

IMPACT OF GOODWILL ON VALUE RELEVANCE IN LISTED OIL AND GAS FIRMS IN NIGERIA

ASINE, Emmanuel Oseiwe
Department of Business Administration
Kaduna State University, Kaduna

MUHAMMAD, Rahilahtu Ahmad
Department of Business Administration
Kaduna State University, Kaduna

and

ANGO, Yusha'u Ibrahim
Department of Business Administration
Kaduna State University, Kaduna

ABSTRACT

The study examines the impact of goodwill on value relevance in oil and gas firms in Nigeria. The period of the study is 2012 to 2019 and the study employed secondary sources of data collection with adoption of correlation research design and multiple regression analysis. Data for the study were extracted from the published annual audited reports and accounts of selected firms and website of Nigerian Stock Exchange. The study employed goodwill as proxy for goodwill and market value as proxy for value relevance. Multiple regression models while multicollinearity and Hausman specification tests were carried out to test the validity of the statistical inference which further necessitated the use of random effects from the fixed effects model. The finding reveals goodwill per share is negatively and significantly impacting market value per share in listed oil and gas firms. The study therefore recommends that currently, international accounting standards (IAS 38) do not capture internally generated goodwill. Standard setters should ensure that these categories of intangible assets are captured in the revised IAS as these can influence firms' share price.

Keywords: Intangible assets, Computer software, Intellectual properties, Market value, Value relevance.

INTRODUCTION

Financial managements are becoming information and innovation based. Goodwill components of firms are becoming crucial determinants of firms' present and future intensity just as firms' worth and development. Central to this perspective is the idea that firms differ in their resource positions and that such resource heterogeneity financials for performance variability across firms (Izedonme, Odeyile, & Kingsley, 2013). The goal of finance is to report an entity's economic activities in a manner that can serve the needs of diverse users and assist them in taking useful and informed decisions. The impact of such financial information can only be beneficial to the stakeholders if it is reliable and relevant. This implies that financial reports must be viewed as helpful in the event that it speaks to the financial substance of an association regarding its significance, unwavering quality, and equivalence (Barth, Beaver & Landsman, 2012).

Value relevance studies became necessary by the fact that listed firms use financial information as a medium of communication to the insiders and outsiders of a company. Value relevance literature deals with the usefulness of financial statement information in equity valuation, financial information assists the owner's, stakeholders and the general public to evaluate and know the performance of firms. Under this context value relevance of financial statement is the ability of financial information to be adequately used in decision process (Bologi 2014).

The idea of goodwill becomes possibly the most important factor when an organization hoping to gain another organization is happy to follow through on a cost essentially higher than the honest evaluation of the organization's net resources. The components or variables that make up the immaterial resource of goodwill are contained things, for example, an organization's decent notoriety, a strong (faithful) client or customer base, brand personality and acknowledgment, and particularly skilled workforce, and restrictive innovation. Opinions are divided regarding the recording of intangible assets (goodwill) during the globalization of accounting standards. The controversy is centered on capitalization, amortization, and impairment among others. Adoption of IFRS in Nigeria in 2012 have change the recognition measurement and reporting procedures for intangible assets of financial service firms in Nigeria. Intangible assets according to International Accounting Standard on Intangibles (IAS 38)

are identifiable non-monetary assets without physical substance, such as goodwill, computer software, patents, and copyrights.

Many studies were conducted on the relationship between goodwill with value relevance (stock prices or market share price, returns) in developed markets (e.g., Jake, Samuel & Watson, 2019; Min 2012; Oliviera, Rodrigues & Craig, 2010; Chalmers, Clinch & Godfrey, 2008; Istrate, 2013; Tsofigkas & Tsalavoutas, 2017), and emerging markets (Alali & Foote, 2012; Tharmila & Nimalathan, 2013). Similarly, a few value relevance studies have been conducted in Nigeria (e.g., Abubakar, 2014; Titilayo, 2011; Abiodun, 2017). These studies document evidence on the value relevance of goodwill in Nigeria, although they indicate conflicting results. However, the studies were conducted before the adoption of IFRS in Nigeria.

The main objective of the paper is to investigate the impact of goodwill on value relevance in oil and gas firms in Nigeria. In order to achieve this objective, the paper hypothesizes as follow:

H_{01} : Goodwill has no significant impact on value relevance of listed oil & gas firms in Nigeria.

The paper is divided into five sections. The first section covers the introduction, the second section is on literature review and the third section is on methodology adopted for the paper. The fourth and fifth are respectively on discussions on findings and conclusion and recommendation of the study.

LITERATURE REVIEW

Theoretical Foundation

The theoretical foundation for the study is the signal theory and agency theory because they best underpin the focus of the study.

Signaling Theory

The signal theory is a theory that assumes that financial figures are a communication tool for signaling trends in the market in as much as they are able to provide help to investors by making them appreciate the real value of firms. Spence (1973) developed the signaling theory to clarify the information asymmetry in the labour market. Value relevance is also based on the signal theory. Investors use the financial statements reported by firms to determine their performance. The investors particularly focus on the stock rates. Value relevance studies provide empirical evidence on financial numbers association with the predicted value of the securities market, where financial information is said to have value relevance if the financial information can be used to predict the company's market share price. Where market share prices become published

information signals are sent to investors in making investment decisions. Investors can also understand the factors affecting company's stock price and anticipate the trend of price changes, thus, making the necessary decisions to buy or not to take stock.

Agency Theory

The agency theory is a theory that explains the information gap between managers and investors. Managers have information that is not known to investors. The investors therefore rely on the information published on the financial reports of firms. Value relevance as related to the agency theory is stressed by Dontoh and Ronen (1993) who posit that the information asymmetry may guide to stock prices reaction on reported financial statements. The information asymmetry between investors and managers makes goodwill to be a tool for managers to communicate to investors.

Concept of Value Relevance

The concept of value relevance has been popular amongst academicians and researchers. According to Barth, Beaver and Landsman (2012), the main objective of studies in the field of value relevance is to increase the awareness level of the users of financial statements in terms of qualitative features of relevance and reliability of reflected financial information in the market value of the owner's equity. This is supported by Takacs (2012), who opined that value relevance is proof of the quality and usefulness of financial numbers for decision making process of investors; and its existence is usually by a positive correlation between market and book values.

The concept of value relevance is based on the four interpretations as offered by Francis and Schipper (1999). These interpretations include the fundamental analysis view, the prediction view, the information view and the measurement view. In their fundamental analysis interpretation, financial information is said to be value relevant if it trigger changes in the share price trends through its inherent value in a similar way and in the same direction as market prices. The prediction view on the other hand, considers financial information to be relevant if it has those values that are considered relevant for the upcoming value evaluation of firms and foreseeing the returns of the coming years. In the information and measurement views, financial information is relevant if there is a statistical association between financial information and prices or returns. The third and fourth interpretations inform the views of Ames (2013), Abubakar & Abubakar (2015), Kargin (2013), Barth, Beaver & Landsman (2012). These

scholars see value relevance as the statistical relationship between the financial information as disclosed in the financial statements and the market prices or returns of the firm's shares.

Concept of Goodwill

Goodwill is recorded as an [intangible asset](#) on the acquiring company's balance sheet under the long-term assets account. Under International Financial Reporting Standards (IFRS), companies are required to evaluate the value of goodwill on their financial statements at least once a year and record any impairment. Goodwill is considered an intangible (or non-current) asset because it is not a physical asset like buildings or equipment (Lucas, 2016).

According to IFRS 3, goodwill is the difference between the aggregate of the fair value of the consideration in a business combination at the acquisition date and the net amounts of the identifiable assets acquired and the liabilities assumed at the acquisition date. The changing economic environment of the 1980s resulted in a large merger wave, thereby increasing the amount of goodwill on company's audited financial statements. As a result, the goodwill gained increased attention with the growing importance of intangibles in company operating assets (Nnado & Ozouli, 2016). An opportunity to make goodwill a clearer accounting object is offered by the International Financial Reporting Standards 3 (IFRS3) on business combinations. Different from its predecessor International Accounting Standard (IAS) 22, IFRS3 evolves the disclosure of goodwill by requiring firms to supply a qualitative description of the factors in goodwill. This regime has been supported by the introduction of mandatory use of IFRS within the European Union. IFRS3 can be considered an attempt to open the "black box" of goodwill (Bugeja & Gallery, 2016)

The global financial crises also gave impetus to a series of merger and acquisition; and flight by companies to countries of profitable investment. This gave rise to business combinations and purchased goodwill. Recognizing these intangible assets in the books of oil and gas firms will increase the quality of financial reporting, promote transparency and deliver high quality annual report through comprehensive disclosure (Shehu, 2012).

Empirical Review

Jake, Samuel and Watson (2019) assessed the value relevance and reliability of reported goodwill and identifiable intangible assets. Using a sample of 500 firm-year observations, drawn from the top 528 UK listed firms for 2016 and 2017, this study employs a multivariate ordinary least squares regression to assess the value

relevance of goodwill impairment losses following the adoption of IFRS No. 3 “Business Combinations”. Empirical results revealed a significant negative association between reported goodwill impairment losses and market value, suggesting that these impairments are perceived by investors to reliably measure a decline in the value of goodwill and incorporated in their firm valuation assessments. The study provided evidence consistent with IASB's objectives in developing the impairment-only standard and reinforces the argument that, through IFRS 3, managers are more likely to use their financial discretion to convey privately held information about the underlying performance of the firms.

Min (2012) explored the value relevance of goodwill by Korean firms. The data was collected from a sample of Korean listed companies over the ten-year period of 2001-2010. Starting of Ohlson's (1995) model, the Correlation analysis and the Linear Multiple Regression has been applied. The study found that intangibles and traditional accounting measures as a whole were value relevant. However, the amortization and impairment charges of intangibles and, cash flows do not affect the market values of Korean companies, unlike other variables, which affect positively and substantially the market values. Also goodwill and book values are more associated with market values than intangible assets and earnings respectively. The study discovered that intangibles improve the value relevance of financial information.

Oliviera, Rodrigues and Craig (2010) assessed the value relevance of the amounts for identifiable intangible assets and goodwill reported in the financial statements of all non-finance companies listed on the main market of the Portuguese Stock Exchange from 1998 to 2008. The study used panel data to explore the impact on value relevance of Portugal's formal adoption of International Accounting Standards [IAS] and International Financial Reporting Standards [IFRS] in 2005. The study found they found evidence of an increase in value relevance of goodwill, and research and development expenditures. The evidence suggested that there was a positive effect on the value relevance of goodwill when the subclasses of identifiable intangible assets are considered.

Chalmers, Clinch and Godfrey (2008) compared the Australian GAAP and IFRS balances for goodwill reported in the annual reports. The results provided partial support for IFRS-measured goodwill being incrementally value relevant to that conveyed under Australian GAAP. They showed that the transition to IFRS did not affect the overall amounts of intangibles, even though it operated substitution effects in favor of goodwill. However, the total amounts of

intangible assets and goodwill together was value relevant under IFRS. They implied that financial markets can better integrate such contributions into share prices and returns, especially for companies with high intensity of intangible assets.

Sahut, Boulerne and Teulon (2011) examined the information content of intangible assets under IAS/IFRS when compared to Local GAAP for European listed companies. The paper employs multiple regression models for a sample of 1855 European listed firms in a six-year period, from 2002 to 2004 in Local GAAP and from 2005 to 2007 in IAS/IFRS to investigate the empirical relationships between market value of European firms and book value of their intangible assets. The findings reveal that the book value of other intangible assets (goodwill) of European listed firms is higher under IFRS than Local GAAP. Thus, identified intangible assets (goodwill) capitalized on European company balance sheets provide more value-relevant information for shareholders than unidentified intangible assets.

Istrate (2013) investigates whether intangible items recognized in financial statements are value relevant in UK context, and whether these items affect the value relevance of other accounting information. Empirical data were collected from a sample of UK listed companies, which included 1440 firm-year observations over 2005 to 2013. The research design was based on Ohlson (1995), in order to develop three models using multiple linear regression, also Correlation analysis and ANOVA were applied. The results indicated that intangible items as a whole explain a part of market values variability. While the results of each item alone showed that only intangible assets are value relevant, intangible assets affect positively the market values of UK companies, unlike goodwill and, amortization and impairment charges of intangibles, which are not value relevant. In addition, intangible items have incremental value relevance and affect positively and significantly the value relevance of accounting information, through improving their explanatory power. The results imply that UK accounting standard setter must facilitate capitalizing intangibles as assets, impose the recognition of intangible assets separately from goodwill, and encourage companies to report more information about intangibles.

Horton, Macve, and Serafeim (2015) examined market reaction and valuation of IFRS reconciliation adjustment from UK firms. Empirical data were collected from a sample of UK listed companies, which included 1000 firm-year observations over 2006 to 2014. The research design was based on Ohlson

(1995), in order to develop a model using multiple linear regression, also Correlation analysis was applied and found that reconciliation goodwill adjustment from UK GAAP to IFRS is value relevant. Similarly, Chalmers, Clinch, and Godfrey, (2008) examined the value relevance of intangible asset on IFRS adoption of Austria. The study reaffirmed that goodwill under Austria IFRS generally conveyed incremental useful information for investors.

Tsoligkas and Tsalavoutas, (2017) examined the value relevance of goodwill in the UK after IFRS mandatory implementation. The sample of the study is UK listed companies that publish consolidated financial statements and the technique used was simple linear regression. The study found that the capitalized portion of goodwill is significantly positively related to market values, suggesting that the market perceives these items as successful projects with future economic benefits. Goodwill expenses are significantly negatively related to market values under IFRS, supporting the proposition that they reflect no future economic benefits and thus they should be expensed.

Dinh, Kang, Morris and Schultze (2018) investigated how the adoption of IFRS in Australia has changed the accounting for goodwill and identifiable intangible assets (IIA). The study used expo facto research design and OLS for technique of analysis. Based on unique hand-collected data for 802 Australian firm-years during 2000–2010, the study found that expenses related to IIA are higher under IFRS, which is consistent with the view that IFRS accounting policies for IIA are stricter than those under Australian domestic accounting standards pre-2005 (AGAAP). The study results showed two effects that accompany higher IIA expenses under IFRS, which reduce a negative impact on earnings: lower goodwill expenses and a shift in recognition of IIA from those with finite useful life to IIA with indefinite useful life. The study suggested that market value analyses do not treat mechanical goodwill amortization as a genuine expense, but does treat as genuine expenses discretionary impairment charges, and more lenient IIA.

Jaafar (2011) examined accounting choice, firm life-cycle and the value relevance of intangible assets. The sample used in this study consists of 900 and 1,225 firm-years for the pre and post AIFRS period, respectively. Sample firms are classified into three life cycle stages; Growth, Mature and Decline, based on Anthony and Ramesh's (1992) classification method. Four regression models based on the Ohlson (1995) valuation model were used in the tests of value relevance. The findings indicated that during the pre-AIFRS period, goodwill is

regarded by the Australian market as value relevant. The results also suggested that although there is a significant difference in value relevance between Decline and Mature firms, the same effect is not present between Growth and Mature firms. Further, the results indicated that goodwill for Growth and Mature firms are value relevant but not for Decline firms.

METHODOLOGY AND VARIABLE MEASUREMENT

For this study correlation research design is used in testing the statistical relationship between and among variables which will allow making predictions regarding correlation. The population of the study comprises of the twelve (12) oil and gas firms in Nigeria. However, the selected sample size for the study consists of six (6) firms for the period of 2012 to 2019. The number was arrived at after applying filter to remove six firms. The choice of the base year is justified because 2012 marks the onset of preparation of International Financial Reporting Standard (IFRS) compliant financial statement in Nigeria. In view of the nature and type of the data adopted for the study, longitudinal unbalanced panel data from secondary sources was used only because it is a quantitative study with positive paradigm and data needed for analysis can be adequately extracted from the annual audited financial reports of the selected firms within the period of the study. Multiple linear regression was employed to examine the model of the study.

The control variable used in this study is book value per share. The book value per share is measured as the value of common equity divided by the number of ordinary shares (Aboody & Lev, 1998).

Multiple linear regression model is specified as follows:

$$MVS_{it} = \alpha + \beta_1 GPS_{it} + \beta_2 BVS_{it} + \varepsilon_{it}$$

MVS = market value per share

GPS = Goodwill per share, measured as the cost of goodwill divided by the number of ordinary shares.

BVS = Book value of equity per share, measured as the common equity divided by the number of ordinary shares.

ε_{it} is the error term used as surrogate for all other variables not included

α is the intercept or constant;

β_1 , to β_2 are the coefficient of the parameter estimates.

i = firm

t = time

Value Relevance

The dependent variable of this study is value relevance which will be proxy by market value per share (MVS). Market value per share of firm *i* in year *t*, 120 days after the accounting date. The 120-day window is necessary because of the weak form of the Nigerian capital market and for the need to ensure that all available information is reflected in the stock price. This implies that by 120 days, all available information must have been fully reflected in the stock price (Mackinlay, 1997).

RESULTS AND DISCUSSION

This section presents the empirical findings and analysis of the data. This is followed closely by interpretations and discussions.

Descriptive Statistics

Descriptive statistics are used to describe the basic features of the data in a study. They provide simple summaries about the sample and the measures. The descriptive statistics of criterion (dependent) variable and predictor (explanatory) variables using STATA are reported in Table 1. It shows the average indicators of variable computed from the financial statements and deviations from those averages.

Table 1: Descriptive Statistics

Variables	Mean	Std.			Skewness	Kurtosis	N
		Div	Min	Max			
MVS	55.6204	3.8012	0.5200	265.2800	1.2611	3.9053	48
GPS	1.5620	0.7114	0.0017	10.6850	2.3952	7.8251	48
BVS	16.3084	14.2352	0.0019	39.8079	0.2897	1.4319	48

Source: STATA Output of Descriptive Statistics, 2020

Table 1 presents the descriptive statistics for the dependent variable (Market Value per Share=MVS) and the independent variables (Goodwill per Share=GPS and Book Value per Share=BVS). From the table, the mean of Market Value per Share (MVS) is 55.6204, with standard deviation of 3.8012 implies that on average, for each share issued by the firms, the market price is N55.62 during the period of the study. There is also a wide dispersion of data from the mean because of the standard deviation over the mean. The result also shows a relatively impressive high share price of N265.28 and a minimum of N0.52 during the study period. The results of the skewness and kurtosis indicate that the data (MVS) is not normally distributed. The table also shows the mean and standard deviation of GPS to be 1.5620 and 0.7114 respectively while the minimum and maximum values stood at 0.0017 and 10.685 respectively. BVS returned a mean of 16.3084 with standard deviation of 14.2352, which show high volatility of the dataset.

Correlation Analysis

The correlation matrix is widely used in statistics to measure the degree of the relationship between linear related variables. For this study, the results of the correlation analysis are reported in table 2.

Table 2: Correlation Matrix

Variables	MVS	GPS	BVS
MVS	1.0000		
GPS	0.3672	1.0000	
BVS	0.4586	0.0648	1.0000

Source: STATA Output of Correlation Matrix, 2020

The correlation matrix shows that market value is positively correlated with the independent variables of the study. This implies that an increase in the market price per share, will result to an increase in the value of goodwill and book value of listed oil and gas firms in Nigerian, as the association is positive.

For validity of all statistical inferences to be drawn, multicollinearity and Hausman specification tests were conducted to robust the result. The variance inflation factor (VIF) and the tolerance values indicate absence of multicollinearity because the smallest tolerance value is 0.50 corresponding with the highest variance inflation factor of 1.99. Where the result obtained from the tolerance value and VIF was above the expected limits and inconsistent with the

rule of thumb of 1 and 10 respectively, then the problems of multicollinearity exist among the independent variables (Singh and Masuku, 2014). Similarly, the result obtained from the Hausman specification test conducted indicated, that the probability value is less than 0.05 which necessitated the use and subsequent interpretation of random effect model in favour of the fixed effect model

Regression Result

Table 3: Summary of Regression Result

Variables	Coefficient	z-statistics	z-sig.	VIF	TV
Constant	0.6399	0.07	0.943		
GPS	-4.7457	-3.58	0.000	1.99	0.502668
BVS	0.5058	0.58	0.563	1.57	0.637915
R ² Overall			0.8565		
Wald Chi2			1253.82		
Prob>Chi2			0.000		

Source: STATA Output of Regression Result, 2020

The results of multiple coefficient of determination (R²) in Table 3 indicates that the independent variables (Goodwill and Book Values) jointly explained about 85.65% of the total variation in the dependent variable (Market Value per Share) of listed oil and gas firms in Nigeria and other factors not captured in the model account for the remaining 14.35%. Similarly, the result of the Wald Chi2 (1253.82) shows that the model is fit at 1% significance (Prob>Chi2=0.0000) meaning that there is a 99.9% probability that the relationship among the variables of the study was not just due to mere chance.

Hypotheses Testing

Goodwill per share is negatively related with market value per share as indicated by the coefficient of -4.746 which is statistically significant at 1% level of significance (0.000). This indicates negative relationship between goodwill and market value. The significant negative relationship between goodwill and market value implies that increase in the value of goodwill decreases market price. This implies that for every 1 point increase in goodwill, market price per share decreases by 4.75 points. The result shows that recognizing goodwill on the statement of financial position of listed oil and gas firms in Nigeria drives the share price of the firms. The significant value relevance of goodwill is supported

by the findings of Min (2012) and Istrate (2013), who found significant relationship between goodwill and stock prices.

The coefficient of book value per share is 0.50577 which confirms their positive relationship with market value per share. The association is however not statistically significant as the p-significance values is 0.563 which is statistically not significant.

CONCLUSION AND RECOMMENDATION

The study examines the impact of goodwill on value relevance. Goodwill is negatively associated with share price. One probable way to explain the negative association of goodwill is to assume that the signaling effect such business combinations or acquisitions might have on the stock prices may only be for a short term. Subsequent amortization of goodwill might not have a substantial impact on the association with market price as information may have douse down with a systematic decrease in the amount of reported goodwill. The study therefore recommends that currently, international accounting standards (IAS 38) do not capture internally generated goodwill. Standard setters should ensure that these categories of intangible assets are captured in the revised IAS as these can influence firms' share price.

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