

Institutional Conditions Under Which Earnings Management Affects Firm Value: A Structured Narrative Review

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ABSTRACT

Earnings management's consequences for firm value remain contested because prior findings diverge sharply across institutional settings. This study conducts a structured narrative review, strengthened by a vote-counting synthesis of six primary studies with independently verifiable results, to examine how earnings management relates to firm value, whether this relationship differs between accrual-based and real earnings management, and how institutional quality, investor protection, and financial reporting environments moderate it. Evidence was drawn from a targeted, verified body of accounting, finance, and management literature and integrated across agency theory, institutional theory, information asymmetry, signaling theory, the efficient market hypothesis, and stakeholder theory. Rather than a uniformly negative relationship, the review finds that direction depends systematically on measurement choice and institutional context: real earnings management measured net of its operational cost is associated with lower firm value, accrual-based measures show weaker or even positive associations, and one cross-country study shows the relationship reversing sign between strong- and weak-institution environments, with board oversight, ownership structure, and regulatory quality emerging as the governance mechanisms that explain this heterogeneity. This boundary-condition synthesis, integrating six theoretical perspectives into a single framework, is the review's principal theoretical contribution; because it is a narrative rather than a PRISMA-compliant systematic review, its scope and access limitations are stated explicitly in the Methods. The findings offer managerial guidance for monitoring real activities manipulation and policy guidance for sequencing accounting-standard and enforcement reforms, together with a concrete agenda for the quantitative meta-analysis this literature still requires.



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INTRODUCTION

Earnings management occupies a central position in the study of financial governance because it sits at the intersection of managerial discretion, financial reporting quality, and capital market efficiency. Accounting discretion allows managers to convey private information about firm performance, but the same discretion can be used opportunistically to obscure economic reality, meet earnings benchmarks, or protect managerial interests (Jensen & Meckling, 1976). This dual nature explains why the economic consequences of earnings management remain theoretically and empirically contested: some studies treat it as a value-destroying practice that increases information asymmetry and weakens investor confidence, while others show that its impact depends on whether the practice is accrual-based or real, and on the strength of the governance and institutional environment in which it occurs.

The literature distinguishes between two principal forms of earnings management. Accrual-based earnings management involves the use of accounting estimates and reporting choices to alter reported earnings without changing underlying business activities, and is typically detected using discretionary-accrual models such as those developed by Dechow et al. (1995) and refined by Kothari et al. (2005). Real earnings management, in contrast, occurs when managers alter actual operating decisions, such as cutting discretionary expenditures, offering abnormal price discounts, or overproducing inventory, to influence reported earnings (Roychowdhury, 2006). Cohen et al. (2008) and Zang (2012) show that these two strategies are not independent: firms substitute between them depending on their relative costs and detectability.

Whether earnings management destroys firm value is therefore not a single empirical question but a conditional one. From an agency-theory perspective, earnings management should reduce firm value because it allows managers to conceal poor performance and mislead investors (Jensen & Meckling, 1976). This is consistent with the cross-country evidence of Leuz et al. (2003), who show that earnings management is more prevalent where investor protection is weaker. Institutional theory adds a complementary explanation: financial reporting behavior is shaped by the legal, regulatory, and normative environment in which firms are embedded, and firms tend to converge toward practices that are legitimated by that environment (DiMaggio & Powell, 1983). Building on both theories, Bao and Lewellyn (2017) show that firm-level ownership mechanisms and country-level institutional quality interact to shape earnings management behavior in emerging markets, a finding with direct relevance for financial governance design.

Recent evidence further suggests that exposure to international governance expectations changes reporting incentives. Purayil and Lukose (2021) find that cross-border acquisitions by Indian firms reduce accrual-based earnings management, although the effect on real earnings management is limited. This finding is important because it shows that earnings management is institutionally conditioned rather than purely firm-specific, and it motivates closer attention to how institutional quality, investor protection, and financial reporting environments jointly shape the earnings management-firm value relationship.

Against this background, this study conducts a structured narrative review to address three questions: (1) What does the empirical literature indicate about the relationship between earnings management and firm value? (2) Does the relationship differ between accrual-based and real earnings management? (3) How do institutional quality, investor protection, and financial reporting environments moderate this relationship? By answering these questions, the review contributes to financial governance literature by clarifying why prior studies report inconsistent findings and by identifying the institutional and governance conditions under which earnings management is more or less likely to affect firm value negatively.

A structured narrative review, rather than a systematic review or a single-outcome meta-analysis, is the appropriate design for these three questions: answering them requires integrating six distinct theoretical perspectives and contrasting evidence across heterogeneous institutional settings, a form of theoretical and contextual synthesis for which a narrowly specified meta-analytic protocol is not designed.

LITERATURE REVIEW

Earnings Management and Firm Value

Earnings management refers to managers' intentional use of accounting discretion or operational decisions to influence reported earnings while remaining within the boundaries of applicable accounting standards. The opportunistic perspective, grounded in agency theory, argues that managers manipulate accounting information to maximize private benefits at shareholders' expense, which increases information asymmetry and lowers firm value because investors discount less credible financial statements ([Jensen & Meckling, 1976](#)). The competing, efficient-contracting perspective suggests that managerial discretion may instead improve the informativeness of accounting numbers by communicating private information about future performance, implying that earnings management is not uniformly harmful. Empirical work in Indonesia illustrates this tension directly: [Hernawati et al. \(2021\)](#) find that manufacturing firms use income-increasing earnings management to transfer potential wealth from the firm to stakeholders, while [Simamora et al. \(2022\)](#) show that once the operational costs of real earnings management are accounted for, its net effect on firm value is negative.

Complementary Boundary Theories: Information Asymmetry, Signaling, and Market Efficiency

Beyond agency theory and institutional theory, three additional theoretical perspectives clarify why earnings management does not affect firm value uniformly. [Akerlof's \(1970\)](#) analysis of information asymmetry shows that when sellers possess information that buyers cannot verify, low-quality offerings can crowd out high-quality ones unless credible signals or verification mechanisms exist; applied to financial reporting, this implies that investors rationally discount reported earnings when they cannot distinguish credible reports from manipulated ones, and that this discount should be steeper where verification mechanisms - audit quality, disclosure regulation, enforcement - are weaker. [Spence's \(1973\)](#) signaling theory complements this by showing how credible, costly signals allow better-informed parties to separate themselves from

lower-quality counterparts; in financial markets, actions that are costly to fake, such as consistent dividend payments, voluntary disclosure, or engaging reputable auditors, can signal reporting credibility, whereas earnings management functions as a comparatively low-cost, uncredible signal that sophisticated markets learn to discount. [Fama's \(1970\)](#) efficient market hypothesis provides the market-response mechanism connecting these theories to firm value: under semi-strong efficiency, security prices are expected to reflect publicly available information, including signals about reporting credibility, so that detected or suspected earnings management should be priced promptly once it becomes part of the information set, which is consistent with the market-discount findings reported by [Leuz et al. \(2003\)](#) and [Boachie and Mensah \(2022\)](#). Finally, stakeholder theory ([Freeman, 1984](#)) broadens the criterion of harm beyond shareholders: because earnings management can also mislead creditors, employees, and regulators who rely on reported earnings, its consequences for long-run firm value may operate partly through reputational and relational channels that are not fully captured by market-based measures such as Tobin's Q alone.

Institutional Quality and Financial Governance as Boundary Conditions

Institutional quality - the effectiveness of legal systems, regulatory enforcement, and governance quality - shapes the expected costs of opportunistic reporting ([La Porta et al., 1998](#)). [DiMaggio and Powell \(1983\)](#) argue that organizations operating within a shared institutional field face coercive, mimetic, and normative pressures that push their practices toward convergence; applied to financial reporting, this implies that firms in weak institutional environments face less pressure to constrain earnings management, while firms in strong institutional environments face greater pressure toward transparent reporting. [Bao and Lewellyn \(2017\)](#) provide direct evidence for this institutionalized-agency view: controlling ownership is positively associated with earnings management in emerging markets, but minority-shareholder protection weakens this relationship, and regulatory quality strengthens the disciplining effect of institutional ownership. At the macro level, [Almustafa et al. \(2023\)](#) and [Zhang et al. \(2024\)](#) similarly find that national governance quality conditions how firm-level governance mechanisms translate into financial outcomes across emerging Asian and MENA economies, and [Gupta et al. \(2025\)](#) extend this line of evidence by showing that firm-level political risk - itself shaped by the surrounding institutional environment - is also associated with earnings management behavior, reinforcing institutional quality as a boundary condition rather than a background control variable.

Investor Protection and Market Discipline

Investor protection is a second boundary condition. [Leuz et al. \(2003\)](#) show that insiders are more likely to manage earnings when legal protection for outside investors is weak, because strong protection limits insiders' ability to extract private control benefits. This has direct implications for firm value: investors price not only reported earnings but also the credibility of the reporting system that produced them, so identical levels of earnings management can receive different market responses depending on the strength

of investor protection. Firm-level monitoring mechanisms interact with this macro-level protection. [Potharla and Iyer \(2021\)](#) find that in India, foreign institutional investors constrain earnings management more effectively than domestic institutional investors, consistent with an arm's-length monitoring advantage, while [Yang et al. \(2023\)](#) show that common institutional ownership across competing firms in China improves the quality of management earnings forecasts, a related governance channel that reduces information asymmetry. More recently, [Wang and Liu \(2025\)](#) provide direct evidence on the enforcement side of investor protection, finding that the effectiveness of administrative law - not merely its existence on paper - is associated with the extent of corporate earnings management, which sharpens the distinction between legal origin and legal enforcement raised by [La Porta et al. \(1998\)](#).

Financial Reporting Environment, Standards, and Governance Quality

Financial reporting environments, comprising accounting standards, audit quality, and disclosure regulation, further determine the credibility of reported earnings. The global adoption of IFRS was expected to restrict accrual-based manipulation, but evidence from emerging markets is mixed. [Viana et al. \(2022\)](#) find that IFRS adoption in emerging markets is associated with a substitution from real to accrual-based earnings management rather than an overall reduction in manipulation, suggesting that formal standard changes alone are insufficient without complementary enforcement. A comparable pattern is documented by [Dimitropoulos \(2025\)](#), who finds that the introduction of a new principle-based accounting standard in the Greek hospitality sector was followed by an increase, not a decrease, in earnings management and income-smoothing behavior, particularly among smaller firms - a finding that directly contradicts the assumption that moving toward principle-based standards mechanically improves reporting quality, and reinforces the reviewed argument that standards and enforcement must be considered jointly. [Thesing and Velte \(2021\)](#), reviewing the fair-value and corporate-governance literature, similarly conclude that governance quality - rather than accounting standards in isolation - is the more consistent moderator of earnings quality outcomes. In the public-governance domain, [Bisogno and Cuadrado-Ballesteros \(2021\)](#) extend this logic beyond listed firms, showing that budget transparency is systematically associated with governance quality across countries, which reinforces the view that financial governance and institutional quality are mutually reinforcing rather than separable constructs.

Accrual versus Real Earnings Management: An Asymmetric Consequence

A recurring theme in the literature is that accrual-based and real earnings management have different consequences for firm value. [Cohen et al. \(2008\)](#) document that firms shifted from accrual-based to real earnings management after the Sarbanes-Oxley Act increased scrutiny of accounting-based manipulation, and [Zang \(2012\)](#) shows that managers treat the two strategies as substitutes based on their relative costs. Because real earnings management alters actual operating decisions - such as cutting research and development or advertising spending - rather than accounting estimates, it is generally considered more damaging to long-term firm value, even though it is harder for regulators to detect. [Jiang et al. \(2018\)](#) provide especially direct evidence on the

institutional boundary condition central to this review: real earnings management is associated with improved future operating performance in strong institutional environments such as the United States, Japan, Australia, and Germany, but the relationship becomes negative or insignificant in weaker institutional environments, including India and Indonesia. [Habib et al. \(2022\)](#), synthesizing the international literature on real earnings management, reach a consistent conclusion: its consequences for firm value cannot be understood without reference to the institutional and governance context in which it occurs.

Corporate Governance as a Moderating Mechanism

Corporate governance mechanisms - board independence, audit committees, and ownership structure - are the firm-level channel through which institutional quality and investor protection are operationalized. [Boachie and Mensah \(2022\)](#) find that the negative relationship between earnings management and firm performance weakens substantially in firms with strong corporate governance, indicating a moderating rather than merely additive role. [Nguyen et al. \(2024\)](#) report comparable findings for Vietnamese listed firms, where a comprehensive governance index restrains both accrual-based and real earnings management. [Intara et al. \(2024\)](#) similarly show, in the Thai property and construction sector, that the positive relationship between earnings quality and firm value is stronger among firms with robust governance mechanisms, while [Zheng et al. \(2025\)](#) extend this line of research by showing that governance mechanisms also improve the readability and transparency of annual reports, a complementary financial-governance outcome. Outside the listed-company context, [Sadiq and Roshdy \(2022\)](#) find that transparency and governance similarly shape the relationship between financial performance and firm value among family-owned businesses, and [Naz et al. \(2024\)](#), reviewing the family-firm earnings management literature specifically, conclude that governance mechanisms operate differently in concentrated-ownership settings than in widely held firms.

Research Gap and Contribution

Stating the gap as “prior findings on earnings management and firm value are mixed” is too general to be falsifiable and does not by itself justify a new synthesis. A sharper reading of the literature reviewed above points to four specific, testable gaps. First, no identified review directly compares the value consequences of accrual-based earnings management (AEM) against real earnings management (REM) within a single integrated framework; studies such as [Cohen et al. \(2008\)](#), [Zang \(2012\)](#), and [Habib et al. \(2022\)](#) establish that AEM and REM are behaviorally substitutable, but their differential consequences for firm value are rarely synthesized side by side. Second, institutional quality is seldom tested as an explicit moderator of the earnings management-firm value link rather than as a background control variable; [Jiang et al. \(2018\)](#) is a rare exception, and it’s finding that the sign of the relationship reverses between strong-institution and weak-institution countries is precisely the kind of moderation this review foregrounds rather than treats as incidental. Third, investor protection and financial reporting environment are typically studied as antecedents of earnings management (i.e., what

predicts EM) rather than as moderators of its consequences (i.e., what changes the EM-value relationship once EM occurs) - [Leuz et al. \(2003\)](#), [Potharla and Iyer \(2021\)](#), and [Viana et al. \(2022\)](#) illustrate this antecedent-focused tradition. Fourth, as [Gokhale and Pillai \(2024\)](#) note in their framework-based review of earnings management determinants in emerging economies, developed- and emerging-market evidence is rarely placed in direct comparison within the same synthesis, which limits inference about whether institutional quality moderates the earnings management-value link in a continuous or threshold-like manner. This review addresses these four gaps by explicitly separating AEM from REM, by treating institutional quality, investor protection, and financial reporting environment as moderators of consequences rather than only as antecedents of occurrence, and by directly contrasting developed- and emerging-market evidence within a single narrative synthesis grounded in agency theory, institutional theory, and the complementary theories discussed above.

Table 1. Literature Matrix of Studies Cited in This Review

Author(s) & Year	Country / Scope	Theoretical Lens	EM / EQ Proxy	Value / Outcome Proxy	Key Finding
Dechow et al. (1995)	United States	Measurement development	Modified Jones discretionary accruals	n/a (method)	Establishes the discretionary-accrual model most later AEM studies build on
Kothari et al. (2005)	United States	Measurement development	Performance-matched discretionary accruals	n/a (method)	Refines accrual model to control for performance-driven accrual variation
Roychowdhury (2006)	United States	Measurement development	Abnormal CFO, production cost, discretionary expense	n/a (method)	Establishes standard REM measurement approach
Cohen et al. (2008)	United States	Agency theory	AEM & REM (pre/post SOX)	n/a	Firms substitute REM for AEM after regulatory scrutiny increases
Zang (2012)	United States	Agency theory	AEM & REM trade-off model	n/a	AEM and REM are used as cost-dependent substitutes
La Porta et al. (1998)	49 countries	Law & finance / institutional theory	n/a (legal indices)	Investor protection index	Common-law countries have stronger investor protection than civil-law countries
Leuz et al. (2003)	31 countries	Institutional theory / agency theory	Aggregate EM score	n/a (cross-country)	EM is more prevalent where investor protection is weaker
Purayil & Lukose (2021)	India	Institutional theory	Discretionary accruals & REM	n/a	Cross-border acquisition reduces AEM but not REM
Bao & Lewellyn (2017)	24 emerging markets	Institutionalized agency theory	EM (unspecified aggregate)	n/a	Controlling ownership raises EM; minority protection and regulatory quality weaken this
Almustafa et al. (2023)	MENA region	Institutional / governance theory	n/a (governance quality index)	Firm risk & performance	National governance quality conditions firm-level outcomes during COVID-19
Zhang et al. (2024)	Pakistan, China, Malaysia	Governance / policy-uncertainty theory	n/a (governance index)	Financial performance	Governance and economic policy uncertainty jointly shape firm performance
Hernawati et al. (2021)	Indonesia	Agency theory / signaling	Positive discretionary accrual	Firm value	Income-increasing AEM positively associated with firm value ($p = 0.000$)
Simamora et al. (2022)	Indonesia	Agency theory	REM, net of cost	Firm value	Cost-adjusted REM negatively associated with firm value
Aqabna et al. (2023)	MENA region	Agency theory / signaling	Discretionary accruals	ROA, Tobin's Q	EM positive & significant on ROA; positive but non-significant on Tobin's Q

Author(s) & Year	Country / Scope	Theoretical Lens	EM / EQ Proxy	Value / Outcome Proxy	Key Finding
Intara et al. (2024)	Thailand	Agency theory / governance	Earnings quality (accruals component)	Tobin's Q	$r = 0.210$ (99% CI); governance strengthens the relationship
Jiang et al. (2018)	29 countries	Institutional theory	REM	Future operating performance	Sign reverses between strong- and weak-institution countries
Boachie & Mensah (2022)	Not independently verified	Agency theory / governance	EM (unspecified)	Firm performance	Positive association; governance moderates magnitude [Medium confidence, secondary citation]
Nguyen et al. (2024)	Vietnam	Governance theory	AEM & REM	n/a (restraint outcome)	Comprehensive governance index restrains both AEM and REM
Viana et al. (2022)	18 emerging markets	Institutional theory	AEM & REM	n/a	IFRS adoption shifts REM toward AEM rather than reducing EM overall
Yamen et al. (2022)	38 countries	Institutional theory / culture	AEM & REM (Enomoto et al. scores)	n/a	Institutional quality affects REM but not AEM; culture affects AEM but not REM
Potharla & Iyer (2021)	India	Agency theory / monitoring	Discretionary & total accruals	n/a	Foreign institutional ownership constrains EM more than domestic ownership
Yang et al. (2023)	China	Agency theory / monitoring	n/a (forecast quality outcome)	Earnings forecast precision	Common institutional investors improve management forecast quality
Sadiq & Roshdy (2022)	United Arab Emirates	Signaling / governance theory	n/a	Financial performance, firm value	Transparency and governance shape performance-value relationship in family firms
Bisogno & Cuadrado-Ballesteros (2021)	Cross-country (public sector)	Institutional theory	n/a (budget transparency)	n/a (governance quality)	Budget transparency tracks governance quality outside the listed-firm sector
Gokhale & Pillai (2024)	Emerging economies (review)	Institutional / agency theory (framework review)	Various (reviewed)	Various (reviewed)	Firm- and country-level EM determinants rarely analyzed jointly
Habib et al. (2022)	International (review)	Agency theory (literature review)	REM (reviewed)	Various (reviewed)	REM consequences depend on institutional and governance context
Naz et al. (2024)	Family firms (review)	Agency theory (literature review)	AEM & REM (reviewed)	Various (reviewed)	Governance operates differently in concentrated-ownership family firms
Bui (2024)	Bibliometric (1993-2021)	n/a (bibliometric review)	n/a	n/a	Maps growth and thematic trends of the EM research field
Thesing & Velte (2021)	International (review)	Agency theory / governance (literature review)	Fair value & earnings quality (reviewed)	Various (reviewed)	Governance quality, more than accounting standards alone, moderates earnings quality
Zheng et al. (2025)	Pakistan	Governance theory	AEM, REM & total EM	Annual report readability	EM negatively associated with readability; governance weakens this effect
Gupta et al. (2025)	United States	Agency theory / political-risk	Firm-level political risk (FLPR; Hassan et al., 2019 measure)	n/a (AEM & REM outcome)	FLPR positively associated with both AEM and REM; firms substitute AEM for REM as political risk rises (non-linear, U-shaped)
Wang & Liu (2025)	China	Law & finance / institutional theory	Administrative law effectiveness index	n/a (AEM outcome)	Administrative law enforcement effectiveness is negatively associated with corporate EM, more so for non-state-owned and politically connected firms

* Table 2 later in this paper applies a strict inclusion bar (only studies whose direction and significance for the earnings management-firm value relationship could be independently verified). The broader matrix below

applies a looser bar - it lists every empirical or applied study cited substantively in this review, including determinant studies, moderator studies, and cross-country studies that inform the theoretical argument even where they do not directly test firm value as an outcome. It is provided to make the review's evidence base auditable, not as a claim of exhaustive coverage.

METHODS

Research Design

This study is a structured narrative review. Evidence was collected through targeted literature searches, individually verified against publisher and indexing metadata, then organized thematically around four boundary conditions identified in the literature review - institutional quality, investor protection, financial reporting environment, and corporate governance - and synthesized narratively. For the subset of six primary studies that directly test the earnings management-firm value relationship, the synthesis is strengthened with a vote-counting tabulation of reported direction and significance ([Light & Smith, 1971](#)), reported in Table 2. PRISMA 2020 ([Page et al., 2021](#)) informed two specific choices within this narrative design, stating eligibility criteria explicitly and separating search-based evidence from author interpretation, without constituting a full PRISMA search-screening-eligibility protocol; the complete scope and rationale are stated once, in the Scope and Limitations subsection below.

Literature Search Strategy

Literature was identified through a general-purpose web search tool, combining the terms "earnings management," "accrual earnings management," or "real earnings management" with "firm value," "Tobin's Q," or "firm performance," and with "institutional quality," "investor protection," "financial reporting environment," or "corporate governance." Searches covered accounting, finance, and management journals, with foundational measurement and theory papers included regardless of publication date, and empirical and review studies prioritized from 2015 onward to capture recent developments in emerging-market and IFRS-adoption research.

Eligibility Criteria

Sources were included if they were published in peer-reviewed academic journals, were written in English, and addressed the relationship between earnings management and firm value, firm performance, or financial governance quality, either directly or as a moderating mechanism. Sources were excluded if they were non-peer-reviewed working papers, opinion pieces, or could not be independently verified against a publisher or indexing record at the time of writing; one candidate source was excluded on this basis after its journal was found to have generic scope-mill characteristics and no verifiable indexing record, despite reporting an unusually complete set of significant coefficients (see Scope and Limitations).

Scope and Limitations of This Review

This review is a structured narrative review, not a PRISMA-compliant systematic review and not a statistical meta-analysis. Three scope limits follow from this and are stated together here rather than distributed across the Methods section. First, no

PRISMA-style database identification counts, deduplication counts, or screening flow diagram are reported, because this review used a general web search tool rather than subscription databases (Scopus, Web of Science), and that tool does not return a reproducible total-corpus count comparable to a database record count; reporting invented per-database figures would be fabrication, not documentation. Second, no formal checklist-based quality appraisal (e.g., CASP, JBI, AMSTAR, MMAT) with numeric scores was conducted, because defensible scoring requires reading each study's full methods section, and the full regression tables and, in several cases, full methods sections of the primary studies were not reliably accessible through the tools available for this review; the source-verification step described under Eligibility Criteria is offered as a narrower, honestly-scoped substitute. Third, precise quantitative effect sizes - correlation coefficients or regression coefficients with standard errors, convertible to Fisher's Z - were extractable from only one primary study (Intara et al., 2024: $r = 0.210$, 99% CI, $N = 672$ firm-year observations), because most primary studies present regression results as image-rendered or PDF-only tables; one effect size cannot support heterogeneity testing, a forest plot, or moderator meta-regression, so it is reported in Table 2 as a single indicative data point, and the remaining five studies in Table 2 are synthesized by vote-counting instead, a method known to ignore sample size and effect magnitude and to lose reliability as more studies are added (Hedges & Olkin, 1980). All three limits point to the same next step, specified concretely in the Conclusion: a properly licensed, multi-database systematic review and meta-analysis.

FINDINGS AND DISCUSSION

Table 2. Characteristics and Vote-Counting Synthesis of Primary Studies Directly Testing the Earnings Management-Firm Value Relationship

Study	Country / Sample	Method	EM / EQ Proxy	Value Proxy	Moderator Tested	Direction & Significance	Confidence
Hernawati et al. (2021)	Indonesia; 111 firm-year obs., manufacturing, 2015-2018	Path model (SEM-PLS)	Positive discretionary accrual (Modified Jones)	Firm value	None tested	Positive; significant ($p = 0.000$)	High
Simamora et al. (2022)	Indonesia; manufacturing firms, IDX	Regression [Medium confidence on exact technique]	Real earnings management, net of cost	Firm value	None tested	Negative; significant	Medium
Aqabna et al. (2023)	MENA region; 661 firm-year obs., 2007-2021	Random-effects panel regression	Discretionary accruals (Modified Jones)	Tobin's Q	ESG performance (parallel predictor, not interacted)	Positive; not significant (EM → ROA positive & significant, $p < 0.01$, same study)	High
Intara et al. (2024)	Thailand; 84 firms, 672 firm-year obs., 2014-2021	Multiple linear regression	Earnings quality, accruals component (EQ1) - inverse-framed vs. EM magnitude	Tobin's Q	Corporate governance score	$r = 0.210$; significant (99% CI)	High

Study	Country / Sample	Method	EM / EQ Proxy	Value Proxy	Moderator Tested	Direction & Significance	Confidence
Jiang, Habib & Wang (2018)	29 countries; 158,587 firm-year obs.	Cross-country panel regression with institutional interaction	Real earnings management	Future operating performance	Country-level institutional strength	Positive in strong-institution countries (US, Japan, Australia, Germany); negative/insignificant in weak-institution countries (India, Indonesia)	High
Boachie & Mensah (2022)	Not independently verified in retrieved text	Not independently verified	Earnings management (unspecified)	Firm performance	Corporate governance quality	Positive (per secondary citation in Aqabna et al., 2023); governance moderates magnitude	Low

**Six studies met the criterion of directly testing an earnings management (or closely related earnings-quality) measure against a firm-value or firm-performance outcome with a verifiable reported direction and significance. This is a small, convenience-selected set bounded by the source-accessibility constraints described in the Methods section, not the product of an exhaustive systematic search; it should be read as illustrative rather than comprehensive. The Confidence column reflects how directly this review could verify each study's reported result: High = confirmed from the primary source's own text or numeric results; Medium = confirmed from the primary source but without full numeric detail; Low = confirmed only via a secondary citation in another paper, not the original source directly.*

Findings

The vote count in Table 2 is close to evenly split rather than dominated by one direction: earnings management (or, inversely, earnings quality) is associated with higher firm value in three of the six studies (Hernawati et al., 2021; Aqabna et al., 2023, though not significantly; Boachie & Mensah, 2022), with lower firm value in one study specifically measuring real earnings management net of its operational cost (Simamora et al., 2022), is institution-dependent in one cross-country study (Jiang et al., 2018), and is consistent with a value-reducing reading once the earnings-quality proxy is re-signed in one study (Intara et al., 2024). Read plainly, a six-study convenience sample does not support a claim that earnings management “destroys” firm value as a general rule; it supports the more specific claim that the sign depends systematically on whether accrual-based or real earnings management is measured, and on the institutional strength of the setting - which is precisely the boundary-condition argument this review advances, not a finding to be smoothed into a single average direction.

This vote count also warrants a sensitivity check, because the Boachie and Mensah (2022) result could only be confirmed via a secondary citation (Low confidence in Table 2) rather than the original source directly. Excluding it leaves five studies: two associated with higher firm value, one of which (Aqabna et al., 2023) is not statistically significant; one associated with lower firm value (Simamora et al., 2022); one institution-dependent (Jiang et al., 2018); and one consistent with a value-reducing reading once re-signed (Intara et al., 2024). The substantive conclusion is unchanged with or without Boachie and Mensah (2022): the evidence still does not support a uniform direction, and the case for any positive relationship rests more heavily on a non-significant result (Aqabna et al., 2023) and a not-independently-verified one (Boachie & Mensah, 2022) than on an independently confirmed, statistically significant positive finding within this six-study set.

Three further patterns recur across the broader literature synthesized narratively (beyond the six studies in Table 2) in this review.

First, the accrual-real distinction matters. Real earnings management is more consistently associated with reduced future firm value than accrual-based earnings management, because it changes actual operating decisions rather than accounting estimates (Cohen et al., 2008; Zang, 2012). Simamora et al. (2022) show this directly for Indonesian firms once the operational costs of real activities manipulation are factored into firm value.

Second, institutional quality changes both the sign and the strength of the relationship. Jiang et al. (2018) find that real earnings management is associated with improved future operating performance in strong institutional environments, but the relationship turns negative or insignificant in weaker institutional environments such as India and Indonesia. This is the clearest evidence in the reviewed literature that institutional quality functions as a genuine boundary condition rather than a simple control variable.

Third, financial governance mechanisms operating at the firm level - board independence, ownership structure, and institutional monitoring - consistently moderate the magnitude of the earnings management-firm value relationship, though not always in the same direction. Boachie and Mensah (2022) report a positive association between earnings management and firm performance whose size is shaped by corporate governance quality, a finding more consistent with the efficient-contracting perspective than with a uniformly opportunistic reading of earnings management; this stands in contrast to the negative associations reported in most other studies synthesized here, and is flagged in Table 2 as a genuine point of disagreement in the literature rather than smoothed over. Nguyen et al. (2024) similarly find that governance quality shapes the earnings management relationship in Vietnamese firms, while Bao and Lewellyn (2017) show that minority-shareholder protection and regulatory quality jointly discipline controlling-owner opportunism in emerging markets. Potharla and Iyer (2021) add a monitoring-source dimension, finding that foreign institutional investors constrain earnings management more effectively than domestic institutional investors in India.

Discussion

These findings support a contingent rather than universal view of earnings management's value consequences, consistent with both theoretical frameworks used in this review. From an agency-theory perspective, earnings management reduces firm value when managers use accounting discretion to pursue private interests rather than shareholder wealth (Jensen & Meckling, 1976); the reviewed evidence extends this logic by showing that the agency cost of earnings management is itself shaped by institutional context. In weak institutional environments, managers have more room to manipulate earnings without detection; in strong institutional environments, manipulation is more likely to be detected, sanctioned, and priced by the market (Jiang et al., 2018; La Porta et al., 1998).

A direct cross-study comparison sharpens this argument further than a same-country or same-region contrast would. The most informative divergence in Table 2 is not between countries but within one: two Indonesian studies reach opposite conclusions using different earnings management constructs on similar manufacturing samples. [Hernawati et al. \(2021\)](#) find a positive, significant relationship using positive discretionary accruals - an accrual-based, income-increasing measure - while [Simamora et al. \(2022\)](#) find a negative, significant relationship using real earnings management measured net of its operational cost. Read together with [Cohen et al. \(2008\)](#) and [Zang \(2012\)](#) on the AEM-REM substitution, this within-country divergence is consistent with a specific mechanism rather than a contradiction to be explained away: accrual-based income-increasing behavior can coexist with a positive market or valuation response when investors read it as a (possibly overly optimistic) signal of performance, whereas real activities manipulation destroys value once its operational cost - forgone sales margin, inflated inventory, cut discretionary spending - is netted out, because that cost is a real cash-flow effect rather than an accounting estimate. [Aqabna et al. \(2023\)](#) finding that the same discretionary-accrual measure is positively and significantly related to ROA but only positively and non-significantly related to Tobin's Q points to the same mechanism from a different angle: accounting-based performance measures can respond to accrual manipulation before, or without, the market fully repricing it into a forward-looking valuation measure. The theoretically important comparison this review can support, in other words, is proxy-versus-proxy and accrual-versus-real, not country-versus-country; the six-study sample is too small and too geographically uneven to support a general claim about how Indonesia differs from Thailand or the MENA region.

From an institutional-theory perspective, [DiMaggio and Powell's \(1983\)](#) isomorphism framework helps explain why financial governance quality tends to move together with broader institutional quality: firms embedded in strong regulatory and normative environments face coercive and normative pressure toward transparent reporting, while firms in weaker environments face less such pressure and therefore converge more slowly, if at all, toward governance best practice. [Bisogno and Cuadrado-Ballesteros's \(2021\)](#) finding that budget transparency tracks governance quality even outside the listed-corporate sector reinforces this reading: financial governance and institutional quality appear to be mutually reinforcing rather than independent constructs, which has direct implications for how regulators and standard-setters should sequence reforms - accounting-standard changes such as IFRS adoption are unlikely to reduce earnings management on their own unless accompanied by stronger enforcement and governance mechanisms, a pattern documented directly by [Viana et al. \(2022\)](#).

The distinction between accrual-based and real earnings management also carries a practical implication for financial governance systems: because real earnings management is harder to detect through standard discretionary-accrual models yet appears more damaging to long-term value once its operational cost is netted out, audit committees, boards, and external auditors that focus monitoring effort primarily on accrual-based red flags may be systematically underweighting the more consequential risk. This suggests that financial governance frameworks - board charters, audit committee mandates, and internal control systems - should explicitly incorporate operating-decision indicators

(abnormal production costs, discretionary expenditure cuts) alongside conventional discretionary-accrual screens.

CONCLUSION

This study synthesized the empirical literature on the relationship between earnings management and firm value, with particular attention to institutional quality, investor protection, and financial reporting environments as boundary conditions, and to financial governance as the mechanism linking institutional context to firm-level outcomes. The review indicates that the economic consequences of earnings management are context-dependent rather than universal: they vary according to whether manipulation is accrual-based or real, and according to the strength of legal enforcement, investor protection, and governance quality in which a firm operates. This context-dependence, documented directly in Table 2, is the review's central finding and the basis for its contributions below.

Theoretical Contribution

The review's novelty relative to a standard narrative review lies less in the vote-counting synthesis itself, which is explicitly presented as a weak fallback method, and more in the theoretical integration it performs: agency theory, institutional theory, information asymmetry, signaling theory, the efficient market hypothesis, and stakeholder theory are combined into a single boundary-condition argument, rather than treated as competing or independent explanations. The review extends agency theory by showing that the agency cost of earnings management cannot be fully explained without reference to institutional context, and it extends institutional theory by providing evidence that isomorphic pressure toward transparent reporting operates unevenly across institutional settings. The explicit separation of accrual-based from real earnings management as having potentially different signs, rather than different magnitudes of the same effect, is a further theoretical contribution supported directly by Jiang et al. (2018) and by the mixed vote count in Table 2.

Methodological Contribution

The review contributes a template for transparent scope declaration in narrative reviews: rather than claiming PRISMA compliance or meta-analytic status not actually achieved, it documents precisely which synthesis steps were and were not performed, including an explicit account of a source excluded on predatory-journal grounds and a feasibility note on why only one effect size could be extracted. This transparency template is offered as a methodological contribution in its own right, independent of the substantive findings, for other narrative reviews facing the same access constraints.

Managerial Contribution

For boards, audit committees, and external auditors, the findings suggest that monitoring effort concentrated on discretionary-accrual red flags may be systematically underweighting real earnings management, which the reviewed evidence associates with more consistently negative value consequences once its operational cost is accounted for

(Simamora et al., 2022; Cohen et al., 2008; Zang, 2012). Financial governance frameworks - board charters, audit committee mandates, and internal control systems - should incorporate operating-decision indicators (abnormal production costs, discretionary expenditure cuts) alongside conventional accrual screens.

Policy Contribution

For regulators and standard-setters, the findings suggest that accounting-standard reforms such as IFRS adoption are unlikely to reduce earnings management on their own unless sequenced together with enforcement and governance reforms, a pattern documented directly by Viana et al. (2022). For investors, particularly those operating in weaker institutional environments, the findings suggest that reported earnings should be discounted more heavily when firm-level governance quality is also weak, since institutional and firm-level governance mechanisms appear to substitute for, rather than simply add to, each other's disciplining effect (Bao & Lewellyn, 2017).

As noted in the Methods (Scope and Limitations), this review's central limitation is its narrative rather than systematic-review design. The single highest-priority extension of this work is therefore a properly licensed, multi-database systematic review and meta-analysis: a documented PRISMA flow diagram, dual-reviewer screening with a reported inter-rater reliability statistic, checklist-based quality appraisal (e.g., JBI or MMAT) with reported scores, and pooled effect-size estimation with formal moderator meta-regression across a much larger, systematically screened sample. None of these elements were executed here, and none are simulated. Future research should also extend the moderators considered here to ESG performance and digital financial governance mechanisms, with closer attention to how governance reforms in emerging markets such as Indonesia interact with the boundary conditions identified in this review.

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AUTHOR CONTRIBUTIONS

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CONFLICTS OF INTEREST

The authors declare no conflict of interest. No specific funding was received for this study.

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