Chapter 17
Externally Financed Growth and Quality Accounting Information: Evidence From Brazil

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ABSTRACT

This study investigates the association between quality accounting information (QAI) and externally financed growth (EFG), taking a sample of 214 firms in Brazilian stock exchange from 1998 to 2015. EFG is estimated from the sales percentage approach to financial planning. QAI is estimated according to the accruals quality model proposed by Dechow and Dichev and modified by McNichols. The hypothesis that signaling efficient accounting information marginally influences and positively EFG is tested by multiple linear regression with estimation by OLS and could not be rejected. It is inferred that QAI is a significant attribute in contributing to the firm's access to the external financing channel. This study broadens the discussions about the themes in the Brazilian scenario, shedding light on the importance of the practice of the dissemination of quality information for the growth of firms in the Brazilian context.

INTRODUCTION

The literature on corporate finance emphasizes the relevance of informational asymmetry in influencing firm growth through its impact on the efficiency of its investments (Stein, 2003). Myers and Majluf (1984), in this sense, argue that more information asymmetry between managers of firms and their capital providers can increase the cost of external financing sources of firms.

This distortion may limit firms' access to low-cost external financing, as well as their ability to pursue potentially lucrative projects (Demirguc-Kunt & Maksimovic, 1998). In addition, the presence of greater informational asymmetry among managers and suppliers of capital of firms can also limit their

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investments to the level of their internal cash flows (Fazzari, Hubbard, & Petersen 1988), which may reflect lower growth (Albring, Huang, Pereira, & Xu 2013).

Under these conditions the accounting information is presented as an informational signal with the capacity to reduce the informational asymmetry among the agents around the firm's operation and, as a consequence, also reduce the cost of external financing sources of firms, if offered with quality attributes, based on empirical evidence (Lambert, Leuz, & Verrechia, 2007, Silva & Nardi, 2017). The evidence suggests that signaling of higher quality accounting information reduces the cost of external financing for firms.

It must be acknowledged that quality accounting information is a broad concept of multiple dimensions (Burgstahler, Hail, & Leuz, 2006), and that there is no consensual metric in accounting literature to define it (Potin, Bortolon, & Sarlo Neto, 2016). Ball and Shivakumar (2005) define such quality as the usefulness of such information for investors, creditors, managers and all other contracting parties with the firm.

In this paper, quality accounting information is defined as the extent to which accrual accounting contribute the measurement of the underlying economic performance (Nivolaev, 2014). The use of accruals by accounting is intended to create a measure that best reflects the performance of the firm (Dechow & Dichev, 2002), such a measure the earnings determined by the accounting system.

These informational signals can improve firms 'access to low-cost external financing by reducing informational asymmetry, as well as increasing firms' ability to finance their growth opportunities, since they would be obtaining low-cost external financing, according to Khurana, Pereira and Martin (2006).

In this sense, firms that would report high quality accounting information, therefore, would have a greater possibility of growth than firms that do not practice such reporting, since, in addition to their internal resources, they would also access sources of external financing at low-cost and would have greater capacity to finance their opportunities growth. On the other hand, firms signaling low-quality accounting information will access higher-cost external financing in the face of greater informational asymmetry, which would force these firms to renounce potential profitable projects and, therefore, would present more restricted growth (Myers & Majluf, 1984).

In the international context, research (Albring *et al*., 2013; Hyytinen & Pajarinen, 2005) has shown evidence of a positive relationship between firm growth and the quality accounting information reported by its managers. According to these studies, firms that signal higher quality accounting information have higher growth rates.

In the Brazilian context, in limited research, no research was found that proposed to investigate such relationship. It is possible point to the study by Carvalho and Kalatzis (2018), that have examined the relationship between the quality accounting information and investment decisions in the context of Latin American countries (including Brazil); showed that low-quality accounting information increases the dependence of firms' investment decisions on the levels of their internal cash flows. Thus, the need for funds to finance possible growth opportunities may contribute to firms reporting higher quality accounting information to raise funds through external financing channels in the Brazilian scenario.

Considering the above discussion, this research examines whether signaling of quality accounting information influence growth of firms listed in Brazil stock exchange. More specifically, the objective is to analyze whether signaling of quality accounting information impact externally financed growth considering those firms, with externally financed growth being estimated from the percentage of sales for financial planning, according to Demirguc-Kunt and Maksimovic (1998), and the quality accounting

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