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A Qualitative Perspective On Earnings Announcement, Stock Return Behaviour And Investment Strategies; A Case Study Of Psx

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Abstract

Purpose of the study: This article addressed the qualitative perspectives on the information content of earnings announcements, stock return behavior, and investors' tactics in the Pakistan stock exchange (PSE) case.

Methodology: Interviews contextualize the quantitative findings in real-world circumstances and help analyze the intricacies arising from the quantitative findings. The semi-structured questionnaire gathers information from a convenient sample of 20 investors (10 institutional and ten private investors).

Main findings: The results of the interviews lead to several conclusions. First, the stock produces much momentum before and after earnings announcements. Particularly in positive news, stock show gain before the event day. Second, despite complaints from individual investors about information leaks, institutional investors overwhelmingly reject them. The reason stated by the interviewee for market momentum is not just the kind of announcement but also the mood of market participants as supported by behavioral finance. Third, in keeping with the literature study, most participants rejected the premise of efficient market theory. Institutional investors think that trading based on the qualitative and fundamental characteristics of the companies might help us achieve substantial returns

Implications of the study: The study contributes to literature and methodology in a manner not previously explored. The study contains background information on the interviews and a description of the sample information. It further examines the investors' thoughts regarding the effect of earnings disclosure on the stock returns, sources of information about the stock, and their investment methods.

Novelty/Originality of the study: This study is the first of its kind that sought the view of Pakistani investors about the information contents of the earnings announcement, their investment strategies, and their view on PSX market efficiency.

Key Words: PSX, Earnings announcement, Stock returns

INTRODUCTION

Companies must declare their earnings on time (quarterly or annually) by capital market regulations to keep investors informed. A wide range of consumers utilizes earnings as a summary indicator of corporate success. It helps investors value securities, predict future earnings, and evaluate management's capacity to provide value to investors, thus signifying its importance in the capital market (Mlonzi et al., 2009). Studies on the earnings announcements content and their relationship to share returns are overwhelmingly supported by studies conducted in developed (Wael, 2004; Tucker et al., 2013, Bartram, 2009) and emerging economies (Kong & Taghavi, 2006; Ganguli, 2010; Khan, 2011). The PSE was deemed to be semi-strongly efficient in Pakistan by Khan (2011), Iqbal and Farooqi

(2011), who noted that investors place higher importance on earnings but failed to generate meaningful gains on the announcement day of earnings.

In comparison, a study by Qureshi et al. (2012) reported PSE as semi-strong inefficient as a significant positive change in stock prices is recorded on the day of the earnings announcement. Fama and French (1970) suggested that markets are efficient since security prices instantly reflect any information upon publication, making it impossible for investors to profit significantly from news-based trading methods. However, academicians and practitioners negate the theory of market efficiency by reporting several anomalies, such as extra premiums for stocks with low price/earnings ratios (Basu, 1977) and low market capitalization firms (Atiase, 1985), the propensity of past winner stocks to outdo past looser stocks (Jegadeesh & Titman, 1993), stock under-reaction (Bernard & Thomas, 1989), and over-reaction (Bartram, 2009) to a different type of news, and the ability of the stock to make substantial gain during January (Rozeff & Kinney, 1976).

Therefore, the research offered compelling evidence refuting the efficient market hypothesis, which holds that no appreciable rewards can be obtained based on readily available knowledge. The explanations for such anomalies arise from risk premia (Fama & French, 2015) and behavioral finance (Neminno & Gempes, 2018). The advocate of risk premia established that riskier assets were more predictable than less risky ones. In comparison, the advocates of behavioral finance asserted that investors' actions are based on individual psychology and so make irrational decisions (as described by Moskowitz, 2015; Devos, 2015). In other words, researchers have yet to agree about what causes the disparate findings in the literature.

Additionally, a literature study reveals that earlier research (Qureshi et al., 2012; Neminno & Gempes, 2018) solely relied on quantitative analysis to ascertain the informational content of earnings announcements. "Event studies are commonly employed to confirm that signaling took place, but there is never the slightest effort at an alternate or parallel verification by the simple expedient of asking at least some of the parties involved about signalling," noted Frankfurter and McGoun (1993). The methodology utilized in this study tries to solve the shortcomings mentioned by Frankfurter and McGoun (1993).

This study is the first of its kind that sought the view of Pakistani investors about the information contents of the earnings announcement, their investment strategies, and their view on PSX market efficiency. Thus, the study contributes to literature and methodology in a manner not explored in the past. The following is how the chapter is set up. Section 2 contains background information on the interviews and a description of the sample information. Section 3 examines the investors' thoughts regarding the effect of earnings disclosure on the stock returns, sources of information about the stock, and their investment methods.

METHODOLOGY

This study adopted a qualitative approach and semi-structured interviews to obtain an in-depth analysis of the stock movement concerning the earnings announcement, investing strategies, and market function from Pakistan stock market participants. Semi-structured questionnaires were created using empirical literature and are preferred to other types because they give respondents more freedom to ask new questions and keep the order of the questions they are asking (He & Ng, 1998). Open-ended and closed-ended questions are included in semi-structured surveys to allow respondents to express themselves. The surveys were written in English because it is Pakistan's official language. A total of 20 investors were chosen for the sample out of convenience. The investors' lack of availability due to their busy schedules and reluctance to give information about their jobs was the cause of the convenient sampling. The identity of the interviewee and his employer are kept secret due to ethical research considerations. However, it is ensured that the chosen sample represents all investors, from the most prominent fund managers to the minor individual investors. The author used his connections to approach the investors and performed the interview at the participant's convenience. Given that Karachi has a stock market and investment firms, all interviews were conducted there.

Ten investors from institutional and individual sources were chosen for the study, and their descriptions are summarised in table 1 below. Individual investors invest and manage their savings in small stocks for return maximization. On the other hand, institutional investors are specialized financial institutions that handle other people's savings and invest them to maximize returns while maintaining a reasonable degree of risk (Davis & Steil, 2004). The face-to-face interviews took anywhere from 30 minutes to an hour. The goal was to ask the right questions to elicit information about the interviewees' behavior and their opinions of the market. By giving each participant a code to make them anonymous, as shown in table 1, the study was able to safeguard their secrecy. With the interviewee's consent, 13 interviews were digitally recorded, while those who preferred not to have their interviews recorded were manually documented. To detect the trends and frequently repeated significant statements of the interviewee, the interviews were transcribed and summarised on a single colossal graphic.

Table 1: Description of Interviewees

Code	Designation	Company	Age	Experience	Qualification
Individual Investors					
IND1	Civil Servant	Ministry of Commerce	48	18	A level
IND2	Civil Servant	Ministry of Education	41	14	Master
IND3	Student		21	3	Bachelor
IND4	Teacher	Agriculture University	44	11	Master
IND5	Businessman		40	13	Graduation
IND6	Manager	Private Company	50	18	MBA
IND7	Project Engineer	NCL	35	6	Bachelor
IND8	Businessman		30	2	LLB
IND9	Public Servant	Capital Development Authority	54	11	MPA
IND10	Vice President	United Bank	55	23	MBA
Institutional Investors					
INS1	Fund Manager	AKD	36	10	CFA
INS2	Fund Manager	UBL	34	9	MBA
INS3	Investment Analyst	ABL Investment Management	33	8	MBA
INS4	CEO	AKD investment	44	24	Bachelor
INS5	CFO	Meezan Investment	46	20	CFA, MBA
INS6	CEO	Safe Fund	38	15	MBA
INS7	Market Analyst	Askari Investment	40	16	BBA
INS8	Investment Analyst	Meezan Investment	32	7	MBA
INS9	Investment Officer	Lakson Investment	34	12	ACCA
INS10	Chief Executive	Fair Deal Securities	37	10	ACCA
Note: INS stand for Institutional investor and IND stand for Individual investor. Source: author thesis.					

3 Findings:

The answers to the questions were condensed into three sections, each of which focused on a different aspect of the stock market. The impact of earnings disclosure and how investors react to announcements were covered in the first section. Information sources and their value to investors were covered in the second section. Investment strategies were covered in the third section, and investors' perceptions of disclosure practices on the Pakistan Stock Exchange were covered in the fourth section.

Impact of Earnings announcements

Earnings convey information content, as objectively demonstrated by a substantial body of literature (such as Su, 2003; Lin, 2009; Chan, 2003). The participants questioned whether or not earnings carried information in this context. Interviewees, including institutional and individual investors, agreed that results reveal information about the business's operation and its prospects. They counter that the kind of the market's response to the news hangs on the relationship between expected market earnings and actual earnings. Such example, "Market moves on expectation but react on the actual announcement," one responder, referred to as IND1 said. In actuality, the market gains traction before the announcement, with expectations setting the direction. However, following the announcement, the actual profits dictate the market's direction, subject to meeting expectations.

The interview findings imply that profits convey essential information to the market and that the market responds to their disclosure. Additionally, based on investors' expectations, the stock gains momentum in the days leading up to the announcement. The early push in stock is either going in the right direction or the wrong direction, though, depending on the actual earnings. For instance, the news will further boost the market if actual earnings exceed market expectations, but the market will correct itself if actual earnings fall short of expectations. However, it is unclear from an investor's standpoint what constitutes positive and negative earnings. Most participants view strong pay-outs and bonus shares as positive, while weaker pay-outs and no bonus shares are considered harmful, in line with the findings of Bernard and Thomas (1989).

The next question sought their perspective on the market's response to both good and negative earnings in light of the earlier discussion. Most respondents indicated that while it is likely that the market has already digested and responded to good news, bad news will cause stock values to move in the opposite direction. The market's response to various types of earnings is described in a precise manner by respondent INS2 who stated that "Once statements are announced, there is often a depressing atmosphere since the market begins to adjust the prices; if earnings are beyond expectations, it rises; if below expectations, it will fall; but it depends on market sentiment." Thus, this provides a solid opinion that both news and market feeling develop market response as behavior finance recommends (see Daniel et al., 1998). The institutional investors' responses also show that they have two main points of view regarding negative earnings: first, they believe that single negative earnings are not concerning, but if it occurs often, they must alter their portfolio. The second is that they wait to act until they understand the circumstances around the bad news. According to the findings of behavioral finance, institutional investors do not immediately react to bad news; instead, they wait until the cause of the bad news has been confirmed (Neminno & Gempes, 2018). Thus, indict institutional investors for the post-earnings announcement drift disagree with Bartov et al. (2000), who reported high individual ownership among firms as a reason for post-earnings announcement drift.

In keeping with the previous sentence, the investors were questioned regarding how quickly they took the news in. Individual investors responded differently from institutional investors, who opted to hold off until the release of comprehensive financial statements. Such as, responder IND4 claimed, "As a daily trader, I must make rapid gains considering the information and rumors regularly injected into the market. According to my observations, market corrections begin immediately following announcements but may take a while if the market needs clarification. The results of the interviews indicate that although individual investors respond quickly, their response is also influenced by market perceptions of earnings. In other words, the sooner the market agrees on the earnings interpretation, information will be reflected in stock prices. This corroborates with Frazzini and Lamont's (2006) results, which showed that individual investors make uninformed trading decisions by investing in stocks that grab their attention due to news associated with them, such as earnings announcements. Comparatively, according to behavioral finance, most institutional investors (50%) claimed that their response is not impulsive and that they prefer to wait for the release of new information, particularly in the case of complex enterprises (Daniel et al., 1998). Overall, interview findings are consistent with Bernard and Thomas' findings and indicate institutional investors' conservative stance, which takes time to alter and results in late stock price adjustments (Bernard & Thomas, 1989).

Stock prices Pre-disclosure behaviour and Information leakage:

Khan (2011), Iqbal and Farooqi (2011), and Kong and Taghavi (2006), among other research, have noted a considerable change in stock values in the days leading up to earnings. Therefore, asking investors why there had been such a significant pre-announcement stock price change was vital. Interestingly, the majority of research participants—a total of 80%—acknowledged that the market started to move ahead of the announcement. The participants said that firms must notify the Pakistan stock exchange of the agenda for the directors' meeting seven days prior to the meeting's holding date in response to questions concerning the causes of the considerable volatility in stock prices during the pre-announcement period. Nevertheless, as soon as the market learns the board meeting's agenda, investors speculate and build hype. According to individual investor IND4, the market began speculating heavily on the payout, which led to the hype and an overvaluation of the stock, but it soon corrected itself. As a result, the participant attributed the market's overconfidence and the speculators' significant gains in the days prior to announcements.

However, participants' reactions to whether information leakage might be the reason for pre-announcement significant returns were divided. The market is informed of the information before it is formally disclosed, according to 60% of individual investors. On the other hand, institutional investors expressed differing opinions from individual investors and refuted the notion that information was being leaked. Seventy percent of institutional investors indicated that there is very little chance of knowledge leaking to the market. Furthermore, they believed that obtaining information in unethical ways prior to its public announcement was illegal and unethical. For instance, INS4 claimed that "it is really difficult to comment on the existence of information leaking at Pakistan stock exchange (PSE) as procedures are strict enough to discourage insider trading. In reality, there are no leaks; instead, speculation raises anticipation for the announcement day. Before official announcement, the market does, however, sometimes discount both positive and negative news".

Overall, the analysis of the interviews revealed individual investors' worries about information leaks, which is consistent with the literature such as (Sehgal & Bejoy, 2015) in India; (Khan, 2011) and (Qureshi et al., 2012) in Pakistan; (Su, 2003) in China). Institutional investors, on the other hand, strenuously disputed its existence. Institutional interviewers were observed to be reticent in providing in-depth responses regarding the insider trading problem. The findings are at odds with those of Hong (1999), who found that weak corporate governance is one of the main reasons for inefficiency in nations like Pakistan, making those nations more susceptible to insider trading.

Announcement timing:

Givoly and Palmanon (1982) and Hart (2013) found that the nature of earnings and the timing of announcements are related. Given this, investors were questioned regarding their thoughts on timely vs. delayed earnings disclosures. Most individual and institutional investors (80%) claimed that prompt results are a mark of effective management. As confirmed by institutional investor INS6 that "Late disclosures are seen negatively, especially if they are an anomaly given the historical pattern of corporate announcements but is not viewed as negative if the genuine reason is provided. On the other hand, premature announcement compared to selected dates of the firm financial year may raise suspicion, but mostly alright."

Overall, the selected interviewees claimed that businesses in Pakistan are becoming more professional due to their adherence to annual timetables. An individual investor, IND1, made a similar claim "While a late assignment reveals management inefficiency, an announcement that is made on time displays management effectiveness." However, suppose they fail to do so within 45 days after the end of the fiscal year. In that case, they must submit a justifiable extension request in line with the rules of Pakistan's Security Exchange Commission (SECP). Most of the interview results concur with Chen et al. (2005) and Tsai (2018), who discovered that bad news is more likely to cause announcement delays than historical patterns. From the management's and investors' perspectives, these findings are beneficial. At the same time, management can lessen the adverse effects of delay announcements on the pricing of firms' shares by timely disclosing the cause for the delay so investors can sell the stock promptly to avoid losses.

Information Sources

According to the assessment of the interviews, financial statements, online and print media, and the company prospectus are the primary information sources for individual investors. However, management meetings, analyst sessions, and an internal library keeps them timely informed and are the primary sources of information for institutional investors. Institutional investors strongly emphasize how analyst recommendations affect their investing choices. This is consistent with the findings of Ang and Ma (2001), who claimed that more robust profit predictions are communicated in analyst reports, preventing massive mispricing and generating solid returns. The importance of financial analysis as a source of information can be gauged from the existence of an internal financial analysis section at each investment firm. As per interview data, institutional investors rely on traditional (print and electronic media) and advanced sources of information (analyst and management briefing), whereas individual investors primarily rely on traditional sources. This deprives small investors of important information. This is owing to the possibility that Pakistan's small investors have the financial constraint to access analyst reports which are not free. At the same time, such information is exclusively available to institutional investors and presents further opportunities for profiting at the expense of small investors.

Malkiel (1981) contends that some analyst reports are unreliable because they replicate other analysts' work or follow earnings projections. A variety of responses were given in reaction to this statement. For instance, institutional investors applaud the financial analyst for being truthful in their assessment of the performance of the firms. The fact that one parent company in Pakistan owns a brokerage firm, runs fund management companies, and owns investment businesses may be the cause of institutional investors' defense of the analyst projection. However, individual investors claimed that the brokerage firm offered the recommendation and withheld the forecast before the release. This demonstrated that emerging economies like Pakistan lack access to professional information such as analyst projections (Tsai, 2018). However, institutional investors stated that it is difficult to forecast earnings in complex industries like the service sector is much more challenging, as opposed to quantified industries like the automobile, cement, fertilizer, oil, and gas, where firms update their sales figures regularly. According to one of the institutional investors, they must compare forecasts with those of other analysts, who made this statement "If the earning variation is a one-off, we try to determine what went wrong on our end and where the inconsistencies are. We also get in touch with the company's management to determine what caused the divergence, because consistent divergence from earnings forecasts will demoralise their customers". But according to Ang and Ma (2001), there is a significant bias in the analyst profit estimates for Asian nations, which is why financial analysts could not foresee the Asian financial crisis in 1997–1998. This raised severe concerns about their effectiveness and capacity to forecast price changes.

Investment strategies

In this section of the interview, the interviewer attempted to investigate Pakistani stock investors' investment practices in this part. The study of the interviews revealed that institutional investors strongly favour using fundamental analysis (such as financial ratios) when making investment decisions. The fund manager INS2 statement, "My investment theory is that although history generates ideas, it's fundamentals which will ultimately win," makes this clear. If you day trade, you will be at the mercy of perception, emotions, supply, and demand. It is difficult to achieve wealth creation in such circumstances". This shows that institutional investors only pay attention to a company's fundamentals since they don't think historical data affects the stock price. Another intriguing finding from the institutional investors' interviews is that they shun companies that disregard dividends and consider it one of many reasons for weak Trading in such companies. As per them, those firms who retain more earnings and distribute less provide no positive signal to investors. This shows that, as McCluskey et al. (2006) reported, investors want to receive dividends and view payouts as an indicator of a firm's future performance.

Individual investor IND4, on the other hand, claimed that "Fundamentals matter but are not independent of the past trading trend which provides insight about stock behavior." This shows that while determining a stock's trading position, individual investors take the price history into account. A possible explanation is that most individual traders are day traders with limited stock knowledge and a short-term outlook. In contrast to institutional investors' desire for long-term investments, the analysis of interview data confirms the individual investor's preference for short-term investments. This does not imply that institutional investors solely focus on long-term investments; instead, they search for opportunities that present themselves in the form of information advantages before engaging in day trading. It is clear from the IND2 comment that "Trading is based on rumor, but not investing, which relies only on facts. As a trader, it is possible to outperform the market but subject to the accuracy of the information because the market reacts to news and fundamentals. This suggests that institutional investors only engage in day trading when they perceive a profit potential and keep their investments for extended periods.

In addition to quantitative factors, institutional investors emphasized the significance of the sponsor and management of the company, which is determined by their qualifications, political affiliation, and track record. As confirmed by INS5 that "firms with the reputed board of directors and decorated Chief executive recovered after the financial crisis of 2008 but not the firms with the less reputed board of directors". On the other hand, individual investors neglected to explain how qualitative company characteristics influenced their trading choices". Moreover, respondents from various investment types note that they like liquid stocks constantly in demand, such as those from the pharmaceutical, beverage, food, and tobacco industries. Additionally, most survey participants agreed that personal emotions play a role in

Trading but disagreed on how much. When making investment decisions, for instance, individual investors argue that personal judgment provides a base for developing their opinions, which is consistent with behavioral finance theory. Comparatively, institutional investors contend that before making a buy, sell, or hold decision, they must take the internal analyst's advice into account. In summary, most institutional investors follow the advice of their analysts and base their selections mostly on fundamentals, with little room for personal judgment. In contrast, investors use personal judgments, rumors, and market mood to decide on daily trade.

Beating the Market:

According to Fama (1970), no investment can continuously do better than the market. Interviewees were questioned regarding their opinions of the Fama preposition in light of this. Most participants differed and argued in favor of the possibility of continuous outperforming of the market subject to investment strategy (80% of institutional investors and 60% of individual investors). Anomalies constantly exist in the market, but only some people can take advantage of these possibilities, according to INS2. As evidenced by our track record, in our situation, we have legitimate and skilled analysts that help us build trading methods that give us returns that are much higher than market returns. Overall, it was discovered that investors were confident in their ability to outperform the market in terms of returns, but only under certain trading conditions. This implies that investors must continuously examine the data for any potential anomalies and, as a result, revise their trading plans.

Announcement procedure:

All businesses listed on Pakistani stock exchanges are expected to publish quarterly financial statements and earnings per share following the Company Regulation 1984. The Securities Exchange Commission of Pakistan expressly specifies the earnings release process for all corporations listed on PSX (PSE rule book, 2015). Anybody can simultaneously view announcements because they are broadcast live online or via KATS (the Karachi automated transmission system). The participants were questioned regarding their satisfaction with the announcement method implemented by the Pakistani Security Exchange Commission in this aspect.

It is important to mention that every participant in the cohort gave a good response and expressed appreciation for the announcement process established by the Pakistani security exchange commission. Sixty percent of the private investors claimed that SECP initiatives were responsible for the recent noticeable improvements in the corporate governance of the Pakistani stock market. However, a small percentage of individual investors (40%) raised concerns of timely access to this information. "Information is not supplied equitably and promptly to everyone," IND6 expressed worry. Information is leaked before the official announcement date, allowing those with access to it to profit abnormally. The respondent was then asked how much information is revealed at earnings announcements. Nearly 90% of the participants (individual and institutional investors) expressed satisfaction with the quantity of information released at the time of results announcements, particularly following the 2012 SECP ordinance's adoption. These results are at odds with Defond et al. (2007), who attributed Pakistan's informational inefficiency largely to poor earnings quality.

CONCLUSION

This study analysed institutional and individual investors' perspectives on earnings announcements and their effects on stock returns. Considering the study objective, the debate aimed to assess investors' conduct around the earnings announcement day, investors' investment strategies, and their perspective on releasing procedures in PSX. Many inferences are formed per opinions stated by individual and institutional investors. First, the interviews indicated substantial interest amongst market players (individual and institutional) regarding the information content of earnings. Individual investors are shown to be quicker and more decisive in their trading around earnings releases. Hence trading varied among market participants as per earnings.

In contrast, institutional investors were cautious yet concerned about discovering the explanation for bad earnings, thus becoming a probable source of post-earnings release drift. Second, while most individual investors expressed concern about information leakage, they argued that SECP did an excellent job of containing or minimizing it. In comparison, considerable institutional investors reject the presence of information leakage and their effect on the share price. Thirdly, the interviews reveal that institutional investors follow your buy-and-hold investment strategy compared to day trading by individual investors. The justification stems from the goals of individual investors who prefer to purchase and sell (make quick gains) instead of retaining the investment over a long period.

Consequently, it can be argued that they engage in information-based trading to a greater extent than institutional investors. Fourthly, most survey participants disagreed with the efficient market hypothesis that it was impossible to consistently outperform the market. Particularly institutional investors who asserted that one could outperform the market if they had trustworthy information. Fifthly, the results from the interview provide an information edge to institutional investors considering their paying ability to analyse suggestions and access management briefing. In contrast, small investors cannot afford to pay for analyst recommendations and need to be made aware of management briefings, depriving them of access to excellent information. Institutional investors can manipulate the market and earn huge returns at the expense of regular investors, thanks to this informational advantage. The analysis of the findings reveals that institutional investors base their investment selections more on qualitative factors (such as management and sponsor) and firm fundamentals studies. Individual investors, in contrast, admit the more decisive influence of history and personal feelings in their investment selection. Seventhly, the interviewees unanimously applauded the institutions and systems that applied for granting equivalent admittance to the announced information. The respondents recognized the improvement made by the SECP in terms of reforms presented regarding disclosing procedures and considered it competitive with developed markets revealing practices.

CONFLICT OF INTEREST

All the authors in the article have no conflict of interest.

AUTHORS CONTRIBUTIONS

Conceptualization, M.I.K. and W.A; methodology, A.A; software, M.I.K; validation, F.S; Data analysis, S.H.K.; investigation, S.M.A.S; data curation, M.J., and S.H.K; writing—original draft preparation, M.I.K; writing—review and editing, M.I.K. and A.A; visualization, F.S; supervision, M.J. The published version of the work has been reviewed and approved by all authors.

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