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Headline Salience, Managerial Opportunism, and Over- and Underreactions to Earnings

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ABSTRACT

Limited attention theory predicts that higher salience of earnings news implies a stronger immediate market reaction to earnings news and a weaker post-earnings announcement drift (PEAD) or reversal (PEAR). Using a new measure, *SALIENCE,* defined as the number of quantitative items in an earnings press release headline, we find strong evidence consistent with salience effects. Higher *SALIENCE* is associated with stronger announcement reaction and subsequent PEAR. Managers are more likely to choose higher *SALIENCE* before selling shares in the post-announcement period and when earnings are high, but less persistent, and to choose lower *SALIENCE* before stock option grants. The results are robust to using residual salience and an extended set of control variables. The findings are consistent with managers opportunistically headlining positive financial information in the earnings press release to incite over-optimism in investors with limited attention.

Keywords: qualitative disclosure, disclosure management, market efficiency, limited attention, behavioral finance, investor psychology, post-earnings announcement drift

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