The Effects of Earnings Quality, Conservatism, and Real Earnings Management on the Company's Performance and Information Asymmetry as a Moderating Variable

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ABSTRACT

This study investigates the role of information asymmetry as a moderating variable to strengthen or to weaken the effects of earnings quality, conservatism, and real earnings management on the company's performance. This study utilized data from Indonesia and Singapore for years 2004-2013. The results suggest that earnings quality positively affects the company's performance; however accounting conservatism does not affect the company's performance and real earnings management negatively affects the company's performance. Moreover, information asymmetry weakens the effects of earnings quality and conservatism on the company's performance but strengthens the effect of real earnings management on the company's performance.

Keywords: Earnings Quality, Conservatism, Real Earnings Management, The Company's Performance, Information Asymmetry
JEL Classifications: G10, G30

1. INTRODUCTION

Information about the company's performance that is provided to shareholders is sometimes difficult to understand in terms of its reliability and accuracy. This is due to a conflict of interest between managers and shareholders, which reflects the condition of information asymmetry (Leland and Pyle, 1977). From an agency perspective, managers as insiders use the information advantage to the disadvantage of outside shareholders as a group (Huang and Skantz, 2008) because managers and principals have different interests (Jensen and Meckling, 1976). Principals require information about the company's performance that has been achieved by management. However, it is often that the information submitted by managers does not comply with the actual conditions because managers wants to maximize their own utility. Lambert (2001) stated that the company that separates the functions of management and ownership would be vulnerable to an agency conflict of interest. The company's performance information can be affected by factors such as earnings quality

(Li, 2014), conservatism (Kazemi et al., 2011), and real earnings management (Gunny, 2010). Management choose and change its accounting policies, accounting estimates and corrections of errors to increase the relevance and reliability of the entity's financial statements and the comparability of financial statements of entities with financial statements of other entities (IAI, 2012).

Earnings quality is one of the important indicators for accurately evaluating the value of a company (Li, 2014). Dechow et al. (2010) explained that the high earning quality provides more information about company's performance that is relevant to a specific decisions made by specific the decision-maker. Furthermore, Demerjian et al. (2013) believed that the high earning quality accurately reflects the company's operating performance.

Another characteristic that affect the company's performance is conservatism. Traditionally, accounting conservatism is described by the adage of "anticipate no profits, but anticipate all losses" (Bliss, 1924; Watt, 2003). This indicates that bad

news is recognized earlier than good news in reported earnings. Basu (1997) suggested that the inconsistency in conservatism for recognizing criteria for profits and losses in accounting standards results in a slower earnings response to good news compared to bad news. Asymmetric timeliness relates to when the information conveyed by an economic event or shock is recorded in periodic accounting earnings earlier if it conveys bad news and later if it conveys good news (Shroff et al., 2013). Asymmetric timeliness in news recognition is expected to manifest itself also as asymmetric persistence in earnings (Watt, 2003).

Real earnings management affects the company's performance. Roychowdhury (2006) used the term of real activity manipulation and defined that it as departures from normal operational practices. It is motivated by managers' desire to mislead at least some stakeholders into believing that a certain financial reporting goals have been met in the normal course of operations. Real earnings management occurs when managers undertake actions that change the timing or structuring of an operation, investment, and/or financing transaction in an effort to influence the output of the accounting system (Gunny, 2010). According to Cohen and Zarowin (2010), a company that has positive abnormal production costs during the implementation of seasoned equity offering (SEO) experienced a decline in the performance of 1-year post SEO. Challen and Siregar (2012) proved that management use either accrual earnings management and real earnings management as a substitute. When management cannot use accrual earnings management to improve the performance of the company because the company audited by industry specialists auditor, then managers replace it with real activity manipulation to achieve desired earnings.

This study provides a broad overview to shed light on: (1) The impact of earnings quality, conservatism and real earnings management on the company's performance, (2) the role of information asymmetry as a moderating variable to strengthen or to weaken the effects of earnings quality, conservatism, and real earnings management on the company's performance. This study used the listed firms in Indonesian stock markets and Singapore stock markets as a research object by considering the same indicator capital market. This is because capital markets have an important role in the economy of a country that has a function as a ways for financing the business and getting funds from investors. In addition, this study expects to contribute to the growing knowledge on the impact of earnings quality, conservatism and real earnings management on the company's performance. Examining the effect of earnings quality on operating performance is important, given the significance of current and future performance of the firm and its owners. Conservatism is a feature financial reporting, which has an important role in limiting the behavior of optimistic managers. Meanwhile, understanding the effect of real earnings management on operating performance are greatly valuable to investor for choosing the correct management of assets with more conservative views.

The remainder of this study is structured as follows: Section 2 provides the literature review and hypotheses development. Section 3 outlines the data and the methodology implemented, while Section 4 describes the results of this study. Section 5 discusses the conclusions, theoretical implications, and future research in this area.

2. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

2.1. The Influence of Earnings Quality on the Company's Performance

Earnings quality is an important indicator to be used as a measure of the company's performance. The higher earnings quality, the higher company's performance. Companies with relatively high earnings quality reflect a high company's performance (Li, 2014; Demerjian et al., 2013; Dechow and Schrand, 2004; Sloan, 1996). It gives more information about the company's performance conditions that are relevant to specific decisions made by specific decision-makers (Dechow et al., 2010). High earnings quality reflects a good metric for the purpose of performance evaluation, prediction, and assessment (Radzi et al., 2011).

Income smoothing is an intentional act carried out by management using accounting policies in an effort to reduce fluctuations in earnings (Francis et al., 2004). Income smoothing is a magnitude of earnings reported in the condition evenly over time during the normal activity of a company (Francis et al., 2004; Dechow and Schrand, 2004; Tucker and Zarowin (2006) and Khaddaf et al. (2014) indicated that income smoothing has a positive effect on the stock returns.

The accrual component is subject to greater uncertainty than cash flow component, because accruals are the product of judgments, estimates, and allocations, while cash flows are realized (Francis et al., 2005). Management is allowed to use accrual accounting recognition so that accrual increases or reduces the ability of managers to use earnings for measuring the company's performance; thus, management can provide private information and/or manipulate earnings through accrual (Dechow, 1994; Dechow et al., 1998). According to Lyimo (2014), the lower is the accrual quality, the better is the reported earnings quality. Accrual quality has additional an information content (Subramanyam, 1996), and tends to reduce fluctuations in cash flows; thus, creating the earning figure to become more useful (Dechow and Skinner, 2000). Earnings were measured by accrual may improve earnings quality (Melumad and Nissim, 2008). Accordingly, the proposed hypotheses are as follows:

H_1: Earnings quality will positively affect the company's performance.

H_{1a}: Income smoothing will positively affect the company's performance.

H_{1b}: Accrual quality will positively affect the company's performance.

2.2. The Influence of Conservatism on the Company's Performance

Shroff et al. (2013) stated that if an accounting profit reflects the results of operations, punctuality acknowledges economic

losses faster than with promptness to recognize the economic advantages. It causes asymmetric timeliness of recognition. Conservatism has an important role in determining the quality of financial information, particularly with regard to the company's performance (Wang, 2013). The higher is the conservatism, the lower is the company's performance.

Immediate recognition of the economic losses compared to the economic benefits do not guarantee the high quality of the company's performance (Watts, 2003). The greater the difference in the degree of verification for gains than losses acknowledge the greater conservatism (Basu, 1997). As a result, earnings contain a downward bias due to the recognition of income (assets) accrual lower than operating cash flow (Givoly and Hayn, 2000). The greater the difference in the degree of verification for gains than losses acknowledges the greater conservatism. The asymmetry causes a positive correlation between cash flow and an increase in the accrual policy recognizes losses (Ball and Shivakumar, 2005). In other words, it indicates that the presence of the recognized loss accrual policy (conservatism policy) causes cash flow to decrease.

Accounting conservatism is considered to provide the low earnings quality in financial reporting because companies maintain the book value of net assets remain low by choosing accounting methods and estimates (Penman and Zhang, 2002). Companies with a high degree of conservatism tend to allocate hidden reserve for the following years, so earnings tend to be persistent (Penman and Zhang, 2002). This study argued that if management creates hidden reserve then led to lower profit making management more flexible reporting profits in the future. Management can increase those reserves to increase investment, thereby reducing profits. The proposed hypotheses are as follows:

H_2: Conservatism will negatively affect the company's performance.

H_{2a}: Accrual based conservatism will negatively affect the company's performance.

H_{2b}: Hidden reserve conservatism will negatively affect the company's performance.

2.3. The Influence of Real Earnings Management on the Company's Performance

Li (2012) found a significant relationship between real earnings management and stock return in the subsequent year. In particular, stock of firms with abnormally low levels of operating cash flows underperform in the subsequent year, and stock of firms with abnormally high levels of operating cash flows outperform perform in the subsequent year. On the other hand, stocks of firms with abnormally low levels of production costs outperform in the next 3 years and stocks of firms with abnormally high levels of production costs underperform in the subsequent 3 years. Real earnings management is a diversion from normal business practices. It is motivated by managers' desire to mislead at least some stakeholders into believing certain financial reporting goals have been met in the normal course of operations (Roychowdhury,

2006). It means that the reported earnings of which are presented in the financial statements are not showing the actual company's performance because of the quality of financial statements presented low.

This study used three proxies of real earnings management as used by Roychowdhury (2006), i.e., discretionary cash flow, discretionary production; and discretionary expenditures. Real earnings management using discretionary cash flow by manipulating sales, which gives a discount price or lenient credit terms to boost sales volumes temporarily during the current year in an effort to increase reported earnings (Gunny, 2010). Sales manipulation refers to the behavior of managers in an effort to increase sales during the year. This led to a net cash flow from operating activities that is lower than normal levels and causes a negative abnormal operating cash flow. The lower is the abnormal operating cash flow, the higher is the reported earnings. According to Li (2012), the acceleration of sales volumes by giving price discounts or lenient credit terms can increase sales and earnings for the current period but reduces the operating cash flow of the current period.

Real earnings management by proxy of discretionary production is done through overproduction in order to the reported cost of goods sold (COGS) is low in an effort to avoid reporting losses (Roychowdhury, 2006). Companies can produce more goods than necessary to meet expected demand to increase earnings. With higher production levels led to a decrease in fixed costs per unit so that the reported COGS is lower, and the companies report larger operating margin (Gunny, 2010). Companies that create overproduction usually show positive abnormal production costs. The higher is the abnormal production costs, the higher is the reported earnings. However, the company's performance has declined due to the holding cost on the over-produced items is greater because the companies maintain a residual unsold production. As a result, cash flows from operations are lower than normal given sales levels.

The firm carries out real earnings management through discretionary expenditures by reducing the burden of research and development, advertising, and administrative expense in an effort to increase reported earnings in the current period. Kothari et al. (2016) proved that real earnings management by reducing the burden of research and development could be detrimental to the competitiveness and profitability in future; however, it could also increase current earnings, profit margins and cash flow from operations. This study argued that firms engage in discretionary expenditures by reducing expenses in order to increase reported earnings could have negative abnormal discretionary expenditures. The lower is the abnormal discretionary expenditures, the higher is the reported earnings. Based on the above arguments, the hypotheses formulated in this study are:

H_3: Real earnings management will negatively affect the company's performance.

H_{3a}: Discretionary cash flow will negatively affect the company's performance.

H_{3b}: Discretionary production will negatively affect the company's performance.

H_{3c}: Discretionary expenditures will negatively affect the company's performance.

2.4. The Moderating Effect of Information Asymmetry on the Influences of Earnings Quality, Conservatism, and Real Earnings Management on the Company's Performance

Information asymmetry reflects that managements of firms have better information on the value of the company's assets and investment opportunities compared to shareholders (Copeland et al., 2005). Less informed investors may not be able to process the information compared to the investors who have more information; this situation creates asymmetry of information (Bhattacharya et al., 2013). Information asymmetry is manifested when informed traders have superior private information relative to uninformed traders in the finance market (Huang and Skantz, 2008). According Jayaraman (2008), information asymmetry factor influences earnings quality on the company's performance. Bhattacharya et al. (2013) proved that lower is the earning quality, the lower is the liquidity of stocks in the capital market. This is because the risk of adverse selection that is realized in trading costs could be increase. If investors differ in their ability to process earnings-related information, then poor earnings quality can result in differentially informed investors and thereby exacerbate information asymmetry in financial markets (Diamond and Verrecchia, 1991; Kim and Verrecchia, 1994). Brown and Hillegeist (2007) found that better quality information reduces the information asymmetry by increasing the uninformed investor trading. Therefore, it reduces the possibility of trade private information. According to Easley and O'Hara (2004), investors need a higher return to hold stocks with greater private information with less public information. This higher return reflects that private information increases the risk to uninformed investors who hold the stocks and the informed investors are capable of shifting their portfolio based on the new information. Meanwhile, Abbasi et al. (2013); Ajward and Takehara (2011) asserted that there is a negative relationship between earnings quality and information asymmetry.

This study argued that conceptually, the degree of information asymmetry which is proxied by bid-ask spread is private information to the informed investor, while uninformed investors do not have such information. In this condition, the informed investors have more favorable conditions from the private information. Information asymmetry causes an imbalance in obtaining and processing information leading to trade imbalances. This would affect earnings quality followed by the company's performance. The lower is the information asymmetry, the higher is the earnings quality. When the liquidity of the stock is higher, then the difference between the bid (buy) and ask price (selling) is getting smaller. In addition, the high earnings quality can play a role in improving company's performance. The argument indicates that the bid-ask spreads associated with information asymmetry would adversely affect the relationship between earnings quality and corporate performance (coefficient of interaction between the asymmetry of information and the quality of earnings will be negative).

Basu (1997) interpreted that conservatism as resulting in earnings reflecting bad news (losses) more quickly than good news (profits). This implies the systematic differences between bad news and good news periods in the timeliness and persistence of earnings. It means that the greater the difference in the degree of verification that is required to recognize a profit compared to a loss, the greater conservatism (Basu, 1997). Conservatism is the asymmetry that requires a high level of verification to recognize good news as favorable compared recognize bad news as detrimental (Watts, 2003). LaFond and Watts (2008) asserted that conservatism reduces incentives for earnings manipulation by the insiders of a corporation and decreases agency problems among stakeholders. In addition, it reduces information asymmetry and increases the corporate value. Conservatism creates fluctuation and in persistent earnings as well as the increase in information asymmetry (Mashayekhi et al., 2010). An extreme conservatism increases the information asymmetry between the internal and external parties of a company (Wang, 2013). Wang (2013) showed that when earnings conservatism is more significant, information asymmetry becomes more severe. In addition, when earnings conservatism is extreme or insufficient, its correlates with information asymmetry that produces a variety of effects and influences. Specifically, when the level of conservatism information is low, the correlation between earnings conservatism and information asymmetry is significantly negative. On the other hand, the effect on information asymmetry is significantly positive when earnings conservatism is high.

This study argued that the higher or lower is the information asymmetry, the higher or lower is the conservatism. A prior study by Wang (2013) argued that firms recognize revenue and expense are too high or low in conservatism can cause investors to perceive that the in formativeness of financial statements published by the company is insufficient. As a result, information asymmetry increases and then investors increase stock bid-ask spread for self-protection. In contrast, foreign investors perceive that firms do "taking a big bath," which negatively affects the in formativeness of financial statements published. In other words, when there is a high information asymmetry, then conservatism will reduce the role in improving corporate performance. The argument indicates that the bid-ask spreads associated with information asymmetry would adversely affect the relationship between conservatism and the company's performance (coefficient of interaction between the asymmetry of information and conservatism will be negative). Therefore, the information asymmetry is thought to strengthen the influence of conservatism on the company's performance.

Lasdi (2013) and Richardson (2000) proved that information asymmetry affects real earnings management. When information asymmetry is high, stakeholders may not have the information necessary to cancel manipulated earnings. This indicates that shareholders do not have sufficient resources, incentives, or access to information that is relevant to management actions, which may lead to earnings management practices, especially in real earnings management. This study argued that when information asymmetry is high, the real earnings management is high. Therefore, the

information asymmetry can strengthen the role of real earnings management in reducing the company's performance. That is, when the difference in bid-ask spread is greater, then the high real earnings management reduces the company's performance. The argument indicates that the bid-ask spreads associated with information asymmetry would adversely affect the relationship between real earnings management and company's performance (coefficient of asymmetry of information and the interaction between real earnings management would be negative). Thus, in this study suspected that the higher information asymmetry, the higher real earnings management, and the lower the company's performance. Accordingly, the proposed hypotheses are as follows:

H_4: Information asymmetry weakens the influence of earnings quality on the company's performance.

H_5: Information asymmetry strengthens the influence of conservatism on the company's performance.

H_6: Information asymmetry strengthens the influence of real earnings management on the company's performance.

3. DATA AND METHODS

3.1. Sample Selection
The research population was all manufacturing companies listed in Indonesia stock exchange (BEI) and the Singapore exchange over 2004-2013, which consisted of 298 firms or 2,384 firm-year observations. The observations that have negative equity is excluded, which amounts to 84 consisted of 59 observations Indonesian companies and 25 observation Singapore companies. So the number of observations in the sample for the study 2,300 consisted of 973 observations Indonesian companies and 1,327 observation of Singapore companies.

3.2. Variables and Measurement
The company's performance is proxied by stock return the formula for the total stock return is the appreciation in the price plus any dividends paid, divided by the original price of the stock. Meanwhile, information asymmetry is proxied by bid-ask spread and was measured by the Callahan et al. (1997) model as:

$$BAS_{it} = \Sigma (Ask_{it} - Bid_{it}) / \Sigma ((Ask_{it} + Bid_{it})/2$$

Where: BAS_{it} = Spread between ask and bid divided by the amount of ask and bid divided by two; Ask_{it} = Highest ask price of the shares of firm i on year t; Bid_{it} = the lowest bid price of the shares of firm i on year t.

Earnings quality is proxied by smoothing income and accrual quality. Smoothing income variable is measured by the Eckel (1981) index and is calculated by dividing $CV\Delta I$ (the coefficient of variation of the annual change in income and $CV\Delta S$ (the coefficient of variation of the annual change in sales). Accrual quality is measured by Lyimo (2014) as net profit before extraordinary items minus cash flow from operations divided by a total average of assets.

Conservatism is proxied by accrual-based conservatism and hidden reserve. Accrual-based conservatism was measured by net income before extraordinary items of firm i in year t plus cash flows from operation minus depreciation expense divided by average total assets (Ahmed and Duellman, 2011). Furthermore, the value of accruals divided by average of accrual over 3 years period. This value is multiplied by negative one (-1) to ensure that a higher value indicates a higher conservatism. Meanwhile, hidden reserve is measured by summing research and development expenditures and advertising expenditures, then dividing by net operating assets.

Real earnings management is proxied by discretionary cash flows, discretionary production and discretionary expenditures. This study generates the normal levels of CFO, discretionary expenses and production costs using the model developed by Dechow et al. (1998) as implemented in Roychowdhury (2006). Normal CFO is a linear function of sales and change in sales. To estimate this model, the following cross-sectional regression for each industry and year was developed:

$$CFO_{it}/A_{it-1} = \alpha_0 + \alpha_1(1/A_{it-1}) + \alpha_2(S_{it}/A_{it-1}) + \alpha_3(\Delta S_{it}/A_{it-1}) + \varepsilon_t \tag{1}$$

Where: A_{it-1} is the total assets of firm i at the end of period t, S_{it} = The sales of firm i during period t and $\Delta S_{it} = S_{it} - S_{it-1}$. For every firm-year, abnormal CFO is the actual CFO minus the normal of CFO calculated using estimated coefficients from the corresponding industry year model and the firm-year's sales and lagged assets, which derived from (1). Production costs are defined as the sum of COGS and change in inventory during the year. The COGS as a linear function of contemporaneous sales which is estimated as:

$$COGS_{it}/A_{it-1} = \alpha_0 + \alpha_1(1/A_{it-1}) + \alpha_2(S_{it}/A_{it-1}) + \varepsilon_t \tag{2}$$

The inventory growth as a linear function of the contemporaneous and lagged change in sales:

$$\Delta INV_{it}/A_{it-1} = \alpha_0 + \alpha_1(1/A_{it-1}) + \alpha_3(\Delta S_{it}/A_{it-1}) + \alpha_4(\Delta S_{it-1}/A_{it-1}) + \varepsilon_t \tag{3}$$

Using 2 and 3, the normal level of production costs is estimated as:

$$PROD_{it}/A_{it-1} = \alpha_0 + \alpha_1(1/A_{it-1}) + \alpha_2(S_{it}/A_{it-1}) + \alpha_3(\Delta S_{it}/A_{it-1}) + \alpha_4(\Delta S_{it-1}/A_{it-1}) + \varepsilon_t \tag{4}$$

The normal level of discretionary expenses can be expressed as a linear function of sales:

$$DISEXP_{it}/A_{it-1} = \alpha_0 + \alpha_1(1/A_{it-1}) + \alpha_2(S_{it-1}/A_{it-1}) + \varepsilon_t \tag{5}$$

Control variables were as follow: (1) Capital structure was measured by the total debt to total equity ratio (Ross et al., 2013), (2) investment opportunity set was measured by market value to book value of equity ratio (Myers, 1997), (3) firms size was measured by natural logarithm of total assets (Wang, 2013), (4) dummy state, which 0 for Indonesia and 1 for Singapore and, and (5) dummy year which 0 for the year of 2008 and 1 for the other year except 2008.

3.3. Research Models

The effects of earnings quality, conservatism, and real earnings management on the company's performance and information asymmetry as a moderating variable is shown by the equation 6.

$$
\begin{aligned}
KINRET_{it} = {} & \gamma_0 + \gamma_1\, SMOOTH_{it} + \gamma_2\, ACCR_{it} + \gamma_3\, CONACC_{it} \\
& + \gamma_4\, CONRES_{it} + \gamma_5\, ABCFO_{it} + \gamma_6\, ABPROD_{it} \\
& + \gamma_7\, ABEXP_{it} + \gamma_8\, BAS_{it} + \gamma_9\, SMOOTH_{it}{*}BAS_{it} \\
& + \gamma_{10}\, ACCR_{it}{*}BAS_{it} + \gamma_{11}\, CONACC_{it}{*}BAS_{it} \\
& + \gamma_{12}\, CONRES_{it}{*}BAS_{it} + \gamma_{13}\, ABCFO_{it}{*}BAS_{it} \\
& + \gamma_{14}\, ABPROD_{it}{*}BAS_{it} + \gamma_{15}\, ABEXP_{it}{*}BAS_{it} \\
& + \gamma_{16}\, DER_{it} + \gamma_{17}\, MB_{it} + \gamma_{18}\, SIZE_{it} \\
& + \gamma_{19}\, DNEG + \gamma_{20}\, DTHN + \varepsilon_{it}
\end{aligned} \tag{6}
$$

Where: $KINRET_{it}$ = Company's performance (stock return) firm i for period t; KL_{it} = Earnings quality firm i for period t, proxied by $SMOOTH_{it}$ and $ACCR_{it}$; $SMOOTH_{it}$ = Income Smoothing firm i for period t; $ACCR_{it}$ = Accrual quality firm i for period t; $KONS_{it}$ = Conservatism firm i for period t, proxied by $CONACC_{it}$ and $CONRES_{it}$; $CONACC_{it}$ = Accrual-based conservatism firm i for period t; $CONRES_{it}$ = Hidden reserve conservatism firm i for period t; MLR_{it} = Real earning management firm i for period t, proxied by $ABCFO_{it}$, $ABPROD_{it}$ and $ABEXP_{it}$; $ABCFO_{it}$ = Discretionary cash flows firm i for period t; $ABPROD_{it}$ = Discretionary production firm i for period t; $ABEXP_{it}$ = Discretionary expenditures firm i for period t; BAS_{it} = Bid ask spread firm i for period t; DER_{it} = Debt equity ratio firm i for period t; MB_{it} = Market to book value firm i for period t; $SIZE_{it}$ = Firm size firm i for period t; $DNEG_{it}$ = Dummy state, value 0 = Indonesia, and 1 = Singapore; $DTHN_{it}$ = Dummy year, value 0 = Year 2008, and 1 = Except year 2008; γ = Constant; ε_{it} = Residual error firm i for period t.

4. RESULTS AND DISCUSSION

4.1. Descriptive Statistics

The descriptive statistics in Table 1 showed that income smoothing and accrual quality have a relatively high standard deviation compared to the mean value. This suggests that the variability of income smoothing and accruals quality sample companies is quite high. Income smoothing and accruals quality of the research sample were very uneven and volatile. The accrual-based conservatism and the hidden reserve conservatism have a relatively high standard deviation compared to the mean value. The accrual-based conservatism has an average value negative score. This indicates that most of the research sample use conservative policies. The hidden reserve conservatism had a positive average value, which indicates that the research sample is quite high on this variable.

Abnormal discretionary cash flow has a negative score of the average value. It indicates that the research sample increases its sales of the current year and are willing to sacrifice future profits. As a result, net cash flow from operations is lower than normal levels, causing abnormal discretionary operating cash flow negative. Standard deviation from abnormal discretionary production is higher than the average value, which indicates that the research sample tends to perform production above level normal. Abnormal discretionary expenses have an average value

Table 1: Descriptive statistics

Variables	Minimum	Maximum	Mean±SD
RET	−1.0000	2.8276	0.1809±0.6496
SMTH	0.0327	25.6004	4.0592±4.8101
ACCR	−1.2641	1.3222	0.0138±0.2242
CONACC	−0.6021	1.6233	−0.0352±0.1583
CONRES	−13.6679	14.2214	0.5280±2.2810
ABCFO	−2.9731	2.6640	−0.0083±0.7168
ABPROD	−2.9446	2.9402	0.0119±0.8172
ABEXP	−2.9322	2.4335	0.0293±0.7451
BAS	−0.7143	1.1111	0.1957±0.2630
SIZE	7.3428	11.3617	8.9366±0.6526
MB	−7.5730	11.2550	1.3411±1.8320
DER	0.0123	25.7797	1.5389±2.7396
DNEG	0.0000	1.0000	0.4230±0.4941
DTHN	0.0000	1.0000	0.8757±0.3300

RET: Stock return, SMTH: Income smoothing, ACCR: Accrual quality,
CONACC: Accrual based conservatism, CONRES: Hidden reserve conservatism,
ABCFO: Discretionary cash flows, ABPROD: Discretionary production,
ABEXP: Discretionary expenditures, BAS: Bid ask spread, SIZE: Firm size,
MB: Market to book value, DER: Debt equity ratio, DNEG: Dummy state,
DYEAR: Dummy year, SD: Standard deviation

negative score, which indicates that the research sample reduces research and development expenses, selling expenses and general and administrative expenses, so it resulting a decline reported earnings.

Standard deviations from debt to equity ratio are higher than the average value, which indicates that the ability of the research sample to provide funds through debt quite volatile and very uneven. Standard deviation from market to book value also are higher than the average value, which indicates that the ability of the research sample in acquiring and managing capital are highly volatile capital. Other control variables such as firm size have a standard deviation lower than the average value. This means that the size of the research sample is homogeneous and low variability.

4.2. The Results of Hypothesis 1

The regression model results are presented in Table 2. Earnings quality measurement uses two proxy that income smoothing and accruals quality. Test results of the effects of earnings quality on the company's performance using income smoothing showed insignificant results. It indicated that management actions were done deliberately to minimize fluctuations in the realization of the company's earnings and was not responded to by the investor. In other words, income smoothing does not improve earnings in formativeness, so it does not improve the quality of earnings. Bhattacharya et al. (2003) stated that if the accounting profit artificially leveled and flattened earnings fail to describe the actual changes in the company's underlying performance. It reduces the in formativeness of reported earnings and then increases the haziness of earnings. Income smoothing artificially occurs when management manipulates the accounting timing. This test, therefore, does not support H_{1a}. This result is in line with Hejazi et al., 2014 that income smoothing does not affect the company's performance but do not support a finding by Francis et al., 2004 that income smoothing as measured by the net profit before exceptional items is significantly positive effect on stock return. Conflicting research results can occur due to the use of different measurement so that the results are different (Lymo, 2014).

Table 2: Empirical results

Variables	Prediction	Coefficients	P value
C		−0.847	0.000***
SMTH	+	0.003	0.130
ACCR	+	0.235	0.000***
CONACC	-	−0.095	0.130
CONRES	-	−0.002	0.372
ABCFO	+	−0.085	0.000***
ABPROD	-	−0.043	0.031**
ABEXP	+	0.060	0.005**
BAS	±	0.725	0.000***
DER	±	−0.022	0.000***
MB	±	0.076	0.000***
SIZE	±	0.030	0.054**
DNEG	±	0.240	0.000***
DTHN	±	0.483	0.000***
F-test sign		61.839	
Adjusted R^2		0.256	
N		2300	

Note: RET: Stock return, SMTH: Income smoothing, ACCR: Accrual quality, CONACC: Accrual based conservatism, CONRES: Hidden reserve conservatism, ABCFO: Discretionary cash flows, ABPROD: Discretionary production, ABEXP: Discretionary expenditures, BAS: Bid ask spread, SIZE: Firm size, MB: Market to book value, DER: Debt equity ratio, DNEG: Dummy state, DYEAR: Dummy year. *Significant at 10%, **Significant at 5%, ***Significant at 1%

Test results of the effects of earnings quality on the company's performance using accrual quality showed positive and significant results as predicted. The result indicated that accrual accounting as a result of the judgments and estimates policies could improve earnings as well as it was responded positively by investors. Thus, accrual quality is a measure that is more effective in earnings in formativeness. This test, therefore, supports H$_{1b}$. The result is in accordance with Demerjian et al. (2013) that a high accruals quality can be associated with high earnings quality. This is consistent with the premise that management is better able to predict better the accrual basis, so the accrual quality is an effective measure in earnings in formativeness.

Test results of the effects of earnings quality using income smoothing on the company's performance showed insignificant results, however, when earnings quality proxied by accrual quality showed positive and significant results. Based on the results of an explanation for the hypothesis 1$_a$ and 1$_b$, the hypothesis 1 confirms that earnings quality positively affect the company's performance. This test, therefore, supports H$_1$. The result is in line with Demerjian et al. (2013), and Dechow and Shrand (2004) that high earnings quality could accurately reflect the company's operational performance. High earnings quality to provide more information about the company's financial performance features that are relevant to a particular decision made by a particular decision maker (Dechow et al., 2010). As Siegel (1982) noted that earnings quality is an elusive concept. When the earnings quality determines by using different measurement resulting in different results. According to Desai (2006), there is no single acceptable method for measuring earnings quality. Both of income smoothing and accrual quality are allowed using accounting policy, however, earnings quality using accrual quality reflects a better metric than cash flows for the purpose of evaluation and assessment of the company's performance (Radzi et al., 2011). Income smoothing makes reported earning disrupted if management intentionally distorts earnings figures. Fluctuations in low earnings increase shareholder value and create more favorable sensation investors to invest in companies.

4.3. The Results of Hypothesis 2

The test for the effect of accrual-based conservatism on the company's performance showed insignificant results. It indicated that conservatism requires sound consideration in the face of uncertainty inherent in the company, especially for measuring and recognizing revenue, expenses, assets, and debts. Income and assets not otherwise too high (not exceed the fair value), as well as the debt burden and not be stated too low (not below fair value). Conservatism is a company policy, and both users of financial statements and auditors who conduct an examination of the financial statements cannot affect the conservatism policy during the policy does not conflict with accounting standards. This test, therefore, does not support H$_{2a}$. The result was consistent with Salehi and Zareijam (2011) which asserted that there was no relationship between conservatism and the company's performance.

The test for the effect of hidden reserve conservatism on the company's performance showed insignificant results. It indicated that conservatism policy conducted by the management allowed by the standard setters did not violate accounting standards. Standard setters do not allow sound judgment to establish hidden reserves or doing excessive allowance. The allowance is not appropriate because it raises the opportunistic practices of management and is detrimental to shareholders. Companies pay out the burden of research and development, and advertising expense immediately after the occurrence and not capitalized as a corporate asset. Therefore, the hidden reserve conservatism does not affect the company's performance. This test, therefore, does not support H$_{2b}$.

The test for the effect of conservatism on the company's performance yielded an insignificant result. This test, therefore, does not support H$_2$. The application of conservatism policy in accordance with accounting standards so the conservatism does not affect the company's performance. It showed that the conservatism concept was not in accordance with one of the attributes in the qualitative characteristics of financial reporting is a faithful representation. Nonetheless, the accounting standards still allow for conditional conservatism, i.e., greater aggressiveness in the recognition of bad news compared to the recognition of the good news. Management uses its judgment in developing and implementing policies conservatism to produce information that is relevant and reliable.

4.4. The Results of Hypothesis 3

Tests result of the effect of discretionary cash flow on the company's performance was negative and significant. The negative coefficient abnormal operating cash flow shows the more abnormal operating cash flow, the lower real earnings management so that the company's performance is getting better. This test, therefore, supports H$_{3a}$. This result is in line with Li (2012) that the discretionary operating cash flows have a negative effect on the company's operations today.

The result of the effect of discretionary production on the company's performance was negative and significant. Companies that perform excessive production lead to positive abnormal production costs. With the high level of production resulted in a decrease in fixed costs per unit, so that the cost of sales to be lower and operating margin to be higher. This test, therefore, supports H_{3b}. This result is consistent with Gunny (2010) that the discretionary production has a negative effect on the company's performance this current year, therefore, discretionary production reduces the company's performance.

The result of the effect of discretionary expenditures on the company's performance was negative and significant. The lower the abnormal discretionary expenses, the higher reported earnings. This test, therefore, supports H_{3c}. This result is consistent with Cohen and Zarowin (2010) who suggested that the more negative abnormal discretionary expenditures, the higher discretionary expenditures manipulation so that the company's performance declined. As Kothari et al. (2016) proved that real earnings management by reducing the burden of research and development can be detrimental to the competitiveness and profitability in future but can increase current earnings, profit margins and cash flow from operations.

The test on H_5 implied the impact of real earnings management on the company's performance using discretionary cash flow, discretionary production, and discretionary expenses showed a negative and significant results as predicted. It means that real earnings management affects negatively on the company's performance. This test, therefore, supports H_3. This result is in line with Gunny (2010) that real earnings management has a significant economic effect on the company's performance in future but has a negative effect in present.

4.5. The Results of Hypotheses 4-6

Table 3 shows test result of a moderating variable. The test result of hypothesis 4 showed that information asymmetry weakens the effect of earning quality on the company's performance. It indicated that information asymmetry conceptually reflecting the information problems resulting from transactions between the informed investor and uninformed investor. The information asymmetry causes an imbalance in obtaining and processing information leading to trade imbalances that affect earnings quality of the company's. The higher is the information asymmetry, the lower is the earnings quality. Thus, the information asymmetry decreases the impact earnings quality on the company's performance.

The test result of hypothesis 5 showed that information asymmetry does not strengthen the effect of conservatism on the company's

performance. The underlying argument that investors' perception asymmetry associated with the in formativeness of good news and bad news does not affect the role of conservatism on the company's performance. The information asymmetry conceptually reflecting the information problems resulting from transactions between the informed investor and uninformed investor. Asymmetry timeliness of recognition occurs when timeliness recognize bad news (economic losses) faster than the timeliness acknowledge the good news (economic profit).

Test of a result of hypothesis 6 showed that the information asymmetry strengthens the effect of real earnings management on the company's performance. This means that the higher information asymmetry, the higher real earnings management, the lower the company's performance. The high real earnings management means the uninformative financial statements, so it was responded negatively by investors. Increasing information asymmetry and encourage investors to increase bid-ask spread as a self-protection. Therefore, the information asymmetry can strengthen the role of real earnings management in reducing the company's performance.

5. CONCLUSION AND IMPLICATION

The impact of earnings quality on the company's performance is inconsistent. Accruals quality affects the company's performance significantly, while income smoothing does not affect the company's performance. Accrual quality is more effective in processing profits than income smoothing. Conservatism as measured by accrual-based conservatism and hidden reserve conservatism does not effect on stock returns. This occurs because of the conservatism policy conducted by the management that allowed by standard setters does not violate accounting standards. Real earnings management is proxied by discretionary cash flow does not affect stock returns. This means that the management policy to increase sales through discounts and waivers granting credit terms in an effort to increase profits does not provide earnings in formativeness so it is not responded by the investor. On the other hand, the discretionary production, and discretionary expenses affect significantly negative stock returns. This indicates that the management policy with excessive increase production and reduce the research and development expenditure, and advertising expenses in an effort to increase profits do not provide earnings in formativeness thus responded negatively by investors.

Information asymmetry weakens the effect of smoothing earnings and accruals quality on stock returns. This occurs because of an imbalance of information for investors and create an imbalance in trade that affect the company's performance. Information asymmetry does not moderate the effect of accrual-based conservatism and conservatism hidden reserve on stock returns. This occurs because the application of conservatism policy by management companies in accordance with accounting standards, so that conservatism does not affect the company's performance. Information asymmetry strengthens the real earnings management influence on company performance. This means that the higher is the asymmetry of information, the higher is real earnings management and the lower is the company's performance. Tests

Table 3: Empirical results of a moderating variable

Variables	Prediction	Coefficients	P value
SMTH_BAS	-	−0.014	0.060*
ACCR_BAS	-	−0.321	0.049**
CONACC_BAS	-	0.790	0.016**
CONRES_BAS	-	0.025	0.043**
ABCFO_BAS	-	0.053	0.193
ABPROD_BAS	+	−0.190	0.003**
ABEXP_BAS	-	0.123	0.033**

*Significant at 10%, **Significant at 5%, ***Significant at 1%

on the control variables show that the capital structure adversely affect the company's performance, whereas the investment opportunity set, company size, dummy country and dummy year affect positively the company's performance.

The results of this study contribute to the theoretical implication concerning the signal theory (Spence, 1973). The announcement of accounting information provides signals that the company has good prospects for the future. The high earnings quality accurately reflects the company's performance (Demerjian et al., 2013) and provides more information about the features of the company's performance that are relevant to a particular decision (Dechow et al., 2010). Signaling as an activity where the individual can change his beliefs or providing information to other parties. Therefore it is necessary efforts to improve intelligence capital market players to be more rational and sophisticated in understanding the significance of financial statement information. Suggestions for further research are as follows: (a) Using a sample of other Asian countries research is then expected to be more comprehensive, (b) it is necessary to calculate stock returns using a risk-adjusted return measure so that the estimation result is expected to be more precise, and (c) it need to consider the behavior of investors in relation to the company's performance using rational expectation models.

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