

Trust, accountants and the economy

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Speaker: Hans Hoogervorst, Chairman, International Accounting Standards Board

Venue: Al Faisaliah Hotel, Riyadh, Saudi Arabia

Intro

His Excellency Dr Majid bin Abdullah Al Qasabi, Minister of Commerce and Investment; other honourable current and former ministers of the Kingdom of Saudi Arabia; Dr Ahmad Almeghames, Secretary General of SOCPA; Michael Izza, chief executive of ICAEW; SOCPA and ICAEW members; ladies and gentlemen.

This is my first opportunity to visit the Kingdom of Saudi Arabia and I am truly delighted to be here in Riyadh. It is also a great honour to be invited to take part in the celebration of SOCPA's 25th anniversary. The International Accounting Standards Board and the IFRS Foundation cherish our cooperation with SOCPA, which we know as a highly competent, professional and reliable body. Over the years, SOCPA has established an excellent track record in strengthening the accounting profession in Saudi Arabia. Moreover, SOCPA is an important actor in the region – and has also played an important role in providing high quality translation of IFRS Standards into Arabic.

We also feel privileged to have Dr Abdulrahman Al-Humaid as one of the IFRS Foundation's Trustees. He has been instrumental in promoting the adoption of IFRS in the Kingdom.

The title of the event – building trust – is a topic close to my heart. In my address today, I will talk about the importance of trust and the role of both accountants and accounting in promoting it.

First, I will touch upon the accounting profession in a changing world. Second, I will talk about the role accountants and accounting play in serving the public interest. And third, I will look at how important information and trust is for the efficient functioning of capital markets.

A changing world

We live in a rapidly changing world. The world of business and finance looks very different today compared with 25 years ago, when SOCPA was established.

Let me illustrate with just a few examples. 25 years ago – in 1992 – several organisations that we today see as a key part of our business and political landscape didn't exist: the World Trade Organization, the G20, the EU single market.

We hadn't yet experienced the crises that have shaped today's regulatory landscape: the Asian financial crisis of the late nineties, Enron's collapse in 2001 and the global financial crisis that unfolded after 2007.

Foreign direct investment (FDI) in 1992 stood at \$153 billion. Today it is more than \$2 trillion. Global trade has expanded tremendously, surpassing GDP growth year by year. A new technological revolution has greatly sped up the dissemination of information around the world. In 1992, the first image was uploaded to the World Wide Web. We now live in a much more inter-connected world where both trade and information-sharing across country-borders are the norm.

Saudi Arabia knows there is more change coming ahead and is determined to help shape that change. The Kingdom's Vision 2030 is an ambitious plan for the future. You are determined to become a global investment powerhouse. You want to use your unique strategic location between key global waterways to make Saudi Arabia a global hub, connecting three continents.

The forthcoming Initial Public Offering (IPO) of Aramco –probably the biggest float in history – will be a landmark development. It is part of your strategy of transforming Aramco from an oil producing company into a global industrial conglomerate. The Capital Market Authority's aim to increase the number of companies on the Tadawul and to promote greater foreign ownership of Saudi Arabian companies reflects far-reaching ambitions.

So where does the accounting profession come in with regards to fulfilling these ambitions?

Accountants can work in many different capacities: as auditors, as external business advisers or in the finance function of all sorts of organisations. Whether they work in the public or the private sector, accountants will have an important role to play in making Vision 2030 come to fruition. They are often on the frontline of introducing and implementing change to the organisations they work for or in. Constant adaptation to the changing world we live in is therefore in the DNA of the profession.

Working in the public interest

Another integral element of the accounting profession should be to act in the public interest. As stated in SOCPA's vision, mission and values; 'we believe in acting responsibly, in the best interests of our members and the general public'.

My organisation, the International Accounting Standards Board, has the public interest as the core focus of its work too. The public interest is embedded in our Constitution.

Our Mission Statement says that we exist to develop accounting standards that bring transparency, accountability and efficiency to financial markets around the world. Our standards serve the public interest by fostering trust, growth and long-term financial stability in the global economy.

Growth and financial stability is important to us all. And growth depends on how well resources are managed and developed. Again, this is a core area for the profession; accountants play a role in ensuring cost efficiency and optimal capital allocation.

The strength of an economy also depends on there being sufficient access to finance. Access to capital is necessary to grow, to develop and to foster change and innovation. This is true for both the public and the private sector. Capital will only be provided on the basis of trust. Banks and investors will only be willing to make funds available if they can trust the information provided by those who will be using these funds. This is also recognised in Vision 2030, which aims to strengthen accountability in your economy. Accountants play a vital role in fostering trust. Their role is to ensure that financial information, the lifeblood of the economy, is solid and trustworthy.

Capital markets & information

I will now move on to talk about the importance of financial regulation in capital markets. A sound regulatory framework is also fundamental to trust. Especially when market participants engage with each other across country borders.

The world's first stock exchange opened in my home country, the Netherlands, in 1602. It was called the Amsterdam Stock Exchange and was established by the Dutch East India Company. Not long after its foundation, the local government started to regulate the activity on the exchange. While these early attempts at regulation were not always successful, they show how capital market trading and regulation have always gone hand in hand.

More than 400 years after the birth of the Amsterdam Stock Exchange, I was honoured to be chair of the Financial Markets Authority, the Dutch securities regulator. I started in 2007 and witnessed the darkest days of the Global Financial Crisis. This crisis, the effects of which are still being felt, taught us many valuable lessons. The main lesson was that a sound financial system needs to be underpinned by high quality standards of corporate governance and a solid regulatory and ethical framework. Only under such conditions can there be sustainable capital market and economic development.

The Global Financial Crisis is probably also one of the reasons why we seem to see a backlash to economic globalisation. Both Brexit and the outcome of the elections in the United States have been widely interpreted as a negative reaction to globalisation. History never develops in straight, flawless lines, so it is entirely possible that the trend towards growing global investment and trade may be temporarily interrupted.

But we have to be careful not to draw hasty conclusions. For example, while the UK has decided to leave the EU, the British are determined to remain a global economic player. The Brexiteers are indeed very keen to be seen as pro-free trade and pro-globalisation.

Even if the level of cross-border transactions ended up reducing, however unlikely for the long haul, the case for global accounting standards remains compelling. Multinational corporations will continue to span the world and investors will continue to seek investment opportunities on a global basis.

Countries' financial systems are increasingly built on a compendium of best-practice international standards (much the same way as the internet is also built on a compendium of technology standards). According to the Financial Stability Board and the International Monetary Fund, IFRS Standards are one of a handful of such standards.

IFRS Standards

IFRS Standards bring transparency by enhancing the international comparability and quality of financial information, enabling investors and other market participants to make informed economic decisions.

They also strengthen accountability. They do that by reducing the information gap between companies and those who have entrusted their money to these companies. They help those on the outside hold those on the inside to account. IFRS Standards are also an important tool for regulators because they generate comparable information to the global regulatory community.

IFRS Standards contribute to economic efficiency. They do that by helping investors to better identify opportunities and risks – in a specific country and across the world. They help improving capital allocation around the world. Your vision of transforming the Public Investment Fund into the world's largest sovereign wealth fund is greatly helped by the adoption of IFRS Standards around the world. Sovereign wealth funds need to invest internationally to build up a diversified and safe portfolio. The spread of IFRS has made this a much less daunting task than in the pre-IFRS world of wildly diverging national accounting standards.

Research shows that moving from national to international accounting standards can bring several benefits, including lowering the cost of capital. This goes back to trust and confidence. When confidence is high, money flows in. When confidence is low, it drains out.

Finally, the use of a single, trusted accounting language is also helpful to businesses at a micro level. Not only as a key facilitator in accessing capital from foreign investors. The use of IFRS Standards can also have internal business benefits. For companies with large international operations, the use of one accounting language brings down accounting costs and helps improve internal management systems among subsidiaries.

Research conducted among companies in Japan, by the Japan Financial Services Agency in 2015, illustrates the benefits seen at a micro level.

In Japan, companies have a choice of different sets of accounting standards. There is a big trend at the moment for large Japanese companies to voluntarily adopt IFRS Standards. A few years ago, only a handful of companies reported using IFRS Standards. Today, the companies that have either adopted, or are in the process of adopting our Standards account for about 30 per cent of the market capitalisation¹. That amounts to just over 140 companies. In addition, more than 200 other companies are considering the adoption of IFRS.

The research showed that companies ranked ‘efficiency in business management’ as the top reason for voluntarily adopting IFRS Standards. This was followed by enhanced comparability with competitors and better communication with international investors.

The Kingdom’s new language

The benefits of adopting IFRS Standards have been recognised here in Saudi Arabia. The silver anniversary celebration of SOCPA coincides with another important event here this year; the requirement for companies to report using IFRS Standards. This sends clear signals to the world that Saudi Arabia welcomes foreign direct investment. With Saudi Arabia on board, 125 countries and 75 per cent of the G20 countries now require the use of IFRS Standards. This is truly a momentous occasion and we are grateful for your vote of confidence.

Close

I would like to close by expressing once again my thanks to SOCPA. It is in our interest as much as in yours that Saudi’s experience with IFRS is a positive one. So we are very happy to work with you on making the transition process a success. As I said in my introduction, we have an excellent relationship with SOCPA and we look forward to very close cooperation in the future.

Through SOCPA, Saudi Arabia plays an important role in helping shape the future direction of IFRS Standards. I wish you all good luck in the next 25 years, which I am sure will also be very fruitful, both for the accounting profession and for the development of the capital market in the Kingdom.

Thank you.

¹ <http://www.ifrs.org/Alerts/PressRelease/Pages/Japan-FSA-study-on-IFRS-May-2015-.aspx>