



ROLE OF FINANCIAL CONSTRAINTS IN THE RELATIONSHIP BETWEEN THE VOLATILITY OF ECONOMIC POLICY UNCERTAINTIES AND ACCOUNTING CONSERVATISM

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ABSTRACT

This study aimed to examine the role of financial constraints in the relationship between the volatility of economic policy uncertainties and accounting conservatism in companies listed on the Tehran Stock Exchange from 2014 to 2022. The volatility of economic policy uncertainties and accounting conservatism were regarded as independent and dependent variables, respectively. The study also used the library method to collect data. In the data section, sample corporate data were collected by examining financial statements, explanatory notes, and monthly stock exchange newsletters. The systematic elimination technique was used to select as many as 133 companies as the statistical sample. Descriptive and inferential statistics were used to describe and summarize the collected data. To analyze the data, initially, the Heteroscedasticity of Variance Pretests, the F-Limer Test, the Hausman Test, the Jarque-Bera Test, and then, the Multivariate Regression Test were used to confirm and reject the study hypotheses, using the EViews software. Findings showed that the volatility of economic policy uncertainties could positively and significantly affect accounting conservatism, with financial constraints moderating the relationship between the volatility of economic policy uncertainties and accounting conservatism. The results obtained in this study were found to correspond to the documents referred to in the study's theoretical framework and the finance literature.

Keywords: accounting conservatism, volatility of economic policy uncertainties, financial constraints.

INTRODUCTION

Accounting conservatism refers to the difference in selected and accepted policies over good

and bad news; by good news, it means positive returns on stocks or events that may increase a profit, whereas, by bad news, it means negative or zero returns on stocks or events that may decrease a profit. Here, conservatism is defined as the process of a decrease in profits and asset underreporting against bad news and the process of non-increase in profits and asset overreporting against good news (Rahmani et al., 2017). Following principles of accounting conservatism, firms recognize their losses on time but recognize their profits with a delay; this is what is called asymmetric timing, which has a conservative influence on profits (Louis et al., 2012). On the other hand, the global economy is suffering from an ongoing economic policy uncertainty caused by natural disasters, policies, and recently the COVID-19 pandemic. To respond to these uncertainties, researchers have begun studying real economic consequences, including uncertainty shocks, on financial markets. Mounting economic policy uncertainties could result in rising corporate value uncertainties, the withdrawal of securities traders from the market, and an acute shortage of liquidity (Nagar et al., 2019). However, research on the impacts of uncertainty of uncertainty on corporate decisions is still lacking. It is expected that bonds between uncertainty of uncertainty and accounting conservatism will be examined. Accounting conservatism requires a higher degree of verification to recognize good news as a profit against recognizing bad news as a loss - this is done by prudent profit recognition and sufficient and timely loss recognition. As an effective contract mechanism, accounting conservatism helps reduce informational asymmetry and agency costs, and thus protect the interests of investors and creditors.

Hui et al. (2012) concluded that customers and resources will require greater levels of accounting conservatism when greater levels of transparency are needed, reasoning that while accounting conservatism is not equivalent to financial transparency, it decreases demand for transparency when it exceeds the supply of transparency. Therefore, it is critical to deal with the relationship between uncertainty of uncertainty and accounting conservatism. Under uncertainty of uncertainty, information asymmetry between managers and creditors will rise, consequently prompting creditors to take more actions to constrain managers' opportunistic behavior and requiring greater disclosure to acquire real and accessible accounting information. Besides, facing higher financial constraints and equity commitments, creditors feel more vulnerable, thereby being more motivated to strengthen regulation over corporate financial information and promote accounting conservatism (Cui et al., 2023). The main question of the study is *"How would financial constraints moderate the relationship between the volatility of economic policy uncertainties and accounting conservatism?"*

The next sections will review Theoretical Foundations and develop hypotheses, as the Methodology section will also provide variables and findings.

THEORETICAL FOUNDATIONS AND LITERATURE REVIEW

Markets have been suffering from financial uncertainties following the global pandemic of Covid-19, escalating political party conflicts in the U.S., climatic changes, volatile energy prices, and Russia's invasion of Ukraine, making economic political changes unpredictably gloomy. This, in turn, has exacerbated the uncertainty of future levels of uncertainty or what is called "uncertainty of uncertainty" (Goodell et al., 2021). Unlike risks, uncertainty of uncertainty refers to an uncertainty that cannot be described by a certain probability measure. To elaborate on this, it is well known that uncertainty measures such as Baker et al.'s (2016) economic policy measures serve as variables and their future values may therefore involve uncertainties. It is also widely known that all techniques of estimating uncertainties are intrinsically subjected to model risks, i.e., "model uncertainty" or "Knightian uncertainty". In the meantime, research has examined the impacts of uncertainty of uncertainty on asset pricing (Anderson et al., 2009), valuation of options, variance premiums, capital investment, and cash holdings. Risk premiums of shareholders' equity also reflect Knightian uncertainty (Goodell et al., 2021). However, research on the impacts of uncertainty of uncertainty on corporate

decisions is still lacking. The present study aimed to examine the bonds between economic policy uncertainties and accounting conservatism to reveal the relationship between economic policy uncertainties and corporate governance. Accounting conservatism requires a higher degree of verification to recognize good news as a profit against recognizing bad news as a loss - this is done by prudent profit recognition and sufficient and timely loss recognition. As an effective contract mechanism, accounting conservatism helps reduce informational asymmetry and agency costs, and thus protect the interests of investors and creditors (Dai et al., 2021).

It was concluded that customers and resources will require greater levels of accounting conservatism when they demand greater levels of transparency. It was also reasoned while accounting conservatism is not equivalent to financial transparency, it would decrease demand for transparency when it exceeded the supply of transparency. Therefore, it is critical to deal with the relationship between uncertainty of uncertainty and accounting conservatism. As stated above, a contract demand plays a key role in the relationship between economic policy uncertainty and accounting conservatism. Under uncertainty of uncertainty, information asymmetry between managers and creditors will rise (Dai et al., 2021).

In firms that operate conservative accounting and auditing systems, managers have fewer opportunities to apply aggressive accounting procedures that may help manipulate the profits (Ghorbani & Pourtaher-Aghdam & Rahnamai Roudposhti, 2022), driving creditors to take more measures to restrict managers' opportunistic behavior and call for greater levels of disclosure to gain real and accessible accounting information. Besides, mounting financial constraints and stock commitments could make creditors more vulnerable. This will indeed prompt creditors to reinforce regulation over corporate financial information and encourage accounting conservatism (DeJong et al., 2020).

Therefore, the first hypothesis is formulated as follows:

First Hypothesis: The volatility of economic policy uncertainties has a bearing on accounting conservatism.

It is understood that the relationship between the volatility of economic policy uncertainties and accounting conservatism is well recognized. Research has shown that as uncertainties in economic policies increase, firms begin to adopt a series of more conservative accounting approaches, which is thought of as the firms' attempts to reduce unexpected profit reporting. Governments' uncertain future policies could make predicting financial outcomes more difficult. Under these circumstances, conservative companies work more cautiously to offer a more conservative image of their financial status, thereby refraining from recognizing revenue and assets unless they certainly become real. Financial constraints can moderate this relationship. In sum, companies with more financial constraints tend less to adopt conservative accounting approaches, as they heavily rely on more robust profit reporting to shore up their finances. Under economic uncertainty circumstances, firms suffering from financial constraints are more likely to adopt more aggressive accounting approaches to help maintain their access to capital. In sum, evidence indicates that the volatility of economic policy uncertainties and accounting conservatism are positively interrelated. However, this relationship can be moderated by financial constraints, as firms with more financial constraints are less willing to adopt conservative accounting approaches to deal with rising economic policy uncertainties.

As reasoned above, the second hypothesis is as follows:

Second Hypothesis: Financial constraints moderate the relationship between the volatility of economic policy uncertainties and accounting conservatism.

METHODOLOGY

This study fell under applied research and examined the effects of managers' overconfidence on the relationship between cash holdings and corporate excess returns on stocks. The data used in this study fell under historical or *Ex post facto* data examining the relationship between the variables based on past events. The study was also administered based on descriptive-correlational studies using mixed data and multivariate regression.

The statistical population of this study involved the companies listed on the Tehran Stock Exchange from 2014 to 2022. The systematic elimination technique was used to select as many as 133 companies as the statistical sample. Assumptions of classical regression included normality, lack of collinearity, reliability of variables, and heteroscedasticity of variance, while Chow and Hausman Tests, Durbin-Watson Statistics, coefficient of determination, adjusted coefficient of determination, and the F statistic were used to examine the relationship between the variables and the study hypotheses.

Study Models and Variables

To test the hypotheses, Kai et al.'s article (2023) was used to examine the first hypothesis based on Equation 1:

Equation 1:

$$\frac{\text{Earnings}_{i,t}}{\text{Accruals}_{i,t}} = \beta_0 + \beta_1 \text{Return}_{i,t} \times \text{vol epu}_{i,t} \times D_{i,t} \\ + \beta_2 \text{Return}_{i,t} \times \text{vol epu}_{i,t} + \beta_3 \text{Return}_{i,t} \\ \times D_{i,t} + \beta_4 \text{vol epu}_{i,t} \times D_{i,t} \\ + \beta_5 \text{vol epu}_{i,t} + \beta_6 D_{i,t} + \beta_7 \text{Return}_{i,t} \\ + \beta_8 \text{Size}_{i,t} + \beta_9 \text{LEV}_{i,t} + \beta_{10} \text{ROA}_{i,t} \\ + \beta_{11} \text{Cash}_{i,t} + \beta_{12} \text{Growth}_{i,t} + \beta_{13} \text{MB}_{i,t} \\ + \beta_{14} \text{FirmAge}_{i,t} + \epsilon$$

Equation 2 below is also used to examine the second hypothesis:

Equation 2:

$$\frac{\text{Earnings}_{i,t}}{\text{Accruals}_{i,t}} = \beta_0 + \beta_1 \text{Return}_{i,t} \times \text{vol epu}_{i,t} \times D_{i,t} \\ + \beta_2 \text{Return}_{i,t} \times \text{vol epu}_{i,t} + \beta_3 \text{Return}_{i,t} \\ \times D_{i,t} + \beta_4 \text{vol epu}_{i,t} \times D_{i,t} \\ + \beta_5 \text{vol epu}_{i,t} + \beta_6 \text{KZ}_{i,t} + \beta_7 \text{Return} \\ * \text{vol epu} * D * \text{KZ}_{i,t} + \beta_8 D_{i,t} \\ + \beta_9 \text{Return}_{i,t} + \beta_{10} \text{Size}_{i,t} + \beta_{11} \text{LEV}_{i,t} \\ + \beta_{12} \text{ROA}_{i,t} + \beta_{13} \text{Cash}_{i,t} + \beta_{14} \text{Growth}_{i,t} \\ + \beta_{15} \text{MB}_{i,t} + \beta_{16} \text{FirmAge}_{i,t} + \epsilon$$

The stated model involves the following:

Earnings

Accruals

Vol_epu: Volatility of economic policy uncertainty

D: Dummy variable for negative returns

Returns

Controls: Control variables include the following:

Corporate Size

LEV: [financial] Leverage

ROA: Return on Assets

Cash

Growth: Operational Growth

MB: The Market Value to Book Value

Firm Age: Corporate Life (Kai et al., 2023)

How variables are measured, continued:

Dependent Variable:

Earnings-to-Accruals Ratio

Earnings: Earnings are equivalent to a profit before extraordinary items to the capital market value (Kai et al., 2023).

Accruals: Accruals are equivalent to a profit subtracting operating cash flows (meaning operating cash flows minus net capital expenditure) to the capital market value (Ibid)

Independent Variable

The volatility of economic policy uncertainties equals the standard deviation of the macroeconomic uncertainty measure in the study (Ibid).

In this study, the variable used for the macroeconomic uncertainty is inflation rates; if the inflation suffers from the heteroscedasticity of variance in its model, the GARCH model is used to develop a proxy for unpredictable macro-economic variations which will be employed as a macro-economic uncertainty variable. As the following equation dictates, the conditional variance of the inflation, estimated in Equation 3 (GARCH), is considered as the macro-economic uncertainty proxy.

Equation 3

$$\Delta \text{inf}_t = \omega + \eta \Delta \text{inf}_{t-1} + \varepsilon_t$$

Equation 4

$$\sigma_t^2 = \alpha + \beta \varepsilon_{t-1}^2$$

ω represents a constant value, η represents the auto-regression parameter, ε represents the residuals and Δinf inflation rate variations; besides, α represents a constant value in the second model.

This model was estimated using the maximum likelihood estimation method; the resulting value of conditional variance $\hat{\sigma}_t^2$ serves as an index to measure macroeconomic uncertainties

(Sadeghi-Sharif, 2016).

Control Variables

The dummy variable for the negative returns: For the negative return (less than zero), it is equal to 1; otherwise, it is equal to 1 (Kai et al., 2023).

Returns on Stocks: Real returns on stocks of companies listed on the Tehran Stock Exchange were extracted from the “Rah Avard” Software, which is used to calculate stock returns using Equation 5 (Rahnamai Roudposhti, 2006):

Equation 5

$$r_i = \frac{P_{i,1} - P_{i,0} + \text{div}_{i,0}}{P_{i,0}}$$

Where $P_{i,1}$ is the price of stocks by the end of the period, and $P_{i,0}$ is the price of stocks at the beginning of the period.

$\text{div}_{i,0}$ is the dividend per share

Other **control variables** include the following:

Size: Corporate size is equal to the natural logarithm of the stock market value (Ibid)

LEV: Financial leverage is equal to the total debt-to-total assets ratio (Ibid)

ROA: Returns on stocks are equal to the net profit-to-book value of assets ratio (Ibid)

Cash: Cash flows are equal to the cash flow-to-total assets ratio (Ibid)

Growth: Operating growth is equal to the cash flow from the firm's operating activities to the book value of assets (Ibid)

MB: The market value to book value

Firm Age: The firm's age is equal to the natural logarithm of the number of years from its establishment (Ibid)

Moderating Variable

Financial constraints: Locally standardized by Tehrani and Hesarzadeh (2010), the financing constraints index (Kaplan & Zingales, 1997) is used to separate financially-restricted companies from other trading units, as noted in Equation 6:

Equation 6

$$KZ_{IR} = 17.330 - 37.486C - 15.216Div + 3.394Lev - 1.402MTB$$

C: Cash-to-asset ratio

Div: Dividend per share-to-assets

Lev: Debt-to-asset ratio

MTB: Ratio of a sum of the market value of shareholders' equity and the book value of debts to the book value of assets

To use this index, real values are first entered into the KZ index equation to calculate the KZ value. The values are arranged from the smallest to the largest and are then divided into five parts; thus, the company's existing in the fourth and fifth quintiles would be identified as suffering from financing restricting (Baradaran Hasanzadeh et al., 2014).

1. Findings

This study applied the data of 133 companies listed on the Tehran Stock Exchange from 2014 to 2022. The study examined data reliability using Levene's, Lin, and Chow Tests. Data reliability prevents false regression between variables. Before model estimation, variables are examined to ensure they are reliable. The probability of Levene's, Lin's, and Chow's Test statistics of all study variables was less than 0.05, underscoring that all the variables were reliable.

Constant Error Term Variance

This study examined the assumption of heteroscedasticity of variance of residuals through the LR Test, the results of which are shown in Table 1:

Table 1: LR Test

Models	Type of Statistics	Value of statistics	Probability
1	F statistic	907.0088	0.0000
2	F statistic	1023.187	0.0000

Source: (Researcher's findings)

Table 1 gives the significance level of the F statistic to be less than 5% for the study hypotheses, rejecting the hypothesis stating the homoscedasticity of variance in the hypotheses; therefore, the GLS method was used to estimate the test regarding the study hypotheses.

Correlation Analysis

The Pearson correlation coefficient was used to examine the pairwise linear relationship between the variables. In Table 2 below, the lower triangle shows the Pearson correlation coefficient, and the upper triangle the probability level of the relationship between the variables:

Table 2: Model pattern correlation results

Correlation	Earnings/ Accruals	Return* vol epu *D	Return * vol epu	Return *D	Return	D	Size	LEV	ROA	Cash	Growth	MB	Firm Age
Earnings/ Accruals	1												
Return* vol epu *D	0.009	1											
Return * vol epu	0.084	0.244	1										
Return *D	0.092	0.360	0.236	1									
Return	-0.102	0.137	0.469	0.444	1								
D	-0.096	-0.156	-0.280	-0.485	-0.492	1							
Size	0.126	-0.076	-0.005	0.025	0.219	0.066	1						

LEV	-0.177	-0.069	-0.080	-0.031	-0.164	0.051	0.105	1					
ROA	0.058	-0.002	0.016	0.023	0.012	-0.050	-0.005	-0.044	1				
Cash	0.219	-0.114	-0.011	-0.113	0.069	-0.011	0.045	-0.135	-0.005	1			
Growth	0.351	0.060	-0.046	0.055	0.050	-0.037	0.190	-0.191	0.002	0.071	1		
MB	-0.038	-0.085	-0.010	0.041	-0.017	0.01	0.102	0.056	0.002	-0.073	0.027	1	
Firm Age	-0.015	-0.027	-0.011	-0.046	-0.008	0.035	0.141	-0.030	-0.020	0.020	-0.038	0.012	1

(Source: Researcher's findings)

Table 2 shows when the correlation coefficient is less than 0.5, there is no collinearity between the independent variables.

Diagnostics Tests in Mixed Data

To determine the estimation method, the F-Limer and Hausman Tests were conducted for the model, the results of which are given in Table 3:

Table 3: F-Limer and Hausman Test results

Model	F-Limer Test	Sig.	Result	Hausman Test	Sig.	Result
1	14.058884	0.0000	Panel pattern	32.838550	0.0010	Fixed effects
2	14.616855	0.0000	Panel pattern	36.536923	0.0009	Fixed effects

(Source: Researcher's findings)

Table 3 gives models of Hypothesis 1 and 2 estimated in a panel pattern. If the model estimation is panel [effects], then one of the methods, either the fixed effects or random effects must be selected. As shown by the Hausman Test results, the model fit using the panel data model was based on the fixed effect method.

A Summary of Study Hypotheses Analysis

Table 6 below gives the results of testing the first hypothesis.

Table 6: Summary of Pattern 1 results

Variable Name	Symbol of Variable	Coefficients	Standard Error	T-statistic	Sig.	Result
Intercept	α_0	-0.238317	0.357035	-0.667491	0.5046	Non-significant
Interaction between returns on stocks and negative returns with the volatility of economic policy uncertainties	Return* vol epu *D	0.001077	0.000289	3.729977	0.0002	Positive
Interaction between returns on stocks and the volatility of economic policy uncertainties	Return * vol epu	0.000422	9.11E-05	4.636063	0.0000	Positive

Interaction between returns on stocks and negative returns	Return *D	0.0034 31	0.001026	3.344460	0.0009	Positive
The volatility of economic policy uncertainty	vol epu	0.0154 31	0.003242	4.758990	0.0000	Positive
Return on stocks	Return	- 0.0007 19	0.000347	- 2.071198	0.0386	Negative
Negative returns	D	- 0.0184 81	0.018686	- 0.989061	0.3229	Non-significant
Corporate size	Size	0.0324 14	0.008585	3.775875	0.0002	Positive
Financial leverage	LEV	- 0.1020 38	0.062227	- 1.639759	0.1014	Non-significant
Returns on assets	ROA	0.0090 65	0.002616	3.465527	0.0006	Positive
Cash flows	Cash	0.3611 18	0.021139	17.08276	0.0000	Positive
Operating growth	Growth	1.1543 58	0.073267	15.75551	0.0000	Positive
Market value-to-book value	MB	- 0.0052 67	0.001946	- 2.707331	0.0069	Negative
Firm age	Firm Age	0.0186 62	0.113597	0.164286	0.8695	Non-significant
Coefficient of determination		0.809582				
Adjusted coefficient of determination		0.783517				
F statistic		31.06035				
Sig.		0.000000				
Durbin-Watson		1.809485				

(Source: Researcher's findings)

Table 6 shows the probability of the t statistic of the fixed coefficient and coefficients of the variables of the interaction between returns on stock and negative returns and the volatility of economic policy uncertainties, the interaction between returns on stocks and economic policy uncertainty, the interaction between returns on stocks and negative returns, the volatility of economic policy uncertainty, returns on stocks, corporate size, returns on assets, cash flows, operating growth, and the market value-to-the book value ratio on accounting conservatism was found to be less than 5%. Hence, the above relationship was statistically significant. Since the coefficient of the variable of the volatility of economic policy uncertainties on accounting conservatism was statistically positive, the probability of the t statistic of coefficients of the variables of negative returns, financial leverages, and firm age on accounting conservatism was greater than 5%, indicating that the above relationship was not statistically significant. This means that the variables were non-significant in the model at a confidence rate of 95%. The adjusted coefficient represents the explanatory power of the independent variables, being capable of explaining variations of the dependent variable by as much as 78%. The F-statistic probability suggests that the entire model is statistically significant.

Here, the Durbin-Watson value is 1.81, which ranges from 1.5 to 2.5, confirming the independence of the model's residuals. Since the coefficient of the variable of the volatility of

economic policy uncertainties on accounting conservatism was positive and significant, the H_0 hypothesis was therefore rejected, suggesting that the volatility of economic policy uncertainties affected accounting conservatism.

The results of testing the second hypothesis are given in Table 7:

Table 7: Summary of Pattern 2 results

Variable Name	Symbol of Variable	Coefficients	Standard Error	T-statistic	Sig.	Result
Intercept	α_0	-0.045683	0.358376	-0.127471	0.8986	Positive
Interaction between returns on stocks and negative returns with the volatility of economic policy uncertainties	Return* vol epu *D	0.001968	0.000341	5.764528	0.0000	Positive
Interaction between returns on stocks and the volatility of economic policy uncertainties	Return * vol epu	0.000382	8.96E-05	4.260596	0.0000	Positive
Interaction between returns on stocks and negative returns	Return *D	0.003041	0.001029	2.955524	0.0032	Positive
The volatility of economic policy uncertainties	vol epu	0.013536	0.003205	4.223663	0.0000	Positive
Financial constraints	KZ	0.035782	0.020304	1.762292	0.0783	Non-significant
Interaction between financial constraints with the volatility of economic policy uncertainties	Return* vol epu *D *KZ	0.002713	0.000445	6.091396	0.0000	Positive
Returns on stocks	Return	-0.000593	0.000354	-1.678730	0.0935	Non-significant
Negative returns	D	-0.015976	0.018580	-0.859825	0.3901	Non-significant
Corporate size	Size	0.041154	0.009795	4.201578	0.0000	Positive
Financial leverage	LEV	-0.067752	0.062243	-1.088521	0.2766	Non-significant
Returns on assets	ROA	0.009058	0.002563	3.534632	0.0004	Positive
Cash flows	Cash	0.365349	0.021342	17.11886	0.0000	Positive
Operating growth	Growth	1.181570	0.073679	16.03681	0.0000	Positive
Market value to book value	MB	-0.006487	0.001859	-3.489021	0.0005	Negative
Firm age	Firm Age	-0.081419	0.118894	-0.684804	0.4936	Non-significant
Coefficient of determination		0.810102				

Adjusted coefficient of determination	0.783491
F-statistic	30.44224
Sig.	0.000000
Durbin-Watson	1.833622

(Source: Researcher's findings)

Table 7 shows the probability of the t statistic of the fixed coefficient and coefficients of the variables of the interaction between returns on stock and negative returns with the volatility of economic policy uncertainties, the interaction between returns on stocks and economic policy uncertainty, the interaction between returns on stocks and negative returns, the volatility of economic policy uncertainties, financial constraints interacting with the volatility of economic policy uncertainties, returns on stocks, corporate size, returns on assets, cash flows, operating growth, and the market value-to-the book value ratio on accounting conservatism was found to be less than 5%. Hence, the above relationship is statistically significant. Coefficients of the variables of the volatility of economic policy uncertainties and financial constraints interacting with the volatility of economic policy uncertainties on accounting conservatism were statistically significant at 0.0135 and 0.0027, respectively.

Since the coefficient of the variable of the volatility of economic policy uncertainties on accounting conservatism was found to be greater than that of the variable of financial constraints interacting with the volatility of economic policy uncertainties on accounting conservatism, it is thus concluded that the variable of financial constraints moderates the relationship between the volatility of economic policy uncertainties and accounting conservatism.

The probability of the t statistic of coefficients of the variables of financial constraints, negative returns, financial leverages, and the firm's age on accounting conservatism was greater than 5%, indicating the relationship is not statistically significant, with the models being non-significant in the model at a 95% level. The adjusted coefficient of determination indicates the explanatory power of the independent variables, being capable of explaining variations of the dependent variable by as much as 78%. The probability of the F-statistic represents that the entire model is statistically significant.

Here, the Durbin-Watson value is 1.83, which ranges from 1.5 to 2.5, confirming the independence of the model's residuals. Since coefficients of the variables of the volatility of economic policy uncertainties and financial constraints interacting with the volatility of economic policy uncertainties on accounting conservatism were statistically significant at 0.0135 and 0.0027, respectively, the H_0 hypothesis is rejected. This confirms that the variable of financial constraints moderates the relationship between the volatility of economic policy uncertainties and accounting conservatism.

DISCUSSION AND CONCLUSION

This study aimed to understand the role of financial constraints in the relationship between the volatility of economic policy uncertainties and accounting conservatism. As stated by the first hypothesis, it was concluded that the volatility of economic policy uncertainties positively and significantly influenced accounting conservatism. This indicated that under such circumstances, firms tend to move toward more conservative financial reporting. This approach is thus adopted due to increased risks and uncertainties in an economic environment. In the meantime, to reduce risks related to economic volatilities and prevent possible financial woes, managers tend to underreport revenues and overreport costs more than they are. The findings of this study corresponded to those of Kui et al. (2023) and Rezaei (2021).

As stated by the first hypothesis, it was concluded that financial constraints moderated the relationship between the volatility of economic policy uncertainties and accounting conservatism. This indicated that under severe economic volatilities, companies tend to move towards more conservative accounting approaches to manage the risks arising from uncertainties, which could help them prevent financial crises and better manage their financial status. If companies encounter severe financial restrictions, they may tend to accounting conservatism. This indicates that financing constraints could represent the credit state of a firm; hence, when an economic firm suffers from financing woes, the stakeholder will oblige the firm's director to employ a more conservative approach. This decision is taken in the wake of more difficult access to new funding, and existing funding has to be managed and controlled with more caution. Accounting conservatism could, under these circumstances, help reduce financing costs and increase creditors and investors' trust, which is key in financing constraints. The findings of this study were in line with those of Kai et al. (2023), Asadi et al. (2020), and Tari-Vardi et al. (2021).

The review of the first hypothesis suggests that the volatility of economic policy uncertainties affected accounting conservatism. Thus, corporate managers are recommended to adjust their financial strategies to reflect greater levels of conservative financial reporting when dealing with economic policies; this will help them reduce the risks that may arise from uncertainties. Also, firms are recommended to apply different scenarios to predict possible economic volatility impacts and devise financial programs, accordingly. Meanwhile, investors and stakeholders are recommended to pay more attention to analyzing economic risks and their impacts on financial reporting. They are also advised to make their policies based on these analyses.

The review of the second hypothesis suggests that corporate managers should be recommended to spend more time managing corporate finances and seek new financing techniques under harsh financing conditions. They are also suggested to increase financial reporting and increase the trust of investors and creditors while facilitating access to funding. Investors and stakeholders are also suggested to pay special attention to the financial state of their companies and the relevant impacts of financial constraints on corporate performance; they are also encouraged to choose the companies that demonstrate better performance when dealing with financial constraints.

Future research is recommended to investigate changes to the impacts of financial constraints in the relationship between volatile economic policy uncertainties and accounting conservatism over time and the role of corporate governance and ownership structure in moderating the impacts of economic policy volatilities and financial constraints on accounting conservatism. Meanwhile, more economic models are recommended to be developed to better measure and predict the impacts of economic uncertainty volatilities and financial constraints on accounting conservatism.

Conflict of Interest

The authors have no conflict of interest over this article with any person or organization.

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