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# Earnings Quality and Firm Performance: Exploring the Moderating Role Managerial Ability

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**Abstract – This study modifies the relationship between company performance and earnings quality using managerial ability. 50 South Asian manufacturing corporations' secondary data from 2014–2021.The study found that managerial ability boosts firm performance. Lower-performing firms also have lower earnings quality regression coefficients on cash flows than higher-performing firms.These findings show that low-performing companies are more likely than high-performing ones to boost earnings (i.e. increase their efforts to manage earnings). Managerial ability also boosts firms' performance's impact on earnings quality.**

**Keywords – Firms Performance, Earnings Quality, Managerial Ability, Cash Flow, Corporation.**

## I. Introduction

Managers manipulating a company's earnings using accounting methods and techniques is known as "equity management" (Le et al., 2022). Many researchers, including Duan et al., (2022), have shown that the quality of earnings and the level of trustworthiness of financial reports are both harmed by the self-interested modification of earnings, according to Kliestik, (2021). This is because managers' inaccuracies in reporting earnings influence key stakeholders' investment and lending decisions inside and outside the organisation.

In recent years, the adverse effects of earnings management have been highlighted numerous times. According to Valaskova, K. et al. (2021), the 2001 Enron bankruptcy and the 2002 Xerox and WorldCom scandals, for example, were both the result of improper earnings management. In light of these scandals, it is essential to recognise that the perceived credibility of financial reporting was significantly reduced due to the highly consequential effect of earnings management practices on the organisation's operations. The SEC's investigation into the WorldCom and Enron cases helped raise global awareness of earnings management.

They are broadly arguing that managers are more capable of adapting their organisations to fluctuating conditions and innovating to ensure the enterprises' long-term survival (Gur et al., 2021). It is reasonable to say that one of the most critical factors affecting a company's worth is the management team's skills. Sophisticated human resources are more critical than ever in emerging-market contexts because of their limited resources. To gain a competitive edge and achieve long-term success in the market, companies can increase productivity by using highly trained employees. According to Durana, P., et al. (2022), human capital is the key to long-term success, especially in emerging markets.

With the support of their professional and academic expertise, competent managers make the most effective use of a company's limited resources in challenging environments. Furthermore, they put their knowledge and expertise to work to achieve long-term success. Optimal resource utilisation directly results from the manager's personality qualities and abilities. Emotional intelligence, for example, is a personality feature that helps an individual understand and manage their own and other people's emotions and uses this information to solve problems. Company managers with vital emotional intelligence and cognitive abilities tend to do better than their competitors, according to Kim (2020).

Intangible resources, such as management skills, are well-documented in the existing literature as a critical component of human capital. Before the vital work of P. Demerjian et al., (2012), quantifying management efficiency was a complex undertaking because of managerial qualities that are both visible (such as education and experience) and invisible (such as emotional intelligence and cognitive ability). Using P. Demerjian et al. (2012) methodology, a firm's managerial skills may be accurately measured. This is a more complete and easy-to-understand model based on the company's financial statements. It's also feasible to compare the managerial abilities of the competitors using this methodology. As evidenced by the current decade's empirical research, this model has grown in popularity and is now commonly employed to assess management skills (Kliestik, 2021).

Managers play a critical part in the company's numerous milestones because of their keen understanding. Effective and timely decision-making is critical for the efficient use of company resources and the successful exploitation of new opportunities (Bertrand & Schoar, 2003). According to Valaskova, K., et al. (2021), managers with more ability increase the actual performance of organisations by making the best use of the existing resources. Capable managers' efficient internal control systems prevent the waste of cash reserves (Lee., 2015; Siao & Chou, 2013). In addition, during the growth phase, businesses can benefit from new, lucrative investment opportunities made possible by lower-cost debt and equity financing made possible by improved risk management by qualified managers. These findings suggest that management is able to accurately predict consumer demand, choose value-adding activities, and manage the company's resources thanks to its deep knowledge of the sector and technological advances that drive them. Researchers and practitioners in the fields of economics and management science would do well to consider the correlation between competent leadership and bottom-line success. To explain, consider the following.

The functioning of businesses and the achievements of their markets are well-documented in both the developed and the developing nations. The costs and benefits of competent management have been the subject of few studies, however, especially in the context of emerging markets. Recent studies have shown that an organization's success is heavily dependent on the quality of its management. According to these experts, this link is further enhanced by management's local expertise and the setting in which decisions are made autonomously. However, a literature review shows that the link between management competence and business performance in the South Asian area, particularly in South Asian countries, is relatively understudied. This study intends to investigate the moderating role of managerial skills in company performance in the South Asian country setting.

Managerial skills may be examined in a particular context in South Asian countries. First and foremost, being the world's fifth-most populous country, South Asian countries have a shortage of highly skilled workers due to the region's high proportion of young people. Human resource development has been identified by a corporate board member of a publicly traded corporation as the region's most pressing issue (Masud, 2019). Second, a recent OECD poll found that South Asian countries had the lowest proportion of well-educated and well-trained adults of any nation studied so far. Competitive industries face bleak prospects in the foreseeable future due to a lack of appealing possibilities for local workers and a significant brain drain. The flawed legal system (La Porta et al., 2000) and due to inefficient financial transparency keep governance practices in the South Asian nations far from those of industrialised countries, even though their governance structures mirror those of Anglo-American countries (Fan et al., 2011).

Fourth, throughout the last three decades, South Asian countries have been undergoing financial and educational reforms to promote financial liberalisation and improve the quality of the labour force. In countries in South Asia, until the financial crisis of 2008, the country's industrial output increased rapidly (Zeeshan et al., 2019). As a result of rising manufacturing costs, South Asian enterprises were unable to recoup momentum and lost their competitive advantage in the overseas market (Afzal, 2012), (Hussain & Javed, 2012). The industrial sector's expansion, notably that of export-oriented enterprises, is hampered by energy scarcity and rising energy costs (Amjad et al., 2012; Komal& Abbas, 2015). Financial limitations are also more considerable in South Asian countries (such as India and Bangladesh) compared to those in higher-income developing economies (such as Malaysia) (Azam & Shah, 2011). Fifth, family enterprises account for over 67% of all businesses in South Asian countries (Javid, 2012). On average, 60% of the company's stock is held by the five largest shareholders (Ullah et al., 2017). Minority and controlling owners may be at odds with each other, negatively influencing the company's success.

Unbalanced panel data from 104 companies registered on the South Asian Countries Stock Exchange between 2014 and 2021 is used in this study to assess if management skill influences business performance. Our research found that a company's worth increases dramatically when its managers are better. Contrarily, value was consistently decreasing for companies with subpar management over the duration of the research. These results corroborate numerous indicators of managerial efficacy and accounting and market performance metrics. Businesses that are struggling financially are also more inclined to hire competent executives. Many alternative measures of monetary constraint have confirmed this. We take into account endogeneity, heteroscedasticity, and serial correlation in two-stage least-squares (2SLS) and cross-sectional Fama-MacBeth analyses. Our findings aren't affected by these three things.

This research contributes significantly to the very little literature on the relationship between management skills and the value of a company. Since enterprises in South Asian countries encounter particular challenges, no previous research has looked at the impact of management competence on company success in this region. This study shows that management skills are essential to a company's success and that managers who are good at their jobs are valuable intangible assets.

The article's structure contains: A brief study history may be found in Section 2. A review of the theoretical literature is discussed in Section 3. A literature review and hypotheses are presented in Section 4. A detailed study design is provided in Section 5. The last section deals with a summary conclusion.

## II. Theoretical Background

IIMD's 1995 World Competitiveness Report found that the ability of a company's managers is one of the essential factors in its ability to compete, with reduced government intrusion, global financial sector integration, well-developed infrastructure, a knowledge society, and effective use of current technology; competitive local economies; and outward-looking economic policies. When a company's activities are integrated, it makes it easier to respond swiftly and effectively to a changing environment. As Mertzanis, (2019) has shown, businesses' performance in emerging markets is positively correlated with their ability to recruit and retain highly trained workers. However, in countries with different levels of economic growth, affluence, education, and technology, the results can be different as well.

The 2019 Global Competitiveness Index ranks South Asian countries low, despite their vast populations and substantial human capital. There are wide discrepancies across South Asia's several pillars of competitiveness. Competitors with the largest markets, fastest-changing businesses, and most innovation capability have the highest competitive index scores (79). On the other hand, the South Asian nations are a long way behind the other South Asian countries, with an aggregate rank of 110 (108). On the other hand, South Asian countries, on the whole, are in even worse shape when it comes to industry-relevant skills and the market for their products. It indicates that the value added by each employee in South Asian economies is much lower than in other economies worldwide. South Asian countries need a long-term competitive advantage through a knowledge-based economy. Still, progress in promoting access to high-quality education and associated training and development has been poor (Asrar-ul-Haq, 2015). A scarcity of highly trained workers may harm the quality of production and innovation in South Asian enterprises. According to a labour force survey, just 8% of employees in South Asian countries have had formal training.

South Asian countries' regulatory agencies have implemented various rules and policies to increase the supply of talented managers and workers to South Asian countries businesses. As a result of education reforms, educational monitoring and regulating authorities were established. To meet these demands, the National Productivity Organization (NPO) was founded to serve corporations' requirements better. As a result, the global business sector could compete more effectively. National training programmes were also created to help new graduates compete in today's workforce. It was recently developed and mandated to the corporations in 2017 that the directors' training programme be designed to increase the governance abilities of the top-level employees.

Reversing rebates on energy prices and a lack of financial sector funding have resulted in rising manufacturing costs, which shortages of competent workers have compounded. Most businesses are run by a small group of proprietors who have complete control over the company's operations and the distribution of profits. In light of the challenging economy and the potential for wealth expropriation by ultimate owners, external stakeholders are putting more pressure on the management to change the firm's policy. According to Andreou and colleagues (2013), firm performance may be improved by greater access to funding and reduced information asymmetry, especially in adverse environments. There was a lot of debate before this study, so it would be interesting to see how management skills play a role in a challenging environment where weak governance has already affected production parameters.

## III. LITERATURE REVIEW

No one agrees on what the quality of earnings is in the literature. If a company's earnings number is high quality, it correctly reflects its current operational success and is an excellent predictor of future profitability. Financial statements are less meaningful if the reported accounting results do not accurately reflect the company's financial activities during the reporting period. (Jannopat, 2022). According to Cheng and Cheung (2021), high-quality earnings should easily convert into cash. There is a high connection between earnings and cash flow and low volatility in accruals. They argue that companies with excellent profit quality should be valued on the stock market. As a result, the quality of earnings is measured by the market's reaction to earnings news. Hicksian income, as defined by Schipper and Vincent (2003), is the highest amount that may be spent while maintaining wealth. According to Kirschenheiter and Melumad (2004), a company's long-term worth is more likely to be influenced by high-quality profits than any other factor. According to Khatib et al. (2022), higher-quality earnings can be sustained over time. Earnings quality is defined by Gur et al. (2021) as the extent to which a company's earnings performance continues.

According to Francis et al. (2022), earnings quality influences are inherent aspects of business models, operational environments, and financial reporting processes. Dechow et al. (2021) developed a conceptual framework for analysing the quality of a company's earnings: Reported earnings = f (x), which reflects the accounting system that turns the X that can't be observed into the observable X that can be observed. Therefore, earnings quality is influenced by the company's underlying performance and the accounting system's capability to monitor performance. The firm-year-specific technique may estimate profitability quality metrics (Durana, P. et al., 2022). The company's post-earnings (or cash flow and accruals, etc.) are used as a benchmark in this time series regression approach. Cross-sectional regression techniques may also be used to estimate earnings quality indicators (McNichols and Stubben, 2008; Cornett et al., 2008). Using an indicator such as total assets as a scale, this strategy uses the industry's average earnings (scaled by an indicator like that) as a benchmark. An earnings-quality metric might be derived using the regressions' estimated coefficients, forecasting errors (such as discretionary accruals), or modified R-squares (such as value relevance). Therefore, the difference between current and benchmark earnings, represented in the parameters, is an essential factor in determining the quality of earnings.

Managerial talent in finance impacts the quality of a business's earnings, which is to say, how efficient a firm in finance is compared to other companies in its industry. According to Demerjian et al., (2006), management abilities positively impact earnings quality. Managerial ability is directly linked to profitability. If a manager has enough education and experience in the field of responsibility, they are regarded as competent. Managers with more extraordinary experience better grasp the current business environment. Managers are also guided by codes of conduct or ethics when carrying out their responsibilities so that every choice they make represents their professional judgement rather than judgments implemented for their advantage. Managerial decisions influence the organisations they lead, indicating the level of competency of various managers at the corporate level. When maximising a company's resources, profit quality is a critical factor to consider. Investors and analysts use the information in the results to evaluate the company's performance and decision-making. High capital expenses are typical in companies with low earnings quality (Francis et al., 2004), as are restatements of the financial statements. Good profit quality is a sign of successful operations for a company (Kliestik, 2021).

It is impossible to separate the management from the company's operational performance. According to setting policies, each manager has their own "unique style," according to Bamber and colleagues (2010). Accounting and corporate disclosure policies are heavily influenced by long-tenured managers (fixed), according to studies by Ge et al., (2011) and DeJong and Ling (2010), both of which looked at the impact of managers on financial reporting policies and found similar results to those of Valaskova, K., et al. (2021). More knowledgeable managers are better equipped to learn about their organisation and industry and synthesise information that may be used to anticipate the future with greater accuracy (Libby and Luft, 1993). It has been shown that higher-capability managers are better able to predict accruals than lower-capability managers, according to Demerjian and colleagues (2013).

According to Francis et al. (2022), more competent managers have a better grasp of how businesses work and how much demand there is for their goods. Consequently, they are more knowledgeable about current market conditions and technological breakthroughs. Adept managers also build adequate internal controls to monitor financial reporting, which helps raise the quality of their profits (Gur et al., 2022). Offering high-quality information and showing superior skill by providing accurate projections makes them less likely to commit financial reporting fraud (Wang et al., 2021). As stated in the paper (Wang et al., 2017), Talented managers, according to research, spend more on R & D more effectively because they are more creative and willing to take risks (Gan, 2019; Mishra, 2019; Yung & Chen, 2018).

### *3.1 Empirical literature review and hypothesis development*

To accurately assess a firm's performance, its earnings quality is an important consideration (Li, 2014). Dechow et al. (2010) state that the high earning quality offers the decision maker with more information about the company's performance that is directly related to the choice at hand. The excellent earnings quality also correctly represents the company's operating success, according to Demerjian et al. (2013). When a company's accounting profits fail to accurately represent its financial activities during the reporting period, investors will have less trust in the company's financial statements (Healy and Wahlen, 1999). High-quality profits, according to Dechow and Schrand (2004), also need being easily convertible into cash. Earnings and cash flow are highly correlated, and the volatility of accruals is minimal. When income can be maintained into the future, Revsine et al. (1999) argue, that's when it's at its highest quality. With respect to future earnings success, Richardson et al. (2005) define earnings quality as the extent to which this performance is sustainable.

*$H_1$: Earnings quality positively impacts firm performance.*

Financial and accounting scholars are beginning to explore the tradeoffs between management skills and their associated expenses. P. Demerjian et al., (2021) created a measure of management aptitude to help address these study issues. According to research, managers that are good at allocating resources have demonstrated that the possible opportunity cost drives them in the form of future income and personal reputation. Managerial attributes like skill, aptitude, quality, or reputation have been studied to see if they impact business decision-making. Management fixed effects might explain the wide range of investment and operational techniques employed by different organisations (Bertrand & Schoar, 2021). Managerial style and business performance have been linked by Chang et al., (2021). Performance might vary widely because of the various managerial backgrounds and characteristics. Managers adept at analysing industry patterns and forecasting product demand can make long-term profits, even during economic downturns. Setiawan (2015) discovered that businesses with competent management make smart choices that boost productivity and profitability. As a result, competent management is important for a company's success. Therefore, the following theory is put out by us.

*$H_2$: Managerial ability has a positive impact on firm performance*

Management competency indirectly influences corporate value via improved financial reporting and information disclosure, better internal control and cash management, and lower-cost financing choices. Studies on the director's role in a company's performance are few and far between. During the global financial crisis, Wang et al. (2021) explored the importance of management competence in the United States. They claim that during a crisis phase, more capable managers outperform because of their ability to effectively and efficiently utilise the firm's resources. Maintaining minimal information asymmetry aids competent managers in seizing and supporting more profitable investment opportunities by providing them with preferred access to debt funding throughout the crisis phase. Anom, an Indonesian market research organisation, confirms the improved firm performance attributed to capable managers. Chuah and Foong (2019) have recently revisited the influence of management competence on company success in a Malaysian context. They support the claim that a company's worth increases when its managers have a higher skill level. On the other hand, local managers have a distinct advantage over international managers. Learning about local markets and doing what management wants are the most critical factors adding value to Malaysia.

*H3: Managerial ability positively moderates the relationship between earnings quality and performance of the firms.*

## IV. RESEARCH METHODOLOGY

### *4.1. Sample selection*

South Asian manufacturing companies listed on the Stock Exchange between 2014 and 2021 are the research population. It was decided to focus on the manufacturing industry because it has many companies with a wide range of data. For this study, 2014-2021 were chosen because the data for these three years are readily available to the public and can be used to describe the most up-to-date financial profile of 104 manufacturing companies. The study sample comprises 50 corporations.

### *4.2. Variables and Measurement*

Accounting conservatism is an important indicator used by Hartam and Kresnawat (2021) to quantify Earning quality. Accounting conservatism in this study was determined using the method of earning/accrual measures. The tool employed by Demerjian et al. (2012) is used to measure management skills (2013). The sales generated by each organisation are compared to the seven inputs that each firm use to assess management ability; (Cost of Goods Sold, Selling and Administrative Expenses, Net PP&E, Net Operating Leases, Net Research and Development, Purchased Goodwill, and Other Intangible Assets). Company performance is measured by using Return on Asset (ROA). ROA can measure the overall profitability of a company's assets .

As a way of gauging a company's size, we look at the natural logarithm of its total assets, leverage is measured using debt-to-equity ratio (Simamora, 2021; Duan et al., 2022.). Interest rate = interest on commodities. Growth =Revenue Growth; (revenue $_t$ – revenue $_{t-1}$)/ revenue $_{t-1}$.

***Estimation Model***

$$FP_{i,t} = \beta_0 + \beta_1 EQ_{i,t} + \beta_2 MA_{i,t} + \beta_3 I_{i,t} + \beta_4 S_{i,t} + \beta_5 G_{i,t} + \beta_6 L_{i,t} + \varepsilon_{i,t} \qquad (1)$$

Note:

Dependent variable: FP = firm performance

Independent variable: EQ = earning quality, MA= managerial ability.

Control variable: I = interest rate, S = firm size, L = leverages, G = growth. and ε = Error Term

Moderated regression analysis conducts a moderating variable test using the following equation:

$$FP_{i,t} = \beta_0 + \beta_1 (EQ * MA)_{i,t} + \beta_2 S_{i,t} + \beta_3 G_{i,t} + \beta_4 L_{i,t} + \beta_5 I_{i,t} + \varepsilon_{i,t} \qquad (2)$$

The purpose of moderation is to strengthen or weaken the relationship between two constructs (Nie et al., 2011; Şanlı, 2021). The positive sign of the interaction term (EQ*MA) concludes that MA enhances the effect of EQ on the FP relationship. The significant negative sign concluded that EQ and FP relationship is weaker.

#### *4.2.1 Earning quality*

Earning quality is a measure of how dependable a company's earnings are for judging a company's present and future performance. The absence of managerial interference and the reliability of the results as a forecast of future cash flows are consistent with a high level of earnings quality.

Earnings quality may be assessed using numerous methodologies and indicators; there is no one formula to determine quality. However, earnings quality analysis frequently involves extensive financial statement analysis to identify non-recurring items of income and cost, large non-cash items of revenue and expense, and a review of balance sheet items that rely on management assumptions.

#### *4.2.2 Managerial Ability*

Managerial ability is a set of traits and characteristics an executive must have to carry out their duties effectively. Among these abilities is the propensity to execute executive tasks in an organisation, emphasising preventing crises and finding practical solutions quickly when they arise. Learning and experience in management positions are the best ways to hone one's managerial chops. The manager's ability to connect with their peers and know how to effectively manage their subordinates is crucial to the smooth operation of the business as a whole.

#### *4.2.3 Interest Rate*

Money may be borrowed at an interest rate or saved at a higher rate. Percentages of the total amount borrowed or saved are used. When you get a mortgage, the bank lends you the money for the down payment and the interest on the loan. Loans for other purposes may finance acquiring a vehicle, home furnishings, or further education. The bank will give you interest in exchange for the use of the money you deposit in a bank. The deposits are used to finance the lending operations. The interest rate that banks charge borrowers is somewhat more remarkable than the interest rate that they pay out on deposits. The disparity represents their gain from the transaction. Competition among banks for customers keeps interest rates stable within a small band.

#### *4.2.4 Firm Size*

Firm size is equivalent to that of a commercial enterprise. Specifically, it refers to the extent or output of a particular company. Enterprise efficiency and profitability are significantly impacted by several factors, including the firm's size. Realising the "size" of a firm and the impact it will have on the company's operations and profitability is a crucial step for every entrepreneur.

#### 4.2.5 Leverage

Leverage uses leverage (loan funds) to pursue an investment or endeavour. In this way, the prospective profits of a project may be increased by a factor of many. However, the danger of losing money on the investment is magnified by using leverage.

Investors and businesses alike may benefit from understanding the notion of leverage. With the use of leverage, investors may considerably boost their profits. Options, futures, and margin accounts are just some of the tools they use to increase the leverage on their assets. The use of leverage is a standard method for financing company assets. In other words, corporations might utilise debt financing to invest in company operations to improve shareholder value instead of issuing shares to obtain cash.

#### *4.2.6 Growth Rate*

The term "growth rate" describes the rate of change of a given variable over a specific time frame. When discussing growth rates, investors often refer to the compound annual growth rate (CAGR) of a company's revenues, profits, dividends, or even macro notions like GDP and retail sales. Two primary growth rates utilised in the analysis are those based on projections and historical performance.

#### *4.2.7 Firm Performance*

How well a firm does in the market is a factor in how well it does, but efficiency inside the organisation is also essential. Stability or health in one's financial situation is another name for it. There are a variety of metrics one may use to assess a business's financial health. Revenue, return on equity, return on assets, profit margin, sales growth, capital sufficiency, liquidity ratio, and stock prices are just a few of the widespread financial measurements. Some financial measures will be more instructive than others depending on the firm's sector. When assessing a company's performance, it's essential to look at how its financial metrics stack up against those of similar businesses in the same industry. This is because every sector has its own peculiarities, and generalising results from one industry can lead to erroneous conclusions.

## V. Estimation of Results

The study encloses data analysis and estimation of a model by using different econometrics techniques. The current chapter of the study is most important because it explores the relationship between dependent and independent variables. The step-wise estimation econometrics techniques are given below,

### *5.1. Statistical Analysis*

Describing the data in terms of their means, medians, modes, and standard deviation minimum and maximum values is an essential part of any data analysis and model estimation process that relies on descriptive analysis. Researchers benefit from this analysis since it illustrates the breadth and basic properties of the data. All of the variables are represented in table 1, which includes the average, standard deviation, minimum, and maximum values.

Table 1 *Descriptive Statistics*

| *Variable* | *Mean* | *Std. Dev.* | *Min* | *Max* |
|---|---|---|---|---|
| ***EQ*** | 12.51048 | 1.710484 | 11.7710 | 19.4311 |
| ***MA*** | 3.550529 | 3.766853 | -9.8538 | 23.6777 |
| ***I*** | 0.570914 | 0.297326 | 0.1665 | 1.24773 |
| ***S*** | 4.385466 | 2.138832 | 8.3399 | 15.4345 |
| ***L*** | 7.375228 | 1.177302 | -18.1086 | 22.5645 |
| ***G*** | 6.980982 | 2.090982 | 1.0998 | 11.9809 |
| ***FP*** | 9.551743 | 1.17585 | 8.8374 | 17.8260 |

Table 1 shows observations with the central tendency of each variable shown in the third column. Using the standard deviation and the minimum and maximum values of the variables' data ranges, researchers may see how much the data deviates from the mean.

Table 2: Correlation Matrix

| | *EQ* | *MA* | *I* | *S* | *L* | *G* |
|---|---|---|---|---|---|---|
| ***EQ*** | 1.0000 | | | | | |
| ***MA*** | -0.493 | 1.0000 | | | | |
| ***I*** | -0.3885 | 0.1840 | 1.0000 | | | |
| ***S*** | -0.3395 | 0.2235 | 0.1735 | 1.0000 | | |
| ***L*** | 0.1722 | -0.1224 | -0.2616 | -0.0490 | 1.0000 | |
| ***G*** | -0.3113 | 0.3081 | 0.0361 | 0.2573 | -0.1315 | 1.0000 |

As a means of demonstrating how several variables are linked, the correlative analysis method is widely used today (Khoo et al., 2022). Table 2 shows the correlation matrix, which makes it easy to see the degree to which one variable is linked to the others. Correlation analysis also aids in determining whether or not variables are perfectly associated, as the name implies. Since no perfect connection can be found, data that is well-organised and suitable for further investigation are considered to exist. All variables appear to be linked in Table 2; however no proof of perfect multicorrelation can be found. The value 1 indicates perfect correlation, yet no correlation exists between the variables. Because of this, we are confident in its accuracy and may use it for regression analysis.

Table 3: Shapiro-Wilk W Test For Normal Data

| *Variable* | *W* | *V* | *Z* | *Prob>z* |
|---|---|---|---|---|
| ***EQ*** | 0.94130 | 8.222 | 4.830 | 0.00000 |
| ***MA*** | 0.89052 | 15.334 | 6.258 | 0.00000 |
| ***I*** | 0.92973 | 9.843 | 5.242 | 0.00000 |
| ***S*** | 0.51619 | 67.766 | 9.665 | 0.00000 |
| ***L*** | 0.89284 | 15.010 | 6.209 | 0.00000 |
| ***G*** | 0.89968 | 14.052 | 6.058 | 0.00000 |
| ***FP*** | 0.98092 | 12.980 | 7.809 | 0.00000 |

Table 3 shows that the sample's distribution differs from the standard distribution. This is a standard test for determining whether or not a sample's distribution is normal. P-values less than 5% (p.05) imply that the samples are distributed regularly.

### *5.2. Empirical Results and Discussion*

Table 4: Empirical Results

| Dependent Variable: FP | | | | | | |
|---|---|---|---|---|---|---|
| | ***Coef.*** | ***Std. Err.*** | ***T*** | ***P>\|t\|*** | ***[95% Conf. Interval]*** | |
| ***MA*** | 0.575819 | 1.658282 | 3.87 | 0.021 | 1.798479 | 1.768919 |
| ***EQ*** | 0.198098 | 0.109833 | 5.94 | 0.010 | 2.870803 | 2.089080 |
| ***MA*EQ*** | 0.012847 | 1.476374 | 3.40 | 0.019 | 2.685344 | 2.453860 |
| ***I*** | -0.798982 | 1.879873 | -4.09 | 0.050 | 1.983983 | 1.798730 |
| ***S*** | 0.087789 | 1.546627 | 2.76 | 0.007 | 3.798749 | 2.768932 |
| ***L*** | 0.017987 | 0.658763 | 2.09 | 0.006 | 2.879870 | 3.879870 |
| ***G*** | -0.280922 | 0.179838 | -3.67 | 0.000 | 3.769879 | 2.769830 |
| ***Cons*** | 5.39820 | 1.979392 | 2.07 | 0.000 | 31.78392 | 39.76828 |
| ***R Square*** | 0.5197 | | | | | |

According to Table 4, managerial skills have a positive and substantial effect on a company's performance. Consequently, the capacity of a company's management to enhance the quality of its profits is enhanced. This result aligns with the findings of Ng et al. (2015), who discovered that managerial competence with effective monitoring increases value creation. According to stakeholder theory, a manager must play a dual function as a person who regulates the company's operational activities and addresses the requirements of corporate stakeholders (Adhiapsari, 2018). This theory supports the findings of this research. In addition, the outcome of earning quality has a substantial and favourable correlation with company performance. A positive coefficient indicates that when profitability grows, so does business performance (Mahmud et al., 2009). This study also proved that Managerial ability will enhance the relationship between earnings quality and firm performance. The significant values of the relationship between earnings quality with firm performance play as moderators' role were lower than 0.050 (0.019).

Looking at the control variable, Growth is negatively and significantly associated with firm performance, indicating that firms with higher sales growth have poorer performance (Chan et al., 2006). The interest rate exhibits a negligible negative result. This study is consistent with Mwangi and Wekesa's (2017) Kenyan study, which showed that interest rate considerably impacted performance. In contrast, firm size and leverage positively relate to firm performance (Mahmud et al., 2009; Morck et al., 1988). The F value of 0.001 means the model is valid and can be used for further analysis. R square value of 0.519 shows that 51% variation in dependent variable is explained by independent variable.

### *5.3. Diagnostic Tests*

#### A. Multicollinearity Test

When the independent variables in a regression model are correlated, a phenomenon known as multicollinearity arises. When comparing two independent variables, it is difficult to find a correlation between them. High levels of correlation between variables might make it challenging to fit the model and comprehend the findings. The Variance Inflation Factor (VIF) test, shown in table 5, is used to construct the multicollinearity test. Each explanatory variable is given its ratio in this study. The multicollinearity in the model is indicated by a high VIF value, which is often larger than 5. Independent variables with VIF values less than 5 appear in Table 5. As a result, the model does not have any multicollinearity in it.

Table 5: VIF Test

| Variable | VIF | 1/VIF |
|---|---|---|
| ***TAX*** | 1.17 | 0.854308 |
| ***FP*** | 1.16 | 0.858525 |
| ***PCI*** | 1.13 | 0.885683 |
| ***C02*** | 1.12 | 0.890344 |
| ***INF*** | 1.09 | 0.913906 |
| **Mean VIF** | 1.14 | |

***B. Heteroskadasticity Test***

When the error variance of the model is not the same for all observations as is often assumed in estimation modelling, this is called heteroscedasticity. The opposite is homoscedasticity, which is of particular relevance in the context of linear regression and time series analysis. The Bruesch Pagan LM test, shown in table 6, determines the heteroskedasticity test. The constant variance null hypothesis is not rejected since the p-value is more than 5%. As a result, the model's variance is fixed, and no heteroskedasticity exists.

Table 6: Breusch-Pagan / Cook-Weisberg test for heteroskedasticity

| | | |
|---|---|---|
| **Number of instruments = 165** | | **Wald chi2(6) = 131.01** |
| **Prob> chi2 = 0.0000** | | |
| **Ho:** | **Constant variance** | |
| **Variables:** | **Fitted values of hc** | |
| **chi2(1)** | 2.23 | |
| **Prob> chi2** | 0.1352 | |

***C. Ramsey RESET Test***

The Ramsey Regression Equation Specification Error Test (RESET) is a generic specification test for the linear regression model used in statistical analysis. Notably, it examines whether or not non-linear combinations of the fitted values contribute to an explanation of the response variable. In the Ramsey RESET test, model misspecification can be spotted. Table 7 provides the information. Because the p-value is greater than 5%, the null hypothesis is that the model does not include any omitted variables. That's why there are no missing variables, and the model is free of misspecification.

Table 7: Ramsey RESET Test

| | |
|---|---|
| **Ramsey RESET test using powers of the fitted values of hc** | |
| **Ho: model has no omitted variables** | |
| **F(3, 177) =** | 1.19 |
| **Prob> F =** | 0.3149 |

### *5.4. Discussion*

It was discovered that managerial abilities significantly impact a company's performance. The findings of this study demonstrate that a competent manager in charge of the company's operational activities will massively increase the firm's performance, making it more attractive to investors and other stakeholders. Managers with a high level of competence will be better equipped to support and open up the vast potential for companies to continue developing and expanding to compete with other businesses. According to Bellner and MacLean (2015), CEOs with superior management skills can recognise risks, opportunities, and competitive advantages. The results depict that earning quality massively enhances the worth of a corporation. Improvements in earnings quality reduce both information asymmetry and erroneous reporting to stakeholders. Because of the reduction in information risk, stakeholders are more confident in purchasing such companies' stocks, driving up the firm's market value. However, some argue that EQ indicators are indicative of managerial opportunistic behaviour regarding accounting standard modifications (Leuz et al., 2003).

Furthermore, macroeconomic elements like interest rates have a negative impact on firm performance. Mnang'at et al. (2016) discovered a correlation between the interest rate and the financial performance of micro companies in Kenya. The importance of interest rates lies in the fact that they regulate the flow of money in the economy. High-interest rates reduce inflation but retard economic growth. Large enterprises can achieve economies of scale and contain a wide array of capabilities, which contribute favourably to their worth. These attributes positively affect the company's value (Ehikioya, 2009). Similarly, leverage favours a company's value and suggests that debt restrictions hinder managers' opportunistic conduct toward free cash flows (Ahmed et al., 2013). Due to the high level of leverage inside the organisation, managers may be more driven to monitor earnings.

In addition, managerial ability strengthen the relationship between earning quality and firm performance. The positive sign of interaction term (EQ*MA) concludes that MA enhance the effect of EQ on the FP relationship. When managers have strong leadership skills, earning quality can have a greater impact on the firm performance. A new study adds to the body of knowledge about how accounting practises, such as accrual accounting, and real activity that deviates from accepted norms, affect the quality of earnings (Simamora, 2021); the ownership of private and public companies (Le et al., 2022); the management of earnings (Hartam and Kresnawati, 2022); and companies that consistently outperform their industry rivals and the strength of corporations (Prior et al., 2008). For example, a large negative impact on profit quality can be seen from macroeconomic conditions proxied by the interest rate. This is most likely due to the 7.28 percent persistence of earnings in the interest rate category during the data collection period (2014–2016). The findings of Vlas et al., (2022); Wang., (2022), which suggest that earnings quality is also connected to the company's infrastructure, are supported by these results.

## VI. Conclusions

The findings of this research add to the body of information on the correlation between management competence and organisational success. This study intends to investigate the moderating role of managerial skills in company performance in the South Asian country setting. The existing literature is silent on the moderating effects of managerial ability association among earning quality and firm performance, thus providing only a partial view (Habib & Jiang, 2015). Keeping this argument in view, this study examines the earning quality and firm performance relationship from a new dimension, that is, the role of managerial ability as a moderator variable in the earning quality-firm value relationship. All of the findings have been interpreted with the scope of the research in mind. For analysis, this study used secondary data from 50 South Asian manufacturing corporations' audited financial statements, which included 104 units of analysis for eight years spanning from 2014–2021. For estimation, the study has used regression analysis.

Our findings indicate that the quality of earnings has a substantial impact on the performance of a business. Higher earnings quality can be viewed as reducing information asymmetry and systematic risk, which reduces the cost of capital and raises the firm's value. The effectiveness of a company is significantly influenced by managerial ability. Managers that are skilled in operating the company's operations will be able to improve the firm's performance so that it appears favourable to investors and other stakeholders in the company. Adopting a personal goal of maximising shareholder interests is the result of managerial talent that significantly affects firm performance and agency theory's criticism. As a result of this study, there is no additional evidence that management skills can significantly impact firm performance. According to a study, managers with high management abilities can increase their companies' earnings, which is good news for both owners and managers. In addition, managerial ability play a moderating role in the relationship between earning quality and firm performance.

Differences in earnings manipulation exist even if nations have grown under identical circumstances. It seems that cultural, social, and legal contexts in each nation have a substantial impact on how earnings manipulation is seen. Changes in the macroeconomic environment, on the other hand, affect companies' operations, finances, productivity, and reputation. Large shifts in the macroeconomic environment offer businesses new opportunities and difficulties, prompting them to engage in earnings management to alter their financial results and, in turn, generate financial statements that give an unduly optimistic picture of the company's commercial operations and financial condition. As a result, protecting the market or investors from financial risk resulting from skewed information necessitates the development of technologies to detect earnings management tactics.

## IMPLICATIONS

The implications of this study's findings have important practical implications for the business, as they can be used to select managers who are not only competent but also able to play a role in aligning organizational goals and maximising the welfare of stakeholders, as well as to assess managers' performance in terms of their managerial ability. Additionally, this study can inspire regulators to assess the efficacy of the implementation and formulation of corporate governance policies. Our analysis provides stakeholders with valuable insights. These insights are helpful for South Asian economy practitioners, policymakers, and regulators. The regulatory bodies of South Asian countries should establish various regulations and policies to improve the supply of qualified managers and workers to South Asian firms. We recommend that investors purchase and hold the shares of companies with highly competent management, as such managers are connected with superior firm performance. Managers must properly evaluate interest rates when determining the cost of debt while making borrowing decisions. Top management must appoint competent individuals to govern and manage corporations.

## LIMITATIONS

This research has some limitations. We advise conducting research in diverse fields and areas. Researchers might, for instance, look at the same subject among small and medium-sized enterprises. Additionally, it enables managers to allocate resources to the projects that will benefit the enterprise and to situations where there are financial constraints. The DEA score for managerial ability was measured using inputs and outputs that did not conform to those proposed by previous studies, which is one of the study's limitations.

Since firm performance is an intangible asset that is notoriously hard to quantify, this study relies on secondary data to arrive at its findings. Thus, it is impossible to assess one's financial adaptability with a single metric. Therefore, semi-structured questionnaires can be used to collect primary data from employees, managers, and other stakeholders in future research, which may lead to a more nuanced understanding of firm performance and earning quality. We recommend that future studies take into account ethical considerations for managers, employ multiple measures of earnings quality (such as earnings persistence, predictability, and earning management), and use samples from sectors other than manufacturing.

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