Regulatory uncertainty and management earnings forecast:

Evidence from a quasi-natural experiment

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Abstract

We adopt the China Securities Regulatory Commission's (CSRC) random inspection policy as a quasi-natural experiment to examine the impact of regulatory uncertainty on management earnings forecasts (MEFs), utilizing a staggered difference-in-differences (DID) model. Our findings indicate that random inspections introduce regulatory uncertainty, prompting inspected firms to increase the disclosure of MEFs in response. Further analysis reveals that the positive effect of random inspections on MEFs is more pronounced for firms facing higher levels of uncertainty, in markets with more pessimistic investors, and in regions with weaker regulatory enforcement. Moreover, we find that random inspections trigger negative market reactions, leading managers to issue more optimistic earnings forecasts and to release more positive information in an effort to stabilize investor expectations. By illustrating how firms adjust their disclosure strategies in response to regulatory uncertainty induced by random inspections, our study contributes to the literature on securities regulation and voluntary corporate disclosure.

Keywords: Regulatory uncertainty; Random inspection; Management earnings forecasts; Forecasting optimism