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Managerial Ability Concept and Measurement Models in Accounting: A Systematic Literature Review

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Abstract

This study aims to systematically review all studies on managerial ability in accounting and identify the gaps between them. The breadth and variety of recent studies highlight the significance of this literature review. We identified 110 relevant studies published from 1990 to 2022 through multiple international scientific search engines, which we reviewed and categorized into ten thematic classes: performance, capital market, reporting quality, audit, investment, dividend policy and cash management, tax, corporate social responsibility, COVID-19, and miscellaneous. Our review shows that a considerable number of studies (43 out of 110) have focused on the relationship between firm performance, capital markets, and managerial ability due to the complex results in this field and various market perceptions of high-ability managers. However, few studies have explored the link between managerial ability, going concern, conservatism, and family firms. Moreover, most studies use Demerjian et al.'s (2012) model to measure managerial ability, which is an indirect method. Finally, we provide possible areas for improvement in the Demerjian et al. (2012) model and identify research gaps for future studies.

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1. Introduction

Two different points of view have been formed about the importance of the manager's role (Bertrand and Schoar, 2003). First, according to neoclassical economics, two firms with similar technologies, factors and market conditions will make the same choices regardless of the characteristics of their managers. In other words, a firm's performance depends on the competitive environment, product quality, corporate governance mechanisms, and other controls its shareholders apply. Industry and firm-specific factors play more important roles than managers. Second, based on agency theory, managers have special discretion to make decisions and reach their goals as agents of different stakeholders. Although differences in firms' behavior can be attributed to heterogeneity in governance mechanisms across firms, these differences cannot just be attributed to the different characteristics of their managers. However, heterogeneity is observed in models that explicitly allow managers to be different in their preferences, risk aversion, skill levels, or opinions (Bertrand and Schoar, 2003). Additionally, stewardship theory (Davis et al., 1997) and contract theory (Sunder and Cyert, 1997) share the same viewpoint as the agency theory. Accordingly, managerial contribution to firm performance and investment decisions has been studied for years with concepts like corporate governance, investment judgments, and cross-country productivity differences (Demerjian et al., 2012).

The current review shows that the characteristics of managers affect firm performance. Specifically, there is a significant share of heterogeneity in decisions, investment methods and practices of firms rooted in managerial traits (Andreou et al., 2017). Characteristics such as ability, talent, reputation, style, efficiency, narcissism and myopia are the most widely used criteria to measure the influence of managers on firm performance. For instance, Barr and Siems (1997) and Leverty and Grace (2012) demonstrated that efficient managers could reduce the likelihood of insolvency. Using four variables to measure reputation, Milbourn (2003) showed a positive relationship between stock-based pay sensitivities and CEO reputation. This relationship became stronger after controlling for age, firm size, dollar variability of the stock returns, and industry. Rajgopal et al. (2006) also found a positive relationship between outside opportunities and managers' talent.

Between various measurements of a manager's role, "managerial ability" has attracted significant attention among accounting and management researchers. There are different definitions and descriptions for the word "ability". Compared to other managers in the same industry, more-able managers are more efficient (Demerjian et al., 2012) and more accurate in forecasting earnings (Baik et al., 2011; Lee et al., 2012). Furthermore, more-able managers have higher expected stock returns (Mishra, 2014) and lower real earnings management (Huang and Sun, 2017). The multiple definitions and descriptions of managerial ability have led to the emergence of various models and variables to measure managerial ability. Consequently, different results have emerged around managerial ability.

The present study intends to systematically review the thematic connections and measurement models and identify gaps among related studies. We try to answer the following main questions: What studies have been conducted around managerial ability? What themes emerge out of these related studies? And what are the most frequently used models and variables to measure managerial ability?

We have reviewed 110 studies published between 1990 and 2022 in this paper. These studies have been classified into 10 categories: performance, capital market, reporting quality, audit, investment, dividend policy and cash management, tax, corporate social responsibility, COVID-19, and miscellaneous. A large number of studies (43 out of 110) have been conducted around the relationship between firm performance, capital market, and managerial ability. Corporate governance, firm performance, firm value, information asymmetry, and real earning management were the most frequently used keywords with managerial ability. Moreover, the model proposed by Demerjian et al. (2012) was the most frequently used to measure managerial ability. The analysis of the studies over time also illustrates that a few studies have been implemented before 2017, while the Demerjian et al. (2012) model was developed five years earlier. Generally, studies have shown that different groups affect or are affected by managerial ability. Investors react to switching able managers (Hayes and Shaffer, 1999; Demerjian et al., 2012); financial analysts revise their predictions based on managerial ability (Gao et al., 2020); creditors assess credit rate and risk of firms under the influence of managerial ability (Chen et al., 2017; De Franco et al., 2017); auditors determine their fees according to managerial ability (Krishnan and Wang, 2015). Additionally, managerial ability affects the financial reporting environment (Lou and Zhou, 2017; Yan et al., 2021), information environment (Baik et al., 2018), investment activities (Chen et al., 2015; Yung and Chen, 2018), dividends (Sarwar et al., 2019), tax avoidance (Park et al., 2016), and social responsibility (Sun, 2017).

Our study has several important contributions. First, studies around managerial ability have been presented in an integrated and classified manner. Second, the evolution of variables and models used and developed to measure managerial ability has been narrated. Third, the existing gaps among related studies and improvable points in measurement models of managerial ability have been presented.

The present research is organized as follows. First, the concept of managerial ability and related theories will be introduced. Then, the research methodology, the analysis based on the thematic classification, the number of citations, the measurement model, keywords, and results will be examined. Finally, the conclusion and suggestions for future research will be provided.

2. Literature Review

2.1 The concept of managerial ability

The concept of managerial ability has different definitions and descriptions. Managerial ability can be defined from a human capital and a strategic perspective. Primarily, managerial ability was defined from the human capital perspective as managers' knowledge, skill and experience. The human capital perspective differentiates between the general and specific abilities of managers. Custódio et al. (2013) define the general managerial abilities of CEOs as skills acquired through a lifetime of work experience, particularly experiences gained in a number of functional areas, in firms and industries and from past CEO positions at other firms and conglomerates. The skills gained through CEO experience are not specific to an entity or sector and readily transferable across firms and industries. Specialist managerial abilities are not readily transferable across firms or industries but may be highly valuable within a particular firm or industry (e.g., May, 1995; Murphy and Zabojnik, 2007; Kaplan et al., 2012). Studies show that managers with higher general abilities have more job opportunities with higher salaries compared to managers with specific abilities (Murphy and Zabojnik, 2004; Holcomb et al., 2009).

According to the strategic perspective, on the other hand, two main sources construct managerial ability: domain expertise and resource expertise. Domain expertise refers to managers' understanding of the industry context and the firm's strategies, products, markets, task environments and routines (Boeker, 1989; Kor, 2003; Spreitzer et al., 1997). Resource expertise represents the ability of managers to select and configure a firm's resource portfolio, bundle resources into distinctive combinations, and deploy them to exploit opportunities in specific contexts (Holcomb et al., 2009). Furthermore, in the accounting framework, Baik et al. (2011) consider the ability to evaluate and forecast changes in the firm's economic outlook to be the definition of a high-ability manager. Besides, managers with executive experience and skills are considered more able (Mishra, 2014; Andreou et al., 2017; Cheng et al., 2020; Gounopoulos et al., 2021; Lin et al., 2021). Finally, Demerjian et al. (2012) presented a definition of managerial ability that met with great success: "more-able managers to generate higher revenue for a given level of resources or, conversely, to minimize the resources used for a given level of revenue" (Demerjian et al., 2012). In summary, a more able manager in a certain industry can more efficiently use resources for others.

We can learn from the evolution of definitions and descriptions of managerial ability over time that the year 2012 and the study of Demerjian et al. can be considered a turning point. Although there were varied definitions for managerial ability before Demerjian et al. (2012), most researchers have accepted their definition, and various descriptions have been created around the concept of managerial ability.

As mentioned above, there are various descriptions of the managerial ability concept. For instance, more-able managers are those who have a positive tone in their earnings announcements (Luo and Zhou, 2017), have less likelihood to engage in opportunistic financial reporting (García-Meca and García-Sánchez, 2018; Krishnan, Wang and Yu, 2021), have a more accurate estimate of capital expenditures (Chen and Chen, 2020), have lower levels of real earnings management (Huang and Sun, 2017), or have higher shareholders' expected return (Mishra, 2014).

2.2 Theories around the managerial ability

As mentioned earlier and discussed by Demerjian and Lev (2021), the neo-classical model of the firm states that the manager has no role except in implementing the objectives of the firm owners. Therefore, the managers do not have opinions independently; they only make decisions that efficiently maximize investors' wealth. Although it has long been established that managers are heterogeneous in their preferences, beliefs, and styles, the literature was largely silent on how differences in managers manifested in various firm policies and outcomes. Agency, stewardship, contracts and signalling theories also highlight the role of managers in firm policies and outcomes.

Bertrand and Schoar (2003) started a line of studies on the role of individual managers. Their study identifies a set of managers who switch firms at some point during their sample period. This "switching" sample allows Bertrand and Schoar to identify the effects of managers incremental to firm effects. Their evidence shows that manager fixed effects provide incremental explanatory power for a variety of corporate policies, such as investment and dividend policies. Bertrand and Schoar also identify various regularities in managerial characteristics, linking age and educational background to aggressiveness in firm policies. Following Bertrand and Schoar (2003), several studies examine the impact of managerial style using a fixed effects framework. Although the fixed effects methodology of Bertrand and Schoar (2003) has been influential, it is not without limitations. First, its identification relies on a relatively small and idiosyncratic set of managers who switch jobs. So, the generalizability of the model is questionable. Second, the tests of effects are relatively abnormal; the joint effects of individual managers are assessed using F-tests and incremental adjusted R2s. Although this provides evidence of an aggregate or collective effect, it is impossible to determine the direction of the effect or the role of individual managers. On the other hand, the initial objective of Demerjian et al. (2012) model is to expand Bertrand and Schoar's (2003) model. They developed a measure that could be measured for a broad cross-section of firms and provide a directional measure of a manager’s influence.

3. Research Methodology

Following the methodology used by Shields (1997), Chenhall and Smith (2011), Hesford et al. (2006) and Hoque (2014), the present research goes through six steps to conduct a systematic review of the research studies. These steps are presented in Figure 1.

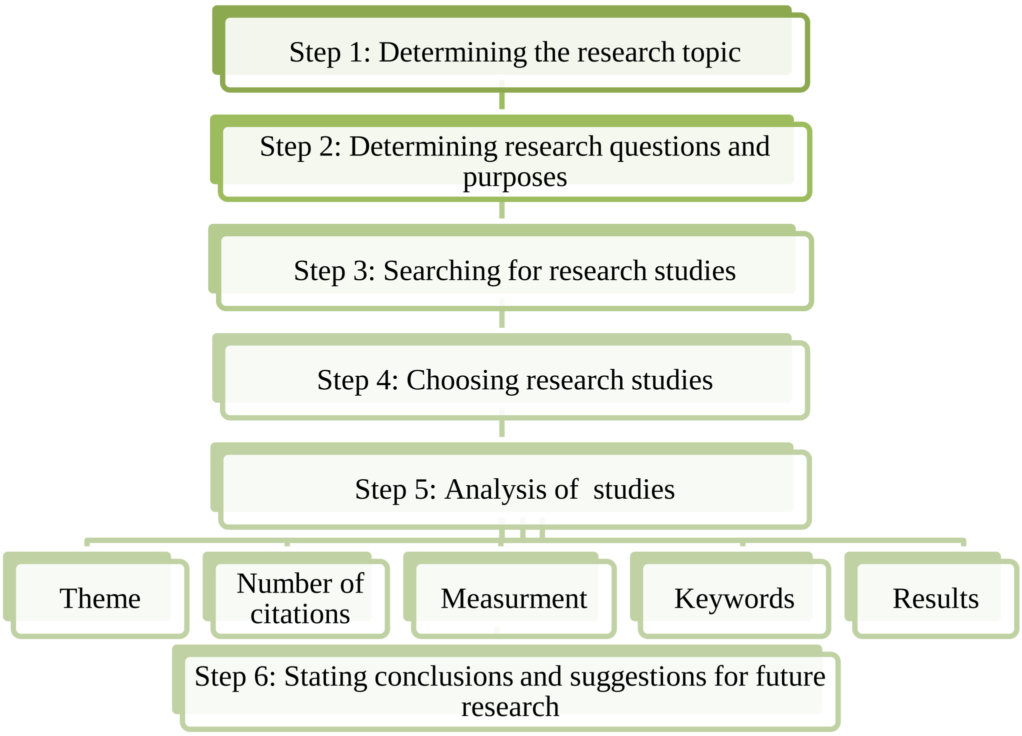

Figure 1. Process and steps of the systematic literature review

The first and second steps were discussed above in the introduction. Concerning the third and fourth steps, four keywords were used to search in the international scientific search engines to identify research studies on managerial ability published between 1990 and 2022 (see Table 1). The abstracts and the article texts were also examined to ensure the accuracy of searches and the relevance of the studies. In the fifth step, the text of the identified articles was analyzed and presented based on the thematic classification, number of citations, measurement models, keywords and results. In the sixth step, the conclusions and suggestions for future research were provided, considering the answers to the research questions. More details are provided in Table 1.

Table 1. The details of the research steps

Title	Details
Keywords	Managerial Ability Managerial Talent CEO Ability CEO Talent
Field of study	Accounting and Management
Search field	Title and keywords
Period	1990–2022
Search engine	www.sciencedirect.com www.emerald.com www.wiley.com www.aaahq.org www.springer.com
Classification basis	Content analysis of the obtained results as well as the analysis of their keywords

4. Analysis of Studies

We found 110 studies published between 1990 and 2022. The frequency of the research studies searched on www.scimagojr.com is presented in Table 2 according to the journal and the journal ranking.

Table 2. Frequency of the analyzed articles according to journals and their ranking

Journal title	Number of researches	Scientific journal ranking
Journal of Corporate Finance	6	Q1
Review of Quantitative Finance and Accounting	6	Q1
Journal of Contemporary Accounting & Economics	4	Q2
Advances in Accounting	4	Q2
The Accounting Review	3	Q1
Journal of Business Finance and Accounting	3	Q1
Journal of Business Research	3	Q1
Asia-Pacific Journal of Financial Studies	3	Q2
Asian Review of Accounting	2	Q2
Contemporary Accounting Research	2	Q1
Corporate Social Responsibility and Environmental Management	2	Q1
Global Finance Journal	2	Q2
International Journal of Auditing	2	Q1
International Journal of Emerging Markets	2	Q2
International Journal of Finance & Economics	2	Q2
International Journal of Productivity and Performance Management	2	Q2
International Review of Economics and Finance	2	Q2
Journal of Accounting, Auditing & Finance	2	Q2
Managerial and Decision Economics	2	Q3
Review of Accounting and Finance	2	Q3
Sustainability Accounting, Management and Policy Journal	2	Q2
The Journal of Finance	2	-
Other journals	50	Q1 to Q4
Total	**110**	**-**

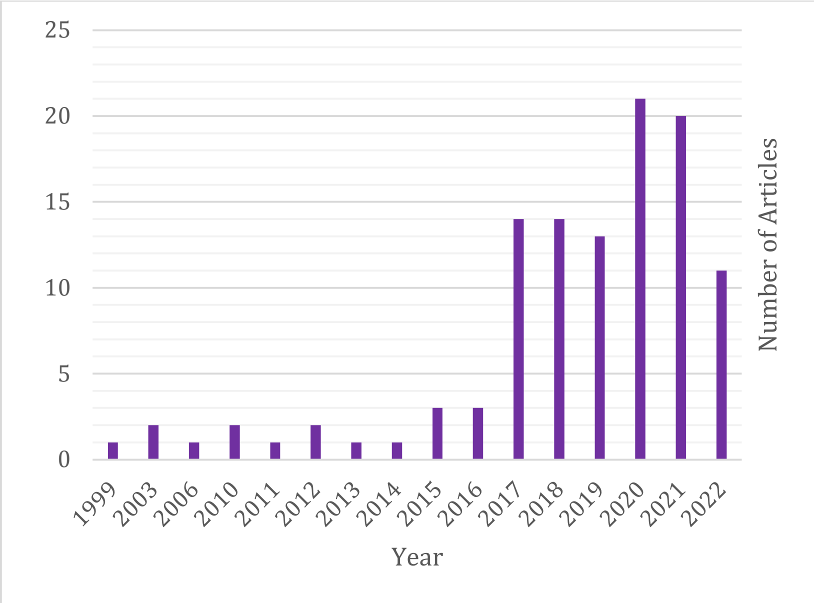

Figure 2. Frequency of the research in the field of managerial ability according to publication year

Figure 2 illustrates that the research conducted on managerial ability has grown significantly over the last 5 years. Only a few studies were done due to the belief in neoclassical economics. According to Bertrand and Schoar (2003), empirical studies were focused on concepts such as firm, industry and market factors until 2003, with only a few studies focusing on managers and their role in the firms. Furthermore, the studies in the management science field concentrated on analyzing factors affecting managerial decision-making, which were criticized for using non-economic variables and relying on laboratory experiments (Bertrand and Schoar, 2003). The lack of a model to measure managerial ability reliably is also one of the main reasons a few studies were done up to 2003. Researchers have favoured the model Demerjian et al. (2012) proposed recently due to its high applicability and operationalizability. This model had a tremendous effect on developing and implementing related studies. Despite the design of the measurement model in 2012, the impact of more-able managers on various research fields occurred with a delay. Only a few studies (10) addressed the issue during 2012–2017.

4.1 Theme

By examining the content of the results as well as keywords in the analyzed research studies, we classified 110 studies into 10 categories: performance, capital market, reporting quality, audit, investment, dividend policy and cash management, tax, corporate social responsibility, COVID-19, and miscellaneous. The frequency of the studies in each category is presented in Table 3. The largest number of studies were done in performance and capital market categories.

Table 3. Thematic frequency in the field of managerial ability

Thematic Category	Number of Studies
Performance	20
Capital market	23
Reporting quality	16
Investment	16
Audit	9
Corporate social responsibility	6
Dividend policy and cash management	6
Tax	4
Covid 19	6
Other	12
Total	**114***

*Some articles thematically belong to more than one category; therefore, the total number of the studies in this table is larger than the number of the reviewed ones (i.e., 110).

4.2 Number of citations

Based on Google Scholar, the number of citations is presented in Table 4.

Table 4. The number of citations

No.	Researcher(s)	Year	Number of citations
1	Bertrand and Scholar	2003	4.142
2	Kaplan et al.	2012	971
3	Demerjian et al.	2013	954
4	Milbourn	2003	739
5	Rajgopal et al.	2006	467
6	Baik et al	2011	453
7	Hayes and Schaefer	1999	276
8	Chang et al.	2010	269
9	Krishnan and Wang	2015	225
10	Lee et al.	2012	209
11	Wang et al.	2017	130
12	Chen et al.	2015	124
13	Demerjian et al.	2020	119
14	Mishra	2014	118
15	Andreou et al.	2017	117
16	Yuan et al.	2019	113
17	Huang and Sun	2017	107
18	Cornaggia et al.	2017	97
19	Habib and Hasan	2017	95
20	Andreou et al.	2016	79
21	Park et al.	2016	71
22	Baik et al.	2020	68
23	García-Meca and García-Sánchez	2018	67
24	Gul et al.	2018	64
25	Lee et al.	2018	63
26	Yung and Chen	2018	62
27	Choi et al.	2015	58
28	García-Sánchez and Martínez-Ferrero	2019	58
29	Sun	2016	57
30	De franco et al.	2017	52
31	Khurana et al.	2018	49
32	Cheung et al.	2017	48
33	Chemmanur et al.	2010	48

34	Abernathy et al.	2018	46
35	García-Sánchez et al.	2019	46
36	Bui et al.	2018	46
37	Baik et al.	2018	44
38	Gan	2019	41
39	García-Sánchez et al.	2020	40
40	Mitra et al.	2019	37
41	Fernando et al.	2020	36
42	Cui and Leung	2020	28
43	Akbari et al.	2019	25
44	Huang et al.	2017	23
45	Luo and Zhou	2017	21
46	Gan and Park	2017	20
47	Cheng et al.	2020	20
48	Phan et al.	2020	20
49	Petkevich and Prevost	2018	19
50	Hesarzadeh and Bazrafshan	2019	19
51	Doukas and Zhang	2020	19
52	Salehi et al.	2020	18
53	Haider et al.	2021	17
54	Akbari et al.	2018	17
55	Kumar and Zbib	2022	17
56	Jebran and Chen	2022	16
57	Li and Luo	2017	16
58	Cox	2017	16
59	Sun	2017	15
60	Chen et al.	2017	15
61	Cho et al.	2018	15
62	Uygur	2018	13
63	Berglund et al.	2018	12
64	Doukas and Zhang	2021	11
65	Gounopoulos et al.	2021	11
66	Oskouei and Sureshjani	2021	11
67	Dong and Doukas	2021	10
68	Sarwar et al.	2019	10
69	Salehi et al.	2019	10
70	Curi and vivas	2020	9
71	Chen et al.	2020	9
72	Mishra	2019	9
73	Yung and Nguyen	2020	8
74	Salehi et al.	2021	8
75	Safiullah et al.	2022	7
76	Khoo	2022	7
77	Lin et al.	2021	6
78	Ujah et al.	2021	6
79	Truong et al.	2020	5
80	Naheed et al.	2021	5
81	Cheng and Cheung	2021	4
82	Cao et al.	2019	4
83	Nadeem et al.	2021	4
84	Krishnan, Wang and Yu	2020	4
85	El Mahdy	2020	4
86	Gong et al.	2021	4
87	Abdesslem et al	2022	4
88	Shang	2021	3
89	Kim	2021	3
90	Bradley and sun	2021	3
91	Chen and Chen	2020	3
92	Harper et al.	2019	3

93	Magerakis	2022	3
94	Xu et al.	2021	2
95	Liu and Lei	2021	2
96	Yan et al.	2021	2
97	Wu et al.	2022	2
98	Driouchi et al.	2022	2
99	Cho et al.	2021	2
100	Wang et al.	2020	2
101	Khan et al	2022	2
102	Putra et al.	2021	1
103	Simamora	2021	1
104	Hwang et al.	2018	1
105	Gao et al.	2020	1
106	Westfall and Myring	2022	1
107	Biswas et al	2022	1
108	Mishra	2022	1
109	Fu et al	2022	0
110	Kim	2022	0

Table 4 demonstrates that rows 1 to 10 show studies with more than 200 citations.

4.3 Measurement

The analysis shows that the model proposed by Demerjian et al. (2012) is the most widely used model to measure managerial ability. This model indirectly measures managerial ability. According to this model, the firm's impact is distinct from the managerial impact and the contribution of the managerial impact on the corporate performance is known as managerial ability. This model initially calculates the firm efficiency using the Data Envelopment Analysis (DEA) technique. However, the calculated efficiency cannot entirely be attributed to managers. Therefore, the regression model is used in the next step. In this regression, efficiency is the dependent variable and the variables representing the firm’s effect are placed as independent variables. By implementing this regression model, the model's residual value is recognized as managerial ability (Demerjian et al., 2012).

Measuring managerial ability based on the executive experience of managers, the model proposed by Custódio et al. (2013) is another model. As a kind of general measurement model, the measurement of this model is not based on accounting structures. Another model is proposed by Bertrand and Schoar (2003), which is based on the extent to which the observed variation in firm policies can be attributed to managers' fixed effects. Since the managers' effects can be correlated with the effects of the firm, they constructed a panel data set that enabled them to track the top managers across different firms over time. This model has no generalizability due to the limited sample used (Demerjian and Lev, 2021). Multiple variables have also been used for measuring managerial ability, including industry-adjusted ROA (Return on Asset), industry-adjusted stock return, CEO press citations, and CEO compensation. Yet, these variables have limitations. For instance, achieving a higher (stocks or assets) return is also influenced by other factors in addition to managerial ability. Consequently, it does not seem plausible to attribute all the achieved excess returns to the managers. Furthermore, the size of the firms, the type of products they produce, the strategic nature of the products and environmental conditions as external factors influence the focus point of media and press. Compensation as a variable, determined based on firm performance, also includes factors beyond managers’ control. Therefore, compensation is not an accurate criterion for measuring managerial ability (Demerjian et al., 2012).

The point that we can learn from the evolution of the measurement of managerial ability over time is that prior to Demerjian et al. (2012) model, managerial ability was limited to some rudimentary measures. According to Demerjian and Lev (2021), some studies were forced to use "best company" lists reported in Fortune magazine, which are inherently subjective and often lack methodological transparency. Some studies also applied Bertrand and Schoar's (2003) model, which required managers to switch firms, which leads to small and idiosyncratic samples. After the development of the Demerjian et al. (2012) model, however, it has been accepted widely as an easily and broadly available measure of managerial ability. Managerial ability measurements have moved from variables that measure managerial ability directly (e.g., industry-adjusted ROA) toward models that measure managerial ability indirectly (the residual value of a regression model). The reasons that the indirect model has succeeded over the past decade probably include two main things: (1) increasing the variety of firm-related information in publicly available databases and, subsequently, (2) the popularity of statistical techniques among researchers. Demerjian and Lev (2021) argued that the managerial score is available for approximately 200,000 firm years from 1980 to 2016.

4.4 Keywords

As diagrams and shapes are more understandable, the analysis of keywords based on the frequency of use and their relationship with managerial ability is shown in Figure 3. The size of nodes in this figure indicates the frequency of the keywords used in the title or abstracts of the searched studies alongside managerial ability. Moreover, the density of the curves indicates the number of joint studies between each keyword and managerial ability.

As illustrated in Figure 3, managerial ability is highly studied in relation to firm performance, corporate governance, firm value, real earning management, and information asymmetry. As Demerjian and Lev (2021) argued, while on the surface, a direct and positive correlation between managerial ability and firm performance shows that characteristics of managers with high ability led to better firm performance, it can be reasoned that managers with superior ability use their skill opportunistically. These dual reasonings have led to contradictory results around managerial ability and firm performance relationships (e.g., Cheungh et al., 2017; Hwang et al., 2018). Therefore, it can be inferred that a high concentration of studies on the relationship between managerial ability and keywords like firm performance, corporate governance, firm value, real earning management and information asymmetry is probably due to the mentioned dual reasonings.

The density of curves in figure 3 also illustrates that only a few studies focused on the relationship between managerial ability and going concern, accounting conservatism and family firms, which provides a suitable road map for future research.

4.5 Results

As mentioned earlier, the studies were classified into 10 thematic categories. In this section, the results of each research will be presented based on each category. This section presents a variety of results around managerial ability that can be interesting and probably open up new avenues for future research.

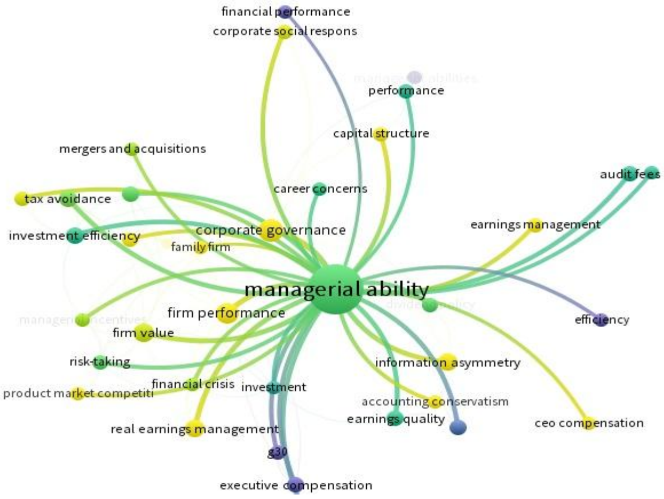

Figure 3. The use and link between managerial ability and keywords

4.5.1 Performance

It is presumed that there is a direct and positive relationship between managerial ability and the firm's performance. In other words, high-ability managers provide higher firm performance with foresight and a better understanding of economic activities and investment decisions (Demerjian and Lev, 2021). The results of Bertrand and Schoar (2003) showed that managers' styles and attitudes can influence constructive decisions (including research and development expenditures) and firm performance. By examining and identifying the manager-specific performance, they found that managers have about a 3% influence on Return on Assets (ROA). Khan et al. (2022) reveal that CEO management ability is positively related to sustainability performance. Chang et al. (2010) and Salehi et al. (2021) indicated that managerial ability influences firm performance. The relationship between managerial ability and firm performance can face a serious challenge when managers are opportunistic (Demerjian and Lev, 2021). Cheung et al. (2017) indicated that managerial ability improves performance only when accompanied by managerial discretion. A high level of managerial discretion requires examinations and supervision in the form of corporate governance structures. Hwang et al. (2018) showed that managerial ability in private firms causes an improvement in firm performance. However, opportunistic behaviors also exist in such firms without monitoring mechanisms.

Some studies have addressed the moderating role of managerial ability. Having investigated the moderating role of the CEO's ability regarding corporate social responsibility and performance, García-Sánchez and Martínez-Ferrero (2019) showed that managerial ability is important in protecting the shareholders' interests. Wang et al. (2020) proved that managerial ability influences the relationship between the asset-light strategy and firm performance in the Asian telecommunications industry. Cheng et al. (2020) indicated that the type of business strategy and general and specialized managerial ability are important success factors that influence firm performance. Phan et al. (2020) showed that managerial ability moderates the negative relationship between crude oil price uncertainty and firm performance.

A number of studies have addressed the role of managerial ability in the performance of acquired and merged firms. For example, Cui and Leung (2020) showed that acquired firms with higher managerial ability achieve higher long-term operating performance and stock returns. This issue is more obvious when the acquirer and the target firm belong to the same industry. To put simply, managers with high ability are more successful in creating synergy in same-industry firms. Doukas and Zhang (2020) showed that acquirers led by high-ability managers engage in more pre-acquisition earnings smoothing and experience more significant announcement abnormal returns and operating performance in post merge and acquisition periods than their low-ability counterparts. Dong and Doukas (2021) investigated the impact of managerial ability on mergers and acquisitions of US firms. After merging and acquiring, they showed a significant positive relationship between managerial ability and firm performance. Their findings also showed that managerial ability influences the identification and selection of target firms. Moreover, firms with strongly ingrained growth potential low financial constraints and bankruptcy risks are highly favoured by high-ability managers as targets. Xu et al. (2021) showed that the average impact of managerial ability on the likelihood of completing cross-border mergers and acquisitions is positive. Several studies also investigated the role and success of high-ability managers in the initial public offerings (Chemmanur et al., 2010; Cox, 2017; Gounopoulos et al., 2021).

Gender and managers' risk-taking are two important concepts researchers in managerial ability have considered. Fernando et al. (2020), by focusing on gender and managerial ability, showed that the presence of women at top levels of management not only has a positive effect on performance (in times of stability and crisis) but also on the enhancement of managerial abilities. Moreover, managerial ability has a high moderating role in the relationship between gender diversity and firm performance. Addressing the simultaneous effects of managerial ability and risk-taking, Simamora (2021) concluded that managerial ability and a manager’s risk-taking behavior improve firm performance.

4.5.2 Capital market

Various managerial ability studies have been conducted related to capital markets, which can be classified into the stock and debt markets. Some studies focused on the market’s reaction to the turnovers of high-ability managers. This reaction shows that the market recognizes managerial ability. Hayes and Shaffer (1999) investigated the negative stock price reaction to high-ability managers’ turnovers. Their research results indicated that firms' market value changes ranging from 12.6 to 53.3 million dollars due to high-ability managers’ turnovers. Considering the market’s reaction to CEO turnover as a test of their designed model, Demerjian et al. (2012) found that the market reaction accompanies these changes. Cho et al. (2021) refer to the market perceptions of high-ability managers. They showed that the market value of firms would not be adjusted for firms with high-ability managers and firms with deviations from the target capital structure.

Some studies also investigated the tone of managers with high-ability in earnings announcements and its impact on the stock market. For instance, Luo and Zhou (2017) showed that more-able managers use a positive tone in their earnings announcements. Furthermore, the stock market reacts positively to this type of announcement. According to Yan et al. (2021), managers with low ability manipulate the tone of the earnings announcements and firm disclosures to avoid losing their labour market—the stance faced with a negative market reaction. Fu et al. (2022) found a negative relationship between managerial ability and stock price synchronicity. Kim (2022) revealed that the quality of non-GAAP earnings is greater for high-ability managers than for low-ability managers.

Other studies concentrated on the impact of managerial ability on the information environment. Baik et al. (2018) showed that highly capable managers impact the quality of a firm’s information environment. In addition, managers’ equity incentives can improve the quality of the information environment. According to the findings of Chen et al. (2020), managerial ability can reduce the negative impact of uncertainty in macro-political and economic environments on analysts’ forecasts. The research conducted by Gao et al. (2020) indicated that financial analysts are attracted to firms with highly-skilled managers so that they can provide more accurate forecasts. Cao et al.

(2019) showed that open market repurchase program completion rates increase with managerial ability and that the quality of management earnings forecasts further moderates the association. Habib and Hasan (2017) indicated that more-able managers lead to future stock price crash risk through over-investing. According to Liu and Lei (2021), managerial ability is positively associated with stock price crash risk only when managerial overconfidence is high.

Among studies in the debt market category, Petkevich and Prevost (2018) concluded that managerial ability improves the information environment and reduces risk and information asymmetry. Other studies investigated the effect of managerial ability on firms' credit risk and loan terms. Cornaggia et al. (2017) and Harper et al. (2019) indicated that more-able managers are considered positive factors for measuring firms’ credit ratings. High-ability managers will improve firms' credit ratings. According to Chen et al. (2017), managerial ability increases credit ratings but decreases credit risk. Several studies investigated the effect of managerial ability on negotiation about loan terms, such as maturity date. For instance, De Franco et al. (2017) concluded that higher managerial ability is associated with lower bank-loan prices. Bui et al. (2018) found that firms with high-ability managers are more likely to continue their prior lower loan spread. The spread-reduction effect of managerial ability is stronger for firms with weak governance structures or poor stakeholder relationships, corroborating the notion that better managerial ability alleviates borrowers’ agency and information risks. Shang (2021) showed the effect of managerial ability on debt maturity. Specifically, high-ability managers prefer short-term debt, amplified for firms with greater growth opportunities and attenuated for firms with refinancing risk. Abdesslem et al. (2022) revealed that both risks significantly affect the likelihood of bank default and that the high skill of managers does not attenuate this effect. Khoo (2022) documents that firms with highly capable managers are associated with more short-term debt financing.

4.5.3 Reporting quality

Two viewpoints have emerged from studies in this category. First, high-ability managers improve reporting quality. Second, the reporting quality of high-ability managers is low. Most of the studies are in line with the first point of view. According to the first view, García-Meca and García-Sánchez (2018) and Krishnan, Wang and Yu (2021) showed that high-ability managers are less engaged with opportunistic financial reporting. Demerjian et al. (2013) investigated managerial ability and earnings quality. The results of their research indicated that managerial ability is associated with fewer subsequent restatements, higher earnings, accruals persistence and lower errors in bad debt provision. Moreover, more-able managers can estimate accruals more accurately. The research findings of Huang and Sun (2017) indicated that higher-ability managers use less real earnings management and reduce the negative impact of earnings management on future firm performance. According to Oskouei and Sureshjani (2021), managers with higher abilities use less real earnings management in crisis conditions. Putra et al. (2021) found that managers with higher abilities in family firms engage less in real earnings management. Choi et al. (2015) revealed the significance of managerial ability in the informativeness of current accruals for future cash flows. Baik et al. (2020) found that managerial ability positively affects income smoothing. Moreover, the earnings informativeness and stock price are higher in firms with highly capable managers. Wang et al. (2017) investigated the relationship between managerial ability, political connections and financial reporting fraud. The results of their research showed that managerial ability reduces financial reporting fraud. Furthermore, this relationship is stronger in firms without political connections. Abernathy et al. (2018) showed a positive effect of managerial ability on financial reporting timeliness. Uygur (2018) and Wu et al. (2022) concluded that higher-ability managers have higher information transparency. According to Bradley and Sun (2021), there is a positive relationship between managerial ability and Level 1 and Level 2 fair value inputs usage.

In the second point of view, Demerjian et al. (2020) suggested that more-able managers use intentional income smoothing. Intentional income smoothing directly relates to firms' future performance, which can benefit both the manager and the shareholders. Gul et al. (2018) found that more-able managers in financial distress situations present low-quality accruals and high restatements.

4.5.4 Audit

The main focus of studies in this category is the relationship between managerial ability and audit fees. For example, Krishnan and Wang (2015) indicated that managerial ability influences audit fees. Simply put, it is justified that auditors' risk is reduced by reducing the risk of bankruptcy or improving the quality of information; therefore, conditions for reducing the audit fee are provided. Extending the work done by Krishnan and Wang (2015), Li and Luo (2017) showed a non-linear relationship between managerial ability and audit fees. They believed that factors such as litigation risk, the post-Sarbanes–Oxley Act (SOX) era and the auditor's familiarity with the manager impacted this relationship. Salehi et al. (2019) found a significant positive relationship between managerial ability and the quality of internal controls, but they observed a negative relationship between managerial ability and audit fees. Inferring a negative relationship between managerial ability and audit fee may change according to the conditions of each firm. Gul et al. (2018) observed a positive relationship between managerial ability and the auditor fee in financially distressed firms, which is caused by the opportunistic financial reporting of managers, hence an increase in audit risk. Following a different method, Berglund et al. (2018) showed that managerial ability decreases the risk of Type I errors in auditing and increases the risk of Type II errors. Westfall and Myring (2022) find that IPO registrants with higher managerial ability are more likely to disclose internal control weaknesses voluntarily than other registrants.

Some studies refer to the moderating role of managerial ability. Mitra et al. (2019) showed that the positive relationship between managerial overconfidence and audit fees is moderated by managerial ability. According to Truong et al. (2020), managerial ability moderates the relationship between political alignment and audit pricing. Kim (2021) showed that overconfident and incompetent managers are more likely to receive an opinion related to the going concern.

4.5.5 Investment

In this category, some studies addressed the attitude and behavior of high-ability managers regarding capital expenditures and research and development expenses. According to Yung and Chen (2018), high-ability managers take higher risks, cut capital expenditures and increase research and development expenses and firm value. Chen and Chen (2020) showed that managers with high ability make more accurate estimates of capital expenditures. Yung and Nguyen (2020) suggested that managerial ability is positively associated with market share growth. Moreover, managers who face competitive threats concentrate on research and development rather than capital expenditures.

A number of studies investigated the relationship between managerial ability and investment efficiency/inefficiency. Investment efficiency is achieved when a firm only invests in positive net present value projects. Since the markets are not complete in terms of efficiency, investment inefficiency which probably is reduced by managerial ability, is possible. However, the results of the studies in this area are incompatible. For example, Habib and Hassan (2017) demonstrated that high-ability managers create investment inefficiency by over-investment. Andreou et al. (2017) revealed that managers with a high ability to mitigate under-investment problems during a crisis increase firm value. According to Khurana et al. (2018), firms with high managerial ability exhibit higher tax avoidance and investment efficiency. Gan (2019) showed that the decisions of high-ability managers enhance investment efficiency. On the other hand, Salehi et al. (2020) showed no relationship between managerial ability, investment efficiency and risk taking. Naheed et al. (2021) found that managerial ability influences investment decisions in both favourable and unfavourable financial conditions.

Several studies focused on the relationship between managerial ability, investment opportunities and innovative activities. Chen et al. (2015) suggested that managerial ability is positively associated with innovative activities, followed by the capital market's positive reaction. Lee et al. (2018) showed a positive relationship between managerial ability and investment opportunities in firms with strong financial positions and those with financial constraints. Mishra (2019) suggested that innovative activities in firms are associated with strategic and operational managerial ability. According to Driouchi et al. (2022), there is a positive relationship between managerial ability and growth opportunities. A number of studies examined the relationship between managerial ability and a specific area of investment. For example, Ujah et al. (2021) found a positive relationship between managerial ability and working capital management. Finally, Nadeem et al. (2021) indicated a significant positive relationship between managerial ability and intellectual capital.

4.5.6 Dividend policies and cash management

Magerakis (2022) examined the role of managerial discretion in the relation between managerial ability and the level of corporate cash. Their findings revealed that the positive association between the ability of chief executive officers and corporate cash savings is weakened by firm-level managerial discretion. Gan and Park (2017) investigated managerial ability and the marginal value of cash. Their study showed that managerial ability significantly increases the marginal value of cash and free cash flow. They also found that the effect of managerial ability on the marginal value of cash is generally greater for firms with stronger corporate governance and financial constraints. Cho et al. (2018) found that managerial ability is negatively related to the adjustment speed of cash holdings toward the target, particularly when the firm has excess cash. Sarwar et al. (2019) considered a positive relationship between managers' ability and dividend payouts to be influenced by factors such as a firm's ownership, financial constrain and emerging markets. Safiullah et al. (2022) and Andreou et al. (2016) showed that the ability of Islamic bank managers and Shariah supervisory board governance increase cash flows and liquidity of banks.

4.5.7 Tax

Considered an important strategy in firms, tax avoidance is strongly influenced by managers' viewpoints. Park et al. (2016) showed that the relationship between managerial ability and tax avoidance is negative, which Akbari et al. (2018) did not confirm in Tehran Stock Exchange and the Over-the-counter market. Some studies were concerned with the moderating role of managerial ability. According to Akbari et al. (2019), managers' ability has a moderating role in the negative relationship between tax avoidance and firm value. Huang et al. (2017) also indicated that managerial ability moderates the positive relationship between environmental uncertainty and tax avoidance.

4.5.8 Corporate social responsibility

Sun (2017) showed that more-able managers consider environmental risks. According to Yuan et al. (2019), a positive relationship exists between social responsibility and managerial ability. Gong et al. (2021) found that managerial ability impacts corporate social responsibility and firm performance in the energy industry. García-Sánchez et al. (2019) found that focusing on corporate governance mechanisms can be a more suitable alternative for less able managers to improve corporate social responsibility. García-Sánchez et al. (2020) showed that managerial ability, directly and indirectly, affects corporate social responsibility information disclosure. Doukas and Zhang (2021) indicated that in acquired firms, more talented managers significantly shape corporate social culture among US firms. These firms were more inclined to engage in corporate social responsibility activities.

4.5.9 COVID-19

After 2019 and the outbreak of COVID worldwide, some researchers have focused on its effect on managerial ability. Jebran and Chen (2022) showed that firms with higher ability managers reduce their investments, financing, and cash holdings yet increase their dividend payouts during the COVID-19 crisis. Kumar and Zbib (2022) also found a positive and significant association between the CEO's managerial ability and cumulative raw and abnormal returns.

4.5.10 Miscellaneous

Sun (2016) found a negative relationship between managerial ability and goodwill impairment. Hesarzadeh and Bazrafshan (2019) showed a negative relationship between managerial ability and regulatory review risk, which is not economically significant. The agency costs and quality of corporate governance mechanisms also influence this relationship. Lee et al. (2012) concluded that the accuracy of management forecasts can be used as an alternative measure of managerial ability. Moreover, CEO turnover is positively related to the magnitude of absolute forecast errors when the firm performance is weak. El Mahdy (2020) revealed that higher-ability managers voluntarily adopt the clawback rule. According to Haider et al. (2021), high ability managers use accounting conservatism to preserve stakeholders' interests. Lin et al. (2021) indicated that firms directed by inventor managers with greater general abilities provide more innovations that fit product market needs. Cheng and Cheung (2021) indicated that managerial ability positively moderates the negative relationship between using derivatives and firm risk. In addition, this positive moderating effect is stronger in firms with weak monitoring, dispersed ownership, weak corporate governance and high information asymmetry. Biswas et al. (2022) examined whether managerial ability moderates the association between product market competition and real earnings management. They argued that this association is different depending on the level of managerial ability and that able managers negatively moderate the association between competition and real activity manipulation. Mishra (2022) found the strategic ability positively influences exploration and exploitation activities, while operational ability positively influences exploitation activities but negatively influences exploration activities unless the managers are provided high risk incentives.

Concerning the bank industry, several studies illustrated that managers with high abilities affect banks' risk-taking levels (Andreou et al., 2016; Curi and Vivas, 2020).

5. Conclusion and Further to the Study

In recent years, the role of managers in firms and their influence has been challenged by numerous studies (Bertrand and Schoar, 2003; Demerjian et al., 2012; Andreou et al., 2017; Demerjian and Lev, 2021; Jebran and Chen, 2022; Kumar and Zbib, 2022; Kim: 2022). Among managers' measurable characteristics, a large extent of related literature is dedicated to managerial ability. The international scientific search engines were searched to identify the studies published between 1990 and 2022 (110 studies). Studies have shown that many were implemented over the last six years, during 2017–2022. The analysis revealed that a large part of studies focused on the relationship between managerial ability and corporate governance, firm performance and firm value. Furthermore, content analysis classified related studies into 10 categories: performance, capital market, reporting quality, audit, investment, dividend policies and cash management, tax, corporate social responsibility, COVID-19 and miscellaneous. The summary of the results of each category was then presented separately. The analysis also revealed that the largest number of studies (43) has concentrated on the relationship between managerial ability, firm performance and capital market. The methods used in the studies were also examined in each category and research gaps were identified for future studies.

Various topics have been investigated around the relationship between firm performance and managerial ability. Most studies used the Demerjian et al. (2012) model to measure managerial ability. Given that managerial ability through the Demerjian et al. (2012) model is derived from firm performance figures, it is not appropriate to use this model to test the relationship between managerial ability and firm performance or the moderating role of managerial ability in this field. We suggest that researchers use other variables and models to measure managerial ability to examine related topics.

In another category, studies have considered the importance of markets' understanding of managerial ability. Further studies can concentrate on the length of time that it takes for the market to recognize managers with high abilities. Most related studies around the debt market focused on managerial ability's impact on reducing credit risk, increasing credit ratings and facilitating loan terms. Future research can investigate the effects of high-ability managers in reducing credit risk and raising credit in firms with financial constraints.

Most studies in the reporting quality category showed that managers with higher ability use less real earnings management. The current accruals they report have higher informativeness for estimating future cash flows. As mentioned earlier, the majority of studies used the Demerjian et al. (2012) model to measure managerial ability. This is while earnings management effects are not included in this model. So, the effects related to earnings management exist in measured managerial ability via the Demerjian et al. (2012) model. Hence, investigating the relationship between managerial ability measured via this model and earnings management and income smoothing includes statistical errors. Future research can be directed toward designing a model to measure managerial ability considering the effects of earnings management.

The studies addressed the relationship between managerial ability and audit fees in the audit category. Future research can investigate the effect of factors such as corporate governance mechanisms, managers' myopia, managers' risk-taking and the firm's life cycle on the relationship between managerial ability and audit fees and audit reports.

The research results in the investment category depend on two basic factors: market efficiency and managers' characteristics and traits. Studies can be followed in markets with different levels of efficiency. Factors like managers' political connections, tenure, industry and myopic behaviors probably influence the relationship between managerial ability and investment.

Investigating the role of managerial ability in different dividend policy theories in the dividend policies and cash management category can provide different results.

Research has focused on tax avoidance and its relationship with managerial ability in the tax category. Applying Schwab et al. (۲۰۲۲) model to measure effective tax planning and investigating its relationship with managerial ability is probably the new direction for future research.

The concept of culture and the rules and regulations of different countries suggest new topics for future research in corporate social responsibility. A comparative study in several countries with different cultures and regulations can be attractive. Moreover, factors such as management tenure and industry can influence the relationship between managerial ability and corporate social responsibility based on their effects on society.

Studies in the COVID-19 category signal that economic, political, and social challenges can affect future studies around managerial ability. For instance, as Russia's War Against Ukraine may affect the economies of other countries, investigating the role of high-ability managers in such a condition can be attractive. Table 5 summarizes suggestions related to each category for future research.

Table 5. Summary of the study

No.	Category	Suggestions
1	performance	Studying the relationship between managerial ability and firm performance via other variables and models to measure managerial ability because Demerjian et al. (2012) model derives managerial ability measure from firm performance
2	capital market	Studying the length of time that it takes for the market to recognize managers with high abilities
3	reporting quality	Adjusting Demerjian et al. (2012) model to measure managerial ability considering the effects of earnings management
4	audit	Studying managerial ability with Audit fees and the moderator role of factors like corporate governance mechanisms, managers' myopia, managers' risk-taking and the firm's life cycle
5	investment	Studying managerial ability in markets with different levels of efficiency
6	dividend policy and cash management	Studying managerial ability with different theories of dividend policy
7	tax	Studying managerial ability with effective tax planning, which is measured with Schwab et al. (۲۰۲۲) model
8	corporate social responsibility	Studying managerial ability in several countries with different cultures and regulations comparatively
9	COVID-19	Studying managerial ability similar crises like Russia's War Against Ukraine

In the current review, we found that although multiple studies used models proposed by Custódio et al. (2013) and Bertrand and Schoar (2003) and variables such as industry-adjusted ROA (Return on Asset), industry-adjusted stock return, CEO press citations and compensation to measure managerial ability, Demerjian et al. (2012) was found to be the most frequently used model in reviewed studies. According to Demerjian and Lev (2021), the primary goal of the output variable designed in the first stage of the model was to find a general variable that would influence the result of all managerial decisions and attitudes. It can be useful and effective to develop different models from the point of view of majority and minority shareholders or even creditors. It is also possible to improve the model through different methods of grouping firms (e.g., grouping firms based on year-industry instead of industry) and compare the results with the original model.

We confront two main limitations in the current study. First, we may not have searched other keywords in international academic search engines. Second, most studies have been published in accounting and management journals. The journals in other disciplines may include more related studies.

Declaration of interest

The authors report there are no competing interests to declare.

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