

# Implications of Past Forecasting Errors Often Underestimated

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(PhysOrg.com) -- When managers issue a forecast of their firm's earnings, they do not always take into account prior forecasting errors, according to research in the current issue of the Journal of Business Finance & Accounting.

Weihong Xu, assistant professor of [accounting](#) in the University at Buffalo School of Management, analyzed more than 11,000 firm-quarter observations. She found that managers often underestimate the implications of their past forecasting errors when forecasting earnings.

This underestimation of past errors can affect how the market responds to a new earnings forecast. Specifically, it can contribute to "post-earnings announcement drift;" that is, stock prices continue to drift in the direction of the initial price response to an earnings announcement.

"Managers underestimate the information in their prior [forecast](#) errors to a greater extent when they make [earnings](#) forecasts with a longer horizon," Xu says.

A copy of the study is available [here](#).

She notes that further study is needed to see if the underestimation is intentional on the part of management in order to provide biased forecasts.

Provided by University at Buffalo ([news](#) : [web](#))

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