



Do Firms Mislead Investors by Overstating Earnings Before Seasoned Equity Offerings?

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Abstract:

I examine earnings management around seasoned equity offerings and, consistent with Rangan (1998) and Teoh *et al.* (1998), find evidence of earnings management around the offerings. However, in contrast to their conclusions, I show that investors infer earnings management and rationally undo its effects at equity offering announcements. The investor naïveté conclusion of Teoh *et al.* (1998) and Rangan (1998) appears to be due to test misspecification. I conclude that seasoned equity issuers' earnings management may not be designed to mislead investors, but may merely reflect the issuers' rational response to anticipated market behavior at offering announcements.