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IFRS Alert

Ethiopia should now be considered a hyperinflationary economy

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Executive Summary

Economic conditions that currently exist in Ethiopia will require reporting entities in that country to follow the requirements set out in IAS 29 'Financial Reporting in Hyperinflationary Economies'. This means that any entities that have interim or annual reporting requirements at 31 December 2022 or thereafter in Ethiopia should reflect this Standard when preparing their IFRS-based financial statements.

Therefore at 31 December 2022 there are eleven countries around the world where IAS 29 should be applied, when entities want to state they are in full compliance with IFRS. These countries are: Argentina, Ethiopia, Iran, Lebanon, South Sudan, Sudan, Suriname, Turkey, Venezuela, Yemen and Zimbabwe.

Currently there are four countries that are potentially hyperinflationary and therefore should be closely monitored. They are: Angola, Haiti, Sri Lanka and Syria.

As further information becomes available, we will continue to update this alert.

Recapping the requirements of IAS 29

IAS 29 requires the financial statements of any entity whose functional currency is the currency of a hyperinflationary economy to be restated for changes in the general purchasing power of that currency, so that the financial information provided is more meaningful.

Indicators of hyperinflation

IAS 29 lists factors that indicate when an economy is hyperinflationary. One of the indicators of hyperinflation is if cumulative inflation over a three-year period approaches, or is in excess of, 100 per cent.

The mechanics of restatement

IAS 29 requires amounts in the statement of financial position that are not already expressed in terms of the measuring unit current at the end of the reporting period, are restated by applying a general price index.

In summary:

- assets and liabilities linked by agreement to changes in prices, such as index linked bonds and loans, are adjusted in accordance with the agreement
- non-monetary items carried at current amounts at the end of the reporting period (such as net realisable value and fair value) are not restated
- all other non-monetary assets and liabilities are restated
- monetary items (ie money held and items to be received or paid in money) are not restated because they are already expressed in terms of the monetary unit current at the end of the reporting period, and
- all items in the statement of comprehensive income should be expressed using the measuring unit current at the end of the reporting period, so all amounts need to be restated from the dates when the items of income and expenditure were originally recorded in the financial statements.

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Other important factors that should be taken into considerations when applying IAS 29

IAS 29 sets out specific requirements on how to restate prior period comparatives. It requires corresponding figures for the previous reporting period to be restated by applying a general price index so that the comparative financial statements are presented in terms of the measuring unit current at the end of the reporting period.

IAS 29 may result in the creation of additional temporary differences under IAS 12 'Income Taxes'. This is because the restatement of items under IAS 29 will often lead to adjustments to the carrying amounts of items without corresponding changes to their tax bases. Be mindful that IAS 12 requires these adjustments to be recognised in profit or loss.

Impairment testing should also not be overlooked. IAS 29 requires any restated non-monetary items to be reduced when it exceeds its recoverable amount, even if those assets were not previously considered impaired under historical cost accounting. It will be important when preparing financial statements to consider whether the restatement of asset carrying values affects the results of impairment tests that were conducted in previous reporting periods, and whether there are any indicators of impairment for assets that were not tested for impairment in previous periods.

Recent IFRIC decisions relating to hyperinflation

The IFRS Interpretations Committee (IFRIC) recently considered a number of accounting issues in relation dealing with hyperinflation. They included:

- translating a hyperinflationary foreign operation and presenting exchange differences
- accounting for cumulative exchange differences before a foreign operation becomes hyperinflationary, and
- presenting comparative amounts when a foreign operation first comes hyperinflationary.

We encourage careful consideration of not only these IAS 29 issues noted above but also an issue they considered earlier this year, which was how to consolidate a non-hyperinflationary subsidiary by a hyperinflationary parent.

Our thoughts

IAS 29 is not a Standard that can be quickly implemented, particularly in group situations. Careful consideration needs to be given to recent IFRIC guidance dealing with situations where there is a hyperinflationary parent that has subsidiaries who also report in a hyperinflationary currency versus situations where a non-hyperinflationary parent has subsidiaries that report in a hyperinflationary currency. Also be mindful of how a hyperinflationary parent with subsidiaries that do not report in a hyperinflationary currency should be accounted for given the requirements set out in IAS 21 'The Effects of Changes in Foreign Exchange Rates'.

Any reporting entity considering IAS 29 for the first time will have to adapt their existing accounting systems to be able to process the hyperinflationary adjustments. It is important they understand the mechanics of adjusting for hyperinflation so they can restate in their financial statements both current and comparative period amounts.

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