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The Effect of Mandatory International Financial Reporting Standards Reporting on Investors' Herding Practice: Evidence from Eu Equity Markets

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Abstract : The purpose of this study is to investigate whether the adoption of International Financial Reporting Standards (IFRS) encourages information-based trading and mitigates investors’ herding practice in emerging EU equity markets. Utilizing a modified non-linear model of cross-sectional absolute deviation (CSAD), we find that the hypothesis that mandatory IFRS adoption improves the information set of investors and reduces irrational investment behavior may in some cases be incorrect, and the reverse may be true. For instance, with regard to herding concerns, the new reporting benchmark has rather aggravated investors’ herding practice. However, we also find that mandatory IFRS adoption does not appear to be the only instigator of the observed herding practice; national institutional factors, particularly regulatory quality, political stability and control of corruption, also significantly contribute to investors’ herd formation around the new reporting regime. The findings would be of interest to academics, regulators and policymakers in performing a cost-benefit analysis of the so-called better reporting regime, as well as financial statement users who make decisions based on firms’ fundamental variables, treating them as significant indicators of future market movement.

Keywords : equity markets, herding, IFRS, CSAD
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