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Income Measures

Analysts' use of income measures and the consistency with IAS 1 Presentation of Financial Statements

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Abstract

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Title: Income Measures - Analysts use of income measures and the consistency with IAS 1 Presentation of Financial Statements

Keywords: IAS 1, income measurement, sustainable earnings, comprehensive income, operating income, net income, performance measurement, financial analysis and analysts' valuation of firms.

Background and background to the problem: The IASB and FASB started a joint project in April 2004 on financial statement presentation with the goal of further developing convergence of international standards. Proposed amendments to IAS 1 resulted in a revision of the standard in September 2007, which came into force in January 2009. The new presentation requires all owner changes in equity to be separated from non-owner changes, and a statement of comprehensive income was introduced due to the revision. Most research regarding comprehensive income concludes that it is not considered superior compared to other measures, with a few exceptions. Furthermore, previous research also discusses that comprehensive income might contribute useful information for the users of financial statements.

Purpose: The purpose of this thesis is twofold: first to come to an understanding of which income measures analysts use and if this is consistent with IAS 1; second to assess whether the IASB's view on what is needed to achieve enhanced usefulness of the financial statements is in line with what analysts use and demand.

Limitations: This thesis focuses on analyst reports concerning firms listed on the Stockholm Stock Exchange, which follows the IFRS, since it is relevant for the thesis to study information about firms who produce their financial statements according to IAS 1. Furthermore, the periods these analyst reports concern are 2006-2007 and 2010-2011.

Method: This study employs both qualitative and quantitative approaches. The main part of the empirical investigation is performed through an investigation of analyst reports. Furthermore, the study of analyst reports is supplemented by qualitative interviews with analysts.

Results and conclusions: The investigation of analyst reports provided evidence that analysts hardly use CI at all when creating their forecasts, and the fact that most of the respondents do not use CI in a great extent, it may indicate that the IASB's motivation regarding the revision of IAS 1 do not correlate with analysts' demands.

Abbreviations and definitions

BC	Basis for Conclusions
CI	Comprehensive Income = Net income + Other Comprehensive Income
EBT	Earnings Before Taxes
EBIT	Earnings Before Interest and Taxes
EBITA	Earnings Before Interest, Taxes and Amortization
EBITDA	Earnings Before Interest, Taxes, Depreciation and Amortization
ED	Exposure Draft
EV	Enterprise Value
FASB	Financial Accounting Standards Boards
IAS	International Accounting Standards issued by the IASB
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
NI	Net Income = Revenues - Expenses
OCI	Other Comprehensive Income = the difference between NI and CI
OI	Operating income = Operating Revenues - Operating Expenses, often referred to as EBIT
SFAS	Statement of Financial Accounting Standards issued by FASB
Users of financial statements	The principal users of financial statements are both investors and analysts who assists investors in the decision making process (Framework IASB pt. 9a & 10).

Content

1. Introduction

The introductory chapter consists of the background to the subject, a discussion of the problem leading to the research questions, and furthermore, the purpose and limitations of the thesis.

1.1 Background

Since its foundation, the standard setting organization IASB has been working to develop high-quality, understandable, enforceable and globally accepted financial reporting standards based upon clearly articulated principles (IFRS 2012a). A step towards reaching this goal was taken in 2002, following what is known as 'The Norwalk Agreement', when the IASB and the American standard setter FASB decided to work together to harmonize and improve international accounting standards (IFRS 2012b). In January 2005, IFRS became mandatory in the consolidated financial statements for all EU firms listed on the EU's stock markets (European Commission 2011a). This meant a major change for producers of financial statements as well as for users of financial information such as investors and analysts, since they had to become familiar with new standards of presenting the financial statements.

According to the IASB's conceptual framework, the users of the financial statements are first and foremost investors, but also analysts who assist investors in the decision making process. They both need information as a basis for evaluating a firm's financial performance (Framework IASB, pt. 9a & 10). Barton *et.al* (2010) evaluate the value relevance of income measures and which measures users of financial statements consider the most useful. The study comes to the conclusion that the measures most used are operating income (OI) and EBITDA (earnings before interest, taxes, depreciation and amortization). This suggests that measures most relevant to users of financial statements are those that include operating items and quickly capture information on a firm's cash flow (Barton *et.al* 2010, p. 786).

The IASB added the performance reporting project (renamed the financial statement presentation project in March 2006) to its agenda in September 2001 with the purpose of improving the usefulness of the information given in the income statement. The FASB also added a performance reporting project to its agenda in October 2001, but with a different model than the IASB. The IASB and FASB decided to work together on financial statement presentation with the goal of further developing convergence of international standards, and started a joint project in April 2004. The two standard setters came to an agreement that the project should not only address presentation in the income statement, but also the other statements in order to achieve a complete set of financial statements. The IASB issued an exposure draft (ED) in March 2006 of proposed amendments to IAS 1 Presentation of Financial Statements and published a revised version of the standard in September 2007, which came into force in January 2009. The new presentation requires all owner changes in equity to be separated from non-owner changes, and a statement of comprehensive income presenting all non-owner changes in equity, was introduced due to changes. As a response to the comments received during the consultation process, the IASB gives the producers of financial statements the option to present income and expenses and components of other comprehensive income in either a single statement of comprehensive income with subtotals or in two separate statements: a separate income statement followed by a statement of comprehensive income (IFRS 2012c).

1.2 Background to the problem

The question of whether or not comprehensive income has contributed to the value relevance of the presentation of financial statements has been frequently discussed in previous research. Furthermore, if the measure is useful for investors and analysts. Although few studies focus solely on Sweden, the authors consider other studies to be relevant since the IFRS issued by the IASB are international. The IASB's and FASB's standards are also converging due to the ongoing project.

Most research regarding comprehensive income concludes that it is not considered superior compared to other measures, with a few exceptions. Cheng *et.al* (1993) evaluate the usefulness of the three income measures, i.e. operating income (OI), net income (NI) and comprehensive income (CI), in explaining residual security returns. The study concludes that CI is the least useful measure, while OI is the most useful measure of the three. An interpretation of this conclusion may be that investors value operating items higher over non-operating items and thereby do not think that CI is relevant. However, the results could depend on the fact that investors are more used to the terms OI and NI and that CI also will appear relevant for investors over time (Cheng *et.al* 1993, pp. 201-202). Furthermore, a generalization made in the study that supports NI is that adding non-operating gains and losses to OI will increase the ability to explain residual returns. More specifically the authors state that non-operating items included in NI have incremental information content (Cheng *et.al* 1993, p. 201). The study made by Dhaliwal *et.al* (1999) where the question whether CI is superior to NI as a measure of firm performance, was found to correlate with the previous research considered by the authors. The study does not support the claim that CI is a better measure of firm performance than other income measures. According to Dhaliwal *et.al* (ibid) CI is less associated with returns than NI and predicts future cash flows and income more poorly than NI (Dhaliwal *et.al* 1999, p. 64).

Even though most research finds CI less useful than other income measures, there are studies that suggest the opposite. According to Kanagaretnam *et.al* (2009), CI does provide investors with useful information. As opposed to Dhaliwal *et.al* (1999), the study provide evidence that CI predicts future cash flow better than NI and that the measure relates more strongly to stock prices and return than NI (Kanagaretnam *et.al* 2009, p. 364). Cahan *et.al* (2000, p. 1297) are also positive to CI and imply that it is a measure more relevant to investors than NI.

As noted above, most research regarding CI has compared the measure to other ones, mostly NI, to come to an understanding of which is the most useful. Another way of valuing CI is to investigate what the measure might contribute to the financial statements. Robinson (1991, p. 112) discusses CI and what a presentation of financial statements that includes CI might bring. Some of the reasons for presenting CI, according to Robinson, are that CI is a way of clarifying changes in net assets and that it gives the users of financial statements information necessary to their decision making process. He also states that CI brings details to highlight the complexity of the numbers and makes it possible for the users of financial statements to make their own judgments. In a report, the CFA Institute, one of the largest and most influential groups of users of financial statements, argue that CI is needed to enhance the usefulness of financial reporting. They believe that CI makes it possible for components of different characters to be noticed and evaluated separately (AIMR 1993, p. 63). Furthermore, the report shows that much effort is required of analysts to locate and evaluate the income statement items when producing their forecasts, which is argued to be easier when CI is displayed (AIMR 1993. p. 88).

An issue that may question the usefulness of CI is that some of the OCI-components can be expected to fluctuate before they are realized. Goncharov and Hodgson (2011) found that the unrealized components, which fall within CI, might introduce disturbance and uncertainty because of their temporary and volatile nature. Some individual components of CI have proven to be value relevant when broken-down but when components of OCI are put together with NI, the usefulness declines for all users (Goncharov & Hodgson 2011, p. 56). Bamber *et.al* (2010) state that literature argues that managers tend to be concerned when making the initial choice regarding how to present CI. CI is generally more volatile than NI, and presenting CI in a single income statement might increase the firm's perceived performance volatility. Research and surveys show that managers expect users who perceive the firm's performance as more volatile to value the stock price lower, and to evaluate the manager as less competent. The concern regarding devaluation in terms of lower stock price, as well as their own job security, might provide incentives for managers to avoid performance reporting and instead report CI in the statement of changes in equity (Bamber *et al*. 2010 p. 121). However, IAS 1 (unlike SFAS 130) only allows CI to be reported in either a single statement of CI or in two statements. Given managers' concerns, the two-statement approach may be favored in this case since it presents CI in a statement separated from NI.

As mentioned in the background section, Barton *et.al* (2010) come to the conclusion that income measures located in the middle of the income statement are used most extensively and that the most relevant measures are OI and EBITDA. Also stated earlier in the current section, the result of the study by Cheng *et.al* (1993) is that OI located in the middle of the income statement is the most useful measure. McVay (2006) argues that managers wanting to maximize their presented performance tend to shift core expenses down (or revenue up) the income statement in order to present a better picture than the economic reality. As a result, managers overstate core earnings in order to meet analysts' forecasts (McVay 2006, pp. 501-502). This may be a factor that decreases the value relevance of income measures solely including operating items, for example OI and EBITDA. Furthermore, Hirst and Hopkins (1998) point out the many different ways firms are able to manage earnings: even the most experienced analyst can miss some occurrences of earnings management. Therefore, one of the primary reasons that AIMR lobbied the FASB to improve CI reporting is that they desire to increase analysts' detection of such activity (Hirst & Hopkins 1998, p. 70). This desire contradicts research that finds CI to be less useful as a measure compared to those located in the middle of the income statement.

1.3 Contribution to previous research

The information presented in the background and background to the problem discusses which measures previous research finds to be the most useful and whether the revision of IAS 1, leading to the introduction of CI, has contributed to the financial statements. This thesis contributes to previous research by analyzing analyst reports in order to find patterns indicating which measures analysts use, and if this is consistent with the changes made due to the revision of IAS 1. This approach addresses the problem and research questions directly. The IASB expresses that it aims to issue accounting standards in line with what the primary users of financial statements, analysts included, need and demand. However, an investigation of which income measures analysts use and if this is consistent with IAS 1, will reflect the usefulness of the revised IAS 1 for analysts. Furthermore, it will show whether CI has contributed in a way that is in line with the IASB's motivation regarding the revision of the standard. The investigation would also reflect the IASB's ability to meet analysts' demand and whether or not the IASB's view on presentation of financial statements has improved or caused disturbance in analysts' use of income measures.

1.4 Problem statement

With the background of the problem in mind the following research question has been stated in order to fulfill the purpose of the thesis.

Which income measures do analysts use and is this consistent with the changes made due to the revision of IAS 1 Presentation of Financial Statements?

The general research question has been divided into two sub-questions to help and guide the answering of the general research question.

- Has analysts' use of income measures been affected by the adoption of the revised IAS 1?
- Is the IASB's motivation regarding the revision of IAS 1 in line with analysts' demand?

1.5 Purpose

The purpose of this thesis is twofold: first to come to an understanding of which income measures analysts use and if this is consistent with IAS 1; second to assess whether the IASB's view on what is needed to achieve enhanced usefulness of the financial statements is in line with what analysts use and demand.

1.6 Limitations

The authors limit the investigation of analyst reports to firms listed on the Stockholm Stock Exchange, which follow IFRS, since it is relevant for the thesis to study information about firms which produces their financial statements according to IAS 1. Furthermore, the authors chose to solely focus on firms listed on the Stockholm Stock Exchange due to the restricted time frame of the study. The years included in the investigation of analyst reports are 2006-2007 and 2010-2011. The reason for this limitation is that the revised version of IAS 1 was adopted in 2009 with a permission of early adoption in 2008. Hence, according to the authors, 2008 and 2009 are transitional years. Furthermore, the authors limit this thesis to concentrating on sell-side analysts with a focus on equity, and will therefore refer to this when using the word analysts throughout the study.

2. Frame of reference

Previous research and theories were of help in the process of interpreting and analyzing the data reviewed in the empirical investigation. Knowledge was obtained by searching in academic databases, for articles and books, which discuss the different areas that the thesis concerns. Depending on the specific area of interest, both old and new articles were relevant. In order to receive reliable information, articles were only collected from peer reviewed journals. Furthermore, the authors are aware of the difference between scientific articles and textbooks, and how scientific articles are considered to be a more reliable source due to the undergone process before being published.

2.1 Description of analysts and their work

In this section analysts' work, their preferences regarding income measures, and their use of income measures are each outlined. Furthermore, the authors discuss valuation approaches for analysts and the importance of sustainable earnings.

2.1.1 The purpose and fundamentals of analysts' work

Analysts belong to the group of primary users of financial information. The main part of their work consists of gathering and processing information given in financial statements in order to assist investors (Schipper 1991, p. 105). Accounting literature often refers to analysts as 'sophisticated agents', whose purpose is to interpret firms' disclosures for investors (Byard & Cebenoyan 2007, p. 442). Therefore, analysts should be looked upon as a part of the group to whom financial accounting should be directed towards (Schipper 1991, p. 105). Analysts usually follow approximately ten to twenty stocks in a specific industry and their main objective is to produce a report that evaluates the securities of a firm, which is their final product. The report contains analysts' ultimate recommendations to the investors, i.e. - to either sell, buy or hold the stock. A forecast of earnings is one part of the information given in the recommendation and an input to the final product. Judging by the focus on earnings forecasts in financial media, this is relevant and important information to investors (Schipper 1991, pp. 112-113). Hirst & Hopkins (1998) also state that analysts are financial intermediaries and are therefore important users of accounting information. The authors suggest that fundamental variation in the way information is presented in the financial statements can be of importance for analysts' stock price estimates. Many investors use these estimates in their decision making process, which leads to a security purchase or sale (Hirst & Hopkins 1998, p. 69). An analyst's goal is to determine the level of investment in a firm and value the firm's residual return in order to fulfill the goal (Petersen & Plenborg 2012, p. 2). Furthermore, analysts want to achieve superior knowledge of an industry in order to possess a competitive advantage, which is the reason why analysts tend to work within a specific industry (Petersen & Plenborg 2012, p. 4).

When evaluating the role of earnings forecasts' impact on analysts' reports and recommendations, the recognition of the group's sell-side and buy-side analysts are of use. Both groups of analysts produce reports and give recommendations regarding which stocks to buy, sell or hold. However, sell-side analysts are referred to as the primary producers of earnings forecasts and are often employed at broker/dealer firms with the purpose of assisting individual and institutional investors. Buy-side analysts, on the other hand, tend to be employed by money management firms or institutional investors. Hence, buy-side analysts may use the reports of sell-side analysts to serve as an input in their own work process. The work of the two groups of analysts is not completely similar, depending largely on the employers and their differing incentives (Schipper 1991, p. 106).

2.1.2 The income statement and primary income measures for analysts

Firms' activities consist of operating, investing and financing. When measuring a firm's profitability, it is favorable to separate operating activities and investment in operations from financing activities. The reason for separating operating items from financing items is that a firm's operation is the core force behind value creation and constitutes the unique characteristics of a firm, which is difficult to replicate. Financing items, on the other hand, are easier to copy. However, the distinction between operating and financing items is not always clear in the financial statements, whereas this is perfectly clear in the analytical income statement (Petersen & Plenborg 2012, pp. 68-70). Barton *et.al* (2010) conclude that subtotals including core items are the most useful measures (Barton *et.al* 2010, p. 786). OI and EBITDA, which are measures located near the middle of the income statement, are more strongly connected with stock returns than subtotals at the top or bottom of the income statement such as sales and total CI (Barton, Hansen & Pownall 2010, p. 754). However, research regarding earnings management, also discussed in the background of the problem, and its effect on income measures states that measures solely including operating items might be overstated. Plummer and Mest (2001) examine a group of firms which can be expected to manage earnings upward in order to meet or exceed analysts' forecasts. The evidence indicates that the firms manage earnings upward by managing the operating revenue sales upward as well as managing operating expenses downward, which leads to overstated operating measures (Plummer & Mest 2001, p. 321). This question the value relevance of what most previous research argues to be the most useful income measures, which are measures located in the middle of the income statement.

In order to achieve greater knowledge concerning the sources of value creation in a firm, the analytical income statement requires all accounting items to be classified as items included in either 'operations' or 'finance'. Analysts reformulate the income statement in order to achieve a statement that reflects operating and financing activities separately, as investors find operating earnings to be the primary source of value creation in a firm, and usually value operations separately from financing activities. Operating earnings show the contribution from the core business with no regard to how it has been financed, and is therefore a key performance measure (Petersen & Plenborg 2012, pp. 70-73).

In recent years the income measures EBITDA and EBITA have become of great interest when valuing firms. One of the reasons for these income measures' popularity is that both EBITDA and EBITA are considered being closer to a firm's cash flows from operations than other measures, for example, NI. Furthermore, by eliminating depreciation, amortization and tax, the firms' different depreciation policies and estimates regarding deferred tax do not affect the measures, and analysts can avoid the impact of such activity. However, the use of EBITDA can be problematic since it is difficult to state that a great portion of a firm's costs are eliminated from operations. One of the problematic areas that is hard to motivate when using EBITDA is that depreciation is an approximate for the use of resources (e.g. property and equipment), and is needed when creating earnings. EBITDA does not include the costs of those resources but does, however, consider the revenues. Another problematic area is the change in accounting regulation regarding intangible assets. Instead of expensing investment in intangible assets, capitalization of intangible assets is required, e.g. - for development costs that in general have to be capitalized. Development costs used to be included in EBITDA but are now eliminated when using the measure. The two measures are not close to being considered as ideal cash flow measures since neither EBITDA nor EBITA consider investments in non-current assets, investments in working capital or non-cash items included in operating earnings, for instance provisions regarding restructuring, etc. (Petersen & Plenborg 2012, pp. 58-59). As discussed in the section background of the problem, OI, also referred to as EBIT, is an important measure similar to EBITA and EBITDA. The measure, in the same way as EBITA and EBITDA, reflects the results from the firms' core business and does not include financing (Petersen & Plenborg 2012, p. 73). However, EBIT as a measure also has weaknesses; for example, EBIT only partly considers investments. Furthermore, firms can manage EBIT growth by increasing interest-bearing debt and thereafter invest the profit in assets with a return below their cost of capital, even though this damages value (Petersen & Plenborg 2012, p. 310).

Although most research argues that CI is less useful as a measure compared to, for example, EBIT, EBITDA and NI, it is not to be said that CI does not bring additional relevant information. Smith and Reither (1996) state that by presenting CI in a statement of financial performance, the financial information of firms will enhance the ability to compare both within and among industries. Furthermore, they argue that the presentation of CI is friendly for the users and also brings more logic compared to the previous format where components of OCI were presented directly in equity (Smith & Reither 1996, p. 19). Kubota *et.al* (2009) recommend the disclosure of NI along with selected components of OCI. They conclude that NI plus the OCI component 'changes in currency translation adjustments' possess the highest information content. However, NI contains more relevant and incremental information than CI in full (Kubota *et.al* 2009, pp. 26-27). Hirst and Hopkins (1998) investigate the transparency of financial statement presentation and whether or not it has a predictable and measurable effect on analysts' estimates. They claim that a clear presentation of CI and its components in the income statement leads to enhanced transparency when compared to the presentation of the same information in the statement of changes in equity (Hirst & Hopkins 1998, p 50). Choi and Zang (2006) also investigate the effects of CI on analysts work and state that CI affects analysts' earnings forecast revisions and forecast errors. The result of the study is in line with analysts' shortcoming of not using the information presented in CI to its fullest extent. Furthermore, the results indicate that analysts revise their forecasts of future earnings downward when CI is smaller than NI, but do not revise the forecast upward when the situation is the opposite. This evidence shows an asymmetric use of CI, which is consistent with the assertion that unrecognized losses are more predictable than unrecognized gains concerning the future recognition of these activities (Choi & Zang 2006, pp. 77-78).

Earnings per share (EPS) constitutes earnings for the common shareholder, and Penman (2010) explains the two types of EPS reported by firms. EPS is defined as NI available to common shareholders divided by the number of common shares outstanding (Penman 2010, p. 38). EPS is a well-known performance measure often used by analysts and frequently reported in the business press. It may seem to be a perfect measure since it has associations with shareholder value. Shareholders aim for the highest earning possible for each invested share, and an increase in EPS should naturally result in increased shareholder value. Nevertheless, EPS does not for example consider risk, investments or time value of money. Furthermore, another important aspect that may affect the measure's usefulness is that EPS depends on applied accounting policies (Petersen & Plenborg 2012, p. 310). Analysts also use growth in EPS when valuing a firm since it may be a favorable correlation between the growth in EPS and firm value. There is a possibility that higher EPS will lead to higher firm value, and analysts may therefore value a firm at a higher rate if EPS is increasing. (Petersen & Plenborg 2012, pp. 140-141).

2.1.3 Valuation approaches and analysts' use of income measures

Analysts use income measures in different ways in order to value a firm. Valuation approaches can generally be divided into four groups: present value, relative valuation (multiples), liquidation and contingent claim valuation. The first approach includes models based on discounted future income streams or cash flows, where the most common types of income streams discounted are, for example, dividends and free cash flows. Relative valuation, also referred to as multiples, can be used by applying the price of a similar firm within the same industry to a variety of accounting numbers, for instance EBIT, EBITDA and NI. The liquidation approach is used in order to estimate a firm's equity. This is achieved by measuring the net yields that can be obtained if a firm liquidates all assets and settle all liabilities. The final approach is contingent claim valuation models, also referred to as real option models. This approach includes option pricing models in order to measure the value of firms sharing option characteristics (Petersen & Plenborg 2012, pp. 210-211).

Surveys have been conducted to investigate which approach analysts use most when valuing a firm. For instance, in one of the surveys made, the results show that analysts use the approaches present value and multiples in almost all cases. Furthermore, the results indicate that analysts use the liquidation approach in less than twenty percent of the cases, and that the real option approach is hardly used at all (Petersen & Plenborg 2012, p. 211). Present value approaches are based on analysts' projections of cash flows, and a discount factor reflecting the cash flow risk and time value of money. The most popular approach regarding present value is the discounted cash flow model, consisting of the two perspectives enterprise value and equity value. Both perspectives of the discounted cash flow model are technically quite simple. However, the valuation approach of both perspectives is time consuming and may generate estimates that are hard to communicate to laymen (Petersen & Plenborg 2012, pp. 212-219). The second valuation approach based on multiples is popular because of its low complexity and the fact that valuation of a firm can be performed quite rapidly. Nevertheless, using multiples when valuing a firm can be both time consuming and complicated. Furthermore, multiples can be deduced from the present value approach, which indicates that multiples and present value approaches may generate similar estimates. Several multiples can be applied, which can be divided into the two groups enterprise value estimates and equity value estimates. Some of the most popular multiples included in the group that estimates enterprise value are, for example, EV/EBIT and EV/EBITDA, while P/E (price-to-earnings ratio) and M/B (market-to-book ratio) are some of the most popular multiples estimating equity value. Furthermore, using multiples as a basis for valuation requires that firms are comparable and share, for example, the same economic characteristics and accounting policies. This requirement critically relies on the assumption that compared firms truly are comparable (Petersen & Plenborg 2012, pp. 226-227).

Analysts' use of some income measures that previous research has argued to be the most useful, are discussed below. For instance, EBIT is used when calculating the earnings measure return on assets (ROA), which measures how operating efficient a firm is in producing profits from its assets. ROA provides a clean measure since it separates financing effects from operating effects, which results in an expression of the true return on the total assets. Furthermore, EBIT is included in the calculation of return on capital (ROC), which is considered to be a more useful measure since it demonstrates the relation between operating income and the firm's invested capital (Damodaran 2002, pp. 43-44). Lie and Lie (2002) investigated earnings-based multiples used by practitioners to estimate the value of a firm. They concluded that the EBITDA multiple is a better estimator of firm value than the EBIT multiple. This indicates that depreciation expenses create disturbance regarding the information value of earnings. An explanation for this may be that the presented depreciation does not fully reflect the actual consumption of the assets (Lie & Lie 2002, pp. 44-47). Positive cash flows are fundamental in the long term if the firm wants to keep the business growing. EBIT is used when calculating cash flow from operations, which in turn is used to measure operating cash flow to capital expenditures. This measure is relevant since it captures cash flow in the long term (Damodaran 2002, p. 50).

2.1.4 Sustainable earnings - elimination of temporary items

Sustainable earnings are defined as earnings that can be repeated in the future and grow. The opposite of sustainable earnings, based on temporary factors, are usually named transitory earnings or unusual items. Since sustainable earnings consist of ongoing earnings that are not affected by one-time items, sustainable earnings are sometimes referred to as normalizing earnings. Furthermore, by identifying sustainable earnings, both the firm's growth and durable competitive advantage can be evaluated (Penman 2010, p. 394).

A substantial part of analysts' work in assisting investors consists of creating earnings forecasts that begin with current earnings. Based on this, it is of importance to investigate how much of a firm's current earnings emerge from the on-going business and how much arise from earnings that are nonrecurring. Different types of nonrecurring items that firms present in the income statement can be identified, for instance, gains and losses arising from the disposal of a division or an asset, restructuring costs or depreciation. Extraordinary items are referred to as unusual incidents, which occur rarely and have a material impact (Damodaran 2002, p. 42). However, firms are not allowed to classify items as extraordinary items in the statement of CI, income statement or notes when applying IFRS (IAS 1 IASB, pt. 87). Instead, many firms report a variety of items as special items in the income statement. An assertion regarding this fact is that firms may give indications to investors and lenders that these items should be eliminated when valuing the firm. However, from an analytical perspective, the inclusion of special items may be necessary in the valuation since IFRS do not define special items or specify how these items should be classified. Managers can therefore use their discretion when deciding what to include. Managers may, for example, label some items as special items when they in fact are recurring, which creates disturbance in the valuation. For instance, firms usually present restructuring expenses as special items and require analysts to eliminate these items when analyzing core operations and risk. Nevertheless, restructuring expenses in a broad sense are part of core earnings since every firm needs to adapt to current market conditions. Therefore, analysts should not disregard these items or other special items when producing their forecasts (Petersen & Plenborg 2012, pp. 398-400).

Kinney and Trezevant (1997) find evidence regarding non-recurring items that may cause disturbance in analysts' work. It is broadly acknowledged that analysts should conduct a thorough investigation of special items, and allocate them to suitable years when analyzing a firm's sustainable earnings. The study's results indicate that it is of great importance to make these adjustments if a firm's earnings for the current year are significantly above or below earnings presented in the prior year. The reason for this is that firms in this situation may recognize special items in order to manage earnings. Furthermore, the study suggests that analysts should consider the information in a firm's notes regarding description of special items, which may bring valuable information. Regarding the recognition of special items, the authors find that more special items are recognized in the fourth quarter than in the other quarters. Hence, analysts should pay more attention to earnings reported in the fourth quarter since these earnings may be subject to more manipulation than the earlier quarters' reported earnings (Kinney & Trezevant 1997, pp. 45-53). Penman & Zhang (2002) also investigate sustainable earnings. The P/E ratio indicates that investors buy a firm's future earnings and therefore look to current earnings in order to receive an indication of future earnings. However, investors question the earnings potential to be sustained in the future and therefore pay less for earnings that are not sustainable. Even though investors can adjust earnings and eliminate non-recurring items, they may still be concerned regarding the earnings' sustainability and wish to decrease their uncertainty. The financial statements can be used to find additional information about earnings and the commentaries work as indicators of future earnings. A competent analysis of a firm performed by investors or analysts includes this information since information about the sustainability of earnings decreases the risk of paying too much for a firm's earnings (Penman & Zhang 2002, pp. 30-31).

2.2 IAS 1 Presentation of Financial Statements

In this section the focus lies on describing the components of OCI, the IASB's motivation for the revision of IAS 1 and responses to the changes of IAS 1. The authors find it relevant for the thesis to present the complexity of OCI and how the users of financial statements have received the revised version of IAS 1.

2.2.1 Components of OCI

The components of OCI according to IAS 1 are presented below:

- Changes in revaluation surplus (see IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets*).
- Actuarial gains and losses on defined benefit plans recognized in accordance with paragraph 93A of IAS 19 *Employee Benefits*.
- Gains and losses arising from translating the financial statements of a foreign operation (see IAS 21 *The Effects of Changes in Foreign Exchange Rates*).
- Gains and losses on remeasuring available-for-sale financial assets (see IAS 39 *Financial Instruments: Recognition and Measurement*).
- The effective portion of gains and losses on hedging instruments in a cash flow hedge (see IAS 39) (IAS 1, pt. 7).

Smith and Reither (1996) discuss the fact that aggregated information concerning the components of OCI earlier was presented directly in equity, which made the individual components difficult to distinguish. According to Smith and Reither (1996) these components derive from a firm's economic decisions and activities, and are therefore necessary in order to evaluate economic performance (Smith & Reither 1996, p. 19). However, the components of OCI are often said to be less useful because of their volatile and unrealized nature. Studies indicate that when unrealized gains and losses are presented together with income components that result from transactions in a single statement, the valuation is more likely to reduce and the usefulness of financial statements is contracted (Goncharov & Hodgson 2011, p. 56). Choi & Zang (2006) discuss managers' ability to choose the timing and measurement of the reported components included in OCI. The authors also discuss the fact that the unrecognized items of OCI will affect future income when recognized, and they therefore investigate the relationship between CI and future earnings. Choi & Zang (2006) argue that the unrecognized gains or losses reveal the underlying economic situation of a firm and that the earnings will therefore be better or worse than estimated in the following periods. Hence, this indicates that current year CI is associated with the following period NI. The results of the study suggest that large unrecognized OCI gains are associated with significant positive changes in both the current and the following period NI. On the other hand, when the situation results in large unrecognized OCI losses, this is associated with negative changes in both current and future NI. The evidence from these results reflects that managers' discretion when choosing the timing of recognition of the OCI components depending upon their underlying economic situation (Choi & Zang 2006, pp. 90-93).

With the results from the studies presented above in mind, it is of importance to investigate whether analysts tend to use the information given in OCI when producing their earnings forecasts. An investigation of this nature requires the components of OCI to be considered and not only the aggregate value of CI. This since analysts may only use some of the components of OCI and not all of them, as well as the fact that the components may be of different association with analysts' earnings forecasts (Choi & Zang 2006, pp. 96-97). Choi & Zang (2006) discuss three of the OCI components included in CI according to IAS 1, and these are also typically the most frequently discussed components in previous research. First, the component available-for-sale financial assets is greatly dependent upon managers' discretion regarding recognition. For instance, managers possess the ability to sell marketable assets in order to increase or decrease earnings, or in some cases, to delay recognition. This behavior may sometimes be difficult for analysts to discover. Second, the component translating financial statements of a foreign operation can affect analysts' work greatly when the foreign currency rate changes dramatically. If such a change occurs, analysts may experience difficulties in anticipating the changes with accuracy. The change does not only affect translation of foreign operations but also the core business, which results in OI being affected even though the recognition itself does not directly influence OI. Third, defined benefit plans as a component of OCI are also associated with managers' discretion. This fact may result in difficulty for analysts when producing their earnings forecasts since it can be hard to see through managers' ability to use their discretion. (Choi & Zang 2006, pp. 97-98). Pronobis & Zülch (2010) state that the actuarial gains and losses on defined benefit plans may solely bring noise when estimating subsequent period's NI and CI. The authors attribute this to the lack of anticipation of future plan amendments and years of service regarding actuarial gains and losses on defined benefit plans, even though there is a possibility of occurrence (Pronobis & Zülch 2010, p. 20).

Choi & Zang (2006) conclude that analysts do not incorporate all of the information presented in CI when valuing a firm. The evidence suggests that analysts use the information reported in the components of OCI in the case of existing unrecognized losses and in these cases revise their forecasts. This is consistent with the assertion that analysts may consider CI more when unrealized losses exist than in the case of unrealized gains (Choi & Zang 2006, pp. 102-107). Furthermore, Pronobis and Zülch (2010) were able to verify the incremental predictive power of OCI components regarding earnings over more than one period (Pronobis & Zülch 2010, p. 20).

2.2.2 IASB's motivation regarding the revision of IAS 1

In the ED (2006) and Basis for Conclusions on IAS 1 Presentation of Financial Statements, IASB present the process of the standard's development and the thoughts behind the changes. As mentioned in the 'background', the IASB added the performance reporting project (renamed the financial statement presentation project in March 2006) to its agenda in September 2001 with the purpose of improving the usefulness of the information given in the income statement. Specifically, the board's goal is to assist management in enhancing the communication of financial information to the users of financial statements, and to help users in their decision-making process (IFRS 2011).

The ED (2006) is a result of phase A in the financial statement presentation project and addresses the complete set of financial statements (ED 2006, BC2). The purpose of the amendments to the standard was to enhance the information given in the financial statements in order to increase the users' capacity to analyze and compare financial information (IASB 2007, p. 1). The process of introducing a statement of CI in the financial statements began with the IASB discovering that an aggregation of items with shared features in the financial statements would be useful. Hence, it would be of interest to separate all equity changes in a period that result from transactions with the owners in their capacity as owners from changes in equity emerging from non-owner transactions. With the above taken into consideration, the IASB came to the conclusion that all changes in equity arising from transactions with the owners should be presented in the statement of equity, and separated from the non-owner changes, which are to be presented in a statement of CI (ED 2006, BC11).

The following area of interest was whether the non-owner changes in equity should be presented in a single statement or in two statements of CI. The two-statement approach would consist of an initial statement presenting the income and expenses that are a part of profit or loss, as well as a second statement presenting the income and expenses recognized outside profit or loss (ED 2006, BC12). The IASB made it clear that it preferred presentation of CI in a single statement. They based this view on the knowledge that all components included in the non-owner changes of capital meet the definitions of income and expenses in the framework. The framework does not define profit or loss, nor does it provide criteria to separate the components that should be a part of profit or loss from the ones that should be excluded (IASB 2009, BC51). Despite the board's own opinion, when considering the views of the respondents to the ED (2006), the IASB gave firms the option of presenting CI in either a single statement or in two statements. The conclusion made by the IASB expressed that the board's preference for a single statement was not as important as the decision to report owner changes separated from non-owner changes. This separation, which results in an improvement of financial reporting, was proven to be the most important goal. (ED 2006, BC15).

2.2.3 Responses to the revision of IAS 1

The proposed changes to IAS 1 regarding the presentation of CI in the income statement, presented in the ED (2006), were seen by respondents as an improvement in financial reporting followed by increased transparency. However, questions concerning the absence of definitions regarding the terms 'owner' and 'non-owner' in the ED, the Framework and the standards were raised. Furthermore, the respondents noticed a lack of consistency concerning the use of the terms 'owner' and 'equity holder' in the ED. Based on these concerns, the board decided to acquire the term 'owner' for further use in IAS 1, consistent with SFAS 130 (IASB 2009, BC38). The respondents to the ED (2006) showed different opinions concerning the option to either present the financial information in a single statement or in two statements. Most of the respondents preferred the two-statement option since it separates profit or loss from total CI. In this way, the income statement will continue to be the primary financial statement (IASB 2009, BC50). This may indicate that the users of financial statements tend to focus on measures like NI, which is a part of the original income statement. In addition to this, Thinggaard *et.al* found that on average NI is a more relevant measure than CI and that two statements thus may be favorable (Thinggaard *et al*. 2006, p. 35).

Discussions regarding the changes of financial statements' formats within the Financial Statement Presentation project of the IASB and FASB have been held. Hällefors (2006) finds that the presentation of financial statements needs to be improved due to the indications of an increasing trend of pro forma reporting, and the use of adjusted subtotals, such as EBITDA. Furthermore, a general argument against a single statement format seems to be that many users of the financial statements tend to focus on the bottom line in the income statement and that OCI does not constitute relevant information for the users of financial statement, but instead confuses them (Hällefors 2006). Thinggaard *et al.* (2006) found support for a single statement format (comprehensive income), however, the study also found NI on average to be more relevant than CI and may therefore support a two-statement approach (Thinggaard *et al*. 2006, p. 35). According to the findings, the results of the study are quite mixed but more in line with a single statement format. Furthermore, the study does not support the IASB's preference for a single statement format since the authors find some merit in the option for presentation format. This due to the fact that over time the actual effects of using the different formats will show and further empirical studies can be made to understand the economic consequences (Thinggaard *et al*. 2006, p. 60). Studies that investigate what impact the presentation of OCI has had on the users of financial statements are fewer than those investigating the best income statement format (Thinggaard et al. 2006, p. 60).

An argument that may support the two-statement preference of the respondents to the ED (2006) is that some of the OCI-components can be expected to fluctuate before they are realized. Goncharov and Hodgson (2011) state that presenting OCI together with NI in a single statement results in deteriorated usefulness. However, the individual components of OCI might be value relevant when separated from NI (Goncharov & Hodgson 2011, p. 56). This suggests that CI might bring usefulness when being presented according to the two-statement approach. Thereby, the individual components of OCI, which Goncharov and Hodgson (2011) argue to be useful, are separated from NI and presented in a separate statement of comprehensive income.

2.3 Debate regarding the IASB and the usefulness of IFRS

This part of the thesis consists of several articles giving rise to debate regarding the IASB and the usefulness of IFRS. Since the information presented in the articles is different views from praxis, it is not possible for the authors to conclude if the information is accurate.

Ratos, a Swedish private-equity conglomerate and one of the largest firms in their sector listed in Europe, have contributed to the debate regarding the IASB and the usefulness of IFRS (Ratos 2011). Strid and Pilebjer-Bosson (2010), economic editor and accounting specialist respectively at Ratos, state that the firm has experienced the use of IFRS resulting in great accounting problems regarding different areas. This has led to Ratos not being able to produce an income statement adjusted to the firm's business that is understandable for users of financial statements. Strid and Pilebjer-Bosson (2010) argue that the fundamental issue concerning IFRS derives from the fact that the IASB is an organization developing accounting standards without a democratic process. The authors state that this has led to unnecessary changes of accounting standards that have not experienced issues and therefore do not need to be revised. A solution to the issues, advocated by Hans Biörck, vice president and CFO of Skanska, would be to implement the model 'comply or explain' in the IFRS. This model is currently functioning as a principle in the

Swedish Corporate Governance Code. 'Comply or explain' means that firms are not forced to follow IFRS when another accounting solution is more appropriate, and will lead to a better reflection of the reality of the firm. The demand for using the principle is to report every deviation from IFRS and to present the alternative solution as well as the reasons for making the change. 'Comply or explain' extends the rule in IAS 1 paragraph 20 to not only be used in extremely rare circumstances. Strid and Pilebjer-Bosson (2010) state that this excellent idea should be put into practice by standard setters as soon as possible.

Marton (2010) responded to Strid and Pilebjer-Bossons criticism of the IASB. He states that the goal of IFRS is for the standards to result in effective capital markets and to achieve harmonization for listed firms within the EU, resulting in the central term comparability. With this goal as a foundation, the evaluation of the IASB and the usefulness of IFRS can be pursued. The author also responses to the critique from Strid and Pilebjer-Bosson (2010) regarding the view that the IASB make changes to accounting standards where no different solution is asked for or needed. He argues that the IASB have clear motivations when proposing amendments to accounting standards and would like to have an example of where this is not the case. Furthermore, Marton (2010) does not consider the model 'comply or explain', which is used in the Swedish Corporate Governance Code, to be a suitable principle for IFRS. For example, implementing this model in accounting would have a negative effect on the global comparability. 'Comply or explain' would make it more difficult to interpret firms' accounting and to read which parts that are established upon IFRS and which are not. This might result in not fulfilling the purpose of harmonization. In addition to this, Marton (2010) argues that firms are able to influence IFRS, when believing that the standards result in incorrect accounting that does not reflect reality, on both a principle as well as standard level. However, to achieve impact on the principle level might be more difficult since the IASB themselves have not found alternative solutions. Marton (2010) comes to the conclusion that the IASB is currently in the process of developing and amending accounting standards which results in the great opportunity of influencing IFRS's to come for different stakeholders. In order to achieve this, we have to understand the intention of the IASB (Marton 2010).

Malmqvist (2009) raises concerns regarding the proposed amendments to IAS 1 included in phase B of the project Financial Statement Presentation**.** The IASB suggests a total structure change regarding the balance sheet, income statement and cash flow statement. Malmqvist questions the IASB's investigators' knowledge regarding how analysts use the accounting information. The standard setter's key question is: what is 'financing'? The current balance sheet is, according to the proposed amendments, supposed to be replaced by a balance sheet based on net accounting. Debts and assets considered to be of an operating nature shall be net accounted, and what is left constitutes 'financing' and equity. However, the IASB do not yet know how to define 'financing', although, they do know that they do not want to define 'financing' in the same way that analysts and firms usually do for the moment, i.e. as net debt. Net debt separates 'operations' and 'financing' in the same way as the current income statement. Hence, debts and assets that create interest costs and revenues in the income statement are considered as interest-bearing. Net debt will arise when interest-bearing debts are larger than interest-bearing assets and net asset will be created when the situation is reversed (Malmqvist 2009).

International views regarding the IASB and IFRS have also been expressed. Whittington states that the IASB has experienced both great success and problems since the creation of the organization (2008, p. 496). The implementation of IFRS in the EU experienced difficulties, and two 'carve-outs' were made in the standard IAS 39 Financial Instruments regarding the fair value option and hedge accounting (European Commission 2011b). Furthermore, the EU-bodies expressed their concern over the fact that the IASB is dominated by English-speaking countries, which have an accounting tradition that often is referred to as Anglo-Saxon accounting (Whittington 2008, p. 496). Dilks (2007) argues that the response from firms regarding the implementation of IFRS for UK firms has been both positive and negative. The experienced downsides of adopting the IFRS, expressed by finance executives, are greater disclosures, followed by higher costs and longer preparation time. Concerns have also been raised regarding the complexity of the financial statements, which results in difficulties in understanding the financial data. Furthermore, more than half of the respondents to the study made by Dilks (ibid) do not find the financial information provided by IFRS to be useful. However, Dilks states that time has made financial executives become more positive regarding IFRS. The executives express that advantages of following IFRS are, for instance, improved consistency and comparable financial information for both firms and groups across Europe (Dilks 2007, p. 83).

3. Method

The chapter consists of the research method, data collection, analysis of data collected and a discussion concerning reliability and validity. Furthermore, the composition of the chapter is mostly divided into the mode in which data was collected.

3.1 Research method

In social science two methodical approaches are usually used and distinguished: the quantitative method and the qualitative (Holme & Solvang 1997, p. 13). The research method chosen in this thesis combines both quantitative and qualitative approaches. The quantitative method is formalized and structured, and the given information enables analysis and comparison of data. Its composition and planning is characterized by selectiveness and distance in relation to the source of information. The qualitative approach has the purpose of creating a deeper understanding of the problem and, unlike the quantitative method, is characterized by its nearness to the source of information. Furthermore, the core purpose of the method is to gather information in order to develop a deeper understanding of the problem investigated, as well as achieving the opportunity to describe the whole impression of the context (Holme & Solvang 1997, p. 14).

In this thesis an investigation of analyst reports as well as interviews were conducted using both the qualitative and quantitative method. The qualitative interviews were the first to be conducted, and the respondents were carefully selected based on their knowledge and experience as financial analysts. Following the interviews, an investigation of analyst reports was accomplished using a mix of the qualitative and quantitative method. Performing the interviews before the investigation of analyst reports facilitated both the understanding of the reports, and the ability to interpret and analyze the presented information. Using both the quantitative and qualitative approach may strengthen the relevance of the empirical investigation since a combination of the two methods can in many cases be favorable (Holme & Solvang 1997, p. 85). Holme and Solvang (ibid) state that the methods' respective weaknesses and strengths often cancel each other out, and it can therefore be beneficial to combine the two approaches. Solely performing an investigation of analyst reports may not provide a complete picture and therefore leave out the complexity of the problem. If only conducting qualitative interviews, the collected information may be questionable because of the respondent's personal opinions or reluctance to share all information regarding the subject for different reasons. Eliasson (2010, p. 31) also supports a combination of quantitative and qualitative methods and states that a combination often leads to a more complete picture than the case when using only one method.

3.2 Data collection

3.2.1 Investigation of analyst reports

The main part of the empirical investigation consists of an examination of analyst reports, to observe which income measures analysts use most. Furthermore, this study considers whether the use of income measures has been affected by the revision of IAS 1. Collection of data from analyst reports has been enabled by access to the database Thomson Research, which provides research reports on firms worldwide from over 1400 sources (Thomson Research, 2012). The analyst reports included in the investigation generally consist of text, tables and figures. Most reports start with an introduction that includes information regarding the firms' recent performance, a summary of the analysis and a valuation made by the analysts, and a recommendation or rating. The distribution between text and tables varies between different reports.

A document study is usually performed with a qualitative approach, although, it is also suitable to use as a data source when summarizing information from documents into quantitative data. This is most frequently done by a comprehensive work of encoding (Gustavsson 2004, p. 49). The analyst reports were examined with a focus on four areas: structure, content, use of income measures in text and use of income measures in tables. Each report was investigated from this perspective in order to understand the construction and to find patterns in the reports. After examining a few reports, income measures were found to be mentioned in the running text as well as in tables. The measures mentioned in the running text were often more extensively analyzed in individual tables. Furthermore, financial statements containing several measures were frequently presented. Many of these measures were never mentioned in the running text, nor presented in individual tables containing more detailed information regarding the specific measure. The separation of measures, as described above, was a result of a discussion regarding the reasons for an analyst to present a measure in text respectively in tables. The measures presented in tables solely containing numbers might be considered to be more concrete by analysts and thus more important than measures in text. Furthermore, if a measure is mentioned in both text and tables this might indicate that the measure is especially important. The investigation of the reports showed that approximately all measures mentioned in text also were presented in tables, except components of OCI.

The first step in examining the analyst reports was to process the data from the reports into categories, as described above. The following step was to transform the data collected from the analyst reports to quantitative data, by creating tables which displayed the frequency of measures mentioned in the reports. Furthermore, the received data was interpreted and described in text in order to better understand the findings. A potential disadvantage regarding the method of examining the analyst reports might be that the investigation was done manually. The human factor might have caused the authors to miss out on measures, leading to errors in the calculation.

However, these potential errors are not believed to have any significant impact on the final result. By performing the described process to examine the reports, statistical generalizations could be made and the authors were able to better understand the work of analysts and gain insight into what their focus is when producing their reports.

3.2.1.1 Selection of firms

As mentioned in the section limitations, the selection was limited to firms listed on the Stockholm Stock Exchange. The segments large, mid and small cap, with a total of 254 firms listed, constituted the basis for the selection. The mode in which the authors chose the firms to be included in the study, was conducted by thoroughly investigating which firms are included in the database Thomson Research. This investigation confirmed 173 firms existing in the database. Furthermore, it was of great importance to determine whether or not the analyst reports on the 173 firms were relevant and useful for the study. In order to determine the usefulness of the analyst reports, and thereby complete the selection of firms, the reports were investigated from a general perspective, hence, not as thoroughly as the actual investigation of the final selection of analyst reports. The criteria considered when performing the overall investigation regarding selection of firms, were the existence of reports concerning the chosen periods to be included in the study and the length of the reports. After performing the overall investigation of the reports on the 173 firms, the authors found that the reports on 154 firms met the requirements to be included in the study (see table 3.1 below for information about the selected firms).

Table 3.1 Description of firms included in the investigation

Industry	No of Firms Small Cap	No of Firms Mid Cap	No of firms Large Cap
Consumer Discretionary	7	14	4
Consumer Staples	3	1	3
Energy	1	1	0
Financials	4	9	9
Health Care	11	3	2
Industrials	18	10	12
Information Technology	21	7	2
Materials	2	0	3
Telecommunication Services	2	0	2
Utilities	3	0	0
Total			**154**

3.2.1.2 Selection of analyst reports

In order to come to the conclusion of which analyst reports to include in the investigation, the authors analyzed all the reports on the 154 selected firms concerning the chosen periods, from a general perspective. Furthermore, in order to limit the investigation of analyst reports due to a restricted time frame, the authors chose to concentrate on the reports issued by the most frequent contributor. In order to select the most frequent contributor issuing reports on the firms, the issuers' number of reports were investigated and an average calculated. Thereafter, the most frequent contributor was chosen to be included as a basis for the selection of reports. In cases where two contributors received the same frequency, the contributor with most periods included or most extensive reports was selected. The authors find the most frequent contributor issuing reports on the firms relevant as a basis since these sources in general distinguish themselves significantly from those regarding the number of reports issued. The criterion for the reports to be considered in the overall investigation was that the reports were extensive enough to include the information needed. Therefore, the authors considered reports consisting of ten pages or more. After performing the overall investigation, two reports issued by the main contributor on each firm, one before and one after the transitional years, were selected. In cases where this was not possible, two reports were selected from either before or after the transitional years. Furthermore, the number of reports in every period was summarized in order to ensure that a suitable balance of periods before and after the transitional years was achieved. Thereby, the final number of reports included in the investigation of analyst reports was determined to be 150 reports. In order to receive a balance regarding the time periods, 75 reports from each period were randomly selected.

Table 3.2 Description of analyst reports included in the investigation

Industry	No of Reports Small Cap	No of Reports Mid Cap	No of reports Large Cap	**Total**
Consumer Discretionary	8	17	8	33
Consumer Staples	3	1	4	8
Energy	1	1		2
Financials	4	12	12	28
Health Care	13	3	2	18
Industrials	16	11	15	42
Information Technology	5	7	2	14
Materials	0	0	2	2
Telecommunication Services	0	0	3	3
Total	**50**	**52**	**48**	**150**

3.2.2 Qualitative interviews

The qualitative interviews were conducted in order to create a deeper understanding of analysts' way of thinking, which income measures they use and how they use the measures in their work. This knowledge facilitated the investigation of analyst reports regarding the understanding of the reports' structure as well as knowing which information to focus on in the reports. Furthermore, it made the interpretation of the retrieved information as well as the finding of patterns in the reports easier.

The process of preparation before conducting the interviews was of great importance to the authors. Possessing as much knowledge as possible regarding the different areas of the investigation was significant in order to obtain a great amount of information from the interviews. Furthermore, it made understanding the information given in the interviews easier. The objective above led the authors to a thorough investigation of, for instance, previous research, which resulted in a large part of the frame of reference being outlined before conducting the interviews. An examination of the analysts' background was also performed, and where possible, articles written by the analysts were reviewed. Such views regarding the capture of knowledge before conducting interviews are in line with those of Patel and Davidsson (2003), who state that an advantage when performing qualitative interviews is for the interviewer to possess great knowledge regarding the area to be investigated. In order to obtain the necessary knowledge and thereby enhance the interviews outcome, the author may, for example, investigate previous research (Patel & Davidsson 2003, p. 79).

Carefully considered respondents were contacted via e-mail in order to evaluate their interest in participating in the qualitative study. The analysts who replied to the e-mail were positive to the idea of participating. After the falling-off of one analyst who did not possess the knowledge needed regarding IAS 1, four qualified analysts were left. The interviews were carried out by telephone given the geographical distance separating the authors and respondents. The interviews were not recorded since both authors took notes, which ensured the obtaining of information. Registering the answers during the interviews by taking notes is a demanding way of conducting interviews. However, recording the interviews may affect the answers given by the respondents since they may not feel comfortable: respondents usually react positively in the absence of a tape recorder and the answers given are more spontaneous (Patel & Davidsson 2003, p. 83).

Furthermore, a set of interview questions was produced which treated the areas *personal background, income measures, IASB, IAS 1* and *others*, complemented with sub questions. According to Holme & Solvang (2012) it is of great importance that relevant areas for the study are discussed during the interviews, and an outline functioning as guidance is necessary. This, however, does not imply that the outline should be followed in detail, and there are no limitations to improving or changing the outline during the interviews (Holme & Solvang 1997, pp. 99-101).

The interview questions were not sent to the respondents prior to the interviews: instead a brief summary of the research subject was presented at the beginning of the interviews. The first two analysts contacted were given the opportunity to receive the interview questions in advance but they explained that this was not necessary. Due to this perceived lack of interest, the remaining analysts were not presented with the option of receiving the interview questions in advance. Furthermore, the analysts did not express this desire themselves. One benefit of not presenting the interview questions prior to the interviews is that spontaneity regarding the answers is ensured. The fact that the respondents did not request the interview questions in advance shows that they possess great knowledge and confidence regarding their work. Furthermore, it may indicate that the respondents wished to discuss the different areas freely.

The interviews were structured and controlled loosely in order to allow the respondents to develop their answers and lead the conversation into other areas that could be of interest for the thesis. Considering this approach, the order of questions was in some cases modified to maintain fluidity in the interview. In the process of carrying out the interviews, new insights and knowledge were brought to the authors, which lead to changes and improvements concerning the interview questions. When performing qualitative interviews the composition must be flexible in order to achieve the possibility of changing it during the investigation. For instance, this requirement enables improvement or correction of the interview questions if needed, which leads to enhanced quality of the interviews. Nevertheless, the flexibility of qualitative interviews may cause difficulty when comparing and generalizing the results (Holme & Solvang 1997, p. 80).

3.2.2.1 Selection of respondents

The respondents to the qualitative interviews were carefully examined and selected. One of the key elements taken into consideration when selecting the respondents was that the respondents possess general knowledge and experience regarding the standards and rules of accounting for listed firms. Furthermore, that the respondents have an analyst's financial perspective and understanding of the meaning and process of analysts' work was of great importance. The criteria above formed a central base in the search for respondents. Regarding the number of respondents, there are limitations when considering, for example, the situations of the interviews, the choice of respondents and the analysis of the gathered information. The selection of respondents should be based on carefully considered criteria, which are strategically and theoretically defined (Holme & Solvang 1997, pp. 100-101). Another key element was that the respondents were positive to the idea of participating. This would, in the view of the authors, ensure a greater amount of information to be received from the interviews. Kvale (1997, p. 135) states that some of the qualities of preferable respondents are that they are willing to cooperate, are motivated and possess knowledge that is of relevance. This supports the authors' view of what a key element in performing qualitative interviews is.

3.2.2.2 Presentation of the respondents

Johan Broström has eighteen years of experience from the financial market and is currently the chairman of the Firm Valuation Group, which is a part of the association Swedish Society of Financial Analysts, SFF (SFF 2012a; JRS Securities, 2012). The group write and update the book *Finansanalytikernas rekommendationer* which assists financial analysts. Accounting rules concerning listed firms in combination with how these rules affect analysts work are also discussed by the group (SFF, 2012). Broström is also the head of research and in charge of special situations of the firm JRS Securities (JRS Securities, 2012).

Robert Gärtner has a background of studying international business and has been working as a financial analyst for approximately eighteen years[1]. Gärtner is currently a member of the Firm Valuation Group, which is a part of SFF (SFF, 2012a). He has also worked as an equity analyst for Handelsbanken Capital Markets since 1998. Since 2003 Gärtner has worked more in general with, for instance, infrastructure of analysis, educating analysts and accounting issues[2].

Peter Malmqvist has approximately twenty years of experience from the financial sector. He started his career as an accountant but was soon found in the world of finance. Malmqvist is currently the chairman of SFF and the CEO of his own firm EQR (SFF, 2012b), which produces analyses of stocks, interests and the state of the market that are frequently presented in magazines such as *Aktiespararen* and *Privata Affärer.* Malmqvist also writes articles concerning accounting problems for the magazine *Balans* (EQR, 2012) .

Martin Nilsson has been working as a financial analyst for approximately eleven to twelve years. He started his career at the independent investment bank Carnegie and stayed there for eight years. Nilsson is currently working as an analyst for Handelsbanken Capital Markets and has been for three years. His main focus is on firms in the telecommunications industry[3]. In 2011 Financial Hearings ranked Martin as analyst of the year (Dagens Industri, 2011).

3.3 Analysis of data collected

3.3.1 Analyst reports

The data collected is analyzed through a qualitative analysis, more specifically a textual analysis. When performing a qualitative analysis the data source usually consists of text and is quite extensive. It is often rewarding to do an ongoing analysis during a qualitative analysis and

[1] Robert Gärtner Equity Analyst Handelsbanken Capital Markets, telephone interview 14th of March 2012
[2] Robert Gärtner Equity Analyst Handelsbanken Capital Markets, telephone interview 14th of March 2012

[3] Martin Nilsson Equity Analyst Handelsbanken Capital Markets, telephone interview 13th of March 2012

thereby gain new ideas regarding the work ahead (Patel 2003, p. 119). All analyses, qualitative included, consist of finding patterns and sorting the material. This is done by encoding the material, which can be explained as a cyclical process where the material is reread several times (Svenning 2000, pp. 151-152).

The data collected from the investigation of analyst reports was analyzed by generating categories, which is a result from encoding the empirical material (Marton 1998, p.70). When this first phase of the analysis had been conducted, the process of attempting to explain the detected patterns received from the collected data and finding evidence in the material for functional explanations began. The tables demonstrating the frequencies of measures mentioned in the analyst reports were presented and described with text in order to create a deeper and clearer understanding of the findings. The presentation and analysis of these results were based on the research questions, which were formulated in order to fulfill the purpose of the thesis. The findings of the examination of the analyst reports were at first analyzed separately. Later on the results was compared with the statements regarding which measures analysts most frequently use, given by the respondents to the interviews. Furthermore, the analysis of the outcome was carried out with the measures discussed by previous research, presented in the background to the problem and frame of reference, in mind. The second phase in the process of analysis was carried out by considering the importance of interaction between the generated categories and the empirical data. Marton (ibid) emphasizes that a continuous one-way logical flow from the categories to the empirical data is not possible. Instead the direction of the logical flow will change during the analysis (Marton ibid, p. 68).

3.3.2. Qualitative interviews

There is no correct or incorrect way of analyzing the data collected from qualitative interviews. The mode in which the gathered information is processed in order to achieve a qualified text is a decision to be made by the researcher. However, the analyses typically involve processing a large amount of text, which is developed into a text with structure and interpretations. Some researchers, for example, work with the text in a physical way by cutting and sorting the text, while others may divide the text into different sections by using software (Patel & Davidsson 2003, p. 121).

As for the analysis of the gathered information when investigating analyst reports, the authors performed ongoing analyses of the data collected from the qualitative interviews. The registered answers, received by taking notes during the interviews, were examined directly after the interviews to ensure that additional information still fresh in mind was transferred into text. An important aspect to take into consideration when conducting interviews is the fact that the spoken language differs greatly from the written language. For instance, gestures, body language and intonation are eliminated when transferring the conversation into text (Patel & Davidsson 2003,

p. 104). With this in mind, the attempt to capture the mood of the interviews with as much precision as possible was made when examining the registered answers. The fact that the examination was performed directly after the interviews may be a factor that enhanced the quality of the registered data. Furthermore, in order to prepare for the final analysis of the interviews, the data was reread several times.

When conducting the final analysis of the interviews the data was sorted into different sections using software. These sections constituted the specific problem areas included in the study, and the authors thereby obtained an overview of the respondents answers regarding the different areas. Thereafter, the text was structured and inte, which made it possible to present a useful and qualified text in the chapter empirical investigation. The final product of the qualitative processing of data is usually a text presenting quotes from interviews and the author's own interpretations of the information. It is of great importance to balance quotes and interpretations. This should be a goal for the final product to make the final text qualified and useful to the reader (Patel & Gustavsson, p. 120). In order to obtain reliability when presenting the empirical findings from the interviews in a structured text, the authors included quotes within the text. This was aimed at giving the reader the opportunity to analyze some of the findings without the authors' interpretations. Nevertheless, the greatest part of the text consists of the authors' own commentaries and interpretations. The reason for this was to present a well analyzed and qualified text that is of use for the reader, without the reader being forced to do an extensive analyze of the presented information.

3.4 Validity and reliability

Both the validity and reliability concerning the qualitative part of a study need to be considered during the whole investigation, and not only when collecting data (Patel & Davidsson 2003, p. 103). This has been accounted for during the whole investigation, and may therefore be seen as a factor increasing the validity and reliability of the thesis.

One concern regarding the validity of interviews is that the respondents might not want to share information concerning themselves or their firm's process when producing analyst reports. This might make the respondents answer questions in a certain way in order to be seen in a positive light, and thus reduce the validity of the thesis (Alvesson & Sköldberg 1994, p, 129). However, one way to ensure the validity regarding interviews is to insert quotes in the text. This will show the connection between the empirical material and the research results, and allow the reader to make their own interpretations (Alvesson & Sköldberg 1994, pp. 167-168). The authors have considered this possibility to ensure the validity of the interviews, and the presentation of the findings therefore includes a mix of the authors' interpretations and quotes from the respondents.

According to Kirk and Miller (1986, pp. 41-42), triangulation generally increases the reliability of a study. Triangulation can be described as using several different methods to investigate one research problem. The technique is applied in this thesis since both interviews and an examination of analyst reports are performed. An additional factor that, according to Silverman (2001), increases the reliability of a study regarding interviews is if notes are taken when conducting the interviews. For the reliability to increase, the notes should be taken in a somewhat standardized system (Silverman 2001, p. 227). The mode in which the authors conducted the interviews is in line with Silverman's statement. Concerning the reliability of the investigation of analyst reports, the data is already available, and textual data is in general more reliable than observations. It is important that the different categories that the researcher use when analyzing the text is used in a standardized way. Hence, any researcher would categorize in the same way (Silverman 2001, p. 229). The authors considered this when creating the categories used in the investigation of analyst reports, and believe that these are suitable.

4. Empirical investigation

In the chapter the authors sort the data collected on the basis of the research questions. The composition of the chapter is divided into the main research question and the first of the two sub-questions, and with a separation of the mode in which the data was collected. The second one will be answered through analyzing the main research question and the first sub-question, and is thereby discussed in the analysis chapter.

4.1 Which income measures do analysts use and is this consistent with the changes made due to the revision of IAS 1 Presentation of Financial Statements?

The empirical findings regarding the main research question are presented below. The section starts with the results of the examination of analyst reports, followed by the respondents' discussions concerning the investigated area.

4.1.1 Data collected from analysts reports

Table 4.1 Most Frequently Used Income Measures in Running Text

Measure	No of reports 2006-2007	Frequency
EBITDA	13	17.3%
EBITDA margin	6	8.0%
EBITA	11	14.7%
EBITA margin	13	17.3%
EBIT (OI)	44	58.7%
EBIT margin	42	56.0%
EPS	39	52.0%
EPS growth	9	12.0%
Gross profit margin	15	20.0%
NI	12	16.0%

The most frequent measure used in running text is EBIT, which is included in 58.7 percent of the 75 reports regarding the period 2006-2007. Two measures also quite frequently used during this period are EBIT margin and EPS. As shown in table 4.1, these three measures significantly distinguish themselves from the others regarding the use in running text.

Table 4.2 Most Frequently Used Income Measures in Running Text		
Measure	No of reports 2010-2011	Frequency
Earnings before extraordinary items	17	22.7%
EBITDA	12	16.0%
EBITDA margin	17	22.7%
EBIT (OI)	30	40.0%
EBIT margin	22	29.3%
EBT (Pre-tax profit)	8	10.77%
EPS	36	48.0%
Gross profit	3	4.0%
Gross profit margin	20	26.7%
NI	19	25.3%

As for the period 2006-2007, EBIT is one of the most frequently used measures during the period 2010-2011. Furthermore, like the period 2006-2007, there are a few measures significantly distinguishing themselves from the others. As presented in table 4.2, the evidence suggests that EBIT and EPS are the most frequently used measures in running text.

Table 4.3 Most Frequently Used Key Ratios in Running Text				
Measure	No of reports 2006-2007	Frequency	No of reports 2010-2011	Frequency
P/E	24	32.0%	31	41.3%
ROC	2	2.7%	0	0.0%
ROCE	6	8.0%	2	2.7%
ROE	2	2.7%	19	25.3%
ROI	1	1.3%	0	0.0%
ROIC	6	8.0%	0	0.0%
ROWC	0	0.0%	3	4.0%

Since income measures are used when calculating important key ratios, and these ratios often are presented in analyst reports, the authors find the presentation of the most frequent key ratios used to be relevant for the study. As shown in table 4.3, P/E is the most frequent key ratio used in running text for both time periods. Regarding the time period 2006-2007, P/E is clearly the most frequent ratio used, and the other ratios have a frequency well below P/E. The time period 2010-2011 differs from 2006-2007 since ROE is used quite widely, giving the time period two significant used ratios in rolling text.

Table 4.4 Most Frequently Used Multiples in Running Text				
Measure	No of reports 2006-2007	Frequency	No of reports 2010-2011	Frequency
EV/EBIT	17	22.7%	8	10.7%
EV/EBITA	10	13.3%	0	0.0%
EV/EBITDA	12	16.0%	2	2.7%
Net debt/EBITDA	7	9.3%	2	2.7%

As for most frequently used key ratio, the most frequent multiple used in rolling text is the same for both time periods, EV/EBIT. As presented in table 4.4, the most frequent multiples concerning the time period 2006-2007 do not significantly distinguish themselves from each other. However, the frequency for the time period 2010-2011 shows that EV/EBIT is a significant multiple used in running text.

Table 4.5 Most Frequently Used Income Measures in Tables		
Measure	No of reports 2006-2007	Frequency
EBITDA	55	73.3%
EBITA margin	34	45.3%
EBIT (OI)	69	92.0%
EBIT margin	62	82.7%
EBT (Pre-tax profit)	64	85.3%
NI	68	90.7%
NI margin	39	52.0%
EPS	67	89.3%
Gross profit	39	52.0%
Gross profit margin	39	52.0%

Table 4.5 shows that EBIT is the most frequently used measure in tables during the time period 2006-2007. NI and NI per share (EPS) are also frequently used, as well as the measures EBIT margin and EBT. Unlike the most frequently used measures in rolling text during 2006-2007, no group of measures significantly distinguishes itself from the others. Instead, as presented in table 4.5, there is a closer frequency regarding the most frequent measures used in tables.

Table 4.6 Most Frequently Used Income Measures in Tables		
Measure	No of reports 2010-2011	Frequency
EBITDA	48	64.0%
EBITDA margin	49	65.3%
EBIT (OI)	56	74.7%
EBIT margin	43	57.3%
EBIT growth	39	52.0%
EBT (Pre-tax profit)	53	70.7%
EPS	68	90.7%
EPS growth	37	49.3%
Gross profit margin	36	48.0%
NI	69	92.0%

NI is the most frequently used measure regarding the time period 2010-2011. Although, as shown in table 4.6, NI per share (EPS) almost have the same frequency. As for the time period 2006-2007, there is a closer frequency between the most frequent measures used in tables than in rolling text.

Table 4.7 Most Frequently Used Key Ratios in Tables				
Measure	No of reports 2006-2007	Frequency	No of reports 2010-2011	Frequency
P/E	66	88.0%	66	88.0%
ROA	4	5.3%	42	56.0%
ROE	45	60.0%	61	81.3%
ROI	0	0.0%	16	21.3%
ROC	4	5.3%	0	0.0%
ROCE	39	52.0%	38	50.7%
ROFA	0	0.0%	12	16.0%
ROIC	61	81.3%	16	21.3%

P/E is used most often in tables, as well as in running text. This is the situation for both time periods, and the ratio also has the same frequency during both time periods. Furthermore, ROE almost has the same frequency as P/E during 2010-2011. Regarding the time period 2006-2007, ROIC is the second most frequently used ratio, and the frequency is close to the one of P/E.

Table 4.8 Most Frequently Used Multiples in Tables				
Measure	No of reports 2006-2007	Frequency	No of reports 2010-2011	Frequency
EV/EBIT	46	61.3%	41	54.7%
EV/EBITA	16	21.3%	7	9.3%
EV/EBITDA	51	68.0%	40	53.3%
Net debt/EBITDA	12	16.0%	23	30.7%

Opposed to the most frequently used multiple in running text during 2006-2007, which was EV/EBIT, EV/EBITDA is the most frequently used in tables for this period. However, EV/EBIT almost has the same frequency, as shown in table 4.8. EV/EBIT is the most frequently multiple in running text as well as in tables during 2010-2011. However, EV/EBITDA almost has the same frequency as EV/EBIT during 2010-2011.

4.1.2 Data collected from qualitative interviews

4.1.2.1 Clean earnings number and elimination of one-time items

Broström[4] (B) explains that analysts adjust historical earnings to come to an understanding of what the underlying earnings are, which are not affected by temporary items. Analysts want to achieve a clean earnings number in order to estimate future earnings. '*One time items are usually poor markers when predicting the future, however, this fact does not imply that analysts automatically eliminate these items'* (B). Sometimes it is of great importance that analysts use their knowledge of the firms' specific industry regarding common expenses. Broström states, for instance, that in some industries it can be of importance to possess great knowledge regarding reconstructing expenses and to what extent these kinds of expenses occur. Similarly, Gärtner[5] (G) explains that it is important to erase nonrecurring costs, such as restructuring costs, when valuing a firm. Today, analysts do not blindly believe what firms choose to call restructuring costs since this has often been systematized. *'It is often a part of the business to operate in a way that makes costs not being one-off costs even though firms want to recognize them as one-off costs'* (G). Furthermore, Gärtner states that impairment of goodwill and depreciation on other assets are overlooked in order to erase one-off costs, which are nonrecurring.

4.1.2.2 NI and EPS

Nilsson[6] (N) states that he rarely chooses which measures to use when valuing a firm. Instead this is more of a custom that is set in different industries. In the industry of telecoms equipment, which Nilsson follows, NI, sometimes by share, is a measure usually used by analysts when

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[4] Johan Broström, chairman of the Firm Valuation Group, telephone interview 8th of March 2012

[5] Robert Gärtner Equity Analyst Handelsbanken Capital Markets, telephone interview 14th of March 2012

[6] Martin Nilsson Equity Analyst Handelsbanken Capital Markets, telephone interview 13th of March 2012

producing long term forecasts. Broström also states that NI is the basis for the forecast. He explains that this measure, as well as turnover, is important with no regard to which standards are applied. Gärtner argues that it is difficult to discuss which income measures analysts use. Depending on which firm is analyzed, he explains that different income measures are of interest. Gärtner states, similarly to Nilsson, that EPS has always been an important measure, and that it still is. Furthermore, it can be of great importance to keep track of the number of shares in firms. One of the reasons for this is the fact that firms regularly buy back shares, which increases the number of shares. Comparing the share price to EPS leads to the price-to-earnings ratio (P/E). *'EPS is an important item since an increase or decrease in EPS provides an image to clients regarding the status of the firm. However, one might think that EPS is a measure of profit, which does not show the whole truth since it is located at the bottom of the income statement and thus includes items that do not reflect slow profitability'* (G).

4.1.2.3 EBITDA, EBIT and EBT

Gärtner explains that since bottom-line measures might not reflect slow profitability, focus has been shifted to measures further up in the income statement. An example of this is EBIT, which is located above net interest in the income statement. This provides a picture of how the firm is financed, not only by shareholders but also by bonds and loans. *'EBIT is the most important measure of operating profit and it gives a fair reflection of a free cash flow since the depreciations are a proxy that should reflect the need for investment'* (G). The measure is often used as frequently as EPS, regardless of interim reports or annual reports. EBIT can be put in relation to the value of the firm generating the result enterprise value (EV). Even further up in the income statement the measure EBITDA is located. Gärtner states that this level is important since it is a simple measure that has not been affected as much by accounting tricks. From a valuation point of view EV/EBITDA is comparable among firms in the same industry as well as over time. Considering this, the P/E ratio should not be rejected. However, it may be harder to refine the measure.

Malmqvist[7] (M) states that there are two time perspectives considered in analysts' work. The first part of analysts' work is to produce long term forecasts regarding the firms followed. Important measures in this area are OI, and often OI before depreciation, which often is referred to as EBIT. EBITDA is also an important measure, and is in general of greater importance than EBIT in long term forecasts. This differs from Nilsson, who stated above that NI, sometimes by share, is the basis for long term forecasts in his industry. Malmqvist explains that the second part of analysts' work is to be able to answer if the quarterly reports presented are in line with what was expected, and if these reports will change the long term assumptions. Furthermore, Malmqvist states that earnings before taxes (EBT) is the most important measure regarding this area. *'EBT is compared to gathered analysts' forecasts in order to receive an analyst average, which in many*

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[7] Peter Malmqvist, chairman of the Swedish Society of Financial Analysts, telephone interview 9th of March 2012

cases directs share price reactions in quarterly reports' (M). Furthermore, this indicates what the market expects of a firm. Analysts within Nilsson's industry primarily use EBIT to come to an understanding if the firms performance is better or worse, regarding follow up on quarterly reports. Nilsson states that approximately eight years ago analysts never considered EBIT or EBITDA, but instead NI was of greater importance. There is significant focus on the qualitative, what can be expressed as the firm's NI. Another important question is whether or not it should be more or less expensive and if the firm has good cash conversion. In general group profit after taxes or EBITDA at a basic level is the foundation. Broström states that EBIT is a good measure if there is transparency in the business model of the firm. For instance, if the judgment can be made that depreciation gives good guidance regarding what the investments are supposed to be. However, if depreciation is just a number that reflects the historical number, it is not favourable to use EBIT. *'If depreciation is a good prediction of what future investments should be I prefer to use EBIT, otherwise I use EBITDA'* (B).

4.1.2.4 CI

Malmqvist finds that CI is a relevant measure when valuing a firm. He explains that the three CI-posts effective portion of gains and losses on hedging instruments in a cash flow hedge, defined benefit plans and available-for-sale assets are usually important for analysts. Furthermore, Malmqvist states that translation differences of foreign firms is not important, and explains that this post has been a part of accounting since the beginning of the eighties but that he has not yet seen any analysis that comments on it. Malmqvist believes that the fact that no analysts comment this post should be proof that it does not have any effect on the share price. The post assets available for sale is the least important of the three posts remaining since the amounts are small and few firms present it. That leaves two posts: defined benefit plans and hedges in cash flows. Malmqvist explains that approximately 15 firms, out of the 200 firms he follows present defined benefit plans. This post is of great importance within these firms since it represents large amounts. Analysts' work regarding this post is to follow the value fluctuations of pension costs. *'As long as the fluctuation is around zero in the long run, there are no systematic errors in the calculation'* (M). Malmqvist states that the post hedging instruments in a cash flow hedge is extremely important in all time perspectives, but primarily in short term forecasts. The post consists of two parts, the first of which presents the fluctuation that arose during the period on the financial instrument. In general this fluctuation depends on the instrument usually being related to the dollar exchange rate or the euro exchange rate. The second part reflects the value of the cash flow hedge when it is mature and realized. The realized amount is eliminated from CI and is instead presented within OI in the income statement as a financial short term gain or loss. Malmqvist argues that it is important for analysts to achieve knowledge of the amount related to the hedge in cash flows that has affected the earnings after being transferred to the income statement.

Gärtner states that most analysts, including himself, generally consider OCI to be positive since it clears out factors that do not have anything to do with the underlying value of the income statement. *'My experience is that because analysts are basically interested in net profit, they hardly consider CI at all unless any extraordinary events occur. If this is the case, it could be of use to investigate the different OCI-posts'* (G). Gärtner believes that it is positive that these posts are located in OCI instead of being spread out in the income statement where analysts had to clear out the posts themselves. He states that the greatest advantage of presenting CI is that it results in a more refined profit. Broström explains that his process when producing a forecast consists of several steps. The first step is to receive a comprehensive picture of the situation followed by the second step, which is to establish a model. The third and final step is to come to an understanding of the details. The additional information presented in CI is included in the third step. Broström does not usually turn to the information presented in CI in order to comprehend what is necessary regarding the firms' situation. However, he can imagine that there may be industries that consider CI more than others. Nilsson states, in line with Broström, that he does not use CI much himself, but says that he cannot speak for all sectors. However, CI is not used that often in Nilsson's industry. *'Analysts within my industry are simple in that way, it is the sector that sets the standard for what analysts look for'* (N).

4.2 Has analysts' use of income measures been affected by the adoption of the revised IAS 1?

This section presents the answers to the first sub-question, and is divided into collected data from analyst reports respectively interviews.

4.2.1 Data collected from analyst reports

Table 4.9 OCI Components Used in Running Text

CI total/OCI components	No of reports 2006-2007	Frequency	No of reports 2010-2011	Frequency
Translation of a foreign operation	2	2.7%	3	4.0%
Gains & losses hedging instruments	0	0.0%	1	1.3%
Changes in revaluation surplus	1	1.3%	0	0.0%
CI	0	0.0%	1	1.3%

Three of the OCI components, as shown in table 4.9, are used in running text in a few reports during 2010-2011. Furthermore, the measure CI is used in one of the 150 reports included in the investigation. Even though the extent to which CI is used is small, there is a change in comparison to the time period 2006-2007. In terms of OCI components or CI in tables, there are no reports for either of the time periods that include the measure.

When considering the tables 4.1 and 4.2, NI is used more frequently in running text during 2010-2011 than 2006-2007, which is a measure considering almost all income areas. Furthermore, the use of EBIT and EBIT margin in running text has decreased during the time period 2010-2011, and measures such as NI before extraordinary items, EBITDA margin and EBT are used more frequently than 2006-2007. According to the evidence presented in the tables 4.5 and 4.6, NI and EPS approximately have the same frequency for both time periods. NI margin and gross profit are two of the ten most frequently used measures in tables during 2006-2007, whereas this is not the situation during 2010-2011. Instead the measures EBITDA margin and EPS growth are included during 2010-2011, which are not considered during 2006-2007. Furthermore, the use of EBITA margin, EBIT and EBIT margin during 2010-2011, in comparison to 2006-2007, has decreased significantly.

4.2.2 Data collected from qualitative interviews

4.2.2.1 Effects of the revision of IAS 1 on analysts' work and discussion regarding the IASB

All respondents state that analysts are a pragmatic group of people. Therefore, changes in accounting standards do not in a significant way change the mode in which analysts create their forecasts.

Malmqvist believes that the revision of IAS is a positive change. The received information has improved regarding hedges in cash flows and defined benefit plans. As mentioned above, Malmqvist finds these changes to be the most important. In addition to this, Malmqvist believes that the IASB are trying to take all users of financial statements into consideration when developing accounting standards. However, this is a difficult task since the users are not a homogeneous group. Furthermore, Malmqvist argues that the IASB are not understanding concerning the fact that analysts need to formulate an opinion rapidly regarding a firm's performance. He explains that the IASB is extremely focused on the annual report and presenting additional information, unlike analysts who usually work with quarterly reports and have a quarterly perspective. The additional information sometimes makes it harder for analysts to grasp the most relevant information. Furthermore, Malmqvist states that the IASB does not receive many answers from analysts regarding amendments to standards. However, the answers they do receive are not preferred. Malmqvist concludes the discussion by saying that the IASB listens to the users, but that the central question is who they are. Broström believes that accounting is and always will be a compromise. He does not think that it is possible to come to a solution regarding the composition of accounting standards that suit everyone. The possible solution, according to Broström, is to find the lowest common denominator that is good for everyone and not too complicated. Broström explains that there is a requirement of speed when a firm releases its report. *'The main part of the movement in share price occurs during the first minutes or hours after the report is released. If it is too complicated to interpret the earnings, it will result in extra time being put into the work and a higher uncertainty'* (B). Broström believes that there should be a balance between simplicity and completeness. This is difficult for the standard setters to achieve since there are different groups of users of financial statements with different demands. Furthermore, Broström explains that there are two types of analyst: those that work fast and present their reports quickly and those who need more time before presenting their reports. Broström is included in the group who takes more time and usually wants to receive more information. He believes that the more information, the better and has no objections regarding more information being presented in the income statement. However, economy journalists, for instance, have a difficult task since they have to come up with fast information for a whole population. If the information presented according to the accounting standards is too complicated to interpret, it can complicate their work. Broström has not been affected by the revision of IAS 1 and his work process has not changed besides that he more easily can find information. As mentioned before, Broström uses CI in the third step when producing analyses.

Nilsson explains that he follows the process of amendments to standards reactively. In general analysts have foundations in their databases and when changes are adopted, the databases are updated. *'The regulation regarding pensions is currently of interest and analysts wonder if there are going to be changes in this standard since these would affect earnings as well as the net debt measures. Furthermore analysts are still wondering what is affecting firms' net debt and NI on group level'* (N). In addition to this, Nilsson states that analysts are not focused on accounting concerns in a great extent. He believes that analysts and the IASB are leading different lives and that analysts' role is to accept the standards and the structure handed to them by the IASB. Nilsson only uses CI when investigating reclassification of currency hedges. *'All large exporting firms have currency hedges, and when the currencies move in the opposite direction of their forward covers, the hedges fluctuate'* (N). This is almost solely what he uses CI for. Nilsson also explains that he investigates cash flows in a great extent, but only by using the ordinary cash flow statement.

Gärtner believes that it is still early for analysts to evaluate if CI is useful. However, he finds CI to be useful in situations where extraordinary events have occurred, as described above. Gärtner considers the joint project between the IASB and FASB to be positive and the basic idea to be attractive, although he believes that some aspects are unnecessarily complicated. He states that the IASB wants to develop accounting standards that satisfy the demands of analysts and investors. However, he explains that when ED's are published, the IASB receive very few answers from analysts. Gärtner believes, in line with Nilsson, that this is a result from analysts only being a group that accepts the accounting and not a group that wants to affect the accounting. He explains that this has to do with the fact that analysts are good at sorting out relevant information from the financial statements. Gärtners opinion is that changes often are made that sometimes take a long time and lead to more complicated accounting. For instance, the information in notes has increased incredibly, which results in more information having to be processed. Sometimes he finds changes to be on such a detailed level that analysts do not find it useful. Most analysts feel that someone needs to put their foot down since the changes are not primarily made for analysts but seems to be a greater satisfaction to auditors and unaware investors. Analysts have a good understanding regardless. However, the fact that changes are made often is not entirely negative for analysts: it might create business opportunities for analysts to help people understand.

4.2.2.2 Improvements of IAS 1

An improvement Malmqvist wants to see regarding IAS 1 is a consistent presentation throughout all financial reports. An example of this is that quarterly reports distinguish value fluctuations in CI from what has been realized and thereby transferred to the operating result in the income statement. Malmqvist believes that one line for value fluctuations in CI and one line for the transferred amount should be presented. He states that this information needs to be separated, otherwise analysts can not use the information. Broström states, in line with Malmqvist, that he wants to have a main thread throughout all financial reporting. He believes that both quarterly and annual reports should contain the same information. *'IR-departments should value their firms the same way analysts do in order to achieve the information that analysts want. This information should be presented on the first page of the financial reports'* (B). Nilsson believes that IAS 1 needs to be improved differently depending on which industry that is being analyzed. He states that analysts are interested in details regarding different business measures and that they try to understand the quality of the reported earnings. The latter is the most difficult part. Gärtner expresses that he believes that more posts should be incorporated in CI. He states that unrealized changes in value should not be included in the income statement since it does not have anything to do with the firms' long term growth in profit nor their endurance.

4.2.2.3 Preference of single statement of CI or two-statement approach

Malmqvist wants to have a clear separation between NI and OCI. He is not interested in NI being presented together with OCI. The reason is that the components of OCI in almost all cases consist of value fluctuations. *'This result is of a totally different character, than the situation when we receive the result from transaction based accounting'* (M). Broström finds it helpful and easier if the income statement is divided in two parts with CI in the end. Usually there are posts that Broström wants to treat separately under all circumstances. Gärtner states that analysts absolutely not have any preferences regarding the single- or two-statement approach. Both approaches provide the exact same information. The most important for analysts is to obtain an understanding and explanation for growth in profit, changes in equity and changes in net debt.

5. Analysis

The analysis chapter's composition is based on all the research questions. Furthermore, the information presented in the chapters frame of reference and empirical investigation was compared and analyzed, leading to the conclusion in chapter six.

5.1 Which income measures do analysts use and is this consistent with the changes made due to the revision of IAS 1 Presentation of Financial Statements?

The statements given by the respondents to the interviews, regarding which income measures analysts use, are found to be similar to the findings from the investigation of analyst reports. Generally, all the measures mentioned in the interviews are in greater or less extent also incorporated in the analyst reports. This applies to, for instance, EBIT, EPS and NI, which are included in the group of the most frequently used measures in running text and tables for both time periods. These measures were also stated by the respondents to be important. Malmqvist mentioned that EBIT is an important measure when producing long term forecasts. Gärtner stated that EBIT is the most important measure of operating profit and that the measure is relevant since it is placed further up in the income statement and thereby consists of core items. This statement is in line with Petersen and Plenborg (2012), who argue that EBIT is an important measure since it reflects the results of the firms' core business (Petersen & Plenborg 2012, p. 73). According to Barton, Hansen & Pownall (2010), measures located near the middle of the income statement, such as OI, are more strongly connected with stock returns than subtotals at the top or bottom of the income statement (Barton, Hansen & Pownall 2010, p. 754). Furthermore, Nilsson explained that he uses EBIT when following up on quarterly reports, and he also finds the measure especially important if depreciation is a good prediction of what future investments should be. The fact that all of the respondents follow different industries, which automatically may lead to a focus on different measures, might explain the differences in the use of EBIT. Some of the respondents also pointed this out.

Regarding key ratios and multiples, Gärtner discussed both P/E and EV/EBITDA during the interview, and stated that these were relevant. He explained that EV/EBITDA is an important multiple since it is comparable among firms in the same industry as well as over time. This is in line with the study of analyst reports, which proved this ratio and multiple to be used by analysts. NI as well as NI per share (EPS) were also measures of interest in both the analyst report study and when conducting the interviews. Gärtner mentioned that EPS has always been an important measure and that it provides an image to clients regarding the status of the firm. Nilsson stated that he uses NI, sometimes per share, when producing long term forecasts and Broström explained that NI is the basis for the forecast.

The results from the investigation of analyst reports showed that the components of OCI are used a few times in running text during 2010-2011, and that the measure CI is only used in one report of the 150 reports. Hence, CI is not frequently used in text or tables compared to other measures. These findings are in line with statements made by most of the respondents, who expressed that CI either is not used at all or in a small extent when specific circumstances exist. Gärtner stated that most analysts hardly consider CI at all, unless extraordinary events have occurred. Broström explained that he does not usually turn to the information presented in CI in order to comprehend what is necessary regarding the firms' situation. However, the interpretation made from the interviews was that all of the respondents might turn to CI in special situations or when more detailed information is required. Furthermore, some of the analysts stated that the different OCI components might bring additional useful information. Nilsson explained that he uses CI when investigating reclassification of currency hedges, and Malmqvist stated that the three OCI components effective portion of gains and losses on hedging instruments in a cash flow hedge, defined benefit plans, and available-for-sale assets are usually important for analysts. The findings of the interviews correlate with previous research, such as the studies made by Cheng *et al*. (1993) as well as Dhaliwal *et al*. (1999), which conclude that CI is a less relevant measure when valuing a firm and making forecasts. Furthermore, the results are in line with for instance Smith and Reither (1996) and Kubota *et al*. (2009), who state that some of the OCI components bring useful information and that the new presentation is more easily available and simple to understand.

5.2 Has analysts' use of income measures been affected by the adoption of the revised IAS 1?

Based on the outcome of the investigation of analyst reports, some shift in the use of income measures between the time periods 2006-2007 and 2010-2011 can be seen. Regarding the most frequent measures in running text, the same measures are in focus, besides the use of EBIT margin, which has decreased in 2010-2011. NI and EPS have approximately the same frequency in tables over the time periods, which may indicate that these measures will continue to be important over time regardless of changes in accounting standards. An even greater focus on EPS is indicated during 2010-2011 since EPS growth during this period has taken a place in the top ten over most frequently used measures in tables. This is in line with Petersen and Plenborg (2012), who state that EPS and EPS growth often is used by analysts and that the measure sometimes is considered to be perfect (Petersen & Plenborg 2012, pp. 140-141). EBT and EBITDA margin are measures, whose frequencies have increased during 2010-2011. Malmqvist expressed that he uses EBT when forming an opinion about whether the quarterly reports presented are in line with what was expected. Furthermore, if the reports will change the long term assumptions. Peterson and Plenborg (2012) state, in accordance with the investigation of analyst reports, that EBITDA is a measure that have become of great interest when valuing firms in recent years (Petersen & Plenborg 2012, pp. 58-59). EBITA is also included in this discussion.

This is, however, not in line with the findings of the analyst report study, which showed that the use of EBITA and EBITA margin have decreased significantly during 2010-2011. The results from the interviews showed, like the investigation of analyst reports, that EBITDA is a relevant measure. Malmqvist stated that EBITDA is the most important measure regarding long term forecasts and Broström explained that he uses EBITDA instead of EBIT if depreciation is only a number that reflects the historical number. Gärtner explained that the measure is important since it has not been affected as much by accounting tricks. This statement is in line with the discussion made by Petersen and Plenborg (2012), who stated that by eliminating depreciation, amortization and tax, the firms' different depreciation policies and estimates regarding deferred tax do not affect the measures (Petersen & Plenborg ibid). Regarding key ratios and multiples, generally the same measures are in focus during both time periods. The use of the P/E ratio is consistent in running text as well as tables in both periods. This correlates with the discussion held by Petersen and Plenborg (2012), who argued that P/E is one of the most popular multiples estimating equity value (Petersen & Plenborg, pp. 226-227).

CI is not a measure that is frequently mentioned in any of the investigated time periods. CI as a measure is only used in one report out of the 150 that the authors have examined. Even though some components of OCI are discussed in a few reports, these components are mentioned in a much less extent than the most frequent measures. These findings are consistent with the results from the interviews, which showed that the revision of IAS 1 has not had any significant effect on analysts' work. Most of the respondents stated that they, when valuing a firm, do not use CI in a greater extent now than before the revision. Broström stated that he has not been affected by the revision of IAS 1, and that his work process has not changed besides that he more easily can find information. Based on the discussion made in the interviews, the authors find Malmqvist and Gärtner to be the most positive concerning the revision of IAS 1. Malmqvist expressed that the received information regarding hedges in cash flows and defined benefit plans had improved since the revision. Furthermore, Malmqvist had a clear understanding of that CI is relevant when valuing a firm and presented detailed explanations to why some of the components of OCI were more important than others. Gärtner stated that most analysts, including himself, generally consider OCI to be positive since it clears out factors that does not have anything to do with the underlying value of the income statement. He showed a positive attitude regarding the fact that the OCI-posts are located in OCI instead of being spread out in the income statement where analysts had to clear out the posts themselves. Furthermore, he explained that the greatest advantage of presenting CI is that it results in a more refined profit.

5.3 Is the IASB's motivation regarding the revision of IAS 1 in line with analysts' demand?

According to the IASB's framework, the primary users of financial statements are investors. This also includes analysts since these have the purpose of assisting investors in their decision making process (Framework IASB, pt. 9a & 10). The data received during the interviews and investigation of analyst reports along with the frame of reference, answers the previous research questions. The answers to these questions also make a statement on the final research question concerning whether or not the IASB issues standards that are in line with what analysts, i.e. primary users of financial statements, demand.

The IASB's goal is to assist management in enhancing the communication of financial information to the users of financial statements, and to help users in their decision-making process (IFRS 2011). The purpose of the amendments to IAS 1 was to enhance the information given in the financial statements in order to increase users' capacity to analyze and compare financial information (IASB 2007, p. 1). The proposed changes to IAS 1 regarding the presentation of CI in the income statement, presented in the ED (2006), were seen by the respondents as an improvement in financial reporting followed by increased transparency. However, questions concerning the absence of definitions regarding the terms 'owner' and 'non-owner' in the ED, the Framework and the standards were raised. The fact that the board decided to acquire the term 'owner' for further use in IAS 1, consistent with SFAS 130 (IASB 2009, BC38), may be seen as an attempt from the IASB to meet the users demands.

Gärtner discussed the joint project between the IASB and FASB in order to generally answer the question whether the revisions of standards are made in line with what analysts demand. He came to the conclusion that the overall project is positive, although certain aspects of it tend to be too complicated. He stated that the IASB wants to develop accounting standards that satisfy the demands of analysts and investors. However, Gärtner explained that changes might not be made primarily for analysts but for auditors and unaware investors, since analysts have a good understanding regardless of the recent changes. Nilsson believes that analysts and the IASB are leading different lives, and that analysts' role is to accept the standards and the structure handed to them by the IASB. Furthermore, he stated that he follows the process of amendments to standards reactively. An interpretation that can be made based on this statement is that he does not actively try to impact the standard setters in order to try and bring changes to standards that are desired by analysts. This interpretation is supported by Gärtner who stated that when ED's are published, the IASB receive very few answers from analysts. He continued to explain that analysts only are a group that accepts the accounting and not a group who wants to affect the accounting. Malmqvist made a similar statement and explained that the IASB does not receive many comments from analysts regarding amendments to standards. Furthermore, Malmqvist believes that the IASB tries to listen to all users of financial statements and take their interests into consideration. However, this is a difficult task since the users are not a homogeneous group. Broström explained, similar to Malmqvist, that he believes that it is not possible to create accounting standards that are suitable for everyone. Since there are a great amount of different users of financial statements, with different demands, the solution is to come to an agreement that can be accepted by everyone and that is not too complicated. Furthermore, Broström explained that, because of this, the balance of simplicity and completeness is difficult to achieve.

The respondents also expressed desired improvements regarding IAS 1. Malmqvist stated that he wants to see a consistent presentation throughout all financial reports. A similar statement was made by Broström who expressed that he wants to have a consistent focus throughout all financial reporting. He believes that both quarterly and annual reports should contain the same information. Furthermore, Nilsson stated that IAS 1 needs to be improved differently depending on which industry that is being analyzed. At last Gärtner thinks that more posts should be incorporated in CI. The reason for this is his beliefs that unrealized changes in value should not be included in the income statement since it does not have anything to do with the firms' long term growth in profit, nor their endurance. The answers received from the respondents show that there are still aspects of IAS 1 that needs to be improved from an analyst's point of view. This indicates that the IASB still have some amendments to make if the standard should be fully in line with what analysts demand. However, one might question if this is possible since analysts, based on the interviews, seem to have a wide variety of demands.

Studies that discuss the usefulness of IFRS and the IASB's ability to issue standards according to the users' demands are analyzed below. Marton (2010) states that global accounting standards are necessary in a world with global capital markets. The author also responses to the critique from Strid and Pilebjer-Bosson (2010) regarding the view that the IASB make changes to accounting standards where no different solution is asked for or needed. He argues that the IASB have clear motivations when proposing amendments to accounting standards (Marton 2010). Furthermore, more than half of the respondents to the study made by Dilks (2007) do not find the financial information provided by IFRS to be useful. However, Dilks states that time has made financial executives become more positive regarding IFRS (Dilks 2007, p. 83). The discussions carried out by Marton (2010) and Dilks (2007) are generally in line with what the respondents to the interviews stated concerning the IASB's ability to issue standards that are of use for all users. Hence, that it is a difficult task to issue standards that are perfectly suitable for all users.

Most of the respondents to the ED (2006) preferred the two-statement option since it separates profit or loss from total CI (IASB 2009, BC50). This may indicate that the users of financial statements tend to focus on measures like NI, which is a part of the original income statement. Hällefors (2006) states that a general argument against a single statement format seems to be that many users of the financial statements tend to focus on the bottom line in the income statement and that OCI does not constitute relevant information for the users of financial statement, but instead confuses them (Hällefors 2006). Furthermore, Goncharov and Hodgson (2011) state that presenting OCI together with NI in a single statement results in deteriorated usefulness. Thinggaard *et al.* (2006) found support for a single statement format, however, the study also found NI on average to be more relevant than CI and may therefore support a two-statement approach (Thinggaard *et al*. 2006, p. 35). The results of the study are quite mixed but more in line with a single statement format. Furthermore, the study does not support the IASB's preference for a single statement format since the authors find some merit in the option for presentation format (Thinggaard *et al*. 2006, p. 60). Most of the respondents to the interviews prefer the two-statement approach or do not have any preferences at all, which is in line with the evidence from the empirical investigation regarding analysts' use of income measures. Hence, CI is hardly used at all by analysts, and may therefore be the reason for the situation when analysts prefer the two-statement approach. The general opinion regarding the two approaches, considering the information from the frame of reference and empirical investigation, seems to be that the two-statement approach is prefered by most users.

6. Conclusions

This chapter consists of the conclusions of the study, which, as mentioned in the previous chapter, were created by analyzing and interpreting the data collected with support of the frame of reference. Furthermore, the research questions are answered and the composition of the chapter is therefore based on all the research questions. Finally, suggestions for further research are presented.

The purpose of this thesis was twofold: first to come to an understanding of which income measures analysts use and if this is consistent with IAS 1; second to assess whether the IASB's view on what is needed to achieve enhanced usefulness of the financial statements is in line with what analysts use and demand. The purpose is fulfilled by answering the research questions below.

6.1 Which income measures do analysts use and is this consistent with the changes made due to the revision of IAS 1 Presentation of Financial Statements?

The investigation of analyst reports showed that the measures EBIT, EPS and NI are included in the group of the most frequently used measures in both running text and tables, for both time periods. All of these measures were also discussed and stated to be important during the interviews. The situation is the same regarding the ratio P/E as well as the multiple EV/EBITDA, who were proved to be used by analysts through the report study and discussed during, for instance, Gärtners interview. The investigation of analyst reports showed that CI as a measure was only used in one report of the 150 reports examined. Some components of OCI were used in reports, however, in a much less extent than the most frequent measures. These findings are in line with the respondents, who stated that CI either is not used at all or in small extent. However, some respondents argued that the individual OCI components might bring additional useful information. Especially in situations when extraordinary events have occurred. The findings from the investigation of analyst reports and the interviews are in line with most previous research which states that CI is less relevant as a measure but that the OCI-components might bring additional useful information. Overall, the conclusion to be drawn from the empirical investigation is that CI as well as the components of OCI are used in a less extent than other measures. An indication may be that analysts' use of income measures is not consistent with the changes made due to the revision of IAS 1.

6.2 Has analysts' use of income measures been affected by the adoption of the revised IAS 1?

The examination of analyst reports provided evidence that the same measures, besides EBIT margin, are in focus in running text during 2006-2007 as well as 2010-2011. The measures NI and EPS have approximately the same frequency in tables over the time periods. Furthermore, the report study indicated an even greater focus on EPS during 2010-2011 since EPS growth had increased significantly and taken a place in the top ten over most frequently used measures in tables. EBT and EBITDA margin are also measures who increased in use during 2010-2011. Regarding key ratios and multiples, generally the same measures are in focus over the time periods. A consistent use of the P/E ratio in both running text and tables was observed. The investigation of analyst reports indicated that the use of CI has not increased significantly since the revision of IAS 1. Furthermore, it is not a measure that is mentioned frequently in any of the time periods. This is in line with the results from the interviews which showed that the revision of IAS 1 has not had any significant effect on analysts' work and their use of CI.

The final conclusion to be drawn regarding the question if analysts' focus on income measures has changed after the revision of IAS 1 is that a minor change can be seen. The changed focus on measures besides CI might not, however, depend on the revision of IAS 1, but on a general change in trends regarding analysts' work and use of income measures. Furthermore, an increased use of CI can not be detected. However, the extended use of measures like NI and EPS in analyst reports might indicate that focus has shifted to measures further down the income statement. This indication contradicts previous research, as well as some of the respondents, where statements were made that focus has shifted up the income statement since these measures include core items. The change in focus, according to the evidence from the examination of analyst reports, possibly indicates that CI, which is positioned at the bottom of the income statement, may be of greater importance in the future.

6.3 Is the IASB's motivation regarding the revision of IAS 1 in line with analysts' demand?

The goal of the IASB is to develop and enhance accounting standards with the interest of the primary users of financial statements, i.e. investors and analysts, in mind. All respondents stated that it is not possible for the IASB to create accounting standards that are suitable for everyone. Since analysts use various information in their daily work, a great amount of different demands exist. Broström stated that the best solution would be to find the lowest common denominator that is good for everyone and not too complicated. However, this balance might be difficult to achieve. Furthermore, all analysts had suggestions regarding how IAS 1 can be improved. An important aspect of the problem might be that most analysts do not present these suggestions to the IASB or make responses to ED's, which some respondents stated to be the case. If this is the case, the task for the IASB to satisfy the demands of analysts becomes even more difficult. Malmqvist also stated, in addition to the statement that the IASB do not receive many comments from analysts regarding amendments to standards, that when the IASB do receive answers these are not preferred. This needs to be taken into consideration in the process of fulfilling the IASB's purpose and satisfying the demands of the primary users.

The fact that the use of CI in analyst reports have not increased since the revision of IAS 1 might indicate that analysts do not find the new presentation to be useful. However, the interpretation made from the interviews was that all analysts might turn to CI in extraordinary situations or when more detailed information regarding a firm is required. This indicates that CI is used, although, in a way that might not be seen in analyst reports. Since the investigation of analyst reports provided evidence that analysts hardly use CI at all when creating their forecasts, and the fact that most of the analysts interviewed do not use CI in a great extent, it may indicate that the IASB's motivation regarding the revision of IAS 1 do not correlate with analysts' demands. However, analysts do not seem to be disturbed by the presentation of CI in their daily work. Instead, it seems that CI may be of use in special situations.

6.4 Suggestion for further research

When conducting the study, the authors became aware of the fact that it would be of interest to further investigate the IASB's process when issuing standards. Since the primary users of the financial statements, according to the IASB, are in focus when the board issues a new standard or a revision of a standard, it may be of importance to further investigate whether or not the IASB succeeds in meeting the primary users' demands. Hence, try to come to an understanding whether or not the IASB issues standards that are of use for the primary users, or if the case is that the board issues standards that may be more in line with their own interests. The reason for this suggestion is that the authors, during the study and when analyzing the findings from the empirical investigation, found a gap between what the IASB consider relevant to present in the financial statements and what analysts, included in the group of primary users, find relevant.

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Appendices

Appendix 1 - Interview questions

- **Background**

  - How many years have you worked as a financial analyst and can you please tell us a little bit about your background?

  - How many firms do you follow at the moment and in which industry are these firms operating? (Title of employment? Sell-side analyst or buy-side analyst? Equity analyst.)

  -Describe the background regarding analysts' work and the aspects that is a part of their job. What general types of analysts are there? The comments we have heard generally divides fast analysts from slower analysts (equity analysts/fixed income analysts). What is your opinion regarding this? (The questions were asked to all respondents but Broström)

- **Income measures**

  - In what way do you use the income measures presented in the income statement according to IAS 1? (Adjust them, use them for multiplying with other factors or calculating other financial ratios)

  - What are the primary income measures that you use when valuing a firm, for example EBIT, EBITDA, others?

  - Do you consider CI a relevant measure when valuing a firm?
    - ■Do you use this measure as a basis or as additional information?

- **IAS 1 Presentation of financial statements**
  - What are your thoughts on the changes made due to the revision of IAS 1 when CI became mandatory to present in the income statement, adopted in 2009?
    - ■Do you believe that this was a step in the right direction towards achieving enhanced usefulness of the financial statements?
    - ■Has this affected your work in any way and do you in general believe that this has affected analysts work?
    - ■Have your use of income measures changed after the revision of IAS 1, adopted in 2009? Maybe focus on other measures etc?

■Which of the two choices firms have of presenting CI, given by the IASB, do you prefer and why? Single income statement or two-statement approach?

- In what way do you believe that IAS 1 needs to be improved, is there some information that you are missing in the financial statements that has not been adopted or discussed to be adopted?

- **IASB and IAS 1 in general**

  - What are your thoughts on the IASB's and FASB's joint project Financial Statement Presentation?

    ■Do you believe that this is a step in the right direction towards enhancing the usefulness of the financial statements and convergence of international standards?

    ■**What are your thoughts on the changes to come in phase B?** Regarding the suggestion of a new structure of the financial statements, for example the suggestion that the balance sheet will be replaced with a new balance sheet that is bases on net accounting, separating debts and assets that are considered to be of operating and financing characteristics ?

    ■What are your thoughts on the definition of “financing” that is a key question for the IASB in the changes to be made in phase B? It has been argued by analysts for example that they should adopt the commonly used definition by firms and analysts; “net debt” (separates operating and financing debts and assets). IASB does not want to put “financing”=net debt.

- Do you believe that the IASB issues standards that are in line with what the primary users of financial statements demand (analysts and investors)? Do they, according to you, understand how analysts use the accounting information?

- **Earnings management**

  - Are operating measures overstated as a result of the different ways that managers can manage earnings? (The question was asked to Nilsson and Gärtner)

- **Other**

  - Is there something else that you think is important to consider regarding income reporting according to IAS 1 or analysts' use of income measures that we have not discussed?