

**LIMPERG INSTITUTE**  
**PhD Seminar: Advanced Financial Accounting. June/July 2011**  
**Reading List**

**Monday:**

**Scale and scale effects in studies of the relation between returns and earnings (this day will also include a discussion of research design issues in market-based accounting research and will include papers introduced in the first Limperg capital markets course)**

The aim of these readings is to provide background materials that will be the basis for a discussion which will attempt to provide an answer to the following question which I have been asked several times:

“I am currently working on a thesis on accounting earnings and ... Within that context I recently read your papers “Scale and Scale Effects in Market-based Accounting Research” and “Earnings Management? The Shapes of the Frequency Distributions of Earnings Metrics are not Evidence Ipso Facto” and would like to ask for your guidance regarding the deflation of accounting data (e.g. EPS, EPS forecast errors) in return regressions. So far I have deflated earnings per share and also earnings forecasts by stock price. Since I am a little concerned about bias in my estimates (due to distribution differences for profit/loss firms but also due to autocorrelation effects from having lagged stock price as the independent variable and returns as dependent variable) I was wondering whether usage of non-deflated, per share accounting data (e.g., EPS) would be better. I understood from your papers that there is no significant scale effect from using per share numbers as independent variables in return regressions. Would you recommend the use of (non-deflated) per-share accounting data in return regressions or shall I maintain price-deflated per-share data in the return regressions?”

Ball, R., 2011, Discussion of Why Do EPS Forecast Error and Dispersion Not Vary with Scale? Implications for Analyst and Managerial Behavior, *Journal of Accounting Research*, 49: 359-401.

Barth, M, and S. Kallapur, 1996, The Effects of Cross-Sectional Scale Differences on Regression Results in Empirical Accounting Research, *Contemporary Accounting Research*, 13: 527-567.

Basu, S, 1997, The Conservatism Principle and the Asymmetric Timelines of Earnings, *Journal of Accounting and Economics*, 24, 1; 3-38.

Cheong, F., and J. Thomas, 2011, Why Do EPS Forecast Error and Dispersion Not Vary with Scale? Implications for Analyst and Managerial Behavior, *Journal of Accounting Research*, 49: 359-401.

Durtschi, C., and P. Easton, 2009, Earnings Management? Erroneous Inferences based on Earnings Frequency Distributions, *Journal of Accounting Research*, 44, 557-592.

\*\*Easton, P., 1998, Discussion of Revalued Financial, Tangible Assets: Association with Share Prices and Non-Market-Based Value Estimates, *Journal of Accounting Research*, 36: 235-247.

Easton, P. and T. Harris, 1991, Earnings as an Explanatory Variable for Returns, *Journal of Accounting Research*, 29, 1; 19-37.

\*\*Easton, P., and G. Sommers, 2002, Scale and the Scale Effect in Market-Based Accounting Research, *Journal of Business, Finance, and Accounting*, 25-56.

Patatoukas, P., and J. Thomas, 2011, More Evidence of Bias in Differential Timeliness Estimates of Conditional Conservatism. *The Accounting Review*, Forthcoming.

## **Studies examining differences in cost of capital across accounting regimes**

### **Summary of this area of research**

Easton, P., 2007. Estimating the Cost of Capital Implied by Market Prices and Accounting Data, *Foundations and Trends in Accounting*. Now Publishers.

### **Tuesday:**

#### **Topic 1A: The main methods**

Botosan, C., 1997, Disclosure Level and the Cost of Equity Capital, *The Accounting Review*, 72, 323-349.

Botosan, C., and M. Plumlee, 2002, A Re-examination of Disclosure Levels and Expected Cost of Equity Capital, *Journal of Accounting Research*, 40, 21-40.

Brav, A., R. Lehavy, and R. Michaely, 2004, Using Expectations to Test Asset Pricing Models, *Financial Management* 34:31-65.

Claus, J., and J. Thomas, 2001. Equity Premium as Low as Three Percent? Evidence from Analysts' Earnings Forecasts for Domestic and International Stocks, *Journal of Finance* 56, 1629-1666.

Easton, P., 2004, PE Ratios, PEG Ratios, and Estimating the Implied Rate of Return on Equity Investment, *The Accounting Review* 79: 73-96.

Easton, P., G. Taylor, P. Shroff, and T. Sougiannis, 2002, Using Forecasts of Earnings to Simultaneously Estimate Growth and the Rate of Return on Equity Investment, *Journal of Accounting Research* 40: 657-676.

Gebhardt, W., C. Lee, and B. Swaminathan, 2001, Towards an Ex-ante Cost of Capital. *Journal of Accounting Research* 39: 135-176.

Gode, D., and P. Mohanram, 2003, Inferring the Cost of Capital using the Ohlson-Juettner Model, *Review of Accounting Studies* 8: 399-431.

Gode, D., and P Mohanram, 2011. Evaluating Implied Cost of Equity Estimates after Removing Predictable Analyst Forecast Errors. Working paper. Columbia University.

Hou, K., Van Dijk, and Y Zhang, 2010, The Implied Cost of Capital: A New Approach, Working paper, The Ohio State University.

O'Hanlon, J., and A. Steele, 2000, Estimating the Equity Premium Using Accounting Fundamentals, *Journal of Business Finance and Accounting* 27: 1051-1084.

Nekrasov, A., and M. Ogneva, 2012, Using Earnings Forecasts to Simultaneously Estimate Firm-specific Cost of Equity and Long-term Growth, *Review of Accounting Studies*, forthcoming.

Monahan, S., 2012, Discussion of Using Earnings Forecasts to Simultaneously Estimate Firm-specific Cost of Equity and Long-term Growth, Forthcoming, *Review of Accounting Studies*, forthcoming.

### **Wednesday:**

#### **Topic 1B: Evaluation of the Methods**

Botosan, C., and M. Plumlee, 2005, Assessing Alternative Proxies for the Expected Risk Premium. *The Accounting Review* 80, 21-53.

Botosan, C., M. Plumlee, and H. Wen, 2011, The Relation between Expected Returns, Realized Returns, and Firm Risk Characteristics. *Contemporary Accounting Research*, forthcoming.

Daske, H., J. van Halteren, and E. Maug. 2009. Evaluating Methods to Estimate the Implied Cost of Equity Capital: A Simulation Study, Working paper, University of Mannheim.

Easton, P., 2006, Use of Forecasts of Earnings to Estimate and Compare Cost of Capital Across Regimes. *Journal of Business, Finance and Accounting* 33: 374-394.

Easton, P. and S. Monahan, 2005, An Evaluation of Accounting-Based Measures of Expected Returns, *The Accounting Review*, 80, 501-538.

Easton, P., and S. Monahan, 2010, Evaluating Accounting-Based Measures of Expected Returns: Easton and Monahan and Botosan and Plumlee *Redux* Working paper, University of Notre Dame.

Easton, P., and G. Sommers, 2007. Effect of Analysts' Optimism on Estimates of the Expected Rate of Return Implied by Earnings Forecasts, *Journal of Accounting Research*: 983-1016.

**Thursday:**

**Topic 1C: Applications**

Baginski, S., and S. Rakow, 2012, Management Earnings Forecast Disclosure Policy and the Cost of Equity Capital, *Review of Accounting Studies*, forthcoming.

Da, Z., P. Easton, and K. Hong. 2010. Variance Decomposition of Returns: Revisions in Dividend Forecasts, Earnings Forecasts, and Implied Expected Rates of Return, Working paper, University of Notre Dame.

Da, Z., P. Easton, and K. Hong. 2010. Improved Accounting-Based Measures of Expected Returns, Working paper, University of Notre Dame.

Daske, H., 2005, Economic Benefits of Adopting IFRS or US-GAAP – Have the Expected Costs of Equity Costs of Equity Capital Really Decreased? *Journal of Business, Finance and Accounting* 33: 329-363.

Hail, L. and C. Leuz, 2006, International Differences in the Cost of Equity Capital: Do Legal Institutions and Securities Regulation Matter? *Journal of Accounting Research* 44: 485-531.

Hail, L. and C. Leuz, 2009, Cost of capital effects and changes in growth expectations around US cross-listings. *Journal of Financial Economics*. 93: 428-454.

**Friday:**

**The quality of financial statements**

- Badertscher, B., Burks, J., and P. Easton, 2012, A Convenient Scapegoat: Fair Value Accounting by Commercial Banks during the Financial Crisis, *The Accounting Review*, forthcoming.
- Badertscher, B., Burks, J., and P. Easton, 2011, When a Loss is More Than Just a Loss: The Market Pricing of Other-Than-Temporary Impairments? CARE working paper.
- Barth, M., W. Landsman and M. Lang. 2008. International Accounting Standards and accounting quality. *Journal of Accounting Research* 46: 467-498.
- Dechow, P., W. Ge, and C. Shrand, 2010, Understanding Earnings Quality: A Review of the Proxies, Their Determinants and Their Consequences, Forthcoming, *Journal of Accounting and Economics*.
- Durnev, A., R. Morck, B. Yeung and P. Zarowin, 2003, Does Greater Firm-Specific Return Variation Mean More or Less Informed Stock Pricing? *Journal of Accounting Research*, 41, 5, p. 797.
- Francis, J., P. Olsson, and K. Schipper. 2008. Earnings Quality. *Foundations and Trends in Accounting*. Now Publishers.
- Kraft, A., A. Leone, C. Wasley, 2005, An Analysis of the Theories and Explanations Offered for the Mis-Pricing of Accruals and Accrual Components, *Journal of Accounting Research*.
- Penman, S. and X. Zhang, 2002, Accounting Conservatism, the Quality of Earnings, and Stock Returns, *The Accounting Review*, 77, 2: 237-264.