Corporate Strategic Difference, High Audit Quality and Earnings Quality

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Abstract. This paper takes the Chinese A-share listed companies from 2014 to 2018 as a sample to study the impact of corporate strategic differences on the earnings quality of listed companies, and examines the role of high-quality audits in regulating the relationship between the two. The study found that strategic differences have a significant negative impact on corporate earnings quality, and high-quality audits can significantly inhibit this negative impact. The research conclusions of this paper are not only conducive to promoting the in-depth understanding of the factors affecting the quality of earnings by external investors and other stakeholders, but also expanding the scope of research on the strategic economic consequences of enterprises.

Introduction

Corporate strategy is the model choice for enterprises to create sustainable value returns for shareholders, creditors and stakeholders. It is the long-term decision-making made by decision-making level to the fundamental and overall issues of all aspects of the enterprise. Enterprise strategic information can reflect the key and key points of business management, and reflect the strategic advantages of the enterprise, such as the development direction of the enterprise and the key points of business growth, reflecting the sustainability of the business advantage and business performance. Therefore, the corporate strategy is important to the enterprise. The degree of strategic difference indicates the degree to which the corporate strategy deviates from the industry's conventional strategy, that is, the degree of difference between the company's strategy and other industry strategies in the industry [1][2].In recent years, the study of the economic consequences of the strategic differences of listed companies has become a new hotspot in the field of financial accounting. Scholars from the company's performance [2], corporate financing [3], analyst forecasts [4], auditor decision [5], etc. In-depth research has been carried out, but there are few studies on the relationship between the strategic differences of listed companies on the quality of earnings and how external supervision mechanisms affect the relationship between them.

The quality of earnings has always been the focus of scholars' research. Compared with other business information, earnings quality information is more easily recognized and relied on by investors. The degree of strategic difference is, to a certain extent, a kind of strategic information that combines industry information with individual enterprise information, which will have a significant impact on the company's risk and performance [6]. The higher the strategic difference, the stronger the degree of information asymmetry between enterprises and external stakeholders [7]. As an important strategic information that can comprehensively reflect the industry and enterprise level, then, does the degree of strategic difference affect the quality of earnings? At present, there are few studies on how the Chinese data research strategy difference affects the earnings quality. Based on this, this paper uses the data of China's A-share listed companies from 2014 to 2018 to empirically test the impact of corporate strategic differences on earnings quality, and from the outside. From the perspective of supervision, the impact of audit quality on the relationship between corporate strategic differentiation and earnings quality is investigated, trying to make up for this research deficiency to some extent.

The contributions of this paper are mainly in the following three aspects: Firstly, the research in this paper helps to enrich the research literature on the factors affecting earnings quality. Secondly, the research in this paper also helps to expand the research on the strategic consequences of enterprises. So far, research on the consequences of strategic differences is extremely lacking, and is

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limited to the impact of strategic differences on financial performance [2]. This paper analyzes how strategic differences affect the quality of corporate earnings and expands the existing analytical framework. Thirdly, this paper finds that high-quality audit can significantly inhibit the negative impact of strategic differences on the quality of corporate earnings. This finding has certain policy and practical significance for the supervision and audit of listed companies.

Theoretical Analysis and Research Hypothesis

Strategic Difference and Earnings Quality. For the economic consequences of strategic differences, scholars have mainly studied from the perspective of operational risk and information risk, and found that different strategic positioning will not only affect the company's own business activities, investment and financing activities, earnings management, risk-taking, tax avoidance, Financial fraud, stock price crash risks, etc. have different degrees of impact [2] [3] [8], and will directly affect the behavioral choices and decisions of external stakeholders such as analysts, auditors, etc. [4], but they ignore the company The degree of strategic difference affects the principal-agent relationship between management and external shareholders, and the management's agency motivation may affect the company's accounting information disclosure motives, which in turn affects the company's earnings quality. The existing literature on the factors affecting earnings quality mainly focuses on the ownership structure, the internal governance structure of the board of directors and the external governance environment [9-11]. Few literatures study the factors affecting the quality of earnings from a strategic perspective. This paper mainly discusses the impact of corporate strategic differentiation on earnings quality from the perspective of corporate strategy, and incorporates high-quality audit into the research framework to analyze the role of audit quality in regulating the relationship between the two.

Relevant management theory holds that enterprises will adopt different behaviors from the industry's conventional strategies to change their own business management behaviors, enhance their competitive advantages, and promote corporate performance. When the company's strategy deviates from the conventional strategy of the same industry, it will lead to the deviation of the company's performance from the industry average [2]. This kind of business uncertainty and performance volatility caused by the company's strategic differences may make the management's performance compensation change a lot, especially when the company's operating performance is not good, the management's performance compensation will be reduced. According to the "rational man" hypothesis in economics, in order to avoid the adverse effects of fluctuations in the company's operating performance on its compensation, management will implement opportunistic behaviors such as earnings manipulation, erode the interests of shareholders, and exacerbate conflicts of interest between management and shareholders. The quality of earnings has been significantly reduced [6].

On the other hand, when the degree of strategic difference is high, it will be difficult for stakeholders to understand and evaluate the business decision-making model, so that it is not possible to make a correct judgment on the business activities and performance of the company based on experience or common sense [7]. That is to say, it is difficult for management to grasp the company's financial status, operating results and cash flow in daily operations. Therefore, in the process of accounting processing and financial report preparation, it is easy to produce misuse of accounting standards or even deliberately choose aggressive accounting policies and other violations of accounting standards. This will exacerbate the company's agency conflict and will inevitably reduce the quality of earnings [12]. Based on this, this paper proposes the following research hypotheses:

H1: Under other conditions, the strategic difference is significantly negatively correlated with the earnings quality. that is, the greater the degree of strategic difference is, the lower the earning quality is.

Strategic difference, high quality audit and earnings quality. The literature has shown that the information verification function of high-quality audit helps the company to improve the fairness and reliability of financial reports, improve the information environment, and alleviate the

agency conflict between management and shareholders caused by information asymmetry[6]. Therefore, high-quality auditing helps to promote synergy between the two, reduce agency costs, protect the interests of shareholders, and thus inhibit the opportunistic behaviors such as management earnings manipulation and accounting fraud, thereby contributing to the quality of earnings. Improve and weaken the negative impact of strategic differences on earnings quality [13].

In addition, high-quality auditing is an important guarantee mechanism for the quality of accounting information. It can guide and supervise management's compliance with and implement accounting standards, thereby improving the quality of earnings [14]. It has been found that industry expertise auditors have rich auditing experience and industry skills, can identify and correct the accounting policy selection bias of the audited entity, enhance management's execution of accounting standards, and thus improve the company's earnings quality [15] .

Therefore, high-quality audits help to alleviate agency conflicts between management and shareholders, and guide and supervise management's compliance with accounting standards, thereby weakening the negative impact of strategic differences on earnings quality. Based on this, this paper proposes the following research hypotheses:

H2: High quality audits can significantly weaken the negative impact of strategic differences on earnings quality, while other conditions remain unchanged.

Research Design

Samples and data sources. This paper selects China's A-share listed companies in 2014-2018 as the initial sample, and conducts the following screenings: (1) Excluding ST and *ST companies; (2) Excluding financial and insurance companies; (3) Eliminating missing data related to earnings quality (4) Excluding the missing sample data in the regression analysis; (5) In order to avoid the influence of outliers, this paper performs a 1% Winsorize tailing treatment on all continuous variables. After the above screening, a total of 8114 observations were obtained. The data and related financial data required to calculate the earnings quality indicators are from the CSMAR Database.

Variable definition.

(1)Dependent variable

According to the analysis of earnings quality by De chow et al. [16], it is concluded that the modified Jones model based on industry classification can better evaluate the earnings quality. According to the modified Jones model, using the panel data of the annual and sub-industry, the model Eq.2 uses the OLS method to estimate α_1,α_2,$\alpha_3$and then substituting it into the model Eq.3 to calculate the unmanageable accrual surplus, and finally based on Model Eq.4 estimates the maneuverability accrual (DA).

$$\mathrm{TA}_t = NT_t - CFO_t \tag{1}$$

$$\frac{TA_t}{A_{t-1}} = \alpha_1\left(\frac{1}{A_{t-1}}\right) + \alpha_2\left(\frac{\Delta REV_t}{A_{t-1}}\right) + \alpha_3\left(\frac{PPE_t}{A_{t-1}}\right) + \varepsilon_t \tag{2}$$

$$NDA_t = \alpha_1\left(\frac{1}{A_{t-1}}\right) + \alpha_2\left(\frac{\Delta REV_t - \Delta REC_t}{A_{t-1}}\right) + \alpha_3\left(\frac{PPE_t}{A_{t-1}}\right) + \varepsilon_t \tag{3}$$

$$DA_t = \alpha_1\left(\frac{TA_t}{A_{t-1}}\right) - NDA_t \tag{4}$$

Among them, TA_t is the total accrued surplus of period t, which is equal to the operating profit of period t minus the net cash flow generated by business activities of period t. A_{t-1} is the total assets at the end of the t -1 period, $\Delta\mathrm{REV}_t$ is the change in the main business income of the t and t -1 periods, PPE_t is the original value of the total fixed assets at the end of the t period, and NDA_t is the period t The non-operating accrued surplus after the adjustment of total assets at the end of the period t -1, $\Delta\mathrm{REC}_t$ is the amount of change in accounts receivable in period t and period t -1, and DA_t is the number of maneuvering surplus in period t. The value of DA_t is treated as a negative absolute value, and the value obtained is recorded as EQ as the basis for evaluating the quality of earnings. The larger the value is, the higher the surplus quality is.

(2) Independent variables

For the degree of strategic difference, refer to the research of Tang et al. [2], Ye Kangtao et al. [6] to measure the strategic difference of enterprises. First, calculate the resource allocation of the company in the following six key strategic dimensions:①financial leverage (total liabilities / total assets); ② degree of fixed assets renewal (net value of fixed assets / original value of fixed assets); ③capital intensity (fixed assets) / Number of employees);④ R&D intensity (net of intangible assets / operating income); ⑤ expenditures for advertising and promotion expenses (sales expenses / operating income); ⑥ management expenses (management expenses / operating income). Each indicator reflects the resource allocation of the enterprise from one aspect, which reflects the strategic model of the enterprise, that is, these six indicators reflect one aspect of the enterprise strategy. Therefore, the strategic difference indicator comprehensively and comprehensively reflects the strategy of multiple dimensions of the enterprise, namely the overall strategy. In this paper, the net value of intangible assets and sales expenses are used as substitute variables for R&D expenses and advertising expenses, respectively, because listed companies disclose less R&D expenses and advertising expenses.

Further, in this paper, the resource allocation of each of the six key areas of each enterprise is subtracted from the industry average of the indicator, and the standard deviation of the indicator is standardized, and then the absolute value is taken. This results in the extent to which each corporate capital is deviated from the industry average in each of the key areas. Finally, the average capital investment index of each enterprise after standardization is averaged, and the strategic difference index is obtained. The larger the indicator is, the greater the difference in the strategic deviation of the company from the same industry in the same year is.

The quality of the audit, with reference to Chen Y., et al. This paper uses the natural logarithm of the annual audit fee of the firm to measure the quality of the audit. The value obtained is recorded as the Autidor Office Size. The larger the value is, the higher the audit quality is[17].

(3) Control variables

Drawing on the practice of Li Chuntao et al. [18], this paper introduces the following six control variables:①Size of the enterprise, using the natural logarithm measure of the total assets at the end of the year;②Asset-liability ratio (Lev), that is, the total liabilities at the end of the year divided by the total assets;③Profitability (ROE), the company's annual return on net assets; ④ Growth ability, measured by total asset growth rate; ⑤Largest, measured by the ratio of the largest shareholder at the end of the year; ⑥Return on assets (ROA), net profit divided by total assets at the end of the period measure.

Model setting. In order to test the research hypothesis, this paper constructs the following empirical model:

$$\mathrm{EQ}_{i,t} = \beta_0 + \beta_1 \mathrm{Strategy}_{i,t} + \gamma \sum Control_{i,t} + \varepsilon_{i,t} \quad (5)$$

$$\mathrm{EQ}_{i,t} = \beta_0 + \beta_1 \mathrm{Strategy}_{i,t} + \beta_2 \mathrm{Autidor\ Office\ Size}_{i,t} + \beta_3\ \mathrm{Strategy}_{i,t} * \mathrm{Autidor\ Office\ Size}_{i,t} + \gamma \sum Control_{i,t} + \varepsilon_{i,t} \quad (6)$$

Among them, EQ is the explanatory variable, which indicates the company's earnings quality; Strategy is the explanatory variable, indicating the degree of corporate strategic difference; this paper introduces the strategic difference degree and the audit quality as the cross term. In model (5), if β_1 is significantly negative, it indicates that the strategic difference is negatively correlated with the earnings quality; in model (6), if β_3 is significantly positive, it indicates that high quality audit can significantly weaken the strategic difference to the surplus. Negative impact of quality.

The Empirical Results and Analysis

Descriptive statistics. Table 1 reports the descriptive statistics of the main variables. It can be seen that the average value of the strategic difference of the sample enterprises is 0.6, the standard

deviation is 0.34, the minimum is 0.176, and the maximum is 2.29. The median is 0. 516, indicating that there is a large difference in the degree to which the sample enterprise strategy deviates from the industry routine.

Table 1 Descriptive statistics

	count	mean	p50	sd	min	max
EQ	8240	-0.08	-0.056	0.08	-0.437	-0.001
Strategy	11469	0.60	0.516	0.34	0.176	2.293
size	11604	22.13	21.980	1.29	19.703	26.047
Lev	11604	0.42	0.403	0.21	0.056	0.894
ROE	11584	0.08	0.076	0.10	-0.390	0.376
Growth	11603	0.23	0.115	0.39	-0.266	2.279
Largest	11604	34.48	32.572	14.68	8.748	74.856
ROA	11604	0.04	0.038	0.05	-0.146	0.190

Correlation analysis. Table 2 reports the correlation coefficient results of each major variable. It can be seen from the table that the correlation coefficient between the number of analysts tracking and the strategic difference of the enterprise is significantly positively correlated at the level of 1%, indicating that the strategic difference will be negative. This affects the company's earnings hypothesis, which initially proves the research hypothesis of this paper.

Table 2 Relationship between major variables

Variable	EQ	Strategy	size	Lev	ROE	Growth	Largest	ROA
EQ	1.000							
Strategy	-0.048***	1.000						
size	-0.008	-0.099***	1.00					
Lev	-0.155***	-0.013	0.531***	1.00				
ROE	0.035***	-0.149***	0.046***	-0.146***	1.000			
Growth	-0.104***	0.011	-0.055***	-0.108***	0.261***	1.000		
Largest	0.004	-0.065***	0.201***	0.073***	0.116***	-0.064***	1.000	
ROA	0.077***	-0.156***	-0.092***	-0.398***	0.881***	0.220***	0.106***	1.00

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

Regression analysis. Table 3 reports the regression results of the impact of corporate strategic differences on earnings quality. From column (1), it can be seen that the impact coefficient of corporate strategic difference on earnings quality is -0.0075, which is significantly negatively correlated at 1%. The greater the difference in corporate strategy, the lower the earnings quality, assuming H1 is verified.

Table 3 Regression results

	(1)	(2)
Variable	EQ	EQ
Strategy	-0.00754***	-0.109**
	(-2.94)	(-2.01)
Auditor Office Size		-0.0395***
		(-5.52)
Auditor Office Size* Strategy		0.0170*
		(1.89)
size	0.00558***	0.0107***
	(6.59)	(9.14)
Lev	-0.0807***	-0.0819***
	(-13.47)	(-13.62)
ROE	0.0387*	0.0440**
	(1.88)	(2.14)
Growth	-0.0243***	-0.0250***
	(-10.44)	(-10.75)
Largest	-0.00008	-0.0000845
	(-1.36)	(-1.37)
ROA	-0.0401	-0.0508
	(-0.90)	(-1.14)
_cons	-0.159***	-0.0361
	(-9.01)	(-0.96)
N	8114	8087

t statistics in parentheses

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

Further Analysis

Cross-term test. Table 3 (2) reports the regression results of the impact of corporate strategic differences on earnings quality. From column (2), it can be seen that the impact coefficient of corporate strategic difference and audit quality cross-overs on earnings quality is 0.017. There is a significant positive correlation at the 10% level, indicating that high quality audits can significantly weaken the negative impact of strategic differences on earnings quality, assuming H2 is validated.

Robustness test. In order to study the robustness of the conclusions, we have carried out the following tests: (1) Recalculating the strategic differences by using the methods of eliminating the net value of intangible assets and sales expenses. The conclusion of this paper is still valid (refer to whether the strategic differences can affect Analyst earnings forecast). (2) The audit quality is divided into two groups according to the average value of Auditor Office Size. The high and low two groups of data are used for group test. The conclusion of this paper is still valid. Due to space limitations, the above test results are not reported in this paper.

Research Conclusions

Corporate strategy has an important impact on earnings quality. This paper further expands the impact of strategy on the quality of corporate earnings. Taking China's A-share listed companies in 2014-2018 as the research object, we found that: (1) Strategic differences have significantly reduced the quality of corporate earnings. (2) High-quality audit can significantly weaken the negative impact of strategic differences on earnings quality. This shows that hiring auditors who can provide high-quality audit services is beneficial to weakening the negative impact of strategic differences on earnings quality.

The conclusions of this paper deepen our understanding of the role of corporate strategy in the quality of accounting information, and at the same time expand the research on the influencing factors of the earnings quality of listed companies. The conclusions of this paper have the following policy implications: First, this paper finds that the strategic difference of the company has an important impact on its earnings quality. Specifically, for companies with high strategic differences, external stakeholders such as investors should pay more attention to the authenticity of their earnings information. Second, this paper finds that high-quality audits have a negative effect on the negative correlation between strategic differences and earnings quality. This suggests that for companies with high strategic differences, relevant regulators and investors should require these companies to hire as much as possible. Quality auditors, lest these companies reduce the level of corporate earnings quality by using information asymmetry and agency conflicts caused by strategic differences.

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