

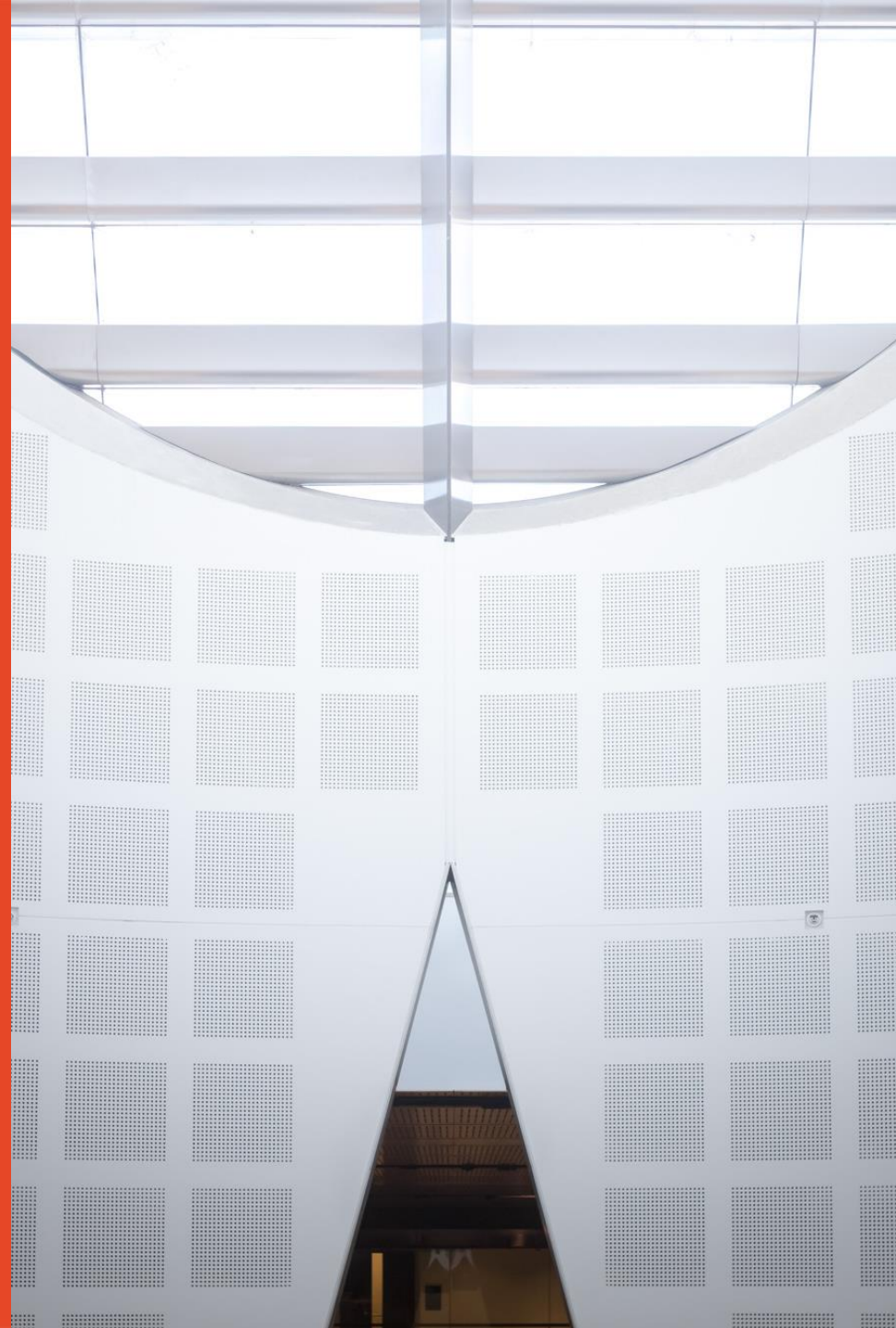
## Discussion

# “R&D Disclosures and the Informativeness of Future Earnings”

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# Overview

- **Research question**: Effect of R&D disclosure on the informativeness of share prices about future earnings
- **Sample**: 6,471 firm-year observations (1,491 unique firms) from 15 countries for the period 2006 to 2015
- **Main findings**:
  - R&D disclosure allows investors to better anticipate future earnings.
  - This is driven by disclosures in the narrative section of annual report, including management discussion.
  - The results hold for firms in countries with low corruption levels and strong enforcement.
  - R&D disclosure topics matter: Development phase of R&D, Conditions for capitalization, and Intellectual property.

# R&D Disclosure Index and Topic Classification

- Use a list of R&D related keywords and terms to search annual reports
- Appendix C: Validation of the R&D disclosure index

## Can we refine this measure?

- “Development Phase”
  - Contains keywords such as *R&D* and *research and development*
- “Conditions for capitalisation”
  - Where do we normally find these keywords?
  - Is it largely boilerplate based on IAS38?
  - Is this category also largely related to the “Development Phase”?
- “Intellectual Property”
  - Keywords such as *innovation* and *invention*; Are they related to the “Research Phase”?

## What is actually being captured in this R&D disclosure index?

- Basu and Waymire (2018): R&D is hard to be separable from the overall value creation of the company

# R&D Disclosure Index and Topic Classification

- *R&D\_Law* included as a control variable
- Results are driven by the disclosure from the narrative section including the management commentary section
- However, as the authors have mentioned, there are differences in regulations across countries.
  - Mandatory R&D Disclosures
    - Germany (GAS 15)
    - China (Article 27c)
  - General Guidance
    - Italy, UK and other European firms

## R&D Disclosure and R&D Capitalization

- Two channels of providing R&D information for IFRS firms
- Capitalized R&D is included as a control variable and the related Inverse Mills Ratio
- More nuanced relation between R&D disclosure and R&D capitalization as suggested by prior studies
  - **Chen et al. (2017)**: R&D disclosure is driven by the collection of capitalization-related information.
  - **Dinh et al. (2020)**: R&D disclosures *complement* R&D capitalization. R&D disclosures can also *substitute* for capitalization.
- More insight on why R&D disclosure appears to be less useful for “Expensers”
  - **Dihn et al. (2020)**: firms with higher levels of R&D disclosure have higher market values when they capitalize lower levels of R&D

## Country-level Variables

- Two variables
  - (1) country level corruption
  - (2) accounting enforcement
- Can we link them more closely to the relationship between R&D disclosure and price informativeness?
  - Dinh et al. (2020) show that R&D information is informative for firms without earnings management.
  - Do these country variables largely capture the propensity to earnings management and overall accounting quality?