

**THE IMPACT OF THE CORPORATE GOVERNANCE ON THE VALUE
RELEVANCE OF ACCOUNTING INFORMATION IN LISTED FIRMS IN
COLOMBO STOCK EXCHANGE**

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INTRODUCTION

Over the past twenty years' corporate governance (CG) systems and practices have gained significant attention because of the numerous business scandals that have occurred around the world. Regarding governance, weak CG is perceived as a structural flaw in most Asian economies and was considered the leading cause of the 1997 Asian economic crisis (Nam et al., 1999). The ability of accounting numbers to explain market price per share is known as value relevance. Beisland (2009) describes value relevance as the capability of financial statement information to tap and summarize firm value. Although investors rely on accounting information for investment objectives, the quality of this information should be reliable and of high quality, as financial accounting information has a significant impact on share prices. Furthermore, CG is supposed to help companies perform better. However, companies listed on the stock exchange must follow the code; it would be interesting to investigate the impact of CG on value relevance, especially since good governance is an essential topic in Sri Lanka these days.

This study contributes to the investors making decisions before allocating resources to companies, whether company financial statements show their actual performance for the current period or not. Moreover, on the other hand, this study answers, is CG improving the quality of accounting information in the Sri Lanka context? It is essential to all parties who use financial information, such as academics, industries, etc. Furthermore, by effectively utilizing accounting information, shareholders can make the best decision possible. Financial statements provide information to users (investors, creditors, and so on) to aid in the decision-making process and motivate value relevance. This study is based on Ohlson's (1995) price regression model to explain the value relevance of accounting information. It explains market value per share using earnings per share and book value of equity per share.

This study was motivated by the mixed results of several studies on CG on the quality of accounting information; some scholars have found a positive relationship between corporate governance and the value relevance of the accounting information (Almujamed & Alfraih, 2020; Bin Khidmat et al., 2018; Fatima et al., 2018; Krismiaji & Surifah, 2020). Meanwhile, there are some negative relationships (Balagobei, 2018; Kalantonis et al., 2021). The results reveal that board independence and ownership structure significantly influence the value relevance of accounting information of listed hotels and travel in Sri Lanka. In contrast, firm leverage influences the value relevance of accounting information. There is a paucity of research on CG on the value relevance of accounting information in the context of Sri Lanka.

The main objective of this paper is to examine the impact of CG on the value relevance of accounting information in listed firms on the Colombo Stock Exchange (CSE).

METHODOLOGY

This study was based on the secondary data and data gathered from audited financial statements of the selected listed CSE companies published from 2017 to 2021. The researcher conducted the statistical analysis as the research follows a quantitative approach. This research used the deductive approach to investigate the research problem because hypotheses are developed based on existing theories. Related previous studies have pointed out several variables to explain the impact of corporate governance on the value relevance of accounting information. According to this study, the independent variables are board size ($B_{SIZE_{it}}$), board independence ($B_{ODIND_{it}}$), audit committee size ($AC_{SIZE_{it}}$), audit committee independence ($AC_{IND_{it}}$), and the dependent variable is share price (SP_{it}). The control variables are earning per share (EPS_{it}) and book value per share ($BVPS_{it}$).

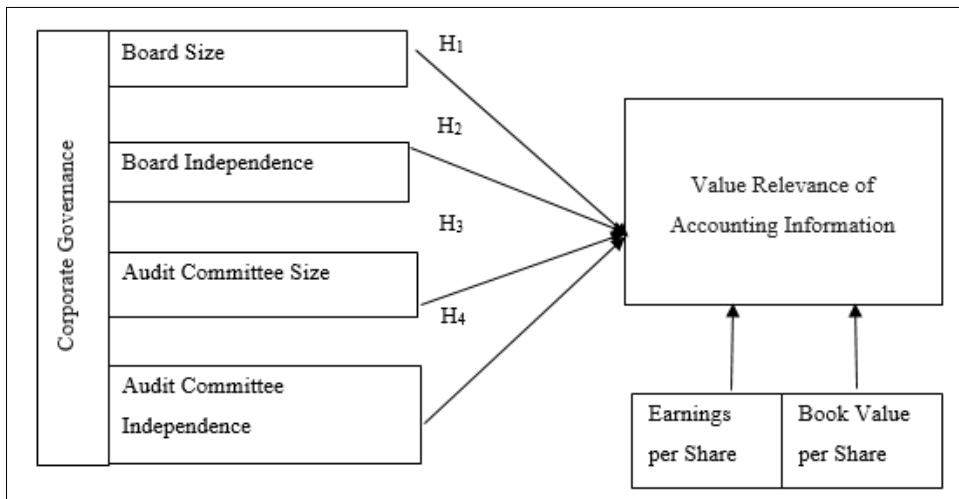


Figure 1 Conceptual Framework

Based on the conceptual framework, the four hypotheses are developed: H₁: BSIZE has a significant impact on the value relevance of accounting information in listed firms in CSE, H₂: BODIND has a significant impact on the value relevance of accounting information in listed firms in CSE, H₃: ACSIZE has a significant impact on the value relevance of accounting information listed firms in CSE, H₄: ACIND has a significant impact on the value relevance of accounting information listed firms in CSE. The total population consists of 288 listed companies. Even though all types of enterprises may engage with CG, only publicly listed companies are evaluated in this study. This study focuses on only companies with a financial year ending 31 March. Sectors of the bank, insurance, and diversified financials are excluded in this study. Because it is a highly regulated sector and previous scholars excluded the banking sector. Accordingly, the sample consists of 126 CSE-listed companies. The

correlation and regression analyses were performed to achieve the research objectives. The hypotheses are interpreted based on the results of the multiple regression analysis.

RESULTS AND DISCUSSION

In order to satisfy the objectives of this study, data cleaning and screening techniques, diagnostic test analysis (i.e., testing for linearity, normality, multicollinearity, and heteroscedasticity), descriptive statistics, and multivariate analyses were performed. According to the descriptive analysis, the average value of $BSIZE_{it}$, $BODIND_{it}$, $ACSIZE_{it}$, and $ACIND_{it}$ are higher than their standard deviation. It represents that they fluctuate by a significant amount in sample companies. As per the correlation analysis, it can be noted that share prices are positively correlated with EPS and BVPS but negatively related with $BSIZE_{it}$, $BODIND_{it}$, $ACSIZE_{it}$, and $ACIND_{it}$.

Table 1 Result of Random Effects Model (Multiple Regression Analysis)

Model	Coefficient	Standard Error	t Value	Significant
Constant	111.453	56.928	1.960	0.050
BSIZE	-0.539	1.849	-0.290	0.771
BODIND	-137.284	39.814	-3.450	0.001
ACSIZE	-0.471	3.448	-0.140	0.891
ACIND	102.172	28.920	3.530	0.000
EPS	0.961	0.308	3.120	0.002
BVPS	0.012	0.004	3.060	0.002
R ²	0.178			
Prob>chi ²	0.078			

Table 1 presents the multiple regression summaries. Based on the Hausman test results, the random-effect panel regression model was chosen as the appropriate effect for the current investigation. The respective R² value of 0.178 denotes that 17.8% of the observed variability in share price can be explained by the differences in variables, namely $BSIZE_{it}$, $ACSIZE_{it}$, $BODIND_{it}$, $ACIND_{it}$, EPS_{it} , and $BVPS_{it}$. This model demonstrates that the coefficient for each of the four variables - $BODIND_{it}$, $ACIND_{it}$, EPS_{it} , and $BVPS_{it}$ is significant at the 0.05 level, demonstrating that these factors have a considerable impact on SP_{it} . The coefficient of $BSIZE_{it}$ and $ACSIZE_{it}$ indicate that these variables do not affect the value-relevance of the accounting information measure of SP_{it} . According to the regression analysis, there was no significant impact of $BSIZE_{it}$ on the value relevance of accounting information (significant value - $p > 0.05$) of listed firms in CSE. Therefore, there is no significant impact of $BSIZE_{it}$ on the value relevance of accounting information in Sri Lanka (Balagobei, 2018). Moreover, there was a significant negative impact of $BODIND_{it}$ on the value relevance of accounting information (significant value - $p < 0.05$) (Balagobei, 2018). According to regression analysis, there was no significant impact of $ACSIZE_{it}$ on the value relevance of accounting information (significant value - $p > 0.05$) (Bahri et al., 2013). According to the test results, the $ACIND_{it}$ has a positive impact on the value relevance of accounting information (significant value - $p < 0.05$) (Ibanichuka & Captain Briggs, 2018).

CONCLUSIONS AND IMPLICATIONS

This study aimed to investigate the impact of corporate governance, specifically the effects of different corporate governance structures, on the value relevance of accounting information in listed firms in CSE. The findings highlighted that independence of the board, independence of the audit committee, EPS, and book value per share significantly affect the share price in listed companies in Sri Lanka. Results further show that CG is also an essential determinant of the value-relevance of accounting information. The study's findings have implications for both practitioners and policymakers. It gives information about the CG characteristics and accounting factors that affect a firm's market value. The study's findings thus imply that it is essential to ensure businesses follow the CG code. The study has several restrictions. This study included only five years of details of 126 non-financial listed companies is the limitation of this study. Larger sample size and the development of governance variables in future studies can lead to more accurate findings. In addition, the time frame of conduct to study is another limitation to collecting data. In the Sri Lanka context, there is a paucity of research in corporate governance on the value relevance of accounting information. The independent variable for corporate governance also only took into account board characteristics. The coverage of a few key control variables has to be expanded when examining how corporate governance impact the value relevance of accounting information in this study.

Keywords: Accounting information, Colombo Stock Exchange, corporate governance, value relevance

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