

The Impact of the Information of Management Forecast Achievement on Japanese Investors' Decision-Making

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Abstract

A company announces financial results to investors and analysts and discloses information on the status of its operating results and financial performance. Therefore, announcements of financial results are important for investors and analysts in making investment decisions. In the financial results announcement, the company reports its performance for the current period (including the details of performance and the financial situation during the period) and announces the earnings forecast by the company's management (referred to as the management forecast). Management forecasts are particularly important for investors' decision-making because they are published by managers who hold inside information.

A previous study tested the counting heuristic in an experimental study of MBA students. The counting heuristic is the theory that investors make investment decisions based on the number of times analyst EPS estimates are achieved, rather than on earnings surprises. The performance surprise is the difference between the actual EPS and the analysts' forecast EPS. Their results showed that the number of times analysts achieved EPS estimates had a strong influence on investors' decisions.

The purpose of this study is to clarify how information on earnings surprises and the number of times management-forecast EPS are achieved affects investors' investment decisions when analyst forecast EPS is changed to management-forecast EPS. We hypothesize that given information on earnings surprises and the number of times management forecasts are achieved, investors will give more weight to information on the number of times management forecasts are achieved compared to earnings surprises in assessing (a) the common stock valuation of the firm, (b) the desirability of the firm (as an investment), (c) the future prospects of the firm, (d) the competence of management, and (e) trustworthiness of management. An internet experiment was then conducted with Japanese investors.

First, the hypotheses were partially supported by the results on stock evaluation and managerial competence, as the results tended to focus on the number of times management forecasts were achieved rather than performance surprises. The results on corporate desirability and future prospects showed equal importance in the number of achievements and performance surprises. These results did not support the hypotheses. Finally, the reliability results showed that the number of times management forecasts were achieved was more important than performance surprises, and the hypothesis was supported. Therefore, it is important for firms to achieve management-forecast EPS to increase their common stock valuation, management competence, and trustworthiness. It is also important for firms to focus on achieving and significantly exceeding management forecasts to increase the desirability of the firm as an investment and the future prospects of each firm.

Keywords

management forecast achievement, investors' decision-making, experimental study, counting heuristic theory, management-forecast EPS

Biographies

Kaori Ojima is a graduate student of the Department of Industrial Engineering and Management at Kanagawa University, Japan.

Ayuko Komura is an assistant professor in the Department of Industrial Engineering and Management at Kanagawa University, Japan. Her research topics include operating profit stability and management controls. She earned her Ph.D. in business administration at Meiji University. She received a fellowship from the Japan Society for the Promotion of Science between 2017 and 2019.

Hirohisa Hirai is a professor in the Department of Industrial Engineering and Management at Kanagawa University, Japan. He earned his Ph.D. in Engineering at Osaka University. His research is an empirical study of management accounting, firm analysis, and applied statistics, particularly firm valuation. He received awards from several academic societies in accounting and management.