Mandatory Earnings Forecast Regulation and Stock Price Informativeness

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Content:
We examine the economic consequences of disclosure regulation using a regulation implemented in a staggered manner that requires publicly listed Chinese firms to issue earnings forecasts under certain conditions. We find the regulation substantially increases the directly affected firms’ frequency of management earnings forecasts, but approximately one third of the firms that are required to issue mandatory earnings forecasts fail to issue the required forecasts (noncompliant firms). The stock market reacts positively to the announcements of mandatory earnings forecasts. More importantly, the mandatory earnings forecast regulation helps increase the directly affected firms’ future earnings response coefficient (FERC), suggesting that the regulation helps increase the total information available to stock market investors. We also find that the regulation creates a spillover effect on some firms that do not issue earnings forecasts in the post-regulation period. Specifically, we find that the noncompliant firms experience a significant increase in the FERC in the post-regulation period when their peer firms in the same industry issue at least one mandatory forecast. However, we find no evidence of a spillover effect for the firms whose expected earnings do not fall into the scope of the regulation and thus are not obligated to issue any earnings forecasts.

Date: November 1, 2017 (Wednesday)
Time: 10:30 a.m. — 12:00 noon
Language: English
Venue: KK1303, 13/F., K.K. Leung Building, The University of Hong Kong