
IFRS[®] Interpretations Committee meeting

Date **November 2024**

Topic **IAS 29 *Financial Reporting in Hyperinflationary Economies* – Feedback**

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Purpose of this discussion

To get input from IFRS Interpretations Committee (Committee) members about:

- (a) your experiences (and any challenges) in applying IAS 29 *Financial Reporting in Hyperinflationary Economies*; and
 - (b) the usefulness of information resulting from applying the requirements in IAS 29.
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Structure

This paper includes:

- (a) background information;
- (b) questions to the Committee; and
- (c) next steps.

Appendix A includes extracts from a stakeholder letter setting out some concerns.

Appendix B provides an overview of IAS 29.

Background information

The Request for Information (RFI) on the IASB's third agenda consultation, identified inflation as a possible project. This was because some stakeholders said information prepared applying IAS 29 could be more useful. Specifically, they said:

- (a) the scope of IAS 29 should be extended to include economies experiencing high inflation, because long periods of high inflation can affect the relevance of the information included in the financial statements;
- (b) the Standard relies on a general price index, which may not be reliable or available; and
- (c) restated financial statements of a foreign operation in a hyperinflationary environment are difficult to understand.

Most respondents to the RFI rated a project about inflation as low priority.¹

Note:

At that time, the IASB decided **not** to add a project about inflation to its work plan.

1. See page 25 of the [Third Agenda Consultation - Feedback Statement](#) and paragraphs 68–71 of [Agenda Paper 24D](#) of the IASB's November 2021 meeting for more information on the feedback to the RFI.

Background information (cont'd)

Stakeholders have informed us that the economic landscape has changed since the IASB completed its third agenda consultation. Stakeholders say the following concerns have become more prevalent:

- (a) assessing when an economy becomes hyperinflationary applying IAS 29;
 - (b) the cost and complexity of applying IAS 29; and
 - (c) usefulness of the resulting information.
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Background information (cont'd)

Agenda Paper 2A of this meeting discusses a submission about assessing the indicators of a hyperinflationary economy in paragraph 3 of IAS 29.

The submitter also expressed concerns about:

- (a) the usefulness of the information resulting from applying constant purchasing power accounting in accordance with IAS 29; and
- (b) the complexity of incorporating a hyperinflationary foreign operation into a reporting entity's financial statements.

Appendix A includes more information about these concerns.

Background information (cont'd)

The letter [see Appendix A] states:

The application of IAS 29 has become increasingly complex as more economies meet the quantitative indicators of hyperinflation...[IAS 29] introduces several challenges that question its reliability and usefulness.

The letter requests the IASB to undertake standard-setting to address these concerns.

We have also heard similar concerns and requests from other stakeholders.

Questions to the Committee

Questions

1. Since the completion of the third agenda consultation (in 2022), have you become aware of significant and more pressing concerns about the application of IAS 29? What has given rise to these concerns?

2. In broad terms, what aspects of IAS 29 are you aware of that are particularly challenging and why? For example, identifying when an economy becomes hyperinflationary, restating financial statements applying a general price index, or other aspects.

3. Are you aware of concerns about the usefulness of information resulting from the application of IAS 29? What are those concerns?

Next steps

We will use your input when reporting to the IASB concerns raised by stakeholders.

Appendix A—Letter from the submitter



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Email: ifric@ifrs.org

Dear Sir/Madam,

Submission on the interpretation challenges relating to the application of the measurement model in terms of IAS 29 *Financial Reporting in Hyperinflationary Economies* (IAS 29)

[We] welcome the opportunity to provide a submission on the interpretation challenges faced in applying the measurement model of IAS 29. [We] have a strong presence and deep capabilities across 20 countries in sub-Saharan Africa. [We] have observed an increasing relevance of IAS 29 within the African continent due to the global economic environment's persistently high inflation.

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Context

The application of IAS 29 has become increasingly complex as more economies meet the quantitative indicators of hyperinflation. [We have] identified several issues that impede consistent and comparable financial reporting across our subsidiaries operating in hyperinflationary and potential hyperinflationary economies. While we acknowledge the need to provide transparent and meaningful financial information, we believe that the current standard, in its existing form, presents several challenges that must be addressed to ensure its effectiveness.

This submission deals with the following key issues:

1. Reliability and Usefulness of Constant Purchase Power Accounting.
2. Presentation of IAS 29 Restatements in Consolidated Financial Statements when the group entity is not hyperinflationary.

Issue 1: Reliability and Usefulness of Constant Purchase Power Accounting

IAS 29 mandates the restatement of financial statements using constant purchase power accounting to reflect the effects of hyperinflation. While this approach aims to preserve the comparability and relevance of financial information, it introduces several challenges that question its reliability and usefulness.

1.1 Distortion of Economic Reality

The current application of constant purchase power accounting under IAS 29 can lead to financial results that do not accurately reflect the economic reality of an entity's operations. This is particularly evident that only non-monetary items are indexed, which creates basis risk when an entity holds non-hyperinflationary monetary assets (such as hard currency) and distorts the true economic performance. This basis risk exists due to exchange rates not always being directly correlated with inflation.

For example, in hyperinflationary economies, entities often hold hard currency as a natural hedge against inflation. However, the current IAS 29 approach can result in a situation where holding hard currency appears less economically beneficial than holding non-monetary assets, despite the former being a more effective hedge against inflation. This disconnect between the accounting outcomes and economic reality undermines the relevance and faithful representation of financial information, as outlined in the IASB's Conceptual Framework. Refer to Appendix 1: *Detailed Example of Basis Risk under IAS 29 in Hyperinflationary Economies*.

1.2 Operational Challenges and Complexity

The process of restating financial statements under IAS 29 involves complex calculations, particularly in identifying and applying appropriate price indices. In many cases, the availability and reliability of such indices are questionable, leading to further subjectivity and variability in the financial statements of entities operating in the same economy.

Case Example: Zimbabwe 2024

In Zimbabwe, the official Consumer Price Index (CPI) exhibited extreme volatility, moving from 65,703 in December 2023 to 258,942 in February 2024. This volatility not only caused significant swings in financial reporting outcomes but also made it challenging for entities to provide consistent and understandable financial information to stakeholders. The current IAS 29 requirements, by not accommodating such volatility, exacerbate the operational difficulties and contribute to less reliable financial reporting.

1.3 Misalignment with Investor Expectations

The restatement of financial results under IAS 29 often produces outcomes that are not aligned with investors' expectations or the economic fundamentals they use to evaluate companies. For instance, investors typically assess returns in nominal terms, not in constant purchase power terms. The adjustments made under IAS 29, with considerable effort, can therefore lead to confusion and reduce the comparability of financial information across entities and industries.

The US GAAP measurement model for entities operating in a high inflationary (hyperinflationary) economy is to change their functional currency to the reporting currency of the immediate parent entity when the parent entity is operating in a non-hyperinflationary economy. This approach eliminates basis risk and provides a more accurate reflection of the economic reality faced by entities in hyperinflationary environments. Refer to Appendix 2: *Comparison of IAS 29 and US GAAP Approaches to Hyperinflation*.

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Issue 2: Presentation of IAS 29 restatements in consolidated financial statements when the group entity is operating in an economy that is not hyperinflationary

The consolidation of financial results of entities operating in hyperinflationary economies into a multinational group's financial statements presents unique challenges particularly regarding the

presentation of restatements. The interaction between IAS 29 and IAS 21 *The Effects of Changes in Foreign Exchange Rates* (IAS 21) often leads to significant volatility in the consolidated group earnings, which may not reflect the underlying economic reality.

2.1 Volatility in the consolidated group earnings

IAS 21.42(a) requires that all amounts of a hyperinflationary entity be translated at the closing rate at the reporting date. For multinational entities, this often results in substantial losses at the consolidated group level, as the combined effects of IAS 29 restatements and IAS 21 exchange rate adjustments can significantly erode reported earnings.

For instance, in cases where the local price index and currency have devalued substantially, the group entity may recognise significant losses on both the IAS 29 restatement and the IAS 21 closing rate translation. These accounting adjustments can sometimes eliminate the total earnings of the hyperinflationary foreign operation, presenting a distorted view of the entity's financial health. One potential solution could involve recognising IAS 29 restatements directly in equity or other comprehensive income, rather than in profit or loss. This approach could help mitigate the earnings volatility that currently arises from the combined application of IAS 29 and IAS 21.

2.2 Inconsistencies in Comparative Information

IAS 21 does not require the restatement of comparative information for group entities whose reporting currency is not hyperinflationary. This creates inconsistencies in the presentation of financial results, particularly when comparing current year results with those of prior periods. The lack of clarity in how these adjustments should be presented further complicates the consolidation process.

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Appendix 1: Detailed Example of Basis Risk under IAS 29 in Hyperinflationary Economies

Zimbabwean entity with ZWL functional currency – 1 January 2024 to 28 February 2024

- The ZWL currency devalued by 145%:
1 January 2024 = USD/ZWL 6 105
28 February 2024 = USD/ZWL 14 939
- The ZWL inflation index devalued by 294%:
1 January 2024 = 65 703
28 February 2024 = 258 942
- On 1 January 2024, assume Zimbabwe is a hyperinflationary economy. An entity has USD100 in capital (kept in ZWL - being the local currency) and immediately the management team decides to hold USD100 as a hedge for hyperinflation risk (often being the best (if not only) hedge compared to other non-monetary hedges available in African markets).
- At the reporting date the monetary item is revalued at the official exchange rate and the non-monetary equity base funding the asset is rebased using the official inflation index.
- This basis risk creates volatility for financial reporting in earnings, and is not reflective of economic reality to shareholders, as the entity had USD100 on 1 January 2024 and still has the same USD value on 28 February 2024.

Applying the accounting

- The entity starts with USD100 funded by the ZWL equivalent of USD100 (being ZWL 610 500).
- The currency position is revalued to spot, and the funding (in equity) is revalued to the current purchasing power using the inflation index.
- If the results are converted back to USD spot on 28 February 2024 at USD/ZWL14 939, then IAS 29 shows shareholders that the entity suffered a USD61 loss in purchase power.
- This is misleading and not reflective of the real cash flow or dividend ability as the entity still holds \$100.

USD/ZWL spot rates		6 105		14 939	
Date		1 January 2024		28 February 2024	
	USD	ZWL	Devaluation	ZWL	USD
Cash	100	610 500	145%	1 493 900	100
Equity	(100)	(610 500)	294%	(2 406 041)	(161)
Profit or loss:				(912 141)	(61)
IAS 21 translation gain				883 400	59
IAS 29 hyperinflation loss				(1 795 541)	(120)

Appendix 2: Example of difference between IFRS reporting and US GAAP for hyperinflation

A South African based group incorporates a Ghanaian entity on 1 January 2023 and injects 1 million Ghanaian Cedi (GHS) in an interest-bearing account within this entity. This GHS 1 million is extracted out of Ghana on 31 December 2023. It is assumed that Ghana has been triggered as a hyperinflationary economy on 1 January 2024.

For illustration purposes, the calculations in this example have been simplified as no tax has been applied and typically the calculations would be prepared monthly rather than on a yearly basis.

The facts and assumptions used in this example are as follows:

Exchange rates	
South African Rand (ZAR) / GHS exchange rate at 1 January 2023	0,60
Average ZAR / GHS exchange rate for 2023	0,63
ZAR / GHS exchange rate at 31 December 2023	0,65
Inflation	
Year-on-year inflation for Ghana in 2023	23,2%
Interest rate	
Average interest rate earned for the year	15%

In this example, the South African based group entity would have injected ZAR 1 666 667 into the Ghanaian entity. The GHS 1 million would have earned GHS 150 000 of interest. The resultant GHS 1 150 000 would be converted back to ZAR 1 769 231 on 31 December 2023 which would represent an economic return of 6,2%.

Application of IAS 29

The journal entries would be recognised by IFRS would be as follows:

Dr	Bank	GHS 1 000 000
Cr	Share capital and share premium	(GHS 1 000 000)
<i>Recognition of capital injection of GHS 1 000 000</i>		
Dr	Bank	GHS 150 000
Cr	Interest income	(GHS 150 000)
<i>Recognition of 15% interest</i>		
Dr	Hyperinflation loss	GHS 232 000
Cr	Equity	(GHS 232 000)
<i>Re-basing or indexing of opening equity using the CPI index</i>		

Note: The indexing of the income statement has not been illustrated as it has no impact on overall profit or loss

Given the above journals, the loss recognised by the Ghanaian entity would be GHS 82 000. This would be translated into the ZAR group at the closing rate of 0,65 ZAR/GHS. A net loss of

ZAR 126 154 would be recognised by the ZAR group entity which would represent a loss of 7,6%. This reflects a vast difference between to the actual 6,2% economic return earned.

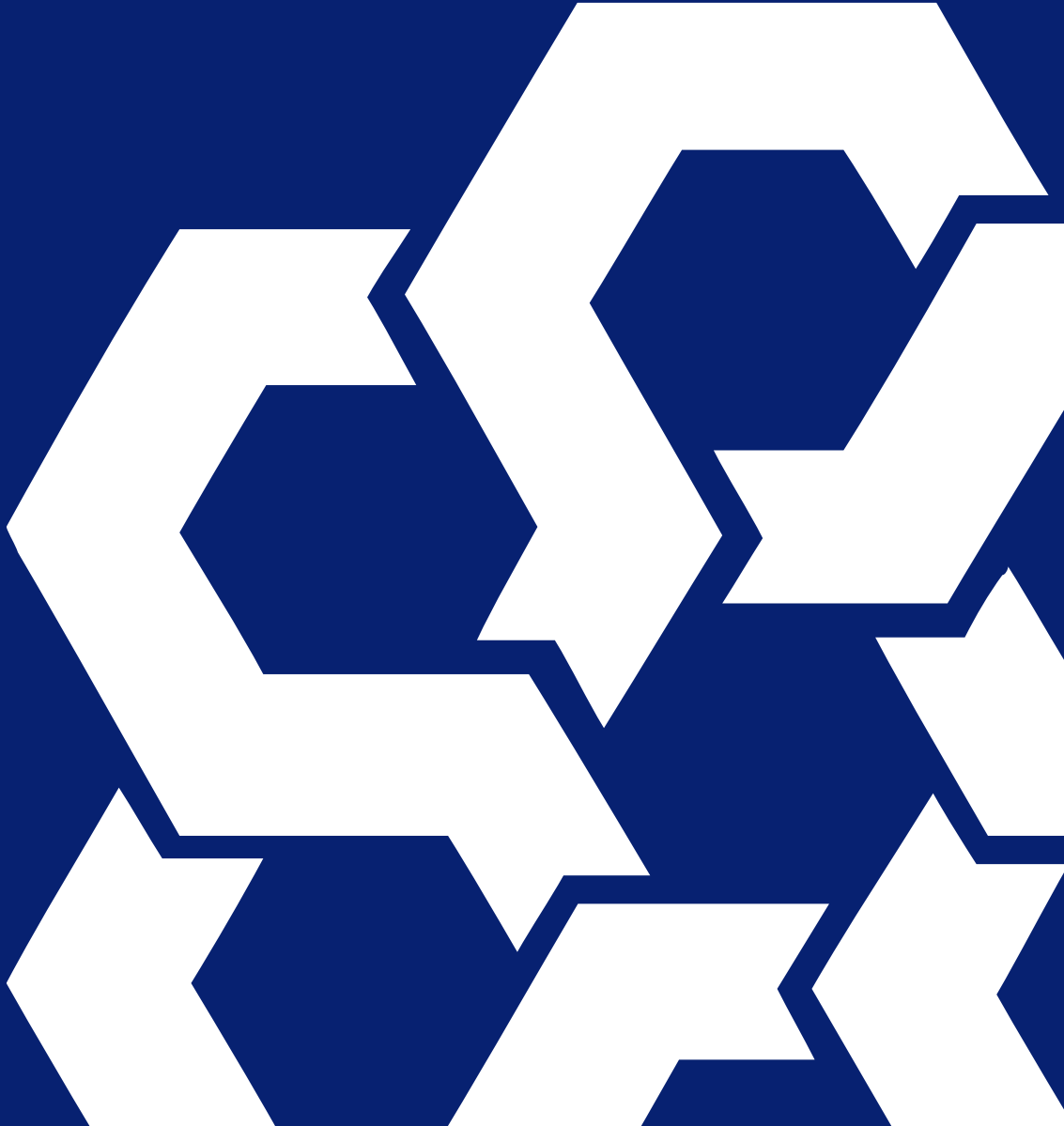
Application of US GAAP

The journal entries recognised by US GAAP, which would use the ZAR reporting currency to account of the subsidiary, would be as follows:

Dr	Bank	ZAR 1 666 667
Cr	Share capital and share premium	(ZAR 1 666 667)
<i>Recognition of capital injection of GHS 1 000 000 at the ZAR exchange rate on 1 January 2023</i>		
Dr	Bank	ZAR 238 095
Cr	Interest income	(ZAR 238 095)
<i>Recognition of 15% interest converted to ZAR at the average exchange rate 2023</i>		
Dr	Exchange loss	ZAR 135 531
Cr	Bank	(ZAR 135 531)
<i>Exchange loss recognised when converting the GHS 1,15 million into ZAR at ZAR at the closing exchange rate for 2023</i>		

Given the above journals, the profit recognised by the Ghanaian entity with the ZAR group entity would be ZAR 102,546 which is reflective of a 6,2% return and is representative of the economic return made.

Appendix B—Overview of IAS 29



Overview¹

IAS 29 applies to any entity whose functional currency is the currency of a hyperinflationary economy.

Hyperinflation is indicated by factors such as prices, interest and wages linked to a price index, and cumulative inflation over three years of around 100 per cent or more.

In a hyperinflationary environment, financial statements, including comparative information, must be expressed in units of the functional currency current as at the end of the reporting period. Restatement to current units of currency is made using the change in a general price index. The gain or loss on the net monetary position must be included in profit or loss for the period and must be separately disclosed...

Note:

IAS 29 was issued by the International Accounting Standards Committee (predecessor to the International Accounting Standards Board (IASB)) in August 1990.

1. Reproduced from the 'About' tab at [IAS 29 Financial Reporting in Hyperinflationary Economies](#)

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