

CONSERVATISM AND THE COST OF EQUITY CAPITAL: A MULTI-DIMENSIONAL MEASUREMENT APPROACH

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ABSTRACT

Conservatism is a permanent phenomenon and issue in the accounting practice. It has been developing in two forms, ex ante and ex post, measured in various ways—the accruals, valuation model, and book-to-market measures. Prior studies document inconclusive findings on the association between conservatism and the cost of equity capital. These inconsistent findings motivate us to examine whether the various measures of conservatism have different effects on the relationship between conservatism and the cost of equity capital. We find that the accruals measure explains the relationship, while the valuation model and book-to-market measures do not. Our findings suggest that different measures of conservatism relate differently to different articulations. Researchers, therefore, should be cautious in interpreting the relationship between conservatism and the cost of equity capital.

Keywords: *ex ante and ex post conservatism, cost of equity capital, various measures of conservatism*