Narrative Conservatism

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Outline

Research Question and Contribution

- **Research Question**
  - Whether narrative disclosure is conservative, i.e., whether narratives reflect bad news in a more complete, news-consistent, and timely manner than good news?
- **Contribution**
  - Filling the gap in conservatism literature by documenting the existence of narrative conservatism.
  - Providing novel evidence to the debate regarding whether managers withhold bad news.
  - Relating to the broader literature on the informativeness of SEC filings.

Theoretical Framework: Recognition and Disclosure

- **Definition (Schipper, 2007)**
  - Recognition: depictions in numbers with captions on the face of the financial statements
  - Disclosure: display in the notes and supporting schedules that accompany financial statements
- **Reporting Requirement (FASB, 1984)**
  - Recognition: an economic event can be recognized if it satisfies all of the following criteria
    - Definition criterion
    - Measurability criterion
    - Relevance criterion
    - Reliability criterion
  - Disclosure: can be deployed to disclose information that fails to meet certain recognition criteria
- **Role of Narratives**
  - Supplement information that cannot be recognized
  - Explain recognized line items

Theoretical Framework: Conservatism

- **Definition**
  - Conditional conservatism: "accountants' tendency to require a higher degree of verification to recognize good news as gains than to recognize bad news as losses" (Basu, 1997, p. 7)
  - Unconditional conservatism: "accountants' preference for accounting methods that lead to lower reported values for shareholders' equity" (Basu, 1997, p. 8).
  - Narrative conservatism: narratives reflecting bad news in a more complete, news-consistent and timely manner than good news

Theoretical Framework: Completeness

- **Completeness**
  - Complete disclosure must include all necessary information for a user to understand the underlying economic event (FASB, 2018)
  - Firms may disclose good news in a more complete manner than bad news to boost performance (Teoh et al., 1998; Lang and Lundholm, 2000).
  - Firms may disclose bad news in a more complete manner than good news to avoid litigation (Skinner, 1994, 1997).
- **Hypotheses**
  - **H1:** Narrative disclosure is completer in response to bad news than to good news.

Theoretical Framework: News-consistency

- **News-consistency**
  - News-consistency implies that disclosure agrees with the underlying economic event in content sentiment.
  - Tone influences how information is perceived or processed, and thus it can be employed both to inform or mislead (Davis et al., 2012; Li, 2010; Huang et al., 2014).
  - Firms may deploy a uniformly positive (negative) tone in both good and bad news disclosure, resulting in higher news-consistency in good (bad) news disclosure.
- **Hypotheses**
  - **H2**: Narrative disclosure is more news-consistent in response to bad news than to good news.

Theoretical Framework: Timeliness

- **Timeliness**
  - Financial information is of higher quality if it is *timely*. Disclosure should be made *in time* to influence users' decisions (FASB, 2018).
  - Managers may delay bad news disclosure to mitigate its negative economic consequences (Chambers and Penman, 1984; Niessner, 2015; Segal and Segal, 2016; Brockbank and Hennes, 2018).
  - Managers may accelerate bad news disclosure due to litigation concerns (Skinner, 1994; Marinovic and Varas, 2016).
- **Hypotheses**
  - **H3**: Narrative disclosure is timelier in response to bad news than to good news.

Research Design: Proxies

- **Narrative Disclosure Corpora**
  - Corpora: 10-Q and 8-K filings because they (a) are more credible, (b) have higher reporting threshold and (c) are more timely than other corporate communication channels.
  - Heterogeneity between 10-Q and 8-K: (a) 10-Q is more diversified in content (b) 8-K is more timely.
- **Proxies for Textual Properties and News**
  - Completeness: the total number of words of SEC filings
  - News-consistency: the marginal change of tone in response to increase (good news) or decrease (bad news) in stock market returns.
  - Timeliness: reporting time lag, defined as the number of days elapsed between the news release date and the filing date of the studied disclosure
  - News: stock returns (Basu, 1997).

Research Design: Model

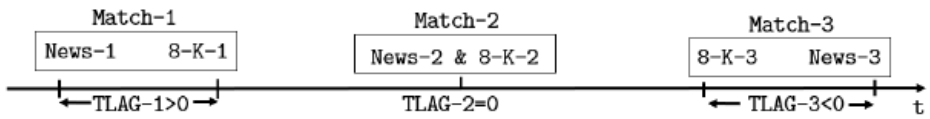
- **Model Specification**
  - Form 10-Q

$$TEX_{i,t} = \beta_0 + \beta_1 QRET_{i,t} + \beta_2 NEG_{i,t} + \beta_3 QRET_{i,t} \times NEG_{i,t} + \sum \beta_n CONTROLS_{i,t} + \epsilon_{i,t} \quad (1)$$

  - Form 8-K

$$TEX_{i,t} = \beta_0 + \beta_1 \Delta DRET_{i,t-tlag} + \beta_2 BN_{i,t-tlag} + \beta_3 \Delta DRET_{i,t-tlag} \times BN_{i,t-tlag} + \sum \beta_n CONTROLS_{i,t} + \epsilon_{i,t} \quad (2)$$

Figure 1: 8-K Matching Process



Research Design: Data

- Data source: Compustat, CRSP and I/B/E/S

Table 1. Sample Selection Process

10-Q

		Numer of observations
Retrieved from EDGAR		575,579
After merging with COMP and CRSP data		303,034
(-) Number of obs. from utility and financial firms	82,612	
(-) Number of firm-quarters with missing values in SIC, SIZE, MTB, LEV, or with non-positive total assets or book value of equity or common shares outstanding, or with common share price less than \$1	26,450	
(-) Number of obs. with total words less than 1% percentile (1,236 words)	1,940	
(-) Number of obs. that contain negative or larger than 99% TLAG	1,696	
After dropping obs. with missing values in key variables and screening		190,336
After merging with I\B\E\S and segment data		110,062
(-) Number of obs. that contain missing EARN, STD_EARN and AF	18,456	
Full 10-Q sample		**91,606**

8-K

		Numer of observations
Retrieved from EDGAR		1,489,626
After merging and matching with COMP and CRSP data		442,611
(-) Number of obs. from utility and financial firms	112,739	
(-) Number of firm-quarters with missing values in SIC, SIZE, MTB, LEV, or with non-positive total assets or book value of equity or common shares outstanding, or with common share price less than \$1	48,230	
(-) Number of obs. with total words less than 1% percentile (133 words)	2,776	
(-) Number of obs. that are reversals of previous news day	5,132	
After dropping obs. with missing values in key variables and screening		273,734
After dropping obs. with negative or larger than 99% percentile TLAG (Full 8-K sample)		**119,616**
After dropping obs. with TLAG larger than four (five) days after (before) the 8-K reform (Restricted 8-K sample)		**40,700**

Results: Summary Statistics

Table 2. Panel A: Summary Statistics 10-Q

	count	mean	std	min	25%	50%	75%	max
Textual Variables								
NW	91606	9.020	0.757	7.120	8.506	9.086	9.547	13.544
nw	91606	10937	10204	1236	4941	8829	13997	752337
TONE	91606	-8.921	7.236	-63.579	-13.127	-7.875	-3.866	24.215
TLAG	91606	39	6	0	36	40	44	52
READ	91606	38.161	42.160	14.580	17.840	20.210	39.660	262.519
Financial Variables								
QRET	91606	0.018	0.253	-1.579	-0.113	0.007	0.130	4.849
NEG	91606	0.483	0.500	0	0	0	1	1
SIZE	91606	6.452	1.772	2.898	5.175	6.317	7.563	11.315
MTB	91606	3.461	3.665	0.416	1.485	2.343	3.902	24.449
LEV	91606	0.192	0.182	0.000	0.011	0.162	0.315	0.705
AF	91606	0.043	0.066	-0.262	0.023	0.049	0.073	0.227
AFE	91606	-0.021	0.067	-0.445	-0.018	-0.002	0.002	0.078
BUSSEG	91606	0.859	0.447	0.693	0.693	0.693	0.693	2.773
GEOSEG	91606	0.898	0.532	0.693	0.693	0.693	0.693	3.045
AGE	91606	8.312	1.033	5.811	7.635	8.420	9.089	10.288
EARN	91606	0.005	0.042	-0.201	0.001	0.012	0.023	0.084
STD_EARN	91606	0.020	0.030	0.001	0.005	0.009	0.021	0.188
STD_QRET	91606	0.089	0.070	0.007	0.040	0.070	0.115	0.379

Results: Summary Statistics Continued

Table 2. Panel B: Summary Statistics 8-K

	count	mean	std	min	25%	50%	75%	max
Textual Variables								
NW	119616	6.093	0.926	4.898	5.553	5.846	6.358	12.486
nw	119616	1339	6398	133	257	345	576	264704
TONE	119616	-0.551	7.424	-97.851	-3.049	0.000	3.677	45.929
TLAG	119616	15	17	0	2	9	21	93
N8K	119616	1	0	1	1	1	1	4
NITEM	119616	2	1	1	2	2	2	16
Financial Variables								
DRET	119616	0.003	0.097	-0.833	-0.039	-0.003	0.041	5.991
ΔDRET	119616	-0.018	0.187	-9.062	-0.121	-0.050	0.100	5.989
BN	119616	0.542	0.498	0	0	1	1	1
SIZE	119616	6.326	1.993	2.122	4.896	6.262	7.664	11.379
MTB	119616	3.740	4.781	0.123	1.366	2.293	4.055	33.390
LEV	119616	0.205	0.193	0.000	0.012	0.171	0.334	0.751

Results: Summary Statistics Continued

Table 2. Panel C: Summary Statistics by 8-K Item

Item	# of appearance	% of appearance	nw	TONE	TLAG
Before August 23, 2004					
1: Changes in Control of Registrant	4376	8.20%	1195	-1.22	17.27
2: Acquisition or Disposition of Assets	6772	12.70%	7184	-4.65	22.33
3: Bankruptcy or Receivership	85	0.16%	9920	-4.05	27.89
4: Changes in Registrant's Certifying Accountant	895	1.68%	1128	-9.50	24.71
5: Other Events	**14835**	**27.82%**	**4431**	**-3.14**	**20.49**
6: Resignation of Registrant's Directors	84	0.16%	8052	-11.32	27.98
7: Financial Statements and Exhibits	18110	33.96%	5239	-3.48	20.70
8: Change in Fiscal Year	153	0.29%	3322	-0.95	27.59
9: Reg FD	**4379**	**8.21%**	**571**	**-1.25**	**15.56**
10: Amendments to the Registrant's Code of Ethics	11	0.02%	353	-2.93	19.64
11: Temporary Suspension of Trading	26	0.05%	309	-3.43	19.31
12: Results of Operation	**3608**	**6.76%**	**316**	**-0.61**	**15.98**
After August 23, 2004 (included)					
1: Registrant's Business and Operations	15672	7.95%	797	-3.43	14.96
2: Financial Information	42226	21.42%	449	1.03	12.76
2.02: Results of Operation	**35910**	**18.22%**	**395**	**1.97**	**12.43**
3: Securities and Trading Markets	3063	1.55%	1081	-4.10	13.03
4: Matters Related to Accountants and Financial Statements	888	0.45%	779	-10.15	16.54
5: Corporate Governance and Management	26776	13.58%	539	-0.06	15.76
6: Asset-Backed Securities	3	0.00%	211	2.91	14.33
7: Reg FD	**15795**	**8.01%**	**555**	**0.29**	**11.04**
8: Other Events	**18735**	**9.50%**	**567**	**-0.86**	**11.66**
9: Financial Statements and Exhibits	73982	37.53%	488	0.41	12.82

Results: Is 10-Q Narrative Disclosure Conservative?

Table 3. Panel A: Is 10-Q Narrative Disclosure Conservative?

Dep. Variables	(1) NW	(2) NW	(3) TONE	(4) TONE	(5) TLAG	(6) TLAG
QRET	0.039***	0.029**	-0.279**	0.335**	-0.081	-0.318***
	(3.23)	(2.21)	(-2.04)	(2.58)	(-0.78)	(-2.72)
NEG	0.006	0.007	-0.113**	-0.116**	0.027	0.039
	(1.29)	(1.45)	(-2.20)	(-2.31)	(0.73)	(1.03)
(Pred. Sign)	(-)	(-)	(+)	(+)	(+)	(+)
QRET×NEG	-0.145***	-0.075***	2.103***	0.760***	-0.771***	-0.189
	(-6.05)	(-3.36)	(6.67)	(2.82)	(-4.07)	(-1.04)
SIZE		0.035***		0.469***		-0.135**
		(3.79)		(5.57)		(-2.06)
MTB		-0.007***		0.077***		-0.023**
		(-5.53)		(4.34)		(-1.98)
LEV		0.332***		-1.260***		0.748**
		(9.76)		(-2.77)		(2.16)
EARN		-0.653***		15.058***		-5.455***
		(-4.27)		(5.93)		(-6.21)
STD_RET		0.110***		-1.921***		0.844***
		(3.54)		(-5.72)		(3.38)
STD_EARN		0.672***		-7.792***		5.217***
		(7.42)		(-5.42)		(6.20)
AGE		-0.065***		-0.046		0.199
		(-4.23)		(-0.20)		(1.32)
BUSSEG		0.015		0.460**		0.094
		(1.02)		(2.10)		(0.52)
GEOSEG		-0.039***		0.266		-0.361**
		(-3.24)		(1.26)		(-1.97)
AF		-0.060		-1.866*		-1.021*
		(-0.65)		(-1.86)		(-1.73)
AFE		-0.192***		5.624***		-2.397***
		(-3.60)		(9.06)		(-6.15)
Constant	8.139***	8.468***	-16.652***	-19.772***	44.074***	43.617***
	(233.65)	(65.88)	(-35.13)	(-11.06)	(113.45)	(36.70)
Observations	91,606	91,606	91,606	91,606	91,606	91,606
Adjusted R-squared	0.649	0.653	0.557	0.570	0.613	0.616

$$TEX_{i,t} = \beta_0 + \beta_1 QRET_{i,t} + \beta_2 NEG_{i,t} + \beta_3 QRET_{i,t} \times NEG_{i,t} + \sum \beta_n CONTROLS_{i,t} + \epsilon_{i,t} \quad (1)$$

Results: Are Lengthier 10-Qs Less Readable?

Table 3. Panel B: Are Lengthier 10-Qs Less Readable?

Dep. Variables	(1) READ	(2) READ	(3) READ	(4) READ
NW	13.048***	13.298***	13.407***	13.697***
	(21.59)	(21.73)	(18.50)	(18.74)
QRET	-1.001	-0.471	8.889	11.146
	(-1.49)	(-0.74)	(0.82)	(1.03)
NEG	0.012	0.028	-0.597	-0.597
	(0.05)	(0.11)	(-0.14)	(-0.14)
(Pred. Sign)	(-)	(-)	(?)	(?)
QRET×NEG	3.686**	2.341*	-37.674*	-43.311*
	(2.52)	(1.66)	(-1.66)	(-1.92)
NW×NEG			0.067	0.068
			(0.14)	(0.14)
QRET×NW			-1.093	-1.285
			(-0.91)	(-1.07)
(Pred. Sign)			(-)	(-)
QRET×NEG×NW			4.568*	5.045**
			(1.81)	(2.02)
Observations	91,606	91,606	91,606	91,606
Adjusted R-squared	0.461	0.462	0.461	0.462
Controls	NO	YES	NO	YES

$$READ_{i,t} = \beta_0 + \beta_1 NW_{i,t} + \beta_2 QRET_{i,t} + \beta_3 NEG_{i,t} + \beta_4 QRET_{i,t} \times NEG_{i,t} + \sum \beta_n CONTROLS_{i,t} + \epsilon_{i,t}$$

$$\begin{aligned} READ_{i,t} = {} & \beta_0 + \beta_1 NW_{i,t} + \beta_2 QRET_{i,t} + \beta_3 NEG_{i,t} \\ & + \beta_4 QRET_{i,t} \times NEG_{i,t} + \beta_5 NW_{i,t} \times NEG_{i,t} + \beta_6 QRET_{i,t} \times NW_{i,t} \\ & + \beta_7 QRET_{i,t} \times NEG_{i,t} \times NW_{i,t} + \sum \beta_n CONTROLS_{i,t} + \epsilon_{i,t} \end{aligned}$$

Results: Is 8-K Narrative Disclosure Conservative?

Table 4. Panel A: Is 8-K Narrative Disclosure Conservative?

Dep. Variables	(1) NW	(2) NW	(3) TONE	(4) TONE	(5) TLAG	(6) TLAG
ΔDRET	0.062*	0.050	-1.066***	-0.878**	-13.541***	-13.924***
	(1.78)	(1.43)	(-2.87)	(-2.48)	(-10.81)	(-10.65)
BN	0.007	0.007	-0.091	-0.082	0.206	0.190
	(1.24)	(1.15)	(-1.42)	(-1.30)	(1.13)	(1.02)
(Pred. Sign)	(-)	(-)	(+)	(+)	(+)	(+)
ΔDRET×BN	-0.129**	-0.108**	2.178***	1.843***	20.163***	20.861***
	(-2.58)	(-2.15)	(3.14)	(2.90)	(11.85)	(11.64)
SIZE		-0.010		0.140***		-0.493***
		(-1.47)		(2.66)		(-5.22)
MTB		0.003***		-0.009		0.016
		(2.72)		(-1.27)		(0.78)
LEV		0.039		-0.872***		-1.867***
		(1.19)		(-2.94)		(-3.70)
Constant	7.242***	7.280***	-6.358***	-6.952***	30.067***	33.040***
	(33.38)	(33.20)	(-3.81)	(-4.25)	(7.54)	(8.16)
Observations	119,616	119,616	119,616	119,616	119,616	119,616
Adjusted R-squared	0.447	0.447	0.157	0.158	0.135	0.136

$$TEX_{i,t} = \beta_0 + \beta_1 \Delta DRET_{i,t-tlag} + \beta_2 BN_{i,t-tlag} + \beta_3 \Delta DRET_{i,t-tlag} \times BN_{i,t-tlag} + \sum \beta_n CONTROLS_{i,t} + \epsilon_{i,t} \quad (2)$$

Results: 8-K Items, Filings and Reporting Time Lag

Table 4. Panel B: 8-K Items, 8-K Filings and Reporting Time Lag

Dep. Variables	(1) NITEM	(2) NITEM	(3) N8K_OL	(4) TLAG_OL
ΔDRET	0.221***	0.222***	1.076***	-0.944***
	(4.26)	(4.44)	(6.73)	(-7.63)
BN	0.011	0.011	0.061	0.107***
	(1.23)	(1.24)	(1.43)	(3.82)
(Pred. Sign)	(-)	(-)	(-)	(+)
ΔDRET×BN	-0.318***	-0.321***	-1.358***	1.436***
	(-4.62)	(-4.86)	(-6.43)	(8.75)
SIZE		0.004	0.103***	-0.160***
		(0.65)	(11.76)	(-29.57)
MTB		0.001	-0.011***	0.006***
		(0.94)	(-2.90)	(3.13)
LEV		0.058*	0.467***	0.100**
		(1.66)	(5.57)	(2.06)
CUT 1			4.240***	-1.007***
			(60.18)	(-22.44)
CUT 2			7.627***	-0.240***
			(69.28)	(-5.38)
CUT 3			10.602***	0.349***
			(27.59)	(7.80)
CUT 4				1.084***
				(23.74)
CUT 5				3.102***
				(53.44)
Constant	1.428***	1.391***		
	(18.64)	(16.17)		
Observations	119,616	119,616	119,616	40,700
Adjusted R-squared	0.126	0.126		
Pseudo R2			0.00563	0.00902
Year-month FE	YES	YES	NO	NO
Firm FE	YES	YES	NO	NO
Industry Clustered SE	YES	YES	NO	NO

$$TEX_{i,t} = \beta_0 + \beta_1 \Delta DRET_{i,t-tlag} + \beta_2 BN_{i,t-tlag} + \beta_3 \Delta DRET_{i,t-tlag} \times BN_{i,t-tlag} + \sum \beta_n CONTROLS_{i,t} + \epsilon_{i,t} \quad (2)$$

Results: Robustness Checks

- Our evidence of narrative conservatism is robust to
  - employing an alternative tone measure using the positive and negative word list from the Harvard General Inquiry dictionary (Loughran and McDonald, 2016);
  - including controls for conditional conservatism and managerial incentives;
  - excluding 8-K items on results of operations that contain quarterly or annual financial statements (Segal and Segal, 2016);
  - using an alternative 8-K reporting time lag definition (Carter and Soo, 1999; Niessner, 2015; Chapman et al., 2019);
  - excluding a priori bad news 8-K items (Segal and Segal, 2016);
  - estimating by fiscal year from 1995 to 2020.

Additional Analyses: MD&A and NFS

Table 5. Narrative conservatism in MD&A and NFS

Dep. Variables	(1) NW_MDA	(2) NW_NFS	(3) TONE_MDA	(4) TONE_NFS
QRET	0.031***	0.022	0.542***	0.451
	(2.60)	(1.08)	(2.94)	(1.39)
NEG	0.015***	0.010	-0.132*	-0.038
	(3.28)	(1.56)	(-1.87)	(-0.41)
(Pred. Sign)	(-)	(-)	(+)	(+)
QRET×NEG	-0.062**	-0.026	0.773**	0.453
	(-2.33)	(-0.78)	(1.98)	(0.87)
SIZE	0.037***	0.011	0.476***	0.986***
	(3.53)	(0.71)	(2.60)	(5.17)
MTB	-0.003**	-0.004**	0.039	0.044
	(-2.20)	(-2.12)	(1.54)	(1.50)
LEV	0.226***	0.360***	-0.459	-1.043
	(4.91)	(5.09)	(-0.61)	(-1.22)
EARN	-0.444*	-0.789***	17.948***	13.412***
	(-1.78)	(-4.21)	(4.89)	(5.34)
STD_RET	0.222***	0.068	-3.637***	-1.011
	(4.67)	(1.44)	(-6.91)	(-1.22)
STD_EARN	0.418***	0.808***	-6.150***	-5.435*
	(2.59)	(5.30)	(-3.20)	(-1.68)
AGE	-0.123***	-0.055**	0.912***	0.093
	(-5.82)	(-2.24)	(2.99)	(0.19)
BUSSEG	0.062***	0.026	0.170	-0.241
	(2.99)	(1.18)	(0.56)	(-0.62)
GEOSEG	-0.096***	-0.046**	0.118	0.922**
	(-3.97)	(-2.10)	(0.32)	(2.29)
AF	-0.221**	0.187*	1.255	0.349
	(-2.20)	(1.88)	(0.96)	(0.18)
AFE	-0.261***	-0.205***	8.043***	3.810***
	(-2.87)	(-2.74)	(6.71)	(3.41)
Constant	8.088***	7.649***	-13.781***	-13.723**
	(16.90)	(17.33)	(-2.96)	(-2.32)
Observations	37,215	37,215	37,215	37,215
Adjusted R-squared	0.741	0.812	0.560	0.568

$$TEX_{i,t} = \beta_0 + \beta_1 QRET_{i,t} + \beta_2 NEG_{i,t} + \beta_3 QRET_{i,t} \times NEG_{i,t} + \sum \beta_n CONTROLS_{i,t} + \epsilon_{i,t} \quad (1)$$

Additional Analyses: Voluntary and Mandatory Disclosure

Table 6. Narrative Conservatism in Voluntary and Mandatory Disclosure

Dep. Variables	NW		TONE		TLAG	
	(1)	(2)	(3)	(4)	(5)	(6)
Disclosure Type	VD	MD	VD	MD	VD	MD
ΔDRET	0.128***	-0.036	-1.254**	-0.804	-15.657***	-6.524***
	(3.11)	(-0.32)	(-2.42)	(-0.64)	(-8.19)	(-4.39)
BN	0.011*	-0.004	-0.026	-0.093	0.425	0.147
	(1.70)	(-0.26)	(-0.39)	(-0.48)	(1.62)	(0.55)
(Pred. Sign)	(-)	(-)	(+)	(+)	(+)	(+)
ΔDRET×BN	-0.221***	0.003	2.826***	1.285	25.419***	9.365***
	(-3.88)	(0.03)	(3.15)	(0.98)	(9.36)	(5.45)
SIZE	-0.003	-0.021**	0.082	0.148	-0.626***	-0.045
	(-0.40)	(-2.07)	(1.46)	(1.62)	(-5.15)	(-0.29)
MTB	0.001	0.005***	-0.006	-0.007	0.001	0.036
	(1.01)	(3.15)	(-0.55)	(-0.43)	(0.04)	(1.42)
LEV	0.097**	-0.055	-1.064***	-0.665	-1.491**	-2.122*
	(2.43)	(-1.00)	(-3.48)	(-1.07)	(-2.47)	(-1.91)
Constant	6.807***	8.426***	-4.472**	-10.793***	30.618***	39.314***
	(34.90)	(15.03)	(-2.40)	(-2.65)	(6.25)	(4.36)
Observations	84,113	35,503	84,113	35,503	84,113	35,503
Adjusted R-squared	0.464	0.522	0.196	0.158	0.140	0.178

$$TEX_{i,t} = \beta_0 + \beta_1 \Delta DRET_{i,t-tlag} + \beta_2 BN_{i,t-tlag} + \beta_3 \Delta DRET_{i,t-tlag} \times BN_{i,t-tlag} + \sum \beta_n CONTROLS_{i,t} + \epsilon_{i,t} \quad (2)$$

Additional Analyses: Intangible Assets and R&D Expenses

Table 7. Narrative Conservatism, Intangible Assets and R&D Expenses

Dep. Variables	NW		TONE		TLAG	
	(1)	(2)	(3)	(4)	(5)	(6)
Panel A: Intangible Assets	LOW	HIGH	LOW	HIGH	LOW	HIGH
(Pred. Sign)	(-)	(-)	(+)	(+)	(+)	(+)
QRET×NEG	-0.024	-0.068***	0.469	0.475	-0.109	-0.093
	(-1.21)	(-2.71)	(1.50)	(1.08)	(-0.44)	(-0.24)
Observations	29,636	29,634	29,636	29,634	29,636	29,634
Adjusted R-squared	0.831	0.798	0.708	0.678	0.654	0.693
Panel B: R&D Expenses	LOW	HIGH	LOW	HIGH	LOW	HIGH
(Pred. Sign)	(-)	(-)	(+)	(+)	(+)	(+)
QRET×NEG	-0.065	-0.075**	0.710	0.048	0.336	-0.029
	(-1.56)	(-2.45)	(1.53)	(0.10)	(1.15)	(-0.06)
Observations	22,899	22,898	22,899	22,898	22,899	22,898
Adjusted R-squared	0.623	0.682	0.581	0.635	0.626	0.619

$$TEX_{i,t} = \beta_0 + \beta_1 QRET_{i,t} + \beta_2 NEG_{i,t} + \beta_3 QRET_{i,t} \times NEG_{i,t} + \sum \beta_n CONTROLS_{i,t} + \epsilon_{i,t} \quad (1)$$

Additional Analyses: Firm Characteristics

Table 8. Narrative, Conditional Conservatism and Firm Characteristics

Quintile	(1) 0% - 20%	(2) 20% - 40%	(3) 40% - 60%	(4) 60% - 80%	(5) 80% - 100%
Panel A: C_SCORE					
NW (-)	-0.198*	-0.174**	-0.179***	-0.044	-0.115***
	(-1.72)	(-2.40)	(-3.11)	(-1.06)	(-3.50)
TONE (+)	1.618	2.547***	2.235***	1.048**	1.614***
	(1.50)	(4.03)	(3.71)	(2.21)	(5.17)
TLAG (+)	-0.596	-1.566***	-1.408***	-0.217	-0.402
	(-0.89)	(-3.12)	(-3.21)	(-0.56)	(-1.11)
Panel B: SIZE					
NW (-)	-0.126**	-0.073	-0.303***	-0.091	-0.196**
	(-2.43)	(-1.43)	(-5.65)	(-1.60)	(-2.46)
TONE (+)	1.837***	1.462**	3.639***	1.733**	1.785*
	(3.97)	(2.23)	(5.50)	(2.39)	(1.72)
TLAG (+)	0.028	-0.268	-1.767***	-1.098*	-1.269
	(0.08)	(-0.71)	(-3.40)	(-1.73)	(-1.59)
Panel C: MTB					
NW (-)	-0.179***	-0.203***	-0.090	-0.181***	-0.127***
	(-3.55)	(-3.34)	(-1.36)	(-2.91)	(-2.68)
TONE (+)	2.426***	3.072***	1.530**	1.557**	2.475***
	(4.45)	(4.69)	(2.06)	(2.38)	(4.51)
TLAG (+)	-0.689*	-0.531	-1.315**	-0.969*	-0.465
	(-1.67)	(-1.03)	(-2.33)	(-1.90)	(-1.23)
Panel D: LEV					
NW (-)	-0.117***	-0.121***	-0.098	-0.140**	-0.123**
	(-2.62)	(-2.80)	(-1.46)	(-2.29)	(-2.33)
TONE (+)	1.564***	0.849	1.662**	1.795**	2.934***
	(3.25)	(1.38)	(2.53)	(2.53)	(5.47)
TLAG (+)	-0.560**	-0.385	-0.647	-1.351**	-0.709*
	(-2.24)	(-1.08)	(-1.14)	(-2.29)	(-1.80)
Panel E: HHI					
NW (-)	-0.116***	-0.139	-0.186***	-0.168***	-0.206***
	(-4.02)	(-1.68)	(-3.63)	(-2.87)	(-4.05)
TONE (+)	1.109***	2.946***	2.485***	2.895***	3.029***
	(3.05)	(3.72)	(3.54)	(4.99)	(4.34)
TLAG (+)	-0.495	-0.864*	-0.698	-0.847	-1.185**
	(-1.61)	(-1.90)	(-1.58)	(-1.26)	(-2.57)

$$TEX_{i,t} = \beta_0 + \beta_1 QRET_{i,t} + \beta_2 NEG_{i,t} + \beta_3 QRET_{i,t} \times NEG_{i,t} + \epsilon_{i,t} \quad (1)$$

Additional Analyses: Managerial Incentives

Table 9. Narrative Conservatism and Managerial Incentives

Dep. Variables	NW		TONE		TLAG	
	(1)	(2)	(3)	(4)	(5)	(6)
Panel A: SEO	NO	YES	NO	YES	NO	YES
(Pred. Sign)	(-)	(-)	(+)	(+)	(+)	(+)
QRET×NEG	-0.113**	-0.128***	1.891***	0.391	0.158	-0.343
	(-2.29)	(-2.61)	(3.29)	(0.63)	(0.32)	(-0.66)
Observations	17,937	17,919	17,937	17,919	17,937	17,919
Adjusted R-squared	0.649	0.678	0.595	0.634	0.632	0.685
Panel B: Option Value	LOW	HIGH	LOW	HIGH	LOW	HIGH
(Pred. Sign)	(-)	(-)	(+)	(+)	(+)	(+)
QRET×NEG	-0.084	-0.216***	0.225	0.654	-0.427	-0.702
	(-0.96)	(-2.97)	(0.29)	(0.89)	(-0.68)	(-1.36)
Observations	11,553	11,552	11,553	11,552	11,553	11,552
Adjusted R-squared	0.456	0.513	0.561	0.623	0.555	0.599
Panel C: Litigation Risk	LOW	HIGH	LOW	HIGH	LOW	HIGH
(Pred. Sign)	(-)	(-)	(+)	(+)	(+)	(+)
QRET×NEG	-0.107***	-0.058**	1.017***	0.691*	-0.290	-0.026
	(-3.11)	(-2.34)	(3.00)	(1.92)	(-1.05)	(-0.10)
Observations	58,945	32,661	58,945	32,661	58,945	32,661
Adjusted R-squared	0.626	0.688	0.532	0.620	0.620	0.611

$$TEX_{i,t} = \beta_0 + \beta_1 QRET_{i,t} + \beta_2 NEG_{i,t} + \beta_3 QRET_{i,t} \times NEG_{i,t} + \sum \beta_n CONTROLS_{i,t} + \epsilon_{i,t} \quad (1)$$

Conclusions

- **Conclusions**
  - We provide evidence that narratives reflect bad news in a more complete, news-consistent, and timely manner than good news.
  - Firms report lengthier 10-Qs to clarify rather than obfuscate bad news, and provide more 8-Ks and 8-K items in response to bad news than to good news.
  - We document greater narrative conservatism in the MD&A section and in voluntary disclosure. Also, narrative conservatism is pervasive in firms with high conditional conservatism, intangible assets, R&D expenses and proprietary costs.
  - We find greater narrative conservatism in settings where managers have strong incentives to disclose bad news.
- **Future Research**
  - An aggregate measure of narrative conservatism
  - Economic implications of narrative conservatism
  - Mechanisms that assure the credibility of narrative conservatism