Impact of accrual reversals on corporate performance: evidence from emerging economy

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Abstract: This study examines the impact of accrual reversal on corporate performance. This study constructs a balanced panel data from the data for the period of 2009–2018. This study used a multivariate econometric model for examining the predictive power of accrual reversals on forecasting the firm performance. The study used the OLS estimation technique as the estimation model. Nevertheless, the relevant test results from random and fixed effect tests were opted using likelihood and Hausman test. The findings of the study revealed that accrual reversals have a significant positive effect on the company's earnings, which is considered beneficial for company growth in the emerging economy. The results help the stakeholders, managers, and investors in fully understanding the effect of accruals on firm performance and predicting the future performance of a firm. However, listed firms must increase the total accruals reversal to attract investment and enhance performance.

Keywords: accrual reversals; earnings before interest and tax; EBIT; ordinary least squares; OLS; firm performance; earning management.

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1 Introduction

One of the most crucial elements in the financial statement is the earnings, also referred to as net income. They are indicative of the degree to which the operating activities of the firm have been involved in the value-added events. According to the theoretical predictions, the present value of future earnings induces the firm's market value. In this way, the increased earnings imply an upsurge to the market value of firms, whereas the decrease in earnings represents a decline in the market value of firms (Lev, 1989). Moreover, earnings are a gadget tool for the stakeholder to gauge their wealth. Also, it reflects the financial health of a business. Hence, firms with better earnings attract investors, which is interpreted into the rise of the market price the firms' stock (Barth and Church, 1999). In contrast, managers and employees are fascinated by higher earnings because their intrinsic and extrinsic rewards are reliant upon the earnings (Degeorge et al., 1999).

Earning management (EM) is a phenomenon that is established by firm management to control the earnings. Executives and managers apply accounting techniques, also referred to as accrual EM, or real accounting activities, which is known as real earnings

management, to raise the revenues and profits. Moreover, the managers manipulate the firm earnings deliberately to present an excellent performance of the company. According to Ali and Zhang (2015), the CEOs manipulate the earnings at the start period of their tenure for building their and firms' reputation. Similarly, Rani et al. (2013) reported that managers, to get higher incentives, mostly manipulate the earnings. Accordingly, earnings management plays a crucial part in the financial accounting system of corporations. Also, the firms are involved in such practices for a smooth process and to diminish future uncertainties.

Empirical studies related to earnings management about the discretionary choice of manager for accounting accruals, the total-accruals are disintegrated into two major constituents of expected accruals (that is non-discretionary or normal) and the unexpected accruals (that is, the discretionary). Nevertheless, neither of the components are directly apparent, and hence, various proxies have been recommended by many research studies. Jones (1991) proposed a model for the distinction between unexpected and expected accruals. However, the accruals are reversed once the future economic benefits are realised. In general terms, the reversal of the accruals should not impose any influence over the subsequent earnings of the firms. However, in the real-world, accrual reversals affect the earnings of the firms.

The performance of a firm is measured through earnings, which includes book-based and market-based earnings that are also called the net income (EBIT) approach, while the latter includes the stock returns. According to Sloan and Ferrie (2011), in the book-based earnings, the accruals are more mean-reverting as compared to cash flows due to accrual reversals. Hence, the accruals are adversely associated through the future-earnings and the return on stocks. On the contrary, empirical studies such as Hirshleifer et al. (2009) presented a positive association. Empirical studies, for instance, Chan et al. (2008), Mather and Ramsay (2006), Hirshleifer et al. (2012), Dejong and Ling (2013), and many others, on the association for accruals and financial performance of corporations have been predominantly on developed economies of the United States and others.

Dechow et al. (1995), Sloan (1996), Bernard and Skinner (1996), Hribar and Collins (2002), Fairfield et al. (2003), Chan et al. (2004), Mather and Ramsay (2006), Hirshleifer et al. (2012), Dejong and Ling (2013), and many others examine the association in developed economies such as the USA, Australia, Canada, and others. However, an enormous gap in the literature prevails in the context of developing economies, particularly in Pakistan.

Nowadays, Pakistan is encountered with substantial levels of economic uncertainties, including energy crises, budget deficits, and macroeconomic volatilities – inflation has gotten to loftiest peak in the history of Pakistan. Therefore, the uncertainties have risen the levels of risks associated with the operations of businesses operating in Pakistan. Hence, an empirical investigation on the performance of Pakistani firms concerning accrual reversals is appropriate and in the interest of investors, managers, policymakers, and academics. The central objective of this paper is an empirical examination of the relationship between accrual reversals and the financial-performances.

This paper will examine the association in the Pakistani context, considered as the emerging economy as per the report of the Financial Times Stock Exchange in September 2015. Listed firms in Pakistan started attracting foreign investors after consistent and improved corporate performance over the period. The behaviour of listed firms in Pakistan is different from developed economies in practices of corporate governance and EM decisions (Baloch and Hassan, 2016). After the event of the Global Financial Crisis

(GFC-2008), listed firms in Pakistan ere less suffered compared to developed stock markets. Due to the great potential to absorb investment and high returns and volatile nature, investors are more attracted to invest in developing economies rather than matured developed countries. Therefore, to portray a better and clear picture for the stakeholder, to understand the growth of companies and investment purposes, this study will explore the role of accrual reversals in the enhancement of firm performance.

Different studies used various approaches, such as balance sheet methods that have the probability of error (Hribar and Collins, 2002). The findings of the study must be revisited by using a cash flow approach because the balance sheet approach may produce an error. The error can be minimised in the estimation procedure by using a cash flow approach that helps us to get unbiased results. A minimal number of studies examined the association. Listed firms in developing countries are more likely to retain the investment for the longer term for growth. Therefore, the main objective of the study is to examine the impact of the reversals of total accruals on earnings in non-financial companies listed on the Pakistani stock exchange. This study will highlight the relationship that helps the investors to make investment decisions.

2 Literature review and hypothesis development

A considerable number of empirical studies are present on the accruals. The majority of the empirical studies, for instance, Dechow et al. (1995), Sloan (1996), and many others have measured the accruals using the cash flow approach where they have taken the variance between EBIT and cash flows from operating activities. Dechow et al. (1995) performed empirical analysis for various circumstances where accruals are predicted to encourage the financial performance of firms. Hence, the author identified that accrual possessed potentials in improving the performance and was reflected by the growth in the stock returns. Similarly, Healy and Goodnow (1998) presented that managers use the discretionary accruals for managing the calculations about the bonus. Bartov et al. (2000) recommended that six models are used for the assessment of the discretionary accruals. This paper includes the models adopted from previous studies such as 'Healy (1985) model, DeAngelo (1986) model, Jones (1991) model, the modified Jones models presented by Dechow et al. (1995), industry models projected by Dechow et al. (1995), and cross-sectional Jones model posited by DeFond and Jiambalvo (1994)'. Moreover, the models above have decomposed the accruals into two broad categories of discretionary and non-discretionary modules. Accrual reversals are calculated through variance between current and previous period accruals.

To avoid multiple taxations and to smooth the procedure over time, corporations make difficult decisions regarding EM by using accrual reversals. In this case, accrual-based transactions are recorded in the current accounting practice in the developing economies. When a transaction takes place, then it is recorded in the next period. There are two approaches to calculate the accrual reversals, which includes balance sheet and cash flow approach. The effect of the transaction is more appropriate when it is recorded in the current period rather than a future period.

Firms can perform their operations and transaction consistently, and the lack of cash has no impact on the company's operations, which is the benefit of accrual business. The business can be run smoothly with the help of the accruals-based system. In the 21st century, the world became a global village, and trade increases across the border

immensely. Firms prefer accrual-based system whenever benefits and economic cost is associated. Usually, accruals must not have any impact on earnings, but in reality, it affects the earning "as a difference exists between the predicted and realized economic benefits" due to the estimation error in the estimation methods. Previous studies reported the "consequential reversals of inventory accruals with high frequency", which has an impact on future earnings and demonstrated by inventory write down (Allen et al., 2013).

Sometimes, long-term accrual reversals increase the earning of the firm and contribute positively, while sometimes it decreases the earning of the firm in an emerging market, where the focus of the listed firms in more on the long-term decision, are more interested in accrual reversals. Baloch and Hassan (2016) argued that "accruals are negatively linked with the persistence of earning rather than the cash flow." Previous studies also reported that accrual reversals are also reflected in the faster means of reverting. Allen et al. (2013) also specified the extreme accrual reversals, and their role is crucial. These accrual reversals contribute positively to the stock return (Hirshleifer et al., 2009; Baloch, 2015) or negatively (Sloan, 1996).

Fairfield et al. (2003) examined the accrued earnings and growth. The study sample consists of the data for firms listed at Standard and Poor's (S&P) covering 1964 to 1993. The data of 32,961 firm-years were collected from Compustat Industrial and Merged Industrial Researcher database. However, the data on share and stock prices were acquired from the Center for Research in Securities Prices (CRSP). The explanatory variables incorporated in the econometric study model are return-on-assets, accruals, growth in the net operating assets, cash flows, and growth in long-term net operating assets. The findings of the study show that accruals play a vital role in the growth of net operating assets and profitability. Further, the study shows that accruals and growth in long-term net-operating assets take antagonistic relationships through one-year future return-on-assets when controlled for current profitability. Thus, the findings of the study are supported by conventional accounting and retreating marginal-returns on investment.

Scott et al. (2003) examined the use of cash and accrual-accounting. They examined the cash and accrual accounting as it shows the dichotomy of financial reporting, and the transition from cash to accrual was a key adjustment in financial management. The study period spanned over the years from 1857 to 1975. The findings of the study show that the reintroduction of accrual-accounting provides insight into the development of financial reporting in both: public as well as private divisions in Australia.

Chan et al. (2004) analysed the consequence of accruals on prospect earnings. They furthermore examined accrual reversals' pattern. Study-sample consisted of data for 2,914 companies registered at NYSE/AMEX/NASDAQ for a period covering 1963 to 1996. The findings of the study show a negative effect of accruals on future earnings. It also shows that organisations having high market-to-book ratios, price-earnings ratios, and more substantial accruals experience the high negative consequence of accruals over their upcoming earnings. Thus, the study concludes the significant and adverse outcome of accruals for prospect earnings.

Francis and Wang (2008) studied accruals and cash flows. In particular, they revisited the studies that have concluded the less perseverance of accruals than cash flows. The sample of the study consists of data of all firms that are on COMPUSTAT for a period covering 1962 to 2001. They developed a model that captured current-period transactions. They measured income by operating income after depreciation and amortisation, and accruals by a change in operating working capital accruals adjusted for depreciation. The findings of the study show that the transactions that do not belong to

the current period lead to a downward bias of accruals. Further, they show that non-current transactions result in an upward bias of cash flows. Therefore, the study concludes that accruals are not less persistent than cash flows.

Pae et al. (2005) investigated the effect of operating cash flows and reversals of accruals following Jones (1991). The study sample is constructed using data of all firms and stock returns on COMPUSTAT and CRSP, respectively, for the period from 1990 to 2002. The findings of the study show that lagged accruals do not have any significant power in explaining the model of Jones, but the cash flows do have. It also shows that accruals that are not expected have an informative effect concerning stock returns. The study concludes that the market does not fully understand the implications of accruals at the commencement of the return period.

Baloch (2015) performed an empirical analysis to identify the presence of accrual anomalies in the context of the Pakistan Stock Exchange (PSX). The variables included in the econometric model of the study comprised of 'cash flows from operations, long-term liability, earnings before interest and tax (EBIT), and the market value of common stocks'. However, the stock returns are introduced as the dependent variable of the study. The findings of the study showed that the accruals have the predicting power for the stock returns of the firms in Pakistan. The findings showed that the stock returns and the accruals are positively associated when the cash flow approach is implemented to gauge the accruals. However, this is contradicted by the accrual anomaly. The study concluded that the accrual anomalies do not appear to be present in the Karachi Stock Exchange.

Baloch and Hassan (2016) observed the effect of total accruals on financial-performance of firms registered in Pakistan. Sample encompassed 100 non-financial companies quoted at PSX covering from 2002–2013. The authors measured the financial performance of firms through EBIT, which is used as a dependent variable in the econometric model. Independent variable comprised of reversal of total accruals for the current and previous period. However, the authors have used three-control variables, namely firm-size, growth, as well as capital structure. Findings showed a positive association between reversals of total accruals and performance of companies. Similar effects on the performance of corporations were evidenced by both current and previous period accrual reversals. After an in-depth analysis of empirical literature on the relationship of accruals and the performance of firms across various countries around the world, this study hypothesised the relationship as reported below:

H_0 Accrual reversals have a significant influence on the financial performance of corporations in Pakistan.

H_1 Accrual reversals have no significant influence on the financial performance of corporations in Pakistan.

3 Methodology

3.1 Data and variables of the study

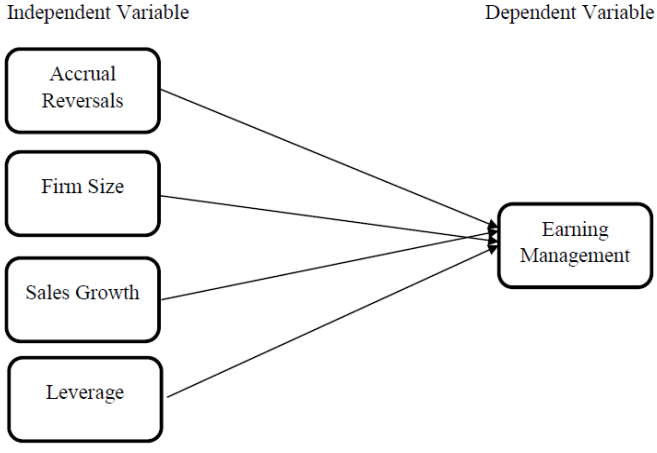
This study considers the top 100 non-financial listed firms in PSX based on market capitalisation due to the availability of data. The listed firms of the KSE-100 index were initially selected, and after the dropping of some firms due to the unavailability of data, the firms on the base of significant market capital are chosen from 2009 to 2018.

This study used various dependent variable and independent variables that include earnings 'EBITs, cash flows from operations, long-term liability, total assets, and market value of common equity'. The source of data collection is from the annual reports and financial statements available for each listed firm. Earnings are measured as the EBIT given in the financial report of the firm, long-term liabilities and cash flow from operations are divided by total assets that are also used by Baloch (2015) to reduce the variation among the variables. Firm size is measured as the natural log of the market value of equity, firm growth measured as the ratio of the book value of equity to the market value of equity, and leverage measured as debt to equity ratio is used as the control variables of the study.

3.2 Framework of the study

The central aim in current research-work encompasses on analysing the influence of accrual reversals on the financial performance of firms. Therefore, the study developed the following empirical framework to scrutinise the impact of accrual reversals on firm-performance (Figure 1).

Figure 1 Conceptual framework of the study



3.3 Model of the study

In this study, the researcher has attempted an inspecting effect of accrual reversals on the financial performance of businesses. To achieve the objective, the survey following Baloch and Hassan (2016) has developed a multivariate model, as shown below in equation (1).

$$Earning_{it} = \beta_0 + \beta_1 \Delta ACC_{it} + \beta_2 SIZ_{it} + \beta_3 G_{it} + \beta_3 Lev_{it} + f_i + f_t + \varepsilon_{it} \quad (1)$$

where *Earning* is the dependent variable and is measured employing *EBIT*. ΔACC_{it} is the current period of the accrual reversals for the firm at the time *t*. *SIZ* denotes the firm size. *G* symbolises the growth. f_i and f_t presents the firm-fixed and year-fixed effects while ε_{it} is the error term.

3.4 Estimation approach

The process of finding an estimate is called the estimation method. This estimate is a value that is used for a purpose. In this study, the researcher first used various normality tests to examine the normality of the data and used balanced panel data. This study has utilised the ordinary least squares (OLS) technique to estimate the empirical model of research-work. OLS, also called linear regression, is an estimation method that minimises the sum of squared differences among predicted and observed values.

3.5 Description of the variables

For analysing the effect of accrual reversals on financial-performance for companies, this paper developed a multivariate model, as shown in equation (1). It consists of a dependent variable (firm performance), an explanatory variable (accrual reversals), and control variables (firm size and growth in sales and leverage). Table 1 contains the construction and measurement of the study. The dependent variable of the study is firm performance. Firm performance is considered as a dependent variable, which is also called firm financial stability or *EBIT* measures financial health. *EBIT* is calculated as revenue subtract expenses, excluding interest and tax. While the independent variable of the study is accrual reversals. Accrual is calculated as *EBIT* minus cash flows from operations. Some of the previous studies have utilised a balance sheet approach that was more difficult and had some errors in estimation. Therefore, the researcher has utilised the income approach to measure the accrual, as shown below:

$$Accrual = EBIT - Cash\ flow\ from\ operations$$

Table 1 Variables of the study

Variables	*Symbol*	*Measurement*
Earning	*EBIT*	Earnings before interest and taxation by total assets
Accrual	*ACC*	EBIT minus cash flow from operations
Accrual reversals	ΔACC	Change in accruals that is, the difference between current-period and previous-period accruals
Firm size	*SIZ*	Natural logarithm of total assets
Growth	*G*	Rate of growth in sales
Leverage	*Lev*	Debt to equity ratio

Moreover, the change in accrual represents accrual reversals. It is the difference between current-period and previous-period accruals. It is measured as below:

$$Accrual\ reversals\ (\Delta ACC) = Acc_t - ACC_{t-1}$$

Many empirical studies use these measurements. However, the researcher has measured accrual and accrual reversals following empirical studies such as Collins et al. (2003) and Baloch and Hassan (2016).

The control variables for the study are the firm size and sales growth that helps to control their particular effect in the model. Firm size is calculated by taking the natural logarithm of the total assets. The natural logarithm is used to linearise and smoothen the

data while sales growth measures the growth in sales of a firm in time *t*. Leverage is calculated as debt to equity ratio (Khan et al., 2019).

4 Results and discussion

4.1 Descriptive statistics

Table 2 depicted the descriptive summary for variables employed in the econometric model of the research-work. The first column shows statistical measures, and subsequent columns present the variable's names.

Table 2 Descriptive statistics

	EBIT	*ΔACC*	*SIZ*	*G*	*Lev*
Mean-value	0.0994	–0.0006	22.690	0.7477	0.0356
Median-value	0.0998	0.0034	22.579	0.0952	0.0110
Maximum-value	0.6114	0.6346	25.710	261.28	0.8100
Minimum-value	–0.6467	–0.5961	19.003	–0.9834	0.5600
Std. deviation	0.1283	0.1550	1.2859	11.722	0.0610

Table 2 depicted that EBIT has a mean value of 0.0094 and a median value of 0.0998. It shows a standard deviation value of 0.1283, which implies that 12.83% of the data is spread around the mean. Also, it shows the maximum and minimum values of 0.6114 and –0.6467, respectively. ΔACC has a mean value of –0.0006 and a median value of 0.0034. It shows a standard deviation value of 0.1550, which implies that 15.50% of the data is spread around the mean. It also shows the maximum and minimum values of 0.6346 and –0.5961, respectively. Firm size has a mean value of 22.690 and a median value of 22.579. It shows a standard deviation value of 1.2859, which implies that 128.59% of the data is spread around the mean. Also, it shows the maximum and minimum values of 25.710 and 19.003, respectively. Growth has a mean value of 0.7477 and a median value of 0.0952. It shows a standard deviation value of 11.772, which implies that 1,172.2% of the data is spread around the mean. Also, it shows the maximum and minimum values of 261.28 and –0.9834, respectively.

4.2 Correlation matrix

Table 3 depicted the linear association among the variables. The coefficients present the strength of association, and sign from coefficient determines the direction for the relationship among variables (Saif et al., 2020). Gujarati and Porter (2003) state that multi-collinearity issues arise in the presence of a coefficient above 0.80. Therefore, considering below values in Table 3, the researcher becomes confident about the non-existence of multi-collinearity issues amongst variables incorporated in the research.

Table 3 Correlation matrix

	EBIT	*ΔACC*	*SIZ*	*G*	*Lev*
EBIT	1.0000				
Δ*ACC*	0.1749	1.0000			
SIZ	0.1483	0.0255	1.0000		
G	0.0088	0.0735	–0.1083	1.0000	
Lev	–0.2879	–0.0755	–0.0305	–0.0081	1.000

From Table 3, we can see that EBIT has positive coefficients equal to 0.1749, 0.1483, and 0.0088 with Δ*ACC*, *SIZ* and *Growth*, respectively. It shows the positive association between the variables. Δ*ACC* has positive coefficients of 0.0255 and 0.0735 with, *SIZ*, and *Growth*, respectively. It shows that positive association prevails among the variables. *SIZ* has a negative coefficient of 0.1083 with *Growth*. It implies that a negative association exists between *Size* and *Growth*.

4.3 Regression analysis

The researcher has utilised the OLS estimation method to analyse the effect of independent-variables (that is, accrual reversals) on dependent-variable (that is, financial-performance). However, likelihood and Hausman tests were implied to opt appropriate test results for the empirical estimation of the study. Table 4 presents the results from the Hausman test. It presents the cross-section random with p-value > 0.05. It implies the acceptance of the null hypothesis. Thus, the relevant test results for the study is a random effect.

Table 4 Hausman test

Test summary	*Chi-sq. statistic*	*Chi-sq. d.f.*	*Prob.*
Cross-section random	0.3386	3	0.9526

Table 4 presents outcomes for a random effect test of regression analysis in the study to examine the influence of accrual reversals for financial-performance of firms, which is measured by EBIT. Results present coefficients along with the p-values. It also includes the value of R-squared, adjusted R-squared, and F-statistics along with the prob. values.

The results from Table 5 depicted that there is heteroscedasticity in the model of the study. The value of the probability value of the test is significant, which rejects the null hypothesis of the study, which confirms the heteroscedasticity in the model.

Table 5 Likelihood ratio test

LR test	LR chi2(99) = 1,126.66
(Assumption: homo nested in hetero)	Prob. > chi2 = 0.000

From Table 6, the researcher states that Δ*ACC* takes a positive value equal to 0.1404 with a probability value of 0.0000. It shows the statistically significant and positive influence on EBIT. A single unit increase in Δ*ACC* increases EBIT by 0.1404 units on average. This positive effect of accrual reversals on earnings implies that cash flow decreases with an increase in accrual reversals. However, earnings increase as it consists of cash flows and accruals. Thus, a positive change in accruals increases the earnings of firms.

Table 6 Multivariate regression analysis

Variable	*Coefficient*	*Std. error*	*t-statistic*	*Prob.*
C	–0.2657	0.2037	–1.3044	0.1928
Δ*ACC*	0.1404	0.0219	6.3858	0.0000
SIZ	0.0161	0.0089	2.6283	0.0338
G	–7.27E–05	0.0003	–0.2388	0.8114
Lev	–0.81	0.1711	–7.36	0.0000
Effects specification				
R-squared		0.6909		
Adjusted R-squared		0.6549		
F-statistic		19.2178		
Prob. value (F-statistic)		0.0000		

Moreover, the previous reversals have a significant impact on future earnings, so the researcher concludes that previous reversals can predict future earnings. *SIZ* as a positive coefficient of 0.0161, having a probability value equal to 0.0338. It shows the significant and positive influence of firm-size for EBIT. A unit increase in firm size increases EBIT by 0.0161 units on average. Growth takes a negative coefficient equivalent to 0.0000727, with the value equal to 0.08144. It shows the insignificant effect of growth for EBIT. Findings from current research-work remain reliable per empirical works, for instance, see Collins et al. (2003), Allen et al. (2013) and Baloch and Hassan (2016).

The R-squared, which is alternately known as the coefficient of determination, has shown a value of 0.6909, which determines that almost 69% of a variant in dependent-variable (earnings) is elucidated through explanatory-variables used. Moreover, adjusted R-squared has shown a value of 0.6549, which means that if one another relevant explanatory variable is incorporated in the econometric model of the study, the R-squared will adjust to 65%. Similarly, the F-statistics equate to 19.2178 (prob. value = 0.000), which demonstrates that the study model remains statistically appropriate for research.

5 Conclusions and discussion

This study examines the association between accrual reversals and corporate performance in the non-financial listed firms in Pakistan. The corporate performance of Pakistani listed firms is measured as EBIT 'book-based earnings'. The main objective of the study was to examine the influence of accrual reversals on firm performance. A balanced panel data from the sample of 100 non-financial firms listed at PSX for the period 2009 to 2019 were taken into consideration. There are two approaches among which this study used the cash flow approach to measure accrual reversals to avoid the error in the estimation.

The study developed an econometric model to examine the effect of accruals on firm performance. The econometric model incorporated EBIT as a measure of firm performance – as the dependent variable, and incorporated accrual reversals as an explanatory variable. However, the research incorporated firm size and growth in sales as control variables. The researcher utilised the OLS estimation method to estimate the empirical model of the study."

The findings of the paper show that accrual reversals (denoted by ΔACC) have a statistically significant and positive effect on EBIT. It implies that cash flow decreases with an increase in accrual reversals. However, earnings increase as it consists of cash flows and accruals, 'thus, a positive change in accruals' increases the earnings of firms. Furthermore, the previous reversals have a significant impact on future earnings, so the researcher concludes that previous reversals can predict future earnings. Firm size, which is symbolised as *SIZ*, also shows a significant and positive effect on *EBIT*, while growth shows a negative effect on *EBIT*. The findings` of the study reveal that when there is an increase in reversals of total accruals, then it contributes positively to earnings in the form of an increase in cash flows. The findings of the study show that "current accrual reversals have a relatively more significant impact on current earnings compared to the impact of previous reversals of total accruals on current earnings." The study showed the unique behaviour of the listed firm. The results show the positive contributions of accrual reversals in the enhancement of corporate performance. The findings of the study reported the importance of accrual reversals in the firm and show the implications of accrual reversals for corporate performance, which is useful for the managers and the academics in the subject area. The results show the critical and significant association between accrual reversals and corporate performance, which needs the attention of the management and directors in making policy and decisions regarding the increase and decrease of accruals. The findings of this study are consistent with empirical studies such as Allen et al. (2013).

6 Limitation and future recommendations

There are some limitations of the paper while examining the effect of accrual reversals on firm performance in Pakistani listed firms only. The results of the study are only limited to the first limitation was the time constraints, while the second limitation was the availability of the data. This will help future researchers to eliminate the limitations faced by this study by developing a proper study plan. A different aspect of the accrual reversals, such as good and bad reversals must be studied that is also recommended by Baloch and Hassan (2016) and their impact must be examined for the betterment of corporate performance. It is also recommended to conduct a comparative analysis between emerging economies, which will help understand the impact and behaviour in different emerging markets. The researcher suggests for scrutinising the influence of accrual reversals on the performance of financial companies as well. It is because financial firms have higher provisions of accruals relative to non-financial firms. Further, the researcher suggests utilising the different measures of accrual reversals. Lastly, the researcher suggests including both developed and developing economies for a comparative study.

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