

# Nicely Dressed: Earnings Management of Private Banking Providers in Switzerland

**Master's Thesis**  
supervised by the

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Prof. Dr. Urs Birchler

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Author: Monika Silvia Egli  
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## **Executive Summary**

During the last decade the banking industry has been faced with challenges. While the early 2000s were booming years for the Swiss banking industry, the financial crisis of 2007 – 2009 was the start of a more difficult phase. Also Swiss private banking providers feel the pressure. As they work with a sensitive customer base, their reputation is crucial. Financial statements thereby have a signaling effect which can fuel the incentive to manage the numbers so that they can be presented in a favorable way.

Earnings management, deliberate actions of management to alter earnings, offers the possibility to illustrate accounting figures in the wanted fashion without violating accounting regulations. If a accounting positions offers areas of discretion as for example estimates need to be used management can use them to actively fit numbers for their purposes.

The goal of this master thesis is to analyze if Swiss private banking providers manage their earnings. Thereby, the position of extraordinary items (net position of extraordinary revenues and extraordinary expenses) is analyzed as the position with which management is assumed to manage earnings.

For the examination of the general hypothesis, different methodologies are used. Descriptive statistics give a first insight on the main accounting figures of the analysis. The distribution of earnings before extraordinary items and net profit give an indication that banks are shifting earnings upwards to avoid small losses.

By formulating hypotheses based on the three main characteristics of earnings management - target accounting, big bath accounting and income smoothing - the influence of these on the amount of extraordinary items is tested using mean comparison and Wilcoxon ranksum tests. Thereby, hypothesis of reaching and beating of benchmarks can be supported.

Additionally, it is tested if the financial crisis has a relevant impact on the amount of extraordinary items. While the hypothesis is supported looking at mean and median values before, during and after the financial crisis, the regression analysis shows a non-significant

influence. The regression analysis show that other variables like depreciation and allowance, have a high explanatory power concerning extraordinary items.

The methodologies used to analyze the data are based on earlier research designs, particularly ? and ?, yet are adapted to fit the available data and the positions analyzed. As both the data and the analyzed figure of extraordinary items are relatively unique to the research of earnings management, a direct comparison to former research and generalization to other banks or industries are not reasonable.

Overall, the general hypothesis can not be answered conclusively. While there are several indications that private banks use extraordinary items to manage earnings, further analysis would be needed to come to a definite conclusions. Especially for the regression analysis more data, mainly balance sheet data, would be necessary to control for different influences like risk or economical environment and to come to confident findings.