowest 40 percent of conditional conservatism. The second group, the medium conservatism group, takes firms into account that are between 40 and 60 percent. The last group includes firms with the highest 40 percent of conditional conservatism. The medium conservatism group will not be used.

After having identified the different conditional conservatism groups a comparison will be made between the value relevance of earnings of both groups. The Easton and Harris model (1991) is used to determine value relevance of earnings. The earnings response coefficients of both groups will be compared in the post-IFRS time period. The prediction is that the earnings response coefficient will be higher for firms with less conditional conservatism in the post-IFRS time period.

Hypothesis 4: Firms with low conditional conservatism will show a higher increase in value relevance of earnings than firms with high conditional conservatism after the implementation of IFRS.

The final hypothesis deals with the growth in value relevance of earnings. The same conservatism groups as in hypothesis 3 will be used. The period examined is the entire period from 2002 until 2007. The increase in value relevance of earnings of both groups will be compared. The R^2 of the Easton and Harris model (1991) is applied to determine value relevance. The R^2 is used instead of the earnings response coefficient because of the small sample size. Each year will be examined separately in this hypothesis. Due to the small sample size, there is a big chance that coefficients will not be significant. However, the R^2 looks at the entire model and the chance that this R^2 is significant is of course much higher. The trend in value relevance is calculated by using the following equation:

$$Value\ relevance_{j,t} = \alpha_j + \beta_j * TIME + \varepsilon$$

The prediction is that Bj will be higher for the low conditional conservatism group.

5.3 Sample

Two countries are examined in this master thesis: France and Germany. These two countries are chosen because they are two big European countries. Furthermore, they countries are very suitable for this thesis because the literature review shows that these countries experience an increase in value relevance of earnings and a decrease in conditional conservatism. Therefore it is interesting to see whether this increase in value relevance of earnings in caused by the decrease in conditional conservatism. Balachandran and Mohanram (2011) did the same in the United States, but they found a decrease in value relevance and an increase in conservatism. The opposite has happened in Europe for France and Germany.

The time period studied in this thesis is 2002-2007. This time period includes three pre-IFRS years (2002, 2003 and 2004) and three post-IFRS years (2005, 2006 and 2007) to make a fair comparison between the periods. Firms that have merged or gone bankrupt during this period are not taken into account. Another condition is that firms need to be continuously active during the entire period. Firms from the financial sector are not taken into account as well. These firms have special accounting rules and therefore they are eliminated. Only the largest firms are taken into account in this master thesis. These firms are selected by looking at the total assets.

The sample consists of 314 firms, 157 for each country. The total firm year observations are 1884 (314*6 years). Compared to other studies, this is a small sample size. There are two reasons for this small sample size. The first one is that all the variables used have to be available for each firm. If one variable is not present, the firm cannot be used anymore because it is then impossible to make a comparison between different measures and different groups. The second reason, which is the main reason, is because conditional conservatism needs to be calculated for each firm individually. This is a time-consuming process so therefore a small amount of firms is chosen. The data used comes from the Wharton Research Database. All the variables used are found there except the returns. These are found in the Datastream database.

5.4 Limitations

The most important limitation of this master thesis is that only conditional conservatism is examined as a factor that could influence the value relevance of earnings. Even if the results show that firms with more conditional conservatism display less value relevance of earnings, it is impossible to conclude that conditional conservatism is the only cause of the low value relevance of earnings. To be able to identify conditional conservatism as the major cause of low value relevance, other possible relevant factors should be examined as well. At most, it can be said that conditional conservatism is one of the factors that influence value relevance of earnings negatively. Another limitation of this master thesis is the short time period used. The period after the introduction of IFRS consists of only three years (2005, 2006 and 2007). The years after 2007 are excluded because of the financial crisis. Furthermore, only two countries (France, Germany) are examined in this study. Generalization is therefore not possible. The relationship between conditional conservatism and value relevance of earnings could be different in other countries. This thesis only focuses on conditional conservatism. This is also a limitation because unconditional conservatism is not studied. Unconditional conservatism could however also influence value relevance of earnings. Only one measure for value relevance of earnings is used in this study, namely the Easton and Harris model (1991). Other measures are not taken into account but could lead to different results. The focus is only on value relevance of earnings. Earnings however are only one number of the many numbers in the financial statements. These other numbers are not studied in this master thesis which is also a limitation.

5.5 Conclusion

This chapter has been devoted to the research design. The different models are explained and, more importantly, explanation is given about why these models are used. Value relevance of earnings will be measured by the Easton and Harris model (1991). The Basu measure and the AACF measure are used to determine conditional conservatism. Groups are formed based on the level of conditional conservatism to determine whether conditional conservatism influences value relevance of earnings. A time trend is used to test the last hypothesis. The most important limitation of this study is that, at most, it can be concluded that conditional conservatism is one of the causes of low value relevance of earnings. It cannot be appointed as the sole cause.

6 Results

6.1 Introduction

The results of the research will be presented in this section. First, the descriptive statistics will be presented. The main features of the data will be described. After that, the results of the different hypotheses will be shown. The focus is on the results of hypothesis 3 and hypothesis 4 which examine the relationship between value relevance of earnings and conditional conservatism. The results of the hypotheses will be shown separately for France and Germany and a distinction will be made between the pre-IFRS time period and the post-IFRS time period. Furthermore, a comparison will be made to see whether the results correspond or contradict with prior research.

6.2 Descriptive statistics

The table below presents the descriptive statistics of the French dataset.

	N	Minimum	Maximum	Mean	Std. Deviation
Earnings per share (deflated by Stock Price)	942	-4.073171390	4.422496469	.0960284689	.3419828654
Change in earnings per share (deflated by Stock Price)	942	-2.151294688	12.86176373	.0464196538	.5257527553
Accruals (deflated by total assets)	942	-1.252339669	.9906665613	-.0523123595	.1232411093
Operating cash flow (deflated by total assets)	942	-.8373222587	.8069822998	.0833353204	.0784981248
Returns	942	-.9099510757	5.525770278	.1512633619	.4614056153
Earnings per share	942	-90.5466	542.0300	5.342240	27.2264221
Stock Price	942	.91000000000000	6589.000000	80.55255817	413.9460502
Valid N (list wise)	942				

One outlier has been detected in the data of France. This is the firm Etablissements Gantois for the variable "Change in earnings per share (deflated by Stock Price)" in the year 2005. This change in earnings per share appeared to be very high (12.86) and will be deleted from the

dataset when testing the hypotheses because this outlier distorts the results. The next table presents the descriptive statistics of the German dataset.

	N	Minimum	Maximum	Mean	Std. Deviation
Earnings per share (deflated by Stock Price)	942	-3.426937269	4.786585366	.0478750724	.3942420487
Change in earnings per share (deflated by Stock Price)	942	-2.969483395	6.219512195	.0762836929	.5732706464
Accruals (deflated by total assets)	942	-2.754164872	.9338375796	-.0651660752	.1874247719
Operating cash flow (deflated by total assets)	942	-1.064050779	.8247726227	.0812741560	.1205912037
Returns	942	-.9600000000	6.307692308	.20385445556	.6434420952
Earnings per share	942	-24.9100	43.8565	1.561433	4.0512818
Stock Price	942	.339000000000	620.000000000	24.53862314	49.23474393
Valid N (list wise)	942				

No outliers have been detected in the German dataset. A big difference between the two datasets is the standard deviation of the variable “Stock Price”. The German dataset shows a much smaller deviation than the French dataset. This is mainly due to the very high stock prices of a French firm named Grand Marnier. Another big difference is the standard deviation of the variable “Earnings per share”. The French dataset has a higher mean for the following variables: Earnings per share (deflated by Stock Price), Accruals (deflated by total assets), Operating cash flow (deflated by total assets), Earnings per share and Stock Price. The German dataset has a higher mean for the variables “Change in earnings per share (deflated by Stock Price)” and “Returns”.

6.3 Results Hypothesis 1

The expectation of hypothesis 1 is that value relevance of earnings, as measured by the Easton and Harris model, will increase after the introduction of IFRS for both France as Germany. The earnings response coefficient of the Easton and Harris model and the explanatory power of the model will be used to measure value relevance. The tables below present the results of hypothesis 1 for France.

$$Ret_{i,t} = \alpha_0 + \alpha_1 \frac{EPS_{i,t}}{P_{i,t-1}} + \alpha_2 \frac{\Delta EPS_{i,t}}{P_{i,t-1}} + \varepsilon_{i,t}$$

France	Pre-IFRS			
	Coefficients	T-value	R^2	Sig.
Constant a_0	0,093	4,274		0,000***
Earnings per share a_1	***0,271***	4,912		0,000***
Change in earnings per share a_2	***0,260***	3,839		0,000***
Full model			***0,111***	0,000***

France	Post-IFRS			
	Coefficients	T-value	R^2	Sig.
Constant a_0	0,103	5,217		0,000***
Earnings per share a_1	***0,725***	7,948		0,000***
Change in earnings per share a_2	***0,052***	0,728		0,467
Full model			***0,173***	0,000***

*** : significant at 1% level
** : significant at 5% level
* : significant at 10% level

The earnings response coefficient for French firms pre-IFRS is 0,531 (0,271+0,260). The R^2 of the model equals 0,111. The earnings response coefficient after the introduction of IFRS is 0,777 (0,725+0,052) and the R^2 has a value of 0,173. Especially the coefficient on "Earnings per share (deflated by Stock Price)" has increased enormously from 0,271 pre-IFRS to 0,725 post-IFRS. The coefficient on "Change in earnings per share (deflated by Stock Price)" has decreased post-IFRS. However, there is still an increase of the earnings reponse coefficient and the R^2. The coefficients are all significant at the 1% level except the variable "Change in earnings per share" in the post-IFRS time period. This coefficient appears to be not signicificant at all. Based on

these results, we can say that value relevance of earnings has increased for France after the introduction of IFRS. The next tables show the results of hypothesis 1 for Germany.

Germany	Pre-IFRS			
	Coefficients	T-value	R^2	Sig.
Constant a_0	0,142	4,186		0,000***
Earnings per share a_1	***0,159***	1,929		0,054*
Change in earnings per share a_2	***0,362***	6,338		0,000***
Full model			***0,144***	0,000***

Germany	Post-IFRS			
	Coefficients	T-value	R^2	Sig.
Constant a_0	0,193	9,070		0,000***
Earnings per share a_1	***0,396***	5,062		0,000***
Change in earnings per share a_2	***-0,049***	-0,925		0,355
Full model			***0,053***	0,000***

*** : significant at 1% level
** : significant at 5% level
* : significant at 10% level

The earnings response coefficient for German firms pre-IFRS equals 0,521 (0,159+0,362) and the R^2 is 0,144. The earnings response coefficient post-IFRS is 0,347(0,396-0,049) whereas the R^2 is 0,053. These results do not correspond with the expectation. Value relevance of earnings has not increased for Germany after the introduction of IFRS but decreased. There is a decrease in earnings response coefficient and a decrease in explanatory power (R^2). The variable "Change in earnings per share" in the post-IFRS period is not significant at all. The results are contradicting with the results of Devalle et al. (2010) who have found an increase in value relevance of earnings for Germany post-IFRS. The difference could arise because they use a slightly different value relevance of earnings measure. They regress stock prices on earnings per share (price model). However, this measure has a major shortcoming compared to the Easton and Harris model applied in this thesis. The earnings per share are deflated by stock price at the beginning of the period in the Easton and Harris model. This mitigates size effects. The coefficients in the price model might be biased due to size effects. Devalle et al. (2010) use

sophisticated techniques in their paper to eliminate these scale effects. An advantage of the price model is that it also takes book value of equity into account whereas the Easton and Harris model only focuses on earnings. As previously stated, the focus of this thesis is on value relevance of earnings and therefore the Easton and Harris model is applied. The tables below present the results when value relevance of earnings is measured by regressing stock prices on earnings per share.

$$Priceit = a0 + a1\,Earningsit + \epsilon it$$

Where:

$Price_{it}$= Stock price for firm i at the beginning of year

$Earnings_{it}$= Earnings per share for firm i in year t

France	Pre-IFRS			
	Coefficients	T-value	R^2	Sig.
Constant a_0	21,012	3,336		0,001***
Earnings per share a_1	***8,574***	45,760		0,000***
Full model			***0,817***	0,000***

France	Post-IFRS			
	Coefficients	T-value	R^2	Sig.
Constant a_0	-45,470	-6,085		0,000***
Earnings per share a_1	***24,222***	65,519		0,000***
Full model			***0,902***	0,000***

Germany	Pre-IFRS			
	Coefficients	T-value	R^2	Sig.
Constant a_0	9,905	9,085		0,000***
Earnings per share a_1	***7,064***	20,690		0,000***
Full model			***0,477***	0,000***

Germany	Post-IFRS			
	Coefficients	T-value	R^2	Sig.
Constant a_0	10,336	5,566		0,000***
Earnings per share a_1	***10,255***	28,944		0,000***
Full model			***0,641***	0,000***

*** : significant at 1% level
** : significant at 5% level
* : significant at 10% level

The results of a regression of stock prices on earnings per share, like Devalle et al (2010) did, show that value relevance of earnings has increased for both France as Germany. The results are thus the same as the results of Devalle et al. (2010). The earnings per share coefficient for France increases from 8,574 pre-IFRS to 24,222 post-IFRS and the R^2 increases from 0,817 pre-IFRS to 0,902 post-IFRS. The earnings per share coefficient for Germany increases from 7,064 pre-IFRS to 10,255 post-IFRS whereas the R^2 increases from 0,477 to 0,641. All the coefficients appear to be significant at the 1% level.

6.4 Results hypothesis 2

The expectation of the second hypothesis is that conditional conservatism will decrease after the introduction of IFRS for both France as Germany. Conditional conservatism is measured with the Basu measure and the AACF measure. The results with the Basu measure will be presented first.

$$Y_{it} = \alpha_0 + \alpha_1 BN_{it} + \alpha_2 R_{it} + \alpha_3 BN_{it} R_{it} +$$

$$+ \alpha_4 IFRS_{it} + \alpha_5 IFRS_{it} BN_{it} + \alpha_6 IFRS_{it} R_{it} + \alpha_7 IFRS_{it} BN_{it} R_{it} + \varepsilon_{it}$$

Where:

$IFRS_{it}$ is a dummy variable that takes the value 1 if the year is 2005, 2006 or 2007 and 0 otherwise;

France			
	Coefficients	T-value	Sig.
Constant a_0	0,131	4,326	0,000***
Dummy constant a_1	0,006	0,124	0,902
Returns a_2	0,125	2,396	0,017**
Dummy*returns a_3	***0,462***	3,487	***0,001****
IFRS constant a_4	0,046	3,036	0,003***
IFRS dummy constant a_5	0,016	0,515	0,607
IFRS returns a_6	0,240	8,712	0,000***
IFRS dummy*returns a_7	***-0,037***	-0,270	***0,787***

Germany			
	Coefficients	T-value	Sig.
Constant a_0	0,036	0,955	0,340
Dummy constant a_1	-0,038	-0,567	0,571
Returns a_2	0,128	3,491	0,001***
Dummy*returns a_3	***0,105***	0,787	***0,432***
IFRS constant a_4	0,056	2,631	0,009***
IFRS dummy constant a_5	0,032	0,762	0,447
IFRS returns a_6	0,107	2,947	0,003***
IFRS dummy*returns a_7	***0,302***	2,170	***0,030****

***: significant at 1% level
**: significant at 5% level
*: significant at 10% level

The results show that conditional conservatism existed in France pre-IFRS. The Basu conservatism coefficient was equal to 0,462. This means that earnings are 4, 6 times more sensitive to bad news than to good news and indicates that costs are taken immediately whereas the recognition of revenues is delayed. No conditional conservatism is observed after the introduction of IFRS. The Basu conservatism coefficient then equals -0,037. Earnings respond more to good news than to bad news in the post-IFRS time period which means that conditional conservatism does not exist. The difference in responsiveness between good and bad news is

negligible. This Basu coefficient is also not significant at all which means there is no significant difference between the responsiveness of earnings to bad news as compared to good news. Conditional conservatism has clearly decreased for France after the introduction of IFRS. The results of Germany do not show a decline in conditional conservatism. The Basu coefficient pre-IFRS is 0,105 whereas the Basu coefficient after the introduction of IFRS is 0,302. The Basu coefficient in the pre-IFRS time period is not significant at all which means no conditional conservatism is observed in this period. In the post-IFRS time period however, the Basu coefficient is significant. This means that conditional conservatism has increased for Germany after the introduction of IFRS. This is not in accordance with prior research (Andre and Filip (2012)) in which a decline in conditional conservatism has been found for Germany in the post-IFRS time period. There are multiple possible explanations for this difference. First of all, the sample used in this thesis is much smaller than the sample used in the research of Andre and Filip (2012). Furthermore, only the largest firms are included in the sample whereas Andre and Filip (2012) include firms with a wide variety of sizes in their sample. Secondly, there is a slight difference in the used measure. Returns are used in the Basu measure as a proxy for news. However, the time frame used in this thesis to calculate returns is not the same as the time frame used in the research of Andre and Filip (2012). Returns are calculated over 12 months in this thesis whereas Andre and Filip (2012) use a time frame of 18 months. This could have an influence on the results. Andre and Filip (2012) use the time frame of 18 months because they want to take possible delays in the announcements of earnings into account. When using a time frame of 18 months, there is more assurance that accounting information is in the public domain. The time frame used in this thesis is also the time frame used by Basu in 1997. Thirdly, there are differences between France and Germany which could explain why firms in Germany experienced a small increase in conditional conservatism and firms in France experienced a large decrease. French GAAP differs more from IFRS than German GAAP does (Bae et al. 2008). This means that French GAAP has a greater distance from IFRS than German GAAP. Therefore there is a big transition for French firms when they change from using French GAAP into using IFRS. This can also be seen by looking at the difference in Basu coefficients pre- and post IFRS. The difference in France is 0,499 whereas the difference in Germany is only 0,197. The difference in Germany is much smaller than in France. This explanation only explains why the difference is smaller but not why France experienced a decrease and Germany an increase. This

could be explained by another important difference between France and Germany. There is more investor protection in Germany than there is in France (La Porta et al. 2000). The investor has more power when investor protection is higher. It could be that firms in Germany reported more conservative under IFRS than under their national GAAP because they were afraid of litigation of investors. Recall that investor litigation is one of the reasons that firms use conservatism. This is especially the case for big firms since they have a lot of shareholders and other investors. IFRS was new at that time and firms did not exactly know how to deal with it. Therefore, it could be that they chose the safe option by not reporting too high earnings to mitigate the risk of litigation in the future. There is also a higher importance of debt in Germany than in France (La Porta et al. 1997). More debt normally means that there are more contracts involved between the firm and its creditors. Contracting is also one of the reasons that firms use conservatism. It could be that big German firms reported more conservatively after the introduction of IFRS to mitigate the risk of problems with creditors. The following tables present the results with the AACF measure.

$$Accit = a0 + a1\,BNit + a2\,CFit + a3\,BNit\;CFit + a4\,IFRSit + a5\,IFRSit\,BNit + a6\,IFRSit\,CFit + a7\,IFRS\,it\,BNit\,CFit + \epsilon it$$

Where:

$IFRS_{it}$ is a dummy variable that takes the value 1 if the year is 2005, 2006 or 2007 and 0 otherwise.

Germany

	Coefficients	T-value	Sig.
a_0	-0,054	-3,543	0,000***
a_1	-0,022	-0,689	0,491
a_2	-0,172	-1,647	0,100
a_3	***0,839***	4,938	***0,000****
a_4	-0,041	-3,093	0,002***
a_5	-0,045	-1,660	0,098*
a_6	-0,127	-1,277	0,202
a_7	***-0,972***	-4,771	***0,000****

The results with the AACF measure are different from the results with the Basu measure. The conditional conservatism coefficient pre-IFRS for Germany equals 0,839 and post IFRS -0,972. This means that conditional conservatism was present in Germany in the pre-IFRS time period but not in the post-IFRS time period. However, these results should be interpreted with some care. This is mainly because of the small sample size which means that there are not much negative cash flows. This could lead to distorted results. The distorted results are clearly visible in the French sample. No conditional conservatism is observed at all, not in the pre-IFRS time period and not in the post-IFRS time period. The AACF measure does not work well in relatively small samples were not much negative cash flows are present. The Basu measure is more appropriate for small samples because negative returns are more common than negative operating cash flows.

France			
	Coefficients	T-value	Sig.
a_0	-0,027	-2,613	0,009***
a_1	-0,036	-1,577	0,115
a_2	-0,187	-2,009	0,045**
a_3	***-0,558***	-2,496	***0,013****
a_4	-0,010	-0,934	0,351
a_5	-0,067	-2,507	0,013**
a_6	-0,587	-6,056	0,000***
a_7	***-0,431***	-2,523	***0,012****

*** : significant at 1% level
** : significant at 5% level
* : significant at 10% level

However, it is interesting to see that the different conditional conservatism measures have different outcomes when using the same sample. Both claim to measure conditional conservatism which should lead to the same outcome. This does not seem to be the case.

6.5 Results hypothesis 3

The goal of hypothesis 3 is to examine whether low conservatism in the post-IFRS time period leads to more value relevance of earnings as compared to high conservatism. There is a clear difference in level of conservatism between the high and low conservatism groups. The high conservatism groups in France and Germany have a Basu measure of respectively 0,559 and 0,533 whereas the low conservatism groups have a Basu measure of respectively -0,104 and -0,268. The list of firms, divided according their level of conditional conservatism, can be found in the appendix. The Easton and Harris model is applied again to determine value relevance of earnings. The tables below present the outcome of hypothesis 3.

France	High conservatism group post-IFRS			
	Coefficients	T-value	R^2	Sig.
a_0	0,005	0,185		0,854
a_1	***1,295***	5,990		0,000**
a_2	***0,036***	0,587		0,558
Full model			***0,18***	0,000**

France	Low conservatism group post-IFRS			
	Coefficients	T-value	R^2	Sig.
a_0	0,132	3,420		0,001***
a_1	***0,559***	3,493		0,001**
a_2	***0,146***	0,806		0,421
Full model			***0,183***	0,000***

Germany	High conservatism group post-IFRS			
	Coefficients	T-value	R^2	Sig.
a_0	0,173	5,416		0,000***
a_1	***0,248***	2,350		0,020**
a_2	***-0,122***	-1,981		0,049**
Full model			***0,036***	0,034**

Germany	Low conservatism group post-IFRS			
	Coefficients	T-value	R^2	Sig.
a_0	0,152	4,165		0,000***
a_1	***0,515***	4,181		0,000***
a_2	***0,162***	1,567		0,117
Full model			***0,125***	0,000***

***: significant at 1% level
**: significant at 5% level
*: significant at 10% level

The results for France show that low conservatism in the post-IFRS time period does not lead to higher value relevance of earnings as compared to high conservatism. The earnings response coefficient for the low conservatism group appears to be 0,705 (0,559+0,146) whereas the earnings response coefficient of the high conservatism group is 1,331 (1,295+0,036). The earnings per share variable is significant for both the high and the low conservatism group at the 1% level. The variable "change in earnings per share" is not significant at all for both the high and the low conservatism group. This could be due to the small sample size. The full model however is significant at the 1% level for both high and low conservatism. The low conservatism sample does have a slightly higher R^2 than the high conservatism sample. However, the difference is negligible. The results for Germany do seem to indicate that low conservatism in the post-IFRS time period leads to higher value relevance of earnings. The low conservatism sample appears to have an earnings response coefficient of 0,667 (0,515+0,152) whereas the high

conservatism sample has an earnings response coefficient of 0,126 (0,248+-0,122). All the variables are significant at the 5% level except the variable "change in earnings per share" for the low conservatism group. The full model is also significant for both groups at the 5% level. The R^2 of the low conservatism group (0,125) is also much higher than the R^2 of the high conservatism group (0,036). Hypothesis 3 is thus rejected in the case of France but confirmed in the case of Germany.

6.6 Results hypothesis 4

Hypothesis 4 examines whether firms with low conservatism will have a greater increase (or smaller decrease) in value relevance of earnings as compared to firms with high conservatism. Value relevance of earnings is measured in this hypothesis by using the R^2 of the Easton and Harris model.

France	**High conservatism group**					
Year	2002	2003	2004	2005	2006	2007
R^2	0,302	0,250	0,378	0,178	0,160	0,269
Sig.	0,000***	0,000***	0,000***	0,003***	0,005***	0,000***

$Valrel = a_0 + B^* TIME + \epsilon$ ***B=-0,018 sig.= 0,406***

France	**Low conservatism group**					
Year	2002	2003	2004	2005	2006	2007
R^2	0,133	0,108	0,208	0,706	0,013	0,250
Sig.	0,014**	0,033**	0,001***	0,000***	0,677	0,000***

$Valrel = a_0 + B^* TIME + \epsilon$ ***B=0,023 sig.= 0,741***

Germany	**High conservatism group**					
Year	2002	2003	2004	2005	2006	2007
R^2	0,232	0,163	0,210	0,029	0,124	0,134
Sig.	0,000***	0,005***	0,001***	0,409	0,019**	0,013**

$Valrel = a_0 + B^* TIME + \epsilon$ ***B=-0,023 sig.= 0,224***

Germany	Low conservatism group					
Year	2002	2003	2004	2005	2006	2007
R^2	0,080	0,170	0,696	0,352	0,123	0,059
Sig.	0,082*	0,004***	0,000***	0,000***	0,019**	0,162

$Valrel = a_0 + B^* TIME + \epsilon$ ***B=-0,017 sig.= 0,807***

***: significant at 1% level

**: significant at 5% level

*: significant at 10% level

The R^2s in the high conservatism sample of France are significant at the 1% level for all the years studied. This is not the case in the low conservatism sample. These are all significant at the 1% level except for the years 2002 and 2003 (significant at the 5% level) and 2006 (not significant at all). The results of the regression indicate that low conservatism firms have a higher increase in value relevance of earnings than high conservatism firms in France. The coefficient of the low conservatism group is 0,023 whereas the coefficient of the high conservatism group is -0,018. The high conservatism group thus shows a decrease of value relevance throughout the years. However, these results should be interpreted with care because both coefficients are not significant at all. The reason that the results are not significant could be due to the small number of years used. The results for Germany are the same as for France. The R^2s in the high conservatism sample are all significant at the 5% level except the year 2005, which is not significant at all. The R^2s in the low conservatism sample are significant at the 5% level for the years 2003, 2004, 2005 and 2006. The R^2 in the year 2002 is significant at the 10% level and the R^2 in the year 2007 is not significant at all. Equal to France, the coefficient of the low conservatism group (-0,017) is higher than the coefficient of the high conservatism group (-0,023). The coefficients are not significant at all. There is some evidence in both countries that firms with low conservatism experience a higher increase (or lower decrease) in value relevance of earnings as compared to highly conservative firms.

6.7 Conclusion

The results of this master thesis are discussed in this section. Using the Easton and Harris model, there seems to be an increase in value relevance of earnings after the introduction of IFRS for France but not for Germany. However, when using a regression of stock prices on earnings per share as a proxy for value relevance of earnings, there is an increase in value relevance for both France and Germany in the post-IFRS time period. The introduction of IFRS is also accompanied by a decrease in conditional conservatism when using the Basu formula for France but not for Germany. Germany seems to have an increase in conditional conservatism. This result is contradicting with prior literature. The third hypothesis shows that firms with low conservatism really experience higher value relevance of earnings but only in the case of Germany. There is no clear difference in value relevance of earnings between high and low conservative firms in France. There is some evidence found in the last hypothesis that firms with low conservatism experience a higher increase (or lower decrease) in value relevance of earnings than high conservatism firms in both countries. These results should be interpreted with care because they are not significant.

7 Conclusion

The objective of this master thesis was to examine the relationship between conditional conservatism and value relevance of earnings after the introduction of IFRS. Conservatism has been described in the literature as "the asymmetrical timeliness of earnings". Bad news is recognized much faster in the profit and loss account than good news. A distinction can be made between conditional and unconditional conservatism. The first type of conservatism is news dependent whereas the latter one is news independent and exists already at the inception of assets and liabilities. The focus of this master thesis has been on conditional conservatism. This is because the literature has shown that this type of conservatism has decreased after the introduction of IFRS. First of all, the results of this thesis show that value relevance has indeed increased after the mandatory adoption of IFRS when using a regression of stock prices on earnings per share. This is not the case when using the Easton and Harris model. When using the Easton and Harris model, there is an increase in value relevance for France but not for Germany. IFRS is more fair value and principle based than most national GAAPs. Therefore a decrease in conditional conservatism is expected. Two proxies have been used to determine whether conditional conservatism has decreased post-IFRS. The Basu coefficient has clearly decreased in the case of France but not in the case of Germany. The result for Germany is not in accordance with prior literature. This conflicting result could arise because of the small sample size and the different time frame used in this thesis. Other explanations are: French GAAP differs more from IFRS than German GAAP, more investor protection in Germany and higher importance of debt in Germany. The AACF measure has also been used to determine conditional conservatism. The results when using this measure are clearly different from the results when using the Basu measure. This is due to the fact that negative operating cash flows, which are used in the AACF measure, are not very common. Therefore the AACF measure is not very appropriate to use in small sample sizes. However, it is still interesting to see that two measures which claim to measure conditional conservatism result in different outcomes. A suggestion for further research would therefore be to develop a robust firm-specific measure of conditional conservatism which can be used in countries outside the United States. Increased use of conservatism has been mentioned in the literature as one of the causes of decreased value relevance in the United States. Balachandran and Mohanram (2011) do not find evidence for this claim. The results of this

master thesis show that there is no clear relationship between conditional conservatism and value relevance of earnings in the case of France. In Germany however, low conservatism firms show higher value relevance of earnings as compared to high conservatism firms. The low conservatism firms also experience a higher increase (or smaller decrease) in value relevance of earnings. This holds for both Germany and France. These results are of importance for standard setters. If standard setters would only be interested in the value relevance of earnings, the results suggest that standard setters should make standards that decrease the level of conditional conservatism. By making less conservative accounting standards in the future, the standard setters could increase the value relevance of earnings. However, more research is needed on this topic. A suggestion for further research would therefore be to examine the relationship between conditional conservatism and value relevance in other countries. It is also interesting to examine why this relationship differs across countries and to identify the moderators that play a role in this relationship. This thesis has only focused on conditional conservatism. A suggestion for future research is to examine the relationship between unconditional conservatism and value relevance. It could be that a negative relationship exists between these 2 variables. This is essential information for standard setters when creating new accounting standards.

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APPENDIX

APPENDIX A: SPSS OUTPUT HYPOTHESIS 1

Model Summary (France pre-IFRS)

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.333[a]	.111	.107	.460291407236282

a. Predictors: (Constant), Change in earnings per share (deflated by Stock Price), Earnings per share (deflated by Stock Price)

ANOVA[a] (France pre-IFRS)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	12.355	2	6.177	29.156	.000[b]
	Residual	99.154	468	.212		
	Total	111.509	470			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Coefficients [a] (France pre-IFRS)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.093	.022		4.274	.000
	Earnings per share (deflated by Stock Price)	.271	.055	.228	4.912	.000
	Change in earnings per share (deflated by Stock Price)	.260	.068	.178	3.839	.000

a. Dependent Variable: Returns

Model Summary (France post-IFRS)

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.416[a]	.173	.170	.395503715771123

a. Predictors: (Constant), Change in earnings per share (deflated by Stock Price), Earnings per share (deflated by Stock Price)

ANOVA[a] (France post-IFRS)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	15.306	2	7.653	48.926	.000[b]
	Residual	73.050	467	.156		
	Total	88.356	469			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Coefficients [a] (France post-IFRS)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.103	.020		5.217	.000
	Earnings per share (deflated by Stock Price)	.725	.091	.396	7.948	.000
	Change in earnings per share (deflated by Stock Price)	.052	.071	.036	.728	.467

a. Dependent Variable: Returns

Model Summary (Germany pre-IFRS)

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.380[a]	.144	.140	.728023274052966

a. Predictors: (Constant), Change in earnings per share (deflated by Stock Price), Earnings per share (deflated by Stock Price)

ANOVA[a] (Germany pre-IFRS)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	41.735	2	20.867	39.371	.000[b]
	Residual	248.048	468	.530		
	Total	289.783	470			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Coefficients [a] (Germany pre-IFRS)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.142	.034		4.186	.000
	Earnings per share (deflated by Stock Price)	.159	.082	.097	1.929	.054
	Change in earnings per share (deflated by Stock Price)	.362	.057	.319	6.338	.000

a. Dependent Variable: Returns

Model Summary (Germany post-IFRS)

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.231[a]	.053	.049	.448796062724671

a. Predictors: (Constant), Change in earnings per share (deflated by Stock Price), Earnings per share (deflated by Stock Price)

ANOVA[a] (Germany post-IFRS)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	5.321	2	2.661	13.209	.000[b]
	Residual	94.264	468	.201		
	Total	99.585	470			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Coefficients [a] (Germany post-IFRS)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.193	.021		9.070	.000
	Earnings per share (deflated by Stock Price)	.396	.078	.243	5.062	.000
	Change in earnings per share (deflated by Stock Price)	-.049	.053	-.044	-.925	.355

a. Dependent Variable: Returns

Regression of stock prices on earnings per share:

Model Summary (France pre-IFRS)

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.904[a]	.817	.817	135.336773829667400

a. Predictors: (Constant), Earnings per share

ANOVA[a] (France pre-IFRS)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	38353170.968	1	38353170.968	2093.966	.000[b]
	Residual	8590223.862	469	18316.042		
	Total	46943394.830	470			

a. Dependent Variable: StockPrice

b. Predictors: (Constant), Earnings per share

Coefficients [a] (France pre-IFRS)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	21.012	6.299		3.336	.001
	Earnings per share	8.574	.187	.904	45.760	.000

a. Dependent Variable: Stock Price

Model Summary (France post-IFRS)

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.950[a]	.902	.901	154.709910059870820

a. Predictors: (Constant), Earnings per share

ANOVA[a] (France post-IFRS)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	102748846.233	1	102748846.233	4292.800	.000[b]
	Residual	11201653.135	468	23935.156		
	Total	113950499.368	469			

a. Dependent Variable: StockPrice

b. Predictors: (Constant), Earnings per share

Coefficients [a] (France post-IFRS)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-45.470	7.472		-6.085	.000
	Earnings per share	24.222	.370	.950	65.519	.000

a. Dependent Variable: Stock Price

Model Summary (Germany pre-IFRS)

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.691[a]	.477	.476	22.472690978047560

a. Predictors: (Constant), Earnings per share

ANOVA[a] (Germany pre-IFRS)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	216188.854	1	216188.854	428.078	.000[b]
	Residual	236855.243	469	505.022		
	Total	453044.097	470			

a. Dependent Variable: StockPrice

b. Predictors: (Constant), Earnings per share

Coefficients [a] (Germany pre-IFRS)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	9.905	1.090		9.085	.000
	Earnings per share	7.064	.341	.691	20.690	.000

a. Dependent Variable: Stock Price

Model Summary (Germany post-IFRS)

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.801[a]	.641	.640	36.844816175583890

a. Predictors: (Constant), Earnings per share

ANOVA[a] (Germany post-IFRS)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1137258.627	1	1137258.627	837.735	.000[b]
	Residual	636686.485	469	1357.540		
	Total	1773945.111	470			

a. Dependent Variable: StockPrice

b. Predictors: (Constant), Earnings per share

Coefficients [a] (Germany post-IFRS)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	10.336	1.857		5.566	.000
	Earnings per share	10.255	.354	.801	28.944	.000

a. Dependent Variable: Stock Price

APPENDIX B: SPSS OUTPUT HYPOTHESIS 2

Basu measure

Model Summary France pre-IFRS

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.331[a]	.110	.104	.386552515674062

a. Predictors: (Constant), dummy returns, Returns , dummy

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	8.612	3	2.871	19.211	.000[b]
	Residual	69.780	467	.149		
	Total	78.392	470			

a. Dependent Variable: Earnings per share (deflated by StockPrice)

b. Predictors: (Constant), dummy returns, Returns , dummy

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.131	.030		4.326	.000
	dummy	.006	.052	.008	.124	.902
	Returns	.125	.052	.149	2.396	.017
	dummy returns	.462	.132	.220	3.487	.001

a. Dependent Variable: Earnings per share (deflated by StockPrice)

Model Summary France post-IFRS

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.417[a]	.174	.168	.216146531445438

a. Predictors: (Constant), dummy_returns, Returns , dummy

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	4.577	3	1.526	32.658	.000[b]
	Residual	21.771	466	.047		
	Total	26.349	469			

a. Dependent Variable: Earnings per share (deflated by StockPrice)

b. Predictors: (Constant), dummy_returns, Returns , dummy

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.046	.015		3.036	.003
	dummy	.016	.032	.032	.515	.607
	Returns	.240	.028	.440	8.712	.000
	dummy_returns	-.037	.137	-.016	-.270	.787

a. Dependent Variable: Earnings per share (deflated by StockPrice)

Model Summary Germany pre-IFRS

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.273[a]	.075	.069	.463267457835693

a. Predictors: (Constant), dummy returns, Returns, dummy

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	8.082	3	2.694	12.553	.000[b]
	Residual	100.226	467	.215		
	Total	108.308	470			

a. Dependent Variable: Earnings per share (deflated by StockPrice)

b. Predictors: (Constant), dummy returns, Returns, dummy

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.036	.038		.955	.340
	dummy	-.038	.066	-.039	-.567	.571
	Returns	.128	.037	.209	3.491	.001
	dummy returns	.105	.134	.053	.787	.432

a. Dependent Variable: Earnings per share (deflated by StockPrice)

Model Summary Germany post-IFRS

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.248[a]	.062	.056	.274423243704720

a. Predictors: (Constant), dummy returns, Returns, dummy

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	2.313	3	.771	10.239	.000[b]
	Residual	35.169	467	.075		
	Total	37.482	470			

a. Dependent Variable: Earnings per share (deflated by StockPrice)

b. Predictors: (Constant), dummy returns, Returns, dummy

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.056	.021		2.631	.009
	dummy	.032	.042	.052	.762	.447
	Returns	.107	.036	.175	2.947	.003
	dummy returns	.302	.139	.144	2.170	.030

a. Dependent Variable: Earnings per share (deflated by StockPrice)

AACF measure

Model Summary Germany pre-IFRS

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.265[a]	.070	.064	.196927769529042

a. Predictors: (Constant), dum, dummy, Operating cash flow (deflated by total assets)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.363	3	.454	11.713	.000[b]
	Residual	18.111	467	.039		
	Total	19.473	470			

a. Dependent Variable: Accruals (deflated by total assets)

b. Predictors: (Constant), dum, dummy, Operating cash flow (deflated by total assets)

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.054	.015		-3.543	.000
	dummy	-.022	.032	-.037	-.689	.491
	Operating cash flow (deflated by total assets)	-.172	.105	-.113	-1.647	.100
	dum	.839	.170	.317	4.938	.000

a. Dependent Variable: Accruals (deflated by total assets)

Model Summary Germany post-IFRS

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.299[a]	.089	.083	.160771915882688

a. Predictors: (Constant), dum, dummy, Operating cash flow (deflated by total assets)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.181	3	.394	15.229	.000[b]
	Residual	12.071	467	.026		
	Total	13.252	470			

a. Dependent Variable: Accruals (deflated by total assets)

b. Predictors: (Constant), dum, dummy, Operating cash flow (deflated by total assets)

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.041	.013		-3.093	.002
	dummy	-.045	.027	-.094	-1.660	.098
	Operating cash flow (deflated by total assets)	-.127	.099	-.080	-1.277	.202
	dum	-.972	.204	-.286	-4.771	.000

a. Dependent Variable: Accruals (deflated by total assets)

Model Summary France pre-IFRS

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.203[a]	.041	.035	.102512715206890

a. Predictors: (Constant), dum, dummy, Operating cashflow (deflated by total assets)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.211	3	.070	6.688	.000[b]
	Residual	4.908	467	.011		
	Total	5.118	470			

a. Dependent Variable: Accruals (deflated by total assets)

b. Predictors: (Constant), dum, dummy, Operating cashflow (deflated by total assets)

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.027	.010		-2.613	.009
	dummy	-.036	.023	-.096	-1.577	.115
	Operating cashflow (deflated by total assets)	-.187	.093	-.127	-2.009	.045
	dum	-.558	.224	-.154	-2.496	.013

a. Dependent Variable: Accruals (deflated by total assets)

Model Summary France post-IFRS

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.416[a]	.173	.167	.126925362876647

a. Predictors: (Constant), dum, dummy, Operating cashflow (deflated by total assets)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.568	3	.523	32.441	.000[b]
	Residual	7.507	466	.016		
	Total	9.075	469			

a. Dependent Variable: Accruals (deflated by total assets)

b. Predictors: (Constant), dum, dummy, Operating cashflow (deflated by total assets)

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.010	.011		-.934	.351
	dummy	-.067	.027	-.124	-2.507	.013
	Operating cashflow (deflated by total assets)	-.587	.097	-.362	-6.056	.000
	dum	-.431	.171	-.142	-2.523	.012

a. Dependent Variable: Accruals (deflated by total assets)

APPENDIX C: SPSS OUTPUT HYPOTHESIS 3

Model Summary France high conservatism group

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.352[a]	.124	.117	.348442957051 7

a. Predictors: (Constant), dummy returns, dummy, Returns

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	6.399	3	2.133	17.568	.000[b]
	Residual	45.287	373	.121		
	Total	51.686	376			

a. Dependent Variable: Earnings per share (deflated by StockPrice)

b. Predictors: (Constant), dummy returns, dummy, Returns

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.064	.034		1.901	.058
	dummy	.075	.051	.101	1.466	.144
	Returns	.135	.058	.168	2.309	.021
	dummy returns	.559	.135	.283	4.133	.000

a. Dependent Variable: Earnings per share (deflated by StockPrice)

Model Summary France low conservatism group

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.381[a]	.145	.138	.319176361609 681

a. Predictors: (Constant), dummy returns, Returns , dummy

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	6.451	3	2.150	21.109	.000[b]
	Residual	38.101	374	.102		
	Total	44.552	377			

a. Dependent Variable: Earnings per share (deflated by StockPrice)

b. Predictors: (Constant), dummy returns, Returns , dummy

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.096	.025		3.860	.000
	dummy	-.040	.048	-.056	-.845	.399
	Returns	.255	.040	.370	6.410	.000
	dummy returns	-.104	.164	-.041	-.631	.528

a. Dependent Variable: Earnings per share (deflated by StockPrice)

Model Summary Germany high conservatism group

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.263[a]	.069	.062	.38603090759247

a. Predictors: (Constant), dummy_returns, Returns, dummy

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	4.129	3	1.376	9.236	.000[b]
	Residual	55.733	374	.149		
	Total	59.863	377			

a. Dependent Variable: Earnings per share (deflated by StockPrice)

b. Predictors: (Constant), dummy_returns, Returns, dummy

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.100	.035		2.882	.004
	dummy	-.006	.059	-.007	-.099	.921
	Returns	-.036	.036	-.065	-.988	.324
	dummy_returns	.533	.131	.291	4.062	.000

a. Dependent Variable: Earnings per share (deflated by StockPrice)

Model Summary Germany low conservatism group

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.422[a]	.178	.172	.427580214696717

a. Predictors: (Constant), dummy returns, Returns, dummy

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	14.824	3	4.941	27.028	.000[b]
	Residual	68.376	374	.183		
	Total	83.201	377			

a. Dependent Variable: Earnings per share (deflated by StockPrice)

b. Predictors: (Constant), dummy returns, Returns, dummy

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.052	.038		-1.369	.172
	dummy	.022	.067	.023	.327	.744
	Returns	.362	.046	.495	7.811	.000
	dummy returns	-.268	.157	-.118	-1.712	.088

a. Dependent Variable: Earnings per share (deflated by StockPrice)

Model Summary France high conservatism group value relevance post-IFRS

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.424[a]	.180	.171	.290801987481079

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	3.432	2	1.716	20.293	.000[b]
	Residual	15.645	185	.085		
	Total	19.077	187			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.005	.025		.185	.854
	Earnings per share (deflated by StockPrice)	1.295	.216	.412	5.990	.000
	Change in earnings per share (deflated by StockPrice)	.036	.061	.040	.587	.558

a. Dependent Variable: Returns

Model Summary France low conservatism group value relevance post-IFRS

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.428[a]	.183	.175	.493499931979580

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	10.176	2	5.088	20.891	.000[b]
	Residual	45.299	186	.244		
	Total	55.475	188			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.132	.039		3.420	.001
	Earnings per share (deflated by StockPrice)	.559	.160	.361	3.493	.001
	Change in earnings per share (deflated by StockPrice)	.146	.181	.083	.806	.421

a. Dependent Variable: Returns

Model Summary Germany high conservatism group value relevance post-IFRS

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.189[a]	.036	.025	.432562285332729

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.291	2	.645	3.449	.034[b]
	Residual	34.802	186	.187		
	Total	36.093	188			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.173	.032		5.416	.000
	Earnings per share (deflated by StockPrice)	.248	.105	.183	2.350	.020
	Change in earnings per share (deflated by StockPrice)	-.122	.062	-.154	-1.981	.049

a. Dependent Variable: Returns

Model Summary Germany low conservatism group value relevance post-IFRS

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.353[a]	.125	.115	.486111648011532

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	6.262	2	3.131	13.250	.000[b]
	Residual	43.953	186	.236		
	Total	50.215	188			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.152	.037		4.165	.000
	Earnings per share (deflated by StockPrice)	.515	.123	.301	4.181	.000
	Change in earnings per share (deflated by StockPrice)	.162	.103	.114	1.576	.117

a. Dependent Variable: Returns

APPENDIX D: LIST OF FIRMS DIVIDED ACCORDING THEIR LEVEL OF CONDITIONAL CONSERVATISM

FRANCE

Company Name	good news	bad news	conservatism measure
MANITOU B F	0,085	7,425	7,34
HAVAS	-4,738	0,035	4,773
BULL SA	0,076	4,465	4,389
GENESYS SA	-1,783	1,377	3,16
AVIATION LATECOERE	0,314	3,01	2,696
BONGRAIN SA	0,156	2,526	2,37
WENDEL	0,208	2,458	2,25
VICAT SA	-0,236	1,999	2,235
RUBIS & CIE	-0,032	2,124	2,156
ETABLISSEMENTS MAUREL & PROM	-0,013	1,544	1,557
FINANCIERE DE L'ODET SA	-0,056	1,464	1,52
ADVINI	0,083	1,511	1,428
ROBERTET SA	-0,081	1,284	1,365
GRAND MARNIER	-0,123	1,192	1,315
DEVOTEAM SA	-0,317	0,79	1,107
GROUPE GASCOGNE	0,685	1,575	0,89
FRANCE TELECOM	0,091	0,931	0,84
CHARGEURS INTERNATIONAL SA	1,06	1,894	0,834
BACCARAT	-0,03	0,737	0,767

CAP GEMINI SA	-0,589	0,154	0,743
LE BELIER SA	0,881	1,614	0,733
MONTUPET SA	-0,57	0,088	0,658
ALCATEL-LUCENT	-0,251	0,406	0,657
GROUPE OPEN SA	0,306	0,845	0,539
BOIRON SA	0,013	0,51	0,497
GROUPE GORGE	1,513	1,974	0,461
HIGH CO SA	0,53	0,962	0,432
RADIALL SA	-0,115	0,301	0,416
SECHE ENVIRONNEMENT SA	-0,2	0,163	0,363
SECURIDEV SA	-0,002	0,327	0,329
ALTRAN TECHNOLOGIES SA	-0,195	0,046	0,241
RHODIA	0,125	0,365	0,24
GFI INFORMATIQUE SA	-0,095	0,109	0,204
DANE-ELEC MEMORY SA	0,004	0,204	0,2
GENERALE DE SANTE	-0,132	0,065	0,197
THALES	-0,069	0,126	0,195
PUBLICIS GROUPE SA	-0,125	0,066	0,191
BRICORAMA SA	-0,052	0,117	0,169
ATOS	-0,215	-0,047	0,168
TECHNICOLOR SA	-0,158	-0,003	0,155
GROUPE CENTRE RECHERCHES IND	0,143	0,295	0,152
IMERYS	-0,048	0,086	0,134
CEGEDIM	0,144	0,266	0,122
LVMH MOET HENNESSY L VUITTON	-0,027	0,09	0,117
SCHNEIDER ELECTRIC SA	0,102	0,206	0,104
OBERTHUR TECHNOLOGIES	0,038	0,139	0,101

CIE GEN DES ETABLIS MICHELIN	0,037	0,125	0,088
CLARINS SA	-0,121	-0,065	0,056
SOPRA GROUP	0,013	0,055	0,042
BIC SOCIETE	0,081	0,116	0,035
SPIR COMMUNICATION	0,042	0,065	0,023
TELEPERFORMANCE	0,078	0,095	0,017
DASSAULT SYSTEMS SA	0,017	0,033	0,016
SOCIETE FINANCIERE DE COMM	0,042	0,058	0,016
EUROFINS SCIENTIFIC	0,029	0,045	0,016
GROUPE STERIA	0,028	0,036	0,008
PPR SA	-0,083	-0,08	0,003
ETABLISSEMENTS GANTOIS		8,403	
PCAS		0,238	
NSC GROUPE SA		0,134	
VALEO SA		0,057	
SYLIS SA		0,052	
GROUPE ONET	-0,899		
EIFFAGE	-0,796		
VIVENDI	-0,792		
STEF	-0,382		
CIE PARISIENNE DE CHAUFFAGE	-0,165		
GROUPE PSB INDUSTRIES	-0,163		
L'AIR LIQUIDE SA	-0,116		
CS COMMUNICATION & SYSTEMES	-0,116		
SAMSE	-0,094		
VRANKEN-POMMERY	-0,055		

MONOPOLE SA			
COLAS SA	-0,029		
ERAMET	-0,017		
TECHNIP SA	-0,016		
DANONE	-0,002		
LISI	0,007		
BOURBON SA	0,022		
RENAULT SA	0,04		
MAISONS FRANCE CONFORT	0,047		
DISTRIBORG	0,047		
GL EVENTS	0,048		
NORBERT DENTRESSANGLE	0,064		
LAFARGE SA	0,065		
CIMENTS FRANCAIS	0,073		
CGG	0,079		
TOUAX SA	0,083		
VIRBAC SA	0,086		
HAULOTTE GROUP	0,087		
ESSILOR INTERNATIONAL SA	0,094		
CAMAIEU SA	0,096		
GROUPE GO SPORT	0,106		
GUERBET SA	0,109		
INGENICO SA	0,117		
BRICODEAL SA	0,121		
BURELLE SA	0,126		
SAINT-GOBAIN (CIE DE)	0,128		
JACQUET METALS SA	0,133		
PLASTIC OMNIUM SA	0,134		

FLEURY MICHON	0,139		
FROMAGERIES BEL SA	0,152		
SYNERGIE SA	0,2		
IMS-INTL METAL SERVICE SA	0,206		
GROUPE GUILLIN	0,215		
VM MATERIAUX SA	0,239		
GEVELOT SA	0,249		
BELVEDERE SA	0,268		
OTOR SA	0,444		
INDUS ET FINANC D'ENTREPRISE	0,49		
VINCI SA	0,536		
SEB SA	0,88		
DELACHAUX SA	0,903		
VALLOUREC SA	0,957		
ROUGIER SA	1,128		
TOTAL SA	1,308		
BUSINESS OBJECTS SA	0,018	0,011	-0,007
HYPARLO SA	-0,16	-0,169	-0,009
TESSI	0,128	0,117	-0,011
PROSODIE SA	0,089	0,075	-0,014
SPERIAN PROTECTION	-0,095	-0,118	-0,023
ALTEN SA	0,056	0,029	-0,027
GROUPE NEURONES	-0,011	-0,039	-0,028
TELEVISION FRANCAISE 1	0,039	0,005	-0,034
NICOX SA	-0,015	-0,051	-0,036
HERMES INTERNATIONAL	-0,033	-0,084	-0,051
NETWORK RELATED SERVICES	0,196	0,143	-0,053

LINEDATA SERVICES	0,061	-0,013	-0,074
GAUMONT SA	-0,3	-0,376	-0,076
FONCIERE EURIS	-0,081	-0,21	-0,129
CNIM-CONTRUCTIONS INDUST MED	-0,005	-0,135	-0,13
CEGID GROUP	0,089	-0,053	-0,142
GUYENNE ET GASCOGNE SA	0,02	-0,14	-0,16
SEQUANA	0,046	-0,119	-0,165
SAFRAN SA	1,242	1,015	-0,227
WAVECOM SA	0,044	-0,201	-0,245
EXACOMPTA-CLAIREFONTAINE SA	0,376	0,118	-0,258
FAURECIA SA	-0,794	-1,103	-0,309
MR BRICOLAGE SA	0,055	-0,255	-0,31
GL TRADE SA	0,233	-0,082	-0,315
SUEZ	0,077	-0,245	-0,322
IPSOS SA	0,382	-0,001	-0,383
ETAM DEVELOPPEMENT SCA	-0,192	-1,019	-0,827
DASSAULT AVIATION SA	0,027	-0,871	-0,898
LECTRA	0,039	-0,859	-0,898
GEODIS	0,627	-0,326	-0,953
UNIBEL	0,614	-0,435	-1,049
FINATIS SA	1,346	0,268	-1,078
BOLLORE	0,08	-1,178	-1,258
INTERPARFUMS	0,463	-0,796	-1,259
PEUGEOT SA	0,643	-0,767	-1,41
L'OREAL SA	0,016	-1,419	-1,435
NEXANS	0,074	-3,237	-3,311
TEAMLOG	2,976	-1,532	-4,508

ESSO SAF	0,301	-4,43	-4,731
JC DECAUX SA	-0,012	-5,665	-5,653
DYNACTION SA	13,736	-0,383	-14,119
OSIATIS SA		-0,176	

GERMANY

Company Name	good news	bad news	conservatism measure
KUNERT AG	-22,287	-0,145	22,142
MEDIGENE AG	-10,073	0,128	10,201
FIELMANN AG	-0,162	8,857	9,019
INDUS HOLDING AG	0,009	3,234	3,225
QSC AG	-0,237	2,914	3,151
CLOPPENBURG AUTOMOBIL AG	0,668	3,619	2,951
ZAPF CREATION AG	-1,862	0,349	2,211
TA TRIUMPH-ADLER AG	-1,255	0,754	2,009
MENSCH & MASCHINE SOFTWARE	-0,575	1,108	1,683
DEUFOL SE	-1,552	0,111	1,663
TOMORROW FOCUS AG	-0,017	1,489	1,506
KAMPA AG	-0,047	1,401	1,448
HOEFT & WESSEL AG	-0,014	1,302	1,316
COMPUTERLINKS AG	0,073	1,328	1,255
PNE WIND AG	-0,446	0,619	1,065
WINKLER & DUENNEBIER AG	0,265	1,316	1,051
MS INDUSTRIE AG	0,209	1,143	0,934
DUERR AG	-1,005	-0,11	0,895
AUTANIA AG	-0,012	0,862	0,874

DEUTSCHE TELEKOM	0,196	1,057	0,861
BEIERSDORF AG	0,028	0,87	0,842
DEAG-DEUTSCHE ENTERTAINMENT	-0,624	0,168	0,792
HANSA GROUP AG	-0,202	0,427	0,629
3U TELECOM AG	0,063	0,59	0,527
PIRONET NDH AG	0,03	0,545	0,515
RUECKER AG	-0,029	0,477	0,506
WIRECARD AG	0,237	0,736	0,499
LEIFHEIT AG	-0,32	0,163	0,483
TECHNOTRANS AG	-0,392	0,071	0,463
NEMETSCHEK AG	0,072	0,49	0,418
GILDEMEISTER AG	-0,061	0,339	0,4
VBH HOLDING AG	-0,055	0,327	0,382
USU SOFTWARE AG	-0,656	-0,284	0,372
STADA ARZNEIMITTEL AG	-0,133	0,189	0,322
BIJOU BRIGITTE MOD ACCESS AG	-0,126	0,186	0,312
REPLY DEUTSCHLAND AG	-0,287	-0,008	0,279
WASGAU PRODUKTIONS & HANDELS	-0,007	0,2	0,207
SUSS MICROTEC AG	-0,247	-0,075	0,172
BIOTEST AG	0,229	0,39	0,161
MUEHLBAUER HOLDING AG&CO	-0,035	0,088	0,123
OHB AG	0,029	0,14	0,111

HYRICAN INFORMATIONSSYSTME	0,034	0,134	0,1
BMW-BAYER MOTOREN WERKE AG	-0,018	0,081	0,099
ALTANA AG	0,302	0,369	0,067
TAKKT AG	0,017	0,081	0,064
LINOS AG	0,309	0,34	0,031
VIVANCO GRUPPE AG	-0,41	-0,379	0,031
SARTORIUS AG	0,055	0,072	0,017
METRO AG	0,001	0,007	0,006
HEIDELBERGCEMENT AG	0,191	0,193	0,002
CONSTANTIN MEDIEN AG		0,364	
BEATE UHSE AG		0,156	
MEDION AG		0,141	
ELMOS SEMICONDUCTOR AG		0,083	
JENOPTIK AG		0,026	
COMPUGROUP MEDICAL AKTIEN	-1,438		
ROHWEDDER AG	-1,251		
D&S EUROPE AG	-0,997		
K&S AG	-0,57		
CREATON AG	-0,363		
KONTRON AG	-0,263		
ITELLIGENCE AG	-0,165		
HENKEL AG & CO KGAA	-0,163		

SOFTWARE AG	-0,125		
JUNGHEINRICH AG	-0,119		
ONVISTA AG	-0,079		
VEREINIGTE SCHMIRGEL	-0,067		
HOCHTIEF AG	-0,002		
AUDI AG	0,017		
PROSIEBEN SAT 1 MEDIA AG	0,024		
AS CREATION TAPETEN AG	0,026		
SCA HYGIENE PRODUCTS SE	0,035		
VOSSLOH AG	0,038		
SEDO HOLDING AG	0,039		
RATIONAL AG	0,049		
FRAPORT AG FRANKFURT AIRPORT	0,054		
DIS-DEUTSCHER INDUSTRIE SERV	0,054		
BETA SYSTEMS SOFTWARE AG	0,054		
KSB AG	0,073		
LINDE AG	0,074		
SCHWARZ PHARMA AG	0,078		
CONTINENTAL AG	0,09		
UZIN UTZ AG	0,102		
PUMA SE	0,103		
PROGRESS-WERK OBERKIRCH AG	0,105		

CONSTANTIN FILM AG	0,11		
RHOEN-KLINIKUM AG	0,114		
BASF SE	0,133		
UNITED INTERNET AG	0,148		
LEONI AG	0,153		
MERCK KGAA	0,168		
BAYER AG	0,179		
FRESENIUS SE & CO KGAA	0,182		
CELESIO AG	0,205		
FRESENIUS MEDICAL CARE AG&CO	0,219		
SALZGITTER AG	0,414		
E.ON SE	0,442		
HAWESKO HOLDING AG	0,787		
SOLARWORLD AG	1,206		
NORDDEUTSCHE STEINGUT AG	0,547	0,545	-0,002
BOEWE SYSTEC AG	0,027	0,018	-0,009
FUNKWERK AG	0,064	0,052	-0,012
AUGUSTA TECHNOLOGIE AG	-0,082	-0,096	-0,014
DEUTSCHE LUFTHANSA AG	-0,058	-0,088	-0,03
SAP AG	0,153	0,123	-0,03
BECHTLE AG	0,09	0,049	-0,041
CENTROTEC SUSTAINABLE AG	0,144	0,078	-0,066
IDS SCHEER AG	0,039	-0,029	-0,068

CTS EVENTIM AG	0,179	0,104	-0,075
DATA MODUL AG	-0,001	-0,081	-0,08
GFK AG	0,088	0,004	-0,084
KOENIG & BAUER AG	-0,032	-0,124	-0,092
MASTERFLEX SE	0,078	-0,021	-0,099
PSI AG	-0,099	-0,204	-0,105
INTERTAINMENT AG	-0,2	-0,31	-0,11
HUGO BOSS AG	0,144	0,009	-0,135
MDB AG	1,758	1,596	-0,162
SYZYGY AG	0,03	-0,153	-0,183
MEDICLIN AG	-0,205	-0,43	-0,225
EVOTEC AG	0,237	-0,006	-0,243
FRIWO AG	0,653	0,398	-0,255
BAYER SCHERING PHARMA AG	0,192	-0,065	-0,257
SINGULUS TECHNOLOGIES AG	0,362	0,067	-0,295
AIXTRON SE	0,047	-0,252	-0,299
SUED-CHEMIE AG	-0,005	-0,31	-0,305
IM INTERNATIONALMEDIA AG	0,555	0,204	-0,351
DURKOPP ADLER AG	0,353	-0,067	-0,42
BALDA AG	0,086	-0,346	-0,432
TUI AG	-0,354	-0,791	-0,437
STRATEC BIOMEDICAL SYSTEM AG	0,231	-0,22	-0,451
BILFINGER SE	0,281	-0,188	-0,469

DEUTZ AG	0,018	-0,511	-0,529
SURTECO SE	0,058	-0,583	-0,641
AXEL SPRINGER VERLAG AG	-0,495	-1,139	-0,644
NORDWEST HANDEL AG	-0,224	-0,918	-0,694
ADVA AG OPTICAL NETWORKING	0,042	-0,713	-0,755
EUROMICRON AG COMM & CTRL	0,443	-0,37	-0,813
STOEHR & CO AG	1,164	0,199	-0,965
RHEINMETALL AG	0,092	-0,973	-1,065
VERITAS AG	1,125	0,04	-1,085
VOLKSWAGEN AG	0,101	-0,992	-1,093
BIEN-ZENKER AG	0,453	-0,667	-1,12
KUKA AG	0,14	-1,209	-1,349
WASHTEC AG	0,102	-1,309	-1,411
BEHRENS (JOH FRIEDRICH) AG	1,498	0,07	-1,428
CEWE COLOR HOLDING AG	0,094	-1,349	-1,443
KAP-BETEILIGUNGS-AG	1,179	-0,403	-1,582
KRONES AG	0,686	-1,019	-1,705
TURBON AG	2,606	0,573	-2,033
COR & FJA AG	3,045	0,876	-2,169
HOFTEX GROUP AG	1,491	-2,009	-3,5
MAXDATA AG	0,15	-3,354	-3,504
GREIFFENBERGER AG	2,133	-6,033	-8,166
SIXT AG	0,207	-17,164	-17,371

CENIT AG	0,138	-29,834	-29,972
DEUTSCHE STEINZEUG CREM & BR		-0,023	
NESCHEN AG		-0,431	

APPENDIX E: SPSS OUTPUT HYPOTHESIS 4

Model Summary France high conservatism 2002

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.549[a]	.302	.279	.25367822609269

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.669	2	.835	12.969	.000[b]
	Residual	3.861	60	.064		
	Total	5.530	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary France high conservatism 2003

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.500[a]	.250	.225	.543192007846972

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	5.895	2	2.947	9.989	.000[b]
	Residual	17.703	60	.295		
	Total	23.598	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary France high conservatism 2004

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.615[a]	.378	.358	.405794330691824

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	6.016	2	3.008	18.267	.000[b]
	Residual	9.880	60	.165		
	Total	15.896	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary France high conservatism 2005

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.422[a]	.178	.151	.316131693076105

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.280	2	.640	6.404	.003[b]
	Residual	5.896	59	.100		
	Total	7.176	61			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary France high conservatism 2006

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.400[a]	.160	.132	.232576202893927

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.619	2	.309	5.721	.005[b]
	Residual	3.246	60	.054		
	Total	3.864	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary France high conservatism 2007

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.519[a]	.269	.245	.233454008431592

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.203	2	.602	11.038	.000[b]
	Residual	3.270	60	.055		
	Total	4.473	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary France low conservatism 2002

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.365[a]	.133	.105	.335441647758899

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.039	2	.520	4.619	.014[b]
	Residual	6.751	60	.113		
	Total	7.791	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary low conservatism 2003

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.328[a]	.108	.078	.293455304901 25

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.623	2	.311	3.617	.033[b]
	Residual	5.167	60	.086		
	Total	5.790	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary France low conservatism 2004

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.456[a]	.208	.182	.504505436440351

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	4.014	2	2.007	7.884	.001[b]
	Residual	15.272	60	.255		
	Total	19.285	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary France low conservatism 2005

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.840[a]	.706	.696	.269822252275628

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	10.471	2	5.235	71.910	.000[b]
	Residual	4.368	60	.073		
	Total	14.839	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary France low conservatism 2006

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.114[a]	.013	-.020	.746683932971086

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.437	2	.219	.392	.677[b]
	Residual	33.452	60	.558		
	Total	33.890	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary France low conservatism 2007

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.500[a]	.250	.225	.209457724045943

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.880	2	.440	10.025	.000[b]
	Residual	2.632	60	.044		
	Total	3.512	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary France high conservatism group

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.421[a]	.177	-.028	.0817687

a. Predictors: (Constant), YEAR

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.006	1	.006	.862	.406[b]
	Residual	.027	4	.007		
	Total	.033	5			

a. Dependent Variable: VALREL

b. Predictors: (Constant), YEAR

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	36.624	39.181		.935	.403
	YEAR	-.018	.020	-.421	-.928	.406

a. Dependent Variable: VALREL

Model Summary France low conservatism group

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.175[a]	.030	-.212	.2690279

a. Predictors: (Constant), YEAR

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.009	1	.009	.126	.741[b]
	Residual	.290	4	.072		
	Total	.299	5			

a. Dependent Variable: VALREL

b. Predictors: (Constant), YEAR

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-45.466	128.909		-.353	.742
	YEAR	.023	.064	.175	.355	.741

a. Dependent Variable: VALREL

Model Summary Germany high conservatism 2002

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.481[a]	.232	.206	.26417191939447

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.262	2	.631	9.041	.000[b]
	Residual	4.187	60	.070		
	Total	5.449	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary Germany high conservatism 2003

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.404[a]	.163	.135	.98608866969853

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	11.363	2	5.682	5.843	.005[b]
	Residual	58.342	60	.972		
	Total	69.706	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary Germany high conservatism 2004

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.458[a]	.210	.184	.755407914097617

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	9.110	2	4.555	7.982	.001[b]
	Residual	34.238	60	.571		
	Total	43.348	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary Germany high conservatism 2005

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.171[a]	.029	-.003	.426954254073899

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.330	2	.165	.906	.409[b]
	Residual	10.937	60	.182		
	Total	11.268	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary Germany high conservatism 2006

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.352[a]	.124	.095	.460998821223147

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.803	2	.902	4.242	.019[b]
	Residual	12.751	60	.213		
	Total	14.554	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary Germany high conservatism 2007

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.366[a]	.134	.105	.36844263889135

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.257	2	.629	4.631	.013[b]
	Residual	8.145	60	.136		
	Total	9.402	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary Germany low conservatism 2002

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.283[a]	.080	.049	.260968389017342

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.355	2	.178	2.608	.082[b]
	Residual	4.086	60	.068		
	Total	4.441	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary Germany low conservatism 2003

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.412[a]	.170	.142	.636076239258906

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	4.962	2	2.481	6.132	.004[b]
	Residual	24.276	60	.405		
	Total	29.238	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary Germany low conservatism 2004

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.834[a]	.696	.686	.456805191835135

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	28.708	2	14.354	68.787	.000[b]
	Residual	12.520	60	.209		
	Total	41.228	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary Germany low conservatism 2005

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.593[a]	.352	.330	.504615778611018

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	8.294	2	4.147	16.287	.000[b]
	Residual	15.278	60	.255		
	Total	23.573	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary Germany low conservatism 2006

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.351[a]	.123	.094	.426463581198298

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.537	2	.769	4.227	.019[b]
	Residual	10.912	60	.182		
	Total	12.450	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary Germany low conservatism 2007

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.243[a]	.059	.028	.417166056816458

a. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.654	2	.327	1.879	.162[b]
	Residual	10.442	60	.174		
	Total	11.096	62			

a. Dependent Variable: Returns

b. Predictors: (Constant), Change in earnings per share (deflated by StockPrice), Earnings per share (deflated by StockPrice)

Model Summary Germany high conservatism group

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.583[a]	.340	.176	.0655452

a. Predictors: (Constant), YEAR

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.009	1	.009	2.065	.224[b]
	Residual	.017	4	.004		
	Total	.026	5			

a. Dependent Variable: VALREL

b. Predictors: (Constant), YEAR

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	45.279	31.407		1.442	.223
	YEAR	-.023	.016	-.583	-1.437	.224

a. Dependent Variable: VALREL

Model Summary Germany low conservatism group

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.129[a]	.017	-.229	.2702732

a. Predictors: (Constant), YEAR

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.005	1	.005	.068	.807[b]
	Residual	.292	4	.073		
	Total	.297	5			

a. Dependent Variable: VALREL

b. Predictors: (Constant), YEAR

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	34.037	129.506		.263	.806
	YEAR	-.017	.065	-.129	-.261	.807

a. Dependent Variable: VALREL