

# **Impact of Trends in Actual EPS and Achievement of Management's Forecasts on Investors' Decision-Making**

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## **Abstract**

Most Japanese listed companies announce earnings forecasts by the CEOs (referred to as 'management forecasts'). Management forecasts are particularly important for investors' decision-making because they are published by managers with inside information. What heuristic decisions do investors make when management forecasts are used? Prior studies examined the decisions of investors who received information on the five-year management forecast EPS achievement rate and five-year earnings surprise (management forecast EPS–actual EPS). However, the trend status of the actual EPS and management forecasted EPS has not been studied. Therefore, in this study, we conducted a 4×3 online experiment on the 4 types of trend status of the 3 periods of 'always increasing', 'always decreasing', 'down then up', or 'up then down', and 3 types of final year achievement status: achieved, not achieved, and not stated. The participants were 600 Japanese stock investors asked to evaluate stock valuation, prospects, reliability, and EPS for the next period to test how they make heuristic judgments. The ANOVA results show that judgments were made by looking at the trend only ( $p < .001$ ) for stock valuation, prospects, trustworthiness, and EPS for the next period. It was also evident that decisions based on the management's EPS forecast achievement ( $p < .07$ ) were made only on a decreasing trend. These results suggest that management should emphasise the trend when the actual EPS is upward and show the achievement status when it is downward for investors to perceive their company as an attractive investment target.

## **Keywords**

management forecast, stock valuation, trustworthiness, actual EPS trends, and management forecast achievement

## **Biographies**

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