Working Paper

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Income Smoothing as a Form of Accounting Policy by Managers

--A Case Study of Onward Kashiyama--

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June 2011

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Abstract

Firms often attempt to control fluctuations in reported earnings and steer them to levels they consider desirable. Either managing reported figures to increase earnings when management thinks its initially planned term-end settlement targets (smoothing level figures) cannot be achieved or managing reported figures to decrease earnings when achievement of earnings higher than planned is certain may be implemented during a given fiscal period. This type of management accounting behavior is called income smoothing or income smoothing behavior.

Provided that other conditions are identical, managers prefer smoothed income to income that fluctuates greatly. Smoothed income enables a firm to avoid discounting in the capital market owing to business performance fluctuation and simultaneously brings about desirable consequences with respect to institutional contracts the firm has entered into with stakeholders (financial covenants, delisting requirements, management compensation contracts, etc.).

Although there are various forms of earnings management, broadly speaking they can be divided into 1) technical accounting policy and 2) real discretion. Technical accounting policy refers to the practice by which management achieves its targeted

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figures in the settlement of accounts by changing accounting policies or accounting estimates. Real discretion refers to the practice by which management achieves its targeted figures in the settlement of accounts by changing contracts or transactions between the firm and its stakeholders.

In this case study, we consider the possibility that Onward Kashiyama, one of Japan's leading general apparel wholesalers, engages in income smoothing by means of accounting policy changes, a form of technical discretion. This case will make it possible to study the significance of accounting bias introduced by management and learn ways of removing that bias and linking that knowledge to financial analysis, the next step in corporate analysis. The purpose of this case study is to acquire the ability to eliminate bias incorporated into settlement figures and close in on the "true situation" in firms as a preliminary step to financial ratio analysis and enterprise value assessment.

Overview

In the apparel industry, in which Onward Kashiyama[3] operates, the term apparel refers to clothing in general. Although the original meaning of the English word "apparel" is to attire in proper clothing, in contemporary Japanese it generally refers to western clothing or western styles of dress as opposed to Japanese clothing or Japanese styles of dress and has become a concept that includes undergarments and such. In this sense of the word, the apparel industry is an intimate presence in our daily lives.

However, during the past two decades and more, public opinion of the apparel industry has been by no means overoptimistic; at times the industry is described in terms such as "An industry that will only continue to decline" (Yamaguchi et. al 1997, pp. 10-14). Japan's apparel industry is an extremely large market; in 2007 annual merchandise sales were approximately ¥16.64 trillion, and the number of employees was approximately 270,000. However, the apparel industry has been shrinking each year since the 1990s. Above all, as shown in Figure 1, annual merchandise sales have continued to decrease since peaking at approximately ¥38.52 trillion in 1991. So competition is intensifying as firms compete for pieces of a continually shrinking pie.

Moreover, since the impact of various risks, as typified by the effect weather can have on seasonal clothing sales, is extreme in the apparel industry, firms must have stable management to cope with risk. Within the apparel market, the women's wear sector in particular (a sector in which Onward Kashiyama offers many brands) is one in which a

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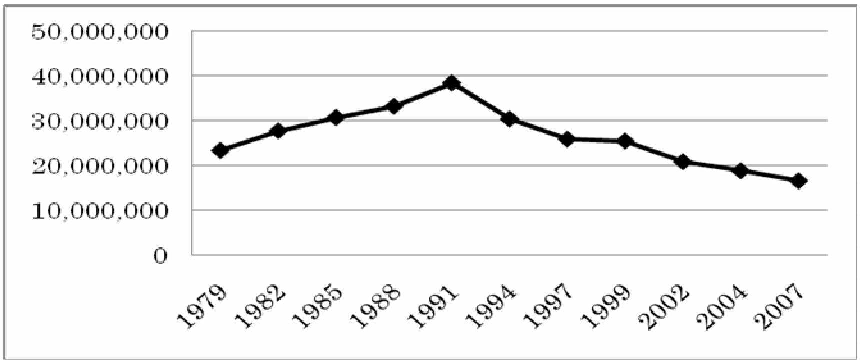
[3] Although the company name as of 2009 is Onward Holdings Co., Ltd., we use Onward Kashiyama, the company name at the time of main period subject to analysis in this case study: the five-year period from the fiscal year ended February 2003 (from March 2002 to February 2003) to the fiscal year ended February 2007 (from March 2006 to February 2007).

Figure 1 Change in Annual Merchandise Sales Value in the Apparel Industry

(Hundred Thousands of Yen)



Source : Prepared by the authors based on the Ministry of Economy, Trade and Industry (2008) *Results of the Census of Commerce for 2007*

firm can obtain enormous profit by releasing hit products but in which fashions change at a furious pace and misjudgment of trends can leave a firm with huge amounts of unsold inventory. In these circumstances, stability in business results is of great value to any given firm.

Background

Onward Kashiyama, the subject of analysis in this paper, was founded in 1927 by Junzo Kashiyama under the company name Kashiyama Shoten. At that time the firm had capital of ¥1,000, and its business was the import and sale of products ranging from skis, climbing gear, and other sporting goods to sundry goods for daily use, such as cosmetics and perfume. However, several years after the founding of the company, light industry in Japan suddenly grew in power, and domestic goods started to replace imported products within a year after their introduction. Accordingly, Junzo Kashiyama gave up on importing and focused his attention on the manufacture of textile products as a consumer goods business. He outsourced the products and sold them to department stores and the like. That marked the first step toward the firm’s current clothing manufacturing and wholesaling business and became the foundation of the Onward Kashiyama of today.

With the outbreak of the Second World War, ready-to-wear companies became subject to the repercussions of a controlled economy and were concentrated into about 100 agencies under the Enterprise Readjustment Ordinance. Although clothing controls continued even after the war, Kashiyama Shoten changed its name to Kashiyama Co., Ltd., obtained a loan from Sumitomo Bank, and undertook preparations for the subsequent period of deregulation, devoting itself to technological innovations such as the introduction of a Hoffman press in the business suit manufacturing process. Then, following the removal of clothing controls in 1951, Junzo Kashiyama conducted three experiments and introduced three key management policies. The three experiments were a consignment system for transactions with department stores, the dispatch of employees to department stores on Saturdays and Sundays, and the introduction of the semi-tailored suit system. The three key policies were financial structure reinforcement by means of rigorous financial control, the segregation of manufacturing and sales through the use of medium-sized “captive” subcontract factories, and a policy of emphasizing Tokyo.

Subsequently, Kashiyama Co., Ltd. grew steadily and in 1960 listed its shares on the Second Section of the Tokyo Stock Exchange, Osaka Securities Exchange, and Nagoya Stock Exchange with Nomura Securities as the lead manager. Following a succession of capital increases, in July 1964 the firm listed its shares on the First Section of the three exchanges.

The firm changed its name from Kashiyama Co., Ltd. to the current Onward Kashiyama in 1988. The firm had made a trademark registration of the name in 1951 because Junzo Kashiyama fondly remembered the hymn “Onward, Christian Soldiers,” which the Mitsukoshi Department Store youth band performed when Junzo Kashiyama worked there in his youth. It was at this time that the foundation of the organizational structure of today’s Onward Kashiyama was completed as the firm streamlined its production system and inventory control and constructed a system that allowed rapid response. Also, for about the past decade the firm has set forth its Brand-Leveraged Management strategy and implemented a responsibility framework in keeping with the management organization it has developed based on that strategy. Brand-Leveraged Management refers to a basic strategy centered on the firm’s brands. Its aim is to maximize brand value. The objectives are core brand reinforcement and management efficiency improvement, and by extension, stable profit expansion in Japan[4].

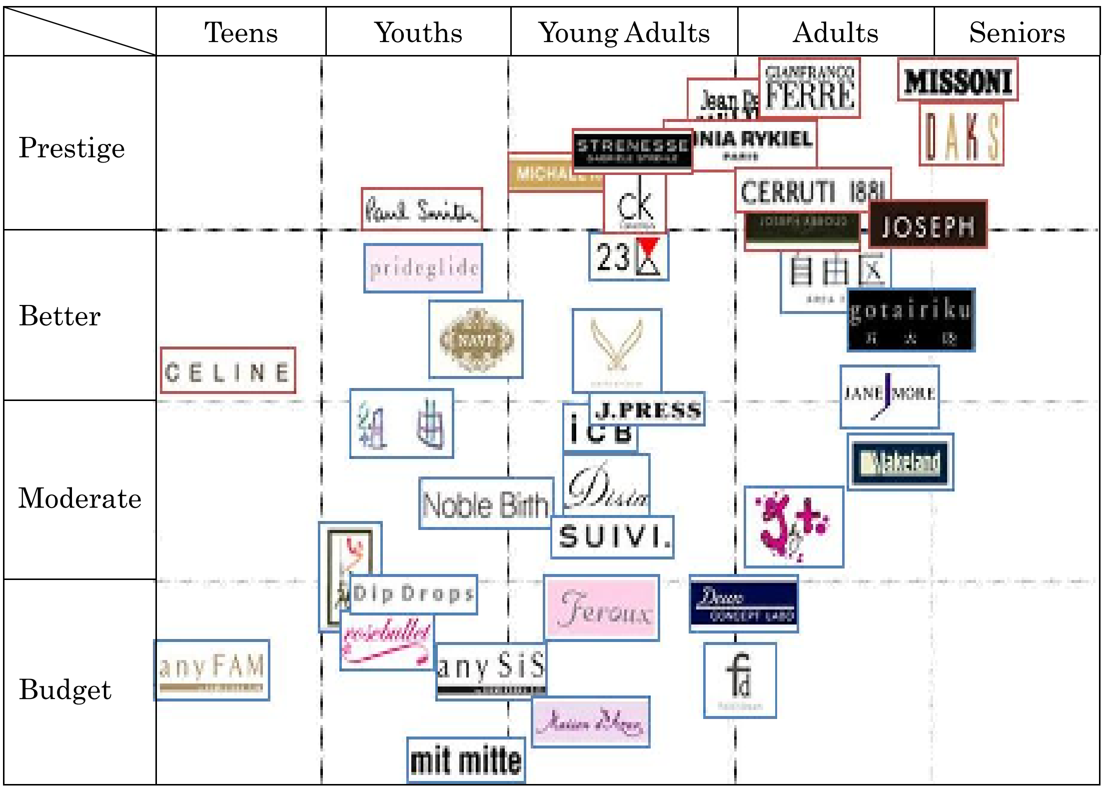
Onward Kashiyama’s stability-oriented management policy and management strategy are also apparent in the brands the firm offers. Figure 2 shows a classification of its major brands by mind grade. “Mind” here indicates attitudinal age rather than actual age and is divided into five categories: teens age 17 and under, youths age 18 to 24, young adults age 25 to 34, adults age 35 to 49, and seniors age 50 and over. “Grade” refers to quality level, and the graph clearly expresses the price range of the brand in question. Brands are broadly divided into four grades, ranging from Prestige for highly

[4] Refer to the IR Library section of the Onward Holdings Co., Ltd. website.

desired brands, to Better, Moderate, and Budget for brands in comparatively low price ranges.

As seen in Figure 2, the brands follow a nearly straight upward-sloping line. That is to say, overall, the lower the age band, the lower the grade, with grade increasing as age increases. This corresponds with ordinary apparel retail merchandise categories (Human Resource Development Research Committee, Apparel Retail Subcommittee [1993], pp. 165-171). We can surmise that firms in the highly risky, unstable apparel industry constantly strive to maintain stable business performance by positioning various brands in this way. Furthermore, in the case of Onward Kashiyama, it is possible that the firm differentiates the use of original brands (brand logos in blue boxes shown in Figure 2) and licensed brands (brand logos in red boxes in Figure 2). The firm sells original brands at lower price ranges than licensed brands and sells them at mass merchandisers and other outlets as well as department stores. On the other hand, it seeks differentiation for licensed brands by selling them through distribution channels

Figure 2 Classifications of Major Brands by Mind Grade



Source: Prepared by the authors based on the Human Resource Development Research Committee, Apparel Retail Subcommittee [1993] and Onward Kashiyama's annual securities reports limited to department stores and other prestigious outlets. Employing a differentiation strategy that occupies a major position in Brand-Leveraged Management, the firm regards each individual brand as a cash-generating unit and has put in place a framework for reliably pursuing earnings.

The Accounting Problem

Income smoothing has long been discussed as a management tactic. Here, income smoothing refers to "The equalization of income in each period to a certain level" (Itoh [2007], p. 207). That is to say, it is behavior to curb fluctuations in income and cause income to approach the level where management's utility is maximized (Copeland [1968]). More specifically, management reduces income in periods when business performance is favorable and income is comparatively high and, by contrast, contrives to create income in periods when business performance is unfavorable and income is comparatively low (Beidleman [1973], Ronen and Sadan [1981], Lambert [1984]).

Monetary compensation, management's reputation, and other factors have been mentioned as motivations for income smoothing. Its use has also been explained from the standpoint of economic rationality (Obinata [2007], Scott [2006]). That is to say, capital cost is expected to decrease if reported earnings have been smoothed (Lev and Kunitzky [1974]). Put in other words, investors rate firms having small fluctuations in earnings higher than firms that having large fluctuations in earnings, and investors presumably provide more capital for smoother earnings flows (Ronen and Sadan [1981], Trueman and Titman [1988]).

The common origin of these diverse motivations is the psychological consideration that "People dislike extreme uncertainty and complexity." (Tomita [2004], pp. 19-21). Accordingly, it can be said that all firms have universal incentives for income smoothing. Furthermore, as previously noted, the impact of various risks is especially high in the apparel industry. The following are examples of risks specific to the apparel industry. First, in the apparel industry product life cycles are exogenously applied, and the value of products declines precipitously at the end of the season. Second, since changes in fashionability characteristic of the industry have rapidly accelerated in recent years, attendant market uncertainty has increased. Third, by reason of frequent new market entries and departures, the industry as a whole is in a state of severe competition, and business performance in a single season greatly affects business success or failure (Choi and Matsuo [2002], pp. 243-244). Conversely, the fact that a firm's ability to avoid these risks characteristic of the apparel industry is reflected in business performance means that the maintenance of stable business performance is vital to firms.

Managers have many methods for actually engaging in various discretionary behaviors, including income smoothing. Itoh [2007][5] proposes technical accounting policies and material accounting policies as a classification framework for those methods. With technical accounting policies, managers "manipulate the accounting figures themselves (the output) without changing actual business activities" (Itoh [2007], p. 197). That is to say, in cases where multiple accounting policies exist and their selection is permitted as an accounting practice, managers select one of those policies or change from one policy to another or engage in manipulation of the inter-period allocation of various accounting figures[6]. Material accounting policies employ "not direct manipulation of the accounting figures (the output) themselves, but rather indirect control of the accounting figures by means of control of the business activity vectors that are the basis for the figures" (Itoh [2007], p. 198). There exist a wide variety of techniques for this, examples of which are channel stuffing to subsidiaries and affiliates, increasing or curtailing expenditures for advertising and publicity costs, R&D costs, and the like, and business restructuring. Also, a firm's accounting figures vary attendant to the manipulation of the firm's circumstances as a result of these behaviors.

Accounting data in the form of annual securities reports and other financial reports, summary statements of financial results, and annual reports are used for the purpose of external analysis of these accounting policies[7]. Of particular importance, the significant accounting policies selected by firms are presented in the Financial Overview section of annual securities reports. Confirmation and assessment of these policies can be considered to be the first step in analysis. Then, as much as possible, analysts eliminate the bias in accounting figures applied through the arbitrary selection of accounting policies, back calculate, and adjust the reported figures. Although it is extremely difficult to remove all bias using only externally disclosed available materials, by making this adjustment the analyst at the very least gets a glimpse of these technical accounting policies (Sakurai [2007]), and it becomes possible to close in on firms' real situations (Palepu et al. [2000]).

[5] At times these methods are classified using the expressions "accounting techniques" and "non-accounting techniques." (Obinata [2007], p. 259). However, the meaning is nearly the same. Also, Suh [1990] classifies income smoothing into "accounting income smoothing" and "real income smoothing."

[6] It is not the case that all instances of accounting policy selection or change or manipulation of inter-period allocation are matters of accounting policy. Of course, some instances of this behavior are for the purpose of accurately expressing the circumstances of firms.

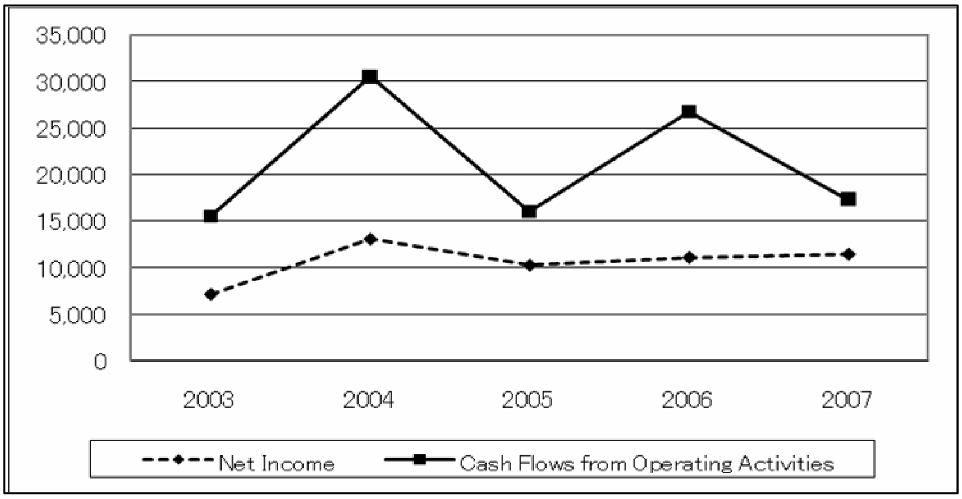
[7] Of course, to conduct exhaustive analysis, one should consider all available materials from outside sources, not only materials issued by firms. Specific examples of information from outside sources useful in analysis are analysts' earnings forecasts and share prices.

Required

Returning to the case of Onward Kashiyama, we have confirmed that sufficient motivation exists for the firm to record stable earnings each period, i.e., to engage in income smoothing. That being the case, has Onward Kashiyama actually applied an income smoothing policy?

Figure 3 Change in Cash Flows from Operating Activities and Net Income

(Millions of Yen)



Source：Prepared by the authors based on Onward Kashiyama's annual securities reports

Figure 3 shows changes in Onward Kashiyama's cash flows from operating activities and net income for the fiscal year ended February 2003 to the year ended February 2007. The figure shows that both cash flows from operating activities and net income show nearly no fluctuation and are comparatively stable. Cash flows from operating activities include eight items: 1) profit from income statements, 2) non-cash profit and loss items, 3) adjustments for changes in assets and liabilities related to operating activities, 4) profit and loss items arising in connection with cash flows from investing and financing activities, 5) items of decrease in surplus, 6) adjustments for interest and dividends received and interest paid, 7) adjustments for transactions other than investing and financing activities, and 8) adjustments for corporate tax, etc. When profit and loss items arising in connection with cash flows from investing and financing activities (which are gains and losses on the sale of tangible fixed assets and investment securities) are excluded, nearly all cash flows for transactions that fall under the category of profit and loss fall under cash flows from operating activities. These cash flows from operating activities include not only the operating profit and loss items sales, cost of sales, and S&G expenses, but even items ranging from non-operating profit and loss items such as interest received and interest paid to extraordinary profit and loss items such as insurance claims and compensation for damage as well as corporate taxes. (Kaneko and Todoroki [1999], Ernst & Young ShinNihon [2002]). For this reason, under ordinary circumstances it is unnatural for movement in cash flows from operating activities and movement in net income to differ substantially and it seems strange for net income to show a nearly uninterrupted increase even as cash flows from operating activities fluctuate, as shown in Figure 3. To be sure, it cannot be categorically stated on this basis alone that the management of Onward Kashiyama engages in income smoothing. However, it is a fact that in many cases there is no cash evidence of earnings being skewed by management's accounting policies (Itoh [2008]), but the evidence above is probably sufficient reason for suspicion that the firm practices income smoothing. This is because cash flow can be more objectively ascertained than earnings, which may change depending on accounting policy and other factors (Nishiyama [2006]). If we suppose that management is deliberately controlling earnings, the significance of removing that bias and ascertaining the actual circumstances of the firm is great. Accordingly, we will perform accounting analysis principally using Onward Kashiyama's annual securities reports.

The accompanying notes to financial statements are utilized to perform accounting analysis to accurately grasp the circumstances of a firm. The notes "record important matters related to information recorded in the body of the financial statements in different locations using words and figures" (Sakurai [2007], p. 312). The notes indicate the accounting policies chosen by firms and, when changes in accounting policies have been made, provide notice of the changes and explain the reasons for and impact[8] of the changes (Article 8, paragraph 3 of the Regulations Concerning Financial Statements; Article 132, paragraph 2 of the Corporate Accounting Regulations).

Confirmation section 5 Financial Overview 1) Consolidated Financial Statements of Onward Kashiyama's annual securities report indicates that accounting policy changes were implemented concerning the following six items[9].

1) Increases in consolidated subsidiaries and equity method affiliates
2) Depreciation and amortization of property, plant and equipment

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8 Impact refers to the difference between the amount of income, etc. attributable to the post-change accounting policy and the amount of income, etc. that would have been recorded if the same accounting standard applied the previous fiscal year had been applied. That is, in principle, except in minor cases, the difference produced by the modified accounting policies is expressed.

9 In addition, in its audit report ChuoAoyama Audit Corporation expressed the unqualified opinion that from an audit standpoint these accounting policy changes had valid reasons.

3) Partial cancellation of retirement benefit trust

4) Accounting standards concerning impairment of fixed assets

5) Accounting standards concerning bonuses to directors and statutory auditors

6) Accounting standards concerning stock options

The number of consolidated subsidiaries and equity method affiliates is increasing each fiscal year. For instance, the firm made the twenty companies of the JOSEPH Group consolidated subsidiaries in the fiscal year ended February 2006. In the fiscal year ended February 2007, the firm not only made 19 subsidiaries in Europe, Asia, and North America consolidated subsidiaries, it also added the 21 companies of the Daidoh Limited Group to its equity-method affiliates. This can be considered a strategic move for the purpose of establishing a pure holding company in September 2007. As for depreciation and amortization of property, plant and equipment, although there was a change in useful life, the method applied remained the straight-line method.

With regard to the retirement benefit trust, the firm recorded an extraordinary gain in the fiscal year ended February 2007 in an amount corresponding to the returned portion of the unrecognized actuarial difference with respect to trust assets at the time of return of retirement benefit trust assets on account of the trust being overfunded owing to assets exceeding liabilities.

Onward Kashiyama has instituted a corporate pension fund plan, a qualified pension plan, and a termination allowance plan as defined contribution schemes. On January 1, 2006 the firm obtained permission from the Minister of Health, Labour and Welfare for the return of the substitutional portion of the employees' pension fund. However, since the fact that approval was received is recorded in the financial statements for the fiscal year ended February 2006 and overfunding in an equivalent amount had already occurred in the fiscal year ended February 2006, we decided that an adjustment[10] should be made on the grounds that by rights, accounting treatment of this termination should have occurred in the fiscal year ended February 2006.

With regard to accounting standards concerning impairment of fixed assets, Onward Kashiyama applied the standards in the fiscal year ended February 2007. Although net income before tax and other adjustments decreased by ¥16,967 million owing to the impact of the application of the standards, since the implementation of impairment accounting in the business year beginning on or after April 1, 2005 was a regulatory requirement, it is likely that the accounting treatment was applied in conformance with the requirement. In addition, with regard to asset grouping, although the firm combines by-brand grouping and grouping for each individual asset, this conforms with the previously noted Brand-Leveraged Management strategy. The firm also applied accounting standards concerning bonuses to directors and statutory auditors in the fiscal year ended February 2007, and operating income, ordinary income, and net income before tax and other adjustments decreased by ¥516 million. Since this too was applied in the business year that began following the date of enforcement of the Companies Act, it can be called a change in accounting treatment in conformance with a new accounting standard. Accounting standards concerning stock options were also applied in the fiscal year ended February 2007. However, since the report states "The impact of this change on profit and loss is negligible," we decided to disregard this change.

Furthermore, although these matters don't fall under the rubric of accounting policy change, with regard to finance leases other than those for which ownership of the leased property is recognized as transferring to the lessee in the lease transaction (finance

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[10] Specifically, we presume that journalization such as the following was performed in accordance with explanatory example 7-2 of the Practical Guidelines on Accounting Standards Concerning Retirement Benefits "Treatment When Retirement Benefit Trust Assets in Trust Are Returned Due to Overfunding," and have made adjustments to securities, accrued retirement benefits, and others (prepaid pension cost, etc.).

Accounting Treatment When Retirement Benefit Trust Assets in Trust Are Returned to the Business Operator Due to Overfunding

Securities	XXX	/	Securities held in trust	XXX
Securities held in trust	XXX	/	Accrued retirement benefits	XXX
Retirement benefit cost	XXX	/	Accrued retirement benefits	XXX
Accrued retirement benefits	XXX	/	Prepaid pension cost	XXX

leases without ownership transfer) the firm applies accounting treatment consistent with that for rental transactions (lease accounting treatment). We also confirmed that the firm engages in the buying and selling of other securities each period. For this reason, we added an adjustment for these matters to more closely approach the actual circumstances of the firm.

First, with regard to the method of treating lease transactions, Onward Kashiyama applies lease accounting treatment to finance leases without ownership transfer. However, according to Corporate Accounting Standard No. 13 issued on March 30, 2007, lease accounting treatment of finance leases without ownership transfer, which is an exceptional accounting treatment, is not permitted and sales/purchase treatment is uniformly applied to such transactions. Accordingly, we decided to adjust Onward Kashiyama's treatment of lease transactions from lease accounting treatment to sales/purchase treatment and recognize lease assets and lease liabilities on the balance sheets. Since the firm applied lease accounting treatment not only in the fiscal year ended February 2007, but also in previous years, we made the adjustment for the entire five-year analysis period.

Also, with regard to other securities, although by rights these are so-called "cross-held shares" held for the purpose of business alliances, etc. or securities held for the purpose of earning profits from long-term change in share prices, Onward Kashiyama engaged in buying and selling each period. In such cases, the securities in question are probably closer in nature to trading securities than other securities. For this reason, we decided to include securities other than securities related to unconsolidated subsidiaries and securities with no market value (that is, securities for which no market exists) in the Securities account, which is in the Current Assets section[11]. Accordingly, with regard to the net unrealized gain (loss) on other securities, we adjusted non-operating profit and loss on the statements of income to reflect gain (loss) on revaluation of securities.

The change in figures before and after these adjustments is shown in Fig. 4-1 and Fig. 4-2.[12] As we see from Fig. 4-1 and Fig. 4-2, fluctuation in net income is greater in the adjusted figures. Also, we can see changes in the adjusted figures for not only net income, but also ordinary income. Although when comparing Fig. 4-1 and Fig. 4-2, net income for the fiscal year ended February 2006 and the fiscal year ended February 2007

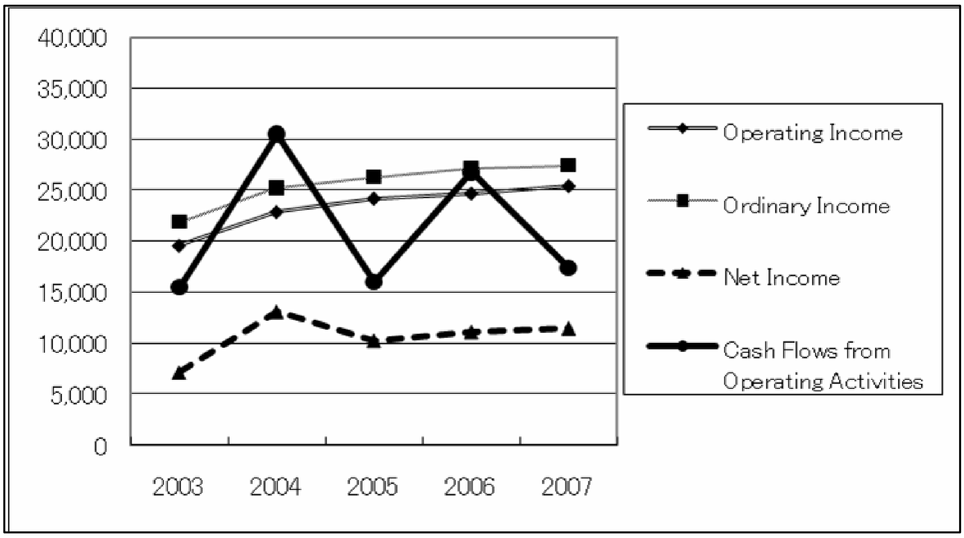
[11] The transfer of other securities to trading securities is prohibited by regulation "In cases where an entity begins securities trading transactions owing to change in fund management policies or to the revision or application of laws or standards" or "In cases where it is objectively determined that an entity engaged in frequent repeated buying and selling of securities" (Practical Guidelines on Accounting Standards for Financial Instruments 83, 86).

[12] We have not included gross profit, because there is no change to the figures before and after adjustment.

show particularly large adjustments, the change in the slope of the line for net income before and after the fiscal year ended February 2004 is also somewhat sharp, and the movement in net income resembles that for cash flows from operating activities.

Figure 4-1 Unadjusted Income Items and Cash Flows from Operating Activities

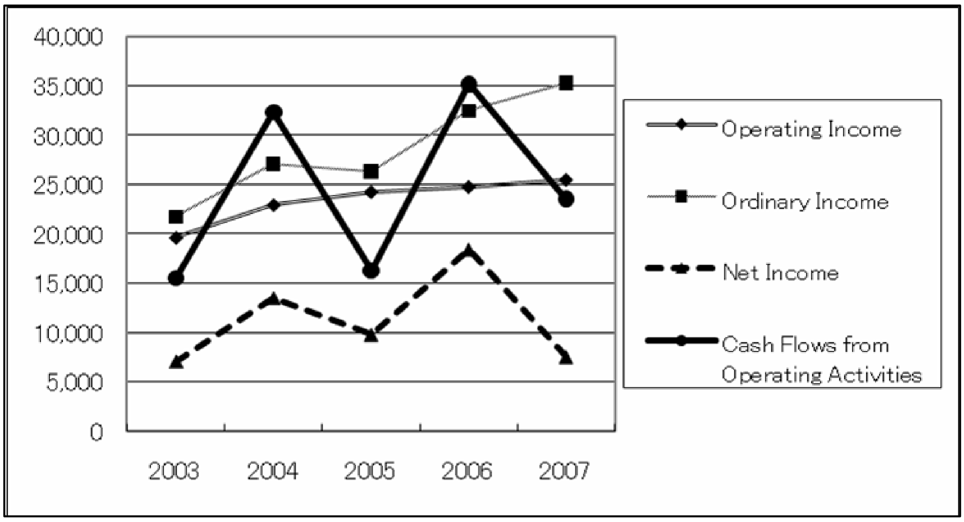
(Millions of Yen)



Source: Prepared by the authors based on Onward Kashiyama's annual securities reports

Figure 4-2 Adjusted Income Items and Cash Flows from Operating Activities

(Millions of Yen)



Source: Prepared by the authors based on Onward Kashiyama's annual securities reports

From the above, it has become clear that the management of Onward Kashiyama may be inclined to perform income smoothing. Since the firm introduced stock options in the fiscal year ended February 2007, this cannot be an incentive for income smoothing during the period of analysis. Nevertheless, as mentioned above, the apparel industry is an extremely unstable industry fraught with risk. In such circumstances, great significance is attached to being the only firm to consistently record earnings at a certain level. The information value of accounting information bias itself is presumably revealed in this piece of information.

Finally, we will consider how investors or markets evaluate changes in Onward Kashiyama's business performance. Figure 5 shows the change in Onward Kashiyama's share price over a five-year period.

Figure 5 Onward Kashiyama Share Price 2002-2007

Source: Yahoo! Finance 8016

http://quote.yahoo.co.jp/q?s=8016.t&d=c&k=c3&a=v&p=m130,m260,s&t=5y&l=off&z=m&q=c&h=on

Comparing Figure 5 with Figure 4-1 and Figure 4-2 enables us to confirm that the change in share price more closely resembles the change in the adjusted figures in Figure 4-2. That is to say, if we assume that the adjusted figures show the reality at Onward Kashiyama, we can surmise that the markets see through the situation to a considerable degree.

Learning Objectives

The following four points can be learned from this case study.

1. We can learn that there is no single measure of earnings and that earnings can be

changed. We can also learn the technical accounting policy of management with respect to earnings accounting.

2. We can learn what should be examined to make accounting analysis possible and remove bias or noise introduced into accounting figures through accounting policy.
3. Through concept 2 above, we can grasp the information value that bias itself can carry.
4. We can examine whether or not the markets have correctly evaluated a firm's business performance through comparison of the accounting figures with share price.

Questions

1. A certain businessman argues, "If a firm's current period cash flow is lower than current period earnings, the firm is unworthy of investment." What do you think about that opinion?
2. If we suppose that the firm in question has sharply reduced net income (or recorded a loss) in a following period, what does that mean?
3. If you were a stakeholder[13] of the firm in question 2 and received an explanation about this information from management at a general meeting of shareholders, what sort of questions would you ask management?
4. It is said that income smoothing by means of accounting policy change is a common occurrence. What examples can you think of in other industries?

Appendix

The following is a list of the figures used in the accounting analysis in this paper and the financial analysis measures before and after adjustment. Figures that changed due to adjustment are shown in red and those that did not change are shown in black. A comparison with two other apparel firms, Renown and Sanyo Shokai, is also included for use in cross-section analysis of financial indicators. The reasons for selection of Renown and Sanyo Shokai as firms for comparison are that both are multi-brand general apparel wholesalers like Onward Kashiyama that rank high in sales value among listed companies in that business. In addition, since in March 2004 Renown shifted to a pure holding company structure together with D'urban Incorporated, we

[13] Many perspectives can be considered, including those of shareholders, institutional investors, business partners, and employees. Consider the question from each of these stakeholders' points of view.

treat only data for the three-year period from the fiscal year ended February 2005 to the fiscal year ended February 2007.

Before Adjustment	2003	2004	2005	2006	2007
Sales	263,398	267,745	271,273	283,110	318,690
Gross Profit on Sales	120,165	123,825	124,825	131,068	142,895
Operating Income	19,607	22,895	24,205	24,707	25,431
Ordinary Income	21,897	25,243	26,283	27,167	27,407
Net Income	7,157	13,053	10,256	11,091	11,438
Business Income	19,797	23,068	24,387	24,983	26,024
Interest Expense	149	127	101	294	849
Current Assets	141,467	165,930	150,968	135,769	135,196
Receivables	28,836	31,463	25,776	27,449	32,144
Inventories	25,133	26,158	27,410	31,116	37,097
Quick Assets	108,027	119,562	107,597	83,585	89,697
Fixed Assets	160,720	152,339	157,201	193,634	212,739
Tangible Fixed Assets	101,188	96,017	96,394	99,687	94,850
Gross Assets	302,187	318,270	308,170	329,403	347,936
Total Capital Employed	241,878	256,892	245,518	258,050	252,950
Current Debt	80,147	92,270	79,025	97,617	103,493
Fixed Debt	13,044	11,434	9,890	10,186	19,304
Debt	93,191	103,704	88,915	107,803	122,798
Equity	190,754	196,796	202,376	203,826	203,846
Cash Flows from Operating Activities	15,501	30,514	15,992	26,758	17,362

(Millions of Yen) Source: Prepared by the authors based on Onward Kashiyama's annual securities reports

After Adjustment	2003	2004	2005	2006	2007
Sales	263,398	267,745	271,273	283,110	318,690
Gross Profit on Sales	120,165	123,825	124,825	131,068	142,895
Operating Income	19,627	22,918	24,227	24,730	25,448
Ordinary Income	21,718	27,068	26,285	32,463	35,269
Net Income	7,081	13,523	9,800	18,432	7,521
Business Income	19,817	23,091	24,409	25,006	26,041
Interest Expense	149	127	101	294	849
Current Assets	144,120	169,442	159,114	154,271	177,774
Receivables	28,836	31,463	25,776	27,449	32,144
Inventories	25,133	26,158	27,410	31,116	37,097
Quick Assets	110,649	123,041	115,710	110,219	132,042
Fixed Assets	160,189	150,415	148,859	176,119	164,193
Tangible Fixed Assets	103,132	97,863	97,897	100,997	96,455
Gross Assets	304,309	319,857	307,973	330,470	341,967
Total Capital Employed	246,474	262,249	255,166	277,860	297,132
Current Debt	80,960	93,093	79,745	98,207	104,186
Fixed Debt	14,255	12,534	10,695	8,616	20,376
Debt	95,215	105,627	90,440	106,823	124,562
Equity	190,853	196,461	200,655	205,875	196,113
Cash Flows from Operating Activities	15,505	32,286	16,239	35,167	23,521

(Millions of Yen) Source: Prepared by the authors based on Onward Kashiyama's annual securities reports

Before Adjustment	2003	2004	2005	2006	2007
Gross Margin Ratio	45.62%	46.25%	46.01%	46.30%	44.84%
Operating Income Ratio	7.44%	8.55%	8.92%	8.73%	7.98%
Ordinary Income Ratio	8.31%	9.43%	9.69%	9.60%	8.60%
Net Income Ratio	2.72%	4.88%	3.78%	3.92%	3.59%
Return on Assets	2.37%	4.10%	3.33%	3.37%	3.29%
Return on Investment	8.18%	8.98%	9.93%	9.68%	10.29%
Return on Equity	3.75%	6.63%	5.07%	5.44%	5.61%
Total Assets Turnover	0.87	0.84	0.88	0.86	0.92
Tangible Fixed Assets	2.60	2.79	2.81	2.84	3.36

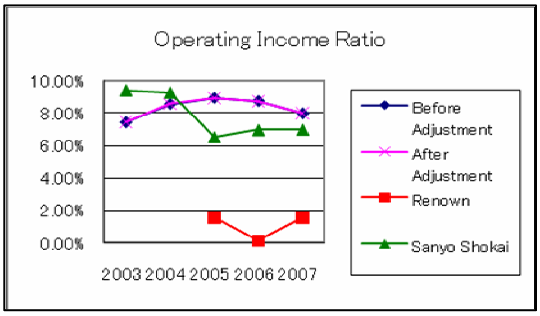
Turnover					
Inventories Turnover	10.48	10.24	9.90	9.10	8.59
Inventories Turnover Period	34.83	35.66	36.88	40.12	42.49
Receivables Turnover	9.13	8.51	10.52	10.31	9.91
Receivables Turnover Period	39.96	42.89	34.68	35.39	36.81
Current Ratio	176.51%	179.83%	191.04%	139.08%	130.63%
Acid Test Ratio	134.79%	129.58%	136.16%	85.63%	86.67%
Equity Ratio	63.12%	61.83%	65.67%	61.88%	58.59%
Debt Equity Ratio	48.85%	52.70%	43.94%	52.89%	60.24%
Fixed Assets Ratio	84.26%	77.41%	77.68%	95.00%	104.36%
Fixed Assets to Fixed Debt Ratio	78.86%	73.16%	74.06%	90.48%	95.33%
Interest Coverage Ratio	132.87	181.64	241.46	84.98	30.65
Sales - Growth Rate	100.00%	101.65%	102.99%	107.48%	120.99%
Operating Income - Growth Rate	100.00%	116.77%	123.45%	126.01%	129.70%
Net Income - Growth Rate	100.00%	182.38%	143.30%	154.97%	159.82%
Total Assets - Growth Rate	100.00%	105.32%	101.98%	109.01%	115.14%
Equity - Growth Rate	100.00%	103.17%	106.09%	106.85%	106.86%

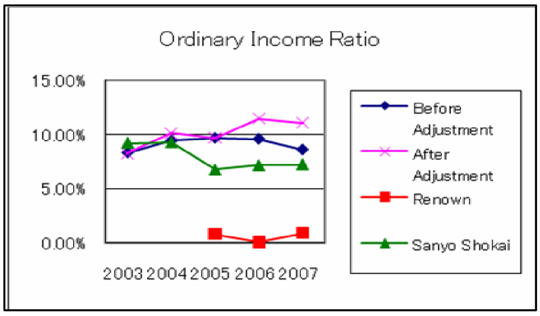
Source: Prepared by the authors based on Onward Kashiyama's annual securities reports

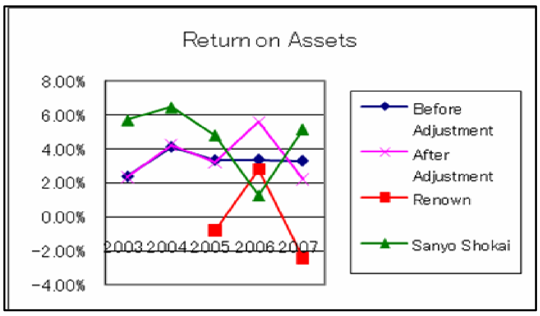
After Adjustment	2003	2004	2005	2006	2007
Gross Margin Ratio	45.62%	46.25%	46.01%	46.30%	44.84%
Operating Income Ratio	7.45%	8.56%	8.93%	8.74%	7.99%
Ordinary Income Ratio	8.25%	10.11%	9.69%	11.47%	11.07%
Net Income Ratio	2.69%	5.05%	3.61%	6.51%	2.36%
Return on Assets	2.33%	4.23%	3.18%	5.58%	2.20%
Return on Investment	8.04%	8.80%	9.57%	9.00%	8.76%
Return on Equity	3.71%	6.88%	4.88%	8.95%	3.84%
Total Assets Turnover	0.87	0.84	0.88	0.86	0.93
Tangible Fixed Assets Turnover	2.55	2.74	2.77	2.80	3.30
Inventories Turnover	10.48	10.24	9.90	9.10	8.59
Inventories Turnover Period	34.83	35.66	36.88	40.12	42.49

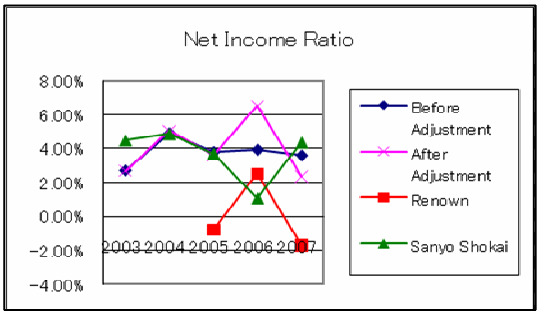
Receivables Turnover	9.13	8.51	10.52	10.31	9.91
Receivables Turnover Period	39.96	42.89	34.68	35.39	36.81
Current Ratio	178.01%	182.01%	199.53%	157.09%	170.63%
Acid Test Ratio	136.67%	132.17%	145.10%	112.23%	126.74%
Equity Ratio	62.72%	61.42%	65.15%	62.30%	57.35%
Debt Equity Ratio	49.89%	53.76%	45.07%	51.89%	63.52%
Fixed Assets Ratio	83.93%	76.56%	74.19%	85.55%	83.72%
Fixed Assets to Fixed Debt Ratio	78.10%	71.97%	70.43%	82.11%	75.84%
Interest Coverage Ratio	133.00	181.82	241.67	85.05	30.67
Sales - Growth Rate	100.00%	101.65%	102.99%	107.48%	120.99%
Operating Income - Growth Rate	100.00%	116.77%	123.44%	126.00%	129.66%
Net Income - Growth Rate	100.00%	190.98%	138.40%	260.30%	106.21%
Total Assets - Growth Rate	100.00%	105.11%	101.20%	108.60%	112.37%
Equity - Growth Rate	100.00%	102.94%	105.14%	107.87%	102.76%

Source: Prepared by the authors based on Onward Kashiyama's annual securities reports









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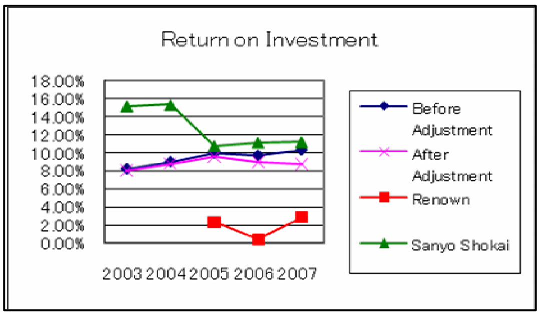

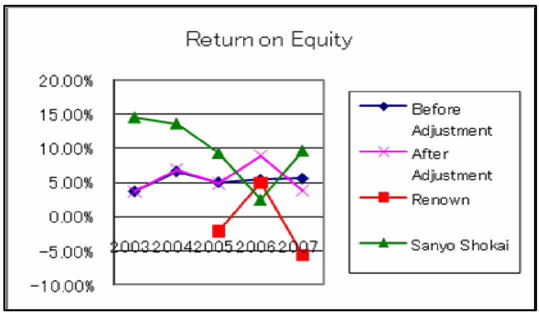

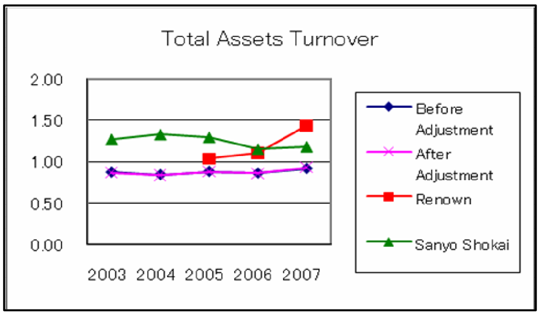

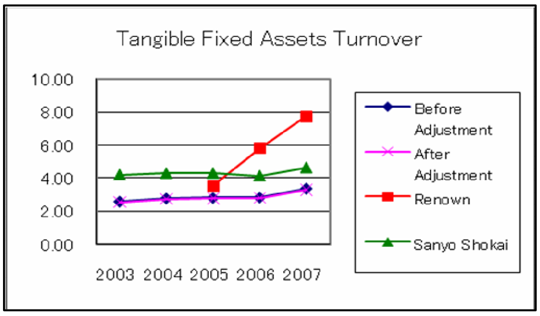

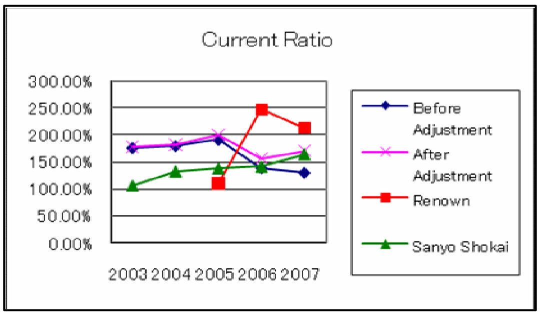

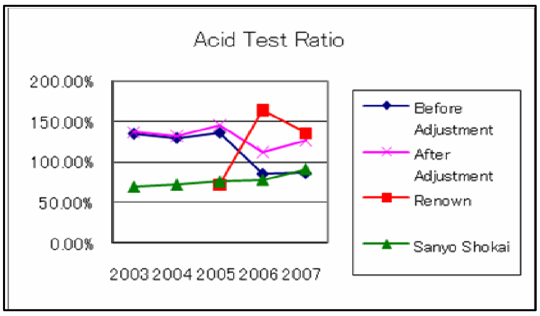

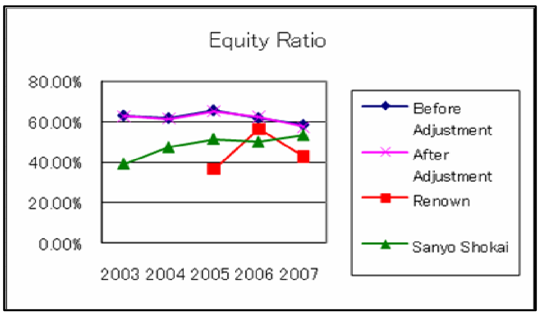

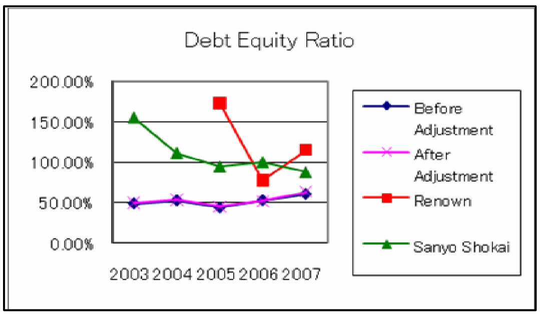

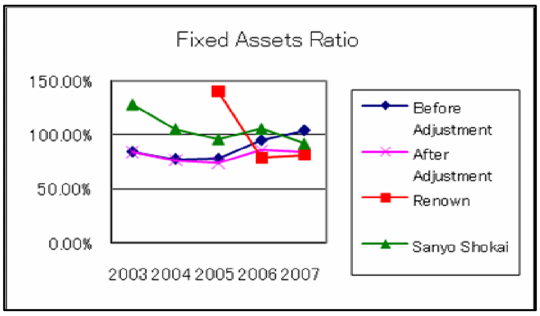

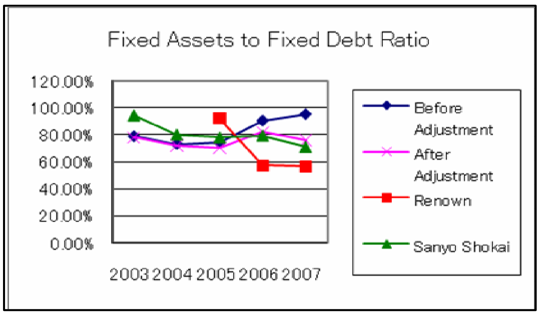

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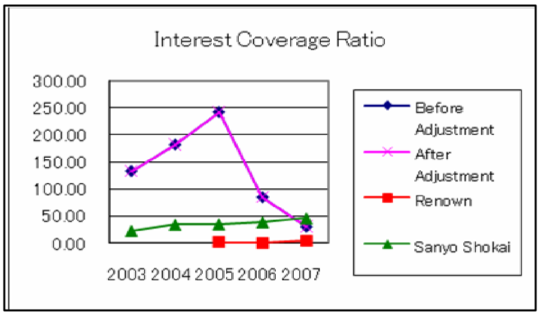

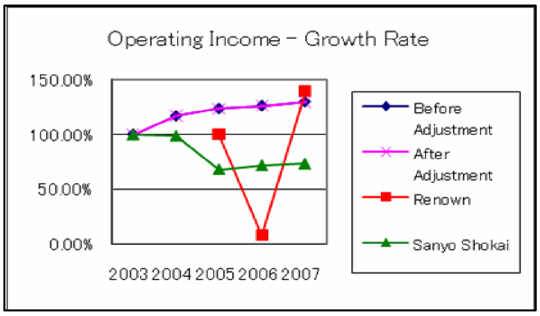

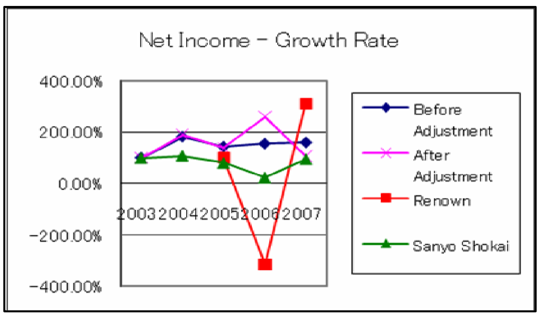

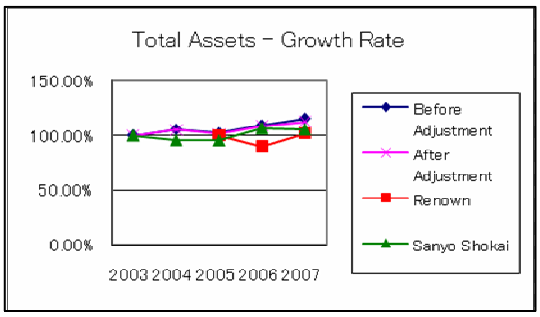

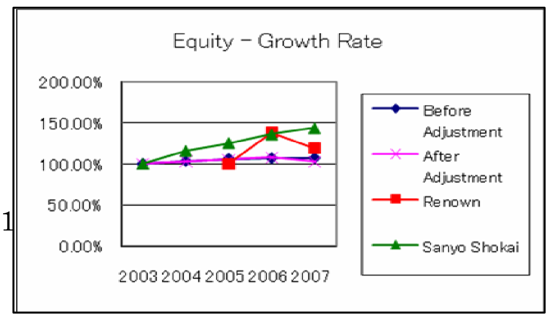

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