Torpedo Your Competition: Strategic Reporting and Peer Firm IPO

Matthew T. Billett, Mark (Shuai) Ma, and **Xiaoyun Yu**

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Abstract

A firm's initial public offering (IPO) generates negative externalities for industry competitors. To mitigate this threat, incumbent firms manage their earnings downward, issue more negative management forecasts, and use a more negative disclosure tone when their industry peers file for an IPO. Negative accruals reverse when the threat subsides. Incumbents manage earnings more aggressively when costs are small and benefits are large, and when they follow negative disclosures of industry leading incumbents. Such strategic disclosure lowers incumbent firm valuation multiples and associates with more negative IPO firm media sentiment. IPO firms obtain lower offer prices, raise less capital, and are more likely to withdraw from the offering. They also invest less, hoard more cash, and experience lower profitability post-IPO, whereas incumbents experience higher profitability and market share growth. Our results highlight the role of strategic reporting on product market competition and identify a new cost of going public.