PROFIT MEASUREMENT UNDER GENERAL PRICE LEVEL ACCOUNTING

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Abstract *This study aims to examine the differences in profit and earning per share under historical cost accounting and general price level accounting system and to correlate them with current market price. A simple random sample of four companies was drawn from thirty BSE SENSEX companies. Financial statements of 2001-02 to 2010-11 were restated under general price level accounting system. The main finding of the study was that the inflation is recurring feature in India. The figure of profit under historical cost accounting is inflated and illusory. The degree of relationship of Earning per Share with current market price of shares under historical cost accounting is higher than general price level accounting. The study suggests to show the inflated adjusted data as supplementary information to make a decision for investors and policy makers.*

Keyword: *Trend of Inflation, Historical Cost Accounting, General Price Level Accounting, Earning per Share, Financial Statements*

INTRODUCTION

Earning per Share (EPS) is an important measure of corporate performance for shareholders and potential investors. EPS numbers are the focus of prospectuses, media discussions, and analyst reports. Accountants calculate the basic earning per share by dividing the net profit or loss for the period attributable to equity shareholders (the numerator) by the weighted average number of equity shares outstanding (the denominator) during the period (IAS 33:10/Ind AS 33:10/ AS 20). Net profit is calculated based on historical cost accounting system. Stable monetary unit is employed for determining profit under this system. Critics argue against this practice, because the general purchasing power of the monetary unit. i.e. rupee changes as the rate of inflation increases or decreases in a country. As per Labour Bureau, Ministry of Labour, Government of India, average annual point to point inflation measured on the basis of Consumer Price Index (Base 2001) was 4% on 2001-02 and 10.53% in 2010-11. Average annual inflation is 6.35% over a period of twelve years, which seriously distorts financial performance and financial position disclosed by financial statements. Inflation brings downward changes in the purchasing power of the monetary unit and makes its myth. Financial statements prepared without any regard to the current purchasing power of the monetary unit lose much of their significance and cannot be properly appreciated by their various users, such as investors, lenders, government, employees and management, who are interested in them, in a meaningful manner. The profit is inflated under historical cost accounting system, because it does not match current revenues with current costs of operation. Inflated profit leads to harmful by over-distribution of dividends, excessive taxation on the corporate sector, under pricing of sales and investors being misled as to the performance of companies. The balance sheet prepared on the basis of historical cost accounting does not truly represent the resources held by an enterprise in terms of current price. In the periods of inflation, historical cost accounting fails to maintain the operating capital by exaggerated and illusory figures of profits (S. A. Effeiong, 2011).

Accounting for price level changes was advocated to overcome these limitations of historical cost accounting system. Inflation-adjusted financial statements would not only achieve the objective of reliable profit and financial position measurements but would also prove useful to management and external users in their decision making. There is no particular accounting standard dealing with inflation accounting. Preparing and reporting of inflation adjusted financial statements is mandatory as per IAS 29, only when the countries experience hyperinflationary economy.

In inflationary period, it is important to examine whether the inflation has significant effect on accounting profit and share prices. The present work contributes to an understanding the issue in three ways. First it examines the status of inflation rate in India. This is done through applying ANOVA for twelve years (2001 to2011) point to point rate of inflation. The result shows that, India has the high rate of inflation next to Turkey and the rate of inflation is statistically significant at 0.001 level. Second part analyzes the differences in profit after tax and earnings per share under historical cost and

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general price level accounting system. This is done through testing of hypothesis by using paired sample t-test for a sample of four companies. The result shows that there is a significant differences in profit after tax and earnings per share between these two accounting system at 0.05 level. Third part examines the relationship between earning per share and current market price of shares. This was tested through applying correlation analysis. The result shows that earning per share under historical cost accounting system highly and positively correlated with current market price of shares than general price level accounting system.

The findings of the present study was, the inflation has impact on accounting figures. Profit and earning per share were overstated under historical cost accounting system. The study suggests that the companies should disclose the inflation adjusted data to know the companies "real profit" and true financial position. Disclosure of inflation adjusted data helps the policy makers and investors for their decision making.

REVIEW OF LITERATURE

A number of exposure drafts and statements for debate were issued related to inflation accounting. However, the first issue of an accounting standard on this subject was in the UK in 1974. Later in the same year, CPP proposals were issued in the USA, and by the Canadian and Australian professional bodies. In 1975 a current purchasing power exposure draft was published in New Zealand and a discussion paper for South Africa came in the same year. There were also important CPP method developments in Brazil and Chile in 1974. In India, recognizing the importance of the effect of changing prices on the financial statements of business enterprises, the research committee of the ICAI has brought out a Guidance Note on accounting for changing prices in 1982 based on UK accounting Standard. The main objective of this guidance note is to encourage the adoption of accounting for changing prices, and to suggest a methodology relevant in the prevailing economic environment in India.

Only few companies i.e. Infosys Ltd and Oil and Gas Ltd companies were disclosing inflation adjusted financial statements in their published annual reports, based on UK's SSAP 16 and Guidance Notes on Accounting for Changing Prices issued by the Research Committee of the ICAI. This guidance note was withdrawn in 2008.

Internationally accounting for price level changes is presently covered by International Accounting Standard 29- "Financial Reporting in Hyperinflationary Economics". IAS 29 prescribes the mode of adjustment of financial statements for inflation and the treatment of gain or loss resulting from such adjustment. IAS 29 mandates that presentation of Inflation Adjusted financial statements are mandatory in nature and not supplementary to Historical Cost Financial Statements during hyperinflation economies.

The study reviewed many literatures, the summary of important literatures are as follows:

Askoan Anandarajan (2005) examined the factors associated with equity valuation in Turkey. The study found that the book value adjusted for inflation has a stronger association with equity values. The result shows that, earnings and inflation–adjusted book values combined virtually explain almost 75% of the variation in equity prices in Turkey.

Berna Kirkulak and Cagnur Kaytmaz Balsari (2009) investigate the role of incremental information content of inflation adjusted data plays in explaining the market value of equity and stock returns on the Istanbul Stock Exchange (ISE). They collected stock prices and fundamental accounting information for firms listed on the ISE from 2003 financial reports. The samples of 140 firms were included for the study. The author used t-test and regression analysis to analyze the data. The author showed the effect of inflation accounting application on basic financial ratios and they affect financial ratios significantly, which may create different risk assessments for the selected firms. The result of the study was both inflation-adjusted and historical cost-based earnings and book values are significantly value relevant. Overall the result shows that the two sets of data are not substitutes but, rather they are complementary. Because of these complementarities, policy makers should require inflation-adjusted data as supplementary data to historical-data to historical-cost information rather than in place of historical cost data.

Yaniv Konchitchki (2011) studied that, while the effects of inflation are not recognized in nominal statements, such effects may have economic consequences. This study found that unrecognized inflation gains and losses help predict future cash flows as these gains and losses turn into cash flows over time. According to this study even low rate of inflation also will effect on financial statements and stock prices.

Dr. Musa Inuwa Fodio (2012) investigates the comparative value relevance of historical cost accounting and inflation-adjusted accounting information in Nigeria. Regression analysis has been used to measure the joint effect of the earning numbers on securities prices. The study recommended that the policy makers in Nigeria should encourage firms to provide inflation adjusted information to compliment, rather than replace the conventional historical cost financial information provided in the annual reports

OBJECTIVES OF THE STUDY

1. To study the trend of inflation among different countries and in India.

2. To restate the financial statements under general price level accounting system.
3. To measure profit and earning per share under general price level accounting and compare them with historical cost accounting.
4. To study the impact of earning per share on current market price of shares.

HYPOTHESES

1. "There is a variation in rate of inflation among countries"
2. "There is a variation in rate of inflation in India"
3. "There exists difference in profit after tax between historical cost accounting system and general price level accounting system"
4. "There is a difference in earning per share between historical cost accounting and general price level accounting system"
5. "Earning per share and current market price is positively and significantly correlated under historical cost accounting system"
6. "Earning per share and current market price is positively and significantly correlated under General Price Level accounting system"

RESEARCH METHODOLOGY

Sample of Companies

The population of the study includes companies listed in recognized stock exchanges. The frame of the study was 30 SENSEX companies which are listed in Bombay Stock Exchange. Four companies were drawn as a sample for the study by using simple random sampling technique. They are Cipla limited, Infosys Technologies Limited, Reliance Industries Limited and Wipro Limited.

Data Collection from Annual Reports

The study was based on secondary data available in the Annual Reports of sample companies. Audited financial statements of ten years (2001-02 to 2010-11) were considered for the study**.** Current market prices of stock were obtained from the website of www.bseindia.com.

Collection of Inflation Data

The sample of eight countries was taken for the study to compare the rate of inflation with India**.** The rate of inflation based on Consumer Price Index (CPI) was collected from the respective countries statistics website, i.e., Bank of Canada (Canada), National Bureau of Statistics (China), Labour Bureau of Statistics (India), Statistics bureau, Director- General or policy planning and statistical Research and Training Institute (Japan), National Statistics Agency (Mexico) Office for National Statistics (UK), Bureau of Labour Statistics (USA), State Institute of Statistics (Turkey).

Restatement of Financial Statements Under General Price Level Accounting

Indian listed companies do not provide the inflation-adjusted data because there is neither legal nor institutional requirement to disclose the inflation-adjusted data. Hence inflation-adjusted information needs to be approximated from historical cost accounting information available in the company's annual reports. The financial statements were restated according to the guidance note on "accounting for changing prices" issued by Institute of Chartered Accountants of India (ICAI). General Price Level adjustments have been done to restate the financial statements. Consumer Price Index was used to restate the historical cost accounting statements into general price level accounting statements. Consumer Price Index publishes in Labour Bureau of India.

Assumption

1. Year 2001 was taken as base year to restate the financial statement
2. Due to lack of asset acquisition data in the annual report, depreciation charge was obtained by multiplying total inflation adjusted value of asset by the proportion of historical cost depreciation charge to total historical cost value assets.

Data Analysis

ANOVA was used to find the difference in the rates of inflation for twelve years. Paired sample t-test was used to test the differences in profit after tax and earning per share between historical cost accounting and general price level accounting. Correlation analysis was used to find the relationship between EPS and current market price.

EMPIRICAL RESULTS AND DISCUSSION

Rate of Inflation

Inflation is a common phenomenon in all the countries around the world. Developing countries as well as developed

Table 1: Rate of Inflation by Countries

Country Year	Canada	China	India	Japan	Mexico	UK	USA	Turkey
2000	2.72	0.35	4.02	-0.65	9.51	0.8	3.38	56.48
2001	2.53	0.73	3.77	-0.8	6.39	1.2	2.83	53.46
2002	2.26	-0.73	4.31	-0.9	5.03	1.3	1.59	47.2
2003	2.77	1.13	3.81	-0.25	4.56	1.4	2.27	21.94
2004	1.86	3.84	3.77	-0.01	4.68	1.3	2.68	8.6
2005	2.21	1.78	4.25	-0.27	4.0	2.0	3.39	8.19
2006	2.01	1.65	5.79	0.24	3.63	2.3	3.24	9.59
2007	2.14	4.82	6.39	0.06	3.97	2.3	2.85	8.78
2008	2.37	5.97	8.32	1.37	5.12	3.6	3.85	10.43
2009	0.31	-0.72	10.83	-1.34	5.31	2.2	-0.34	6.28
2010	1.78	3.17	12.11	-0.72	4.16	3.3	1.64	8.58
2011	2.91	5.53	8.87	-0.28	3.41	4.5	3.16	6.45
Mean	2.16	2.29	6.35	-0.3	4.98	2.18	2.54	20.49
S. D	0.68	2.34	2.98	0.69	1.65	1.12	1.14	19.74
Rank	7	5	2	8	3	6	4	1

Source: Bank of Canada (Canada), National Bureau of Statistics (China), Labour Bureau of Statistics (India), Statistics bureau, Director- General or policy planning and statistical Research and Training Institute(Japan),National Statistics Agency (Mexico) Office for National Statistics (UK), Bureau of Labour Statistics (USA), State Institute of Statistics (Turkey).

countries have experiencing/ have experienced inflation of a very high magnitude during different time spans. Inflation is a rise in general price levels. If the amount of money in a country - the money supply - grows faster than production in that country, the average price will rise as a result of the increased demand for goods and services. These price rises cause the value of money to fall. Low inflation encourages consumers to buy goods and services. Maintaining low inflation is therefore an important goal for governments and central banks because of the economic benefits.

CPI is a measure of inflation. In order to calculate the CPI, the prices of a collection of goods and services need to be collected. These prices are then weighted on the basis of the share that they have of average consumer spending. The index is usually calculated annually, but in some countries it is also done quarterly. For most countries the inflation based on the CPI is viewed as the most important inflation figure for the country. The rate of inflation based on the CPI of eight countries including India from the year of 2000 to2011 is given in Table 1.

Testing of Hypothesis

H0: "There is no difference in the average rate of inflation among countries"

H1: "There is a difference in the average rate of inflation among countries"

The result of ANOVA is given in Table 2. The result rejects the null hypothesis and accepts the research hypothesis as the p-value associated with the mean difference in the rate of inflation between the years of 2000 to 2011 is <0.001. The result shows that there is a significant difference in the rate of inflation among the countries.

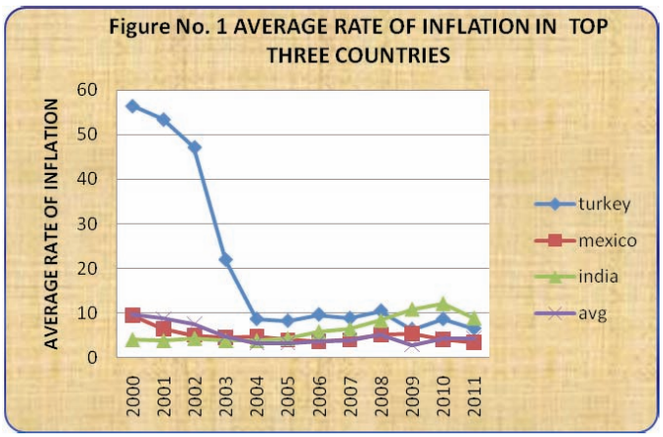
India is one of the countries that live with high inflation rates. In this period, the economical conditions prevented

Table 2: ANOVA Result of Rate of Inflation between the Countries

Rate of inflation	Sum of squares	df	Mean square	F	P value
Between the countries	3592.659	7	513.237	10.005	*0.000
Within the country	4514.381	88	51.30		
Total	8107.040	95			

*p value significant at 0.001 level

the managers of the enterprises to perceive the position of their businesses and to make predictions for the future. Additionally, information derived by accounting is vital in decision-making. The fluctuation rate of inflation affects the financial performance and position of the enterprise. Over the period of twelve years, the average rate of inflation of eight countries was 5.082.The rate of inflation in India is high i.e 6.35% next to Turkey (20.5%). Figure 1 shows the position of Indian rate of inflation.



India is a developing country with GDP rate is 6.9% in 2011(World Bank). Over the period of twelve years the rate of inflation is low with 3.77 per cent in the year of 2001 and high with 12.11 percent in the year 2010. The average rate of inflation for the same period in Japan was -0.3%, Mexico 4.98% and Turkey 20.5%.

Testing of hypothesis

H_0: "There is no variation in rate of inflation in India"

H_1: "There is a variation in rate of inflation in India"

The result of ANOVA is given in Table 3. The result rejects the null hypothesis and accepts the research hypothesis as the p-value associated with the mean difference in the rate of inflation between the years of 2000 to 2011 is <0.001. The result shows that there is a significant variation in point to point rate of inflation in India. The general purchasing power of money is not constant in India. It varies in different span of time. This proves that the assumption of "stable monetary unit" is not true in the time of inflationary period. It affects on financial performance and financial position of the company.

Measurement of Profit

Profit is a measure of performance of business entities. The accounting document which sets out to display profit measurement is known in India as the profit and loss account. The profit and loss account is prepared under historical cost accounting in India.

Table 3: ANOVA Result of Rate of Inflation from 2000 to 2011 in India

Rate of inflation	Sum of squares	df	Mean square	F	P value
Between the years	1169.584	11	106.326	61.114	*0.000
Within the years	229.653	132	1.740		
Total	1399.238	143			

*p value significant at 0.001 level

Table 4: Profit After Tax under Historical Cost Accounting System

Years	Profit After Tax (Rs in Crores)				
	Cipla Limited	Infosys Limited	Reliance Industries Limited	Wipro Limited	Average
2001-02	235.10	807.96	3242.70	866.11	1287.96
2002-03	247.70	957.93	4104.31	813.23	1530.79
2003-04	306.69	1243.47	5160.14	914.88	1906.29
2004-05	409.61	1904.38	7571.68	1494.82	2845.12
2005-06	607.64	2421.00	9069.34	2020.50	3529.62
2006-07	668.03	3783.00	11943.40	2842.10	4809.13
2007-08	701.43	4470.00	19458.29	3063.30	6923.25
2008-09	776.81	5819.00	15309.32	2973.80	6219.73
2009-10	1081.49	5755.00	16235.67	4898.00	6992.54
2010-11	960.39	6433.00	20286.30	4843.70	8130.84

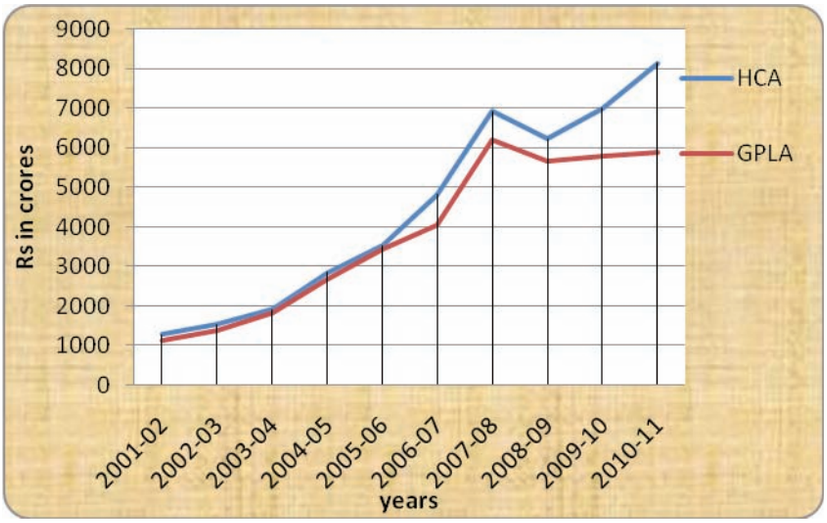
Source: Financial statements in the annual reports of sample companies

Table 5: Profit After Tax under General Price Level Accounting System

Years	Profit After Tax (Rs in Crores)				
	Cipla Limited	Infosys Limited	Reliance Industries Limited	Wipro Limited	Average
2001-02	234.10	500.76	3163.94	646.69	1136.37
2002-03	242.80	904.30	3901.41	572.26	1405.19
2003-04	304.40	1197.39	4960.76	817.53	1820.02
2004-05	402.10	1842.92	7055.18	1463.80	2691.00
2005-06	597.45	2300.00	8909.26	1962.80	3442.37
2006-07	620.15	3500.00	9333.11	2713.00	4041.56
2007-08	642.99	3978.00	17451.91	2746.40	6204.82
2008-09	655.28	5107.93	14373.76	2475.60	5653.14
2009-10	854.16	4078.68	14193.39	4002.30	5782.13
2010-11	759.18	4799.00	14092.13	3916.30	5891.65

Source: Restated figures of financial statements in the annual reports of sample companies

Figure 2: Average Profit After Tax Under Historical Cost Accounting and General Price Level Accounting System



Profit Measurement under Historical Cost Accounting System

Indian companies prepare the financial statements under the historical cost convention, in accordance with the generally accepted accounting principles in India and the provisions of the Companies Act, 1956. Profit measured by the sample companies under historical cost accounting system without considering price level changes is given in Table 4.

The average profit of sample companies was increased from 2001-02 to 2010-11. The average profit is Rs 1287.96 crores in the year of 2001-02 and high with Rs 8130.84 crores in the year of 2010-11.

Profit Measurement Under General Price Level Accounting System

Indian companies are not providing the information of inflation adjusted data. Therefore the financial statements under historical cost accounting are restated to general price level accounting by using consumer price index. Profits obtained by restating the sample company's financial statements to general price level accounting are given in Table 5.

The average profit of sample companies is increased from 1136.37crores to Rs 5891.65 crores from 2001-02 to 2010-11.

Figure 2 shows the average profit after tax of sample companies from 2001-02 to 2010-11 under historical cost accounting system and general price level accounting system. There is a difference in profit figures determined under historical cost accounting and general price level accounting. The level of difference was tested by the following hypothesis.

Testing of Hypothesis of Profit After Tax Between Historical Cost Accounting System and General Price Level Accounting System

H_0: "There exists no difference in profit after tax between historical cost accounting system and general price level accounting system"

H_1: "There exists difference in profit after tax between historical cost accounting system and general price level accounting system"

The result of t-test is given in Table 6. The result rejects the null hypothesis and accepts the research hypothesis as the p-value associated with the mean difference in profit after tax between historical cost accounting system and general price level accounting system is <0.05. Result shows that there is statistically significant difference in the profit after tax between these two accounting system.

The historical cost-based accounting ignores the shrinkage in the value of rupee as a measuring rod and keeps adding transactions which are represented by rupees of differing value over a period of time. In historical cost accounting, the monetary unit (rupee) used to measure incomes and expenditures, assets and liabilities, has a mixture of values and related to different period of time. Revenues are measured in inflation (current) rupees whereas production costs are a mix of current and historical cost. Some costs are measured in very old rupees; some are measured in current rupees. Calculation of depreciation based on historical cost of the asset is less than the current cost of the asset. Undercharging of depreciation provides the huge profit in profit and loss statement. Inventories consumed are valued at their money cost of acquisition but they are matched with sales revenue expressed at current prices. The end result is that the reported profit gets swollen by a capital element representing inventory gain.

A historical cost account does not consider the monetary gain or loss on the monetary assets and liabilities held by a company during the time of rising prices.

Thus whenever there is a time lag between acquisition and utilization, historical cost accounts gives the "inflated and illusory" figures of profit instead of "real profit"

Table 6: T-Test Result of Profit After Tax Between Historical Cost Accounting System and General Price Level Accounting

System of Accounting	Mean	SD	Mean differences	SD	t-value	Df	p-value
HCA	4417.5	2534.0168	610.7	217.393	2.809	9	0.020*
GPLA	3806.8	1991.910					

*p value is significant at 0.05 level

Table 7: Earning per Share as per Historical Cost Accounting System

Years	Earning per Share				
	Cipla Limited	Infosys Limited	Reliance Industries Limited	Wipro Limited	Average
2001-02	39.20	122.12	23.36	37.47	55.53
2002-03	41.31	144.68	29.25	35.17	62.60
2003-04	51.14	187.38	36.79	13.19	72.12
2004-05	13.66	70.95	54.24	21.48	40.08
2005-06	20.66	88.67	65.80	14.37	47.37
2006-07	8.59	67.93	82.17	19.92	44.65
2007-08	9.02	78.24	134.19	21.11	60.64
2008-09	9.99	101.65	96.76	20.44	57.21
2009-10	13.69	100.37	49.65	20.16	45.96
2010-11	11.96	112.26	62.00	19.88	51.52

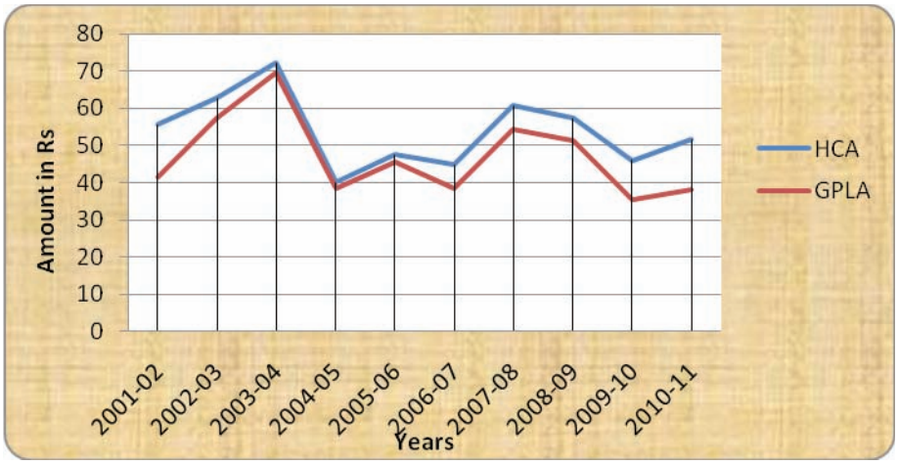
Source: Financial statements in the annual reports of sample companies

Table 8: Earning per Share as per General Price Level Accounting System

Years	Earning per Share				
	Cipla Limited	Infosys Limited	Reliance Industries Limited	Wipro Limited	Average
2001-02	39.03	75.68	22.79	27.97	41.36
2002-03	40.49	136.58	27.80	24.74	57.40
2003-04	50.75	180.43	35.36	11.78	69.58
2004-05	13.40	68.66	50.54	21.03	38.40
2005-06	19.92	84.23	64.63	13.95	45.68
2006-07	7.97	62.85	64.21	19.01	38.51
2007-08	8.26	69.62	120.35	18.92	54.28
2008-09	8.47	89.22	90.84	17.15	51.42
2009-10	10.81	71.10	43.40	16.47	35.44
2010-11	9.45	83.61	43.06	16.07	38.04

Source: Restated figures of financial statements in the annual reports of sample companies

Figure 3: Earning Per Share as per Historical Cost Accounting and General Price Level Accounting



Earning Per Share (EPS)

Earning per share is one of the most important variable in determining the share price and is also serves as an indicator of a company's profitability. Growth in EPS is an important measure of management performance because it shows how much money the company is making for its shareholders. The EPS is calculated by dividing net profit after taxes and preference dividends by the number of outstanding equity shares.

Calculation of Earning per share under Historical Cost Accounting System

The average earning per share of sample companies is high with 72.12 in the year of 2003-04 and low with 40.08 in the year of 2004-05.

Calculation of Earning Per Share under General Price Level Accounting System

Table 8 shows the Earning per Share based on General Price level accounting system after considering the price level changes.

The average earning per share of sample companies under general price level accounting is high with 69.58 in the year of 2003-04 and low with 38.04 in the year of 2010-11.

Figure 3 shows the average earning per share of sample companies from2001-02 to 2010-11under historical cost accounting system and general price level accounting system. There is a gap in Earning Per Share calculated under historical cost accounting and general price level accounting system.

Table 9: T-Test Result of Differences in Earning Per Share Between Historical Cost Accounting System and General Price Level Accounting System

System of Accounting	Mean	SD	Mean differences	SD	t-value	Df	p-value
HCA	53.7709	9.74362	6.759	1.44369	4.682	9	0.001*
GPLA	47.0110	10.97501					

*P value is significant at 0.05

Table 10: Current Market Price of Shares

↓Years/Company→	Cipla Limited	Infosys Limited	Reliance Industries Limited	Wipro Limited	Average
2001-02	1101.78	3634.80	317.13	1443.60	1624.32
2002-03	916.88	3860.00	273.63	1453.68	1626.04
2003-04	999.15	4250.50	428.83	1245.33	1730.90
2004-05	366.79	2701.80	508.11	849.53	1106.55
2005-06	383.83	2512.89	709.34	542.59	1037.16
2006-07	265.50	2321.31	1152.87	541.55	1070.30
2007-08	198.49	1790.33	2198.25	484.60	1167.91
2008-09	205.78	1477.25	1795.46	344.87	955.84
2009-10	286.66	2147.59	1685.69	542.52	1165.61
2010-11	330.39	2947.86	1024.36	482.83	1196.36

Source: www.bseindia.com

Testing of Hypothesis of Earning Per Share Between Historical Cost Accounting System and General Price Level Accounting System

H_0: "There is no significant difference in earning per share between historical cost accounting and general price level accounting system"

H_1:"There is a significant difference in earning per share between historical cost accounting and general price level accounting system"

The results of t-test are given in Table 9. The result rejects the null hypothesis and accepts the research hypothesis as the p-value associated with the mean difference in earning per share between the historical cost accounting system and general price level accounting system is <0.05. The result shows that there is statistically significant difference in the earning per share between historical cost and general price level accounting.

Earning per share is higher under historical cost accounting, because of its "inflated profit". Earning per share is low under general price level accounting, because it matches the current revenues with the current expenses by adjusting of all the incomes and expenditure at general price level changes.

Current Market Price

Table 10 shows the current market price of shares of sample companies from 2001-02 to 2010-11.

Testing of Hypothesis of Relationship Between Earning Per Share and Current Market Price of Shares Under Historical Cost Accounting

H_0:"Earning per share and current market price of shares is not positively and significantly correlated under historical cost accounting"

H_1: "Earning per share and current market price of shares is positively and significantly correlated under historical cost accounting"

Table 11 shows the Relationship between Earning per share and current market price of shares under historical cost accounting. Result shows that there is a positive correlation between EPS and current market price of shares. EPS under HCA is positively (0.689) and significantly correlated (0.028) with current market price of shares. Hence research hypothesis is accepted and null hypothesis is rejected.

Table 11: Results of Correlation Analysis

Independent variable	Dependent Variable	r-value	p-value
Earning Per Share (EPS)	Current Market Price	0.689	0.028*

* p value is significant at 0.05 level

Table 12: Results of Correlation Analysis

Independent variable	Dependent Variable	r-value	p-value
Earning Per Share	Current Market Price	0.549	0.100*

* p value is insignificant at 0.05 level

Testing of Hypothesis of Relationship Between Earning Per Share and Current Market Price of Shares Under General Price Level Accounting

H_0:"Earning per share and current market price of shares is not positively and significantly correlated under General Price Level Accounting"

H_1: "Earning per share and current market price of shares is positively and significantly correlated under General Price Level Accounting"

Table 12 shows the relationship between EPS and current market price of shares under general price level accounting system. Result shows that there is a positive correlation between EPS and current market price of shares under general price level accounting with r-value 0.549. The degree of relationship is insignificant with p value of 0.100. Hence the null hypothesis is accepted and research hypothesis is rejected.

Earning per share is positively correlated with current market price of shares under both system of accounting. But the degree of relationship is insignificant under general price level accounting system. It is so because the companies in India are following historical cost accounts. The ignorance of inflation under historical cost accounts leads to huge profit, higher earning per share and higher correlation with the current market prices of shares. Historical cost accounting is not reporting the "real profit" of the company.

Current market price of shares is determined based on historical cost accounting profit. Prices based on historical cost accounting financial information which is incomplete or misleading will result in poor pricing and allocation decisions.

IMPLICATIONS FOR PRACTICE

Inflation, especially at rates varying widely from year to year, introduces increased uncertainty into business activities. Most management appreciates the need to consider inflation in making decisions. But communicating the effects of inflation is hindered by the lack of systematic and explicit recognition inflation's effects in financial reports. By introducing a system of inflation accounting, the external users will be able to make better decisions; shareholders will be more realistic in their dividend expectations and investment valuations. The study suggests that the accounting system should consider the rate of inflation to provide the "real profit" and maintain the true financial position of the company. Policy makers should require inflation adjusted data as supplementary data to historical cost information. In addition to adjusting this set of financial statements; the company should present a statistical supplement in which financial elements significant the investor- per share earnings, dividends, book value etc., are indexed to the general price level.

IMPLICATIONS FOR FURTHER RESEARCH

The study suggests a direction for future studies on impact of inflation on company's debt and equity capital and dividend decisions.

CONCLUSION

The present study found that the rate of inflation is statistically variance at 0.01 significant levels over the period of ten years (2001-02 to 2010-11). Hence consideration of inflation in accounting is value relevant. Profit after tax and earning per share was calculated under historical cost and general price level accounting system. The differences in profit after tax and earning per share between these two accounting systems have tested by using paired sample t-test. The result found that there is a difference in profit after tax and earning per share under both the system. Earning per share under historical cost accounting is highly correlated with current market price of shares than general price level accounting system.

The present study is limited to only the sample of four companies listed in BSE SENSEX and period of ten years (2001-02 to 2010-11). In spite of this limitation the findings of this paper have several important implications.

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