

Consolidated or Standalone earnings - What do investors react to?

Sudhakar V Balachandran, University of Illinois Chicago

Sudershan Kuntluru, Indian Institute of Management Kozhikode

Hariom Manchiraju, Indian School of Business Hyderabad

Sumeet Rajput, Indian School of Business Hyderabad

Abstract:

When an entity exerts control over one or more entities, providing consolidated financial statements is the norm in several countries around the world. However, a unique financial reporting rule in India requires firms to provide annual financial statements at both the consolidated (parent + subsidiary) and standalone levels (parent only). The availability of two sets of financial information allows us to decompose the overall earnings in two components – parent and subsidiary. This decomposition allows us to examine whether stock market reacts differently to these two components. We find that the market places more weight on earnings surprise of parent compared to the earnings surprise of subsidiary. This differential treatment of parent versus subsidiary earnings surprise is consistent with the persistence of these two components of earnings. Overall, the findings of our paper indicate that the stock market finds disaggregation of earnings as parent versus subsidiary as informative and processes such information efficiently.

Keywords: Consolidated financial statements, Standalone financial statements, Information disaggregation, underreaction.

1. Introduction

Accounting standards (both US GAAP and IFRS) typically require an entity (the parent) to present consolidated financial statements if it controls one or more other entities (subsidiaries). These consolidated statements present combined financial information of the parent and its subsidiaries as if they were a single economic entity. In contrast to these well-established reporting practices prevalent in many countries across the world (Walker [1976]), India has a unique reporting requirement that requires firms to disclose both consolidated and standalone financial statements¹. The objective of this paper is to empirically examine the usefulness of these two sets of financial statements. Following extensive prior literature (Ball and Brown [1968], DeGeorge, Patel, and Zeckhauser [1999], Graham, Harvey, and Rajgopal [2005] etc), we consider earnings as a primary summary output of financial statements that is used by investors, analysts, boards, and various stakeholders in their decision making process. Hence, our specific research question is – how does the market incorporate consolidated and standalone earnings information in determining stock prices?

A priori the usefulness of standalone financial statements is unclear. On one hand it can be argued that consolidated financial statements are more comprehensive and subsumes all the information present in standalone statements. Hence standalone statements have limited or no information role in the presence of consolidated statements. However, on the other hand, theory suggests that any process of information aggregation can lead to a loss of information (Demski [1973], Pendlebury [1980]). This additional disclosure of standalone financial statements effectively allows the decomposition of the consolidated earnings in two components – one attributable to the standalone/parent (parent, hereafter) and the other attributable to all subsidiaries combined (subsidiary, hereafter). Such disaggregated earnings information allows

¹ Illustration of mechanics behind construction of Consolidated and Standalone statements as per the Indian Standards is provided in Appendix A1.

market to differentially price these components as per their respective quality. Therefore, standalone statements can still have a use despite the presence of consolidated statements.

To better explain the importance of our research question, we provide an illustration where we compare the earnings performance of two companies - Mphasis Ltd and HCL Technologies. Both these companies belong to the same industry (Information Technology) and have similar financial characteristics in terms of size, profitability, growth, etc. In the year 2019, Mphasis Ltd, reported a consolidated EPS of INR 56 / share, an improvement of INR 13 / share over the previous fiscal year. For the same year 2019, HCL Technologies reported a consolidated EPS of INR 73 / share which was an improvement of INR 11 / share over the previous fiscal year. Both these companies show similar earnings surprise and hence we can expect similar market reaction. However, when we examine the disaggregated EPS information, the difference in earnings performance is stark. In the case Mphasis Ltd, Δ EPS of INR 13 / share can be decomposed as Δ EPS of INR 2 / share coming from the parent company (standalone) and INR 11 / share coming from all the subsidiaries put together. In contrast, Δ EPS of INR 11 / share for HCL Technologies can be decomposed as Δ EPS of INR 7 / share coming from the parent company (standalone) and INR 4 / share coming from all the subsidiaries put together, Thus, in the first case the improvement over the previous period's consolidated EPS is driven by the improvement in the subsidiary EPS, whereas the improvement over the previous period's consolidated EPS in the second case is driven by the Change in the parent EPS. It is therefore important to examine whether investors consider improvement in earnings driven by parent and subsidiary differentially or do they just make their decision based on the improvement as in the consolidated earnings?

We draw our sample from the Prowess database maintained by CMIE (Centre for Monitoring Indian Economy). Our sample period is 2000-2020 and final sample comprises of

9,500 firm-year observations relating to 1,413 unique firms. This database is widely used in prior literature that uses India related data (Khanna and Palepu [2000], Bertrand, Mehta, and Mullainathan [2002], Gopalana, Nanda, and Seru [2007] , Manchiraju and Rajgopal [2017] , Li [2021]). The financial statement data is available for the consolidated entity as well as for the standalone parent level. We impute the financial performance of subsidiary as the difference between consolidated level measure and standalone measure. We find that on average subsidiary constitute 20% of the consolidated total assets, suggest that subsidiary can significantly affect the overall performance of the consolidated entity.

To address our research question, we regress the stock market reaction on consolidated earnings surprise ($ESUR_C$) decomposed as earnings surprise attributable to parent ($ESUR_P$) and earnings surprise attributable to subsidiaries ($ESUR_S$). We measure market reaction as a one-year market-adjusted buy-hold returns. Earnings surprise is defined as earnings (scaled by total assets) for the current year less earnings (scaled by total assets) for the previous year. Prior research (Bartov, Givoly, and Hayn [2002]) suggests that there is also an added premium in returns for meeting or beating (MBE) and penalty for missing ($MISS$) prior year targets. In our setting MBE can be achieved on three possible ways (i) improvement in both parent's and subsidiary's earnings, (ii) improvement in parent's earnings alone and not in subsidiary's, and (iii) improvement in subsidiary's earnings alone and not in parent's. Similarly, $MISS$ can also be achieved in three possible ways (i) decline in both parent's and subsidiary's earnings, (ii) decline in parent's earnings alone and not in subsidiary's, and (iii) decline in subsidiary's earnings alone and not in parent's. We include separate indicator variables for each of these indicator variables in our regression model.

When we consider contemporaneous stock returns as the dependent variable, we find that the market places a greater weight on the parent's earnings surprise compared to subsidiaries' earnings surprise. Furthermore, reward for MBE that is achieved due to surprise

in parent's earnings is greater than the reward for MBE that this achieved due to surprise in subsidiaries' earnings. When it comes to penalty for *MISS*, we find that there is no penalty if at a consolidated level the company misses the earnings benchmark but at a standalone level *MBE* is achieved. In fact, there is a reward in such a case. Overall, these findings suggests that the stock market differentially treats parent's earnings surprise and subsidiary's earnings surprise, giving greater weightage to the former.

We argue that the relationship between earnings components and returns is driven by the expected persistence of such earnings components. Thus, to determine whether the market is efficiently pricing the parent's and subsidiaries' earnings surprise, we examine the extent to which parent's vs subsidiaries' current period earnings predict one year ahead earnings. We find that parent's earnings has a greater explanatory power than the subsidiary's earnings in predicting future consolidated earnings and cashflows. The results of contemporaneous market reaction tests combined with earnings persistence tests indicate that the stock market finds the disaggregation of consolidated earnings as parent and subsidiary useful, and it prices these two components efficiently. To further rule out any mispricing, we regress one year ahead stock returns on components of current year earnings surprise and indicator variables represents various ways in which *MBE* or *MISS* is achieved based on the earnings surprise at parent and subsidiaries level. Any over or under reactions to parent vs subsidiary earnings surprise in the current period is likely to be reversed in the future period. We do not find evidence of mispricing of the subsidiary's earnings surprise getting corrected in the future.

Our final set analysis examines the cross-sectional variation in how stock market differentially prices parent versus subsidiary earnings surprise. We argue that the cross-sectional variation is driven by need for disaggregated information and the quality of information. We also posit that investors are likely to put lower weight on subsidiary earnings component when the quality of such subsidiary earning in poor as proxied by level of

discretionary accruals. We also expect that investors are likely to put lower weight on subsidiary earnings component when there are greater opportunities to manage earnings. Since the higher levels of monitoring, as indicated by institutional ownership and board independence, are likely to keep earnings management under check, we expect to see lower weight on subsidiary earnings component in firms with lower monitoring. Finally, following Beaver, Cascino, Correia, and McNichols [2019], we argue that standalone financial statements will be incrementally useful in highly levered firms because such standalone financial statement together with consolidated financial statements can help investor infer intragroup exposures relating to borrowing and lending. Hence, we expect to see differential weighing on parent versus subsidiary earnings surprise in firms with higher levels of leverage. Results of our cross-sectional analysis are consistent with these expectations.

Our paper contributes to the literature in several ways. First, we add to the literature that examines the relative advantages and disadvantages on disaggregated earnings. Theory work in this area (Demski [1973], Pendlebury [1980]) shows that disaggregation prevents information loss and hence is beneficial. There is limited empirical support, especially in the context of disaggregated information along the lines on parent and subsidiary financial statements. In the context of debt contracting, Francis [1986] and Beaver, Cascino, Correia, and McNichols [2019] show the usefulness of parent and subsidiary level information in addition to the consolidated financial statements. However, there is not much evidence on the usefulness of parent and subsidiary level disaggregated information in setting stock prices. Our paper is the first to examine how the market reacts to earnings surprise decomposed as parent and subsidiary component. We want to highlight that our decomposition of reported earnings into parent and subsidiary is possible only in countries such as India where the regulation mandates the disclosure of both standalone and consolidated financial statements. The same decomposition would not be possible in, for example, the United States since only consolidated

financials are required under US GAAP Accounting. Second, extensive prior literature decomposes earnings in its components and examines the persistence and market pricing of such components. Some prominent earnings components examined in the prior literature include - accruals and cash flows (Dechow [1994], Sloan [1996]), discretionary and non-discretionary components of accruals (Xie [2001]), GAAP and street components of earnings (Bradshaw and Sloan [2002]), regular and special items of earnings (Burgstahler, Jiambalvo, and Shevlin [2002]), etc. Unlike several studies in this area, our findings suggest that the stock market prices the earnings components efficiently. Finally, we also add to the literature that examines the market reaction to meeting or beating earnings benchmarks Bartov, Givoly, and Hayn [2002]. We show that the market reaction to MBE varies depending on whether such MBE is achieved based on parent or subsidiary earnings surprise.

The rest of the paper is structured as follows: Section 2 gives an overview of regulatory framework, Section 3 reviews the related literature and describes our research question, Section 4 outlines our research design and describes the data, Section 5 presents our empirical analysis, and Section 6 provides conclusion.

2. Regulatory Framework

In this section, we briefly describe the evolution of the regulatory framework around the reporting of consolidated and standalone financial statements in India and the rest of the world. When an entity (parent) controls one or more other entities (subsidiaries), many countries across the world require presentation of consolidated financial statements. For instance, the first reporting requirement for the preparation of a consolidated financial statement was issued by the New York Stock exchange (NYSE) in 1919 (Walker and Mack [1998]). Consolidated statements are required over parent-company reports in the United States since the early 1900s (Walker [1976]). The consolidated statements are mandated in the United

Kingdom since the 1920s. Australian Accounting Standard Board (AASB 1024) made the publication of consolidated statements mandatory for parent entities² in 1990. Regulators prefer a consolidated perspective rather than the parent firm disclosing subsidiaries as equity investments in its balance sheet because in essence parent and subsidiaries are single economic entity (even though they remain separate legal entities). Under this process (after making necessary adjustments), the consolidated balance sheet includes the gross assets and liabilities of both the parent and subsidiary company, and the income statement includes gross sales and expenses of the parent and subsidiary company rather than just the parent's share of the subsidiary company's net assets or income. Doing so, provides the overview of the whole group of businesses under the parent company's control.

Compared to the rest of the world, the reporting requirements in India have been very different historically. The Companies Act of 1956 administered by the Ministry of Corporate Affairs (MCA) under the Government of India (GOI), provides the regulatory framework for reporting of financial statements. Section 212 of The Companies Act 1956 requires that the parent company should provide the standalone financial statements where its investments in the subsidiaries are reported under the equity method. In addition, the parent company is also required to separately provide the financial statements of subsidiaries as an attachment. The standard setters were of the view that the disclosure of consolidated financial statements is not needed because financial statements of subsidiaries provide all the required information, and consolidated statements would not have added any more information on the same (Srinivasan and Narasimhan [2012]). However, a major drawback of this approach is it imposes significant costs on the users of financial statements if there were to construct, on their own, the consolidated financial statements from separate financial statements of the parent and

² Australian stock exchanges had required consolidated financial statement as part of listing obligation way before the AASB 1024

subsidiaries. Moreover, investors also do not have access to necessary information such as intercompany transactions that are needed to post elimination entries during the process of consolidation.

However, post-liberalization³ when India opened its economy to foreign capital, convergence with international accounting standards was felt necessary because increased financial comparability and reporting quality is known to facilitate foreign investment (Li, Ng, and Saffar [2021]). Around that time, the requirement for consolidated financial statements was outlined in the International Accounting standard 27, *Consolidated Financial Statements and Accounting for Investments in Subsidiaries*.⁴The IAS 27 mandated the consolidated financial statements of direct subsidiaries (> 50% of shareholding) and also where the parent firm exercises influence. With the objective to improve the comparability of Indian financial statements with those prepared in the rest of the world, the Institute of Chartered Accountants of India (ICAI) introduced Accounting Standard (AS) 21, *Consolidated Financial Statements*, effective from April 1, 2001.⁵ This accounting standard is broadly in line with the IAS 27. However, it is important to note that AS 21 does not mandate companies to present consolidated financial statements, but it states that if a company prepares consolidated financial statements to comply with some other statute or legislation, then it should be in accordance with AS 21. Taking this initiative, a step further, the Securities Exchange Board of India's (SEBI) modifies its listing obligation and disclosure requirement (LODR) in 2002 and mandates consolidated financial statements for all listed companies.⁶

³ Until 1991, India was closed economy. 1991-92 onwards India undertook economic reforms which focused on liberalization and privatization.

⁴ The International Accounting Standards Board (IASB), a London-based independent international standard-setting body, released the International Accounting Standards (IAS) in the past. In 2001, International Financial Reporting Standards took the place of the IAS (IFRS).

⁵ ICAI (equivalent to AICPA, in the USA) is statutory body which sets standards for accounting and auditing processes. Ministry of Corporate Affairs under the Government of India then notifies these standards.

⁶ SEBI is regulator of capital markets in India (equivalent to the Securities Exchange Commission SEC in the USA) and specifically Regulation 33 mentions regarding consolidated financial statements preparation

In 2013 India implemented a major policy reform by overhauling the old Companies Act 1956 to incorporate several provisions relating to improving the ease of doing business, protecting shareholder rights, improving corporate governance and other oversight mechanisms, improving the transparency and disclosure norms, etc. The revised Companies Act 2013, requires all the firms, listed and unlisted, to prepare consolidated and standalone financial statements. Following this regulatory Change, the ICAI developed IFRS converged Ind AS110, *Consolidated Financial Statements*, This Standard shows a parent's and subsidiary's financial statements as a unified economic entity. Ind AS 27, *Separate Financial Statements*, provides separately the parent's financial statements on a standalone basis.⁷ Unlike AS 21, Ind AS 110 prepares consolidated financial statements mandatory for the parent firms without being conditioned on any other statute.

We summarize the evolution of this regulatory requirement in India in Figure 1.

< Insert figure 1 here >

3. Related Literature and research question

In India, the regulations enacted in 2001 made two sets of financial statements available for the investors. Standalone statements are for the reporting entity commonly referred to as the “parent”. Consolidated is the combination of the parent, and any subsidiaries that the parent may control. Correspondingly we can view the difference between standalone and consolidated as financial information about the subsidiaries. Given that there is information now at both the parent and subsidiary level, a question that users of financial statements often face is - which

⁷ These Indian Accounting Standards (Ind AS) were adopted on April 1, 2016, initially for listed firms with a net worth of more than 500 crores. Moreover, companies with a net worth of 250 crores have been subject to the law since April 1, 2017. From April 1, 2019, the regulatory requirement applied to banks, insurance firms, and financial service companies.

of these financial statements are more important and whether there are guidelines on when we should focus on one vs the other.

In interviews, financial executives and analysts offer differing perspectives on the relative importance of the two sets of financials. Paritosh Basu, former CFO of Essar Group argues “Both are required for any decision making. The logic behind this is standalone financial statements like stem of a tree and consolidated financial statements like full tree which includes various branches, fruits, flowers, etc.” Others such as Dr S. R. Korivi of NIFM argue that information in standalone may be more useful for assessment of profit, while information for consolidated may be more useful for assessing leverage and the strength of the firm’s capital structure overall. In addition, executives suggest that both the relative size of the subsidiaries (S. Guntapalli, Kotak Mahindra Asset Management) or the extent of influence or control the parent has over the subsidiaries (Yadnaya Investment Academy) may determine the relative usefulness of standalone vs. consolidated financial statement information. These differing views motivate us to undertake an empirical analysis of the usefulness of consolidated vs standalone earnings to investors as there are benefits and shortcomings in each of these measures.

Consolidation of financial statements has several advantages. First, consolidating financial statements involves aggregating parent and subsidiary information as if they were a single economic entity. The process of consolidation therefore ensures that the parent company is unable to use intercompany transactions to show improvement in its performance. For instance, in the year 2000 when consolidation was not required in India, the profit before tax for Zee Telefilms Ltd. (ZTL) increased from INR 80.6 crore in 1999 to INR 288.2 crore. Due to this improvement in profits, there was a significant positive stock price reaction. However, at a later point of time when detailed annual reports were made available, it was observed that the main driver of the profits was and intercompany transaction where the parent company ZTL

sold a part of its library to its subsidiary Asia Today, Ltd. If consolidated statements had been in place, such intercompany transaction would have been eliminated and the stock market reaction would have been more modest. This illustrates the necessity of reporting consolidated financial statements. Second, under the constraints of information processing costs, consolidated financial statements provide information to investors that is sufficient for their decision making. Simon [1990], argues that, following the concept of bounded rationality, limited knowledge and information processing capacity influences the rational choices of the decision maker. Similarly, Lu [2019] demonstrates that when investors' attention is limited, providing more data alters the nature of the information extraction process, which can cause information loss. Hence consolidated statements prevent information overload and hence prevent information loss. For instance, in our sample Tata Steel Ltd. has 287 subsidiaries. We argue that it will be practically impossible for investors to efficiently process the disaggregated information of all 287 subsidiaries. The overall subsidiary performance measure that can be imputed by subtracting parent earnings from consolidated earnings is also highly aggregated as it combines performance of 287 subsidiaries. Such overall subsidiary measure also suffers from the same limitations that a consolidated earnings measures does, thereby making consolidated earnings measure a more parsimonious measure. Finally, Arya and Glover [2014] argue that aggregation of information can aid decision-making because it can communicate appropriate information and allow for offsetting errors. Along similar lines, Dye and Sridhar [2004], as well as Arya and Glover [2014] argue that aggregate information can play a vital role in designing an agent's contract. Designing contracts based on aggregate information can increase the principal's monitoring due to the limited cost and time involved, limit managers' ability to cherry-pick the performance component of their choice, improve managerial productivity and reduce information asymmetry for the other stakeholders. These arguments suggest that consolidated financial statements (as required in the US GAAP and IFRS) provide

sufficient information to investors and there might not be much role for additional reporting of standalone financial statements.

Nevertheless, the consolidation process has several disadvantages thereby making additional reporting of standalone statements useful. First, prior literature on benefits of disaggregation (e.g. Demski [1973], Pendlebury [1980]) argues that consolidation leads to information loss. They contend that consolidated statements represent a financial overview of the entire group, hence diversity in operations among group firms and crude form of line-by-line aggregation would not satiate the informational needs of the investors. For instance, consolidated financial statements of Reliance Industries Limited (RIL) would reflect a combined performance of oil refinery and distribution, retail, telecom, and other businesses. Clearly, any additional information about the performance of standalone and various subsidiaries will be incrementally useful over and above the information on consolidated performance. This would be consistent with the findings documented in Song [2021] who shows that disaggregation along industry segments is associated with more analyst following, lower error and dispersion in analyst forecasts, and more robust information transfers. Second, to prop up the consolidated entity performance, parent entity can take advantage of fact that subsidiaries are often unlisted and do not need to provide detailed financial statements. For instance, Beuselinck, Cascino, Deloof, and Vanstraelen [2019] find that in the absence of subsidiary-level information and subsidiary operating in a weak institutional setting, firms can manage subsidiary earnings due to low visibility to present favourable financials at the consolidated level. Presence of standalone financial statements is likely to provide useful information to investors to identify propping up behaviour. Overall, the availability of the disaggregated parent and subsidiary information in addition to the consolidated information give investors an opportunity to examine the relative quality of the two earnings components and price them accordingly.

The empirical evidence on the usefulness of disaggregated earnings information relating to parent vs subsidiary earnings is limited, but points to usefulness of disaggregated information. Francis [1986] show that disclosure of standalone as well as consolidated statements is incrementally valuable to creditor over the disclosure of only consolidated financial statements. Similarly, Beaver, Cascino, Correia, and McNichols [2019] show that subsidiary information, over and above group-level consolidated information improves the prediction of parent level default, possibly because the process of consolidation nets off the intragroup exposures relating to borrowing and lending. There is scant evidence on the usefulness for disaggregated parent and subsidiary information for equity investors. Our paper fills this gap in the literature.

4. Research Design and data

4.1. Regression model

Our research design builds on extensive prior research that examines the stock market reaction to earnings surprise (Ball and Brown [1968], Degeorge, Patel, and Zeckhauser [1999], Skinner and Sloan [2002]) and its components (Dechow [1994], Sloan [1996], Burgstahler, Jiambalvo, and Shevlin [2002], Hsu and Kross [2011]). We regress the stock market reaction on earnings surprise decomposed as earnings surprise attributable to parent ($ESUR_P$) and earnings surprise attributable to subsidiaries ($ESUR_S$), and an indicator variable to capture whether current year consolidated earnings meets or beats (MBE) expectation. Our baseline model is –

$$BHR_{i,t} = \alpha_0 + \beta_1 * ESUR_{P_{i,t}} + \beta_2 * ESUR_{S_{i,t}} + \beta_3 * MBE_{i,t} + \beta_4 * Size_{i,t} + \beta_5 * Beta_{i,t} + \beta_6 * BM_{i,t} + \varepsilon_0 \quad (1)$$

where BHR is contemporaneous one-year market-adjusted buy-hold returns for a firm i during year t . For calculating BHR, compounding starts nine months before the fiscal year ends and

three months after the fiscal year ends. $ESUR_{P_{i,t}}$ is the earnings surprise for parent firm i in period t defined as the difference between the profit after tax in period t and $t-1$ as reported in standalone financial statements, scaled by total assets reported in the consolidated balance sheet in period t . $ESUR_{S_{i,t}}$ is the earnings surprise for all subsidiaries of firm i in the period t and $t-1$, scaled by total assets as reported in consolidated financial statements, where subsidiaries earnings are imputed as the difference between profit after tax reported in the consolidated income statement and profit after tax reported in the standalone (parent) statement in period. $MBE_{i,t}$ is an indicator variable for meeting or beating prior year earnings; it receives a value of 1 if earnings improved over the previous period i.e. $\Delta Earnings_{C_{i,t}} \geq 0$, otherwise 0. In our model we also control for variables that are known to affect stock prices. These variables include - $Size_{i,t}$ which is the natural logarithm of the market value of equity, $Beta_{i,t}$ is a three-year market beta introduced to control for systematic risk. $BM_{i,t}$ is calculated by dividing the company's book value of equity by its market value of equity at the end of period t . We use the Fama-MacBeth 1973 method with the Newey-West 1987 correction for serial correlation to estimate this equation. We expect positive signs on β_1 , β_2 and β_3 coefficients, consistent with the stock market reacting positively to earnings surprise and there is a reward for MBE. A finding of $\beta_1 = \beta_2$ would indicate that the market gives equal weightage to parent and subsidiary earnings surprise while determining stock price.

We further expand equation (1) to examine whether the stock market reward for MBE and penalty for $MISS$ (missing the earnings target) varies depending on the relative contribution of parent and subsidiary earnings surprise in achieving MBE or $MISS$. Specifically, we estimate the following equation -

$$\begin{aligned}
BHR_{i,t} = & \alpha_0 + \beta_1 * ESUR_{P_{i,t}} + \beta_2 * ESUR_{S_{i,t}} + \beta_3 * MBEP1S1_{i,t} + \beta_4 * MBEP1S0_{i,t} \\
& + \beta_5 * MBEP0S1_{i,t} + \beta_6 * MISSP1S0_{i,t} + \beta_7 * MISSP0S1_{i,t} + \beta_8 * Size_{i,t} \\
& + \beta_9 * Beta_{i,t} + \beta_{10} * BM_{i,t} + \varepsilon_0
\end{aligned} \tag{2}$$

where *MBEPISI* is an indicator variable that equals 1 if a firm achieves *MBE* at consolidated entity level and such *MBE* is achieved due to positive earnings surprise at both parent and subsidiary level, and zero otherwise. *MBEPISO* is an indicator variable that equals 1 if a firm achieves *MBE* at consolidated entity level and such *MBE* is achieved due to positive earnings surprise at parent level alone and subsidiary reports negative earnings surprise, and zero otherwise. *MBEPOS1* is an indicator variable that equals 1 if a firm achieves *MBE* at consolidated entity level and such *MBE* is achieved due to positive earnings surprise at subsidiary level alone and parent reports negative earnings surprise, and zero otherwise. *MISSPISO* is an indicator variable that equals 1 if a firm misses the earnings target at consolidated entity level and such *MISS* is achieved due to negative earnings surprise at subsidiary level alone, with parent reporting positive earnings surprise, and zero otherwise. *MISSPOS1* is an indicator variable that equals 1 if a firm misses the earnings target at consolidated entity level and such *MISS* is achieved due to negative earnings surprise at parent level alone, with subsidiary reporting positive earnings surprise, and zero otherwise. All other variables are as previously defined for equation (1). For the ease of reference, in Appendix A2 we lay out the possible paths in which *MBE* and *MISS* can be achieved. If the stock market does not differentiate how *MBE* is achieved i.e. whether it is driven by earnings surprise of parent or that of the subsidiary, then we expect $\beta_4 = \beta_5$. Similarly, if the market does not differentiate how a firm misses the earnings benchmark, then we expect $\beta_6 = \beta_7$.

We further examine whether the market pricing of these earnings components is consistent with their persistence. *Ceteris paribus*, in determining stock prices the market will place greater weightage on the component of earnings that has higher persistence. To test the persistence of parent and subsidiary earnings, we regress one year ahead earnings on current year earnings Dechow, Ge, and Schrand [2010]. Specifically, we estimate the following model:

$$\begin{aligned}
EARN_{C_{i,t+1}} = & \alpha_0 + \gamma_1 * EARN_{p_{i,t}} + \gamma_2 * EARN_{s_{i,t}} + \gamma_3 * Size_{i,t} \\
& + \gamma_4 * Beta_{i,t} + \gamma_5 * BM_{i,t} + \varepsilon_0
\end{aligned}
\tag{3}$$

where *EARN* is profit after tax scaled by total assets and subscript C, P and S refer to consolidated, parent, and subsidiary, respectively. All the other variables are same as described in model (1) and also described in Appendix A3. A finding of coefficient $\gamma_1 = \gamma_2$ will indicate that both parent and subsidiary earnings have equal persistence.

4.2. Sample and data

Our starting sample consists of 26,455 firm-year observations from 2000 – 2020. We use the Prowess database maintained by CMIE (Centre for Monitoring Indian Economy), which is widely accepted and used in academic research utilizing India related data (Khanna and Palepu [2000], Bertrand, Mehta, and Mullainathan [2002], Gopalana, Nanda, and Seru [2007], Manchiraju and Rajgopal [2017], Li [2021]). We impose the following restrictions to arrive at our final sample. First, we retain only firms with march year-end, which reduces our sample size by 1,449 firm-year observations. Second, to reduce the effect of extremely small firms, we discard firm-year observations with sales and total assets reported on a consolidated and parent basis of less than INR 1 million. In this step we lose 3,210 firm-year observations. Third, we also eliminate observations with total assets at a consolidated level less than total assets at the parent level. Such observations are likely to reflect data quality issues. We lose 5,306 firm-year observations in this step. Fourth, we drop 335 observations with missing values of sales, total assets, net income, the book value of equity, and cash flow from operations on both consolidated and parent basis. Fifth, for our empirical analysis, we need earnings surprise, the difference between profit after tax in periods t and t-1 scaled by total assets as reported in consolidated statements. Therefore, we drop 2,397 firm-year observations with a missing earnings surprise. An essential part of our analysis is the contemporaneous and future returns

tests. Hence, our final data filter relates to availability of stock price data. We drop unlisted firms. We then use stock prices from the National Stock Exchange (NSE) and Bombay Stock Exchange (BSE), two of the country's major stock exchanges⁸. Since BSE has more firms listed on it, we primarily considered NSE stock prices and market capitalization and used BSE data wherever NSE data is missing values. For our returns test, we calculate BHR (Buy-Hold return), which is one-year market-adjusted buy-hold returns where compounding starts 9 months before the fiscal year-end and ends 3 months after the fiscal year-end Hsu and Kross [2011]. Therefore, we need 12 months of data to calculate BHR; hence we eliminate all those values with less than 12 months of returns data. We use book-to-market and market beta as controls in our return test. Beta calculated is 3-year market beta, and the benchmark index used is NIFTY 500⁹. We drop observations with missing values of stock returns, index returns, market capitalization, beta, and book-to-market ratio. We also eliminate observations with a beta value and book-to-market ratio of less than 0. Overall, we lose 4,258 firm-year observations due to these stock price related data. Hence, our final sample consists of 9,500 firm-year observations. Table 1 summarizes the sample selection.

<<Insert Table 1>>

We describe the year-wise and industry-wise sample distribution, in panel A and panel B of Table 2, respectively. We find that the data availability increases with time. Our industry classification is based on industry divisions as specified in National industry classification 2008, by Central Statistical Organisation, Ministry of Statistics and programme implementation, Government of India. We find that Manufacturing, Information and communication, and Construction are the top three industries in terms of sample data.

⁸ Market cap of both the stock exchange is around \$3 Trillion <https://www.livemint.com/market/stock-market-news/after-bse-market-cap-of-nse-firms-hits-a-record-3-tn-as-stocks-rally-11622094856033.html>

⁹ It reflects the top 500 firms in the eligible universe based on complete market capitalization. https://www1.nseindia.com/products/content/equities/indices/nifty_500.htm

<<Insert Table 2>>

Table 3 provides descriptive statistics for our overall sample. In panel A, we report statistics relating to consolidated financials. On average a firm in our sample has 8.7 subsidiaries. Mean consolidated total assets is 24.45 (INR Billions). Subsidiary firms contribute, on average, around 19.44% of the total assets of the consolidated total assets suggesting that they form an important component of the overall economic entity and have potential to significantly affect the performance at a consolidated level. The average return on asset (ROA) for firms in our sample is 3.9%. In our sample 45.8% firm-year observations show improvement in previous year ROA. In terms of governance, in 24.38% of our sample the ownership of institutional investors is greater than the ownership of non-promoter retail investors. Further, on average 44.79% of the board members are independent.

In panel B, we compare the mean and median values of certain key financial indicators at parent and subsidiary level. ROA is higher for the parent or standalone component of the consolidated entity compared to the subsidiary component. However, earning volatility measured as the standard deviation of ROA estimated over 5-year estimation period, is much higher for subsidiaries (34.1%) than for parent (3.5%) and consolidated level (3.3%). The discretionary accruals of subsidiaries are also higher than the discretionary accruals of the parent entity. Another noteworthy statistic in this table relates to leverage, defined as the ratio of total liabilities to total assets. The average leverage at the parent level is 0.49, whereas the average leverage for subsidiaries is 0.85, suggesting that companies prefer to have more debt in their subsidiaries than in the parent company.

<< Insert Table 3>>

5. Empirical Analysis

5.1. Contemporaneous market reaction to earnings surprise

We present the results from estimating equation (1) in Table 4. In column (1) we regress 12-month BHR on earnings surprise at a consolidated level and an indicator variable from meeting or beating earnings expectations. As shown in model (1), we find a positive and statistically significant coefficient of $ESUR_C$. This is consistent with extensive prior literature starting Ball and Brown [1968] that documents a positive association between earnings and stock returns. The coefficient on MBE is positive and statistically significant at a 0.01 level. Controlling for earnings surprise and other determinants of stock returns, firms achieving MBE have 16.0% higher return compared to firms that do not achieve MBE. The finding is consistent with the premium for meeting or beating expectations documented in the prior literature (Bartov, Givoly, and Hayn [2002]). We find similar results in column (2) where we regress one-year contemporaneous stock returns on earnings surprise at a standalone level and an indicator variable from meeting or beating earnings expectations. We find a positive association between returns and standalone earnings surprise and there is a premium for MBE.

In column (3) we regress one-year contemporaneous stock returns on earnings surprise at a consolidated and standalone level and an indicator variable from meeting or beating earnings expectations. This test enables us to determine whether the stock market relies more on consolidated or standalone earnings in determining stock prices. We find the coefficient on both consolidated earnings surprise $ESUR_{C_{i,t}}$ (coeff = 0.618, p-value < 1%) and standalone earnings surprise $ESUR_{P_{i,t}}$ (coeff = 1.228 p-value < 1%) are positive and significant, suggesting that stock market incorporates both components of earnings in determining stock prices. However, the coefficient on the standalone earnings surprise is statistically greater than the coefficient on the consolidated earnings surprise (F-stats = 3.83, p-value < 10% level),

suggesting that standalone earnings surprise is more useful in determining stock prices. Since consolidated earnings comprises of both parent and subsidiary, the overall coefficient on parent earnings surprise can be considered as 1.846 (=1.228 + 0.618) and that on the subsidiary earnings surprise will be 0.618.

A similar result is shown in column (4), where we decompose the consolidated earnings surprise into $ESUR_{p_{i,t}}$ (parent component) and $ESUR_{s_{i,t}}$ (Subsidiary component). We find that positive and significant coefficients on both $ESUR_{p_{i,t}}$ (coeff = 1.854, p-val < 1%) and $ESUR_{s_{i,t}}$ (coeff = 0.85, p-val < 1%). However, the coefficient on the parent component of earnings surprise is statistically greater than the coefficient on the subsidiary component of earnings surprise (F-stats = 7.59, p-value < 1%). Overall, these results indicate that the stock market differentially weighs the parent's and subsidiary's component of earnings surprise and more weight is given to the parent's component.

<< Insert Table 4 >>

In table 5, we present our analysis where we attempt to identify whether reward to *MBE* and penalty for *MISS* vary depending on whether parent or subsidiary earnings surprise leads to such *MBE* or *MISS*. In panel A, we present the univariate results. We find that 46% of all our firm-year observations achieve *MBE* at the consolidated earning level whereas the remaining 54% do not show improvement over previous year's earnings and hence classified as *MISS*. There is substantial variation in how *MBE* is achieved. In the sub-sample of firm-year observations that achieve *MBE* at the consolidated earnings level, there is improvement over previous year's earnings - at both parent and subsidiary level (*MBEPIS1*), only at parent level and not at subsidiary level (*MBEPIS0*), and only at subsidiary level and not at parent level (*MBEPOS1*), in 52%, 30%, and 18% observations, respectively. The average one-year BHR (Buy-Hold return) for firms classified *MBEPIS1*, *MBEPIS0*, and *MBEPOS1* is 23%,

15.6%, and 3.6%, respectively. This result suggests that the stock market performance of firms classified based on improvement in consolidated earnings varies based on the source of improvement, i.e., markets reward is greater if parent firms drive the improvement. We also examine the stock market penalty for not showing improvement in the previous year's earnings. In the sub-sample of firm-year observations that are classified as *MISS*, there is decline over previous year's earnings - at both parent and subsidiary level (*MISSPOS0*), only at parent level and not at subsidiary level (*MISSPISO*), and only at subsidiary level and not at parent level (*MISSPOSI*), in 51%, 14%, and 35% observations, respectively. The average one-year BHR (Buy-Hold return) for firms classified *MISSPOS0*, *MISSPISO*, and *MISSPOSI* is -13%, -2.2%, and -9.9%, respectively. This finding suggests that penalty for missing the earnings target is greater if such negative surprise is driven by decline in the parent's earnings.

In panel B of Table 5, we present the results from estimating model (2). In this model, our coefficients of interest are- *MBEPIS1*, *MBEPISO*, *MBEPOS1*, *MISSPISO*, and *MISSPOSI*, that capture various ways in improvement or decline in previous year's consolidated earnings. The intercept term captures *MISSPOS0* will relate to firm that *MISS* the earnings target and such decline is driven by negative earnings surprise at both parent and subsidiary level. Results of regression analysis are similar to those documented in the univariate analysis. The coefficient on *MBEPIS1* is 0.221, statistically significant at a 0.01 level. This can be inferred as firms registering an improvement in consolidated earnings due to improvement in both parent and subsidiary earnings has a BHR of 22% higher than firms that register a decline in consolidated earnings due to a decline in both parent and subsidiary earnings. The coefficient of *MBEPISO* (0.184) is statistically significant, greater, and different than the coefficient on *MBEPOS1* (0.089). This result validates that market underreacts to consolidated earnings improvement driven by the subsidiary. Additionally, in *MISSPISO*, we find a reward indicated by 0.095 at 0.01 level significance, despite missing the target or declining consolidated

earnings. Hence this result indicates that despite a decline in consolidated earnings driven by subsidiary earnings, if parents' earnings improve, the market responds favourably to such firms. Taken together, the results so far suggest that the stock market does not fixate at consolidated earnings and that it differentially reacts to the parent and subsidiary component of earnings surprise.

<< Insert Table 5 >>

5.2.Persistence of parent and subsidiary component of earnings

From the contemporaneous returns test, we can infer that market underweights subsidiary earnings relative to the parent's earnings surprise. To investigate whether the market's underweighting of the subsidiary's earnings is appropriate, we examine the extent to which the parent's vs. subsidiary's earnings predict future earnings and future cash flows. Extensive prior research e.g, Dechow, Ge, and Schrand [2010] suggests that market should price different components of earnings as per their relative persistence. In determining stock prices, components of earnings that are less persistent should be weighed lower than components of earnings that are more persistent. Given our previous finding that the market places lower weight on subsidiary earning surprise compared to parent earnings surprise, efficiently pricing would suggest that the persistence of subsidiary earnings are likely to be lower than the persistence of parent earnings. Any finding contrary to this would be indicative of mispricing.

We present the results from estimating model (3) in Table 6. The ability of current year parent and subsidiary earnings in predicting one year ahead parent, subsidiary and consolidated earnings is shown in columns (1)-(3), respectively. In column (1) the coefficient on parent's earnings is positive and significant (coeff = 0.583, p-val <1%). It shows that 58% of current year parent earnings map into future parent earnings. In column (2) the coefficient on

subsidiary's earnings is also positive and significant (coeff = 0.478, p-val <1%) indicating that 47.8% current year subsidiary earnings map into future subsidiary earnings. These results suggest that both parent and subsidiary earning are persistent. To evaluate which of these two components are more persistent, in column (3) we examine the predictive ability of parent and subsidiary earnings for future consolidated earnings. The coefficient on both the parent and subsidiary components are positive and significant. However, both coefficients are statistically different, and the coefficient on the parent component (0.645) is greater than the subsidiary component (0.551). An F-test rejects the hypothesis of equality of these coefficient (p-value < 1%). The nature of the results is similar in columns (4)-(6), where we document the ability of current year parent and subsidiary earnings in predicting one year ahead parent, subsidiary, and consolidated cash flows, respectively.

Overall, the findings of persistence tests and contemporaneous returns tests are consistent with one another. Subsidiary's earnings are less persistent than parent's earnings and hence the stock market places lower weight on subsidiary's earnings surprise compared to parent's earnings surprise in determining stock prices. These results suggests that the disaggregated earnings information of earnings is useful to the market.

<<Insert Table 6>>

5.3.Future Return Test:

While the contemporaneous stock market reaction and earnings persistence tests provide evidence of stock market efficiently processing the disaggregated earnings information, as an additional check, we also examine the association of current year disaggregated earnings surprise and one year ahead returns. To the extent there is any over or underreaction to parent versus subsidiary earnings surprise in the current year, such mispricing is likely to be corrected in the subsequent year(s). We use a modified version of model (2) to

check this possibility. We regress future *BHR* (one-year market-adjusted buy-hold returns for a firm *i* during year *t+1*) on both current year earnings surprise components, and indicator variables for various ways in which improvement or decline over previous year earnings is achieved. We find the coefficients on $ESUR_{P_{i,t}}$ and $ESUR_{S_{i,t}}$ to be statistically insignificant. This can be inferred as investors having fully incorporated the information contained in the parent and subsidiary earnings surprise in the contemporaneous stock returns itself, leaving no need for a correction in future period returns. The coefficient on *MBEPISI* is positive and significant, which is indicative of post earnings announcement drift Bernard and Thomas [1989] drift reverses in the last quarter of the annual year.

<< Insert Table 7 >>

5.4. Cross sectional variation

Next, we focus on cross-sectional variation in the market response to the decomposed components of earnings surprise (parent and subsidiary). The purpose of the cross-sectional tests is to understand conditions in which market impose differential weights on the parents and subsidiary components. We predict that markets differentially weigh components based on the need for disaggregated information and the quality of such information. Accordingly, we identify level of discretionary accruals, monitoring and leverage as factors that drive the cross-sectional variation of our results.

First, we divide sample based on quality of subsidiary earnings. Following prior literature, we use discretionary accruals to proxy for accrual-based earnings management. We use the following modified Jones model (Dechow, Sloan, and Sweeney 1995) to estimate discretionary accruals:

$$ACCRUALS_t/A_{t-1} = \alpha_0 + \alpha_1[1/A_{t-1}] + \alpha_2[(\Delta SALE_t - \Delta TR_t)/A_{t-1}] + \alpha_3[PPE_{t-1}/A_{t-1}] + \varepsilon_{i,t} \quad (4)$$

Where consistent with previous studies on earnings management $ACCRUALS_t$ is computed as change in current assets from $t-1$ year to year t ($\Delta Current_Assets_t$) minus change in current liabilities from $t-1$ year to year t ($\Delta Current_Laibilities_t$) minus change in cash and cash equivalent from $t-1$ year to year t ($\Delta Cash_t$) plus change in debt included in current liabilities from $t-1$ year to year t ($\Delta Short_term_borrowing_t$) minus depreciation expense in year t ($Depreciation_t$); $\Delta SALE_t$ is change in net sales from year $t-1$ to year t ; ΔTR_t is change in trade receivable from year $t-1$ to year t ; and PPE_t is property, plant, and equipment in year t . We estimate the above regression cross-sectionally for industry-years with at least 10 observations. The residuals from equation (4) represent discretionary accruals ($DACC$). We consider firms' earnings quality as poor if the accruals and discretionary accruals are positive. We present the results of this subsample analysis in table 8. Columns (1) and (2) relate to subsample where total accruals at subsidiary level are positive and negative, respectively. Similarly, in column (3) discretionary accruals are positive whereas in column (4) discretionary accruals are negative. For the sake of parsimony, we discuss results relating to discretionary accruals. In column (3) the coefficient on parent's earnings surprise is positive and significant (coef: 2.115, p-value < 1%) whereas the coefficient on subsidiary's earning surprise is statistically insignificant. This finding suggests that when the subsidiary earnings quality is poor the market places lower weight in its earnings surprise. No such differential pricing of earnings surprise components is seen in column (4) where discretionary accruals are negative and hence less indicative of poor earnings quality.

<<Insert Table 8>>

Next, we divide sample based on the level of monitoring. We consider two dimensions of monitoring – institutional ownership and board independence. We expect the earnings quality to be low when monitoring is low. In such cases we expect the market to place lower weight on subsidiary's earnings surprise. We estimate equation (1) separately for these

subsamples and present the results in Table 9. Columns (1) and (2) relate to high versus low institutional ownership. We define institutional ownership as high if the percentage of institutional ownership in a firm is greater than non-institutional ownership, and zero otherwise. Similarly, columns (3) and (4) relate to high versus low board independence, where we classify firms as having high board independence if the ratio of number of independent directors divided by total number of directors is above median, and zero otherwise. We find that in the subsample of firms with high institutional ownership there is no differential weighing of the parent and subsidiary earnings surprise evident from the F-test (0.05). It suggests that market relies on the monitoring role of institutional investors in ensuring earnings quality and hence does not undertake costly processing of disaggregated information. However, in the subsample where institutional ownership is low, we find that the market places higher weight on parent's earnings surprise and lower weight on subsidiary's earnings surprise. Results documented in columns (3) and (4) are similar. Overall, these results suggest that market weighs components of earnings based on their perceived quality.

<<Insert Table 9>>

Finally, we examine the cross-sectional variation of our results based on leverage. Beaver, Cascino, Correia, and McNichols [2019] find that disaggregated information about the parent and subsidiary financial statements is informative about intergroup lending and borrowing transactions, thereby improving the prediction of default. Building on these arguments, we expect investors to pay greater attention to parent versus subsidiary earnings surprise and price them differentially in firms with higher leverage. To test this prediction, we divide firm-year observations into groups of above and below annual industry median leverage at consolidated, standalone and subsidiary level, respectively. We estimate equation (1) separately in each of these subsamples and present the results in Table 10. In columns (1) and (2) we show results relating to subsamples based on above and below median leverage at

consolidated level. We find that in the subsample of firms with above median leverage the stock market places greater weight on parent earnings surprise (coeff = 1.73, p-value < 1%) and on the subsidiary earnings surprise (coeff = 0.49 , p-value insignificant) in determining stock prices. However, in below median group stock market does not differentially weigh parent (coef = 2.06, p-value < 1%) and subsidiary (coef = 1.41, p-value < 5%) components of earnings surprise in determining stock prices. The results relating to sub-sample analysis for above and below median leverage at parent level (columns (3)-(4)) and subsidiary level (columns (5)-(6)) are similar. Overall, these results suggest that investors find disaggregated information useful in highly levered firms.

<<Insert Table 10>>

6. Conclusion

Unlike several countries in the world where a firm is required to present only its consolidated financial statements, India has a unique financial reporting requirement because of which firms disclose both standalone (parent only) and consolidated financial statements. The availability of two sets of financial statements in India raises the question of whether standalone statements are useful at all, given that the consolidated financial statements subsume all the information present in the standalone statement. We address this question by examining the stock market response to parent and subsidiary earnings surprise (which can be imputed by subtracting parent earnings surprise from consolidated earnings surprise).

We find that stock market differentially reacts to the parent and subsidiary component of earnings surprise. The coefficient on the parent component is weighted higher than the subsidiaries earnings surprise. Reward for MBE is higher when parent is source of consolidated MBE. Similarly, the penalty for MISS is lower when subsidiary (and not the parent) is the source of consolidated MISS. Hence, market systematically underweights subsidiaries. To

investigate whether the market's underweighting of the subsidiary's earnings is appropriate we perform persistence test. Dechow, Ge, and Schrand [2010] suggests that market should price different components of earnings as per their relative persistence. We find that subsidiary earnings and cash flow have lower persistence. Hence, we infer that market efficiently prices parent and subsidiary components. Overall, our results indicate that market weighs components of earnings efficiently based on the quality of information.

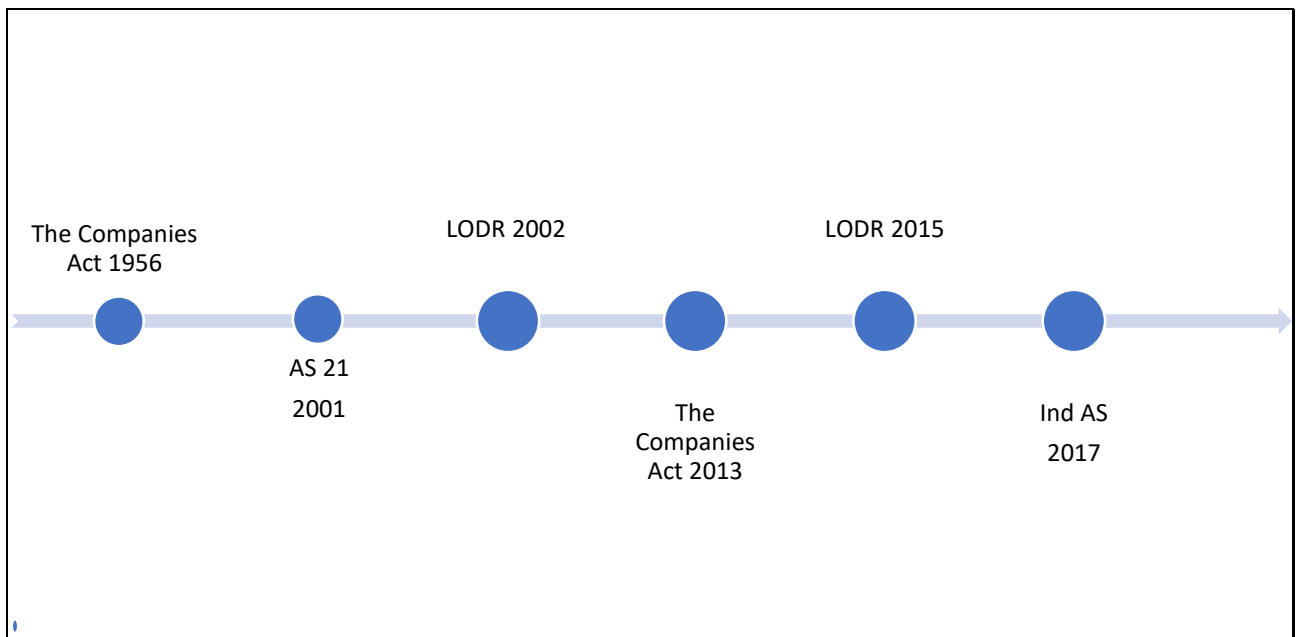
References

- Arya, A., and Glover, J. C. (2014). On the upsides of aggregation. *Journal of Management Accounting Research*, 26(2), 151-166.
- Ball, R., and Brown, P. (1968). An Empirical Evaluation of Accounting Income Numbers. *Journal of Accounting Research* .
- Bartov, E., Givoly, D., and Hayn, C. (2002). The rewards to meeting or beating earnings expectations. *Journal of accounting and economics*. *Journal of accounting and economics*, 33(2), 173-204.
- Beaver, W. H., Cascino, S., Correia, M., and McNichols, M. F. (2022). Group Affiliation and Default Prediction. *Management Science*, 65(8), 3559–3584.
- Bernard, V., and Thomas, J. (1989). Post-Earnings-Announcement Drift: Delayed Price Response or Risk Premium? *Journal of Accounting Research*, 27(Supplement).
- Bertrand, M., Mehta, P., and Mullainathan, S. (2002). Ferreting out tunneling: An application to Indian business groups. *The Quarterly Journal of Economics*, 117(1), 121-148.
- Beuselinck, C., Cascino, S., Deloof, M., and Vanstraelen, A. (2019). Earnings management within multinational corporations. *The Accounting Review*, 94(4), 45-76.
- Bradshaw, M. T., and Sloan, R. G. (2002). GAAP versus the street: An empirical assessment of two alternative definitions of earnings. *Journal of Accounting Research*, 40(1), 41-66.
- Burgstahler, D., Jiambalvo, J., and Shevlin, T. (2002). Do stock prices fully reflect the implications of special items for future earnings? *Journal of Accounting Research*, 40(3), 585-612.
- Dechow, P. M. (1994). Accounting earnings and cash flows as measures of firm performance: The role of accounting accruals. *Journal of accounting and economics*, 18(1), 3-42.
- Dechow, P. M., Sloan, R. G., & Sweeney, A. P. (1995). Detecting earnings Management. *Accounting review*, 193-225.
- DeGeorge, F., Patel, J., and Zeckhauser, R. (1999). Earnings management to exceed thresholds. *The journal of business*, 72(1), 1-33.
- Demski, J. S. (1973). The general impossibility of normative accounting standards. *The Accounting Review*, 48(4), 718-723.
- Doyle, J. T., Lundholm, R. J., and Soliman, M. T. (2003). The Predictive Value of Expenses Excluded from Pro Forma Earnings. *Review of Accounting Studies*, 145–174.
- Dye, R. A., and Sridhar, S. S. (2004). Reliability-relevance trade-offs and the efficiency of aggregation. *Journal of Accounting Research*, 42(1), 51-88.
- Francis, J. R. (1986). Debt reporting by parent companies: parent-only versus consolidated statements. *Journal of Business Finance and Accounting*, 393-403.

- Gopalana, R., Nanda, V., and Seru, A. (2007). Affiliated firms and financial support: Evidence from Indian business groups. *Journal of Financial Economics*, 86(3), 759-795.
- Graham, J. R., Harvey, C. R., and Rajgopal, S. (2005). The economic implications of corporate financial reporting. . *Journal of accounting and economics*, 40((1-3)), 3-73.
- Hsu, C., and Kross, W. (2011). The Market Pricing of Special Items that are Included in versus Excluded from Street Earnings. *Contemporary Accounting Research*, 28(3), 990-1017.
- Jones, J. J. (1991). Earnings management during import relief investigations. *Journal of accounting research*, 29(2), 193-228.
- Khanna, T., and Palepu, K. (2000). Is group affiliation profitable in emerging markets? An analysis of diversified Indian business groups. *The journal of finance*, 55(2), 867-891.
- Li, N. (2021). Do majority-of-minority shareholder voting rights reduce expropriation? Evidence from related party transactions. *Journal of Accounting Research*, 59(4), 1385-1423.
- Li, X., Ng, J., and Saffar, W. (2021). Financial reporting and trade credit: Evidence from mandatory IFRS adoption. *Contemporary Accounting Research*, 38(1), 96-128.
- Lougee, B., and Marquardt, C. (2004). Earnings Informativeness and Strategic Disclosure: Empirical Examination of "Pro Forma Earnings". *The Accounting Review*, 79(3), 769-795.
- Lu, J. (2019). Limited attention: Implications for financial reporting. *Journal of Accounting Research*.
- Manchiraju, H., and Rajgopal, S. (2017). Does corporate social responsibility (CSR) create shareholder value? Evidence from the Indian Companies Act 2013. *Journal of Accounting Research*, 55(5), 1257-1300.
- Pendlebury, M. (1980). The application of information theory to accounting for groups of companies. *Journal of Business Finance and Accounting*, 7(1), 105-117.
- Pendlebury, M. (1980). The application of information theory to accounting for groups of companies. *Journal of Business Finance and Accounting*, 7(1), 105-117.
- Simon, H. (1990). Bounded rationality. *In Utility and probability*, 15-18.
- Skinner, D. J., and Sloan, R. G. (2002). Earnings surprises, growth expectations, and stock returns or don't let an earnings torpedo sink your portfolio. *Review of accounting studies*, 7(2), 289-312.
- Sloan, R. G. (1996). Do stock prices fully reflect information in accruals and cash flows about future earnings? *Accounting review*, 289-315.

- Song, S. (2021). The Informational Value of Segment Data Disaggregated by Underlying Industry: Evidence from the Textual Features of Business Descriptions. , 96(6). *The Accounting Review*, 96(6), 361-396.
- Srinivasan, P., and Narasimhan, M. (2012). Srinivasan, P., and Narasimhan, M. S. (2012). The value relevance of consolidated financial statements in an emerging market: The case of India. *Asian Review of Accounting*.
- Velury, U., & Jenkins, D. S. (2006). Institutional ownership and the quality of earnings. *Journal of business research*, 59(9), 1043-1051.
- Walker, R. G. (1976). An evaluation of the information conveyed by consolidated statements. *Abacus*, 12(2), 77-115.
- Walker, R., and Mack, J. (1998). The influence of Regulation on the publication of Consolidated Statements. *ABACUS*, 34(1).
- Xie, H. (2001). The Mispricing of Abnormal Accruals. *The Accounting Review*, 76(3), 257-373.

Figure 1: Timeline of important regulations related to consolidated and standalone financial statements



Appendix A1: Illustration of mechanics behind construction of Consolidated and Standalone statements

At the beginning of the year, the balance sheet of two entities P and S is as follows -

(INR)	P	S
Cash	500	50
Investments	0	0
Other assets	1,700	550
Total assets	2,200	600
Liabilities	1,500	400
Shareholders' equity	700	200
Total Liabilities & Shareholders' equity	2,200	600

Let us assume that at the beginning of year 1, P pays INR200 to buy 100% shares of S.¹⁰ Since both P and S are separate legal entities, both will prepare their separate financial statements. In addition to the standalone financial statements, P also needs to provide consolidated financial statements where the financial statements of P and S are combined as if they are a single economic entity. The separate financial statements of P and S as well as consolidated financial statements of the combined entity at the end of the year are given below-

	P	S	C
<u>Income statement</u>			
Sales	1,000	200	1200
Cost	800	120	920
PBT	200	80	280
Tax @ 25%	50	20	70
PAT	150	60	210
<u>Balance sheet</u>			
Cash	300	50	350
Investments	200	0	0
Other assets	1,700	550	2250
Total assets	2,200	600	2,600
Liabilities	1,350	340	1,690
Shareholders' equity	850	260	910
Total Liabilities & Shareholders' equity	2,200	600	2,600

Ind AS 27 *Separate Financial Statements* (paragraph 10) requires that the parent entity should account for an investment in its subsidiary at cost.¹¹ In appendix 1, the standard clearly disallows

¹⁰ For the sake of simplicity we assume that the price paid by P to acquire 100% shares of S is exactly equal to the book value of S at the time of purchase. If the price paid is different that the book value of S then goodwill (or gain on bargain purchase) is recognized during the consolidation following the purchase method of accounting for consolidation.

¹¹ Ind AS 27 allows the parent company to select fair value option to account for its subsidiary. Further, the parent entity can opt for equity method when accounting for joint ventures and /or associates.

the use of equity method to account for subsidiaries. If P were to use equity method to account for its subsidiaries, the net income of P would be equal to the consolidated net income as equity method is often called as single line consolidation. But since P records its investment in S at cost, the consolidated income statement is obtained by simply adding all the line items of P and S.¹² The standalone income statement in addition to consolidated income statement thus gives a valuable piece of information to investors about how well the parent company is performing on its own without combining the performance of its subsidiaries.

Similarly, the consolidated balance sheet is obtained by adding all the assets and liabilities of P and S, respectively. The investment of P cancels out the shareholders' equity of S. While we do not consider more several elements of the consolidation process such as the difference between purchase price and the book value of S, intercompany transactions, revaluation of S' assets and liabilities, the process of consolidation in the Indian accounting standards is broadly similar to the process outlined in US GAAP and IFRS. In addition to the consolidated financial statement, the parent entity P also provides it separate balance sheet where it shows its investment in S at cost.

¹² If intercompany transactions are present, P and S still record them as P and S are separate legal entities. However, such intercompany transactions are eliminated during the process of consolidation.

Appendix A2: Variable Description

Variable	Variable Name	Description
$EARN_{C_{i,t}}$, $EARN_{P_{i,t}}$, $EARN_{S_{i,t}}$	ROA	Profit after tax divided by total assets at the end of year t . Further the subscripts C , P , and S relate to consolidated, parent (or standalone), and subsidiary, respectively.
$ESUR_{C_{i,t}}$, $ESUR_{P_{i,t}}$, $ESUR_{S_{i,t}}$	Earnings Surprise	Difference between the profit after tax (pat) in period t scaled by total assets reported in the period t and profit after tax (pat) in $t-1$, scaled by total assets as reported in period $t-1$. Further the subscripts C , P , and S relate to consolidated, parent (or standalone), and subsidiary, respectively.
$BHR_{i,t}$	Buy Hold Return	One-year market adjusted buy hold returns where compounding starts 9 months prior to the fiscal year end and ends 3 months after the fiscal year end, company's stock return for the month – market return (NSE500 index)
$SIZE_{i,t}$	Firm Size	Natural log of the market value of equity
$BETA_{i,t}$	Market Beta	Market adjusted (Nifty 500 index) beta, with estimation window of 36 months
$BM_{i,t}$	Book to Market Ratio	It is the ratio of Book value of equity to the market value of equity
$MBE_{i,t}$	Dummy for Meeting or beating expectation	Indicator variable that receives a value of 1 if earnings improved over the previous period i.e., $ESUR_{C_{i,t}} \geq 0$, otherwise 0.
MBEP1S1	Dummy for Source of Meeting or beating expectation	There is an improvement in consolidated earnings that is driven by improvement in Earnings of both parent and subsidiaries
MBEP1S0	Dummy for Source of Meeting or beating expectation	There is an improvement in consolidated earnings that is driven by the improvement in earnings of the only parent
MBEP0S1	Dummy for Source of Meeting or beating expectation	There is an improvement in consolidated earnings that is driven by improvement in Earnings of only subsidiaries
MISSP1S0	Dummy for Source of Missing expectation	There is a decline in consolidated Earnings that is driven by the decline in Earnings of only subsidiaries
MISSP0S1	Dummy for Source of Missing expectation	There is a decline in consolidated Earnings that is driven by a decline in Earnings of the only parent
MISSP0S0	Dummy for Source of Missing expectation	There is a decline in consolidated Earnings that is driven by the decline in Earnings of both parent and subsidiaries

$CFO_{C,t}$ $CFO_{P,t}$ $CFO_{S,t}$	Cash flow from Operations	Cash flow from a firms' operating activities during a year t scaled by consolidated total assets. Further the subscripts <i>C</i> , <i>P</i> , and <i>S</i> relate to consolidated, parent (or standalone), and subsidiary, respectively.
$ACCRUALS_{C,t}$ $ACCRUALS_{P,t}$ $ACCRUALS_{S,t}$	Accruals	Profit after tax minus Cash flow from operations for year t scaled by consolidated total assets. Further the subscripts <i>C</i> , <i>P</i> , and <i>S</i> relate to consolidated, parent (or standalone), and subsidiary, respectively.
<i>DACC</i>	Discretionary Accruals	<p>The level of discretionary accruals calculated following modified Jones model (1991) suggested by Dechow, Sloan, and Sweeney (1995), as the residuals from the following industry-year regression:</p> $ACCRUALS_t/A_{t-1} = \alpha_0 + \alpha_1[1/A_{t-1}] + \alpha_2[(\Delta SALE_t - \Delta TR_t)/A_{t-1}] + \alpha_3[PPE_{t-1}/A_{t-1}] + \varepsilon_{i,t}$ <p>Where $ACCRUALS_t$ is computed as change in current assets from $t-1$ year to year t ($\Delta Current_Assets_t$) minus change in current liabilities from $t-1$ year to year t ($\Delta Current_Liabilities_t$) minus change in cash and cash equivalent from $t-1$ year to year t ($\Delta Cash_t$) plus change in debt included in current liabilities from $t-1$ year to year t ($\Delta Short_term_borrowing_t$) minus depreciation expense in year t ($Depreciation_t$); $\Delta SALE_t$ is change in net sales from year $t-1$ to year t; ΔTR_t is change in trade receivable from year $t-1$ to year t; and PPE_t is property, plant, and equipment in year t. We estimate the above regression cross-sectionally for industry-years with at least 10 observations. The estimated residuals (<i>DACC</i>), capturing discretionary accruals, are our proxy for accrual-based earnings management. <i>DACC</i> is calculated separately at parent and subsidiary level.</p>
Earnings volatility	Earnings volatility	The standard deviation of profit after tax scaled by total assets (ROA) estimated over 5-year estimation period.
Leverage	Leverage	The total liabilities are divided by total assets for the year t on consolidated, Standalone, and subsidiary basis

Table 1: Sample Selection

Sample Operations	Number of observations
Initial Sample	26455
Year-end other than March	(1449)
Eliminating Small Firms	(3210)
Eliminating Data Issues	(5306)
Eliminating Missing Earnings Surprise	(2397)
Eliminate Missing values	(335)
Missing Market data	(4258)
Final Sample	9500

Note: Removing small firms discard firm-year observations with sales and total assets reported on a consolidated and parent basis of less than INR 1 million. We retain non-missing values of an earnings surprise, sales, total assets, net income, the book value of equity, and cash flow from operations on both consolidated and parent basis. We retain stock return data with non-missing values of Beta and Buy hold return (BHR).

Table 2: Distribution of sample across years and industries

Panel A: Year-wise Sample distribution		
Year	Frequency	Percent
2003	130	1.37
2004	163	1.72
2005	198	2.08
2006	232	2.44
2007	284	2.99
2008	358	3.77
2009	432	4.55
2010	519	5.46
2011	577	6.07
2012	625	6.58
2013	640	6.74
2014	662	6.97
2015	691	7.27
2016	759	7.99
2017	793	8.35
2018	809	8.52
2019	825	8.68
2020	803	8.45
Total	9,500	100

Panel B: Industry - Wise sample distribution		
Industry group	Freq.	Percent
Manufacturing	4,866	51.22
Information and communication	978	10.29
Construction	919	9.67
Financial and insurance activities	724	7.62
Wholesale and retail trade; repair of motor vehicles and motorcycles	689	7.25
Diversifies	258	2.72
Transportation and storage	236	2.48
Accommodation and Food service activities	152	1.6
Electricity, gas, steam, and air conditioning supply	132	1.39
Mining and quarrying	106	1.12
Administrative and support service activities	103	1.08
Professional, scientific and technical activities	96	1.01
Agriculture, forestry, and fishing	73	0.77
Human health and social work activities	58	0.61
Education	37	0.39
Other financial activities	33	0.35
Arts, entertainment, and recreation	20	0.21
Other service activities	20	0.21
Total	9,500	100

Note: Industry classification is based on industry divisions as specified in National industry classification 2008, by Central Statistical Organisation, Ministry of Statistics and programme implementation, Government of India.

Table 3: Descriptive Statistics

Panel A: Summary statistics at consolidated level

Variable	N	Mean	Median	SD	P25	P75
# Of subsidiaries	9099	8.7254	3.0000	18.9839	2.0000	8.0000
Assets (INR Billion)	9500	24.4451	10.3862	28.4976	3.0251	37.0725
Subsidiary Assets / Consolidated Assets	9500	0.1944	0.1156	0.2092	0.0294	0.2981
ROA	9500	0.0398	0.0343	0.0675	0.0061	0.0729
CFO	9500	0.0621	0.0624	0.0874	0.0136	0.1115
Accruals	9500	-0.0227	-0.0241	0.0863	-0.0684	0.0201
ESUR	9500	-0.0044	-0.0022	0.0547	-0.0225	0.0143
MBE (Dummy)	9500	0.4584	0.0000	0.4983	0.0000	1.0000
Institutional Ownership > non-institutional (Dummy)	9500	0.2438	0.0000	0.4294	0.0000	0.0000
Proportion of Independent directors	9087	0.4479	0.4444	0.1067	0.3846	0.5000

Panel B: Summary statistics at parent and subsidiary level

Variable	N	Standalone			Subsidiary			Difference	
		Mean	Median	SD	Mean	Median	SD	Mean	Median
ROA	9500	0.0432	0.0359	0.0690	-0.0225	0.0117	0.4573	0.0656***	0.0243***
Discretionary Accruals	9500	-0.0021	0.0000	0.0273	-0.0001	0.0000	0.0045	-0.0019***	0.0000***
ESUR	9500	-0.0040	-0.0016	0.0453	-0.0005	0.0000	0.0248	-0.0035***	-0.0016***
Earnings Volatility	8172	0.0355	0.0227	0.0418	0.3409	0.0739	1.0523	-0.3054***	-0.0512***
Leverage	9500	0.4956	0.5185	0.2210	0.8549	0.7643	0.9828	-0.3593***	-0.2458***

Note: This table reports the mean, median, standard deviation, 25th percentile and 75th Percentile of various firm characteristics at consolidated, standalone, and subsidiary (consolidated minus standalone) level. It comprises of 9,500 firm-year observations for 1,413 unique firms. The detailed variable description is provided in Appendix A2. To adjust for outliers, we winsorize all the variables.

Table 4: Contemporaneous market reaction to earnings surprise

	(1)	(2)	(3)	(4)
Dependent Variable →	$BHR_{i,t}$	$BHR_{i,t}$	$BHR_{i,t}$	$BHR_{i,t}$
$ESUR_{C_{i,t}}$	1.427*** (6.022)		0.618*** (3.316)	
$ESUR_{P_{i,t}}$		1.771*** (6.296)	1.223*** (4.954)	1.854*** (6.344)
$ESUR_{S_{i,t}}$				0.851*** (3.917)
$MBE_{i,t}$	0.160*** (8.944)	0.169*** (8.487)	0.156*** (8.628)	0.152*** (8.207)
$SIZE$	-0.012 (-1.061)	-0.013 (-1.098)	-0.013 (-1.097)	-0.013 (-1.103)
BM	-0.045** (-2.904)	-0.045** (-2.906)	-0.045** (-2.887)	-0.045** (-2.892)
$BETA$	0.006 (0.248)	0.004 (0.180)	0.004 (0.173)	0.005 (0.214)
F-Stat				
$ESUR_C = ESUR_P$			3.83*	
$ESUR_P = ESUR_S$				7.59**
Observations	9,500	9,500	9,500	9,500
Adjusted R-squared	0.130	0.131	0.132	0.131

t-statistics in parentheses

*** p<0.01, ** p<0.05, * p<0.1

Note: Table 4 represents the results for the contemporaneous returns test; we regress 12-month BHR on consolidated earning Change over the previous year (column 1) , we regress 12-month BHR on parent earning Change over the previous year (column 2), In column 3 we regress 12-month BHR on both parent and consolidated earnings change. In column 4 we decompose earning change over the previous year (earnings surprise) into parent earning surprise and subsidiary earnings surprise. We estimate regressions using the Fama-MacBeth [1973] method, with the Newey-West [1987] correction. For a detailed variable description, refer to Appendix A2.

Table 5: Rewards to MBE conditioned on parent vs subsidiary earnings surprise

Panel A – Univariate analysis

	MBEP1S1	MBEP1S0	MBEPOS1	MISSP1S0	MISSPOS1	MISSPOS0	Total
N	2248	1318	789	731	1778	2636	9500
Mean	0.230	0.156	0.036	-0.022	-0.099	-0.132	0.022
Median	0.049	0.022	-0.062	-0.119	-0.179	-0.208	-0.099

Panel B – Regression analysis

Dependent variables →	(1) <i>BHR_{i,t}</i>
<i>ESUR_{Pi,t}</i>	1.517*** (5.416)
<i>ESUR_{Si,t}</i>	1.107*** (4.147)
<i>SIZE</i>	-0.012 (-1.060)
<i>BM</i>	-0.045** (-2.937)
<i>BETA</i>	0.005 (0.218)
<i>MBEP1S1</i>	0.221*** (7.687)
<i>MBEP1S0</i>	0.184*** (7.341)
<i>MBEPOS1</i>	0.089*** (4.234)
<i>MISSP1S0</i>	0.095** (3.117)
<i>MISSPOS1</i>	0.026 (1.543)
<u>F-test</u>	
<i>MBEP1S1 = MBEP1S0</i>	0.94
<i>MBEP1S0 = MBEPOS1</i>	8.44**
<i>MBEPOS1 = MISSP1S0</i>	0.03
Observations	9,500
Adjusted R-squared	0.132

t-statistics in parentheses;

*** p<0.01, ** p<0.05, * p<0.1

Note: Table 5 A represents BHR (Buy-Hold return), a one-year market-adjusted buy-hold return where compounding starts 9 months before the fiscal year-end and ends 3 months after the fiscal year-end. we divide firm-year observation on the basis i.e MBE(MISS) at consolidated level driven by improvement (decline) in parent and subsidiary earnings. Table 5 Panel B represents regression analysis in which we regress BHR (Buy-Hold return), a one-year market-adjusted buy-hold return where compounding starts 9 months before the fiscal year-end and ends 3 months after the fiscal year-end on Earnings surprise decomposed into parent and subsidiary earnings surprise, MBE in earlier model is decomposed into 5 indicator variables as defined in section 4 and Appendix A2. We estimate regressions using the Fama-MacBeth [1973] method, with the Newey-West [1987] correction. For a detailed variable description, refer to Appendix A2.

Table 6: Persistence of standalone and subsidiary earnings

Dependent Variable →	(1)	(2)	(3)	(4)	(5)	(6)
	$EARN_{p_{i,t+1}}$	$EARN_{s_{i,t+1}}$	$EARN_{c_{i,t+1}}$	$CFO_{p_{i,t+1}}$	$CFO_{s_{i,t+1}}$	$CFO_{c_{i,t+1}}$
$EARN_{p_{i,t}}$	0.583*** (22.550)		0.645*** (17.266)			
$EARN_{s_{i,t}}$		0.478*** (12.701)	0.551*** (14.131)			
$CFO_{p_{i,t}}$				0.320*** (12.174)		0.334*** (12.908)
$CFO_{s_{i,t}}$					0.205*** (9.869)	0.256*** (15.327)
<i>SIZE</i>	0.002*** (7.642)	0.000 (1.409)	0.002*** (5.006)	0.003*** (5.772)	0.001*** (3.491)	0.004*** (7.730)
<i>BM</i>	-0.004*** (-3.858)	-0.000 (-0.584)	-0.004*** (-3.110)	-0.003*** (-4.164)	0.001 (0.916)	-0.001 (-0.894)
<i>BETA</i>	-0.005*** (-3.583)	-0.001 (-1.354)	-0.007*** (-3.490)	-0.010*** (-5.126)	-0.001* (-2.163)	-0.011*** (-4.970)
<u>F-test:</u> $EARN_{p_{i,t}} = EARN_{s_{i,t}}$			3.02*			
$CFO_{p_{i,t}} = CFO_{s_{i,t}}$						6.49**
Observations	8,087	8,087	8,258	8,087	8,087	8,087
Adj. R-squared	0.412	0.200	0.410	0.153	0.050	0.152

t-statistics in parentheses

*** p<0.01, ** p<0.05, * p<0.1

Note: In Table 6, in column 1-3 we estimate equation (3). In column (1) we regress t+1 period earnings (profit after tax) as reported in standalone financial statements scaled by consolidated total assets on t period earnings (profit after tax) as reported in standalone financial statements scaled by consolidated total assets. In Column (2) we regress t+1 period earnings (profit after tax) as reported in consolidated financial statements minus standalone financial statements scaled by consolidated total assets on t period earnings (profit after tax) as reported in consolidated financial statements minus standalone financial statements scaled by consolidated total assets. In Column (3) we regress t+1 period earnings (profit after tax) as reported in consolidated financial statements scaled by consolidated total assets on parent earnings (profit after tax) as reported in standalone statement scaled by consolidated total assets and subsidiary earnings (Consolidated minus standalone profit after tax) scaled by consolidated total assets. In column (4-6) we undertake similar analysis as column (1-3) but we test the persistence of cash flow from operations. We control for Size, BM and Beta. We estimate regressions using the Fama-MacBeth [1973] method, with the Newey-West [1987] correction for serial correlation. For a detailed variable description, refer to Appendix A2.

Table 7- Future Returns Test

Dependent Variable →	(1)	(2)	(3)
	BHR_{t+1}	BHR_{t+1}	BHR_{t+1}
$ESUR_{C_{i,t}}$	-0.004 (-0.020)		
$ESUR_{P_{i,t}}$		-0.085 (-0.289)	-0.191 (-0.565)
$ESUR_{S_{i,t}}$		0.077 (0.365)	0.050 (0.220)
$SIZE$	-0.029** (-2.460)	-0.029** (-2.426)	-0.029** (-2.425)
BM	0.012 (1.502)	0.012 (1.459)	0.011 (1.450)
$BETA$	-0.046* (-1.972)	-0.043* (-1.864)	-0.046 (-1.884)
MBE	0.028 (1.358)	0.031 (1.399)	
$MBEP1S1$			0.060* (1.896)
$MBEP1S0$			0.049 (1.318)
$MBEPOS1$			0.045 (1.167)
$MISSP1S0$			0.050 (1.266)
$MISSPOS1$			0.024 (0.980)
Observations	9,500	9,500	9,500
Adj. R-squared	0.054	0.056	0.064

t-statistics in parentheses

*** p<0.01, ** p<0.05, * p<0.1

Note: BHR_{t+1} one-year market-adjusted buy-hold returns for a firm i during year $t+1$ regressed on all the variables mentioned in the contemporaneous returns test in Table 5 and 6. We estimate regressions using the Fama-MacBeth [1973] method, with the Newey-West [1987] correction for serial correlation. For a detailed variable description, refer to Appendix A2. These results are sensitive to the effect of the outliers.

Table 8: Cross sectional variation based on level of total Subsidiary accrual and Subsidiary discretionary accruals

	(1)	(2)	(3)	(4)
Dependent Variables →	$BHR_{i,t}$	$BHR_{i,t}$	$BHR_{i,t}$	$BHR_{i,t}$
Subsample Criteria →	Accruals > 0	Accruals < 0	DACC > 0	DACC < 0
$ESUR_{P_{i,t}}$	2.115*** (4.119)	1.771*** (6.401)	2.390*** (6.663)	2.013* (3.076)
$ESUR_{S_{i,t}}$	0.377 (1.019)	1.194*** (5.087)	0.890 (1.880)	1.828* (2.480)
$MBE_{i,t}$	0.118** (2.768)	0.164*** (11.108)	0.158** (4.854)	0.150*** (9.107)
$SIZE$	-0.021 (-1.382)	-0.010 (-0.948)	-0.004 (-0.376)	-0.014 (-1.111)
BM	-0.059*** (-3.474)	-0.050** (-2.521)	-0.026** (-5.016)	-0.046* (-2.695)
$BETA$	0.007 (0.474)	0.012 (0.341)	0.002 (0.080)	-0.057 (-2.080)
<u>F-test</u> $ESUR_P = ESUR_S$	7.54***	2.53	6.37*	0.04
Observations	3,639	5,861	2,544	2,380
Adj, R-squared	0.134	0.134	0.153	0.163

t-statistics in parentheses

*** p<0.01, ** p<0.05, * p<0.1

Note: Table 8 represents cross sectional variation based on Subsidiary accruals. We divide sample on the basis of positive and negative subsidiary accruals. Secondly, we compute discretionary accruals for imputed subsidiary measure as per the Modified Jones model. We divide samples on the basis of positive and negative discretionary accruals, and we estimate equation (1) on the subsamples using the Fama-MacBeth [1973] method, with the Newey-West 1987 correction for serial correlation. For a detailed variable description, refer to Appendix A2.

Table 9: Cross sectional variation Based on Monitoring and Governance

	(1)	(2)	(3)	(4)
Dependent Variable →	$BHR_{i,t}$	$BHR_{i,t}$	$BHR_{i,t}$	$BHR_{i,t}$
Subsample Criteria →	Institutional Ownership		Board Independence	
	Inst > non- Institution	Inst < non- Institution	Above median	Below Median
$ESUR_{P_{i,t}}$	2.063* (1.847)	1.857*** (7.476)	1.800*** (4.796)	1.704*** (8.091)
$ESUR_{S_{i,t}}$	1.783*** (3.641)	0.692*** (3.305)	1.061*** (3.605)	0.724 (1.526)
$MBE_{i,t}$	0.078** (2.472)	0.169*** (7.243)	0.147*** (7.541)	0.152*** (6.603)
$SIZE$	-0.014 (-0.777)	0.000 (0.039)	-0.012 (-0.968)	-0.019 (-1.344)
BM	-0.090** (-2.797)	-0.041** (-2.888)	-0.041*** (-3.422)	-0.064** (-2.519)
$BETA$	0.044 (1.625)	-0.012 (-0.477)	-0.024 (-1.478)	0.051 (0.951)
<u>F-test</u> $ESUR_P = ESUR_S$	0.05	12.86***	2.4	3.56*
Observations	2,316	7,184	4,433	5,064
Adj. R-squared	0.162	0.128	0.132	0.133

t-statistics in parentheses

*** p<0.01, ** p<0.05, * p<0.1

Note: Table 9 represents cross-sectional variation based on institutional ownership and independent directors. We divide sample on the basis of Institutional ownership greater than non-institutional ownership and Institutional ownership less than non-institutional ownership. Secondly we divide sample above and below annual industry median on the basis of proportion of independent directors to total directors. We estimate equation (1) on the subsamples using the Fama-MacBeth [1973] method, with the Newey-West 1987 correction for serial correlation. For a detailed variable description, refer to Appendix A2.

Table 10: Cross sectional Variation based on level of Leverage

	(1)	(2)	(3)	(4)	(5)	(6)
Dependent Variable →	$BHR_{i,t}$	$BHR_{i,t}$	$BHR_{i,t}$	$BHR_{i,t}$	$BHR_{i,t}$	$BHR_{i,t}$
Subsample Criteria →	Consolidated Leverage		Parent Leverage		Subsidiary Leverage	
	Above Median	Below Median	Above Median	Below Median	Above Median	Below Median
$ESUR_{p_{i,t}}$	1.738*** (4.686)	2.060*** (4.381)	2.158*** (6.054)	1.557*** (4.911)	2.129*** (3.539)	1.975*** (7.045)
$ESUR_{s_{i,t}}$	0.499 (1.064)	1.417** (2.945)	0.571 (0.960)	1.009* (1.970)	0.939*** (3.366)	1.161** (2.933)
$MBE_{i,t}$	0.184*** (6.282)	0.115*** (3.599)	0.167*** (4.920)	0.144*** (9.119)	0.156*** (5.113)	0.132*** (3.984)
$SIZE$	-0.014 (-0.930)	-0.014 (-1.396)	-0.018 (-1.209)	-0.011 (-1.188)	-0.014 (-1.003)	-0.016 (-1.493)
BM	-0.060*** (-3.233)	-0.042** (-3.023)	-0.061*** (-3.125)	-0.038** (-3.065)	-0.069** (-2.317)	-0.036** (-2.696)
$BETA$	-0.009 (-0.280)	0.014 (0.660)	-0.022 (-0.987)	0.035 (0.991)	0.007 (0.243)	-0.006 (-0.322)
<u>F-test</u> ESUR _p = ESUR _s	4.29*	0.91	5.24**	0.83	3.22*	2.82
Observations	4,668	4,827	4,668	4,832	4,668	4,832
Adj. R-squared	0.143	0.138	0.149	0.123	0.134	0.136

t-statistics in parentheses

*** p<0.01, ** p<0.05, * p<0.1

Note: Table 10 represents cross-sectional variation based on leverage. Panel A We divide sample above and below annual industry median on leverage on consolidated level, standalone level and subsidiary level. We estimate equation (1) on the subsamples using the Fama-MacBeth [1973] method, with the Newey-West 1987 correction for serial correlation. For a detailed variable description, refer to Appendix A2.