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Extended Abstract

The Association between Accounting Information Quality, Overinvestment and Free Cash Flow

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Introduction

One of the challenging issues today is economic development. With regard to this subject, the measure of investment is very important; so that, decisions about investment and capital allocation are some of the key and essential decisions in the company. Hence, an entity for investing in various projects, should considers limits or measure of investment according to limited resources. In an inefficient market, information asymmetry and agency conflicts prevent optimal investment and desirable decisions. Overinvestment is an example of a non-optimal investment the main reason for it being the free cash flow of company. Hence, the main object of this research is related to overinvestment of free cash flow of companies. In order to solve or reduce this problem and according to the significant role of the quality of accounting information to reduce information asymmetry, in this study, the role of accounting information quality to reduce overinvestment was studied.

Research questions

According to theatrical model, the questions of this study was designed and given the purpose of the study and related literature (e.g., Yang, J. and Y. Jiang, 2008, Biddle, et al. 2009), the following hypotheses were presented and tested:

1. There is a meaningful relationship between free cash flow and

Overinvestment.

2. There is a meaningful relationship between accounting information quality and Overinvestment.

3. There is a stronger meaningful relationship between accounting information quality and Overinvestment in companies with high free cash flow compared with companies with low free cash flow.

Methods

Past event inquiry studies have been used in this research (using historical information). This research is of descriptive-correlative type. The multiple regression method is used to examine the hypotheses. All models are examined at the 0.05 level or better. All the examinations for the total independent variables are performed separately but the conclusions are represented totally in the table.

The variables being considered are: overinvestment as the dependent variable, accounting information quality as the independent variable, free cash flow as the Dummy Variable and the controls variables (e.g., size, Cash, Grow, Leverage and...).

In this research, sample size after limitation sample was determined in Tehran Stock Exchange and the data of 64 companies from years 1380 to 1389 were collected. Then the measure of overinvestment and accounting information quality of companies according to their free cash flow were determined. For statistical analysis and to test hypothesis, descriptive statistics (mean and standard deviation) and inferential statistics (simple and partial correlation, single and multiple linear regression and analysis of variance) were used.

Results

After testing hypothesis, this result was obtained that overinvestment in companies with higher accounting information quality occurs less. In addition, overinvestment in companies with high free cash flow compared to companies with low free cash flow occurs much more and the influence of decreasing through the quality of accounting information on these companies is considerably higher.

Discussion and conclusion

Results from testing the first hypothesis of the study show that there is a meaningful relationship between accounting information quality and Overinvestment. In that, accounting information quality is important factor in decries Overinvestment. In fact, useful information and use of accounting information with higher quality, decries information asymmetry and solves agency conflict problems and therefore improve an investment efficient.

Results from testing the second hypothesis of the study show that there is a stronger meaningful relationship between accounting information quality and Overinvestment in companies with high free cash flow compared with companies with low free cash flow. That is, free cash flow is an important factor in the creation of Overinvestment problems and causes problems as information asymmetry and agency are conflicting.

Keywords: 1. Investment, 2. Overinvestment, 3. Accounting information quality, 4. Free cash flow.