The Value Relevance of Intangible Assets: The Italian Adoption of International Accounting Standards (IAS/IFRS) by Morricone, Oriani, and Sobrero

Discussion

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What is value relevance?

• The reporting of information that helps to predict firm value conditional on other available information
• If the assets are valued correctly, this is essentially an econometric “prediction” problem, and can be analyzed as such.
• If not, a very difficult problem – what is value relevance when the value is “wrong”?
  – But this may not matter, since the investor wants to predict the market value, even if it is wrong in some fundamental sense
Another problem

• Investors are entitled to use any functional form they like to predict value from information received.

• We have no idea what they are using, but it is probably not linear.

• Better to try a more general form with power terms (in logs)
Two possible approaches

• Out of sample prediction comparisons using MSE (standard in the forecasting literature)
  – Could be done here by splitting samples
• Nested or non-nested hypothesis testing
  – Compare R-squares for two different sets of information
  – Build the best fitting model using one set of information and add additional information to see if it improves the fit
    • Do you have the data to do this?
Approach taken in this paper

• Two time periods: before and after intro of IAS (1996-2004;2005-2006)
  – Regress market value on the identical sets of variables and test if coefficients are the same

• Does this make sense?
  – Not if the valuation equation is changing over time (and note the absence of time dummies)
Discussion

• If equations for both periods have the same observables on the right hand side, differences say something about the left hand side, not about the value relevance of the RHS variables.

• E.g., book value coefficient falls from 1.3 to 0.5 and net income coeff. rises from 1 to 2.3, but presumably these were reported the same in both periods – so what does this mean?

• R&D and strategy
Minor questions

• Were time dummies included?
  – Change in number of years from Italian GAAP to IAS – implications for R-squares and changing functional form
  – Useful to look at partial R-squares after time effects removed
• Need to explain more precisely what the impairment test is.
• Were right hand side variables logged?
• Expensed R&D is not value relevant in Italy – see Hall and Oriani