The Effect of Accounting Conservatism on Cost of Capital: A Quantile Regression Approach for MENA Countries

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Abstract : Prior empirical studies have investigated the economic consequences of accounting conservatism by examining its impact on the cost of equity capital (COEC). However, findings are not conclusive. We assume that inconsistent results of such association may be attributed to the regression models used in data analysis. To address this issue, we re-examine the effect of different dimension of accounting conservatism: unconditional conservatism (U_CONS) and conditional conservatism (C_CONS) on the COEC for a sample of listed firms from Middle Eastern and North Africa (MENA) countries, applying quantile regression (QR) approach developed by Koenker and Basset (1978). While classical ordinary least square (OLS) method is widely used in empirical accounting research, however it may produce inefficient and bias estimates in the case of departures from normality or long tail error distribution. QR method is more powerful than OLS to handle this kind of problem. It allows the coefficient on the independent variables to shift across the distribution of the dependent variable whereas OLS method only estimates the conditional mean effects of a response variable. We find as predicted that U_CONS has a significant positive effect on the COEC however, C_CONS has a negative impact. Findings suggest also that the effect of the two dimensions of accounting conservatism differs considerably across COEC quantiles. Comparing results from QR method with those of OLS, this study throws more lights on the association between accounting conservatism and COEC.