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**THE USE AND PERCEIVED USEFULNESS
OF IAS 29 GENERAL PRICE LEVEL INFORMATION
IN ZIMBABWE**

Research Dissertation

Presented to

**THE DEPARTMENT OF ACCOUNTING
UNIVERSITY OF CAPE TOWN**

**In Fulfilment of the
Requirements for the**

**MASTERS IN COMMERCE (DISSERTATION ONLY)
IN
FINANCIAL ACCOUNTING**

BY MALCOLM LEVY

MARCH 2003

DECLARATION

I declare the following:

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ACKNOWLEDGEMENTS

First and foremost, I wish to thank Professor Geoff Everingham of the University of Cape Town, the supervisor of this study, for his direction, review and guidance. At times, communication has been difficult, the fieldwork being performed in Harare. I am most grateful for his continued encouragement and refocusing in order to allow this study to be completed, despite the logistical difficulties encountered.

Secondly, I wish to express my appreciation to Mr. Les Anderson, senior partner at Deloitte & Touche Harare and highly respected member of the Institute of Chartered Accountants of Zimbabwe, sitting on several of their committees. Mr. Anderson was the Institute appointed supervisor to this study and I am extremely grateful for the way in which he gave this study a practical relevance that would otherwise have been sorely lacking. He has put up with continual quizzing on the technical aspects of the implementation of '29' in Zimbabwe and despite numerous other commitments, has always found the time to give guidance in the preparation and review of the material. His knowledge of the Zimbabwean market-place has proved invaluable.

I would also like to extend my appreciation to others within the institute who have given their full-fledged support and advice when I have required it. In particular, I must single out Mr. Bryan Thorn, Managing Senior Partner at Deloitte & Touche Harare and head of the 'IAS 29 Task Force', for his contribution to various aspects of this study.

SYNOPSIS

Hyperinflation, as defined in IAS 29, was identified in Zimbabwe in November 1999. Accordingly, the standard, and its General Price Level adjustments, was adopted for financial years beginning on 1st January 2000. However, there has been much resistance to the implementation of the standard, which is considered to require the provision of costly, meaningless information that is not used by anyone in the investment process. This study attempts to determine the use and perceived usefulness of IAS 29 in Zimbabwe and to identify the significant problems and weaknesses in the restatement process that have caused this.

The study found both the use and perceived usefulness of IAS 29 General Price Level information to be extremely low. The major reason cited for this was the lack of user understanding. The other major problems related to the perception of inconsistent methods and assumptions in the restatement process, as well as the use of the CPI, accused of being manipulated by government, as the basis of restatement. These issues need to be addressed by the Institute of Chartered Accountants, in consultation with the other accounting regulatory bodies, before the use and perceived usefulness of the IAS 29 General Price Level information can improve. Further, the study indicates that, whilst the preparers of financial information are extremely undecided as to the manner in which the accounting regulatory bodies in Zimbabwe should proceed, the analysts using such information are very much in favour of retaining the disclosure of inflation adjusted figures in some form, until such time as the inherent usefulness of the information is either proved or disproved.

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University of Cape Town

Introduction

“The Edgars group has accepted that it should conform with the requirements of IAS29 and has included inflation adjusted statements in its published accounts. However, the board of directors disassociate themselves from these statements as they are grossly misleading and have little value in assessing the true results of the business.” (Edgars Annual Report: January 2001).

In November 1999, hyperinflation as defined in IAS 29 was identified in Zimbabwe. IAS 29 requires General Price Level (GPL) adjustments to be made to financial statements, thereby representing a significant move away from traditional historic cost accounting to adjusted historic cost accounting. However, as is suggested in the above quote from the Edgars annual report, the implementation of this standard has not been well received in Zimbabwe. Appendix A contains a selection of published comments in this regard, demonstrating much antagonism to the adoption of IAS 29. This study attempts to determine the **use and perceived usefulness** of the IAS 29 GPL information that is required to be disclosed in Zimbabwe.

The objective of this study is to address the problem presented in the previous paragraph through a comprehensive collection of the views and opinions of a broad spectrum of users of financial information. The study has been performed in consultation with the Institute of Chartered Accountants of Zimbabwe and it is hoped the findings will be useful, in particular, to the Institute appointed ‘IAS 29 Task Force’. This task force has been charged with determining the appropriate manner in which to proceed with respect to the implementation of this difficult standard.

Chapter 2 will give readers an introduction to the Zimbabwean context, the accounting regulatory structure and an overview of the economy. This is followed in chapter 3 by an in-depth look at the conceptual framework for inflation accounting, together with a discussion on the development of these concepts through experiences in various countries. Chapter 4 then examines, in some depth, the prior research into the usefulness of inflation adjustments in accounting.

Chapter 5 introduces the methodology followed, being a questionnaire based approach to two sets of users, namely to the preparers of financial information and to the analysts of such information on the Zimbabwe Stock Exchange. Chapters 6 and 7 discuss the findings of these questionnaires, from which conclusions and recommendations are drawn in chapter 8.

An Introduction to the Zimbabwean Context

2.1 The Zimbabwean Economy

The Zimbabwean Economy is in turmoil. Simba Makoni, the Minister of Finance, stated in his 2002 / 2003 budget speech that all major sectors of the economy have suffered real declines of more than 5% due to the high rate of inflation, which increased production costs (Zimbabwe Independent, 7th June 2002). Low commodity prices for agricultural and mining exports, and acute foreign currency shortages, made the import of raw materials and spare parts increasingly difficult. As a result it was estimated that the economy shrunk in real terms by 7.3% in 2001, compared to a decline of 4.2% in 2000. At the end of February 2003 the year-on-year inflation as calculated by the Central Statistical Office stood at a staggering 220%, with no sign of slowing.

Three particular events are commonly cited as leading to Zimbabwe's rapid decline from having been a relative economic powerhouse in Southern Africa. In August 1997, President Robert Mugabe ordered unbudgeted pension payments of some Z\$3.6 billion to veterans of the country's 1970's liberation war (Hawkins, 2002). This was followed in November 1997 with an initial list of 1,471 farms gazetted for compulsory acquisition. Then in August of 1998, Zimbabwe entered the civil war in the Democratic Republic of the Congo (DRC) in support of the embattled President Laurent Kabila. This was again at a huge extra, and unbudgeted, cost. These actions in time lost the much-needed support of the IMF and World Bank and left Zimbabwe to its own devices. More recently, following the presidential elections in March of this year, investor confidence is at an all-time low. The government has attempted to control inflation with the implementation of price controls. Consequently the economy has been plagued with the concomitant shortages of these price-controlled products, together with a growing black market in which these goods change hands at often unscrupulous prices. The rate of unemployment exceeds 70% and 80% of people live below the Poverty Datum Line (PDL) (Bloch, 2002).

Despite the backdrop of ballooning inflation, government has pegged the exchange rate at 55 Zimbabwe dollars to the US dollar. This has created a parallel market where much needed foreign currency changes hands at more realistic rates. At the time of writing, the parallel rate against the US dollar is in the region of ZWD1500-2000 to USD1 and 150-200ZWD to ZAR1 against the South African rand. This is between 27 and 36 times the official exchange rate. In an

attempt to control this parallel market, the government is threatening to return to a system whereby all foreign currency is administered centrally through the Reserve Bank.

The other area that has led to the Zimbabwean economy being described as dysfunctional is that of interest rates. Government has maintained a surplus in the money market in order to keep interest rates at low levels, currently 25 – 30%. This is nearly a phenomenal 200% below the rate of inflation. In search of real returns, investors have had to look to the real estate and stock markets, which have boomed over the last 3 years. The manner in which the government is encouraging borrowing and a highly geared economy, in times when real GDP is declining, is contrary to usual economic principles.

In summary, the Zimbabwean economy is plagued with numerous factors that show no sign of resolution in the immediate future. Accordingly, the high rates of inflation, and other economic ills, will undoubtedly continue in the short to medium term. The economy outlined above creates an interesting challenge for accountants in trying to portray fairly the substance of what has occurred over a financial period.

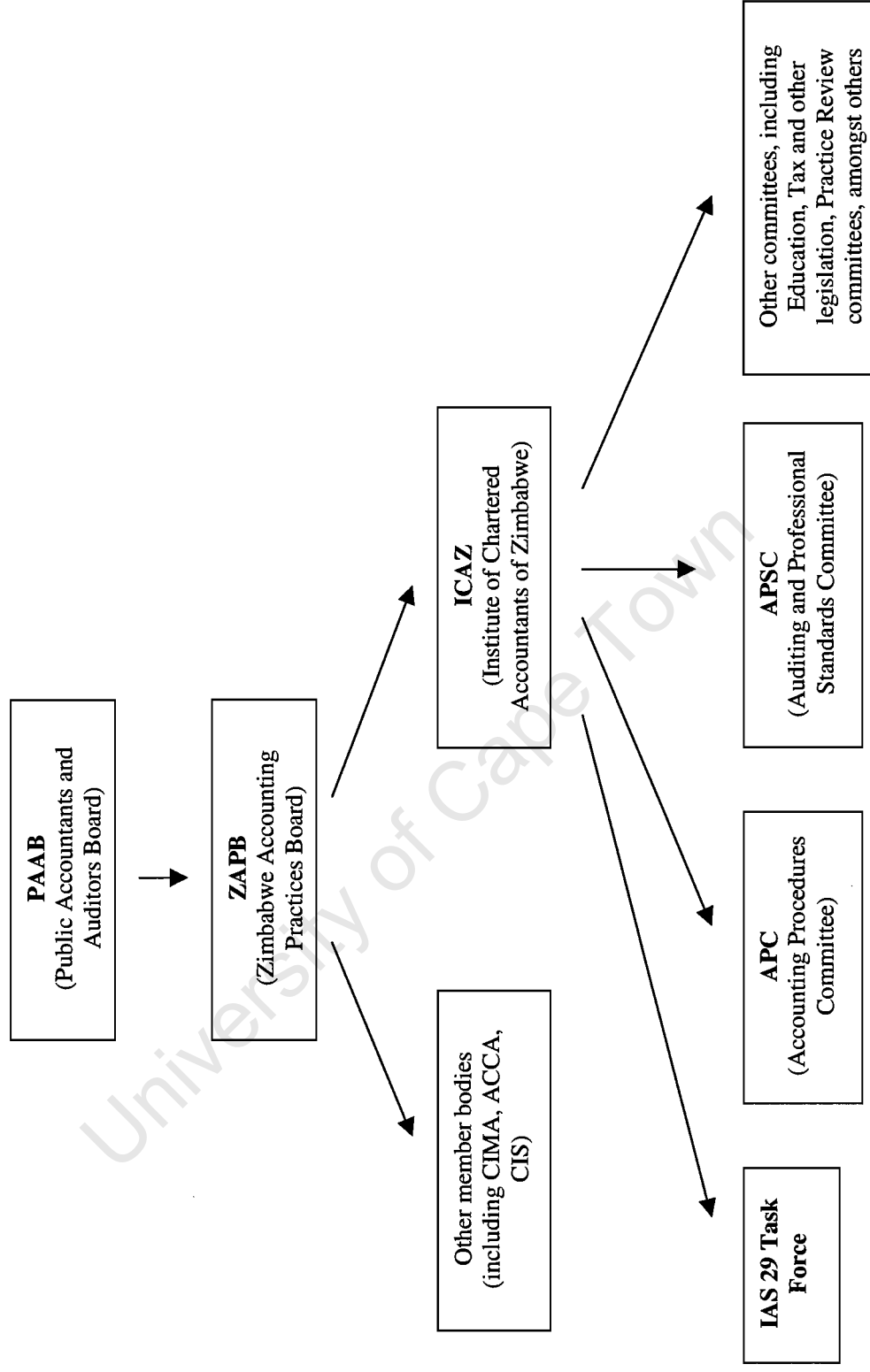
2.2 The Accounting Regulatory Structure and Situation in Zimbabwe

The situation in Zimbabwe is somewhat unusual in that it is one of very few English speaking countries, with a regulated accounting body, that has suffered the effects of hyperinflation. This section initially outlines the regulatory accounting structure in Zimbabwe, followed by a discussion on the current situation and problems faced by these regulatory bodies.

2.2.1 The Regulatory Structure

In figure 2.1 on the next page is a diagrammatic representation of the regulatory accounting structure in Zimbabwe. The overall regulatory body is the Public Accountants and Auditors Board (PAAB), which has ultimate control over accounting regulation in Zimbabwe. The PAAB has formed the Zimbabwe Accounting Practices Board (ZAPB) as its standard setting body, although ultimate authority still rests with the PAAB. The ZAPB and PAAB have as their members several institutions, all with an equal vote. These include the Institute of Chartered Accountants of Zimbabwe (ICAZ), Chartered Institute of Management Accountants (CIMA), Association of Chartered Certified Accountants (ACCA) and the Chartered Institute of Secretaries (CIS). Most of the deliberation with respect to IAS 29 has occurred at ICAZ. However, they have only one equal vote on the ZAPB, which remains an area of concern insofar as any initiatives by the Institute of Chartered Accountants may be stifled by the ZAPB.

Figure 2.1 The Accounting Regulatory Structure in Zimbabwe



ICAZ, on the other hand, has various committees falling beneath it. The relevant committees include the Accounting Procedures Committee (APC), the Auditing and Professional Standards Committee (APSC) and the IAS 29 Task Force. All of these bodies refer directly to ICAZ (Council). The IAS 29 Task Force is the body that has been tasked with investigating the impact and relevance of inflation accounting and IAS 29 in Zimbabwe and recommending proposals for the way forward. Council considers these proposals, together with the APC's and APSC's comment. If accepted by Council (ICAZ), the proposal is then presented to the ZAPB. However, as mentioned, ICAZ have only an equal vote to each other individual member of the ZAPB.

2.2.2 The Current Situation

Hyperinflation as defined in IAS 29 was identified in November 1999. Due to the obvious difficulty of immediate compliance, ICAZ, in consultation with the Zimbabwe Stock Exchange (ZSE), agreed that all financial statements needed to be IAS 29 compliant only from financial year-ends beginning 1 January 2000. This effectively gave the December year-end companies (the majority of companies on the ZSE) an extra year in which to put together the necessary information for compliance. After consultation with the ZSE, it was agreed that there be a three year phase-in period during which the historic accounts be placed alongside the inflation adjusted results to allow a period of user familiarisation.

In July of 2001, ICAZ indicated in a newsletter that members were having many difficulties and problems with IAS 29 and that Council had decided to set up a task force to examine these. Commerce, industry and the profession are all represented and both the regional representative of the International Accounting Standards Board, Bob Garnett, and the IASB itself were asked to participate.

After much deliberation, the first recommendation of the IAS 29 Task Force was accepted by Council and presented to the ZAPB at the beginning of 2002. The Task Force considered several proposals. "One proposal was for the income statement to be adjusted by an index applicable to the industry or group of industries with an adjustment for depreciation on restated fixed assets. The mining industry believed that, given the extent of dealing in foreign currency in the trading cycle, historical cost financial statements should be translated to US\$ financial statements by using a fair exchange rate in terms of purchasing and selling" (Report of the IAS 29 Task Force: pg 1).

Deliberations resulted in three options being proposed for consideration:

1. To continue application of IAS 29 in its current form.
2. To provide information that would result in a true and fair 'override' (IAS 1 allows the 'override' of a standard where it is deemed to be inappropriate – this is discussed in detail below). The details of this option would have been:
 - Restated income statement and balance sheet alongside the historic accounts;
 - Show monetary gain / loss as part of income;
 - Examine the non-monetary balance sheet on the basis of fair value (checking that restated figures approximate fair values);
 - Do not repeat the preparation of notes to the financial statements to disclose restated items;
 - Only prepare a historic cost cash flow statement;
 - For specific industries, where significant transactions are aligned to a foreign currency, such as mining, permit restatement on the basis of translation to a foreign currency, disclosing the exchange rate used;
 - Where the general CPI is deemed to be inappropriate in the restatement exercise, use of an industry specific index would be allowed, with disclosure of such indices;
 - All ZSE companies would be required to comply with these disclosures, those companies not complying with the 'override' being qualified.
3. Recommend non-compliance with IAS 29 and return to the old system of the PAAB having a set of standards "adopted for use in Zimbabwe." (This system allowed the Institute to selectively adopt International Accounting Standards, but was abandoned prior to the adoption of IAS 29.)

The report concluded that proposal 2 was favoured, but that proposal 3 should also be considered (Report of the IAS 29 Task Force: pg 1).

It is perhaps not surprising that the ZAPB rejected these proposals and indicated that companies were to continue in the current format of comprehensive IAS compliance. Allowing certain companies to use industry specific indices destroys comparability of the financial statements across entities and goes against the overall objective of general purchasing power accounting. It is akin to two companies translating to US dollars at different exchange rates. The official reasons for the non-acceptance of ICAZ's proposal were the concerns that non-compliance with the standard could affect Zimbabwe's standing as a member of the IASB and that non-

compliance with IAS 29 might also set a precedent for non-compliance with other standards such as 'IAS 12: Income Taxes' and 'IAS 39: Financial Instruments: Recognition and Measurement'.

Proposal 2 might have been an attempt to move in the direction of an IAS 1 'fair presentation override', but fell short in certain areas. IAS 1, paragraph 13, states that in "the extremely rare circumstances when management concludes that compliance with a requirement in a Standard would be misleading, and therefore that departure from a requirement is necessary to achieve a fair presentation, an enterprise should disclose:

- (a) that management has concluded that the financial statements fairly present the enterprise's financial position, financial performance and cash flows;
- (b) that it has complied in all material respects with applicable International Accounting Standards except that it has departed from a Standard in order to achieve a fair presentation;
- (c) the Standard from which the enterprise has departed, the nature of the departure, including the treatment that the Standard would require, the reason why that treatment would be misleading in the circumstances and the treatment adopted; and
- (d) the financial impact of the departure on the enterprise's net profit or loss, assets, liabilities, equity and cash flows for each period presented" (author's underlining.)

From the above discussion, it is clear that the intention of the Standard is for management to make the decision that the application of a Standard is misleading, and not for the regulatory accounting body to make the decision for commerce and industry as a whole. The focus on the decision being made by management also appears in the recently released 'Exposure Draft of Revised IAS 1'. However, the exposure draft does state that such departure must be in line with the 'relevant regulatory framework' (para. 13) indicating that the regulatory authority should take a position in this regard. The exposure draft goes further than the current IAS 1 and states in paragraph 16 that there is "a rebuttable presumption that if other entities in similar circumstances comply with the requirement, the entity's compliance with the requirement would not be so misleading that it would conflict with the objective of financial statements set out in the Framework".

Critics of IAS 29 frequently state that the Standard is not applicable for reasons including the existence of managed interest rates, exchange rates and Consumer Price Indices in Zimbabwe. These are discussed in detail later in this report. However, to state that these issues produce misleading results, across the board and for all industries, is a bold move and may be indicative more of a feeling of the irrelevance of general purchasing power accounting than merely due to

the peculiarities of the Zimbabwean economy. If the peculiarities of managed interest rates, exchange rates and Consumer Price Indices were removed, it is likely that the critics would still be calling for the removal of the standard. It has been commented by analysts in discussions relating to this study that the peculiarities of the Zimbabwean economy are being used as scapegoats for critics of IAS 29 to win their way.

With the rejection of their first report, the 'IAS 29 Task Force' reconvened to further consider the various alternatives. The second report has been sent to Council for consideration, but as at the end of February 2003 has yet to receive the official position of the APC and APSC on the recommendations proposed. These measures are more of an interim nature and not necessarily the final solution. This time it is proposed that companies be given the choice to follow one of three options:

- Option 1: Continue to prepare financial statements in the current format, i.e. with the primary set of financial statements being the restated figures and the inclusion of the historical figures for comparative purposes.
- Option 2:
- 2.1 A commentary addressing how management has addressed the impact of inflation on the entity.
 - 2.2 Prepare inflation adjusted income statement and balance sheet as schedules without detailed supporting notes. The aim of this would be to cover the IAS 1 true and fair 'override', which requires the quantification of the impact of non-compliance on material components of the financial statements.
- Option 3: Prepare inflation adjusted financial statements as the only set of financial statements.

On this occasion, the Task Force recommended a move towards a situation whereby the companies themselves would be given a choice of which option to follow, possibly in an attempt to compromise between varying schools of thought. What is also significant in this second proposal is the removal of the option of abandoning the use of IAS 29 altogether. Thus IAS 29 shall remain, in one form or another, for some time to come. However, with respect to this second document, Council has yet to consider the views of both the APC and APSC. In particular, the above options would have a significant impact on the audit report and the position of the APSC in this regard will be critical to the acceptance of the proposal by Council, before it

goes once again to the ZAPB. However, given the carte blanche the above proposal gives to management as to which option they may follow, it seems unlikely that either the APC or APSC will view the recommendations favourably, let alone the ZAPB.

Nonetheless, option 2 moves far closer to the IAS 1 true and fair 'override' in that it fulfills the requirement of quantifying the financial effect of non-compliance. Option 1 is not much different from option 3 and requires little extra work, all numbers for either option being readily available. The only difference is the non-disclosure of the historic results in option 3, a strict interpretation of the standard that recommends the non-disclosure of historical figures as they are misleading (IAS 29: Financial Reporting in Hyperinflationary Economies, para. 7.) However, given the understanding in the market place of the inflation-adjusted figures, or lack thereof, option 3 is not a practical solution. This is strongly confirmed in this study through the questionnaire to analysts.

2.2.3 Conclusion

From the above discussion, it can be seen that there remains tremendous uncertainty as to the way forward, particularly from the ICAZ perspective. It appears as though the critics of IAS 29 are focussing their retort at the Institute, which in turn, whilst trying to please both proponents and antagonists, has to contend with having only one vote on the ZAPB. Attempts by the writer to determine the extent of work being done on inflation accounting by the various other member bodies of the ZAPB have been fruitless, probably due to these other bodies not doing anything in this regard. The fact that they have individually an equal vote to ICAZ on the ZAPB is concerning. Nonetheless, ICAZ have attempted to move forward and continue their attempts at resolving the contention in the market-place as to the relevance and usefulness of IAS 29. However, in the meanwhile, the proponents lead the way and IAS 29 is here to stay, at least for the present time.

Theoretical Framework

3.1 Introduction

This chapter aims to build the theoretical framework for inflation accounting. Initially a discussion in terms of the Conceptual Framework illustrates the need for the impact of changing prices to be conveyed to users. The relevance of the income concept is investigated, and the definition of income will essentially form the basis of various methods of accounting for changing price levels. This leads to the four schools of thought concerning the measurement of business income, which stem from the underlying concepts of capital maintenance. With this foundation, the development of inflation accounting is then examined in some detail, with reference to the situations in various countries. In conclusion to the chapter, a section on 'IAS 29: Financial Reporting in Hyperinflationary Economies' is included, summarising the requirements of the standard.

3.2 The Conceptual Framework

The following discussion centres on the South African framework for accounting, with which the author is most familiar. However, it does not differ materially in any respect from Accounting Frameworks elsewhere in the world, and is a mirror image of the IAS framework. The Conceptual Framework states that the objective of financial statements is to "provide information about the financial position, performance and changes in financial position of an enterprise that is useful to a wide range of users in making economic decisions." (AC000, para .12). Useful information is then discussed in terms of the qualitative characteristics of financial statements, the principal four characteristics being understandability, relevance, reliability and comparability. Accordingly, financial statements should express the impact of inflation if the information content of such disclosures is considered useful.

Changing price-levels may distort the financial well-being of an enterprise. The conceptual framework would indicate that an expression of this distortion is necessary to fully explain the financial performance of an enterprise. However, this is difficult to do given that there remains no fully accepted system of comprehensively incorporating the impact of changing price-levels.

3.3 The Relevance of the Income Concept

The concept of income is important to both economists and accountants and is particularly relevant in the development of accounting for changing price-levels. In order to develop an appropriate system of accounting, there is a need to clearly define what is being measured. Belkaoui (2000: 390) points out that Adam Smith was the first economist to define income, which he said was an increase in wealth. Hicks, following the work of Von Bohm Bawerk, Fisher and Lindahl, went on to define income as “the maximum value (one) can consume during a week, and still expect to be as well off at the end of the week as at the beginning” (Hicks, 1946: 172). Belkaoui (2000) indicates the problem raised by this definition, being the manner in which to determine ‘well-offness’. “The most accepted interpretation is that of capital maintenance, in which case the ‘Hicksian’ income is the maximum amount that may be consumed in a given period and still maintain the capital intact” (Belkaoui, 2000: 391).

Accounting income, on the other hand, has historically been concerned with revenues and expenses. This is evidenced, for example, in the AICPA’s statement of ‘Basic Concepts and Accounting Principles’ (1970) which defined net income (loss) as “the excess (deficit) of revenue over expenses for an accounting period” (AICPA, 1970: para .134). However, Mathews and Perera (1991) point out that significant attempts have been made at widening the scope of the accounting concept of income. Edwards and Bell (1961) in particular promoted a more comprehensive view of income which “advocates the reporting of holding gains and losses during a period, on the grounds that such reporting would increase the information content of financial statements” (Mathews and Perera, 1991: 157). The FASB’s conceptual framework has since recognised the importance of adopting a more comprehensive approach to income. “FASB (1980), later superseded by FASB (1985), attempts to widen the scope of the measurement of the business enterprise operations by using an asset-liability approach instead of the traditional revenue-expense approach” (Mathews and Perera, 1991: 159-60). FASB (1985) defined comprehensive income as the change in equity of an entity during a period from transactions with non-owners.

The use of the words “holding gains and losses” by Edwards and Bell (1961) is significant in that it represents a move away from one of the conventional rules of accounting that determines that income is only recognised when ‘realised’. Mathews and Perera (1991) loosely define ‘realised’ as converted into money, or a claim to money. Thus Edwards and Bell (1961) proposed that unrealised holding gains should also be included in income. Under the historical cost assumption of constant price-levels, no unrealised holding gains or losses should arise. However, as inflation increases, these holding gains or losses become significant, and an expression of them becomes

necessary. The seminal contribution by Edwards and Bell (1961), however, “while well received in academic circles, had little influence on accounting practice” (Everingham and Watson, 1999: 220).

Antagonists to any change of the traditional concept of income have not been without their say and have presented several advantages of the traditional model of accounting income. Belkaoui (2000: 389) presents these as follows:

- Accounting income has survived the test of time. Had users not found this information useful over the years, changes would long since have been made
- Accounting income is reported objectively and is basically verifiable
- Accounting income is prudent, as evidenced by the realisation principle
- Accounting income is useful for control purposes, especially in reporting on stewardship, and conveys the way in which management has met its responsibilities

Nonetheless, attempts have been made at widening the scope of the definition of income. No one definition of income has been readily accepted. “Indeed, the various methods proposed and their rapid appearance and withdrawal probably resulted more in confusion than in enlightenment” (Tweedie & Whittington, 1985: 156). With inflation having declined significantly in the mid-1980’s in the developed world, this problem relating to the definition of income remains unresolved.

3.4 Concepts of Capital Maintenance

3.4.1 Definition of Income

This section aims to look in more detail at the various definitions of income mentioned in the preceding section, discussing in more detail their theoretical roots. Belkaoui (2000) indicates that the measurement of business income can basically be broken down into four schools of thought.

The first group, which he calls the ‘*classical school*’, “is characterised primarily by adherence to the unit-of-measure postulate and the historic cost principle” (Belkaoui, 2000: 385). This classical school essentially regards historic cost accounting income as business income and conforms to the money maintenance definition of income.

The ‘*neo-classical school*’ abandons the “unit of measure postulate” (Belkaoui, 2000: 385) and recognises changes in the general level of prices. This school regards general price level adjusted

accounting income as business income and conforms to the general purchasing power money maintenance definition of income.

The '*radical school*', on the other hand, "is characterised by its choice of current values as the valuation basis" (Belkaoui, 2000: 385) and is essentially divided into two forms. The first form makes no adjustments for changes in the general level of prices. "Generally known as current value accounting, this school's concept of business income is 'current income'" (Belkaoui, 2000: 385), and conforms to the productive capacity maintenance definition of income. The other form of the '*radical school*' also makes adjustments for changes in the general level of prices. "Generally known as general price level adjusted current value accounting, this school's concept of business income is 'adjusted current income'" (Belkaoui, 2000: 386), and conforms to the general purchasing power productive capacity maintenance definition of income. Belkaoui (2000:392) alludes to problems in the interpretation of 'productive capacity' and refers to the *Sandilands Report* in the United Kingdom, which posed the question of what was meant by a company's 'productive capacity' and how was it to be maintained intact? The *Sandilands Report* presented three alternative classifications of productive capacity:

- Productive capacity defined as the physical assets of the company. Thus profit is the amount that could be distributed after making sufficient provision for the replacement of the physical assets.
- Productive capacity defined as the capacity to produce the same **volume** of output.
- Productive capacity defined as the capacity to produce the same **value** of output.

As mentioned, each school of thought makes reference to an underlying concept of capital maintenance. The implication of capital maintenance is that income should only be recognised after capital has been maintained or costs have been recovered. (Belkaoui: 2000). The conceptual framework states that "profit is the residual amount that remains after expenses (including capital maintenance adjustments, where appropriate) have been deducted from income." (AC000, para 105). This distinguishes between return on capital (income) and return of capital (cost recovery).

The various concepts of capital maintenance discussed above give rise to differing definitions of income. It is important to note that if both the general and specific level of prices were to remain constant, all of the above definitions would arrive at the same income. The definition of income, with respect to inflation accounting, only becomes relevant as the general and / or specific levels of prices begin to change.

3.4.2 The Definition of Income in a Zimbabwean Context

At this point it is relevant to discuss the concepts of capital maintenance with respect to Zimbabwe and the situation under investigation. 'IAS 29: Financial Reporting in Hyperinflationary Economies' requires companies to make adjustments for changes in the general level of prices, irrespective of whether the underlying basis of valuation is historic or current cost. This implies that if companies have been following the money maintenance concept of capital maintenance discussed above, they are required to incorporate general purchasing power adjustments with that concept. If, however, companies have been following a form of current value accounting, such as current costing, then they would be required to conform to a general purchasing power productive capacity maintenance definition of income. Nonetheless, no companies listed on the Zimbabwe Stock Exchange have adopted a comprehensive form of current value accounting, except to the extent that property, plant and equipment and financial instruments may have been revalued or inventories or other current assets reduced to net realisable value. Accordingly, the money maintenance and general purchasing power money maintenance concepts are relevant to the determination of income in Zimbabwe, current value accounting not being encountered in any comprehensive manner. The example of the application of IAS 29 in Zimbabwe included in Appendix B follows this definition of income.

3.5 Systems of Accounting for Inflation

Following from the above discussion on the definition of income, it can be seen that there are two separate methods of accounting for the impacts of inflation, general price level accounting and current value accounting. A third method, a combination of these two, is also possible.

3.5.1 Current Value Accounting

Current value accounting follows from the productive capacity concept of capital maintenance. Thus adjustments are made for changes in the specific level of prices in order to maintain operating capacity. However, in its pure form, this ignores the general purchasing power of capital. Current cost accounting has historically been the preferred method of current value accounting and gained popularity when the British Government's Inflation Accounting 'Sandilands' Committee "recommended a fundamental change from (the) historic cost convention to 'value to the business'" (Mathews and Perera, 1991; 174). However, Mathews and Perera go on to discuss the manner in which current value accounting does not escape the

criticism of being partial, in that it tends to disregard the effects of inflation on the significance of the monetary unit in which financial statements are presented.

Current cost accounting, following the 'Sandilands Committee's' recommendation, was initially met with resistance. The 1977 'Hyde Committee' attempted to clarify the issues identified and suggested that three adjustments be made to the historic accounts. These were the cost of sales, depreciation and gearing adjustment. Mathews and Perera indicate that the gearing adjustment, not initially proposed by the 'Sandilands Committee', was an acceptance that monetary adjustments could not be completely ignored in an inflation accounting system. IAS 15 'Information Reflecting the Effects of Changing Prices', however, makes it very clear that there remains no fully accepted method of current value accounting, discussing in particular whether the gearing adjustment mentioned above should include adjustments for all monetary liabilities, or for only those included in working capital. Further, there is disagreement as to whether adjustments to equity should be made to reflect the change in the general level of prices.

It is interesting to note that the South African guideline AC201 has adopted a current value approach and makes no mention of adjustments for general purchasing power. IAS 15 on the other hand suggests that either a current value or a general purchasing power approach be adopted.

3.5.2 General Purchasing Power Accounting

General Purchasing Power Accounting is frequently referred to as General Price Level accounting (GPL) and such a classification is used for consistency throughout this report. This method of accounting for changing price-levels attempts to remove the effect of general increases in the level of prices. All items in the income statement and balance sheet are adjusted to a consistent price-level, usually the price-level at the end of the reporting period. Monetary items are already stated in terms of the purchasing power current at year-end and thus do not require adjustment. Monetary gains or losses arise from movements in monetary position and are included in income.

Mathews and Perera (1991:172) point out that the degree of objectivity under general purchasing power accounting (GPL) and historic cost are virtually the same, apart from the selection of an index. As the effect of this method is to maintain the purchasing power and not the nominal value of capital, the income figure becomes somewhat of a better guide to economic performance. However, the weakness of pure GPL relates to adjustments to the values of assets not being good indicators of current values, even if these are better in times of inflation than the

unadjusted figures (Mathews and Perera, 1991: 172). Changes in the specific level of prices lead to a distorted balance sheet in terms of general purchasing power accounting. The example of electronic and computer goods is much cited in that these often decrease in price, even in times of inflation. Making general purchasing power adjustments to such assets is meaningless.

At this point it is worth pointing out the difference between what is often referred to in the literature as constant dollars and current dollars. Constant dollars merely refers to the presentation of financial information in terms of the purchasing power of some base year. Accordingly adjustments may be required to deflate the current unit to that of the base year. Current dollars, however, relate to the monetary unit current at the end of the reporting period. The adjustments, whether inflating or deflating, are conceptually identical.

3.6 The Development of Inflation Accounting

As can be seen from the table 3.1 on the next page, early attempts by standard setters to account for the impact of inflation were focused on a general purchasing power approach, with standards and exposure drafts to that effect in both the UK and the USA. Other countries, including Canada, Australia and New Zealand, also appeared to show interest in general purchasing power accounting around the similar time, up until the mid-1970's. However, the much-cited Inflation Accounting ('Sandilands') Committee in the UK, discussed above, published its report in September 1975. This recommended that, as soon as practicable, "all companies should adopt an accounting system to be known as current cost accounting, the main features of which were:

- a. Money is the unit of measurement.
- b. Assets and liabilities are shown in the balance sheet at valuation.
- c. Operating profit is struck after charging the value of the business of assets consumed during the period, thus excluding holding gains from profit and showing them separately." (Mathews and Perera, 1991: 190).

This 'Sandilands Report' changed the thinking with respect to inflation accounting and standard setters moved towards a system of current value accounting, GPL losing popularity. However, the concept of current cost accounting was also not well received and in the early 80's all of the countries that had flirted with the idea withdrew any mandatory requirements for application of the respective statements, such disclosures becoming entirely voluntary. There has been negligible voluntary compliance throughout the world. It is also important to note that at the time the rate of inflation in the developed world had once again declined to single digits. Accordingly, the focus moved onto more topical issues, leaving unresolved, in the first world, the debate on inflation accounting.

DEVELOPMENT OF STANDARDS IN THE UK AND THE USA

Table 3.1

The UK Experience

Year	Standard	Detail
1973	ED 8 – Accounting for Changes in the Purchasing Power of Money	Proposed supplementary general purchasing power accounts for listed companies
1974	PSSAP 7 – Accounting for changes in the Purchasing Power of Money	Provisional standard issued based upon ED 8
1975	‘Sandilands report’	Rejected general purchasing power accounting and recommended as system of current cost accounting
1976	ED 18 – Current Cost Accounting	Proposed introduction of a phased-in system of current cost accounting, based on the Sandilands Report
1977	Inflation Accounting - an Interim Recommendation by the Accounting Standards Committee (‘Hyde Guidelines’)	Recommended cost of sales, depreciation and gearing adjustment as supplementary disclosures in supplementary current cost income statement
1979	ED 24 – Current Cost Accounting	Proposed supplementary current cost accounts for large / listed companies.
1980	SSAP 16 - Current Cost Accounting	Statement issued, based upon ED 24, supplementary current cost accounts
1984	ED 35 – Accounting for the Effects of Changing Prices	Draft standard to replace SSAP 16 requiring current cost information as supplementary disclosures
1985	ED 35 – Accounting for the Effects of Changing Prices	Withdrawn
1985	SSAP 16 - Current Cost Accounting	Following widespread non-compliance, SSAP 16 becomes voluntary

The US Experience

Year	Standard	Detail
1969	APB 3	Recommended supplementary general price level information
1974	FASB Exposure Draft - Financial Reporting in Units of General Purchasing Power	Recommended supplementary general price level information
1976	ASR 190	Required supplementary disclosure of replacement cost information
1978	FASB Exposure Draft - Financial Reporting and Changing Prices	Recommended either supplementary current cost or supplementary general purchasing power accounts
1979	FAS - 33 - Financial Reporting and Changing Prices	Followed from exposure draft, but differed in requiring supplementary disclosures of both current cost and general purchasing power information
1980	ASR 190	Withdrawn
1984	FAS - 82 - Financial Reporting and Changing Prices: Elimination of Certain Disclosures	Issued as an amendment to FAS 33 removing the requirement of the general price level income statement disclosures
1986	FAS 89 - Financial Reporting and Changing Prices	Superseded FAS 33, making voluntary the current cost / general purchasing power disclosures

In 1977, the International Accounting Standards Committee issued IAS 6, soon followed by IAS 15 in 1982, neither of which took a view as to the appropriate method of accounting for prices (Everingham and Watson, 1999). However, at its meeting in October 1989, the Board of IASC approved the following statement to be added to IAS 15, Information Reflecting the Effects of Changing Prices:

“The international consensus on the disclosure of information reflecting the effects of changing prices that was anticipated when IAS 15 was issued has not been reached. As a result, the Board of IASC has decided that enterprises need not disclose the information required by IAS 15 in order that their financial statements conform to International Accounting Standards. However, the Board encourages enterprises to present such information and urges those that do to disclose the items required by IAS 15.”

At the same time, however, they issued ‘IAS 29: Financial Reporting in Hyperinflationary Economies’. The technicalities of the standard are discussed below, but it is important to note that at the time of issue there was certainly no consensus on the appropriate method of accounting for inflation. The thinking of the IASC at the time was the theoretical argument that high rates of inflation destroy comparability of figures over time, even where a current cost basis is used. This standard had minor adjustments in 1994 to bring the wording into line with other standards, but otherwise remains unaltered and forms part of the core standards submitted to and accepted by IOSCO. A quote by an analyst on the Zimbabwe Stock Exchange captures the sentiment of the standard in some corners of the Zimbabwe market-place, “it is an archaic remnant of an unresolved debate.”

Partial attempts at incorporating the impacts of inflation are entrenched in many standards in many countries. These include the revaluation of fixed assets and, more recently, the fair valuation of financial instruments. While these adjustments are undoubtedly attempts to bring to account the impact of inflation, they do not escape the criticism of being partial. Notably, from a current value point of view, they make no adjustment for the replacement of inventory, nor a gearing adjustment of any sort. More recent developments, such as the release of ‘IAS 40: Investment Properties’ and ‘IAS 41: Agriculture’ are significant in that they represent bold moves towards the carrying of non-financial assets at fair value, with adjustments being taken to income, and are the result of a definite move towards a fair value balance sheet. This move indicates a continued preference in the developed world for some form of current value accounting. Nonetheless, the argument remains that at high levels of inflation, comparability of figures is lost over time, even when a current costing system is in place.

Other countries have experienced high inflation, most notably in South America. "Financial statements in countries such as Argentina, Brazil and Chile have been adjusted by means of a general price index, which in some cases also form the basis for calculating taxation" (Everingham and Watson, 1999: 223). In this regard, the situation and system that has developed in Brazil is particularly interesting and worth discussion. However, as is continually alluded to in the literature review in the following chapter, the language barrier is significant in preventing an in-depth review of much of the available literature. Following the discussion on Brazil, IAS 29 is examined in more detail to investigate the methods of inflation accounting required and permitted in Zimbabwe.

3.7 The Brazilian Experience

The following discussion is drawn from a paper entitled "Innovations in Brazilian Inflation Accounting" by Douppnik, S; Martins, E and Barbier, G and appearing in 'The International Journal of Accounting' (1995). Brazil has experimented with methods of inflation accounting since the late 1950's. In 1976 a new 'Corporation Law' introduced the "System of Monetary Correction" (SMC). However, this system suffers several limitations and in 1987 the Brazilian Securities Commission (CVM) introduced a second system of inflation accounting, known as the "Integral Monetary Correction System" (IMCS). This section reviews these two methods and their development in Brazil, both of which have to be disclosed for public companies.

The SMC is very similar to other systems of GPL accounting. The only significant difference is the non-restatement of inventories. The reason for this is an attempt to make the system as feasible as possible and the system serves as the basis of financial reporting and taxation in Brazil. However, Douppnik et al. (1995: 304) criticise the system stating that "(a)nother problem inherent in such a relatively simple system is the loss of information which results from the accumulation of various inflation adjustments into one monetary correction amount. It is not possible to desegregate the various inflation adjustments incorporated into the monetary correction amount for the purpose of enhancing the information provided in the financial statements." From a taxation point of view, companies are allowed to defer unrealised 'inflationary profits', defined as the credit balance monetary correction amount, adjusted for interest income / expense. This has been challenged as having no conceptual backing but is nonetheless still followed by the authorities. Further limitations of the SMC relate to the use of indices that have suffered government manipulation. Douppnik et al. (1995: 304) describe this as by far the most serious limitation, reaching a peak in 1990 when reported inflation of 845% compared to a more realistic rate of 1,795%. This underlines the importance on the selection of index with GPL accounting.

The early to mid-1980's saw new governments and the introduction of new policies. On two occasions, the local currency had to be repudiated and replaced. The extreme rates of inflation exacerbated the weakness of the SMC and in 1987 the CVM introduced the "Integral Monetary Correction System" (IMCS). This has several conceptual improvements over the SMC, as well as other systems of GPL accounting encountered across the world. The three major refinements relate to the restatement of inventory, the disclosure of income statement items net of the monetary gain / loss that arose from delayed payment / receipt and the discounting of receivables / payables.

The restatement of inventory is obviously necessary in any system of GPL accounting, particularly in climates where inflation is as extreme as it has been in Brazil. The second refinement, however, is somewhat more interesting. Doupnik et al (1995) indicate that under IMCS, purchasing power gains and losses are treated as components of income. The 'major innovation' is that these gains and losses are not reported as a single line-item, but are adjusted to their related income statement amounts. To illustrate this, Doupnik et al (1995) give the example of wages. The expense is restated over the period over which it accrues, and for the sake of indexation this may be assumed to be the middle of the month. However, the payment of these wages is delayed to the end of the month and a purchasing power gain therefore arises. Under the IMCS, this gain is written back against the wage expense, giving a more real reflection of what was expended, from a purchasing power point of view, on wages for the month. This is certainly progressive and does not appear in the literature of accounting systems from other parts of the world. Further, the application of this idea in practice would be extremely difficult, particularly in Zimbabwe where significant grievances have been expressed over a somewhat simpler system.

As mentioned earlier, this study does not attempt to refine the mechanics of GPL accounting. Nonetheless, it is worth mentioning that the issue of the monetary adjustment and its meaning has been raised as an area of concern in Zimbabwe. In this regard, the thinking on this matter, headed by Les Anderson, the Zimbabwean supervisor to this study, has been towards disclosing separately a breakdown of the monetary adjustment. This has been illustrated, for completeness purposes, in the example of IAS 29 in Zimbabwe included in Appendix B. This breakdown of the monetary adjustment has not been implemented in any companies in Zimbabwe, although at least one is seriously considering such a disclosure.

The third refinement referred to by Doupnik et al. (1995) relates to the discounting of receivable / payables. This is probably not so much a refinement as an acknowledgement of its necessity. Doupnik et al (1995) do give an example that illustrates the interest component that would be

factored into a credit sale. Ordinarily, the discounting of such a sale would not be done for materiality reasons. However, with inflation and interest rates increasing, this adjustment becomes somewhat more significant. It is submitted that this is not a situation peculiar to GPL accounting, but is also present in the historic accounts. One point that is interesting to note is that in their example, the purchasing power loss that arises from restatement of sales (and delayed receipt of the cash), is not included in the monetary adjustment line item, but rather written back against the interest income from unwinding of the receivable. This effectively leaves only the real interest expense in the accounts, which is probably more useful to users of accounts. This point is particularly relevant to Zimbabwe, whereby interest rates range between 20% and 40%, against inflation of over 120%. This is similar to the second refinement mentioned above, whereby there is the argument that the monetary gains, for example, on a financing loan, should be included directly with the interest expense, to give a real interest expense / income. In Zimbabwe, this would result in the bizarre case of an interest expense of 40% converting into an interest income of 80% (120% inflation less 40% interest expense.) However, from a real point of view, this is correct, in that the cost of borrowing has been significantly below inflation and accordingly there is a gain on borrowing inherent in GPL accounting.

To summarise, the Brazilian system is very progressive as to the manner in which it applies a system of GPL accounting. These innovations should be considered in Zimbabwe and may go some way to resolving some of the contentious issues, such as that of interest. The next section looks at the requirements of IAS 29, the standard that outlines the system of GPL accounting to be used in Zimbabwe.

3.8 'IAS 29: Financial Reporting in Hyperinflationary Economies'

IAS 29 starts off by stating that its objective is to establish specific standards for enterprises reporting in the currency of a hyperinflationary economy, so that the financial information provided is meaningful. The basic principle in the standard is that the financial statements should be stated in terms of the measuring unit current at balance sheet date, irrespective of whether the underlying valuation basis is historic cost or current cost. Comparative figures should also be restated to the same measuring unit.

Restatement is done by applying a general price index, such as the Consumer Price Index (CPI). Monetary items, defined as money held and items to be received or paid in money, are not restated as they are already stated in a monetary unit current at balance sheet date. Other items are restated based on the change in the general price index between the date those items were

acquired, revalued or otherwise incurred and the balance sheet date. A gain or loss on net monetary position is included in net income and should be disclosed separately. Various income statement figures, such as depreciation and profit on sale of assets, will need to be recalculated and are not simply restated, for obvious reasons.

The standard does not establish an absolute rate at which hyperinflation is deemed to arise but allows judgement as to when restatement becomes necessary. Characteristics of the economic environment of a country which indicate the existence of hyperinflation include:

- The general population prefers to keep its wealth in non-monetary assets or in a relatively stable foreign currency.
- The general population regards monetary amounts not in terms of local currency but in terms of a relatively stable foreign currency. Prices may be quoted in that currency.
- Sales and purchases on credit take place at prices that compensate for the expected loss of purchasing power during the credit period, even if the period is short. (Refer IAS 29, para. 3.)
- The cumulative rate of inflation over three years approaches, or exceeds, 100%.

When an economy ceases to be hyperinflationary and an enterprise discontinues the preparation and presentation of financial statements in accordance with IAS 29, it should treat the amounts expressed in the measuring unit current at the end of the previous reporting period as the basis for the carrying amounts in its subsequent financial statements.

A detailed example of the application of IAS 29 in Zimbabwe is included in Appendix B. This also points out some of the technical difficulties encountered in Zimbabwe and the consensus in overcoming these issues.

3.9 Conclusion

As is evident from the above discussion, there remains no fully accepted system of accounting for inflation. At the milder rates of inflation experienced in the developed world, no consensus has been reached as to a more favourable approach. However, the IASC is clear in indicating that at higher rates of inflation, general price level adjustments are required, and sanctions these in IAS 29. As is evident in the literature review in the following chapter, two particular issues have been identified as hindering the resolution of the inflation accounting debate:

- The low rate of inflation in the developed world.
- The language barrier with those countries that have continued to suffer rampant inflation and from which significant lessons could be learnt.

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Literature Review

This literature review examines two distinct sets of literature. First the literature on inflation accounting is examined in some detail. However, inflation accounting in Zimbabwe was not mandated by any accounting standard until hyperinflation was identified in November 1999, as defined in terms of IAS 29: Financial Reporting in Hyperinflationary Economies. Accordingly, the literature on voluntary disclosures, and underlying theories, is also relevant to inflation accounting in the period prior to this date.

4.1 Research into the Relevance of Inflation Adjustments and Disclosures

Much literature has been published on inflation accounting, going back as far as Sweeney (1936). However, the impact of changing prices only became of widespread interest in the 1970's when prices in most parts of the world soared due to the energy crisis, with many developed countries experiencing double-digit inflation. During this time, and into the early 1980's, there followed a natural abundance of literature on accounting for inflation. But as inflation slowed in much of the developed world in the early to mid-1980's, the focus of researchers shifted elsewhere, leaving the inflation accounting debate unanswered. The issue was then no longer about the type of inflationary adjustments to make, but also whether there was still a real need for such a system. Accordingly, the number of articles appearing in published journals reduced, with limited research in this field in recent times. The more recent studies have also tended to be market-based. Review of other methods of research has thus tended to relate to studies which are now fairly dated. Further, it should be noted that substantially most of this research has been conducted in first-world English speaking countries. Little research has come from third-world countries, which also happen to be the ones to suffer rampant inflation. This is worsened by the language barrier, which is alluded to by Frishkoff (1982). This is limiting in that there are non-English speaking countries that are in a position similar to that in which Zimbabwe now finds itself. Turkey is such an example. The previous chapter contains a discussion on the accounting system in Brazil. However, the literature on studies aimed at determining use and usefulness of inflation adjusted information is relatively scant. The reason presented for this relates to the bulk of research into usefulness, utility, value relevance and information content generally tending to be statistical market based studies. Third world countries, that are the ones to suffer rampant inflation, generally do not have financial markets that would support such studies. This combined with the language barrier makes such research difficult.

The relatively low rates of inflation experienced in the developed world must also be considered a limiting factor on the results found in this literature review. At rates barely ever reaching 20%, the literature is continually pointing out the limiting factor that users' own adjustments may be adequate at these mild rates.

This literature review does not focus on empirical studies that attempt to refine the mechanics of accounting for changing prices, but rather on the use and usefulness of inflationary disclosures and whether these disclosures are meeting the information needs of users. This review draws heavily on the work of Paul Frishkoff (Financial Reporting and Changing Prices: A Review of Empirical Research, 1982). In this regard, Frishkoff reviews 56 major empirical studies that have examined the usefulness and perceived usefulness of inflationary disclosures. However, being commissioned by the FASB, his focus is American. Other relevant research is added to supplement this, primarily from the United Kingdom, together with limited findings from third world countries. Frishkoff breaks the studies he reviews into two main sections;

- Studies of the behaviour of individuals
- Capital Market Studies

This review follows a similar categorisation, but also focuses on the aims of the various methodologies employed. The categorisations are as follows:

4.1.1 Studies of the Behaviour of Individuals

Category M1: Comparing the usefulness of Price-Level information to other voluntary disclosures

Category M2: Investigating the usefulness of Current Value information

Category M3: Investigating the usefulness of General Price-Level financial information

Category M4: Comparing the usefulness of Current Value and General Price-Level information

Category M5: Management use of changing price information

4.1.2 Capital Market Studies

Category C1: Usefulness of General Price-Level information

Category C2: Usefulness of Current Value information - Cross-sectional studies

Category C3: Usefulness of Current Value information - Time Series Analysis

Of the 56 major empirical studies examined by Frishkoff, usefulness was indicated in only 12, compared to 28 that indicated no usefulness. The remainder indicated either mixed usefulness, or that such a classification was not appropriate based on the nature of the study.

4.1.1 Studies of the behaviour of individuals

These studies have generally adopted a questionnaire or interview approach, although a few laboratory and field experiments have been conducted.

Category M1: Comparing the usefulness of Price-Level information to other voluntary disclosures

Chandra (1974) conducted a comprehensive questionnaire study that involved the ranking of numerous items of information from most to least useful in making the investment decision (Frishkoff, 1982). His audience was 1000 CFA's and CPA's, in America, of whom 500 responded. The relevant piece of information was 'price level adjusted annual corporate reports as supplementary statements'. This ranked last, or almost last, of the 58 items presented. Thus it would appear that other voluntary disclosures were considered far more useful than information on the impact of inflation. However, it must be borne in mind that inflation at the time was only approaching ten percent. Price-level adjustments were thus not a primary concern. As alluded to above, it would be interesting to repeat the study in an economy with more rampant inflation.

Category M2: Investigating the usefulness of Current Value information

Studies on the usefulness of current value information have proved inconclusive. Brenner (1970) sent questionnaires to 4 000 shareholders, bankers and financial analysts, receiving a 31% response rate (Frishkoff, 1982). His focus related to the inclusion of current values in earnings per share figures. His findings are consistent with other studies at the time that showed users desiring current value information in only supplementary form and not being willing to forego historic cost information. Adkerson (1978) points out that users will obviously cling to familiar techniques and that such a drastic move from historic cost would be disconcerting. Further, not all users have the sophistication to interpret GPL accounts. This is backed up by the findings of Stanga (1979) who demonstrates in his study that the chief lending officers of some of the largest banks perceived the historical cost measure as 'considerably more reliable' than current cost disclosures (Stanga in Frishkoff, 1982: 13).

One of the most comprehensive and authoritative interviews ever conducted in this context relates to that by Louis Harris and Associates (1980) for the Accounting Foundation. "Sixty-one percent of the respondents felt that current cost would slowly become more important than historical cost should inflation continue and more than three-quarters felt this to be a positive trend" (Frishkoff, 1982: 15). However, the results are not as convincing as one might have expected. 25% of the respondents still felt that this increase in significance of current cost information was not a positive trend, implying a preference for historic cost information.

Another significant study into the area of Current Cost Accounting was commissioned by the ICAEW and is frequently referred to as the Carsberg report. This work was published in 1985 in three volumes entitled "Current Cost Accounting: the benefits and the costs." Much of the work discusses the practical technicalities of CCA. However, the authors found difficulties with the concept of physical capital maintenance in particular industries, particularly the extractive industries, and that CCA has little relevance for companies in which physical capital maintenance is not relevant, for example, mining companies. For these industries the authors discuss GPP accounting as a possible means of overcoming the problems in these industries, but conclude that for most industries CCA would be of some value to the users of accounts.

Accordingly, studies have shown limited usefulness of current value disclosures, but usefulness has nonetheless been indicated.

Category M3: Investigating the usefulness of General Price-Level financial information

With regard to GPL information, a study by Buzby is frequently cited (Frishkoff, 1982: 7). 144 out of 500 analysts responded to his questionnaire, which required the determination of usefulness of 38 items of financial information on a scale of 0-4, the pertinent item of information being the usefulness of price indices and GPL information. This information rated 28th out of the list of 38, but again the rate of inflation must be considered to be a limiting factor in the determination of conclusions.

A survey by Arthur Young and Company (Berliner, 1983) to determine the use by analysts of Statement No. 33 information (requiring disclosure of both current value and GPL accounting) indicated no great enthusiasm for the information. However, there was also no demand for a removal of the requirements of Statement No. 33, or "clear disavowal of the information's usefulness" (Berliner, 1983: 65). This study, entitled "Do Analysts Use Inflation-Adjusted

Information? Results of a Survey”, forms the basis of the second set of questionnaires in this study, namely to analysts on the Zimbabwe Stock Exchange.

Category M4: Comparing the usefulness of Current Value and General Price-Level information

Estes (1968) examined both current cost and GPL information and is one of very few behavioural studies to compare their usefulness. The study involved 300 subjects from each of the following groups; CFA's, loan officers and financial executives. The subjects were to assume that this current cost and price level information would be supplementary only, historical cost still being the primary form of measurement. Estes shows that the differences in responses are statistically significant, with the current cost disclosures being favoured as more useful. It is interesting that this is the method favoured by the Sandilands committee some seven years later in the United Kingdom.

From the above studies it can be seen that there has been significantly more research into the usefulness of current value information than GPL information, with current value information tending to be somewhat favoured. However, studies on both sets of information have shown limited usefulness and a strong preference to retaining historic cost as the primary basis of reporting.

Category M5: Management use of changing price information

Two other research studies into the use by management of GPL information are also relevant. Schwarzbach and Swanson (1978) received responses from 280 out of 450 randomly selected financial controllers of public corporations. “Responses indicated that CC (current cost) information was provided to managers about half the time both to determine selling prices and for use in internal allocation of funds, and about one-third of the time for cost-volume-profit analysis and for evaluating the results of holding inventory” (Frishkoff, 1982: 14). Casey and Sandretto (1981) had similar findings. However, they also indicate that about half of those companies that did provide inflation adjusted data routed it only to top management and not operating management. Frishkoff makes reference to the theme that appears frequently in these reports, that management education is required on how to use changing prices data, alluding to the problem of the lack of user understanding.

In conclusion to the study of the behaviour of individuals, it can be seen that the usefulness of inflationary information is not definitive. Again, emphasis is placed on the moderately low

inflationary climate in which these studies were conducted, in comparison to that in which Zimbabwe now finds itself.

4.1.2 Capital Market Studies

In the late 1970's and early 1980's, researchers began to find themselves with the ability to use personal computers as a research tool. Accordingly this allowed large volumes of security price information to be examined and studied in considerably less time. This led to an abundance of market-based research and somewhat of a shift away from behavioural research into inflation accounting.

This section reviews these studies of capital markets, but focuses more on the indication of usefulness than on an in depth analysis of the methodologies involved. This is due to the fact that any sort of market based accounting research on the Zimbabwe Stock Exchange is impracticable given its lack of liquidity, particularly at the present time, and would be inconclusive at best. However, the findings of these studies elsewhere are nonetheless relevant and helpful in determining the value content of inflationary information.

Numerous studies have examined the value-relevance of inflationary disclosures by looking for an impact on securities prices. The issue that presents itself in capital market studies relates to the efficiency of the market and the question of whether the impact of inflation is impounded quickly and efficiently into the share price, long before the accounting disclosure of such information. Revsine (1978) poses the problem as follows:

'Some of the people who believe in the efficiency of the securities market are not terribly upset by the apparent divergence between inflation-adjusted and reported earnings. They would argue that the market is not unaware of these kinds of effects and is trying as best it can to make adjustments for the differential impact of inflation across firms. It turns out that I, too, believe in the efficiency of securities markets but I am nevertheless somewhat worried by these figures; while I believe in the efficiency of markets, I do not believe in the omniscience of securities markets. I do not believe that the market is able to magically infer accurate inflation accounting adjustments without some sort of disclosure on the part of companies in the economy. [p29]' (Revsine (1978: 29) in Frishkoff, 1982: 24).

In essence, this is what capital market studies have tried to determine.

Category C1: Usefulness of General Price-Level information

Market based studies of GPL disclosures have found inconclusive and frequently contradicting results. Morris (1975) studied the disclosure of GPL information on companies in the United

Kingdom and found no reaction to these data. However, broader studies by Noreen and Sepe (1981) and Basu (1981) have found the market reaction to be far less clear-cut (Frishkoff, 1982.)

Beaver and Ryan (1985) conducted cross-sectional correlations between stock returns and each of six income measures required by Statement No. 33. Historic cost had significantly higher correlation over the four-year period examined than any of the other six income variables. "These simple correlations suggest that historical cost income has greater explanatory power with respect to stock returns than any of its rivals. However, this perspective treats the other earnings variables as competitors and does not address the question of gains from using more than one earnings measure" (Beaver and Ryan, 1985: 68). Beaver and Ryan (1985). then test for this by comparing the proportions of variance explained under two regressions, historic cost earnings alone, and, both historic cost earnings and one additional Statement No. 33 variable. They conclude from their findings that "Statement No. 33 variables provide no incremental information beyond that already provided by historical cost earnings, when explanatory power is defined in terms of the ability to explain cross-sectional stock returns" (Beaver and Ryan, 1985: 69). However, as is common in inflation accounting research, these findings contradict the findings of Baran, Lakonishok and Ofer (1980) in an earlier study. Baran et al. conclude that price-level restated data contains incremental information content over and above historic cost earnings.

"In the South African context Du Plessis, Archer and Affleck-Graves (1986) and Gevers (1991) used the informational content approach as used by Beaver et al (1982) and found very little information content in the estimated inflation adjustments. Gevers (1992) also found that estimated AC201 inflation adjustments did not contain income measurement properties" (Gevers, 1994: 31.)

The most recent research found on inflation accounting is that by Gordon (2001). Her paper "investigates the value relevance of historical cost, price level and replacement cost accounting using a sample of Mexican firms from 1989 to 1995. It contributes to prior research by distinguishing between two distinct aspects of changing prices: (1) the change in the general price level, and (2) the change in the value of specific non-monetary assets" (Gordon, 2001: 177). Mexico is unique in requiring separate disclosure of price level and replacement cost disclosures. "A sample of Mexican firms also addresses a key reason cited for mixed results in previous assessments of the usefulness of price level and replacement cost accounting: the effects of inflation are too weak to detect" (Gordon, 2001: 177). Inflation reached up to 52% in her study, still mild by Zimbabwe's terms. Value relevance is determined by testing for statistical association between the level and changes in historic cost, price level and replacement cost

earnings and annual returns. Her findings indicate that “replacement cost adjustments are relatively and incrementally relevant beyond historical cost and price level measures while price level adjustments are incrementally relevant beyond historical measures” (Gordon, 2001:178).

As can be seen, various studies have reached different conclusions with respect to the information content of price level financial information. These results indicate that usefulness may be circumstance specific and cannot be concluded on across the board.

Category C2: Usefulness of Current Value information - Cross-sectional studies

A much-cited study in the literature is that of Beaver, Christie and Griffin (1980). Their “study examines the security price behaviour of firms at the time of three events: the proposal of the SEC’s accounting series release (ASR 190) to require replacement cost disclosures, the adoption of ASR 190, and the initial filing of the data with the SEC. The primary analysis focuses upon differential security return behaviour among reporting firms. Several extensions, including a comparison with non-reporting firms, are also conducted” (Beaver, Christie and Griffin, 1980: 127). The findings of the study indicated that there was no security price impact during the three time intervals studied. In other words, the security prices had already impounded the impact of inflation and the information contained in the disclosures, disproving somewhat the comments of Revsine mentioned earlier. Studies by Gheyara, Kelly and Boatsman (1980), as well as Ro (1981), also found no proof of information content in the ASR190 disclosures. Watts and Zimmerman (1980) point out that three different methodologies all reached the same conclusion and that it was therefore unlikely that future research would find statistically significant stock price reactions. They conclude that even if the information is relevant, other sources already supply it and therefore ASR 190 disclosures are redundant. Ball and Brown (1977) also reach the same conclusion concerning the reaction of the market to current cost disclosures in Australia. Matolcsy (1984: 567) finds consistent results with Beaver, Christie and Griffin (1980) and “could not find significant marginal information content of specific price-level adjusted accounting income numbers”.

Callard and Kleinman (1985), however, investigated which return on investment (ROI) measure correlated better with market prices, historic or inflation-adjusted. This was done by comparing regressions of historic risk adjusted ROI and (Market Value of Equity and Debt / Historic Net Assets), against regressions of inflation-adjusted ROI and (Market Value of Equity and Debt / Replacement Cost of Net Assets). Their findings, in contrast to those discussed above, indicated that inflation-adjusted ROI consistently accounted for a significantly greater portion of market

price movements than did the same information without inflation adjustments. However, this did not hold in the short-term and was only consistently significant when examined in blocks of at least three-year periods from 1964 to 1981.

A more recent study by Peasnell, Skerrat and Ward (1987) investigated the share price impact of UK current cost disclosures. They investigated the impact of the experimental standard, SSAP16 (current cost accounting), on share returns on the London Stock Exchange. "The results suggest that (current cost accounting) information has a small but significant impact on stock returns in the days leading up to the announcement. However, (current cost accounting) does not seem to be the main driving force behind long period returns. These findings correspond to those of Lustgarten (1982) whose study found replacement cost data to also have an impact on stock prices in the period leading up to the official announcement date of such figures. These findings are in stark contrast to the Callard and Kleinman (1985) study mentioned above with respect to the current value information driving long-term returns. Peasnell et al (1987) find "returns in the long run to be associated more closely with historic information than with that generated by SSAP16" (Peasnell et al, 1987: 3).

Nonetheless, the more recent studies tend to contradict the earlier studies in that there appears to be small but significant information content in current value disclosures. This may be due, particularly in the Peasnell et al (1987) study, to the learning effect mentioned in the literature, users having learnt to interpret the information.

Category C3: Usefulness of Current Value information - Time Series Analysis

Bernard and Ruland (1987) adopted a time series analysis rather than the cross-sectional analysis adopted by Beaver et al. They state that some "evidence of incremental information content in current cost income is found in the time-series analysis, even though none is evident in a cross-sectional analysis. However, incremental information content is (at best) evident only for a small subset of industries where the correlation between historical cost income and current cost income is low; for the majority of industries, the two income measures convey essentially the same information" (Bernard and Ruland, 1987: 707). A degree of usefulness is nonetheless indicated.

4.1.3 Conclusion

The findings of research into inflation accounting have been far from conclusive, with usefulness and information content being demonstrated in some studies, but not in others. Behavioural

studies have tended to be relatively dated, but have found inflation adjusted information to not be of primary concern. Further, users have indicated that inflation adjusted information should be merely provided as supplementary information and not form any part of the primary historic cost accounts. Behavioural studies that have compared the usefulness of GPL and current value information have shown a preference for the current value information, usually in the form of replacement costing. The more recent studies, which have tended to be market-based, have also shown very inconclusive results. With respect to GPL accounts, incremental information content has been demonstrated only occasionally. This has indicated that usefulness may be circumstance specific. Market studies on the usefulness of current value information have been just as inconclusive. The earlier research, focussed on the ASR 190 disclosures, found no usefulness. However, later studies have indicated marginal incremental information content. This has been explained as possibly relating to the learning curve effect, users having learnt to use the information.

In all, the results of research have been inconclusive at best. Most studies have been hampered by only mild rates of inflation, distorting the usefulness of inflation adjusted financial information. The abundance of research up to the mid-1980's came to an abrupt halt with the decline in the rate of inflation, leaving the inflation accounting debate unanswered.

4.2 Research into theories underlying voluntary disclosures

As mentioned earlier, this section aims to provide a very brief overview and introduction to three of the theories underlying voluntary disclosures that have been proposed in the literature. These are relevant to the period prior to the identification of hyperinflation in Zimbabwe in November 1999, in terms of the indications contained in 'IAS 29: Financial Reporting in Hyperinflationary Economies.'

Various theoretical perspectives have been established in an attempt to understand the factors influencing voluntary disclosures. These differ from the more frequently cited theories underlying voluntary social disclosures, such as legitimacy and social contract, which are not appropriate when considering voluntary inflationary disclosures. The most prominent of the theories proposed to underlie voluntary disclosures are:

4.2.1 Proprietary Cost Theory

Verrecchia's (1983) proprietary cost theory states that the incentive to disclose information is a decreasing function of the potential proprietary costs attached to a disclosure and an increasing

function of the favourableness of the news in a disclosure” (Scott, 1994: 26). Thus a firm will disclose information to the extent that the benefit to be gained exceeds both the direct and indirect costs of providing that information. This would thus indicate a preference to disclosing favourable information. However, unfavourable information would only be disclosed if the cost of non-disclosure, such as litigation costs, exceeds the negative impact of the information.

4.2.2 Estimation Risk

Seminal work by Grossman (1981) and Milgrom (1981) forms the basis of an adverse selection argument for complete disclosure of relevant information. Maguire (1997) builds on this in stating that risk averse investors will invest relatively more in those securities about which they have the most information. Thus this argument proposes that investors assume, in the lack of other contrary information, a worst case scenario. It is therefore beneficial for firms to disclose information as this reduces uncertainty.

4.2.3 Information Cost Savings

Diamond (1985) explains the reason for voluntary disclosures as being related to information cost savings (Scott: 1994). This theory proposes that managers will disclose information in an attempt to reduce overall societal costs. It follows from this that investors will accordingly reduce the premium they impose on particular securities due to reduced information gathering costs and accordingly reduced cost of capital.

4.2.4 Conclusion

This section of the literature review has examined three frequently cited theories underlying voluntary disclosures. The study attempts to determine which of these dominated in the period prior to November 1999. However, this study focuses on the period after the implementation of ‘IAS 29: Financial Reporting in Hyperinflationary Economies’. Accordingly, a more detailed literature review on voluntary disclosures is not warranted.

The Research Problem and Research Methodology

5.1 The Research Problem

P1: What is the use and perceived usefulness of IAS 29 General Price Level Accounting in Zimbabwe?

The research problem stems from the comments received in the Zimbabwean market place with respect to IAS 29 and its usefulness and relevance in that context. Appendix A contains the quotes of spokespersons of several companies airing their views with respect to IAS 29. This research aims to investigate whether IAS 29 restated figures, and the resultant GPL accounts, are being used in practice and whether this information is considered useful. Further, it aims to identify where problems have been encountered and to determine the reasons for these problems, with a view to answering why the standard has not been well received in some circles. This information should be useful to those tasked with determining the way forward with respect to the contentious adoption of this standard in Zimbabwe.

5.2 Reasons why the Specified Problem is Worth Researching

The current economic climate in Zimbabwe provides the ideal opportunity for research on inflation accounting and, more specifically, into GPL accounting. Although inflation accounting has not been a primary focus in research journals since the 1980's, when inflation in the first world reduced to single figures, the debate nonetheless continues. IAS 29 is seldom encountered in Anglo-Saxon countries. The adoption of this standard in Zimbabwe requires research into the success of its implementation and use. A comprehensive collection of the views and opinions of those involved in the entire process, from preparation to use, is required. This will facilitate the relevant accounting regulatory bodies in moving forward appropriately. Accordingly, much input has been received from the ICAZ appointed supervisor to this study, Les Anderson, together with various other sources, in order to ensure the practical relevance of the findings. It is hoped that the findings of this study will, in particular, be useful to the 'IAS 29 Task Force' of the Institute of Chartered Accountants of Zimbabwe.

5.3 Research Methodology

This study follows a questionnaire approach. Other approaches were considered but deemed to be inappropriate. In particular, the idea of a market-based study was contemplated for some time, in addition to the questionnaires. However, after the data collection process had begun, this was abandoned for the reason of significant inefficiencies on the Zimbabwean Exchange. At best, the results would have been inconclusive. Despite investigation, no market efficiency studies were evident in the research journals, and this has been raised as an area for future research in the last Chapter to this study. Further, given the current political influence on the economy as whole, price adjustments due solely to the disclosure of inflation adjusted information would be near impossible to determine.

5.3.1 Sample selection and research limitations

The questionnaire specifically addresses two audiences, the preparers and the external users of financial information. Technically, the preparers are also users of financial information from a management and operational control perspective, and accordingly a third user group could be identified as 'managerial users' of financial information. However, for the purposes of distinction in this study, which does not focus on investigating the use of IAS 29 GPL information by management, directors and managers shall be referred to as 'preparers'. The remainder of the user group - external users - is referred to as 'users'. The focus of this study is on these two groups – the preparers of financial information, and the external users of this information. However, the use of this information by management is also investigated, but not within the realms of a separate user group. Per the 2000 / 2001 Zimbabwe Stock Exchange Handbook, there were 68 listed companies in Zimbabwe. These form the population for the first set of questionnaires, which were sent to the Financial Directors of 60 of those companies. These were sent in March 2002, with almost all responses received in the following 6 weeks. The timing of the questionnaire means that companies would have had two full years for the production of IAS 29 adjusted annual reports given the effective date of implementation of the standard. 8 companies from the initial sample were deemed inappropriate for various reasons as discussed in Appendix Civ. Of the 60 remaining companies, 35 responses were received, giving a 58.3% response rate.

The second questionnaire was aimed to obtain the views of external users of financial information. As a surrogate for external users, financial analysts were considered appropriate. The justification for using analysts as a surrogate for the entire user group comes in fact from the Conceptual Framework itself. Paragraph 10 of the Conceptual Framework (AC000) states that

“While all of the information needs of ... users cannot be met by financial statements, there are needs which are common to all users. As investors are providers of risk capital to the enterprise, the provision of financial statements that meet their needs will also meet most of the needs of other users that financial statements can satisfy.” This statement in the Framework is contentious (Everingham and Watson, 2000), but nonetheless justifies the selection of financial analysts as a reasonable surrogate of all users of financial information. In the study, the sample was defined as obtaining at least one response from every Stockbroking and Asset Management firm listed in the 2000 / 2001 Zimbabwe Stock Exchange Handbook. After adjusting the sample for various reconstructions and mergers in the industry, questionnaires were sent to the research departments of 6 Asset Management firms, 5 Asset Management / Stockbroking firms and 9 Stockbroking firms. These were sent in June 2002, and all responses were received before the end of July the same year. From the population of 20 firms, 34 responses were received. This indicates a 100% response rate, in that at least one response was received from every company in the sample, which was the defined objective of the sample. The respondents were all identified as ‘market analysts’, and their functions involved the preparation and use of market research reports. The issue of bias resulting from the fact that more than one response was received from several firms is not considered to impact the results of this study, as the analysts were given and answered questionnaires independently of one another and their firms. The responses in the questionnaires are those of the responding individual, and not the firm that they represent. In order to improve the response rates, a top-down approach was used, whereby permission for the completion of the questionnaires was initially gained from the respective direct senior of the analysts in the firms. These seniors then indicated who in their firm would complete these questionnaires. This explains the very high response rate. Response details are included in Appendix G.

The questionnaires have been put together in such a way as to answer the research problem presented earlier. However, in an attempt to answer the problem, various sub-problems have to be considered that, in their entirety, will give indications towards the overall problem. The sub-problems mentioned below, under each relevant questionnaire, result from consultation with the following:

- Prior research, as discussed in Chapter 4;
- Discussion with the Research Supervisor for this project from the University of Cape Town, Professor Geoff Everingham, as well as the Institute of Zimbabwe appointed supervisor, Les Anderson, Senior Partner, Deloitte & Touche, Harare;
- Review of the minutes of the ‘IAS 29 Task force’ meetings;

- Review of published comments from various sources, including annual reports, industry publications and the press. As mentioned, a selection of these comments is included in Appendix A, and
- Discussion with colleagues and members of ICAZ in the profession.

The first questionnaire had a 58.3% response rate. Tests, including the comparison of early respondents to late respondents, indicated that any response bias in the results was negligible, and accordingly such a bias in no way impacts the results of the questionnaire. The fact that the study was conducted in the third year of publishing inflation-adjusted information is also another limitation in that users may not have had adequate time to understand the new set of accounts. Other limitations relate to the fact that the study covered only one external user group, namely financial analysts, as is the fact that 5-year trend analysis would have been difficult, although not impossible, to produce.

5.3.2 Questionnaire 1 – Preparers of Financial Information

The questionnaire (Appendix C) is broken into seven sections, which attempt to answer the following sub-problems relating to the preparers of financial information:

Pre – IAS 29

Sub Problem 1: Prior to the identification of hyperinflation in Zimbabwe, did preparers consider whether it would be necessary to attempt to disclose the impact of inflation on published accounts, and were such disclosures being made?

(Questions 1a., 3a. & 3b.)

This sub-problem focuses on the period prior to the identification of hyperinflation in Zimbabwe and the adoption of IAS 29. As mentioned earlier, inflation was approaching 60% at the end of 1999, and had been steadily rising for several years. These responses to this sub-problem should give insights into the perceived usefulness and necessity of inflationary adjustments and disclosures at increasing rates of inflation.

Impact of Inflation

Sub-Problem 2: Do preparers perceive there to be a differential impact of inflation and disclosure practices between organisations and industries?

(Questions 2a., 2b. & 2c.)

This sub-problem is specifically aimed at determining whether preparers perceive certain industries and organisations to be differentially impacted by inflation, and accordingly whether there exists an industry relationship with respect to the usefulness of inflationary disclosures.

Management Use

Sub-Problem 3: Do management use IAS 29 information in their management and operational decision-making process?

(Question 4a.)

In the Zimbabwe Sun 2002 annual report, the Chairman indicates that the “Company does not use hyperinflation accounts as a business management tool” (see appendix A). Management is a significant user group and this sub-problem aims to identify whether the lack of use of IAS 29 information is widespread. From a management perspective, it can be argued that information that is produced only once or twice a year, some time after the balance sheet reporting date, can only be of limited use.

Sub-Problem 4: Do IAS 29 results have any impact on dividends and the dividend policy?

(Question 4b.)

This sub-problem relates to the issue of the payment of dividends out of capital on a real basis, and flows from the concept of capital maintenance identified by the entity. If management were aware of inflation and its impact on the equity of the firm, dividend policy would be based on some form of real profit. The responses to this question will give insight into the acceptance by management of the concepts of inflation adjustments and real income.

Usefulness of IAS 29 in Zimbabwe

Sub-Problem 5: What is the cost / benefit relationship of IAS 29 in Zimbabwe?

(Question 5a. & 5b.)

The Haddon and Sly Ltd 2001 annual report included a comment that the company had complied with IAS 29, from which they found “the cost incurred and effort were out of all proportion to the deemed benefits” (see appendix A). Numerous other companies have had similar complaints, particularly with respect to the cost involved at the initial adoption of IAS 29. In certain cases, where systems have not maintained the necessary information for restatement, set-up costs have been considerable. This sub-problem aims to identify the significance of these costs and their impact on the perceived usefulness of IAS 29 results.

Sub-Problem 6: What do the preparers feel are the reasons for the level of use of IAS 29 restated results in practice?

(Question 5c., 5d., 6a. & 6b.)

This sub-problem attempts to identify the reasons for the level of acceptance and perception of usefulness of the inflation adjusted information. In particular, this sub-problem allows the preparers to indicate their perceived areas of concern, which shall then be compared to the concerns raised in other studies, as well as to those raised in the second questionnaire to the financial analysts.

Sub-Problem 7: Do preparers perceive users as able to understand the information presented to them?

(Questions 5e., 5f. & 5g.)

This sub-problem focuses on the issue of user understanding. Numerous studies have found user understanding to be a significant problem, even in sophisticated markets (Adkerson (1970); Stanga (1979)). Prior to the fieldwork for this study, lack of understanding of the IAS 29 information was widely felt to be one of the most critical areas impacting on the relevance of IAS 29 in Zimbabwe. This sub-problem addresses this issue directly.

The Way Forward

Sub-Problem 8: How should the regulatory accounting bodies in Zimbabwe proceed?

(Questions 7a.)

Chapter 2 discussed the regulation of accounting in Zimbabwe. In this regard, the Institute of Chartered Accountants of Zimbabwe has appointed an 'IAS 29 Task Force' to address the concerns raised with respect to the standard and to propose a way forward. However, there is much disagreement in this regard, with numerous proponents and antagonists. This sub-problem attempts to obtain the suggestions of the preparers of financial information as to the way forward. The results to this sub-problem should also indicate the balance between these proponents and antagonists amongst the preparers.

The questionnaire follows a very similar layout and order to the above, with only a few exceptions to allow for a seemingly more logical flow for respondents. The results to each of these problems are discussed in Chapter 6, with the detailed responses and quotable comments received being included in Appendices C and F.

5.3.3 Questionnaire 2 – Analysts of Financial Information

As discussed earlier, financial analysts are being used as a surrogate for all external users of financial information. This questionnaire (Appendix D) follows a very similar format and structure to that of Berliner (1983), being adjusted where necessary to be applicable to the Zimbabwean context. The following sub-problems were identified relating to the users of financial information:

Sub-Problem 1: To what extent do analysts use IAS 29 financial information in their technical analyses of company performance, and what are the reasons for this?
(Questions 1,2 & 3)

Prior to the fieldwork for this study, it was widely considered that no user group was using IAS 29 GPL information. Zimbabwe Sun Limited, in their 2002 annual report, clearly state that analysts have made it clear to them that they take very little inflation adjusted information into account (see appendix A for quote). This sub-problem aims to identify on a systematic and comprehensive basis the use of IAS 29 GPL information by market analysts.

Sub-Problem 2: Have analysts been formally trained to assist them in the understanding and interpreting of General Price Level adjusted information?
(Question 4 & 5)

As mentioned above, numerous studies have identified user understanding as a significant problem in the use of GPL information, even in sophisticated markets. This sub-problem addresses directly this issue of user understanding. Further, the issue of the availability of the resources needed by users to be able to learn about and understand IAS 29 and GPL accounting is also examined, and will be of particular relevance to those tasked with addressing the problems encountered in the implementation of the standard.

Sub-Problem 3: What are the major reasons for the lack of use of inflation-adjusted information by analysts?
(Question 6)

This sub-problem attempts to identify the perceived factors that have detracted from the usefulness of IAS 29. Prior studies, in particular the Berliner (1983) study, have identified several 'hindrances' to use. This sub-problem will be addressed in such a manner as to address any

further 'hindrances' that may be indicated, and to give weighting to the relative importance of these factors in detracting from use.

Sub-Problem 4: Do analysts perceive inflation-adjusted accounts to be more useful for some industries than others?

(Question 9)

This sub-problem follows from that identified with respect to the preparer user group and is simply aimed at identifying an industry relationship with respect to GPL information.

Sub-Problem 5: Would analysts be satisfied if only the primary IAS 29 accounts were disclosed, and not the historic accounts, as is recommended by IAS 29?

(Question 10)

IAS 29 recommends that only the restated accounts be disclosed, despite the prior research that has never shown an overwhelming preference for GPL information. On the contrary, prior studies (Brenner (1970); Adkerson (1978); Stanga (1979); Louis Harris and Associates (1980); Berliner (1983); amongst others) have always indicated a strong preference for the retention of historic cost as the primary basis of accounting, GPL or any other inflationary information being purely supplementary in nature. This sub-problem is aimed at determining whether this is also the case in a much higher inflationary environment.

Sub-Problem 6: How should the regulatory accounting bodies in Zimbabwe proceed?

(Question 11)

As with the preparer user group, this sub-problem is aimed at determining the views of the analyst user group as to their suggested way forward. This information is critical in that this user group represents the ultimate users of financial information, particularly from an investment point of view. A clear disavowal of the IAS 29 information by this user group would be useful information to those tasked with determining the way forward with respect to inflation accounting in Zimbabwe.

The results to each of these problems are discussed in Chapter 7, with the detailed results and quotable comments received from respondents being included in Appendices D and G.

5.3.4 Conclusion

The above two sections have identified several sub-problems that should provide an answer as to the use and perceived usefulness of GPL accounting in Zimbabwe. The methodology involves a questionnaire based approach that is aimed at two specific audiences, the Financial Directors of the companies listed on the Zimbabwe Stock Exchange, and the research analysts that necessarily have to use financial information in their technical reviews of companies. Results to the questionnaires are discussed in the following two chapters, and detailed in Appendices C and D, and F and G respectively. The results will be analysed by calculating the percentage of respondents and the determination of rankings where appropriate. Where rankings are considered necessary, such as in the computation of the significance of certain factors to the usefulness of inflation adjusted information, the Friedman non-parametric test will be used

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Results and Conclusions – Questionnaire 1

6.1 Introduction

This chapter reviews the results of the first set of questionnaires, which were sent to the Financial Directors of the companies on the Zimbabwe Stock Exchange and is referred to as the questionnaire to the 'preparers' of financial information (Appendix C). The results are presented in a format similar to the questionnaire itself and shall be discussed in the context of the sub-problems that they attempt to answer. Following the examination of results per sub-problem is a discussion that focuses on and summarises the more significant of those findings.

6.2 Discussion of Results

Pre – IAS 29:

Sub Problem 1: Prior to the identification of hyperinflation in Zimbabwe, did preparers consider whether it would be necessary to attempt to disclose the impact of inflation on published accounts, and were such disclosures being made?

(Questions 1a., 3a. &3b.)

63% of respondents stated that they did not consider whether inflationary disclosures would have been useful or necessary prior to the implementation of IAS 29. This response is disappointing given that in 1999 the rate of inflation had risen to nearly 60%, yet few companies even contemplated inflationary disclosures, as encouraged in IAS 15. It is therefore perhaps not surprising given these results that many preparers have responded negatively to IAS 29 restatements being imposed upon them. 83% of respondents stated that they did not actually include any inflationary disclosures or discussions in that period, indicating that few of those that did contemplate these disclosures acted upon such consideration.

Confirming the above findings, a very significant 86% of respondents indicated that in the period prior to the implementation of IAS 29, inflationary disclosures would not have been useful and users were able to adequately make their own adjustments. Accordingly, it can be concluded that the preparers do not feel that such disclosures are of much use at milder rates of inflation of up to the region of 60%. It should be noted that this rate of inflation is nonetheless extreme when compared to the environments in which much similar research has been conducted, but

responses seem consistent – preparers have no great liking for GPL accounting (see also Gordon (2001)).

Impact of Inflation

Sub-Problem 2: Do preparers perceive there to be a differential impact of inflation and disclosure practices between organisations and industries?

(Questions 2a., 2b. & 2c.)

When presented with the first question regarding the perceived impact of inflation across industries, it is significant to note that not one of the respondents felt that the industry in which they operate was impacted less by inflation than any other. On the other hand, 54% felt that their companies were more impacted by inflation. In general, however, the companies felt that their disclosure practices did not differ much from those other firms. This indicates that management do not perceive there to be any significant industry relationship with respect to inflation and inflationary disclosures. However, section 6.3 below investigates all of the responses to this questionnaire in total in order to examine in detail whether such an industry relationship exists with respect to the responses.

Management Use

Sub-Problem 3: Do management use IAS 29 information in their management and operational decision-making processes?

(Question 4a.)

Sub-Problem 4: Do IAS 29 results have any impact on dividends and the dividend policy?

(Question 4b.)

With respect to the use of IAS 29 figures by management, an overwhelming 63% stated that they do not use inflation adjusted information at all for purposes of management decision making. Discussion with several of the directors does indicate that management is certainly aware of inflation on such activities as the pricing of their products. However, as can be seen in the responses to question 4a., none of the respondents indicated any extensive use of the GPL information required by IAS 29.

This is a significant finding. If management are not using the information themselves and showing no faith in the restated figures, then it is extremely unlikely that users would want to base investment decisions upon the same information. One of the respondents went as far as stating that “IAS 29 (is) regarded as totally useless – other means of measuring ‘real results’ are used.”

Further, 86% of companies stated that the IAS 29 inflation adjusted results have no impact on the dividend policy. On the other hand, it is perhaps more significant that 14% of companies stated that the restated results do have an impact on dividends, which would seem to go against the general sentiment regarding IAS 29, being that no-one at all places any reliance on these numbers. Interestingly, it was a financial institution that commented that their "dividend policy is a times cover the inflation adjusted profit." Nonetheless, it is clear that few companies bring into account the impact of inflation on dividends, with many companies undoubtedly repaying real capital.

Usefulness of IAS 29 in Zimbabwe

Sub-Problem 5: What is the cost / benefit relationship of IAS 29 in Zimbabwe?

(Question 5a. & 5b.)

Two questions were posed to determine whether a cost / benefit relationship exists. However, results were somewhat contradictory. When asked to ignore costs, users responded fairly evenly between no usefulness, slight usefulness and moderate usefulness of IAS 29 information. Only 3% stated that, ignoring costs, IAS 29 was 'certainly' beneficial. However, when asked to consider if this benefit outweighed the cost, 20% responded yes, with a further 26% responding possibly. This seems to indicate that even the benefit of only moderate usefulness outweighs the increase in cost, implying that the costs of producing IAS 29 information are perhaps not as significant as may have been anticipated, particularly after the first year of restatement.

Sub-Problem 6: What do the preparers feel are the reasons for the level of use of IAS 29 restated results in practice?

(Question 5c., 5d., 6a. & 6b.)

From review of the many published comments and discussion with those involved in the restatement process, three particular areas were identified as being significant contributors to the lack of use of IAS 29 in practice. These were a 'Lack of User Understanding', a 'Perceived Lack of Intrinsic Information Content' in the IAS 29 results, and a perception that 'Practical Implementation Problems', such as choice of indices and inconsistent methods and assumptions, detract significantly from usefulness.

Based on a simple weighted averaging of responses, the respondents ranked 'Lack of User Understanding' as the factor contributing most to the poor use of IAS 29 information in practice, and 'Perceived Lack of Intrinsic Information Content' as the least contributing factor.

However, these rankings relate only to the sample and need to be tested statistically in an attempt to determine that the rankings of the sample are reflective of the population at the 95% confidence level. In order to do this, the non-parametric 'Friedman Test', with pair-wise comparisons, was used. The statistical output and workings for these tests are included in Appendix Ci. The Friedman test rejected H_0 , indicating that not all of the mean ranks were the same and that some form of ranking could be determined. Pair-wise comparisons indicated that 'Lack of User Understanding' was significantly different from 'Lack of Intrinsic Information Content' at the 95% level. Further, whilst the other mean ranks were not statistically different from each other at the 95% level, the pair-wise comparisons indicated that the difference was still significant. The finding here of the 'lack of understanding' being the most significant contributing factor to lack of use of IAS 29 is investigated further in Sub-Problem 7.

The second point in question 5c, 'Perceived Lack of Intrinsic Information Content', was ranked last by the preparers. This issue was posed more directly to respondents in question 5d, enquiring whether users perceived there to be such a lack of inherent value. Interestingly, as much as 45% of preparers stated that there is a lack of intrinsic information content in the GPL IAS 29 figures, whereas 49% took the opposite view. Further, this illustrates the divide that is becoming evident in the opinions of the preparers, which seem fairly evenly split between proponents and antagonists.

Question 6a expanded the three points raised in question 5c. and asked respondents to rank six hindrances to the use and usefulness of restated information that have been cited in the published quoted comments and through discussions with both antagonists and proponents. These are really only an expansion of the three generic reasons quoted in 5c. and are an attempt to confirm, more specifically, the findings of question 5c. The six reasons are:

- i. Cost
- ii. Lack of user understanding
- iii. Lack of intrinsic information content in the restated results
- iv. Inconsistent methods and assumptions in the restatement process
- v. Indices chosen are not appropriate
- vi. The fiscus does not recognise inflation adjusted figures in the assessment of taxation

The Friedman statistical output and pair-wise comparisons are included per Appendix Cii. Reason 'ii. Lack of user understanding' is statistically different from all other reasons, except Reason 'iv. Inconsistent methods and assumptions in the restatement process', at the 95%

confidence level. Further, whilst Reason ii. is not statistically different from Reason iv. at the 95% level, the difference is still nonetheless relatively significant. The actual rankings, with weighted mean ranks, from largest impact to least impact on lack of use, were as follows:

Table 6.1
Ranking of Reasons for Non-Use of Restated Results

	Reason	Mean Rank
Largest impact 1	ii – Lack of understanding	2.03
2	iv – Inconsistent methods and assumptions	3.25
3	v – Indices chosen are not relevant	3.44
4	i – Cost	3.78
5	vi – Fiscus does not recognise restated results	4.13
Least impact 6	iii – Lack of intrinsic information content	4.38

The results of this question strongly confirm the results of question 5c. discussed above. Again, 'Lack of understanding' was significantly the largest contributing factor. Further, 'Lack of intrinsic information content' again ranked last of the reasons presented. This also confirms the findings in 5c. However, this goes somewhat against the findings of 5d., in which 45% of respondents stated that there was a lack of intrinsic information content in the General Purchasing Power results. It is submitted that in response to 5d., regarding intrinsic information content, preparers, by their own admission, may not understand enough about restatement to comment on such inherent information content.

The other significant findings were that 'Inconsistent methods and assumptions' and 'Indices (not being) relevant' ranked second and third respectively, indicating the apparent lack of faith in the basis and manner in which the accounts are prepared. It is also interesting to note, that whilst cost is frequently cited as the reason for non-compliance with IAS 29, it only ranked fourth, being closely followed by the non-use of such figures by the fiscus.

Question 6b. addressed the use of the CPI (Consumer Price Index) as the basis of restatement. An overwhelming 74% of respondents felt that this index was neither relevant nor appropriate. Comments received referred to the perception of political interference in the process of compiling the index and also to the distortion of price controls on numerous products included in the basket of goods making up the index, which are largely unavailable. One respondent went as far as stating that the "indices are irrelevant! The index is composed of tomatoes and cabbages which are not bought using parallel market rates."

However, this section has found the most significant problem to be the lack of user understanding of restated results. User understanding has been tested in more detail in Sub-Problem 7 below, which finds similar results.

Sub-Problem 7: Do preparers perceive users as able to understand the information presented to them?

(Questions 5e., 5f. & 5g.)

In order to obtain the perceptions of preparers with respect to the ability of users to understand the restated information, three questions were posed. The first question addressed whether the preparers perceive 'industry and commerce' as being adequately educated and understand enough about IAS 29 and the restatement process for the restated figures to be meaningful. Not surprisingly, an overwhelming 77% of preparers responded 'No'. This confirms that a significant reason for the resistance to IAS 29 from preparers relates to the fact that they do not feel the information will be of much use to users who are not able to interpret the little information content that may be contained in the restated results.

The second question addressed the accounting profession itself and questioned whether the preparers perceived the accounting profession to have enough understanding of the restatement adjustments and what they mean for them to be useful. It is very interesting that 54% of respondents, Financial Directors of listed companies, felt that the accounting profession itself did not understand the restated results. This indicates the manner in which the accounting profession, or those very close to the profession, perceives their own ability to interpret the IAS 29 information. One company quoted that the "level of understanding is vague, even among accountants."

These results are significant in indicating that user and preparer understanding of IAS 29 is perceived to be generally very weak. Question 5g. followed up the prior two questions in order to determine whether an education drive from the Institute of Chartered Accountants with respect to IAS 29 would result in a significant increase in use and perceived usefulness of restated results. In this regard, 57% of preparers felt that such a drive would not result in improved use of the results. Comments received ranged from "the task would be too big to yield permanent results" to comments that it is unlikely that the people who need to attend actually would. Nonetheless, 37% of the respondents did feel that an education drive would result in an increase in usefulness. This further illustrates the gap that is becoming evident in the opinions of the preparers, as mentioned above.

The Way Forward

Sub-Problem 8: How should the regulatory accounting bodies in Zimbabwe proceed?

(Questions 7a.)

As discussed in Chapter 2, the 'IAS 29 Task Force' and the Public Accountants and Auditors Board have effectively 3 options that can be followed. These are:

- i. Continue in the current format, with IAS 29 non-compliant accounts being qualified.
- ii. Adopt the IAS 1 "Fair Presentation Override." However, this override requires the quantification of the financial impact of non-compliance to be disclosed. Essentially, therefore, the workings will still need to be performed, but merely disclosed in a note quantifying the financial impact of such non-compliance.
- iii. Remove IAS 29 from the set of standards 'adopted for use in Zimbabwe.' This will effectively result in Zimbabwe no longer being seen as an IAS compliant country and carries with it the related difficulties for foreign investors and analysts. There may be a time lag in regaining the confidence of investors, should Zimbabwe return to being IAS compliant.

It is the responses to this question that best illustrate the difference in opinion of preparers with respect to IAS 29. The mean ranks of the 3 options were almost identical, as can be seen in the table below, reproduced from the Friedman statistical output in Appendix Cii.

Table 6.2
Mean Ranks – Question 7a

	Mean Rank
Option I	1.94
Option ii	2.00
Option iii	2.06

The Friedman test indicated that no rankings were possible at the 95% confidence level, which is obvious from the closeness of the mean ranks.

This confirms the divide in opinions of preparers that became evident earlier in the questionnaire. Comments received ranged from "Zimbabwe still needs to maintain a positive image for its professionalism in accounting...(and) cannot afford to be ruled off as non-IAS compliant", to "(t)here is no value ... investors and analysts have the ability to make their own

adjustments for inflation. I cannot believe that non-compliance will damage our reputation at all.”

6.3 Other Findings

The purpose of this section is to discuss other findings from the study which do not address a specific sub-problem. These include questions relating to the monetary adjustment and its disclosure, as well as an analysis of responses to the questionnaire by industry.

6.3.1 Perceptions about the Monetary Adjustment

The monetary adjustment is a very significant number in the income statement, frequently converting sizeable profits into sizeable losses, and vice versa. It has been commented that particularly little is understood about this number and how it has arisen. As discussed earlier, Brazil have refined GPL accounting in such a way as to disclose the purchasing power adjustments directly with the income statement line items to which they relate. When asked whether a breakdown / analysis of the monetary adjustment would be a helpful disclosure with published inflation adjusted accounts, 54% responded ‘Yes’. A prominent financial director of one of the largest companies in Zimbabwe captured the sentiment of the antagonists, stating that it “would be a self-indulgence by a technician, of no value to a reader.”

Another issue that has been raised is that of the restated Cash Flow Statement. Theoretically, all cash flows should be restated from the monetary unit at the transaction date to the monetary unit current at year-end. There has however been a school of thought that would suggest indicating, together with the relevant cash flow, the monetary gain or loss that resulted from that particular cash flow. This follows from the more favoured ‘indirect’ method of preparing Cash Flow Statements amongst Zimbabwean companies. Ordinarily, the net profit before tax figure will include the monetary adjustment in order to arrive, after adding back non-cash items in the income statement and adjusting for working capital changes, at ‘Cash Generated from Operations’. The issue, therefore, is whether the monetary adjustment should also be added back to net profit before tax, and then be broken up and re-included with the particular line items in the cash flow statement to which that portion of the monetary adjustment relates and from which such adjustment arises. This was a consideration from the Institute perspective at the time of sending the questionnaire. Only 43% of respondents replied ‘Yes’, confirming the perception that information contained in a restated Cash Flow Statement is already difficult to interpret and further breakdowns would probably not be beneficial to readers of financial statements.

6.3.2 Industry Analysis of Responses

Following from sub-problem 2 regarding a perceived differential impact of inflation upon industries, this section attempts to determine whether any significant industry relationships can be identified. Weaknesses of doing this result from the low number of companies in certain industry classifications, which may themselves be debatable. In particular, the manufacturing and retail sectors have been placed together due to many of the large corporates being involved in the entire spectrum from manufacturing through to retailing of their product. By their nature, these two industries differ with respect to their capital intensity, which is a critical factor when considering the impact of inflation. It is therefore submitted from the onset of this section that the results are inherently far from conclusive. Rather, this section attempts to determine where industry relationships may be indicated and hypothesise reasons for this. The attempt at analysing responses by such industry classifications is included in Appendix E. Where significant variances to the overall industry average are identified, the appropriate responses have been greyed out for ease of identification and are discussed below.

Before the results of the analysis are examined, it is necessary to discuss the differential impact of inflation with respect to financial institutions. Financial institutions, by their very nature, have very substantial monetary assets and liabilities in the balance sheet. Accordingly, there is frequently little net impact on the balance sheet when restating the accounts of these entities, with any monetary adjustment arising primarily from the extent to which the entity is financed by equity. This is very different to the impact of inflation on capital-intensive firms, which require significant restatement of non-monetary assets on the balance sheet. The monetary adjustment in capital-intensive firms is particularly related to the extent to which capital assets exceed equity financing. Financial institutions have no, or minimal, such capital assets.

Firstly, it appears from the responses to question 1a. that entities in the mining industry tended to give more thought to the disclosure of the impact of inflation than any other industry. This is probably not surprising given the capital intensity of this sector. This is confirmed in question 3b., in which 50% of mining companies felt that inflationary disclosures were necessary prior to the adoption of IAS 29, as opposed to an across the board average of 11%. However, what is perhaps more surprising is that 100% of financial institutions perceive their industry to have been more impacted by inflation than any other. Across the board, 54% of all respondents felt the same. This is possibly indicative of corporate directors tending to feel that the negative consequences of inflation will have a disproportionately unfavourable impact upon their own firm.

Analysis of the responses to question 4a. indicate that 63% of the management of all firms do not use IAS 29 results for the purposes of management decision making. However, in the industry analysis, 100% of the entities that described themselves as conglomerates use IAS 29 results to at least a moderate extent. The reason for this is debatable, but it can be argued that, where only one industry / line of business is being considered, management prefer to monitor financial results against a more specific benchmark that better reflects the impact of inflation on that specific firm. Where several lines of business are considered, however, it appears that management may more readily accept the analysis of results with a more general benchmark such as the CPI.

The last point worth mentioning with respect to the industry analysis is with respect to the question posed in 6d., regarding the breakdown of monetary adjustment in the cash flow statement. 100% of financial institutions agreed that this would be good idea, against an overall average of only 43%. This is probably due to financial institutions having large monetary assets and liabilities, therefore being the companies with the largest monetary adjustments, generally substantial losses.

No other significant industry relationships in the responses were found. An analysis of the questions requiring ranking did not show any particular trend, thereby indicating that there are no particular perceptions of industry relationships, other than those mentioned.

6.4 Summary of Findings

This section summarises the significant findings of the above questionnaire and draws reasons and conclusions for the results found. These are discussed under the relevant sub-headings to which they relate.

6.4.1 Pre-IAS 29

It is evident that little consideration was given by companies to disclosing the impact of inflation prior to the adoption of IAS 29. No company incorporated any form of comprehensive inflation accounting into their reporting prior to the identification of hyperinflation in 1999. (Edgars Ltd. did make an attempt at a current cost income statement prior to 1999.) Accordingly, at milder rates of inflation, management do not generally perceive there to be any real need for disclosing the impact of inflation on their results, and users are perceived as being able to make their own adjustments.

6.4.2 Use of IAS 29 General Purchasing Power Information

Management do not use the IAS 29 information to any meaningful extent in their decision making process. Following from this, it is not surprising that management do not perceive any meaningful use of the information in practice.

6.4.3 Reasons for Lack of Use / Problems Identified

The major reason for the lack of use of IAS 29 inflation adjusted information that is continually indicated in the questionnaire is the lack of user understanding. This was perceived to be significantly more important at the 95% level than a perceived lack of information content in the IAS 29 figures, although a fairly substantial number of respondents still expressed their reservations about inherent usefulness. This is to be expected given that 77% of respondents felt that users were not able to understand the results. Even more surprising is the perception that 54% of respondents, who are themselves directly involved in the restatement process, do not feel the accountants and preparers themselves are able to understand the results. In addition, a significant 57% felt that an education drive would be a fruitless exercise.

The other problems that were found to be significant hindrances to the usefulness of IAS 29 were the perceptions of inconsistent methods and assumptions in the restatement process, as well as a lack of faith in the Consumer Price Index (CPI), the basis of restatement. The issue of a perception of inconsistent methods and assumptions is probably one that will be addressed with time, directly with the preparers and users. However, the issue of the CPI not being perceived as an adequate basis for restatement is somewhat more difficult to overcome. Perceptions of political interference and manipulation will detract significantly from the faith placed in the results by users. Possible options that can be followed in this regard are addressed in *Chapter 8*, 'Conclusions and Recommendations.' 74% stated that the CPI was an inappropriate basis for restatement.

Interestingly, cost did not emerge as one of the major concerns with respect to IAS 29, as is frequently cited in the comments about the standard. On the contrary, and the most significant of the findings, is the perceived lack of user understanding, which is continually emphasised. About much else, there appears to be a fair amount of disagreement. This is best illustrated in the responses as to the manner in which the regulatory bodies in Zimbabwe should proceed. Almost identical numbers of respondents favour continuing with the current format, moving towards an IAS 1 'Fair Presentation Override' and the abandonment of IAS 29 in Zimbabwe.

Results and Conclusions – Questionnaire 2

7.1 Introduction

This chapter reviews the results of the second set of questionnaires, which were sent to analysts of the companies on the Zimbabwe Stock Exchange and is referred to as the questionnaire to the 'preparers' of financial information. As before, the results are presented in a format similar to the questionnaire itself and shall be discussed in the context of the sub-problem that they attempt to answer. Following the examination of results per sub-problem is a discussion that focuses on and summarises the more significant of those findings.

7.2 Discussion of Results

Sub-Problem 1: To what extent do analysts use financial information in their technical analyses of company performance, and what are the reasons for this?
(Questions 1,2 & 3)

The aim of this question was to determine whether the perceptions of the preparers regarding the lack of use of IAS 29 is justified and in fact correct. As was expected, an overwhelming 65% of respondents stated that they do not use the information at all, with none of the analysts using the information extensively. Several reasons were presented to explain this:

- "The market seems not to accept the concept fully ..." (Respondent 9, Kingdom Securities);
- "Difficult to comprehend ..." (Respondent 10, Continental Securities (Pvt.) Ltd);
- "Unfortunately securities are not priced on inflation adjusted information ..." (Respondent 5, Barbican Asset Management);
- "Analysts lack the knowledge to comprehend the results" (Respondent 34, Mast Securities);
- "Not amenable to trend analysis" (Respondent 19, Bard Stockbrokers (Pvt.) Ltd).

Particularly interesting, and a comment that was confirmed through discussions with several of the respondents, is that the perception that the market is not priced on inflation adjusted information. Respondent 32, Interfin Asset Management, stated that to base investment decisions on the inflation adjusted results would be 'swimming against the stream' and, while abnormal returns may be generated in the medium to long term, it would be unlikely that any investment manager who followed such a strategy would still be employed when such excess returns would in fact be realised." Such comments clearly indicate a perception that the market is

priced on historic information, as would be expected given that little use is made of the IAS 29 results.

Also significant from the responses is the confirmation of the problem of a lack of user understanding. This came through strongly in the first questionnaire and is becoming a frequently recurring theme throughout this study. This is discussed in more detail under sub-problem 2 below.

Another point of concern that is frequently raised is that of the difficulty in performing trend analysis, particularly as there are now only three years to compare results against. It is submitted that this is a short-term problem at the time of implementation of a standard, but that will disappear after a few years of use. IAS 29 uses current dollars as the base level for restatement, which is no different in principle to using constant dollars. Prior period restated results merely need restating to current dollars by the simple application of the movement in the relevant indices over the particular period.

In conclusion to this first sub-problem, it is evident that IAS 29 information is not being used to any significant extent by the analysts on the exchange. On the contrary, several problems have been presented that need to be addressed before such reliance can be placed on the restated information.

Sub-Problem 2: Have analysts been formally trained to assist them in the understanding and interpreting of General Price Level adjusted information?

(Question 4 & 5)

When asked if respondents had attended a formal training course with respect to IAS 29 and the restatement process, only 29% responded 'Yes'. 68% stated that they considered an education drive with respect to IAS 29 to be a good idea, many giving their full-fledged support of such a proposal. Respondent 4, UKI Securities, went as far as stating that she "would ... appreciate any training course brought to her attention, even for a fee." Many other analysts also indicated a willingness to learn and gain an understanding of the restatement process should a formal opportunity arise. Respondent 34, Mast Securities, stated that this is "required as a matter of urgency." This again confirms the earlier findings of a lack of user understanding.

The pessimists, or perhaps realists, however, have not been without their say. Respondent 23, Temple Asset Management, pointed out that the investment community would probably not make the effort to attend. Further, other analysts evidently perceived there to be a lack of

intrinsic information content in the results, stating that no amount of education would help understanding in a process that is riddled with assumptions. On the whole, however, the majority of analysts appear to concede that they do not have the necessary understanding to interpret the information and that an education drive would assist this.

Sub-Problem 3: What are the major reasons for the lack of use of inflation-adjusted information by analysts?
(Question 6)

Several reasons for the non-use of IAS 29 information are presented in the discussion under sub-problem 1. This section aims to analyse which of the possible problems presented are perceived to be more significant in detracting from use. The potential difficulties presented in the questionnaire, and reproduced with results over-page, have been constructed from the findings of the first questionnaire, as well as from the Berliner (1983) study, that also attempted to determine if analysts use inflation-adjusted information.

From the table over-page (table 7.1), the following is evident:

- The most significant perceived problems and reasons for the non-use of IAS 29 information from the analysts' perspective is the level of flexibility allowed in the assumptions and methodology used in the restatement process, together with the fact that only one year of information is readily available due to the constantly moving base from year to year. Lack of user understanding also ranked fairly highly, with 55% of the analysts themselves stating that they do not understand the information presented in the IAS 29 inflation accounts.
- The less significant factors appear to be the availability of the relevant information elsewhere and the use of the Consumer Price Index (CPI) as the basis of restatement. The apparent lack of concern over the use of the CPI is somewhat surprising given the manner in which it was ranked as a relatively more important and fundamental flaw in the first questionnaire.

However, it is perhaps more significant to note that most of the reasons presented actually ranked fairly highly. Probably the major conclusion that can be drawn from this information is that analysts do perceive many factors to hamper their use of restated results. Only data redundancy and the choice of the CPI as the index for restatement were not considered as being major detractors from use.

Table 7.1

REASON	Significant	Moderate	Little or None	No Response
<i>Non-comparability</i>				
Too much flexibility is allowed in the assumptions and methodology used in the restatement process	73%	21%	6%	0%
Assumptions and methods used in preparing the information are not disclosed	53%	35%	9%	3%
Only one year of comparative information is available because of constantly moving base	73%	21%	6%	0%
<i>Lack of intrinsic value</i>				
General Price Level adjusted information is not relevant because it does not portray the effects of inflation on individual companies	44%	38%	12%	6%
<i>Redundancy</i>				
All the information needed for analysis is already available elsewhere	26%	29%	29%	16%
<i>Other</i>				
Not yet enough trend data available for the IAS 29 General Purchasing Power results to be useful	47%	35%	15%	3%
Many analysts do not understand the information presented in the IAS 29 inflation accounts	55%	24%	18%	3%
Use of the Consumer Price Index as the basis of restatement	35%	38%	21%	6%

Sub-Problem 4: Do analysts perceive inflation-adjusted accounts to be more useful for some industries than others?

(Question 9)

59% of respondents stated that there is no particular industry for which inflation adjusted results would be more useful. This confirms the results of the first questionnaire, which also found no such relationship. It is interesting to note, however, that the few who mentioned the particular industry in which restated results were particularly useful tended to mention the financial sector. IAS 29 results are perceived by some as being more useful for those companies with more significant monetary items on their balance sheets. On the whole, however, no substantial industry relationship is indicated in the results.

Sub-Problem 5: Would analysts be satisfied if only the primary IAS 29 accounts were disclosed, and not the historic accounts, as is recommended by IAS 29?

(Question 10)

As is to be expected, an overwhelming 97% of respondents stated that the abandonment of the disclosure of historic results would not be a satisfactory alternative, despite this recommendation in IAS 29. This is most certainly not surprising given the earlier findings about the negligible use of IAS 29 results and the perceived pricing of the market on historic results. Further, this confirms the earlier research into GPL accounting, being that users require that the information be only supplementary to the historic cost information.

Sub-Problem 6: How should the regulatory accounting bodies in Zimbabwe proceed?

(Question 11)

On a simple weighted averaging, the analysts preferred 'Option ii', the fair presentation override, followed by 'Option i', continuing in the same format, and lastly 'Option iii', the abandonment of IAS 29. Using the Friedman statistical test, with pair-wise comparisons (Appendix Di), it is evident that 'Option ii' is significantly preferred to both other options at the 95% level. Further, the preference of option i to option iii is not significant at the 95% level, but working back, this difference is significant at the 88% significance level. Accordingly, 'Option iii', the abandonment of IAS 29, is not a favoured alternative on the part of the analysts.

Analysts seem far more conclusive with respect to this question than do the preparers of financial information. Abandonment of the standard altogether is not a favoured option. Rather, the continued disclosure of both sets of information appears to be preferred. The preference to option ii over option i indicate a preference to the historic cost accounts forming the primary accounts, with the inflation adjusted accounts being secondary, either alongside the historic figures, or in the notes. It is submitted that which set of accounts forms the primary accounts is somewhat of a moot point, so long as an audit opinion is expressed on both.

7.3 Other Findings

As in the previous chapter, this section focused on the monetary adjustment and investigated its significance and usefulness. Two questions were posed in this regard. Firstly, analysts were asked in question 7 whether an analysis / breakdown of the monetary adjustment would be a helpful disclosure with the published inflation adjusted information. A significant 79% stated 'Yes'. This is undoubtedly due to the significance of this number in many cases. This was confirmed in their response to question 8, in which 85% of respondents stated that it would be beneficial for management to provide a discussion of this number to aid in understanding the impact of inflation on the accounts. This contrasts with the findings of the questionnaire to the preparers, where far fewer feel that such a discussion, or disclosure of the breakdown of the

monetary adjustment, is warranted. Annual reports in Zimbabwe seldom have any meaningful comment on the restated accounts.

From the above results, it can be seen that analysts appear to want more information about the IAS 29 results presented to them. If such accounts are presented with no commentary, other than that management do not place any reliance on such information, it is not surprising that the analysts do the same.

7.4 Summary of Findings and Conclusions

This questionnaire found that, generally, analysts do not use inflation adjusted IAS 29 accounts. Various reasons were cited to explain this, including the lack of user understanding and the perception that the Stock Exchange is priced on the historic cost information. Following from this, only 29% of analysts stated that they had received any formal training with respect to GPL accounting, with 68% indicating that attempts to educate analysts would be a good idea. More detailed investigation into the problems with respect to IAS 29 indicated that the two major reasons for non-use are:

- The flexibility in assumptions and methodology given to the preparers of such information, and;
- The constantly moving base leaving only one year of comparative information readily available for comparison.

As was to be expected, an overwhelming 97% of analysts stated that the non-disclosure of the historic cost results, as recommended in IAS 29, would be unacceptable. However, analysts also did not show any desire to have the restated information removed, favouring some form of disclosure of both sets of information.

In conclusion to this section, it appears analysts would like to learn more about the IAS 29 information presented, whilst still retaining the more familiar techniques of analysing historic information. With analysts, the ultimate users of financial information, encouraging the continued disclosure of inflation adjusted results in one form or another, it is unlikely that IAS 29 and its concepts can be abandoned in their entirety.

Recommendations

8.1 Major Conclusions Drawn from Findings

Several major conclusions can be drawn from the findings of the two questionnaires, and have already been discussed with the relevant results. Firstly, it is clear that prior to the implementation of IAS 29 companies were making negligible effort to portray the effects of inflation on their financial results. From the results it is not possible to determine which theories underlying voluntary disclosures predominated in Zimbabwe in the period prior to IAS 29. However, it is obvious that most companies felt that either such information was not necessary or that it was not beneficial for management to disclose the restated figures.

Secondly, the results of the two questionnaires are conclusive in indicating that the IAS 29 figures are not being used to any great extent by either management or by the analysts. It is interesting to note that Frishkoff (1982) concluded, in his review of 52 empirical studies, that both management and user education were required before any significant change in perceived usefulness of inflation accounting would be evident. This study confirms that a similar situation exists in Zimbabwe in which there is little use of the inflation adjusted information. Management and user understanding need to improve before any significant increase in perceived usefulness can be seen.

The results also indicate that both management and analysts cling to familiar techniques when reviewing company performance and are overwhelmingly not prepared to forego the disclosure of historic cost information. This confirms the findings in several other studies on inflation accounting as discussed in the literature review in Chapter 4. In fact, no study reviewed throughout the course of the fieldwork indicated that users felt that historic cost information should not be disclosed, as is recommended in IAS 29. Such a move would not sit comfortably with the investment community. It is evident that the perceived usefulness of IAS 29 GPL information, particularly in Zimbabwe, is extremely low.

Three points have been emphasised as significant problem areas in the restatement process:

- Lack of user understanding;
- Assumptions and methods used in the restatement process, and;
- The use of the CPI as the basis of restatement.

On the other hand, the following problems are not considered to be as important in the restatement process:

- Fiscus does not recognise restated results
- Lack of intrinsic information content

Further cost was also not as significant a problem as initially perceived by antagonists prior to the study.

8.2 Additional Conclusions drawn from Findings

Management do not use IAS 29 information in their operational decision-making process, nor do they use such information in the determination of dividend policy. Preparers feel that neither the users, nor the preparers themselves, understand the IAS 29 results adequately for them to be of any use.

There is mixed opinion amongst preparers regarding disclosures relating to the monetary adjustment. Analysts, however, would like to see more information and discussion about this often significant figure. With respect to the investigation of industry relationships, the only major finding was that relating to the usefulness of a breakdown and discussion of the monetary adjustment. 100% of financial institutions favoured more information on the composition of the monetary adjustment and a discussion in the annual report, compared to far weaker results from all other industries. This is expected given the push by the Institute of Bankers to have the uplift on the opening balances of monetary items taken directly to equity and not through the income statement in the monetary adjustment line.

Analysts also admitted to not using IAS 29 in their technical analyses of company performance. The major problems hindering such use include the flexibility allowed to preparers and the availability of only limited trend information making time series analysis difficult.

Other conclusions drawn from the findings were as follows:

- Analysts do not want to see the abandonment of IAS 29 in Zimbabwe.
- Analysts overwhelmingly want the disclosure of both historic and restated information.
- Preparers do not feel that an education drive would be successful, although analysts generally do and are encouraging such an initiative.

8.3 Recommendations and Implications for the Future

Several studies examined in the literature review in chapter 4 make reference to a 'learning curve' with respect to inflation accounting and its use. Brazil has been in a hyperinflationary situation for many years and users appear, with time, to have accepted the necessity for such information. Before the abandonment of IAS 29 in Zimbabwe, sufficient time should be allowed to pass in order to give the users a reasonable opportunity to familiarise themselves with the standard and the restatement process. Further, inflation continues to increase, with the reported inflation for August 2002 rising to an all time year-on-year high of 135%. This will continue to inflate the need for a comprehensive system of bringing to book the impact of inflation. The Institute of Chartered Accountants of Zimbabwe, together with the other accounting regulatory bodies in Zimbabwe, should consider facilitating this learning process. Despite several negative comments received from the preparers, many users indicated a willingness to obtain an understanding of the information presented.

As mentioned above, the use of the CPI as the basis of restatement is also a significant area of concern. The very foundation of the indexing process is plagued by a perception of government manipulation. As discussed in Chapter 3, Brazil is a country that has also followed an indexing procedure for restating financial results. It is interesting to note that Doupnik et al (1995), referred to earlier, indicate that, in the light of several significant conceptual weaknesses of the 'System of Monetary Correction', including the non-restatement of inventory, the issue of a manipulated index was the most severe. Brazil suffered this problem until 1991, at which point an independent non-governmental body started compiling an index that was adopted for restatement. Accordingly, it is recommended that the Institute of Chartered Accountants, and the other regulatory bodies in Zimbabwe, consult with a view to determining the use of an alternative index, which will be prepared independent from government influence. It is conceded that such indices are not readily available in Zimbabwe, but if the rate of inflation continues to increase and government intervention continues to be perceived, the regulatory authorities should appoint a suitable body to prepare a transparent and appropriate index. In the extreme case, the regulatory bodies may have to consider the use of an index prepared by a particular 'sub-committee', appointed either at the institute level, or by the Public Accountants and Auditors Board. Whilst the foregoing may sound desirable in theory, this is obviously a difficult issue in practice. Consideration would of course have to be given to such factors as the antagonising of the relevant government departments.

Further, should the rate of inflation continue to rise uncontrollably, consideration may need to be given to the use of more frequent indices. While antagonists may despair, Brazil had such a system in place for many years, whereby results were indexed daily. The set-up costs may be

large, but should inflation continue to spiral, monthly adjustments will not be adequate to capture the relevant changes in purchasing power. It would be wise for the regulatory bodies to give consideration to this issue, as the government's current economic policies do not make such a situation inconceivable.

Lastly, it is recommended that 'sub-committees' be formed to address the various weaknesses that have been identified in the restatement procedure. These would include consideration of the conceptual problems identified in Zimbabwe and an in-depth review of various refinements that may overcome these concerns. In this regard, the refinements learnt through the Brazilian experience may be useful. Further, such 'sub-committees' should also address the issue of the perceived inconsistent assumptions and methods in the restatement process. It is submitted, the writer having assisted numerous companies in the preparation of IAS 29 accounts, that this may be more than a naïve concern. Issues such as the treatment of the deferred taxation uplift year on year should be resolved. Further, as inflation continues to rise, such assumptions may need to be regulated more closely. For example, the use of a single yearly average index for the restatement of income statement items may be acceptable at the rates of inflation currently being experienced. However, further increases would demand more specific assumptions. It is submitted that many companies obtain the use of their auditors in the restatement exercise, not having the necessary skills and resources to do the necessary work themselves. In this regard, a standardising of the restatement procedure would be made somewhat easier, primarily through consultation with the 'Big 4' - Deloitte & Touche, PWC, Ernst and Young and KPMG.

8.4 Areas for Future Research

This study has focussed on the use and perceived usefulness of IAS 29 GPL accounting. Throughout the fieldwork, several areas that are in urgent need of research have presented. These include the following:

- Investigation into the Consumer Price Index, the consistency of preparation of the index and the composite bundle of goods making up the relevant basket. Consideration should be given to the reasonableness of the goods in the bundle and whether they give a fair view of the changing price levels in the economy. Other possible indices that may be used need to be sought. Further, should other suitable indices be found, a comparison between the impact of these indices on the accounts, as opposed to the current CPI, should be investigated.
- Investigation into the conceptual refinements of GPL accounting as used in other countries such as Brazil, with a view to subsequent implementation, if feasible, of such refinements in Zimbabwe.

- Similar to the conceptual refinements mentioned above, an investigation is required into the preferred method of disclosing the monetary adjustment. Various options may be explored, including the Brazilian system of writing the monetary adjustment amounts back against the particular income statement line items to which they relate, or possibly through a separate statement as has been suggested in Zimbabwe.
- Investigation into the usefulness and meaning of a Restated Cash Flow Statement.
- A market-efficiency study. Through the coursework of this research, and in particular during attempts at a market-based study, significant concern was raised in many corners about the efficiency to the Zimbabwe Stock Exchange, and accordingly on the validity of results of any market-based study. Such a study would open the way for further market-based research aimed at determining whether inflation adjusted figures are better predictors, or have greater explanatory power, of stock returns than historic results. In time, a corporate failure prediction model could also be useful, with a view to determining whether restated results are superior to historic figures.

8.5 Summary

The objective of this study was to investigate the introduction of IAS 29 in Zimbabwe, with a view to determining the use and perceived usefulness of the standard. The study has found that both the use and perceived usefulness of the GPL information, particularly on the part of the preparers of financial information, is extremely low at the current time. The major reasons presented to explain this are the lack of user understanding, inconsistent methods and assumptions in the restatement process and the use of an inappropriate index. This resulted in recommendations based upon findings in other countries, where research has found the existence of a learning curve, and accordingly time is needed for user familiarisation. The abandonment of IAS 29 is not considered the best alternative at the current time and the standard should remain until such time as all parties have had reasonable time to obtain an understanding of the respective concepts. This could possibly be facilitated through focused training courses to assist where possible. Also recommended was a review of the index used, so as to remove the perceptions of government intervention.

In closing, this study has found there to be no significant use or perceived usefulness of IAS 29 GPL information in Zimbabwe. It is hoped that the findings of this study will be useful to the various accounting regulatory authorities and in particular, to the 'IAS 29 Task Force'.

APPENDICES

University of Cape Town

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“Selection of Published comments”

The following is an extract from a supplement to the Radar Holdings Limited 2001 Annual Report, together with a further quote from the Zimbabwe Sun 2002 Annual Report, of quotable comments by listed companies with respect to IAS 29:

EDGARS STORES LIMITED

Final results for the 52 weeks ended 6 January 2001

Results – Inflation Adjusted

The Edgars group has accepted that it should conform with the requirements of IAS 29 and has included inflation adjusted statements in its published accounts.

However, the board of directors disassociate themselves from these statements as they are grossly misleading and have little value in assessing the true results of the business. It would be more appropriate to simply convert current and previous year figures to US dollars at the prevailing exchange rate.

14 March 2001

ZIMBABWE SUN LIMITED

2002 Annual Report

Hyperinflation Financial Reporting

In conformity with the requirements of International Accounting Standard 29, inflation adjusted financial statements have been produced and have been reported upon by our auditors. These are based on the historical data which has been adapted in accordance with the accounting standard to take account of the effects of inflation. The majority of comment contained within this annual report relates to the historical information; the reason for this is quite simple, analysts have make it clear to us that they take very little of the inflation adjusted

information to account as they consider there is a high risk that different assumptions made by different companies will result in it being impossible to compare results between companies. It is a source of concern to us that the enormous effort and cost which goes into producing inflation adjusted information is not delivering a product which the users want. If this remains the case, it is not money well spent and consideration will need to be given by both this company and the business community to opting out of this standard as being good in theory, but poor in practice. The Company does not use hyperinflation accounts as a business management tool, though clearly concepts like fixed asset and stock replacement values are of vital importance in an inflationary environment and have been recognised and taken to account in decision making for some years.

17 May 2002

HADDON & SLY LTD.

Unaudited group results for twelve months ended 31 December 2000

Inflation accounting:

Although we have strong reservations about the suitability of and value of IAS 29 in its present format, we have complied with the requirements unwillingly and at substantial professional cost. Until the Inspector of taxes accepts inflation adjusted figures in computations, a simple, more user friendly basis should be considered.

28 March 2001

HADDON AND SLY LTD.

Unaudited interim group results for six months ended 30 June 2001.

Inflation accounting:

We complied with the International Accounting Standard 29 for our results to December 2000 from which we have found the cost incurred and effort were out of all proportion to the deemed benefits. Shareholders have complained that the volume of figures and notes were of no benefit to them and non-accounting investors found the format more confusing rather than being of more help to them.

For these reasons we have reported only on a historical cost basis and have submitted our views and suggestion to a task force instigated by the Zimbabwe Stock Exchange and the Institute of Chartered Accountants of Zimbabwe.

29 September 2001

COLCOM HOMDINGS LIMITED

Unaudited results: Six months ended 30 June 2001

Notes:

There has been considerable debate on reporting under International Accounting Standard 29. Whilst there is no doubt that the economy is operating under hyperinflationary conditions, management has received little benefit from traditional inflation adjusted accounting methods to interpret company results. Instead a combination of factors like volumes, margins and hard currency measures have proved more meaningful yardsticks to assess day to day performance. For this reason, the directors are of the opinion that the costs of producing inflation adjusted figures at the interim results stage, outweighs the

benefits to stakeholders. To comply with statutory requirements, it is the intention of the company to produce inflation adjusted accounts at its year end.

9 August 2001

INNSCOR AFRICA LIMITED

Audited Financial Information for the year ended 30 June 2001.

Directors Report

The directors have reviewed the Group's position on International Accounting Standard 29. Acknowledging the complex multi-country structure of the Group and the impracticality of applying the Standard, the directors believe that no useful purpose will be served by complying with the Standard and that compliance with the Standard will produce results that are not meaningful. The Group has therefore not complied with the provisions of IAS 29 in its financial statements for the year ended 30 June 2001.

23 August 2001

INTERMARKET DISCOUNT HOUSE LIMITED

Unaudited results for the half-year ended 30 June 2001

Accounting Policies:

Whilst the company complied with IAS 29 at the time of the publication of the year-end financial statements, it is the opinion of the directors that no useful purpose will be served by complying with the standard. The company will therefore not comply with IAS 29 until the taskforce on IAS 29, set up by the Institute of Chartered Accountants of Zimbabwe, has recommended a practical way forward of reporting in a hyperinflationary economy.

31 August 2001

TA HOLDINGS LIMITED

Unaudited results for the six months ended
30 June 2001

Inflation adjusted results

Inflation adjusted accounts are being published to comply with IAS 29 (Financial Reporting in Hyperinflationary Economies). In view of the current controversy surrounding the usefulness of the accounts to stakeholders, the directors do not see any value in producing a commentary on them.

31 August 2001

**THE COTTON COMPANY OF
ZIMBABWE**

Audited report for the year ended 31 March
2001

**Hyperinflation adjusted financial
statements**

These financial statements have been prepared in compliance with International Accounting Standard 29 (IAS 29) "Financial Reporting in Hyperinflationary Economies" as the directors wish to satisfy the requirements of the Zimbabwe Stock Exchange. The directors, however, believe that the time and effort spent by senior personnel, and the cost incurred in preparing inflation adjusted accounts is far greater than any benefit that might be derived by the group. We further believe that users of financial statements will give more weight to those figures based on historical cost and will already be aware of the effect of the high rate of inflation in Zimbabwe.

31 May 2001

Illustration of IAS 29 as Applied in Zimbabwe

The following serves as an illustrative example of IAS 29 as commonly applied in Zimbabwean companies. The historical balance sheets of XYZ Ltd. are given for the last three years together with income statements and cash flow statements for the previous two years. These financial statements will then be restated and the process documented. The monetary adjustment is also discussed and an additional disclosure proposed.

The first three pages include the historic accounts of XYZ Ltd. The restated balance sheet and income statement follow, together with the proof and breakdown of the monetary adjustment - effectively a breakdown of where the monetary adjustment has arisen. This breakdown / proof of the monetary adjustment is then presented as an additional recommended disclosure. This format illustrates the school of thought, headed by Mr. Les Anderson, which believes that additional information is required for users to fully appreciate the monetary adjustment. All workings are included at the back of this appendix, together with the indices used in the restatement process on the last page of appendix B.

A Note on the Cash Flow Statement

Zimbabwean companies almost without exception prepare cash flow statements on the 'indirect method'. Cash flows are determined from movements in the relevant balance sheet accounts. An identical method is used in preparing the restated IAS 29 cash flow statement. This method of preparation does not result in actual cash flows being restated to a monetary unit current at year-end. For example, a long-term loan of 100, on which there is no movement in the current year, remains at 100 in the closing accounts. Restatement of the prior year accounts results in the uplift of the prior year balance by the rate of inflation over the period to, for example, 200. It is not uncommon in Zimbabwe for that movement, actually a monetary adjustment and not a cash flow, to be included in the cash flow statement.

Historic Cost Balance Sheets of XYZ Ltd. as at F04

Capital Employed

		F04 ZWD	F03 ZWD	F02 ZWD	
Share capital	Note 1	1,500	1,500	1,500	Non-monetary
Retained Income		2,500	1,200	500	Balancing Figure
		<u>4,000</u>	<u>2,700</u>	<u>2,000</u>	
Long-term liabilities (15%)	Note 4	2,900	2,700	2,700	Monetary
Deferred Taxation		474	420	315	
		<u>7,374</u>	<u>5,820</u>	<u>5,015</u>	

Employment of Capital

Fixed assets					
Cost	Note 2	4,200	3,500	3,500	Non-monetary
Accumulated depreciation	Note 2	(1,580)	(1,400)	(1,050)	Non-monetary
NBV		<u>2,620</u>	<u>2,100</u>	<u>2,450</u>	
Current assets					
Inventory	Note 3	3,600	1,900	1,300	Non-monetary
Debtors		3,850	1,800	1,065	Monetary
Cash at bank		-	1,020	700	Monetary
		<u>7,450</u>	<u>4,720</u>	<u>3,065</u>	
Current liabilities					
Creditors		(1,296)	(500)	(200)	Monetary
Taxation		(600)	(500)	(300)	Monetary
Cash at bank - overdraft		(800)	-	-	Monetary
		<u>(2,696)</u>	<u>(1,000)</u>	<u>(500)</u>	
		<u>7,374</u>	<u>5,820</u>	<u>5,015</u>	

NOTES

Note 1

The share capital was issued at incorporation on 1/1/F00.

Note 2

Fixed assets are depreciated on a straight line basis over 10 years. However, the tax authority allows a five-year "wear and tear" allowance. At incorporation \$3 500 of machinery was purchased. On 1/1/F04 machinery with a cost of \$600 and an accumulated depreciation of \$240 was disposed of for \$700. This was replaced immediately with machinery costing \$1 300.

A full years depreciation is provided in the year of acquisition and none in the year of disposal.

Note 3

Inventory has consistently turned over 4 times every year.

Income statement of XYZ Ltd for the period ended 31/12/F04

		F04 ZWD	F03 ZWD
Sales		12,560	8,000
Cost of Sales		<u>(9,000)</u>	<u>(5,500)</u>
Gross profit		3,560	2,500
Operating costs		(900)	(450)
Depreciation	Wkg 1	(420)	(350)
Profit on sale of fixed assets	Wkg 2	340	-
Finance Charges	Wkg 3	(420)	(405)
Profit before taxation		<u>2,160</u>	<u>1,295</u>
Taxation		(860)	(595)
Normal (at 30%)		<u>(806)</u>	<u>(490)</u>
Deferred	Wkg 4	<u>(54)</u>	<u>(105)</u>
Net profit		<u>1,300</u>	<u>700</u>
Opening retained earnings		1,200	500
Closing retained earnings		<u><u>2,500</u></u>	<u><u>1,200</u></u>

Cash flow statement for the year ended 31/12/F04

	F04 ZWD	F03 ZWD
CASH GENERATED FROM OPERATING ACTIVITIES		
Profit before tax	2,160	1,295
Adjustments:		
Profit on sale of fixed assets	(340)	-
Depreciation	420	350
Finance charges	420	405
	<u>2,660</u>	<u>2,050</u>
Working capital changes:		
Inventory	(1,700)	(600)
Debtors	(2,050)	(735)
Creditors	796	300
Taxation	(706)	(290)
	<u>(1,000)</u>	<u>725</u>
CASH (USED IN) / GENERATED FROM INVESTING ACTIVITIES		
Proceeds on disposal of fixed assets	700	-
Acquisition of fixed assets	(1,300)	-
	<u>(600)</u>	<u>-</u>
CASH (USED IN) / GENERATED FROM FINANCING ACTIVITIES		
Increase in borrowings	200	-
Finance charges paid	(420)	(405)
	<u>(220)</u>	<u>(405)</u>
(Decrease) / increase in cash / cash equivalents	<u>(1,820)</u>	<u>320</u>
Opening balance per bank	1,020	700
Closing balance per bank	<u><u>(800)</u></u>	<u><u>1,020</u></u>

Restated Balance Sheets of XYZ Ltd. as at F04
All figures at purchasing current at end of F04

Capital Employed

		F04 ZWD	F03 ZWD	F02 ZWD
Share capital	Wkg 5	30,000	30,000	30,000
Retained income	Balancing figure	(5,876)	1,813	5,301
		<u>24,124</u>	<u>31,813</u>	<u>35,301</u>
Long-term liabilities (15%)	Wkg 6	2,900	4,909	8,571
Deferred taxation	Wkg 9	9,098	12,295	13,406
		<u>36,122</u>	<u>49,017</u>	<u>57,278</u>

Employment of Capital

Fixed assets				
Cost	Wkg 7	60,364	70,000	70,000
Accumulated depreciation	Wkg 7	(29,236)	(28,000)	(21,000)
NBV		<u>31,128</u>	<u>42,000</u>	<u>49,000</u>
Current assets				
Inventory	Wkg 8	3,840	3,707	4,262
Debtors	Wkg 6	3,850	3,273	3,381
Cash at bank	Wkg 6	-	1,855	2,222
		<u>7,690</u>	<u>8,835</u>	<u>9,865</u>
Current liabilities				
Creditors	Wkg 6	(1,296)	(909)	(635)
Taxation	Wkg 6	(600)	(909)	(952)
Cash at bank - overdraft	Wkg 6	(800)	-	-
		<u>(2,696)</u>	<u>(1,818)</u>	<u>(1,587)</u>
		<u>36,122</u>	<u>49,017</u>	<u>57,278</u>

Restated income statement

For the period ended 31/12/F04

All figures at purchasing current at end of F04

		F04 ZWD	F03 ZWD
Sales	Wkg 10	16,747	20,000
Cost of sales	Wkg 11	(14,134)	(15,805)
Gross profit		2,613	4,195
Operating costs	Wkg 12	(1,200)	(1,125)
Depreciation	Wkg 13	(6,036)	(7,000)
Profit on sale of fixed assets	Wkg 14	(5,928)	-
Finance charges	Wkg 15	(560)	(1,013)
		(11,111)	(4,943)
Monetary adjustment	Balancing figure	1,031	1,235
Profit before taxation		(10,080)	(3,708)
Taxation		2,391	220
Normal (at 30%)	Wkg 16	(806)	(891)
Deferred	Wkg 17	3,197	1,111
Net profit	Computed	(7,689)	(3,488)
Opening retained earnings	Per restated b/s	1,813	5,301
Closing retained earnings	Per restated b/s	(5,876)	1,813

Restated cash flow statement for the period ended 31/12/F04

	F04 ZWD	F03 ZWD
CASH GENERATED FROM OPERATING ACTIVITIES		
Profit before tax	(10,080)	(3,708)
Adjustments:		
Profit on sale of fixed assets	5,928	-
Depreciation	6,036	7,000
Finance Charges	560	1,013
	<u>2,444</u>	<u>4,305</u>
Working capital changes:		
Inventory	(133)	555
Debtors	(577)	108
Creditors	387	274
Taxation	(1,115)	(934)
	<u>1,006</u>	<u>4,308</u>
CASH (USED IN) / GENERATED FROM INVESTING ACTIVITIES		
Proceeds on disposal of fixed assets	1,272	-
Acquisition of fixed assets	(2,364)	-
	<u>(1,092)</u>	<u>-</u>
CASH (USED IN) / GENERATED FROM FINANCING ACTIVITIES		
Increase in borrowings	(2,009)	(3,662)
Finance charges paid	(560)	(1,013)
	<u>(2,569)</u>	<u>(4,675)</u>
Increase in cash / cash equivalents	(2,655)	(367)
Opening balance per bank	1,855	2,222
Closing balance per bank	<u><u>(800)</u></u>	<u><u>1,855</u></u>

Proof / breakdown of monetary adjustment

	F04 - in F04 monetary unit		F03 - in F03 monetary unit		Adjustment F04 Monetary Unit
	Historic	Restated	Historic	Restated	
Opening Net Monetary Position					
Long-term liabilities	(880)	(1,599)	(1,435)	(2,505)	1,946
Debtors	(2,700)	(4,909)	(2,700)	(4,714)	3,662
Cash at bank	1,800	3,273	1,065	1,860	(1,445)
Creditors	1,020	1,855	700	1,222	(949)
Taxation	(500)	(909)	(200)	(349)	271
Cash at bank - overdraft	(500)	(909)	(300)	(524)	407
Turnover	12,560	16,747	8,000	11,000	(5,454)
Cost of sales / operating expenses					
Per income statement	(11,600)	(15,467)	(6,550)	(9,006)	4,466
Add opening inventory	(9,900)	(15,334)	(5,950)	(9,312)	6,112
Less closing inventory	1,900	3,707	1,300	2,344	(1,898)
	(3,600)	(3,840)	(1,900)	(2,039)	252
Proceeds on disposal of fixed assets	700	1,272	-	-	-
Purchase of fixed assets	(1,300)	(2,364)	-	-	-
Interest payable	(420)	(560)	(405)	(557)	277
Taxation	(806)	(806)	(490)	(490)	0
Normal tax	(806)	(806)	(490)	(490)	0
Calculated net monetary position	(1,746)	(2,777)	(880)	(1,559)	1,235
Actual net monetary position					
Long-term liabilities	(1,746)	(1,746)	(880)	(880)	-
Debtors	(2,900)	(2,900)	(2,700)	(2,700)	-
Cash at bank	3,850	3,850	1,800	1,800	-
Creditors	-	-	1,020	1,020	-
Taxation	(1,296)	(1,296)	(500)	(500)	-
Cash at bank - overdraft	(600)	(600)	(500)	(500)	-
	(800)	(800)	-	-	-
Calculated monetary adjustment	1,031	1,031	679	679	1,235
Actual monetary adjustment	1,031	1,031	679	679	1,235
Check of monetary adjustment	-	-	-	-	-

Composition of monetary adjustment

	F04		F03	
	Adjustment		Adjustment	
GAINS FROM OPENING MONETARY LIABILITIES				
Long-term liabilities	2,209		3,662	
Creditors	409		271	
Taxation	<u>409</u>	3,027	<u>407</u>	4,340
LOSSES FROM OPENING MONETARY ASSETS				
Debtors	(1,473)		(1,445)	
Cash at bank	<u>(835)</u>	(2,308)	<u>(949)</u>	(2,394)
FIXED ASSETS				
Gains from additions sourced from monetary assets	1,064		-	
Loss on monetary assets realised on disposal of fixed assets	<u>(572)</u>	492	<u>-</u>	-
STOCK				
Gains arising from stock sourced from monetary assets	240		252	
Loss arising from stock brought forward	<u>(1,807)</u>	(1,567)	<u>(1,898)</u>	(1,646)
INCOME STATEMENT				
Loss arising on restatment of turnover	(4,187)		(5,454)	
Gain arising on restatement of net cost	5,434		6,112	
Gain arising on restatement of interest	<u>140</u>	1,387	<u>277</u>	935
Monetary adjustment	<u>1,031</u>		<u>1,235</u>	

Reconciliation of historic profit before taxation to restated profit before taxation

	F04		F03	
Profit before tax - historic		2,160		1,295
Sales	4,187		12,000	
Cost of Sales	(5,134)		(10,305)	
Operating costs	(300)		(675)	
Finance charges	<u>(140)</u>	(1,387)	<u>(608)</u>	412
Depreciation	(5,616)		(6,650)	
Profit on sale of fixed assets	<u>(6,268)</u>	(11,884)	<u>-</u>	(6,650)
GAINS FROM OPENING MONETARY LIABILITIES				
Long-term liabilities	2,209		3,662	
Creditors	409		271	
Taxation	<u>409</u>	3,027	<u>407</u>	4,340
LOSSES FROM OPENING MONETARY ASSETS				
Debtors	(1,473)		(1,445)	
Cash at bank	<u>(835)</u>	(2,308)	<u>(949)</u>	(2,394)
FIXED ASSETS				
Gains from additions sourced from monetary assets	1,064		-	
Loss on monetary assets realised on disposal of fixed assets	<u>(572)</u>	492	<u>-</u>	-
STOCK				
Adjustment arising from stock sourced from monetary assets	<u>240</u>	240	<u>252</u>	252
INCOME STATEMENT				
Loss arising on restatement of turnover	(4,187)		(5,454)	
Gain arising on restatement of net cost	3,627		4,214	
Gain arising on restatement of interest	<u>140</u>	(420)	<u>277</u>	(963)
Profit before taxation - restated		(10,080)		(3,708)

WORKINGS**Working 1**

F03 Depreciation	$= 3\,500 \times 1/10$
	<u>$= 350$</u>
F04 Depreciation	$= (3\,500 - 600 + 1\,300) \times 1/10$
	<u>$= 420$</u>

Working 2

Profit on sale	$= 700 - (600 \text{ (cost)} - 240 \text{ (acc dep)})$
	<u>$= 340$</u>

Working 3

Finance charges F03	$= 2\,700 \times 15\%$
	<u>$= 405$</u>
Finance charges F04	$= 2\,700 \times 15\% \times 6/12 + 2\,900 \times 15\% \times 6/12$
	<u>$= 405$</u>

Working 4**Fixed Assets**

	NBV	ITV	Diff	Deferred Tax B/s (30%)	Deferred Tax I/s (30%)
1/1/F00	3,500	3,500	-	-	-
31/12/F00	3,150	2,800	350	105	105
31/12/F01	2,800	2,100	700	210	105
31/12/F02	2,450	1,400	1,050	315	105
31/12/F03	2,100	700	1,400	420	105
31/12/F04	2,620	1,040	1,580	474	54

Working 5

Share Capital - F02	$= 1\,500 \times 2\,000/100$
	<u>$= 30\,000$</u>
Share Capital - F03 & F04	As above

Working 6

Long-term liability - F02	$= 2\,700 \times 2\,000 / 630$ <u>$= 8\,571$</u>
Long-term liability - F03	$= 2\,700 \times 2\,000 / 1\,100$ <u>$= 4\,909$</u>
Long-term liability - F04	<u>$= 2\,900$ (monetary)</u>
Debtors - F02	$= 1\,065 \times 2\,000 / 630$ <u>$= 3\,381$</u>
Debtors - F03	$= 1\,800 \times 2\,000 / 1\,100$ <u>$= 3\,273$</u>
Debtors - F04	<u>$= 3\,850$ (monetary)</u>
Cash - F02	$= 700 \times 2\,000 / 630$ <u>$= 2\,222$</u>
Cash - F03	$= 1\,020 \times 2\,000 / 1\,100$ <u>$= 1\,855$</u>
Cash - F04	<u>$= -800$ (monetary)</u>
Creditors - F02	$= -200 \times 2\,000 / 630$ <u>$= -635$</u>
Creditors - F03	$= -500 \times 2\,000 / 1\,100$ <u>$= -909$</u>
Creditors - F04	<u>$= -1\,296$ (monetary)</u>
Taxation - F02	$= -300 \times 2\,000 / 630$ <u>$= -952$</u>
Taxation - F03	$= -500 \times 2\,000 / 1\,100$ <u>$= -909$</u>
Taxation - F04	<u>$= -600$ (monetary)</u>

Working 7

Fixed assets - Cost - F02	$= 3\,500 \times 2\,000 / 100$ <u>$= 70\,000$</u>
Fixed assets - Cost - F03	$= 3\,500 \times 2\,000 / 100$ <u>$= 70\,000$</u>
Fixed assets - Cost - F04	$= 2\,900 \times 2\,000 / 100 + 1\,300 \times 2\,000 / 1\,100$ <u>$= 60\,364$</u>
Fixed assets - Acc Dep - F02	$= -1\,050 \times 2\,000 / 100$ <u>$= 21\,000$</u>
Fixed assets - Acc Dep - F03	$= -1\,400 \times 2\,000 / 100$ <u>$= 28\,000$</u>
Fixed assets - Acc Dep - F04	$= -1\,450 \times 2\,000 / 100 + -130 \times 2\,000 / 1\,100$ <u>$= 29\,236$</u>

Working 8

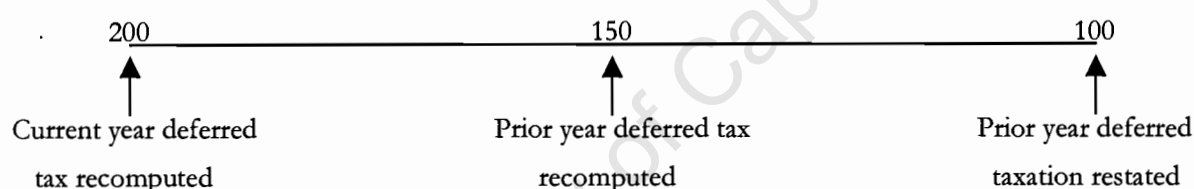
is the cause of a certain amount of difficulty in practice and generally requires the use of assumptions,

Computation of Index - F02	$= ((Y/\text{end index} - \text{mid index}) \times 4.5/6) + \text{mid index}$ $= ((630 - 550) \times 4.5 / 6) + 550$ <u>$= 610$</u>
Computation of Index - F03	$= ((Y/\text{end index} - \text{mid index}) \times 4.5/6) + \text{mid index}$ $= ((1\,100 - 800) \times 4.5 / 6) + 800$ <u>$= 1\,025$</u>
Computation of Index - F04	$= ((Y/\text{end index} - \text{mid index}) \times 4.5/6) + \text{mid index}$ $= ((2\,000 - 1\,500) \times 4.5 / 6) + 1\,500$ <u>$= 1\,875$</u>
Restated inventory - F02	$= 1\,300 \times 2\,000 / 610$ <u>$= 4\,262$</u>
Restated inventory - F03	$= 1\,900 \times 2\,000 / 1\,025$ <u>$= 3\,707$</u>
Restated inventory - F04	$= 3\,600 \times 2\,000 / 1\,875$ <u>$= 3\,840$</u>

Deferred Taxation

The calculation of deferred taxation and its treatment has been another contentious issue in Zimbabwe. In compliance with International Accounting Standard 12, the fully comprehensive method is used. This example illustrates the 'simple' way of computing deferred taxation. For completeness purposes, the major competing method of computing deferred taxation, that has gained significant acceptance, is discussed briefly below.

In historic cost accounting, the movement in the deferred taxation account on the balance sheet will be the corresponding income statement charge, adjusted where necessary for such items as revaluations. In the restatement process, however, the prior year restated deferred taxation balance is restated to the monetary unit at the end of the current year. If the same approach were used to compute the income statement charge as in the historical accounts, this would simply be the movement in the deferred taxation balance sheet accounts. However, antagonists to this approach argue that a portion of this movement in the deferred taxation balance relates to prior periods. Their belief is that the prior year deferred taxation balance should be recalculated at the end of the following year. Only the movement from the recalculated deferred taxation balance of prior year to the current balance should be charged against income. The difference should be brought through the statement of changes in equity as a prior year adjustment. This is illustrated below:



In this example, the prior year restated deferred taxation is 100 and the current year's is 200. However, had prior year's deferred taxation been recomputed in the current period, the balance would have been 150. The reason for this difference is that in recomputing the prior year balance in the current year, the carrying values of the assets and liabilities are uplifted by the movement in the inflation index, but the tax bases remain at historical amounts. Accordingly, the temporary differences that arise are different from those that arise from the restatement of the temporary differences themselves, due to the non-restatement of the tax bases. Accordingly, in the above example, 50 would be brought directly to equity and therefore only 50 would be the income statement charge.

This treatment is fairly widespread in Zimbabwe with several companies computing and disclosing deferred taxation in this manner. It, however, remains a debatable issue that needs resolving at Institute level. For the purposes of this example, the more 'simple' method of computing deferred taxation in the monetary unit of the balance being calculated, and then restating that balance to the monetary unit current at the end of the period being presented, is followed. Other issues, such as the increased need to discount the deferred taxation balance, or at least the tax base used in the computation, in times of high inflation, have been also been raised as areas of concern, but are not addressed in this document. Note that on restatement, a temporary difference arises relating to stock that is not present in the historic accounts. This is frequently overlooked in practice.

Deferred taxation - F02 In F02 monetary unit:
 $= (\text{Restated carrying value} - \text{tax base}) * \text{tax rate}$
 $= ((2450 * 630 / 100) + (4262 * 630 / 2000) - (1400 + 1300)) * 30\%$
 $= 4\,223$

Restated to F04 monetary unit:
 $= 4\,223 * 2\,000 / 630$
 $= 13\,406$

Deferred taxation - F03 In F03 monetary unit:
 $= (\text{Restated carrying value} - \text{tax base}) * \text{tax rate}$
 $= ((2100 * 1100 / 100) + (3707 * 1100 / 2000) - (700 + 1900)) * 30\%$
 $= 6\,762$

Restated to F04 monetary unit:
 $= 6\,762 * 2\,000 / 1\,100$
 $= 12\,295$

Deferred taxation - F04 In F04 monetary unit:
 $= (\text{Restated carrying value} - \text{tax base}) * \text{tax rate}$
 $= ((31128 + 3840) - (1040 + 3600)) * 30\%$
 $= 9\,098$

Working 10

Note: All sales, purchases and operating expenses have been assumed to have occurred in the middle of the year.

Sales - F03 $= 8\,000 * 2\,000 / 800$
 $= 20\,000$

Sales - F04 $= 12\,560 * 2\,000 / 1\,500$
 $= 16\,747$

Working 11

Note: Only purchases is restated, not the entire cost of sales figures. Inventory is restated

Restated Cost of Sales - F03	Historic:	
	Opening inventory	= 1 300
	Purchases	= 6 100
	Closing inventory	= -1 900
	Restated:	
	Opening inventory	= 4 262
	Purchases	= 6 100 * 2 000 / 800
		<u>= 15 250</u>
	Closing inventory	= - 3 707
	Cost of sales therefore	<u>= 15 805</u>

Working 11 (Continued)

Restated Cost of Sales - F04	Historic:	
	Opening inventory	= 1 900
	Purchases	= 10 700
	Closing inventory	= -3 600
	Restated:	
	Opening inventory	= 3 707
	Purchases	= 10 700 * 2 000 / 1 500
		<u>= 14 267</u>
	Closing inventory	= - 3 840
	Cost of sales therefore	<u>= 14 134</u>

Working 12

$$\begin{aligned} \text{Operating costs - F03} &= 450 * 2\,000 / 800 \\ &= \underline{1\,125} \end{aligned}$$

$$\begin{aligned} \text{Operating costs - F04} &= 900 * 2\,000 / 1\,500 \\ &= \underline{1\,200} \end{aligned}$$

Working 13

$$\begin{aligned} \text{Depreciation - F03} &= (3500 * 2000 / 100) * 10\% \\ &= \underline{7\,000} \end{aligned}$$

$$\begin{aligned} \text{Depreciation - F04} &= (2900 * 2000 / 100) * 10\% + (1300 * 2000 / 1100) * 10\% \\ &= \underline{6\,036} \end{aligned}$$

Working 14

$$\begin{aligned} \text{Restated profit on sale:} & \\ \text{Restated proceeds} &= 700 * 2\,000 / 1\,100 \\ &= \underline{1\,272} \end{aligned}$$

$$\begin{aligned} \text{Restated NBV} &= (600 * 60\%) * 2\,000 / 100 \\ &= \underline{7\,200} \end{aligned}$$

$$\begin{aligned} \text{Restated (loss)} &= \underline{-5\,928} \end{aligned}$$

Working 15

Note: Finance charges are restated from when they arose. For the purposes of this example, they are assumed to have arisen in the middle of the year.

$$\begin{aligned} \text{Restated finance charges - F03} &= 405 * 2\,000 / 800 \\ &= \underline{1\,013} \end{aligned}$$

$$\begin{aligned} \text{Restated finance charges - F04} &= 420 * 2\,000 / 1\,500 \\ &= \underline{560} \end{aligned}$$

Working 16

Note: As is common practice, normal taxation is assumed to arise at the end of the year.

$$\begin{aligned}\text{Normal taxation - F03} &= -490 * 2\,000 / 1\,100 \\ &= \underline{-891}\end{aligned}$$

$$\text{Normal taxation - F04} = \underline{-806}$$

Working 17

$$\begin{aligned}\text{Deferred taxation - F03} &= 12\,295 - 13\,406 \\ &= \underline{-1\,111}\end{aligned}$$

$$\begin{aligned}\text{Deferred taxation - F04} &= 9\,098 - 12\,295 \\ &= \underline{-3\,197}\end{aligned}$$

The following CPI's apply for the example

Date	Index
01/01/F00	100
30/06/F00	150
31/12/F00	200
30/06/F01	280
31/12/F01	410
30/06/F02	550
31/12/F02	630
30/06/F03	800
31/12/F03	1100
30/06/F04	1500
31/12/F04	2000

Hyperinflation Questionnaire – Listed Companies

Population: 60 listed companies – see final page for details of companies
Responses: 35
Percent cover: 58.3%

Pre – IAS 29

- 1a. Prior to the identification of hyperinflation in November 1999, did you consider whether it would have been useful or necessary to attempt to disclose the impact of inflation on published financial information?

37%	Yes	63%	No
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Comments:

- Co. 4: “The financial information that was being reflected was out of touch with reality. There were distorted values of the resultant information in terms of financial performance, cash flow positions and the value of assets that were being reported.”

Impact of Inflation

- 2a. In what way do you feel that inflation has impacted the industry in which your organisation operates in relation to other industries in the economy?

Impact:

54%	More	37%	Same	0%	Less	9%	No Response
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- 2b. Do you feel that the disclosure practices of your organisation with respect to the impact of inflation, both before and after IAS 29, differ from other organisations in the **same** industry?

17%	Yes	71%	No	11%	No Response
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- 2c. Do you feel that your organisation has attempted to disclose more, less or the same amount of information with respect to the impact of inflation on the results of the organisation when compared to other organisations in **other industries**?

23%	More Disclosure	60%	Same Disclosure	14%	Less Disclosure	3%	No Response
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Usefulness of Inflationary Disclosures

- 3a. At the end of 1996, the year-on-year rate of inflation was 20%, and had increased to 60% by the end of 1999. However, during this period no inflationary disclosures were necessary. During this period, did your organisation include any **inflationary** disclosures and discussions in the annual report?

17%	Yes	83%	No
-----	-----	-----	----

- 3b. In your opinion, would inflationary disclosures in the annual report in the period prior to the implementation of IAS29 have been useful, given the milder rates of inflation, or were users able to make their own adjustments adequately?

11%	Definitely useful	86%	Not useful	3%	No Response
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Comments:

Co. 1: "Users were able to make their own adjustments."

Co. 2: "The full-scale impact of inflation had not been felt economy-wide and to disclose such information before users had been educated would have not yielded much as the extra cost would have been unjustifiable."

Management Use

- 4a. To what extent are inflation adjusted figures used for purposes of management decision making in your organisation?

0%	Extensive	14%	Moderate	23%	Slight	63%	Not at all
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Comments:

Co. 14: "IAS 29 inflation adjusted information is not used in any way in any part of our business."

Co. 18: "IAS 29 regarded as totally useless – other means of measuring 'real results' are used."

Co. 21: "Only accountants seem to understand the mechanics of IAS 29 reporting."

- 4b. Do IAS 29 inflation adjusted results have any impact on the dividend policy in your organisation?

14%	Yes	86%	No
-----	-----	-----	----

Comments:

Co. 7 "Dividend policy is a times cover the inflation adjusted profit."

Usefulness of IAS 29 in Zimbabwe

- 5a. Ignoring any related costs of producing the information, do you feel that inflation adjusted IAS 29 figures are useful to the users of financial statements?

31%	Not at all	34%	Slightly	29%	Moderately	3%	Certainly	3%	No Response
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Comments:

Co. 1: "Users generally don't understand the figures, and there is much that requires subjective decision. The accuracy is debatable because I believe two different people adjusting the same set of results will get two different answers."

- Co. 11: "I do not believe users make decisions, investment or otherwise, on the basis of inflation adjusted accounts / results – they relate entirely with the historical results."
- Co. 12: "Until income tax computations are based on IAS 29 figures, two yardsticks appear to be used, for a questionable end result."
- Co. 14: "They are not understood except at simple turnover level. They are not trusted because the process and the assumptions are considered 'wide open'."
- Co. 15: "Analysts are beginning to ask questions on that information, signifying the start of the process of understanding them."
- Co. 17: "Commentaries are normally based on historical accounts and little attention given to inflation adjusted results."
- Co. 18: "Not one user of accounts in my extensive experience regards (IAS 29) as useful."
- Co. 21: "Resistance is felt due to ignorance."

- 5b. Do you feel that the benefit in terms of improved information to users outweighs the cost of producing such information?



- 5c. Restated IAS 29 figures are not being used much in practice. Three of the more commonly cited reasons for this are:

- i. Users do not understand the numbers presented to them in the restated accounts and are not able to interpret their meaning.
- ii. There is a lack of intrinsic information content in the restated IAS 29 figures. Put differently, there is a school of thought that adjustments for changes in the general level of prices are not useful and meaningless.
- iii. Practical problems in the implementation of the standard make analysis of the numbers pointless. These problems range from questions over the appropriate indices to inconsistent methods and assumptions in the restatement process.

In your opinion, which of these problems i, ii or iii, detract the most from the use of IAS 29 restated figures?

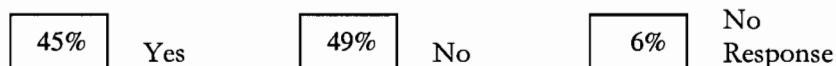
Rankings done per Freidman Ranking test – see statistics at back of this questionnaire.

Based on a weighted average, the rankings are as follows:

Detract most	i
	iii
Detract least	ii

Reason i is statistically different from reason ii at the 95% confidence level. In other words, we are 95% confident that the entire population would consider the lack of user understanding as a larger contributor to the lack of use of IAS 29 figures than any perceived lack of information content in the numbers. However, reason iii, the practical problems in implementation, is not statistically different from option i or ii, and we cannot therefore conclude the above ranking with 95% confidence.

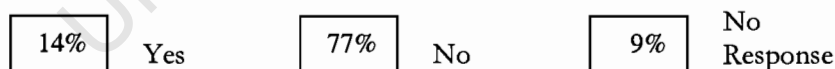
5d. Do you agree with reason ii stated above?



Comments:

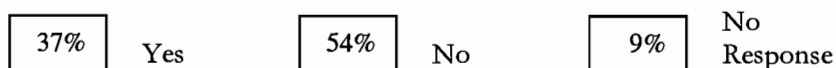
- Co. 1: "Users don't understand what the figures represent. Restating to USD's would also involve some assumptions which may also be debatable, but the end result would be more meaningful."
- Co. 3: "The CSO index is good enough provided everyone uses it. The major problem as I see it is the lack of understanding by the users of accounts."
- Co. 12: "To most shareholders (and directors) there is no overall acceptance, the subject is highly technical and restated figures seem to add to the confusion of the majority of the users of the information."
- Co. 17: "This is a technically difficult standard for the accountant himself – more so for the non-accountant!"
- Co. 21: "Historical cost accounts should always be permitted as a comparative as this is the only fixed base to compare to."
- Co. 26: "The indices used are irrelevant! Index composed of tomatoes and cabbages which are not bought using parallel market rates."

5e. Do you feel that commerce and industry are adequately educated and understand enough about IAS 29 and the restatement process for the restated figures to be meaningful?



Comments:

- Co. 5: "If IAS 29 is useless, then no amount of 'education' will work."
- Co. 11: "Corporate finance executives are resorting to using auditors for the preparation of adjusted accounts – even they do not understand them fully! Otherwise they would prepare them."
- 5f. Do you feel that the accounting profession is adequately educated and understand enough about IAS 29 and the restatement process for the restated figures to be meaningful?



Comments:

Co. 29: "The level of understanding is vague even among accountants."

- 5g. Do you feel that an education drive from the Institute of Chartered Accountants with respect to IAS 29 and its implications would result in a significant improvement in the usefulness of the restated figures to the various user groups?

37%	Yes	57%	No	6%	No Response
-----	-----	-----	----	----	----------------

Comments:

Co. 16: "The task would be too big to yield permanent results."

Co. 27: "Unlikely that the people you need to attend will."

Technical Problems

- 6a. Several practical and technical problems have been identified as hindering the usefulness of the restated IAS 29 figures. Please rank the following problems from those having the most impact on the usefulness of restated results to those having the least impact.

- i. Cost
- ii. Lack of understanding of the meaning of restated results.
- iii. Lack of information content in the restated results.
- iv. Inconsistent assumptions and methods in the process of restatement.
- v. Indices chosen are not appropriate or relevant.
- vi. The fiscus does not recognise inflation adjusted figures in the assessment of taxation.

Based on weighted averaging, the results are as follows:

Problem		
Largest impact	1	ii
	2	iv
	3	v
	4	i
	5	vi
Least impact	6	iii

Reason ii (understanding) is statistically different from all the other reasons, except reason iv (inconsistent assumptions and methods), at the 95% confidence level. Further, whilst not significant from iv at the 95% level, the difference between the two in the pair-wise comparisons is still very

significant – see statistical test at the back of this questionnaire. Note that, as in question 5c, understanding again ranked top, and was significantly at the 95% level to just about all the others. Further, intrinsic value (iii) again, as in 5c, ranked last.

- 6b. Do you feel that the indices produced by the Central Statistical Office and adopted for use in the restatement process are appropriate and relevant?

26% Yes

74% No

Comments:

Co. 2: "Reasonable guide to inflation, although there is evidence of political interference."

Co. 7: "The basket of goods ... no longer reflects spending patterns ... (and) there is the perception that the figures are sometimes "managed" for political reasons.

Co. 12: "You have to start somewhere, but many would prefer the comparisons to be with an international yardstick (USD)."

Co. 14: "I question the quality of the CSO index."

Co. 15: "There is a need to build an acceptable level of trust in the method of computation of these indices by the CSO."

Co. 16: "I do not think that the indices are materially defective."

Co. 18: "Political, vary greatly from industry to industry, and distorted by price controls."

- 6c. Would an analysis / breakdown of the monetary adjustment be a helpful disclosure with published inflation adjusted financial information?

54% Yes

40% No

6% No Response

Comments:

Co. 12: "Notes to the accounts are already unwieldy. More would be even worse."

Co. 14: "It would be a self-indulgence by a technician, of no value to a reader."

- 6d. It is common practice for companies to include the entire monetary adjustment arising from restatement in the Operating Activities section of the Cash Flow Statement. Do you feel that it would be useful to split the monetary adjustment into the section of the Cash flow Statement to which it relates, as determined from underlying monetary items from which it arose?

43% Yes

51% No

6% No Response

Comments:

Co. 30: "This is a cash flow from operating in this environment."

The Way Forward

- 7a. The Public Accountants and Auditors Board is now faced with essentially three options with respect to IAS 29. These options are:
- Continue in the current format, with IAS 29 non-compliant accounts being qualified.
 - Adopt the IAS 1 "Fair Presentation Override." However, this override requires the quantification of the financial impact of non-compliance to be disclosed. Essentially, therefore, the workings will still need to be performed, but merely disclosed in a note quantifying the financial impact of such non-compliance.
 - Remove IAS 29 from the set of standards 'adopted for use in Zimbabwe.' This will effectively result in Zimbabwe no longer being seen as an IAS compliant country and carries with it the related difficulties for foreign investors and analysts. There may be a time lag in regaining the confidence of investors should Zimbabwe return to being IAS compliant.

In your opinion, please rank these options in order of the most to least favourable course of action for the PAAB.

	Option
Most favourable	Indeterminate
	Indeterminate
Least favourable	Indeterminate

The means of the three options are all extremely close (see statistical tests at end of this questionnaire.) Accordingly, no ranking of any sort is determinable.

Comments:

- Co. 4: "IAS 29 is essential and there should be consensus on presentation of results. There should also be consensus of treatment of certain line items so that there is common understanding amongst preparers and users."
- Co. 5: "I do not subscribe to the "assumption" that investors only look at IAS compliance and even then question whether any sane investor would invest in a hyperinflationary economy in the first place given a choice!"
- Co. 7: "The inflation adjusted accounts have been revealing in some instances (where inflation adjusted losses have been recorded) and therefore ensures that companies do not pay capital as dividends."
- Co. 11: "Practicality is of essence, not financial convenience. Representations could be made to the world body for non-compliance with IAS 29 – and reason says the case would not be unreasonably thrown out. There are excellent grounds in our environment to discredit IAS 29."
- Co. 12: "If you accept (removing IAS 29 from the set of standards 'adopted for use in Zimbabwe') then international groups can decide what they want and at what cost and manpower effort, specifically to them."

- Co. 13: "I do not know where we get the idea that foreign investors are particularly concerned with IAS 29 considering the other problems the country faces. The foreign investors I have spoken to do not take notice of IAS 29 but work on equivalent exchange rates."
- Co. 15: "Hyperinflation in Zimbabwe is a reality we cannot afford to turn a blind eye to."
- Co. 16: "We must not damage the country's image from an investor / analyst's point of view for the sake of the future."
- Co. 17: "Zimbabwe still needs to maintain a positive image for its' professionalism in accounting. We cannot afford to be ruled off as non-IAS compliant."
- Co. 18: "...IAS 29 should be rejected because Zimbabwe's Institute jumped the gun ... IAS 29 does not comply with the Companies Act ... Zimbabwe's Institute has lost the respect of its members, and deservedly so."
- Co. 19: "We see no alternative other than to drop the standard."
- Co. 20: "It is important that the current format is maintained. Hyperinflation affects the way companies do business. These effects need to be reflected in the accounts. It is imperative that inflation accounts are the main accounts as long as the economy is hyperinflationary."
- Co. 28: "There is no value. Investors and analysts have the ability to make their own adjustments for inflation. I cannot believe that non-compliance with IAS 29 will damage our reputation at all."
- Co. 29: "We need to spend more time on education ... option ii is pointless given that it doesn't reduce the amount of work involved. Option iii is better because you are not sitting on the fence."
- 7b.** Please detail any others ways of accounting for the impact of inflation for the purposes of presenting interim or annual financial information to shareholders that in your opinion provide a more representative account of the transactions of your organisation. Should you mention accounting in a more stable foreign currency, please stipulate how the rate to be used for translation should be determined, for both the income statement and balance sheet.

Comments:

- Co. 2: "Restated US dollar accounts, using an average rate between the official and parallel."
- Co. 3: "The indices should be more representative and should seek to cover all goods – capital and otherwise."
- Co. 9: "Many companies already prepare annual budgets and management accounts in a stable currency therefore this would mean little extra work or cost and obviates the necessity of showing high gearing as a 'beneficial impact' on the performance of the enterprise."
- Co. 12: "These questions should have been put to us 12 months ago."
- Co. 18: "Foreign currency translation using trade-weighted exchange rate."
- Co. 25: "Use USD based reporting. Obviously the determination of rates can be arrived at by research from your technical team."
- Co. 26: "Use USD's – the ICAZ can come up with a monthly average blend rate for purposes of the conversion."

Co. 30: "... The current set-up where a few companies, notably the listed companies, are the sacrificial lambs is unacceptable. If it is deemed good accounting practice why should it be for only a few. Right now the situation is much more confusing and less uniform than before inflation accounting came by."

University of Cape Town

QUESTION 5c, QUESTIONNAIRE 1
FREIDMANS RANKING TEST (NON-PARAMETRIC)

Ranking by option (y) vs company (x)

Company Number	Option i	Option ii	Option iii
1	2	3	1
2	1	2	3
3	1	2	3
4	1	3	2
5	3	2	1
6	3	2	1
7	3	2	1
9	1	2	3
10	1	3	2
11	2	3	1
12	1	3	2
13	1	2	3
14	3	2	1
15	1	3	2
16	1	2	3
17	1	2	3
18	2	3	1
19	1	2	3
20	1	2	3
21	1	3	2
22	1	2	3
23	1	2	3
24	1	3	2
25	1	3	2
26	1	2	3
27	2	3	1
28	1	2	3
29	3	2	1
30	1	2	3
31	2	3	1
32	2	3	1
33	2	3	1
34	2	3	1
35	1	2	3
n = 34	52	83	69

STATISTICAL OUTPUT

Npar Tests

Descriptive statistics

	N	Mean	Std. Deviation	Minimum	Maximum
Option i	34	1.53	.75	1	3
Option ii	34	2.44	.50	2	3
Option iii	34	2.03	.90	1	3

Friedman Test

Ranks

	Mean Rank
Option i	1.53
Option ii	2.44
Option iii	2.00

Test Statistics^a

N	34
Chi-squared	14.176
df	2
Asymp. Sig.	.001

a. Friedman Test

M = Mean rank

Hypothesis to be tested:

$$H_0: M_i = M_{ii} = M_{iii}$$

Reject H_0 as Asymptotic significance (p) < α (error rate)

$$.001 (p) < 0.05 (\alpha)$$

Therefore rankings can be identified - perform pairwise comparisons.

PAIRWISE COMPARISONS

Hypothesis to be tested:

$$H_0: M_i = M_{ii}; M_i = M_{iii}; M_{ii} = M_{iii}$$

Computation of critical component:

$$\alpha = 0.05 \text{ (error rate)}$$

$$\begin{aligned}\alpha^1 &= \alpha / (k(k-1)) \\ &= 0.05 / 6 \\ &= \underline{0.0083}\end{aligned}$$

$$\text{Critical component} = z_{\alpha^1} (bk(k+1) / 6)^{1/2}$$

$$z_{\alpha^1} = 2.41 \text{ (per normal distribution tables)}$$

$$\underline{\text{Therefore critical component} = 19.873}$$

Pairwise Comparisons

	M_i	M_{ii}	M_{iii}
M_i		31	17
M_{ii}			14
M_{iii}			

Key

= Reject H_0
 No fill = Accept H_0

Conclusion:

At the 5% error level:

M_i is statistically different from M_{ii} .

M_i and M_{ii} are not statistically different from M_{iii} .

QUESTION 6a, QUESTIONNAIRE 1
FREIDMANS RANKING TEST (NON-PARAMETRIC)

Ranking by option (y) vs company (x)

Company Number	Option i	Option ii	Option iii	Option iv	Option v	Option vi
1	6	1	5	3	2	4
2	3	1	4	5	6	2
3	3	1	5	6	4	2
4	2	1	5	4	6	3
7	4	5	6	1	2	3
8	3	1	2	4	5	6
9	3	5	6	4	1	2
10	4	1	5	2	3	6
11	5	2	4	1	3	6
12	1	2	4	5	6	3
13	2	1	6	4	5	3
15	5	1	6	4	3	2
16	6	1	2	5	3	4
17	3	1	4	5	6	2
18	2	1	4	3	5	6
19	6	2	5	1	3	4
20	2	1	6	5	4	3
21	1	4	6	5	3	2
22	6	3	5	4	1	2
23	2	1	5	3	4	6
24	5	1	2	3	4	6
25	2	1	4	3	5	6
26	5	1	3	2	4	6
27	5	4	3	1	2	6
28	6	1	2	5	3	4
29	6	1	4	2	3	5
30	5	1	4	2	3	6
31	4	5	6	3	2	1
32	5	1	2	4	3	6
33	4	6	5	1	2	3
34	1	4	5	2	3	6
35	4	3	5	2	1	6
n = 32	121	65	140	104	110	132

STATISTICAL OUTPUT

Npar Tests

Descriptive statistics

	N	Mean	Std. Deviation	Minimum	Maximum
Option i	32	3.78	1.66	1	6
Option ii	32	2.03	1.58	1	6
Option iii	32	4.38	1.34	2	6
Option iv	32	3.25	1.48	1	6
Option v	32	3.44	1.48	1	6
Option vi	32	4.13	1.76	1	6

Friedman Test

Ranks

	Mean Rank (M)
Option i	3.78
Option ii	2.03
Option iii	4.38
Option iv	3.25
Option v	3.44
Option vi	4.13

Test Statistics^a

N	32
Chi-squared	31.625
df	5
Asymp. Sig.	.000

a. Friedman Test

M = Mean rank

Hypothesis to be tested:

$$H_0: M_i = M_{ii} = M_{iii} = M_{iv} = M_v = M_{vi}$$

Reject H_0 as Asymptotic significance $(p) < \alpha$ (error rate).

$$.000 (p) < .05 (\alpha)$$

Conclude that some ranking can be determined - perform pairwise comparisons.

PAIRWISE COMPARISONS

Hypothesis to be tested

$$H_0: M_j = M_k$$

Computation of critical component:

$$\alpha = 0.05$$

Where α = error rate

$$\begin{aligned}\alpha^1 &= \alpha / (k(k-1)) \\ &= 0.05 / 30 \\ &= 0.002\end{aligned}$$

Where k = number of options to be ranked

$$\text{Critical component} = z_{\alpha^1} (bk(k+1) / 6)^{1/2}$$

Where b = number of banks (respondents)

$$z_{\alpha^1} = 2.88 \text{ (per normal distribution tables)}$$

$$\text{Therefore critical component} = 43.104$$

Pairwise Comparisons

	M_i	M_{ii}	M_{iii}	M_{iv}	M_v	M_{vi}
M_i		56	19	17	11	11
M_{ii}			75	39	45	67
M_{iii}				36	30	8
M_{iv}					6	28
M_v						22
M_{vi}						

Key

 = Reject H_0

No fill = Accept H_0

Conclusion:

At the 5% error level:

M_{ii} is statistically different from M_i , M_{iii} , M_v and M_{vi} .

QUESTION 7a, QUESTIONNAIRE 1
FREIDMANS RANKING TEST (NON-PARAMETRIC)

Ranking by option (y) vs company (x)

Company Number	Option i	Option ii	Option iii
1	1	2	3
2	1	2	3
3	2	1	3
4	1	2	3
5	3	2	1
6	3	2	1
7	1	2	3
9	2	1	3
10	2	1	3
11	3	2	1
12	2	3	1
13	3	2	1
14	2	1	3
15	1	2	3
16	1	2	3
17	1	2	3
18	2	1	3
19	3	2	1
20	3	2	1
21	1	2	3
22	3	1	2
23	1	3	2
24	1	3	2
25	2	1	3
26	2	3	1
27	3	2	1
28	3	2	1
29	2	3	1
30	1	3	2
31	3	2	1
32	1	3	2
34	3	2	1
35	1	2	3
33	64	66	68

STATISTICAL OUTPUT

Npar Tests

Descriptive statistics

	N	Mean	Std. Deviation	Minimum	Maximum
Option i	33	1.94	0.86	1	3
Option ii	33	2.00	0.66	1	3
Option iii	33	2.06	0.93	1	3

Friedman Test

Ranks

	Mean Rank (M)
Option i	1.94
Option ii	2.00
Option iii	2.06

Test Statistics^a

N	33
Chi-squared	.242
df	2
Asymp. Sig.	.886

a. Friedman Test

M = Mean rank

Hypothesis to be tested:

$$H_0: M_i = M_{ii} = M_{iii}$$

Accept H_0 as Asymptotic significance (p) = 0.886 > 0.05 (error rate).

$$.886 (p) > .05 (\alpha)$$

Conclude that the three means are the same. Hence no ranking can be identified.

Population of Companies Selected

Selection Criteria

All companies included in the 2000/2001 Zimbabwe Stock Exchange "The Investors' and Financial Markets Handbook" have been included in the initial population. Certain companies have been excluded for the reasons mentioned below.

Companies in population:

- | | |
|---------------------------------------|--|
| 1 ABC Holdings Limited | 31 Mashonaland Holdings Limited |
| 2 African Distillers Limited | 32 Meikles Africa Limited |
| 3 Apex Corporation | 33 Murray and Roberts (Zimbabwe) Limited |
| 4 Ariston Holdings | 34 National Foods Holdings Limited |
| 5 Barclays Bank | 35 National Tyre Services Limited |
| 6 BICC CAFCA | 36 NMBZ Holdings Limited |
| 7 Bindura Nickel Corporation | 37 PG Industries (Zimbabwe) Limited |
| 8 Border Timbers | 38 Radar Holdings Limited |
| 9 British American Tobacco | 39 Randalls Holdings Limited |
| 10 CAPS Holdings Limited | 40 Rio Tinto Zimbabwe Limited |
| 11 CFI Holdings Limited | 41 Rainbow Tourism Group Limited |
| 12 Chemco Holdings Limited | 42 Schweppes Zimbabwe Limited |
| 13 Circle Cement Limited | 43 Seed Co |
| 14 Clan Holdings Limited | 44 Southern African Reinsurance Co. Ltd |
| 15 Colcom Holdings Limited | 45 TA Holdings Limited |
| 16 Commercial Bank of Zimbabwe | 46 Tanganda Tea Company Limited |
| 17 Dairiboard Zimbabwe Limited | 47 Tedco Limited |
| 18 David Whitehead Textiles Limited | 48 TH Zimbabwe Limited |
| 19 Delta Corporation Limited | 49 The Cotton Company of Zimbabwe Ltd. |
| 20 Dunlop Zimbabwe Limited | 50 Trans Zambezi Industries Ltd. |
| 21 Econet Wireless Holdings Limited | 51 Truworths Limited |
| 22 Edgars Stores Limited | 52 TSL Limited |
| 23 Falcon Gold Zimbabwe Limited | 53 Wankie Colliery Company Limited |
| 24 Gulliver Consolidated Limited | 54 Zimbabwe Alloys Limited |
| 25 Haddon and Sly Limited | 55 Zimbabwe Financial Holdings Limited |
| 26 Hippo Valley Estates | 56 Zimbabwe Newspapers (1980) Ltd. |
| 27 Hunyani Holdings Limited | 57 Zimbabwe Sun Limited |
| 28 Innscor Africa Limited | 58 Zimplow Limited |
| 29 Interfresh Limited | 59 Zimbabwe Reinsurance Company Limited |
| 30 Kingdom Financial Holdings Limited | 60 ZSR Corporation Limited |

Companies excluded from population:

- | Company |
|--|
| 1 Ashanti Goldfields Limited |
| 2 Astra Limited |
| 3 Commercial and Industrial Holdings Limited |
| 4 Macmed Holdings Limited |
| 5 Mhangura Copper Mines Limited |
| 6 Old Mutual plc |
| 7 Portland Holdings Limited |
| 8 Rothmans of Pall Mall |

Reason excluded

- | |
|------------------------|
| Not issue ZWD accounts |
| Unbundled |
| Delisted |
| Not issue ZWD accounts |
| Suspended |
| Not issue ZWD accounts |
| Taken over by PPC |
| Merged with BAT |

Companies that disclosed identity**Company**

#	Company Name
1	National Foods
2	Zim Alloys Ltd.
3	Southern African Reinsurance Co.
4	Commercial Bank of Zimbabwe
5	Radar Holdings
6	Border Timbers
7	NMB Bank
8	Apex corporation
9	Dunlop
10	TZI
11	CAPS
12	Haddon and Sly
13	National Tyre Service
14	Delta Corporation
15	Tedco

Analysts Questionnaire

Response Details:

Sample definition: Obtain at least one response from every Stockbroking and Asset Management firm listed in the 2000 / 2001 Zimbabwe Stock Exchange Handbook. Where the Stockbroking and Asset Management firm work together closely and use the same research department, only one response required. Where discussions with analysts have indicated other significant market players, these have also been included.

Sample response rate: 100%

1. To what extent do you use IAS 29 inflation adjusted information in your technical analyses of company performance?

0%	i. Extensively	35%	ii. Occasionally	65%	iii. Not at all
----	----------------	-----	------------------	-----	-----------------

2. If you answered 'iii. Not at all' to the above, please state reasons for non-use:

Quotable comments:

Barbican Asset Management:

"Unfortunately, securities are not priced on inflation adjusted information."

Barbican Asset Management:

"I feel that inflation adjusted information does not give the true financial status of a company considering that there are disparities from one financial report to another, for different companies with probably similar figures. There is no benchmark of the adjustment level."

Kingdom Stockbrokers (Pvt) Limited

"The market seems not to accept the concept fully and therefore a tendency to use historic accounting dominates in technical analysis."

Continental Securities Trading (Pvt) Limited

"Difficult to comprehend, easier to use historic accounts and then adjust for inflation."

Continental Securities Trading (Pvt) Limited:

"Historical cost figures are better than inflation adjusted figures."

Trust Corporate Securities (Pvt) Limited:

"Hard to perform trend analysis or make counter to counter comparisons ..."

Trust Corporate Securities (Pvt) Limited:

"... difficult to use inflation adjusted accounts because the base changes every year and interferes with comparison."

Bard Stockbrokers (Pvt) Limited:

"Not amenable to trend analysis."

Old Mutual Asset Management:

"Difficult to relate to."

Old Mutual Asset Management:

"i. Rest of the market uses historical accounts. ii. One index has limited usefulness to many companies in many sectors. iii. In practice, historic performance is simply measured against inflation for the year – eg. EPS growth vs inflation growth for the year. iv. The monetary adjustment figure, even though huge at times, is of no practical significance. It is of an accounting interest only."

Fleming Martin Edwards (Pvt) Limited:

“(Not at all) (d)ue to the difficulty of accurately forecasting earnings for companies.”

First Mutual Asset Management:

“(IAS 29 accounts) compare only two years – what about the other prior periods? It would be better to restate accounts for the previous five years as well!”

Mast Securities:

“i. Not yet understood by the many stakeholders. ii. Figures used to calculate the inflation index are wrong because of the operation of the parallel market (and price controls.) iii. Analysts lack the knowledge to interpret the results.”

Intermarket Asset Managers:

“The information provided does not make much sense and above all the companies themselves state that they do not place much emphasis on the inflation adjusted accounts.”

3. If you answered ‘i. Extensively’ or ‘ii. Occasionally’ to question 1. above, please outline the manner in which the information is used. Please be as specific as possible.

Quotable comments:

Barbican Asset Management:

“We occasionally look at inflation adjusted information for interest’s sake and not for investment decisions.”

NDH Equities (Pvt) Limited:

“Mainly for cross-sectional analysis when comparing counters in the same sector / business.”

Tetrad Securities:

“Difficult to forecast IAS 29 data as base constantly moving.”

Sagit Stockbrokers (Pvt) Limited:

“Mainly to get growth rates in real terms of comparative companies.”

Sagit Stockbrokers (Pvt) Limited:

“... However, all pricing and intrinsic valuations are based on historical cost accounts – largely as these are the accounts the individual investor understands.”

Temple Asset Management:

“IAS 29 revenues and cost figures are more useful for comparative purposes as the analyst doesn’t know the timing of historic figures and may therefore make incorrect assumptions. IAS 29 accounts also show if companies are paying dividends out of capital.”

UKI Securities (Pvt) Limited.

“Assessment of real growth in particularly revenue, cost and profit figures (ie income statement focus.)”

4. Have you attended any formal training courses, either within your firm, or externally, in order to assist you in learning, understanding and interpreting the IAS 29 General Price Level adjusted financial results?

29%

Yes

59%

No

12%

No response

Quotable comments:

Kingdom Stockbrokers (Pvt) Limited:

“...but I read that staff are personally using GAAP and the internet (to obtain an understanding of what the IAS 29 results mean.)”

Trust Corporate Securities (Pvt) Limited:

"I went to one session where I couldn't hear run by CIMA in 2000 – there were too many people and space was not sufficient."

UKI Securities (Pvt) Limited:

"I would very much appreciate any training course brought to my attention, even for a fee."

5. Do you feel that an education drive from the Institute of Chartered Accountants with respect to IAS 29 and its implications would result in a significant improvement in the usefulness of the restated figures to the various user groups?

68%	Yes	29%	No	3%	No response
-----	-----	-----	----	----	-------------

Quotable comments:

Kingdom Stockbrokers (Pvt) Limited:

"(Education) is very necessary for analysts ..."

Continental Securities Trading (Pvt) Limited:

"One needs to understand the basis and advantages of inflation adjusted accounts to make full use of them. To do this it is important that one understands how they are prepared."

Momentum Stockbrokers (Pvt) Limited:

"... to educate analysts on the use of IAS 29 as most have not even done it at tertiary level."

Trust Corporate Securities (Pvt) Limited:

"Too many assumptions involved in the process, no amount of education will help."

Trust Corporate Securities (Pvt) Limited:

"(An education drive is not useful) unless it can address the issue of ... comparability from year to year. USD based conversion of earnings may achieve the same result."

Bard Stockbrokers (Pvt) Limited:

"No, because (IAS 29 accounts are) not amenable to Discounted Cash Flow (analysis) or Price / Earnings valuation."

Bard Stockbrokers (Pvt) Limited:

"Hopefully ICAZ would prove its usefulness."

Temple Asset Management:

"Suspect the analyst community have not put enough effort into understanding the IAS (29 accounts) and would probably not make the effort. If you can get them to go then yes it would be useful in changing mindsets."

Old Mutual Asset Management:

"FY 2002 is the last year, or should be, (in terms of the three year roll over period of both historic and inflation adjusted information being disclosed) that historic accounts will be in use and it is therefore pertinent that all users be conversant with IAS 29."

Barnfords Stockbrokers (Pvt) Limited:

"The inflation adjusted figures are, in the main, meaningless. It is easier to do our own comparison of results vs inflation than to unravel the effects of IAS 29. For some companies it works, but mostly not."

Fleming Martin Edwards (Pvt) Limited:

"Further (education) drives would be good, however it probably would be difficult to alter the view of many of the users."

Interfin Asset Management:

"There appears to be wide-spread apathy in attempting to understand IAS 29. The education drive should have examples of where IAS 29 has been implemented before. I feel more has to be done to educate company management because they drive the process – their commentary and forecasts."

First Mutual Asset Management:

"People are set in their ways. A lot of company Financial Directors believe it is a total waste of time – Delta for one."

Mast Securities:

"This is required as a matter of urgency."

UKI Securities (Pvt) Limited:

"The reason why I hardly use the (IAS 29 accounts) is because of lack of knowledge and I do not have the laid down facts to explain to my clients and authorities. More education about the inflation adjusted accounts will go a long way for me."

6. Below is a list of reasons that have been cited as reasons for the non-use of IAS 29 inflation adjusted information. For each reason please indicate whether this reason has significant, moderate or no influence on the use of the inflation-adjusted information in company analyses. Significant influence would imply that the reason is a major contributor in reducing the use of the information, and vice-versa.

REASON	Significant	Moderate	Little or None	No Response
Non-comparability				
Too much flexibility is allowed in the assumptions and methodology used in the restatement process	73%	21%	6%	0%
Assumptions and methods used in preparing the Information are not disclosed	53%	35%	9%	3%
Only one year of comparative information is available because of constantly moving base	73%	21%	6%	0%
Lack of intrinsic value				
General Price Level adjusted information is not relevant because it does not portray the effects of inflation on individual companies	44%	38%	12%	6%
Redundancy				
All the information needed for analysis is already available elsewhere	26%	29%	29%	16%
Other				
Not yet enough trend data available for the IAS 29 General Purchasing Power results to be useful	47%	35%	15%	3%
Many analysts do not understand the information presented in the IAS 29 inflation accounts	55%	24%	18%	3%
Use of the Consumer Price Index as the basis of restatement	35%	38%	21%	6%

Quotable comments:

Trust Corporate Securities (Pvt) Limited:

"I have a problem with how the CPI is calculated in the first instance ..."

First Mutual Asset Management:

"What (other than the CPI) can you use (for restatement)?"

7. Would an analysis / breakdown of the monetary adjustment be a helpful disclosure with published inflation adjusted financial information?

79%	Yes	18%	No	3%	No response
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8. There has been little discussion in annual reports regarding the monetary adjustment. Do you feel that it is beneficial for management to provide a discussion of this number in order to fully appreciate its' impact on the accounts?

85%	Yes	12%	No	3%	No response
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9. Do you feel that inflation adjusted accounts are more useful for certain industries than others?

38%	Yes	59%	No	3%	No response
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If yes, please detail those industries on which you would consider inflation adjusted results to be more useful:

Quotable comments:

Kingdom Stockbrokers (Pvt) Limited

"Financial services industry, as they have the most monetary assets."

Sagit Stockbrokers (Pvt) Limited:

"Financial industry, because it's asset base is mainly cash / equivalent."

Barnfords Stockbrokers (Pvt) Limited:

"It varies more between companies than industries."

10. IAS 29 requires the inflation-adjusted results to form the primary accounts of the company. It is further recommended that the historic results not be disclosed. Do you think that it would be satisfactory for analysts to only have access to the inflation-adjusted results and not the historic results?

3%	Yes	97%	No	0%	No response
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Quotable comments:

Barnfords Stockbrokers (Pvt) Limited:

"Absolutely not!"

Thomas, First Mutual Asset Management:

"Definitely not!"

The Way Forward

11. The Public Accountants and Auditors Board is now faced with essentially three options with respect to IAS 29. These options are:
- Continue in the current format, with those companies that comply producing the inflation adjusted results. The accounts of non-compliant companies would continue to be qualified.
 - Adopt the IAS 1 "Fair Presentation Override." In other words, the inflation-adjusted information would merely be included as supplementary in a summarised form, quantifying the effect of non-compliance. The historic figures would form the primary accounts.
 - Remove IAS 29 from the set of standards 'adopted for use in Zimbabwe.' Accordingly companies would not be required to produce inflation-adjusted results. This will effectively result in Zimbabwe no longer being seen as an IAS compliant country and carries with it the related difficulties for foreign investors and analysts. There may be a time lag in regaining the confidence of investors should Zimbabwe return to being IAS compliant.

In your opinion, please rank these options in order of the most to least favourable course of action for the PAAB (Public Accountants and Auditors Board).

Option	
Most favourable	See Freidman statistical test
	See Freidman statistical test
Least favourable	See Freidman statistical test

Quotable comments:

Barbican Asset Management:

"Priority should be give to the historic accounts since these are the ones that are realised. The inflation adjusted results can then compliment these since these give the analyst a picture of the inflationary effects."

NDH Equities(Pvt) Limited:

"...those companies that do not produce inflation adjusted results should start doing so."

Kingdom Stockbrokers (Pvt) Limited:

"Historical accounts should go side by side the inflation adjusted accounts, such that an analyst can choose the set he / she would like to use. Most local analysts look at the historical accounts and compare those with the average rate of inflation."

Continental Securities Trading (Pvt) Limited

"Whilst I feel that general market wide education on the inflation adjusted accounts is necessary, I **STRONGLY** object to the non-disclosure of the historic accounts."

Continental Securities Trading (Pvt) Limited:

"I believe the current system is ideal as it gives analysts and the market in general the time to learn to use inflation adjusted accounts while still using the historical figures."

Continental Securities Trading (Pvt) Limited:

"More dabate is required so that all users of accounting information are fully appraised of the consequences of not using IAS 29 (accounts)."

Sagit Stockbrokers (Pvt) Limited:

"Option (iii) is completely out of the question."

Temple Asset Management::

"Would be a step backwards in terms of credibility to lose IAS compliant status. Both the historic and inflation adjusted accounts should be disclosed giving the investor the choice of which information to use."

Old Mutual Asset Management:

"Management of the companies being asked to comply with IAS 29 don't understand their usefulness either. There is need for them to be educated on this as well!"

Old Mutual Asset Management:

"In my opinion, inflation adjusted accounts should be supplementary rather than primary in nature. Valuation methods such as Free Cash Flows can be done successfully based on historical accounts. Adding fictitious figures (the monetary adjustment) to the accounts is futile. It is of academic interest only, a product of an academic exercise."

Fleming Martin Edwards (Pvt) Limited:

"The one comment about IAS 29, as I understand it, is that the original statement has not been updated since its conception (in 1980 - the standard was reformatted in 1994, but merely to bring the terminology into line with other standards and there were not other changes to the text), whereas most standards have continued to develop. It's a comments on its relevance."

First Mutual Asset Management:

"Hardly anyone in the industry is using the IAS 29 data."

First Mutual Asset Management:

"I think the market needs to be given a choice between the two sets of accounts. Produce both sets and let each analyst choose a set they are comfortable with."

Mast Securities:

"... but proper education is required ... because some interpretations are misleading."

UKI Securities (Pvt) Limited:

"The most crucial issue is to educate analysts, fund managers and company executives about the use of inflation adjusted accounts."

QUESTION 11, QUESTIONNAIRE 2
FREIDMANS RANKING TEST (NON-PARAMETRIC)

Ranking by option (y) vs company (x)

Analyst Number	Option i	Option ii	Option iii
M. Mpofu	2	1	3
N. Goche	2	1	3
M. Mahmed	2	1	3
N. Sagiya	2	1	3
F. Musakwa	3	1	2
K. Basira	2	1	3
C. Manyesu	3	1	2
F. Vengesai	2	1	3
P. Saziwa	2	1	3
B. Machekano	2	1	3
B. Matulila	1	2	3
T. Chimusimbe	1	2	3
P. Thomas	3	2	1
R. Mudala	2	1	3
S. Nzima	2	1	3
T. Chikamba	2	1	3
C. Masenda	3	1	2
B. Mugabe	2	1	3
S. Shumba	3	1	2
P. Brien	2	1	3
D. Masaiti	2	1	3
O. Lutz	2	1	3
R. Fourie	1	2	3
M. Mapondera	2	1	3
M. Mahwendepi	2	1	3
W. Ford	2	1	3
A. Chakurira	2	1	3
G. Molyneaux	3	2	1
N. Prior	3	2	1
A. Lopes Pinto	3	1	2
S. Asbury	3	1	2
C. Shenjere	1	2	3
N. Maferera	2	1	3
T. Magodora	2	1	3
n = 34	73	41	90

STATISTICAL OUTPUT

Npar Tests

Descriptive statistics

	N	Mean	Std. Deviation	Minimum	Maximum
Option i	34	2.15	0.61	1	3
Option ii	34	1.21	0.41	1	2
Option iii	34	2.65	0.65	1	3

Friedman Test

Ranks

	Mean Rank (M)
Option i	2.15
Option ii	1.21
Option iii	2.65

Test Statistics^a

N	34
Chi-squared	36.412
df	2
Asymp. Sig.	.000

a. Friedman Test

M = Mean rank

Hypothesis to be tested:

$$H_0: M_i = M_{ii} = M_{iii}$$

Reject H_0 as Asymptotic significance (p) < α (error rate)

$$.000 (p) < 0.05 (\alpha)$$

Therefore rankings can be identified - perform pairwise comparisons:

PAIRWISE COMPARISONS

Hypothesis to be tested:

$$H_0: M_i = M_{ii}; M_i = M_{iii}; M_{ii} = M_{iii}$$

Computation of critical component:

$$\alpha = 0.05 \text{ (error rate)}$$

$$\begin{aligned}\alpha^1 &= \alpha / (k(k-1)) \\ &= 0.05 / 6 \\ &= \underline{0.0083}\end{aligned}$$

$$\text{Critical component} = z_{\alpha^1} (bk(k+1) / 6)^{1/2}$$

$$z_{\alpha^1} = 2.41 \text{ (per normal distribution tables)}$$

$$\underline{\text{Therefore critical component} = 19.873}$$

Pairwise Comparisons

	M_i	M_{ii}	M_{iii}
M_i		32	17
M_{ii}			49
M_{iii}			

Key

 = Reject H_0

No fill = Accept H_0

Conclusion:

At the 5% error level:

M_{ii} is statistically different from M_i and M_{iii} .

M_i is not statistically different from M_{iii} .

Analysis by Industry

		Industry average	Agri-industry	Conglomerate	Financial	Food and leisure	Manuf. and retail	Mining
1a.	Yes	37%	29%	67%	33%	25%	18%	75%
	No	63%	71%	33%	67%	75%	82%	25%
2a.	More	54%	29%	0%	100%	50%	55%	75%
	Same	37%	57%	67%	0%	50%	36%	25%
	Less	0%	0%	0%	0%	0%	0%	0%
	No response	9%	14%	33%	0%	0%	9%	0%
2b.	Yes	17%	29%	67%	0%	25%	0%	0%
	No	71%	57%	33%	100%	75%	73%	100%
	No response	11%	14%	0%	0%	0%	27%	0%
2c.	More disclosure	23%	29%	33%	33%	0%	18%	25%
	Same disclosure	60%	29%	33%	67%	100%	64%	75%
	Less disclosure	14%	43%	33%	0%	0%	9%	0%
	No response	3%	0%	0%	0%	0%	9%	0%
3a.	Yes	17%	29%	33%	0%	0%	18%	25%
	No	83%	71%	67%	100%	100%	82%	75%
3b.	Yes, useful	11%	14%	0%	0%	0%	9%	50%
	No, not useful	86%	86%	100%	100%	100%	91%	50%
	No response	3%	0%	0%	0%	0%	0%	0%
4a.	Extensive	0%	0%	0%	0%	0%	0%	0%
	Moderate	14%	29%	0%	100%	0%	0%	0%
	Slight	23%	0%	0%	0%	25%	36%	25%
	Not at all	63%	71%	100%	0%	75%	64%	75%
4b.	Yes	14%	14%	0%	33%	50%	9%	0%
	No	86%	86%	100%	67%	50%	91%	100%
5a.	Not at all	31%	29%	67%	0%	25%	45%	0%
	Slightly	34%	43%	0%	67%	25%	18%	50%
	Moderately	29%	29%	33%	33%	50%	27%	25%
	Certainly	3%	0%	0%	0%	0%	0%	25%
	No response	3%	0%	0%	0%	0%	9%	0%

		Industry average	Agri-industry	Conglomerate	Financial	Food and leisure	Manuf. and retail	Mining
5b.	Definitely not	34%	29%	67%	0%	25%	36%	25%
	No	17%	14%	0%	33%	25%	18%	0%
	Possibly	26%	29%	33%	67%	50%	9%	25%
	Certainly	20%	29%	0%	0%	0%	27%	50%
	No response	3%	0%	0%	0%	0%	9%	0%
5d.	Yes	46%	71%	0%	33%	25%	45%	50%
	No	49%	14%	100%	67%	75%	45%	50%
	No response	6%	14%	0%	0%	0%	10%	0%
5e.	Yes	14%	14%	0%	33%	0%	10%	25%
	No	77%	71%	67%	67%	100%	82%	75%
	No response	9%	14%	33%	0%	0%	10%	0%
5f.	Yes	37%	29%	0%	67%	0%	45%	75%
	No	54%	57%	67%	33%	100%	45%	25%
	No response	9%	14%	33%	0%	0%	10%	0%
5g.	Yes	37%	29%	33%	67%	25%	36%	50%
	No	57%	57%	67%	33%	75%	55%	50%
	No response	6%	14%	0%	0%	0%	9%	0%
6b.	Yes	26%	14%	0%	33%	25%	27%	75%
	No	74%	86%	100%	67%	75%	73%	25%
6c.	Yes	54%	57%	67%	67%	50%	36%	75%
	No	40%	29%	33%	33%	50%	55%	25%
	No response	6%	14%	0%	0%	0%	9%	0%
6d.	Yes	43%	43%	33%	100%	50%	27%	50%
	No	51%	43%	67%	0%	50%	64%	50%
	No response	6%	14%	0%	0%	0%	9%	0%

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[illegible]

Analysis of Results of Questionnaire to Analysts

[illegible]