

**Torhea Education Group**  
**FINANCIAL REPORTING, ASSET PRICING, AND STOCK TRADING STRATEGIES**  
**Summer 2019**

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## 1. Introduction

This introductory accounting and finance course assumes no prior academic knowledge of accounting or finance. The purpose of this course is two-fold. The first is to introduce you to the concepts of financial reporting, the language of business, asset pricing, and informationally efficient capital markets. The second purpose is to expose you to academic empirical research in asset pricing, stock trading strategies, corporate governance, and financial reporting strategies. To that end, we will cover a wide range of articles published in top tier finance and accounting academic journals.

## 2. Required Textbook

The textbook is Horngren, Sundem, Elliott & Philbrick, *Introduction to Financial Accounting*, 11<sup>th</sup> edition (2014, Prentice Hall, ISBN-13: 978-0-13-325103-6).

## 3. Preparation for Class Sessions

### Assigned Chapters and Problems

The most effective and efficient use of classroom time teaching introductory-level finance and financial accounting aims at reinforcing or clarifying what you have tried to learn on your own before entering the classroom. Hence, prior to each class you should read the assigned chapters and papers, and do the assigned problems listed on the syllabus. I recommend that all assigned problems be completed before coming to class, and turned in at the beginning of class. The assignments will be graded as either zero (no credit due to insufficient effort) or one, and be returned the following class. The assigned problems will be used in class discussions; be prepared to answer questions regarding them in class.

### Mini-Cases

The class discussions will also focus on one “mini-case.” The case will be collected at the beginning of class, and returned the following class. This is a group project, and you should work with your assigned study group or on your own. The cases will also be graded as either zero or one.

## 4. Research Project

You alone or with your group are to write an empirical research paper. Given your status as students and the relatively short time-frame with which we have to work, the paper is not expected to be publishable as submitted. Rather, the primary purpose is to expose you to the process of writing an academic manuscript.

Concisely, the process begins with clearly stating the research question, and explaining why the question is important in light of extant literature. Next, design the tests, identify the data sources and make sure they are available; many good ideas are inexecutable due to data limitations. Then, run the tests and put the results in carefully designed tables. If the results are consistent with your hypotheses, you want to

increase confidence in the inference validity by ruling out alternative hypotheses. Once your analysis survives a battery of sensitivity tests, you are ready to write up the paper.

## 5. Reading List

### 1. Earnings information and security prices

- Background reading:

Kothari, S.P., 2001, Capital markets research in accounting, *Journal of Accounting & Economics* 31, 105-231. Read sections 1-3 and section 4.1.1.

#### 1.1. Early studies

- Ball, Ray, and Philip Brown. 1968. An empirical evaluation of accounting income numbers, *Journal of Accounting Research*, 159-178.
- Beaver, William H. 1968. The information content of annual earnings announcements, *Journal of Accounting Research*, Supplement, 67-92.

#### 1.2. Recent study

- Bartov, Eli, Lucile Faurel and Partha Mohanram. Can Twitter Help Predict Firm-Level Earnings and Stock Returns? *The Accounting Review* 93(3), July 2018, pp. 25-57.

### 2. Management of accounting appearances

#### 2.1 Classificatory earning management

- McVay, S. 2006. Earnings management using classification shifting: An examination of core earnings and special items, *The Accounting Review* 81, 501 – 531.

#### 2.2 Does it pay to manipulate earnings?

- Bartov, E., and P. Mohanram. 2014. Does income statement placement matter to investors? The case of gains/losses from early debt extinguishment,” *The Accounting Review* 89(6), 2021-2056.

#### 2.3 Earnings expectations management to exceed thresholds

- Bartov, E., D. Givoly, and C. Hayn. 2002. The rewards for meeting-or-beating earnings expectations, *Journal of Accounting and Economics* 33, 173 – 204.

### 3. Stock price anomalies and trading strategies

- Background reading

Fama, Eugene, and Kenneth French. 2008. Dissecting Anomalies. *The Journal of Finance* 68(4), 1653-1678.

Bernard, V. L., and J. Thomas. 1990. Evidence that stock prices do not fully reflect the implications of current earnings for future earnings, *Journal of Accounting and Economics* 13, 305-340.

Bartov, E. 1992. Patterns in unexpected earnings as an explanation for post-announcement drift. *The Accounting Review* 67, 610-622.

#### 3.1. *Post earnings announcement drift*

- Ball, R., and E. Bartov. 1996. How naive is the stock market's use of earnings information? *Journal of Accounting and Economics* 21, 319-337.
- Bartov, E., S. Radhakrishnan, and I. Krinsky. 2000. Investor sophistication and patterns in stock returns after earnings announcements. *The Accounting Review* 75, 43 – 63.
- Ng, J., T. O. Rusticus, and R.S. Verdi. 2008. Implications of Transaction Costs for the Post-Earnings Announcement Drift. *Journal of Accounting Research* 46(3), 661 – 696.

#### 3.2. *Pricing of accruals and cash flows*

- Sloan, R.G. 1996. Do stock prices reflect information in accruals and cash flows about future earnings? *The Accounting Review* 71, 289 – 306.
- Xie, H. 2001. The mispricing of abnormal accruals. *The Accounting Review* 76(3), 357 - 373.
- Collins, D.W., G. Gong, and P. Hribar. 2003. Investor sophistication and the mispricing of accruals. *Review of Accounting Studies* 8, 251-276.
- Bartov, E. 2003. Discussion of 'investor sophistication and the mispricing of accruals.' *Review of Accounting Studies* 8, 277 – 281.

#### 3.3. *Post loss/profit announcement drift*

- Balakrishnan, K. E. Bartov, and L. Faurel. 2010. Post Loss/Profit Announcement Drift. *Journal of Accounting and Economics* 50, 20-41.

## 6. Learning Finance and Accounting

Experience in this course suggests the following:

- Classes make extensive use of homework problems assigned from the text and the mini cases. I will not discuss all the assigned work in class. You will learn accounting better (and will perform better on the problem-oriented exam) if you do the assigned reading and if you work on the assigned problems prior to each class.
- Each class builds on material from previous classes. You therefore must keep up to date, or you will find subsequent classes difficult.
- Experience suggests the course requires a relatively large amount of time devoted to both reading and working on problems and cases.
- Showing up late to class disrupts class, so I do not permit late entrance, defined as arriving at the door more than one minute after scheduled start time.

### Grading Procedure

There are two cumulative in-class examinations. You should bring a calculator (simple, financial, or scientific) to these exams; laptops or smart phones are not allowed. I will not give a makeup midterm examination for any reason. All in-class exams are closed books/notes; you may bring in one 8.5"x11" sheet of notes, which may be hand written or typed on the front, back, and edges.

### Course Grade Computation

Classroom Professionalism	20%
Weekly Problem assignments and in-class presentation	30%
Research Project	25%
Midterm Examination	<u>25%</u>
	<u>100%</u>

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CLASS SCHEDULE		
	Reading Assignment	Assigned Problems / Papers / Mini-Case <sup>1</sup>
1.	<b>Introduction:</b> Organizational Issues, and Introduction to Financial Accounting (purpose; users; institutional setting)	
2.	<b>Chapter 1:</b> The Balance Sheet	1-40, 1-43, 1-55
3.	<b>Chapter 2:</b> Income and Cash Flow Statements; Accrual vs. Cash-Basis Accounting; Income Recognition	2-33, 2-52
4.	<b>Chapter 2(cont'd):</b> Income and Cash Flow Statements; Accrual vs. Cash-Basis Accounting; Income Recognition	2-55
5.	<b>Chapter 3:</b> Recording Transactions and the Accounting Cycle	3-28, 3-39, 3-51
6.	Chapter 4: The Adjustment and Closing Processes	4-22, 4-31, 4-47
7.	Chapters 1-4: Communicating Financial Information	<b>Case: AOL (Handout)</b>
8.	<b>Research Seminar:</b> 1. Structuring / Evaluating a Research Paper 2. Are the Accounting Income Numbers Useful to Investors?	Ball and Brown (1968)
9.	<b>Research Seminar (cont'd):</b> Are the Accounting Income Numbers Useful to Investors?	Beaver (1968); Bartov, Faurel, Mohanram (2018)
10.	<b>Review:</b> Chapters 1-4	Sample midterm exam (Handout)
11.	<b>Introduction to asset pricing and Informationally efficient markets</b>	Handout
12.	<b>MIDTERM EXAM (Chapters 1-4)</b>	
13.	<b>Research Seminar:</b>  Management of accounting appearances	McVay, (2006); Bartov and Mohanram (2014).

<b>CLASS SCHEDULE</b>	
<b>Reading Assignment</b>	<b>Assigned Problems / Papers / Mini-Case<sup>1</sup></b>
<b>14. Research Seminar (cont'd):</b>  Management of accounting appearances	Bartov, Givoly, and Hayn (2002).
<b>15. Research Seminar:</b> Stock price anomalies and trading strategies	See syllabus

<sup>1</sup> Assignments are due at the beginning of class on the date shown; no need to turn in sample exams.