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Research Article

Impact Of International Financial Reporting Standards (IFRS) Adoption On Financial Performance Of Information Technology Companies In India

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ARTICLE INFO | **ABSTRACT**

This research paper explores the impact of International Financial Reporting Standards (IFRS) adoption on the financial performance of the top 10 information technology (IT) companies in India. The study evaluates financial metrics before and after the implementation of IFRS, which was mandated for Indian listed companies starting April 1, 2016. By analyzing key performance indicators such as profitability, liquidity, and valuation ratios, the research aims to identify significant changes and trends resulting from the transition to IFRS. The findings indicate that while IFRS adoption generally enhanced financial transparency and comparability, the effects on specific financial metrics varied across companies. Profitability metrics showed improvements for some companies, whereas liquidity ratios remained stable, and valuation ratios exhibited mixed results. The study underscores the importance of understanding IFRS impacts for investors and company management, providing insights into how IFRS adoption influences financial reporting and performance in the Indian IT sector.

Key words: IFRS, Convergence of IFRS, Financial Ratios, Financial Performance, IT Companies

1. Introduction

IFRS stands for International Financial Reporting Standards that are global accounting principles set by the International Accounting Standards Board, or IASB. They detail international standards to enhance transparency, consistency, and comparability of financial statements across national boundaries. The general objective of IFRSs is to improve the transparency and consistency of financial reporting together with making possible investment choices and cross-border capital flows based on comparable and understandable information about the financial position and performance of enterprises.

Adoption of IFRS in India

Adoption of IFRS is a massive shift from its former accounting framework, which has been dominated by the predominantly Indian Generally Accepted Accounting Principles, whereas the adoption of IFRS was based on an urge to harmonize the financial reporting practices of India with global standards driven by an increasing global character of capital markets and the burgeoning role of Indian companies in international markets.
The Securities and Exchange Board of India made IFRS mandatory for all listed companies in April 2016, marking a critical point in the financial reporting landscape in the country. It is adopted in phases for the largest companies and, subsequently, extended to other entities. The huge attraction of foreign investments and economic growth were believed to be guaranteed by the credibility and comparability of the financial statements.

1.2. Relevance to the Information Technology Sector

IFRS adoption, for the first time, will pose significant importance to India's information technology sector due to a number of important reasons inherent in the nature of the industry. The relevance of IFRS to this sector can be highlighted as follows.

1.2.1. Complex Financial Transactions

Most of the IT companies carry on such complicated financial transactions which are heavily influenced by IFRS standards. These include:

- **Long-term Contracts**: Most IT companies pursue long-term contracts in software development, support, and services. IFRS 15, related to revenues from contracts with customers, presents a five-step model for revenue recognition. The standard directly affects how and when revenue is recognized, which might change reported earnings and financial performance.
- **Tangible Assets:** Most of the investments put by IT companies went into intangible assets which consist of software, patents, and research and development. There is very elaborate guidance on recognition and measurement under IFRS as applied through IFRS 38. Almost entirely changes in valuation and amortization would result in differences in the financial statements.
- **Research and development costs**: IFRS differs from previous standards on how research and development costs should be treated. It directly writes off the research costs to expenses upon incurrence and the development costs may be capitalized when proper criteria are met as indicated by IFRS 38, thus affecting profitability and asset base as reported by IT organizations.

1.2.2. Global Operations and Comparative Analysis

Indian IT companies belong to the major players of the world market as they have international clients and operate in more than one jurisdiction; hence, the adoption of IFRS will have far-reaching implications for them.

- **Facilitates International Comparison**: One global standard of accountancy under IFRS allows for seamless comparability of the Indian IT firms and their international counterparts. This is crucial to the investors and analysts in comparing performance in different countries.
- **Institutional Appearance of Attractiveness of Foreign Investment:** By conforming to international accounting standards, Indian IT firms will be able to present their accounts in a manner such that foreign investors get accustomed to the structure. In this context, the attractiveness that these companies extend to foreign investors and hence by increased capital inflows might rise.

1.2.3. Impact on Financial Metrics

The adoption of IFRS has a direct impact on various financial metrics that are crucial for evaluating IT companies:

- **Profitability Ratios:** Changes in revenue recognition and the treatment of intangible assets can significantly affect profitability ratios such as net profit margin and return on capital employed. Understanding these impacts is essential for assessing the true financial health of IT companies.
- **Liquidity Ratios:** IFRS may affect the reporting of current and non-current assets and liabilities, which can influence liquidity ratios such as the current ratio. Accurate liquidity assessment is critical for evaluating a company’s ability to meet short-term obligations.
- **Valuation Metrics:** Metrics like earnings per share (EPS) can be influenced by changes in how revenues and expenses are recognized under IFRS. These valuation metrics are closely monitored by investors and analysts.

2. Literature Review

A vast number of research studies addresses effects of IFRS in the countries. The proponents state that IFRS adoption results in high-quality disclosures compared to local generally accepted accounting principles. IFRS is mostly considered more fair value-based, and hence less accommodating in accounting for financial statement issuers and relates economic events sooner to the financial statements (Coopers & Lybrand, 1993; Dumontier & Raffounier, 1998; GAAP, 2000). Transparency and improvements in accounting quality, regulators and investors continue to argue that this translates into reduced cost of capital for a firm. Theoretically, higher-quality information reduces the risk in future returns (Barry & Brown, 1985) or information asymmetry problems between the managers and investors. This can reduce the extent of asymmetries and could decrease adverse selection, enhance liquidity, and thus reduce the required rate of return (Diamond & Verrecchia, 1991).

One of the recent, and very important studies on the economic effects of the imposition of IFRS reporting requirements is from Daske et al. (2008), who reported that market liquidity tends to rise in the years surrounding adoption using a sample spanning 2001 through 2005 from 26 countries. Many other studies have shown that the cost of capital declines or equity valuation increases with the adoption of IFRS. However, various scholars are in contradictions concerning the effect of IFRS on earnings management (Van Tendeloo & Vanstraelen, 2005; Zéghal et al., 2011).

Lantto and Sahlstrom (2009) analyzed the effect of IFRS adoption on some critical financial ratios using data from Finland. According to their study, IFRS adoption alters the magnitude of these ratios. Padrtova and Vochozka (2011) compared CEZ Inc. financial statements prepared under IFRS and Czech accounting standards for the years 2004 and 2005. According to the findings, the Czech standards depicted the firm as healthier than the IFRS statements. According to Aisbitt (2006) and Cordazzo (2008), adoption of IFRS has significantly impacted net income compared to shareholder equity, therefore affecting key profitability and gearing ratios. On the contrary, Iaruga et al. (2007) did not find any consistent pattern regarding increased profits upon adoption of IFRS changes in profit were not influenced by firm size or nominal profit, as it is pointed out in Perramon & Amat, 2006.

The study by Kamath and Desai was on the adoption of IFRS by Indian companies and its implications on financial activities, which were spread over financial risk, investment activities, operating activities, and debt covenants. The findings on investment and operating activities were positive, but change in financial risk and debt covenants was not reported. However, adoption of IFRS did not improve earnings management in India as IFRS was transparent and fair value-based as compared to conservative Indian GAAP (Swamynathan & Sindhu, 2011).

Conversely, Ferrer et al. (2011) has been accomplished in investigating the effect of liquidity and leverage ratios on IFRS disclosure compliance in the Philippines; in this study, no impact was observed either positively or negatively on the practice of IFRS disclosures with respect to the disclosure indices as measured from the balance sheet and income statement.

It is relatively few studies that have directly related the adoption of IFRS with economic activities such as investments, financial risks, operations, and debt covenants in Indian companies. As the context of adoption under IFRS is more or less to ensure better disclosure practices, further research is warranted to understand the very specifics on how these economic activities will be influenced in the Indian context.

3. Objectives

1) To examine the Return on Capital Employed (ROCE) to assess the efficiency with which a company utilizes its capital to generate profits.
2) To analyze the company's capacity to meet its long-term obligations by comparing debt to equity.
3) To determine the financial health of the company in terms of its short-term liquidity.
4) To examine the earnings per share (EPS) as a key indicator of a company's profitability on a per-share basis.

4. Research Methodology

4.1. Data Collection

Data for this study was gathered from the financial statements of the top 10 IT companies in India, based on market capitalization and revenue. The companies included are:

1. Tata Consultancy Services (TCS)
2. Infosys
3. HCL Technologies
4. Wipro
5. Larsen & Toubro Infotech (LTI)
6. Tech Mahindra
7. Oracle Financial Services Software Ltd
8. Persistent Systems Ltd
9. Mphasis
10. KPIT Technologies Ltd

(Source: https://www.forbesindia.com/article/explainers/top-10-it-companies-in-india/87143/1)

The financial statements for these companies were analyzed for the years preceding and after IFRS adoption. IFRS adoption in India was mandated for listed companies starting April 1, 2016.

4.2. Data Analysis

The analysis focuses on key financial metrics, including:

- **Profitability Ratios:** net profit margin, Return on Capital Employed
- **Solvency Ratio**: Debt-Equity Ratio
- **Liquidity Ratio:** Current ratio
- **Valuation Ratios:** Earnings per share (EPS).

4.3. Statistical tools such as paired t-tests were used to assess the significance of changes in these metrics before (2010 to 2016) and after IFRS adoption (2016 to 2023).

4.4. Hypotheses

H01: There is no significant effect of IND AS on earning per share of selected IT companies.
H02: There is no significant effect of IND AS on return on Capital Employed of selected IT companies.
H03: There is no significant effect of IND AS on net margin ratio of selected IT companies.

H04: There is no significant effect of IND AS on debt-equity ratio of selected IT companies.
H05: There is no significant effect of IND AS on Current ratio or liquidity.

5. Data Analysis and Interpretation

Table I*: Basic EPS of IT Companies

Companies	Before IFRS	After IFRS
TCS	38.36	88.998
Infosys	145.05	54.05
HCL Technologies	52.514	53.373
Wipro	27.464	22.539
Larsen & Toubro Infotech (LTI)	65.786	65.058
Tech Mahindra	79.282	44.414
Oracle Financial Services Software Ltd	134.342	181.189
Persistent Systems Ltd	44.718	60.74
Mphasis	31.75	60.121

Table II*: Summary of Paired T-Test on Basic EPS prepared from IGAAP and IND AS Financial Statements

Paired Samples Test									
		Paired Differences							
		Mean	Std. Deviation	Std. Error Mean	95% Confidence Interval of the Difference Lower	Upper	t	df	Sig. (2-tailed)
Pair 1	BeforeIFRS – AfterIFRS	-1.24622	43.77327	14.59109	-34.89333	32.40089	-.085	8	.934

The paired t-test results also show that the statistical difference in Earnings Per Share (EPS) before and after the adoption of IFRS is not there. The actual t-value is -0.085, which further shows that there is a very negligible difference in the EPS before and after IFRS adoption. The p-value or Sig. (2-tailed) value is 0.934 and that is significantly greater than the conventional value of 0.05.
This high p-value means we fail to reject the null hypothesis; there's no significant evidence for a meaningful change in the EPS related to this adoption of IFRS. In other words, based on this test, the transition to IFRS appears not to have any statistically significant impact on the earnings per share.

Table III*: Return on Capital Employed (%) of IT Companies

Companies	Before IFRS	After IFRS
TCS	35.632	46.971
Infosys	25.084	31.932
HCL Technologies	24.9	26.682
Wipro	21.626	20
Larsen & Toubro Infotech (LTI)	11.88	8.782
Tech Mahindra	20.148	20.29
Oracle Financial Services Software Ltd	19.522	35.979
Persistent Systems Ltd	18.504	20.898
Mphasis	13.712	20.622

Table IV*: Summary of Paired T-Test on Basic Return on Capital Employed (%) prepared from IGAAP and IND AS Financial Statements

Paired Samples Test									
		Paired Differences							
		Mean	**Std. Deviation**	**Std. Error Mean**	**95% Confidence Interval of the Difference Lower**	**Upper**	**T**	**Df**	**Sig. (2-tailed)**
Pair 1	**BeforeIFRS – AfterIFRS**	**-4.57200**	**6.39422**	**2.13141**	**-9.48704**	**.34304**	**-2.145**	**8**	**.064**

The t-value of -2.145 indicates a moderate difference in ROCE before and after IFRS adoption. However, the p-value of 0.064 is slightly above the common significance threshold of 0.05. It thus means that although there

might be some evidence that the differences of ROCE are associated with IFRS adoption, the difference is not statistically significant in particular at the level 5%.
Generally, in the results of the findings, it appears that there is a difference in ROCE both before and after the adoption of IFRS; however, the evidence cannot be as strong enough to conclude with confidence that any such difference found is also statistically significant. It thus implies that all the effects noticed might have been due to random fluctuations rather than being an actual effect caused by the adoption of IFRS.

Table V*: Net Margin Ratio of IT Companies

Companies	Before IFRS	After IFRS
TCS	22.38	20.667
Infosys	23.47	19.267
HCL Technologies	15.61	16.129
Wipro	17.094	15.184
Larsen & Toubro Infotech (LTI)	8.102	7.089
Tech Mahindra	12.636	10.493
Oracle Financial Services Software Ltd	32.752	30.181
Persistent Systems Ltd	15.392	10.898
Mphasis	13.406	12.389

Table VI*: Summary of Paired T-Test on Net Margin Ratio prepared from IGAAP and IND AS Financial Statements

Paired Samples Test									
		Paired Differences							
					95% Confidence Interval of the Difference				
		Mean	Std. Deviation	Std. Error Mean	Lower	Upper	T	Df	Sig. (2-tailed)
Pair 1	BeforeIFRS – AfterIFRS	2.06056	1.57174	.52391	.85241	3.26870	3.933	8	.004

The t-value of 3.933 indicates a strong difference in the Net Margin Ratio before and after IFRS adoption with the positive sign, which the Net Margin Ratio increased after IFRS adoption. The p-value of 0.004 is well below the conventional significance level of 0.05.
The low p-value therefore suggests that the observed difference in Net Margin Ratio is statistically significant. That is to say, therefore, that there is significant evidence to reject the null hypothesis which instead leads to the fact that adoption of IFRS has an impact on the Net Margin Ratio. Findings are therefore such that the results indicate a meaningful change in the Net Margin Ratio related to the adoption of IFRS and reflects, therefore a potentially noteworthy effect on financial performance in this regard.

Table VII*: Debt/Equity ratio of IT Companies

Companies	Before IFRS	After IFRS
TCS	0	0
Infosys	0	0
HCL Technologies	0.098	0.046
Wipro	0.194	0.199
Larsen & Toubro Infotech (LTI)	0.636	1.702
Tech Mahindra	0.18	0.073
Oracle Financial Services Software Ltd	0	0
Persistent Systems Ltd	0	0.031
Mphasis	0.078	0.081

Table VIII*: Summary of Paired T-Test on Debt/Equity ratio prepared from IGAAP and IND AS Financial Statements

Paired Samples Test									
		Paired Differences							
					95% Confidence Interval of the Difference				
		Mean	Std. Deviation	Std. Error Mean	Lower	Upper	t	df	Sig. (2-tailed)
Pair 1	BeforeIFRS – AfterIFRS	-.10511	.36264	.12088	-.38386	.17364	-.870	8	.410

The t-value of -0.870 shows a small difference between the periods prior to and following the adoption of IFRS in the Debt/Equity ratio; the negative sign shows a slight decline in the ratio. However, the p-value of 0.410 is greater than the conventional significance threshold of 0.05.

This high p-value shows that the change found with the Debt/Equity ratio is not significant at a statistical level. That means there is insufficient evidence to reject the null hypothesis, and thus, the introduction of IFRS has not had a statistically significant impact on the Debt/Equity ratio. Therefore, in general, the findings of this study show that the adoption of IFRS did not bring about a significant change to the debt equity ratio for the firms under study.

Table IX*: Current Ratio of IT Companies

Current Ratio	Before IFRS	After IFRS
TCS	2.72	3.589
Infosys	3.992	2.823
HCL Technologies	2.388	1.83
Wipro	2.036	2.38
Larsen & Toubro Infotech (LTI)	1.312	1.301
Tech Mahindra	1.656	2.186
Oracle Financial Services Software Ltd	6.504	5.247
Persistent Systems Ltd	3.562	2.898
Mphasis	2.442	2.482

Table X*: Summary of Paired T-Test on Current Ratio prepared from IGAAP and IND AS Financial Statements

Paired Samples Test									
		Paired Differences					t	df	Sig. (2-tailed)
		Mean	Std. Deviation	Std. Error Mean	95% Confidence Interval of the Difference Lower	Upper			
Pair 1	BeforeIFRS – AfterIFRS	.20844	.74699	.24900	-.36574	.78263	.837	8	.427

With a t-value of -0.837, the difference in Current Ratio between the periods before and after adopting IFRS is relatively small, and the negative sign shows slight decline. The p-value of 0.427 is much higher than the standard significance level of 0.05.
This high p-value implies that the observed difference in the Current Ratio is not statistically significant. Thus, we can't reject the null hypothesis; this means that there is no strong evidence that has been presented indicating a consequential impact of IFRS adoption on the Current Ratio. Simply put, the results suggest that the adoption of IFRS does not lead to meaningful changes to the Current Ratio of these companies.

6. Results and Discussion

The analysis results of the paired t-test show that IFRS adoption affects financial metrics in different ways. In EPS, the outcome of t-tests is that EPS does not change as the p-value is 0.934 and the t value is -0.085, meaning that IFRS adoption has not particularly affected EPS. Similarly, The Debt/Equity ratio and Current Ratio showed non-significant changes, having p-values of 0.410 and 0.427, respectively. Those high p-values signify that IFRS has not caused differences that are meaningful in these ratios.
On the other hand, there has been a significant effect on the Net Margin Ratio as shown by the high t-value of 3.933 and a low p-value of 0.004. This very low p-value suggests that the change in the Net Margin Ratio might be statistically significant and there exists a significant impact of adoption of IFRS on the Net Margin Ratio.

7. Conclusion

This study reveals that, in fact, the adoption of IFRS does not appear to have a significant impact on the EPS, the Debt/Equity ratio, or the Current Ratio while having demonstrated a meaningful and statistically significant effect on the Net Margin Ratio. This study suggests an influence of IFRS adoption on some financial metrics but not on others, and the examined financial metrics are such that have revealed a clear reaction to the aforementioned new reporting standards.

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