



Effect of Conservatism and Firm Value in Financial Distress

Hamid Saremi¹, Mohamad Reza Shorvarzi² and Ali Akbar Barati³¹Accounting Department, Quchan Branch, Islamic Azad, Quchan, Iran.²Accounting Department, Neyshabur Branch, Islamic Azad University, Neyshabur, Iran.³Accounting Department, Neyshabur Branch, Islamic Azad University, Neyshabur, Iran.

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ABSTRACT

Accounting conservatism in financial reporting is one of the salient features of the recent financial crisis has attracted more attention. Requiring a high degree of conservatism verifiable knowledge of good news for such benefits, the recognition of bad news, such as loss of productivity. The results show that conservatism has a negative and significant relationship with firm financial distress. The findings of an inverse relationship between firm value and the significant stresses of corporate financial distress. The results of this study, an effective contractual mechanisms to limit the conservative bias of the manager knows the companies financial distress. Increase the corporate value of the Company's long-term financial distress is reduced.

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Introduction

The introduction of accounting conservatism and firm value in terms of financial distress of listed companies in Tehran Stock Exchange is evaluated. Previous studies in different countries have shown that yield losses between accounting conservatism and bankruptcy of the company and there are correlated. (Gyvly and Hine, 2000) [9]. Loss of continuity of the companies listed on the stock is rising. So that in 1387 over 30 companies heading and bankruptcy due to losses from the Tehran Stock Exchange are excluded (Bani Baghani Mahdavi, 1388) [2]. Among some of the research areas of PAT theorists such as Watts (2003) [12], believes that accounting conservatism as an effective mechanism to regulate contracts between different groups, by delaying the recognition of good news, such as earnings, biased behavior. The Director shall recognize offsetting gains. Therefore, this research develops theoretical concepts associated with conservative values and corporate financial distress and experimental way to financial analysts, investors, creditors, managers, and other users of accounting information, indicate whether Conservatism can deal with the various groups to reduce bias acts as an efficient mechanism to act as a director or not.

The theoretical research

Definition of accounting conservatism:

Many researchers have proposed different definitions of accounting conservatism of some of Basu (1997) [7] requiring a high degree of conservatism such as income verification for recognizing good news in the face of bad news is defined as a loss. The definition of conservatism is described from the perspective of profit and loss. But another definition, definition of conservatism is a balance sheet perspective. According to this view, in cases of doubt, there is a choice between two or more reporting method, the method must be chosen to be the least favorable effect on equity. Fltham and Olson (1980) [11] can be defined conservatism Accounting: expectation of the net asset value reported by the company in the long term is less than its market value. Beaver (1966) [8] the difference between market value and book value accounting conservatism as their assets.

According Gyvly and Hine (2000) [9] conservatism, which is an accounting concept of retained earnings was reduced by more rapid recognition of income and expense later. Lower assessment of assets and liabilities are measured. In our country, the Technical Committee of the theoretical concepts of auditing, financial reporting, conservatism word instead of the word of caution is used.

Discreet is to application the degree of care exercised judgments in the estimation. The ambiguity of the situation is needed. So that income or assets or liabilities, and costs less than actually is not provided. Financial Accounting Standards Board, conservatism is defined: Prudent reaction to uncertainty to try to ensure that ambiguity of and risks inherent in the business are properly considered. In this research a conservative estimate of the definition Gyvly and Hine (2000) [9] is used.

Accounting Conservatism and Firm Value:

Accounting Conservatism Brass proven ability to identify and confirm the variability of profits and losses of the business. Based on accounting conservatism improves firm value through two channels: 1. Improve borrowing capacity 2. Reduce opportunism of managers. Experimental studies show that accounting conservatism reduces the cost of borrowing (Ahmed, 2002) [5]. Accounting conservatism tightening the gap between internal and external costs of funds, financial constraints and firms to reduce investment project "lasting marginal" give. If companies are not conservative and a further gap between internal and external costs of funds for this project will have a positive net present value (NPV) of those who did not. Therefore, the possibility of reducing the borrowing capacity of firms will invest less than the potential. (NPV) of the positive final results of this project belong to stock investors and may increase firm value. Accounting conservatism and opportunistic behavior of managers is limited (Watts, 2003) [12]. Despite the limited horizon Ltd, managers have incentives to net assets and profits during his tenure are higher than the actual words. Also, they tend to increase in size over the desired area and causing losses to continue the project. In turn, this raises the equity value of the firm (Watts et al 2011) [13].

Financial Distress

In Oxford dictionary, the word "Distress" means pain, sadness, lack of financial resources and monetary poverty has different definitions in the literature of financial distress is presented. Altman (1993) [6] failure, weak realizability ability, inability to pay the debt in terms of maturity and Bankruptcy argue that the financial distress of a company. In terms of economic, financial distress can be interpreted to the detriment of tens of companies that have participated in this case is not successful. In this case the company's rate of return is less than the cost of capital rate. better allocation of capital and resources to help assess financial distress. The evaluation of corporate financial distress has always been one of the topics of interest to investors, creditors, and has governments. Early diagnosis of the companies that are going to develop financial distress, is highly desirable.

History of Research

1. Krami and Omrani (1389) [4] to study the life cycle of the firm and the firm have conservative values. Conservative influence on investors' reactions to an abnormal operating profit and net operating assets at various stages of the life cycle were examined. and the reverse is true in the decline stage.

2. Baghani and Bani Mahd (1388) [2], the effect of accounting conservatism, state ownership, firm size and leverage of the firms reported losses, were examined. Their results indicated a significant positive relationship between accounting conservatism corporate loss is reported. Also, there is a direct relationship between firm size and leverage ratio of loss and loss of elongation and inversely the yield was emphasized. Their results show that state ownership of companies has no effect on yield loss.

3. Ramazani Khybari (1390) [3] as the relationship between income smoothing research Vdrmandgy financial companies do. The results indicate a significant relationship between income smoothing and the financial distress of a company. The results showed that none of the components of the cash benefit is significantly associated with financial distress. Bani Mahb bahman (1385) [1] research as "a model for defining and measuring accounting conservatism" did, the results of this study indicate that conservative accounting firms surveyed decreased. This decline was due to a decrease in the efficiency of the company's assets, liabilities and cash is under investigation. The evidence shows that assets may reduce yields and lack of commitment and lack of agency theory, managers have a duty to respond.

4. Beaver (1966) [8] to investigate the ability of financial ratios to predict corporate bankruptcy using univariate analysis. His analysis than that relating to cash flow ratios were used. Beaver Research results showed that the ratio of cash flow to total debt, the most accurate in predicting financial distress to five years before it happened.

Basu (1997) [7] to determine the index of conservatism in relation to this study results showed the company paid dividend yield stocks with negative stock returns than firms with positive stock returns, the profits and return on equity have highly correlated there. The research also showed that reduction profitability and Hine

5. Gyvly past four decades, will often result in cash flows in America yet. The findings of faster recognition of bad news than good news, and to increase the degree of conservatism in financial reporting.. Gyvly and Hine (2000) [9] during studies showed benefits over the past four decades, the U.S. has decreased. But this loss, cash flows have been reduced. Ahmed et al (2002) [5] in their research showed that corporate accounting methods were more conservative than other

companies use. be conservative accounting managers from investing in projects with returns is negative. He also finds a direct relationship between the percentage of shares owned by members of the board and there are conservative. Ross Watts and Lyvzyv (2011) [13] study the role of accounting conservatism in the synergy of the global financial crisis and they concluded that accounting conservatism increases firm value through two channels. Research shows that between conservative accounting and stock returns, there is a positive relationship between debt and investment. Evidence suggests that the benefits of accounting conservatism to increase corporate value and the contract is converted to equity.

Hypothesis

Hypothesis is as follows:

First hypothesis: accounting conservatism is correlated with financial distress.

Second hypothesis: the company has a significant relationship with financial distress.

Materials and Methods:

The aim of the present study and applied research is descriptive in nature. In this study, the measurement of conservatism and Hin Gyvly model is used to calculate the index of financial distress (z) Altman used.

Because of these two indicators is that most of these parameters were used as indicators for They are also required data is available. Also Rkrsyvn logistic analysis was used to test the hypotheses.

The population and sample:

The target population includes all firms listed on the Stock Exchange.

The study sample consisted of 123 firms with financial distress and lack of financial distress of listed companies in the Stock Exchange Vavraq before 1380, which are listed on the Stock Exchange.

Companies of the six-year period from 1384 to 1389 are selected.

The sample is selected according to the following conditions:

1. They can be financial period ending March. This is due to the ease of data analysis.
2. Before 1382 are listed on the Stock Exchange.
3. Data are available to them.
4. Stop trading no more than three months.
5. Altman model from the beginning of the end of 1384, subject to a minimum of 1389 companies are distressed.

Time and Place scope of the study:

Place territory, it is all listed companies on the Stock Exchange. The scope of the study period, 1384 to 1389 (a period of 6 years old) has been determined.

The data collection:

The study used data collected from this research, library resources, study dissertations, articles, Persian and Latin were used. Source of data collected in this study was the company's financial statements. The collected data using Excel software and the necessary corrections and classification is based on the variables entered into the computer. The final analysis was performed using spss software.

Variables

Dependent variables in the study of financial distress. The evaluation of companies financial distress financial ratios are used as financial ratios Always creditors, shareholders and financial analysts have been. Timely and accurate predictions can be evaluated and financial decision makers in finding optimum solutions to help prevent financial distress.

Table 1 Descriptive Statistics Data

Standard deviation	Average	Minimum	Maximum	The number of observations	Variable	Company status
.15279	-.0171	-.59	.31	80	CON	Lack of financial distress.
.12985	5.1876	4.87	5.54	80	FV	
.18550	.4641	.10	.86	80	LEV	
.48171	11.6787	10.64	13.47	80	SIZE	
.39527	.3081	-.18	2.15	80	SGR	
.11652	.2576	.00	.63	80	PI	
.65265	3.5731	2.91	6.43	80	Z	
.15189	.0092	-1.09	.67	653	CON	Financial distress.
.14209	5.1083	4.81	5.57	653	FV	
.18587	.6911	.22	2.21	653	LEV	
.57479	11.6820	10.25	14.52	653	SIZE	
.33826	.1326	-1.00	3.22	653	SGR	
.10466	.0829	-.31	.53	653	PI	
.73472	1.5192	-2.58	2.90	653	Z	

In this study, the prediction of financial distress of companies Altman Z model is used multiple discriminant analysis Altman model to predict financial distress of companies that are not in any financial distress prediction models such as Altman Probability of financial distress into three regions with very low probability of financial distress, financial distress, and likelihood of financial distress region are highly classified.

However, the effect of independent variables on the dependent variable financial distress of companies is analyzed as follows conservatism index and firm value.

In this research for conservative accounting measurement model Gvly and Hine (2000) is used. Conservatism index is calculated based on the following:

Conservative Index= Operating accruals/ First-period total assets *(-1)

Difference between net income and operating cash flow from operating accruals plus depreciation is calculated. The Dqydh Gvly and Hine (2000) developed an Index of change in the degree of accrual accounting conservatism is over a long period.

In other words, if the accrual increases, then decreases, and vice versa conservatism.

Therefore, to determine the direction of a negative number is multiplied by the accrual conservatism. To evaluate and assess a company's value, the financial statements of listed companies on the Stock Exchange will be reviewed by the company's value will be evaluated by the following equation:

Firm Value = Number of shares on balance sheet date * The market price of shares at balance sheet date
Other control variables are variables that are finding financial leverage, firm size, sales growth and profitability Index. The control variables may affect the relationship between conservatism and firm value may affect the company's financial distress.

Analysis and hypothesis test results:

In the following, a summary of findings, including statistical data, results of testing hypotheses derived from the model are presented.

Descriptive statistics of the data:

Table 1 Statistical parameters such as mean, standard deviation, minimum and maximum for continuous variables

separately firms facing financial distress and lack of financial distress is calculated. These indicators show the statistical distribution of these variables as well.

For continuous variables, the mean, median and standard deviation of the data, the distribution of the data shows. The standard deviation values of the company's financial distress and lack of financial distress can be observed Standard deviation amount the variables in these two floors is relatively close together and there is no difference.

Firms facing financial Distress the distress index in 1.5192 and the lack of companies financial Distress, the 3.5731 is. It shows the correct classification of companies facing financial Distress and lack of financial Distress.

Hypothesis test:

In this study the effect of independent variables accounting conservatism and firm value and the control variables on the dependent variable financial distress of the test and logistic regression analysis are.

The first test of The linear among the variables:

Most of the independent variables is linear. But if the line is high, the model would not be appropriate. The linear correlation matrix is provided a method of testing. the correlation coefficient matrix is computed between each pair of variables. Lack of correlation between the independent variables means that the correlation coefficient between each pair of variables is equal to zero. But in practice it is not possible to obtain a the correlation coefficient of zero, and as a rule, less than 50 percent correlation between each pair of independent variables can be considered acceptable and there is also concerned was not linear. In the first hypothesis, the correlation coefficient between all variables except leverage, and profitability index of less than 50 percent.

To fix the problem of The linear between these two variables in all possible ways, including changing the scale variable (using logarithmic variables) were examined, But because the ultimate solution to this problem as the financial leverage variables have to be removed from the model and the remaining independent variables, there is no problem of The linear. The linear variation of the independent variables in the model are listed in Table 2.

Table 2: Correlation matrix of the independent variables in the model

PI	SGR	SIZE	LEV	CONS	variables
				1	CONS
			1	.201	LEV
		1	-.038	-.034	SIZE
	1	.033	-.071	-.057	SGR
1	.184	.097	-.639	-.357	PI

The results of the first hypothesis:

The results of the first hypothesis based on logistic Rkrsyon model are given in Table 3.

$$\text{Probability of failure} = p(\text{FD}_{it}=1) = \frac{1}{1+e^{-Y}}$$

$$Y = \text{LN}(\text{Probability of failure} / \text{Probability non of failure}) = \beta_0 + \beta_1 \text{CONS}_{it} + \beta_2 \text{LEV}_{it} + \beta_3 \text{SIZE}_{it} + \beta_4 \text{SGR}_{it} + \beta_5 \text{PI}_{it}$$

According to the results of the second step regression is observed, which is probability amount to less than 5% is a conservative variable, So assuming the null hypothesis was rejected in favor of the first research hypothesis is accepted at 5% level. 1.945 coefficient of this variable is a variable that conservatism showed a negative relationship with the probability of financial distress.

Of approximately 90% is forecast models, the Chi square probability value is less than 5% of the adequacy of the model to test the hypothesis is confirmed. According to Cox and Snell coefficient rate to determine the probability of financial crisis to about 20% could be explained by the independent variables are related to other factors that are not observed in this study.

Table 3: Statistical analysis of the results of the first hypothesis based on logistic regression models

Exp(B)	P-value	Wald	β	variabel	Pitch Two
.143	.038	4.325	-1.945	CONS	
.374	.005	7.942	-.985	SGR	
.000	.000	102.475	-	PI	
103.15	.000	188.458	4.636	Constant	
P-value			89.9	Percent predicted	
.000	164.660	Statistic Chi Square.	.201	Cox and Snell coefficient of	

In column Exp (B) is the ratio of the observed values, indicating the probability of a failure (chance of success) more than non-failure (fracture) has a value less than one means the failure probability (chance of success) is less than the failure to failure (failure) is. Note that this value for the conservative variables .143, the result is an increase in conservatism, would reduce the probability of failure.

Table 4: Pearson correlation matrix of the independent variables in the model

PI	SGR	SIZE	LEV	FV	variables
				1	FV
			1	-.300	LEV
		1	-.038	.833	SIZE
	1	.033	-.071	.080	SGR
1	.184	.097	-.639	.429	PI

The linear hypothesis test between two variables:

The linear swing of the independent variables in the model are given in Table 4. As can be seen, the correlation between the variables of firm size and financial leverage and firm value and profitability index is greater than 50%, To overcome the problem of The linear between the variables in all possible ways, including changing the scale variable (using logarithmic variables) were examined, But due to this problem as the solution Firm size and profitability of the variables had to be

eliminated from the model and the remaining independent variables, there is no problem of the linear.

The results of the second hypothesis:

The results of the second hypothesis based on logistic regression model are shown in Table 5.

$$\text{Probability of failure} = p(\text{FD}_{it}=1) = \frac{1}{1+e^{-Y}}$$

$$Y = \text{LN}(\text{Probability of failure} / \text{Probability non of failure}) = \beta_0 + \beta_1 \text{FV}_{it} + \beta_2 \text{LEV}_{it} + \beta_3 \text{SIZE}_{it} + \beta_4 \text{SGR}_{it} + \beta_5 \text{PI}_{it}$$

According to the results of the regression can be seen, the value of the variable firm value (FV) slightly more than 5%, so the error level of 10% of the null hypothesis in favor of the hypothesis to be rejected and the second hypothesis of the study in 10% of cases are being accepted. 851/1- coefficient of this variable is a variable that indicates a negative relationship between firm value is the probability of financial distress. Cent against 90 per cent is forecast models, The value of chi-square statistic is less than 5%, thus confirming the adequacy of the model is to test the hypothesis. According to Cox and Snell coefficient to determine the probability of financial crisis to about 16 percent is explained by the independent variables and the rest are caused by factors that are not observed in this study. According to the company, the value of the variable equal to 0.157, the result is an increase in firm value, reducing the probability of failure will follow.

Table 5: Results of statistical analysis of the second hypothesis based on logistic regression models

Exp(B)	P-value	Wald	β	variable	Pitch One
.157	.056	3.652	-1.851	FV	
1815.420	.000	73.303	7.504	LEV	
.281	.001	12.113	-1.271	SGR	
1916.467	.137	2.210	7.558	Constant	
P-value			90.0	Percent predicted	
.000	129.022	Statistic Chi Square	.161	Cox and Snell coefficient of determination	

Conclusion:

This study examines the effect of accounting conservatism on firm value in conditions of financial distress discussed. This variable is used in line with the second hypothesis and test hypotheses include corporate financial distress, accounting conservativeness, firm value, financial leverage, firm size, sales growth rate and profitability indicators are.

The results have no significant relationship between accounting conservatism and the value of of companies financial distress has emphasis that the relationship is reversed. In other words, firms in financial distress, accounting conservatism causes to losses than profit to be identify. This makes the bias Tarftar manager, the exponential profit more identification and delayed Additional payments to managers and shareholders of the company is limited, and thus increase the long term value of the of companies is in financial distress.

Proposals based on the research results:

Proposals resulting from the research can be expressed as follows:

1. Stock Exchange or the organization responsible for the company's financial failure is Proposals based on action recognition in real time financially distressed companies And monitor their performance and taking appropriate action and most importantly, correctly and timely information to shareholders and investors and capital market participants are Perhaps we can get through this process with transparent in the capital market and eliminate the information rents has created an

effective and efficient market And economic activists in these markets to rotate the better business cycle and correctly guidance of the national capital and wealth creation and employment Will lead to economic growth and development We encourage and support.

2. Companies to investors, financial analysts and other stakeholders propose Optimal investment decisions for the basket rate returns, and only such as accounting ratios derived from financial statements of companies do not rely, And factors such as the choice of conservatively or non conservatively management approach, Actions and applied of management estimates in terms the timing of recognition of his research and development and advertising expenses, accruals and adjust their decisions to consider.

Some suggestions for future research:

Some suggestions for further research in this field can be expressed as follows.

1. The use of non-stock companies in improving results of this research
2. Use different industries according to the present research.

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