ANALYST FORECAST ACCURACY ON GAAP VS. NON-GAAP FINANCIAL MEASURES: CASE OF REAL ESTATE INVESTMENT TRUSTS

The Real Estate Investment Trust (REIT) industry extensively reports an industry standardized, non-GAAP summary performance measure, Funds From Operations (FFO), as an alternative to net income. In this study, we explore analysts’ relative forecasting ability for FFO and earnings per share (EPS) and contribute to the debate over the usefulness and reliability of non-GAAP performance measures. Contrary to expectation that the heavily regulated GAAP measures are more reliable and more easily understood, we find that analysts are more effective at forecasting FFO than net income. Their forecast errors for EPS are larger than their forecast errors for FFO. We then explore the determinants of these forecast errors and find that forecast errors become larger when managers have more incentives to manipulate a performance measure, when analysts exert larger optimism biases, and when analyst coverage is less extensive.