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HOW DO BROKERS' EQUITY ANALYSTS COMPETE?
PERCEPTIONS OF THE SOURCES OF SUCCESS

BY

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How Do Brokers' Equity Analysts Compete?

Perceptions of the Sources of Success

Abstract: *This exploratory study considers the nature and sources of success for brokers' equity analysts in the UK. A conceptual model of success is derived from semi-structured interviews internet questionnaire. For the analyst, success is position in published ratings, based on investor and company management surveys, as well as mandates for new share issues, mergers and acquisitions. Analysts' management of stakeholder relationships, and inevitable conflicts of interest, is found to be the richest source of this success.*

Introduction

The importance of equity analysts is evinced by their ability to move markets (c.f. Bulkeley and Harris, 1997), and being fundamental to equity market efficiency (c.f. Fama, 1970). However, in recent times they have attracted negative attention from the press. Analysts “...*have fallen from grace...*” and are accused of “...*crossing the line towards trying to please companies.*” (Financial Times 10th April 2001). “*Everyone these days, Congress included, likes to bash the share analysts at Wall Street’s big investment banks for their shoddy or conflicted investment research*” (Economist 7th July 2001). The analysts’ role has come under increasingly critical scrutiny, particularly focusing upon supposedly damaging conflicts of interest. This study examines what constitutes success (and therefore failure), and its attainment, for the analyst.

Prior discussions of analysts skirt the issue of how one analyst gains advantage over another. The literature is rich in discussion of their uses of accounting data, and valuation techniques, forecast accuracy, and possible links to stock market efficiency and share price volatility. It is strong in accounting and financially based quantitative analysis of analysts at an aggregated level. It largely omits the social or commercial forces on analysts that might cause them bias or conflict of interest.

This paper sheds light on how equity analysts compete and thereby explores the sources of their success. This requires insight to what equity analysts do, how they do it, who they influence and who influences them; a picture more comprehensive than developed in most prior research. This paper is a step towards a more agent-centric and qualitative view. It attempts to create an integrative and characteristic account of analysts, from which such reported phenomena as conflict or bias can be viewed afresh.

We begin the paper by reviewing extant studies on analysts that show significant attention has been applied to financial processes and outcomes. However, past studies lack regard to activities beyond the formal role of financial analysis. In addressing this gap in the literature, we selected a dual methodology. This allowed an inductive approach to analysts’ perceptions of success and its sources, which we were then able

to test by means of questionnaire. From our results we developed a performance model. The paper concludes with discussion of the importance of stakeholder relationships to analysts' success and suggests future research directions.

Prior research on analysts

This section initially discusses research of analysts' use of accounting material and valuation methodologies. It next reviews literature of analysts' forecast accuracy and supposed bias, before addressing the more theoretically based work on market efficiency and the hypothesised underlying rationality of market participants. Finally, there is discussion of less common research that develops the analysts' role beyond its assumed, direct relationship to equity price determination.

The literature on analysts has largely focused upon analysts' function in forecasting earnings per share (eps). These studies are concerned with quantitative analysis of stock market dynamics, or analysts' sources and use of accounting and other data. The question of fashioning advantage via means other than improved forecast accuracy remains largely untried. Moreover, the literature has rarely discussed the significance of forecast accuracy. This appears to derive from a dominant conception of analysts as engaged in rationally estimating the changing values of equities. In this view, accuracy is the very purpose of their existence.

The literature on analysts' uses of accounting data and valuation techniques is rich and consistent in finding that PE (price to earnings) ratios are most common (c.f. Govindarajan, 1980; Lee and Tweedie, 1981; Arnold and Mozier, 1984; Previts et al ,1994; Yap, 1997). More complex valuation models, such as discounted cash flows or beta analysis, have been little used (Arnold and Mozier, 1998; Pike et al, 1993; and Vergoossen, 1993). These authors also find that analysts are more likely to perform detailed analysis on fewer stocks than Fund Managers (FMs), although all market participants show similar use of valuation techniques and data sources. Indeed, both Lee and Tweedie (1981), and Breton and Taffler (1995), question the refinement of market participants' use of accounting material.

Olsen (1996) finds that, “...*earnings forecasts have been positively biased and quite inaccurate – human need is to seek consensus...*” This is argued to result in abnormally low returns for stocks with more uncertain earnings streams. The theme of analysts’ forecast inaccuracy is common, with De Bondt and Thaler (1990), Dreman and Berry (1995) and, in rebuttal, Brown (1996), being three examples. The formers’ contention that analysts overreact to market events in their forecasts has relevance to Bulkley and Harris (1997), who find that “*excess volatility of stock prices may be due in part to a failure of the market to form rational expectations.*” McNichols and O’Brien (1996) take up the cause of explaining the analyst over-optimism argued in Darlin (1983) for instance. They find that analysts tend to add firms to their research coverage that they view favourably, and drop firms they view unfavourably, and that this is at least a partial explanation for analysts’ forecasts being generally over-optimistic relative to the market.

We next extend the themes of analysts’ uses of accounting and financial information, forecast accuracy and bias, into discussion of market efficiency and the underlying assumption of the rationality of market agents. There are three salient theoretical studies. Fama (1970) presented a trichotomous model of market efficiency. It serves to emphasise the dependency of market efficiency upon grades of informational efficiency. This foundation was built upon by Grossman and Stiglitz (1980), who hold that because market information (from those such as analysts) is, “...*costly, prices cannot perfectly reflect the information which is available, since if it did, those who spent resources to obtain it would receive no compensation. There is a fundamental conflict between the efficiency with which markets spread information and the incentives to acquire information.*” Moreover, the value of such market information is asserted to diminish with an increasing number of people in possession of it, because the resulting asset price changes provide in themselves information to those who have not made the purchase. Thus an “equilibrium” point is created at which market participants’ incentives act to maintain disequilibrium of their levels of information. In this way, informationally efficient markets are implausible. In contrast, DeMarzo et al (1997), create an algebraic model of persuasion in which agents (such as Fund Managers) overweight the information of individuals they “listen to” (such as favoured analysts). Agents can be described as acting rationally according to a misspecified model of the world – or “near-rationally”. The model incorporates types

of agent, and their changing influences upon one another, as well as quantified benefits from interaction. The authors demonstrate that market participants can profit from being influential as well as accurate.

Moving finally to more detailed discussion of the analysts' function, Barker (1998a) argues that the analysts' role in the determination of share prices has been exaggerated. The author develops, "...a grounded theory of the market for information, based on an empirical analysis of the economic incentives of Finance Directors, analysts and Fund Managers with respect to stock market information flows." The methodology involved participant observation of UK-based analysts, combined with questionnaires and interviews with analysts, FMs and Finance Directors (FDs). The conclusions are rooted in empirical findings, and are concerned with accounting research. Barker claims that analysts play two main roles. Firstly - qua conduits of market efficiency - as distributors and users of breaking market news; and secondly, as providers of condensed and filtered views on market consensus. The author argues that it is the latter that provides "benchmarks" that enable FMs to assess risk and the potential for out-performance. Furthermore, FDs and FMs are described as having similarly long-term interests in share price performance. In contrast, analysts are suggested to favour price volatility due to their incentives to maximise commission income on share trading. Barker (1998b) finds that FMs commonly have a corporate governance role in the stocks they own. Analysts, in contrast, treat business performance as an exogenous variable in their equity valuations. This fuels the thesis that FDs and FMs have more closely coincident interests than analysts have with either group.

In summary, prior research has focused upon analysts' data sources, valuation methods, forecast accuracy, bias and incentives, causal links with market volatility, and analysts' role in market efficiency. It is rooted in procedural elements of the analytical role, with relevance to accounting research or financial economics. However, these studies largely omit a more socially orientated understanding of analysts' incentives, actions or basis for competition. Many prior studies focus upon performance outcomes from analysts, but this is commonly at a highly aggregated level, and it is typically related to equity price determination. We present a more "person" and behaviourally centred view. Compared with the literature, it applies a

different level of analysis and different research methods, but we connect with the literature in addressing dimensions of analysts' performance. In the next section, we describe how this study has sought to reveal how analysts outperform.

Research Process and Study Sample

Traditionally, analysts have been examined in accounting or financial economic terms. To date, the question of competition between analysts has been largely ignored. This paper therefore aims to create a model of analysts' sources of success, rather than to test existing theories or hypotheses.

The analysts studied are framed by the UK's geographical boundary, with the majority working in the City of London. To assess their sources of success, we chose a methodology with two stages. Phase One consisted of semi-structured interviews with, firstly, analysts, and secondly, those defined by analysts as stakeholders to success. This method allowed an exploratory, inductive and flexible approach, in order to gain insight to a relatively unexamined subject. Phase Two consisted of data gathering with a questionnaire and, in parallel, case studies of individual analysts (the discussion of which is beyond the scope of this paper). This method produced quantitative, large sample findings with which to test and deepen the Phase One findings.

We now discuss each of the two research Phase methodologies in turn, briefly considering their aims, theoretical basis and then practical elements, finishing with how the resulting data were analysed. Phase Two was contingent on the findings of Phase One, and therefore some of these earlier findings are provided before a full discussion of Phase Two.

The goal of Phase One was the induction of a model of analysts' sources of success, via understanding of the process, content and context of the analysts' role. It involved gaining opinions on the nature of success and its creation from analysts and their stakeholders. Such methods have the advantage of allowing interviewees to answer broad questions, and permit the interviewer to request further explanation. The method is ideal for gaining insight to a little understood subject and, by its inherent

subjectivity, is well suited to studies of stakeholders. Against these benefits lies the risk of bias or presupposition from the researcher (Glaser and Strauss, 1967). Note also that both authors of this paper have worked as equity analysts in the City of London and therefore brought knowledge of the role to the research process.

We now discuss the practical elements of Phase One; the participants, methods used and specific data requirements. Participants were largely selected on the basis of their availability for interview; a constraint reflecting the high status and busyness of this study sample. Interviews were, where possible, recorded on audiotape. The number of interviews performed was guided by the search for “saturation” – the point at which the questioning of further participants appeared unlikely to furnish deeper insights (Glaser and Strauss, 1967). The Phase One study participants are summarised below in Figure 1.

Figure 1: Participants to Phase One of the Research

Participants	Number Interviewed
Analysts	8
FMs	7
FDs	4
Sales	4
Finance	4
PR*	2
Journalists*	2

* For background – not used in analysis

Data was gathered in Phase One via semi-structured interviews of around 25 minutes with analysts and, subsequently, with stakeholders, as defined by analysts. Most interviews were conducted by telephone, on a one-to-one basis, over the period March to November 1998. The interview guide was designed to probe the process, content and context of the analyst, while focusing on success; its definition, and its realisation.

The data from Phase One were analysed using the process of “coding” (Miles and Huberman, 1994). This involved converting all tape recordings and notes from interviews with Phase One participants into typed text, and then extracting meaningful fragments, or “codes”, in order to reconstruct a relevant picture of participants’ perspectives. Codes were then grouped into higher level, relevant themes for each stakeholder group until a workable summary and model of success could be derived. The themes uncovered by the researchers form the column headings in each of the summary tables in the next section. The model of success was derived from particular focus on causal references from participants within all stakeholder groups. Summaries for each stakeholder group are shown in the results section.

Before progressing to discussion of Phase Two, it is necessary to briefly address some of the Phase One findings on which Phase Two was contingent. The stakeholder groups were identified in interviews with analysts in Phase One, and thereafter individuals from those groups were scheduled for interview. Two further groups are introduced in this section. Firstly, the corporate finance specialists who work with analysts in the employing banks, described here as “financiers”. Secondly, the equity salespeople, also within an analyst’s employing bank, who are responsible for promoting and taking orders for the purchase or sale of equities, largely from their Fund Manager clients.

Following the interviews with the analysts, the stakeholder groups were identified as:

- the Fund Manager clients (FMs)
- the Finance Director and senior management of the analysed companies (FDs)
- the equity sales colleagues
- the corporate finance colleagues (financiers)

Having described the Phase One methodology and having established the stakeholder groups on which Phase Two depended, we progress to the aims of Phase Two, its theoretical and practical basis, ending with how the resulting data were analysed.

While Phase One enabled us to generate an initial model of the sources of success, Phase Two involved comparing that model with the results of further empirical investigation, to both test the model and deepen the findings. The model related to how analysts act for success, rather than being centred on their traits or skills. To test a hypothesised causal link between analysts' actions and performance outcomes we examined the correlation of metrics of activity with metrics of success.

We now discuss the practical elements of Phase Two; the participants, data collection methods used and specific data requirements, before concluding this section with a description of the analytical methods used. Those surveyed or interviewed in Phase Two were nearly all rated in the published surveys by Reuters (Reuters, 1998) or Extel (Extel, 1998). The use of published rankings as performance metrics had been validated by Phase One, but rankings also provided a metric of performance to aid statistical testing. By definition, this performance metric can only be applied to rated analysts, and therefore the survey sample emphasised this elite group. All case studies and questionnaires were completed over a six-week period from late September to early November 1999. A total of 43 analysts from 25 banks, ranging across 30 industrial sectors were respondents to the questionnaire. The survey sample from responding banks is shown in Figure 2 below, along with a modest response rate of 13%, perhaps reflecting the pre-occupation of the target group.

Figure 2: Sample description of respondents in Phase Two

Bank	No. of Analysts Approached	No. of Respondents	Response Rate
ABN AMRO	31	2	6%
Beeson Gregory	2	2	100%
Cazenove	10	1	10%
Commerzbank	8	1	13%
Credit Lyonnais	6	1	17%
Credit Suisse First Boston	27	2	7%
Deutsche	33	2	6%
Donaldson Lufkin & Jeanrette	2	1	50%
Dresdner Kleinwort Benson	28	7	25%
Fox-Pitt, Kelton	2	1	50%
Goldman Sachs	17	2	12%
Greig Middleton	2	1	50%
Henderson Crosthwaite	3	1	33%
HSBC	27	1	4%
Lehman Brothers	7	1	14%
Merrill Lynch	42	4	10%
Morgan Stanley Dean Witter	18	1	6%
Paribas	3	1	33%
Saloman Smith Barney	22	2	9%
Schroders	12	1	8%
SG Securities	5	1	20%
Sutherlands	3	2	67%
Warburg Dillon Read	9	1	11%
West LB Pannure Gordon	5	1	20%
Williams De Broe	7	3	43%
TOTAL	331	43	13%

Questionnaire respondents were selected on two main criteria. To reflect an interest in analytical success, mainly rated equity analysts were sampled. Secondly, to achieve a representative sample, respondents were spread across industry sectors and banks; the sector spread is shown in Figure 3 below.

Figure 3: Sector Coverage of Responding Analysts in Phase Two

Sector Coverage	Number of Respondents
Banks	2
Biotech	1
Building, construction and housing	2
Chemicals	2
Drinks	1
Engineering	1
European Utilities	1
Food manufacturing	1
Food retail	2
Healthcare	1
Household goods and food producers	1
Insurance	3
IT Services	1
Leisure & hotels	1
Media	1
Metals and mining	2
Motor retailing	1
Oil & Gas	2
Oil Integrated	1
Other Construction, Business Support Services, Distribution	1
Other Financials	1
Paper	1
Pharmaceuticals	2
Property	1
Support services, chemicals, tobacco, mining	1
Technology	3
Tobacco	1
Transport	1
UK Electricity, UK Water	1
Utilities	3
TOTAL	43

Data were collected from respondents via questionnaire. The findings of Phase One focused attention upon analysts' stakeholder priorities and interactions in the quest for success. The Phase Two questionnaire therefore captured three types of data in order to explore relationships between analysts' priorities, actions, and performance outcomes. There were, for each of the four stakeholder groups, questions of analysts' basic activities; hours spent, the number of people contacted, and the priority of relations. The questionnaire also captured data on performance outcomes mentioned by the Phase One participants – published rankings from FDs and FMs (c.f. Extel, 1998; Reuters 1998), and salary level.

Having described the study sample and data gathering process, we conclude this section with discussion of data analysis in Phase Two. It was planned to produce two

kinds of data; largely quantitative, statistically analysable data from the questionnaires, and largely qualitative, social network-centric data from the case studies (which are beyond the scope of this paper). The former would facilitate testing of the hypotheses resulting from the model of analytical advantage.

The data resulting from the questionnaires was largely multivariate in nature and correlation was used for testing relationships between sub-sets of the data¹.

Limitations

The findings should be viewed in the context of the research programme. There is a risk of unconscious presupposition or bias from the researcher, the sample size in Phase Two was not large and we do not distinguish causation from correlation. However, some research value derives the difficulty of gaining access to analysts and having researchers with experience in the area adds insight. Whilst we have not distinguished causation, we do observe later that our findings from Phase One support the proposed relationships; that social actions cause performance advantage.

Perceptions of Success

Results from the Phase One study of analysts, and then from each of the four stakeholder groups suggested by the analysts, are provided below. This structure is used as findings from analysts suggested that a “stakeholder view” permeates much of their world-view. The whole of Phase One is then summarised. Following, is a synopsis of the higher-sample, quantitative findings from Phase Two. Finally, the conclusions from both phases are drawn together and a model of analysts’ sources of success is derived.

Analysts’ Perceptions of Success

We summarise the interpretation of the interviews from analysts (and, subsequently, *mutatis mutandis*, each of the four stakeholder groups) in five parts. Firstly, we discuss their perceptions of success – how it can be defined and how it is manifested.

¹ For hypothesis testing, structured equation modelling (SEM) would have been a suitable technique but needed, as a risky minimum, fifty questionnaire responses (Hair et al, 1994).

Secondly, we present the causal conditions for success, and thirdly, the actions and interactions that analysts undertake for and with the stakeholder groups. Fourthly, we discuss outcomes relating to analysts, and finally we analyse analysts' perspectives on the industry context.

Success, to analysts, is nebulous. As analyst one ('A1')² put it, *'I don't think there's any set answer except that it's for you to set your priorities among those four constituents [the stakeholders] and satisfy them better than anyone else.'*, and *"...I would define success around building those [stakeholder] relationships"* (A3). However, in the comment that, *"Commission is the best guide to how good an analyst is."* (A5), there is the suggestion that commission – or the underlying phenomenon of secondary market³ deal flow – is more a manifestation of success than the thing in itself. As A2 added, *"...a lot of people define themselves only in those terms, as number one rated..."*, suggesting that the clients' evaluation of analysts, as evinced by published surveys (c.f. Extel, 1998, Reuters, 1998), is as good a measure as any.

For analysts the ingredients of success consisted of managing communications and relationships with stakeholders, technical mastery, and of positive feedback from having a good reputation. The following quotation summarises a popular view, *"...if they realise you are highly rated by the clients they will take you more seriously and the clients who realise you've got good relationships with the companies will also take you more seriously. What differentiates a good analyst is those two areas."* (A7) The path to a high ranking from Fund Managers is likewise elaborate. It is described as involving a blend of knowledge, insight, and – especially – good and thoroughgoing communication. As A3 put it, *"...you almost have to pummel the poor old clients into submission."*

³ The *"secondary market"* refers to the market for banking services - most relevantly research relating to equity valuation, agency share dealing and market making - in subsequent support of primary activities. The *"primary market"* refers to the market for banking services in support of mergers and acquisitions (M & A), share issues, and other such activity resulting in a newly funded commercial entity. This market is the prime concern of the analyst's contacts from corporate finance.

In the formal capacity as analyst, the focus is on valuation techniques, *‘It has to be accurate and it has to be clear’*, (A1) and on the quality of written reports, *‘You have to be able to write reports very well.’* (A1) There is evidence that analysts are highly sensitive to the context of their recommendations, *‘It’s a matter of understanding where you stand in the spectrum of opinions.’* (A3) However, there is acknowledgement that, despite its emphasis, there is little *differential* value to be gained from “sound” valuation techniques: *“...increasingly it’s an entry ticket.”* (A3) Thus, pure analytical tasks appear as “hygiene factors” and are foundational to the role.

Not all outcomes from analysts are easily reconcilable with their “classic” analytical role. One of the most engaging findings was how analysts (and salespeople) use favouritism with Fund Managers in their “call order”. This results from the fact that analysts and salespeople can only make one advisory telephone call at a time, and therefore contact favoured clients early in the order of calls. One analyst extended the idea: *‘An analyst has Fund Managers on an A list and tries to bail out their favourite stocks.’* (A5). A1 described how, with Finance Directors, *“... the ideal situation is when you’ve got a very close and professional and often interactive relationship with these guys.”* Another analyst claimed that, *“...what I refer to as my opinion is really an amalgam of my opinion plus what I get back from my best clients.”* (A6) Furthermore, the importance of reciprocity, and the link between primary and secondary deals, is suggested by the comment, *“...you build up your reputation and then you are able to draw on that – almost call in the favours I suppose – when it comes to primary market deals...”* (A3)

Conflict is the other central theme in outcomes of interactions, and it appears to be a consequence of the contrasting needs of the stakeholder groups. With Fund Managers, analysts are, *“...aiming for them to think you’re the best in the industry and therefore to give you the highest ranking.”* (A1) Moreover, *“...houses definitely favour some Fund Managers based on the volume of business or the commission earned.”* (A5) Earning commission is a clear goal of analysts, and linked to the aim of gaining, *“...some idea of...what their investment criteria are”* (A4). A buy for a “growth” investor could be a sell for a “value” or a “momentum” investor, and analysts need a firm grasp of their clients’ methods. Corporate Finance, in contrast, *“...are asking you*

to help them on M & A deals... which is a huge drag on your time” (A2). Furthermore, “...you get conflicts between what you want to say about a company and what corporate finance want to say about a company” (A2). The result of this conflict can be dire; “...in extreme cases people have been sacked for refusing to change things.” (A2). Conflicts are a frequent and forceful part of the analyst’s life.

The equity salesforce is important to analysts, “...only in that they deal with the client base” (A7). But, given the obvious influence of the client base - *‘I think the really influential people are probably the Fund Managers...’* (A3) - the position of Salespeople cannot be overlooked. Some analysts believe that salespeople have influence over Fund Managers, while others dismiss it altogether.

With Finance Directors and senior managers, analysts, “...aim to establish a relationship of real trust...and [Finance Directors] are therefore willing to talk relatively frankly...” (A7). They are, “...one of your best sources of information” (A1). Hence the emphasis on openness and trust. Notably, because companies’ managers are the best source of the information on which most analytical work – and therefore, to some extent, all the stakeholder relationships - depends, they have a kind of centrality to analysts.

In terms of the broader industry context, secondary market competition is significant to the analyst; “...there’s huge over-capacity...” (A1). “*The dynamics of the industry have changed so much that the returns from satisfying the needs of the institutional investors are simply not enough to run a business, so the primary side of the business has become increasingly important*” (A1). Parallel to this trend, “...research these days is becoming more of a commodity product...” (A2).

In summary, the analyst perceives the differing perspectives of each set of stakeholders are essential to the task, and therefore to attaining success. Analysts appear to focus more on stakeholder relations than on activities qua analysts. Social network concepts – such as reciprocity, conflict, favouritism and prestige – are prevalent. The findings from analysts are summarised in Figure 4 below.

Figure 4: Overview of Analysts' Perspectives on Success

Defining Analytical Success	Causal Conditions for Analytical Success	Actions & Interactions Relating to Analysts and Their Stakeholders	Outcomes Relating to Analysts	Perspectives on the Industry Context
Ranking; Deal flow - primary & secondary; "Self-determining"	Diversity & quality of stakeholder relationships; Good communications; Conflict management; Diverse skills	Provide "right" service to each stakeholder group; Manage conflict between stakeholders; Become sensitised to spectrum of opinion; Create reciprocity with fund managers and FDs	Pressure to perform; Conflict; Favour FMs who provide most commission	Homogeneity of banks; Bigger is better for banks & FMs; Power is with FMs; Price-based competition in secondary market & over-capacity.

With the realisation that analysts focus substantially on stakeholder interactions, we now move attention from analysts' views of their domain, to the views of their stakeholders. In turn we shall review the perspectives of FMs, FDs, equity salespeople and financiers.

Fund Managers' (FMs) Perceptions of Analysts' Success

The evaluation by FMs of analysts and their work can be highly personal, *"If I know a guy, I know their judgement."* (F2) and *"...you build [preferences] up at a number of levels – it's really a sense of trust for their judgement"* (F6). The power of personal relations is clear. FMs perceive that the route to success for analysts is made of strong stakeholder relationships, knowledge, and valuable insights. *"It is crucial that analysts are well-known and popular with the fund management community"* (F3), and *"I need to be aware what an influential analyst says in the short to medium term...because there's an element of self-fulfilling prophecy"* (F3). Poor analysis can be attributed to bias, which is attributed to a lack of independence, *"It's good if analysts...don't have corporate level contacts"* (F7). But, FMs appreciate the analyst who has, *"...very good access to the companies..."* (F6)

Moving to the nature of interactions, FMs commonly have regular contact with equity salespeople, *“Salespeople tend to be the first port of call whenever I need information”* (F1). Furthermore, salespeople can wield special influence, *“I like those who tell me which analysts are good and where their strengths and weaknesses are.”* (F6) The assistance requested from analysts appears polarised between “strategic” or sector-level analysis, and detailed event and company-specific work. As F6 put it, *“...increasingly useful is the concept of strategic research.”* In contrast, *“We very often use sell-side analysts to process data.”* (F5) and *“They tend to do the legwork for you, which then ties in with your own analysis.”* (F2) Contact with analysts is usually prompted by a valuation-relevant development, *“I’ll often call an analyst during a change of investment strategy...”*, (F3) or by, *“...the impact of some news.”* (F3) And in an elaboration on previous comments on bias, *“...[analysts] need to be seen to be supportive of their stocks. It’s often this that prompts the need to talk with the analyst to get the full picture or clarification.”* (F4)

FMs are strident in their preferences between analysts, *“...there are huge gaps between the best and the worst.”*, (F3) and *“...some stand out.”* (F7) Opposing this is the view that, *“If you’ve read one you’ve read them all.”*, (F2) and *“Much of it is far too consensual and lacking insights. The majority of reports are of little use.”* (F4) To the Fund Manager, the best analysts offer a complex set of products that are wrapped up in the notion of “good service”, and are thereby highly rated. But as one F7 put it, *“The surveys of analysts are about who you know and don’t mean too much.”*

Assumptions about the economic value of investment recommendations are perhaps central to the most common misconceptions about analysts. One fund manager stated that, *“Analysts do prove themselves via their calls and I’ll remember good calls.”*, (F7) and, *“You tend to respect analysts – and I’m thinking about one guy in particular – who doesn’t make many recommendations but when he does he’s thought long and hard about them – four out of five times he’s right.”* (F6) However, a Fund Manager also stated that, *“I read the reports not so much for investment recommendations as for background or trends...”*, (F4) and *“...[analysis] is useful in that it provides factual information as much as in the recommendation itself.”* (F1) Moreover, *“...analysts get points for analysis – even if it’s not right, this is what they are rated on.”* (F2)

FMs are also highly sensitive to the banking industry environment. The banking industry is predicted to become, “...much more US-style, which is quantitative driven and based on valuation techniques. Fund Managers rely less on a feel for the market and more on valuation.” (F2) While certain FMs welcome this, there are reservations. Some analysts with US banks are described as, “...lacking independence of mind...” (F5) Continuing this, independence and analytical coverage form the two dimensions into which FMs appear to classify banks, “I see houses in roughly two camps – large ones that are rarely independent...There’s also good independent ones...that give an alternative view.” (F4) Finally, cost control, or the “duty of best execution”, is an obligation; “...we must pursue [trades] where the price is best.” (F6)

In summary, FMs appear to have reconciled their need for thorough and “rational” investment recommendations with keen preferences for just a few analysts. Personal judgements of trustworthiness are important, although equity salespeople can have influence over FMs. Figure 5 summarises the findings from FMs.

Figure 5: Overview of Fund Managers’ Perspectives on Analysts’ Success

Defining Analytical Success	Causal Conditions for Analytical Success	Actions & Interactions Relating to Analysts and Their Stakeholders	Outcomes Relating to Analysts	Perspectives on the Industry Context
Ranking; Analytical "Usefulness"; Good investment calls	Trust & respect; Knowledge & insight; Good communication; Good access to FDs; Good investment calls; Independence; Focus	Regularly contact sales or analysts; Emphasise personal evaluation; Contact for share or sector valuation changes; Use analysts for data intensive work; Use sales people to evaluate analysts	Aware of bias & consensual view; Sceptical regarding rankings; Aware of favouritism; Strong preferences between analysts; Follow good analysts because they are self-fulfilling	Strong "quant" US influence; Emphasise duty of best execution; View banks in terms of independence & coverage

Finance Directors' and Senior Management's Perceptions of Analysts' Success

For Finance Directors and senior management (FDs), there is evidence of preoccupation with analysts' knowledge and understanding of the relevant sector and company; *"A star analyst understands the industry – which is what sorts the wheat from the chaff."* (D2) Similarly simple is the FDs' view of the route to success: *"...a really intense focus – a really short portfolio..."* and, *"...great contacts."* (D1)

Contact between analysts and FDs is infrequent, but regular, *"I talk with analysts two times per month on the phone. We meet at least twice per year."* (D2) Contact is motivated by a need to keep analysts updated, but also to acquire insights from them, *"I'm keen to verify what's going on with competitors; to verify rumours."* (D1) From the FDs' perspective, the tone of discussions with analysts is one of prudence, *"...it requires great care – especially to keep the attention of the City focused on what we want them to know."* and *"Every Company has to be incredibly careful about being too loquacious – tremendous effort goes into investor relations."* (D1)

FDs exhibited general disappointment in most analysts' understanding of business, *"...their depth of understanding is pretty superficial."* (D3) FDs have, *"...problems with analysts not understanding the...market."* (D2) and, *"...they don't have an amazing understanding of the market."* (D4)

FDs' interest in analysts rarely extends beyond the, *"steady relationship."* (D1) There is also little evidence that analysts have a great impact on FDs' choice of bank for primary deals, *"...the choice was made really not on the basis of the analysts..."* (D2)

In summary, FDs appear to be primarily engaged in a search for financial stability, which can be considered consistent with the goal of securing or augmenting funding. Analysts are seen as part of the means to those ends. But while FDs are appreciative of analysts' ability to interpret and understand an industry, they appear preoccupied with a lack of analysts' understanding of their own Company and markets. Figure 6 summarises the findings from FDs.

Figure 6: Overview of FD's Perspectives on Analysts' Success

Defining Analytical Success	Causal Conditions for Analytical Success	Actions & Interactions Relating to Analysts and Their Stakeholders	Outcomes Relating to Analysts	Perspectives on the Industry Context
Good sector & company understanding	Detailed knowledge	Regularly but infrequently contact analysts; Feed "right" information; Create reciprocity with analysts	Disappointment in lack of detailed knowledge	FDs engaged in search for funds & stability

Equity Salespeoples' Perceptions of Analysts' Success

Salespeople project a strong affiliation with their clients – the FM. But analytical success, to the salespeople, can be related to commission earnings, “...*we must do everything possible to make sure we get revenue...*” (S2). This is, in turn, related to, “...*regular, unforced, differentiated views on stock valuation...*” (S4) from the analysts. Furthermore, the importance attached to analysts' rankings is evinced by the comments that, “*We have ways to make sure they become highly rated...*” (S1) and, “*The highly rated analyst tends to be read more.*” (S1) In common, then, with FMs, salespeople are impressed by high rankings. However, the cost to FMs of trading commission is the chief source of revenue and impetus to salespeople. So, despite salespeoples' enthusiasm to identify with their clients' interests, it is obvious that - in one sense - the FMs' loss is their gain.

Salespeoples' understanding of the path to analytical success is – consistent with that of FM – complex. S3 commented that, “...*valuation is everything,*” and, “*We tend to place...a very high requirement in terms of valuation methodology.*” S1 summed it up with, “...*it's a whole mix of factors.*”, and S4 described the highly rated analyst as, “...*the jack of all trades...*” Finally, S3 stated that the real secret was to follow sound valuation with, “...*an angle that's going to hook the client...*” Hence, salespeople

appear engrossed with analysts' valuation methodologies, and also with a broad range of interrelated skills. To them, constructing analytical success requires many parts.

Interaction between salespeople and analysts is almost continual; they have, *'Daily contact with [the] in-house team...'* (S1) Salespeople are keen to emphasise analysts' communication skills: *"...it's not the story, it's how it's told."* (S3) Also held to be crucial is, *"...the ability to communicate complex ideas in a simple way."* (S4) Indeed, communication skills are seen to be core to many interactions; not least those involving conflict. As S2 put it, *"...analysts don't like to be too controversial in what they write."*, and more radically, *"...if...the clients don't like you then your research is worthless."* (S3) The greatest conflict was seen by S2 to be with corporate finance, in which, *"...the analyst is torn to work on the corporate finance side and...write the story as the company wishes it to be seen."* Furthermore, *"...by calling it a sell you are working yourself out of a job."* (S3)

Additionally, it is clear that all clients are not equal; *"The salesforce will give the best information to higher commission clients, such as those who give 0.4% instead of 0.2%. We can only make one call at a time."* (S1) Salespeople perceive that they have influence over FMs and their views on analysts; *"...we often form the trigger as to whether the client should read the research report or not."*, (S3) and, *"...the salesman is always going to be closer to his institutional client..."* (S2) The close identification that salespeople feel towards their clients is summed up; *"...the salesman demands what the...clients want..."* (S3)

Salespeoples' preferences between analysts are strong; *"...very quickly you develop a feel for who you regard as good and who you don't."*, (S3) and, *"I have strong preferences between analysts..."* (S1) Preferences can also be based on, *"...those who do less better work."*, (S3) and, *"...marketing skill...understanding modern valuation theory...understanding an industry in detail...understanding stocks in detail."* (S4) Salespeople, perhaps because of their interest in sound valuation, are aware that analysts are subject to pressures that could compromise that objectivity. As S2 put it, analysts are *"...worried...about upsetting their clients...perhaps worried about what the corporates, who may be clients, are thinking."*

In common with analysts, salespeople view some FM as particularly powerful, “...there are a lot of analysts on the buy-side who know just as much, if not more, than us.” (S2) In the context of their employer, Salespeople can view themselves as, “...the biggest clients of any stockbroking firm...” (S2)

In summary, the salespeople’s role shows identification with that of the Fund Manager. Some salespeople hint that this is the best way of securing commission revenue. In common with FMs, they have strong preferences between analysts, based on many (often-intangible) factors. Salespeople consider that their views of analysts can have a significant effect on those of the FMs. The findings from salespeople are summarised in Figure 7 below.

Figure 7: Overview of Salespeople’s Perspectives of Analysts’ Success

Defining Analytical Success	Causal Conditions for Analytical Success	Actions & Interactions Relating to Analysts and Their Stakeholders	Outcomes Relating to Analysts	Perspectives on the Industry Context
Ranking; Commission	All-round skills; Creating "stories"; Sound valuation	Continually work with analysts; Emphasise communication; Emphasise quality of research; Use "call order" to favour FMs; Influence FMs preferences between analysts	Strong preferences; Also Sales develops strong preferences between FMs; Aware of analysts' bias	Sales People are the "Voice of the Clients"; Power is with the FMs

Corporate Financiers’ (financiers) Perceptions of Analysts’ Success

Financiers represent a stakeholder group with highly focused interests. Their account of analytical success is almost entirely defined by analysts’ ability to win primary deals. As one financier put it, “A good analyst...gives us a crack at getting an M and A mandate.” (C3)

Success is perceived to be – consistent with the views of other stakeholder groups – based on, “...*good contacts with the FD...*”, (C2) and, “*Depth of knowledge.*” (C1) However, in contrast to others, financiers refer to the importance of forecast accuracy and, “...*the commercial value of [analysts’] recommendations.*” (C4)

Contact with analysts is typically occasional and is prompted by the need for detailed information or, “...*background...*” (C2) In order to fulfil primary deals, the analyst is seen as someone who, “...*understands the industry.*” (C3) More particularly, contact with an analyst helps, “...*to claim knowledge and independence.*” (C3) and, “*You need to sound credible and it’s helpful to talk with an analyst...*” (C3)

Financiers typically claim that, between analysts, they, “...*don’t have strong preferences...*”(C3) but they have few doubts about the practical value of analysts, “*In winning M and A mandates, for example, the analyst relationship can be very important...*” (C3) Primary deals, in the context of banking, are occasional, but highly remunerative. As C3 put it, “*An M and A mandate can be worth £100’s of millions, and it’s this that justifies the huge salaries.*” Financiers view analysts’ worth very much through the lens of corporate finance.

In summary, financiers perceive that analysts provide occasional but crucial assistance in winning high-value primary deals – and both groups appear highly rewarded to do so. However, it is ironic that financiers claim to value independence so highly in analysts, when this is precisely the quality that other stakeholder groups claim that financiers endanger.

Figure 8: Financiers' Perspectives on Analysts' Success

Defining Analytical Success	Causal Conditions for Analytical Success	Actions & Interactions Relating to Analysts and Their Stakeholders	Outcomes Relating to Analysts	Perspectives on the Industry Context
Primary deal flow	Being close to FDs; Detailed & broad knowledge	Irregular contact; Discuss with analysts in-depth to help win and fulfil deals	Modest preferences; Greater knowledge through analysts; Contact for primary deals via analysts	Need support for highly lucrative primary deals

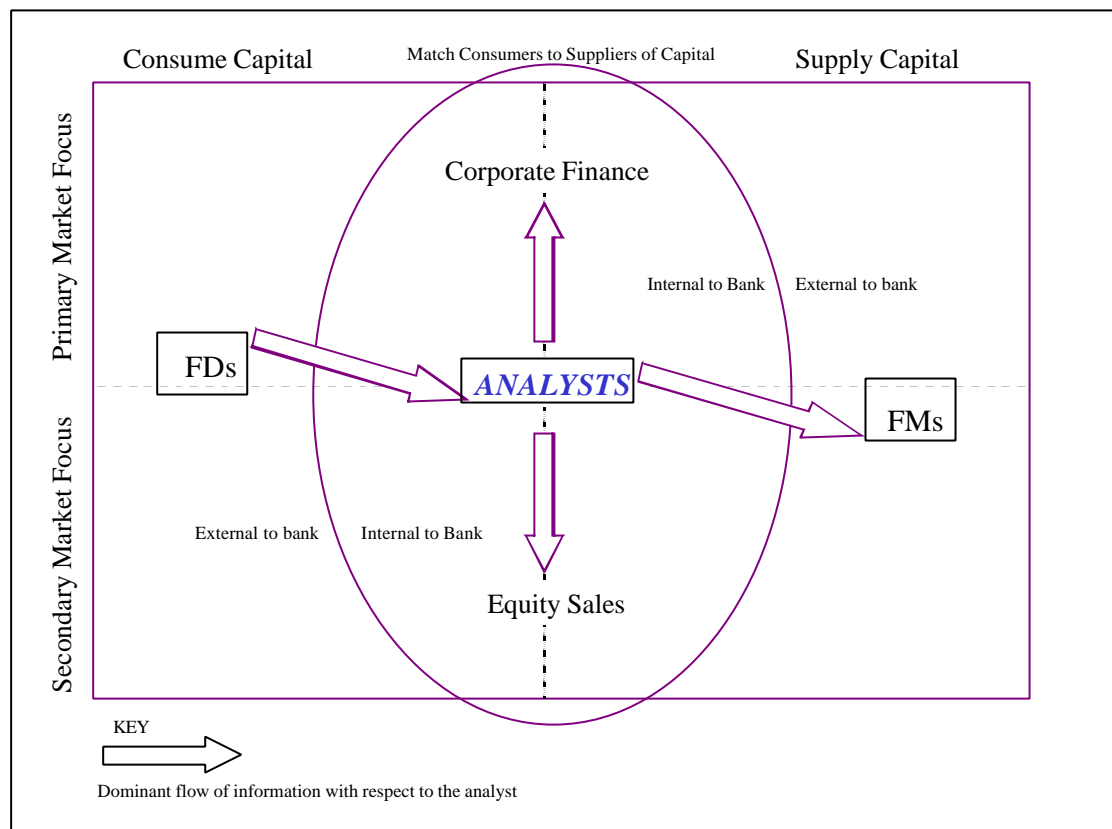
Towards a Model of Success: Summary of Phase One

The sections above have discussed how analysts operate in a complex world, without one distinct definition of success. Accomplishment depends on the number and quality of stakeholder relationships. But analysts' perspectives on what constitutes quality in a relationship are not perfectly mirrored by each group. Moreover, each group has perspectives on analysts' success and its realisation that differ from the other stakeholder groups. We next summarise the themes in analysts' and each stakeholder group's perspectives of success and its sources, before creating a conceptual model of analysts' sources of success.

With the exception of the financiers, all stakeholders have regular contact with analysts. This is usually married to strong preferences from stakeholders between analysts. From the point of view of analysts, FD's are the best source of information and FMs the likely destination of most of that information and related opinion. In this sense, analysts are informational intermediaries between those who demand capital and those who supply it. But the passage of information and advice is not purely mechanical or democratic. Analysts appear to favour some FMs on the basis of commission earned. Likewise, stakeholders can prefer analysts on the basis of their knowledge, reputation, character or moneymaking ability.

Successful relations with stakeholders appear to depend on the quality of execution of analysts' "core" tasks – detailed analysis, well thought out recommendations, and "saleable stories". The desired (and undesired) performance outcomes from analysts are mediated through stakeholder relations. For example, analysts' remuneration can be strongly influenced by winning mandates for primary market deals, and this in turn is aided by good relations with FDs. Furthermore, all the above can be influenced by the banking business environment. The sophistication of this picture mounts when one considers that feedback loops are common. Hence, improved ranking might lead to closer relations with FDs, and this leads to better-focused analysis and investment recommendations.

Conflict is a strong theme. For example, analysts are motivated to gain knowledge and insight from FDs, while FDs' preoccupation with "prudence" can constrain information flow. Equity salespeople, FMs and financiers all appear to favour "sound valuation" and accurate forecasts, while acknowledging that analysts can be highly motivated to avoid making "sell" recommendations. Furthermore, because the secondary market is said to suffer over-capacity, the importance of the primary market has increased. While FMs and salespeople are largely involved with the secondary market, some analysts and all financiers are engaged in the primary market. But the lucrative nature of primary deals is claimed to further endanger analysts' objectivity, by creating huge incentives to avoid releasing any analysis that could displease those who fund the deal. Moreover, these conflicts are not merely discomfiting to analysts; some have been sacked as a result of failing to reconcile clashing interests. Continuing this theme of conflict, Figure 9 below provides an overview of brokers' operations and analysts' information flows. It emphasises analysts' centrality within the four stakeholder groups, each of which has different commercial interests and therefore different expectations of analysts.

Figure 9: Brokers' Equity Operations and Analysts' Information Flows

The analyst's role can be modelled in two parts. Firstly, the role qua "analyst", which principally concerns valuing equities and communicating those findings to help create investment value. Secondly, the role qua "networker", which embraces diverse activities. These include favouring certain Fund Manager clients with speedier or more extensive analysis in "exchange" for commission earnings, or using a reputation gained from ranking surveys to help win merger and acquisition (M & A) mandates. The essence of the analyst's role is proposed to be in serving or "binding" the divergent interests of the four relevant stakeholder groups. The evidence suggests that this networker role is the best source of success. The next section takes forward the notion of analyst as networker and tests how analysts' priorities and actions with stakeholders are linked to success.

Successful Goals and Actions: Phase Two Findings

In order to explore hypothesised causal links, between analysts' priorities and actions with stakeholders and success, Phase Two departs from the rich, qualitative, small

sample approach of Phase One to large sample, quantitative, questionnaire based investigation. The results of Phase Two, derived from the responses to the questionnaire, and which resulted in around 1,200 correlations, are summarised below in three correlation tables. These are considered in the light of expectations derived from Phase One, in which analysts' priorities with stakeholders were described as linked to the level of interaction, which are, in turn, linked to success. We therefore discuss correlations between activities and priorities, activities and success, and then priorities and success.

In discussing significant correlations between analysts' activities and priorities, we focus on analysts' contact of stakeholder members by telephone. In the correlation matrix presented in figure 10, we find no notable links between activities and priorities⁴ but strong links between contact levels for one stakeholder group and another. These strong links are evident where analysts who contact FDs more often also contact sales more often, with a correlation of 72.8%, significant at 5% level. Similarly, FD and FM contact levels are correlated at 33.5%, and FD and financier contact levels at 32.3%, both significant at the at 5% level. Overall, and as suggested within Phase One, FDs could have an informational centrality, in that contact levels with all three other stakeholder groups are well linked to analysts' contact levels with FDs. In conclusion, the issue of prioritising stakeholder groups appears relatively unimportant to contact levels, but contact levels with FDs might affect all others.

Figure 10: Correlation Table for Activities and Priorities

		Correlations							
		FM ORDER	Finance order	Sales order	FD ORDER	FM-Hours on phone per month	FD-Hours on phone per month	Sales-Hours on phone per month	Fin-Hours on phone per month
FM ORDER	Pearson Correlation			**					
Finance order	Pearson Correlation	.007			**				
	Sig. (2-tailed)	.962							
	N	43							
Sales order	Pearson Correlation	-.540**	-.202		*				
	Sig. (2-tailed)	.000	.194						
	N	43	43						
FD ORDER	Pearson Correlation	-.069	-.612**	-.331*					
	Sig. (2-tailed)	.658	.000	.030					
	N	43	43	43					
FM-Hours on phone per month	Pearson Correlation	-.253	.031	.050	.131		*		
	Sig. (2-tailed)	.115	.847	.760	.422				
	N	40	40	40	40				
FD-Hours on phone per month	Pearson Correlation	-.044	.162	.075	-.211	.335*		**	*
	Sig. (2-tailed)	.790	.316	.646	.191	.037			
	N	40	40	40	40	39			
Sales-Hours on phone per month	Pearson Correlation	-.092	.069	.063	-.043	.224	.728**		
	Sig. (2-tailed)	.582	.679	.705	.796	.182	.000		
	N	38	38	38	38	37	37		
Fin-Hours on phone per month	Pearson Correlation	.076	-.126	-.061	.104	.168	.323*	.221	
	Sig. (2-tailed)	.644	.443	.711	.531	.313	.048	.189	
	N	39	39	39	39	38	38	37	

** . Correlation is significant at the 0.01 level (2-tailed).

* . Correlation is significant at the 0.05 level (2-tailed).

Note: Questionnaire respondents placed the four stakeholder groups in order, 1 to 4, with the highest priority as 1.

In discussing links between analysts' activity levels and metrics of success we find, from figure 11, that:

- Salary level is correlated at 73%, at 1% significance level, to years of experience as an analyst.
- Top 300 ranking (the ranking within just the top 300 ranked analysts in the UK) from Extel (Extel, 1998) is correlated at -68.2%, at 1% significance level, to number of hours on the 'phone with corporate finance. Note that this can be viewed as a positive relationship because a better ranking is recorded with a lower number.
- Extel ranking from FDs (Extel, 1998) is correlated at 60.9%, at 5% significance level, to hours on the 'phone with FDs i.e. more talk is linked to worse ranking.
- Extel ranking from FMs (Extel, 1998) is correlated at -45.4%, at 5% significance level, to hours on the 'phone with sales i.e. more talk is linked to better ranking.

⁴ We ignored the three statistically significant correlations between priority levels for stakeholder

- Salary growth level is correlated at -44.2% , at 5% significance level, to the number of equities covered.
- Salary growth level is correlated at 40.2% , at 5% significance level, to hours on the phone with FMs.
- Salary growth level is correlated at -38.9% , at 5% significance level, to years of experience

Hence, more experienced analysts earn more, but their salaries grow slower. Those with faster growing salaries tend to cover fewer equities. More saliently to stakeholder interactions, a better ranking from FMs appears linked to more talk on the 'phone with sales people. A better ranking from FDs appears linked to less talk on the 'phone with FDs. Also of note is the finding that Top 300 ranking is linked to more talk on the 'phone with financiers. From Phase One, we interpret this as more a result than a cause of success; this elite of analysts was suggested to be a driver of primary deals and therefore to work more with financiers. Figure 11 also shows that the performance metrics are significantly inter-linked, with, for example, salary level correlated at -56.1% , at 5% significance level, to Reuters ranking from FMs (Reuters, 1998) i.e. better ranking is linked to better pay.

Figure 11: Correlation Table for Activities and Success

		Correlations										
		1998 Reuters ranking FMs	1998 Extel Ranking FMs	1998 Reuters ranking FDs	1998 Extel Ranking FDs	Salary Growth %	Salary Level	Top 300 weighted ranking from FM	FM ORDER	FD ORDER	Sales order	Finance order
1998 Reuters ranking FMs	Pearson Correlation		**		*		*	*				
	Sig. (2-tailed)											
	N	20										
1998 Reuters ranking FDs	Pearson Correlation	.439	.561*		**							
	Sig. (2-tailed)	.060	.037									
	N	19	14									
1998 Extel Ranking FDs	Pearson Correlation	.674*	.657*	.887**								
	Sig. (2-tailed)	.016	.020	.000								
	N	12	12	13								
Salary Growth %	Pearson Correlation	.078	.127	.126	.380				*			
	Sig. (2-tailed)	.737	.604	.617	.223							
	N	21	19	18	12							
Salary Level	Pearson Correlation	-.561*	.015	-.078	.237	-.029						
	Sig. (2-tailed)	.037	.963	.843	.701	.905						
	N	14	12	9	5	20						
Top 300 weighted ranking from FM	Pearson Correlation	.582*	.609*	.612	.073	.180	-.407					
	Sig. (2-tailed)	.037	.021	.080	.864	.556	.276					
	N	13	14	9	8	13	9					
FM ORDER	Pearson Correlation	.106	.289	-.111	-.113	-.348*	.014	-.011			**	
	Sig. (2-tailed)	.586	.193	.613	.714	.043	.953	.969				
	N	29	22	23	13	34	20	14				
FD ORDER	Pearson Correlation	.026	-.137	-.179	-.121	.070	.384	-.002	-.069		*	**
	Sig. (2-tailed)	.893	.542	.414	.693	.695	.094	.995	.658			
	N	29	22	23	13	34	20	14	43			
Sales order	Pearson Correlation	-.014	-.182	.202	-.010	.193	-.041	-.083	-.540**	-.331*		
	Sig. (2-tailed)	.943	.417	.356	.974	.274	.863	.778	.000	.030		
	N	29	22	23	13	34	20	14	43	43		
Finance order	Pearson Correlation	.001	.152	.184	.224	.050	-.268	.233	.007	-.612**	-.202	
	Sig. (2-tailed)	.998	.489	.401	.462	.779	.252	.422	.962	.000	.194	
	N	29	22	23	13	34	20	14	43	43	43	

** Correlation is significant at the 0.01 level (2-tailed).

* Correlation is significant at the 0.05 level (2-tailed).

Finally, examining the links between priorities and success metrics, figure 12 shows that the only link of note is that salary growth level is correlated at -34.8%, at 5% significance level, to FM priority. In other words, a higher priority for work with FMs is linked to higher pay growth.

Figure 12: Correlation Table for Priorities and Success

		Correlations												
		1998 Reuters ranking FMs	1998 Extel Ranking FMs	1998 Reuters ranking FDs	1998 Extel Ranking FDs	Salary Growth %	Salary Level	Top 300 weighted ranking from FM	No. Equities covered	Years experience (current sector)	FM-Hours on phone per month	FD-Hours on phone per month	Sales-Hours on phone per month	Fin-Hours on phone per month
1998 Reuters ranking FMs	Pearson Correlation		**											
1998 Extel Ranking FMs	Pearson Correlation Sig. (2-tailed) N	.808** .000 20		*	*			*					*	
1998 Reuters ranking FDs	Pearson Correlation Sig. (2-tailed) N	.439 .060 19	.561* .037 14		**									
1998 Extel Ranking FDs	Pearson Correlation Sig. (2-tailed) N	.674* .016 12	.657* .020 12	.887** .000 13								*		
Salary Growth %	Pearson Correlation Sig. (2-tailed) N	.078 .737 21	.127 .604 19	.126 .617 18	.380 .223 12				*	*	*			
Salary Level	Pearson Correlation Sig. (2-tailed) N	-.561* .037 14	.015 .963 12	.078 .843 12	-.237 .701 9	-.029 .905 20				**				
Top 300 weighted ranking from FM	Pearson Correlation Sig. (2-tailed) N	-.582* .037 13	.609* .021 14	.612 .080 9	.073 .864 8	-.180 .556 13	-.407 .276 9							**
No. Equities covered	Pearson Correlation Sig. (2-tailed) N	-.284 .143 28	-.360 .108 21	-.081 .720 22	-.160 .619 12	-.442* .010 33	.118 .621 20	-.527 .064 13						
Years experience (current sector)	Pearson Correlation Sig. (2-tailed) N	-.254 .184 29	.137 .542 22	.086 .696 23	.143 .640 13	-.389* .023 34	.730** .000 20	-.365 .290 14	.290 .063 42					
FM-Hours on phone per month	Pearson Correlation Sig. (2-tailed) N	-.099 .623 27	-.110 .646 20	.073 .748 22	.031 .923 12	.402* .023 32	.377 .112 19	.276 .361 13	-.236 .148 39	.143 .379 40		*		
FD-Hours on phone per month	Pearson Correlation Sig. (2-tailed) N	.191 .350 26	-.105 .651 21	-.164 .478 21	.609* .035 12	-.239 .181 33	-.387 .092 20	-.492 .074 14	-.087 .597 39	-.175 .281 40	.335* .037 39		**	*
Sales-Hours on phone per month	Pearson Correlation Sig. (2-tailed) N	.064 .760 25	-.454* .044 20	.091 .703 20	-.320 .337 11	.289 .115 31	-.332 .165 19	-.029 .925 13	-.195 .247 37	-.207 .214 38	.224 .182 37	.728** .000 37		
Fin-Hours on phone per month	Pearson Correlation Sig. (2-tailed) N	-.086 .682 25	-.337 .136 21	.211 .360 21	-.125 .698 12	.184 .306 33	-.055 .818 20	-.682** .007 14	.068 .683 38	-.154 .350 39	.168 .313 38	.323* .048 38	.221 .189 37	

** Correlation is significant at the 0.01 level (2-tailed).

* Correlation is significant at the 0.05 level (2-tailed).

In comparing our correlations with the expectations of Phase One we find that overall, Phase Two lends some support to the findings of Phase One. It showed statistical relationships between certain combinations of analysts' priorities, actions and performance outcomes. However, there were more and stronger relationships between actions and success, than between either of those two bases and priorities. In accordance with Phase One, FDs appear to have informational centrality, while sales people appear critical to analysts' relationships with FMs. For the elite of analysts who have top 300 ranking, corporate finance is a relatively large part of their work. There is however, a potential intrinsic conflict between the finding that all communication levels (as measured here by 'phone use) are linked to more communication with FDs, whereas phase one suggests this is unhelpful to ranking from FDs. Nevertheless more communication between analysts and salespeople or FMs is well linked to success, as Phase One suggested.

In summary, success appears to be partly explained by an analyst's higher level of priority and, especially, communication with secondary market participants - both salespeople and Fund Managers. But success in secondary markets appears linked to

success in primary markets, with the highest ranked analysts of all spending more time with corporate finance. The implications of these findings and those from Phase One are discussed in the next section.

How Analysts Compete

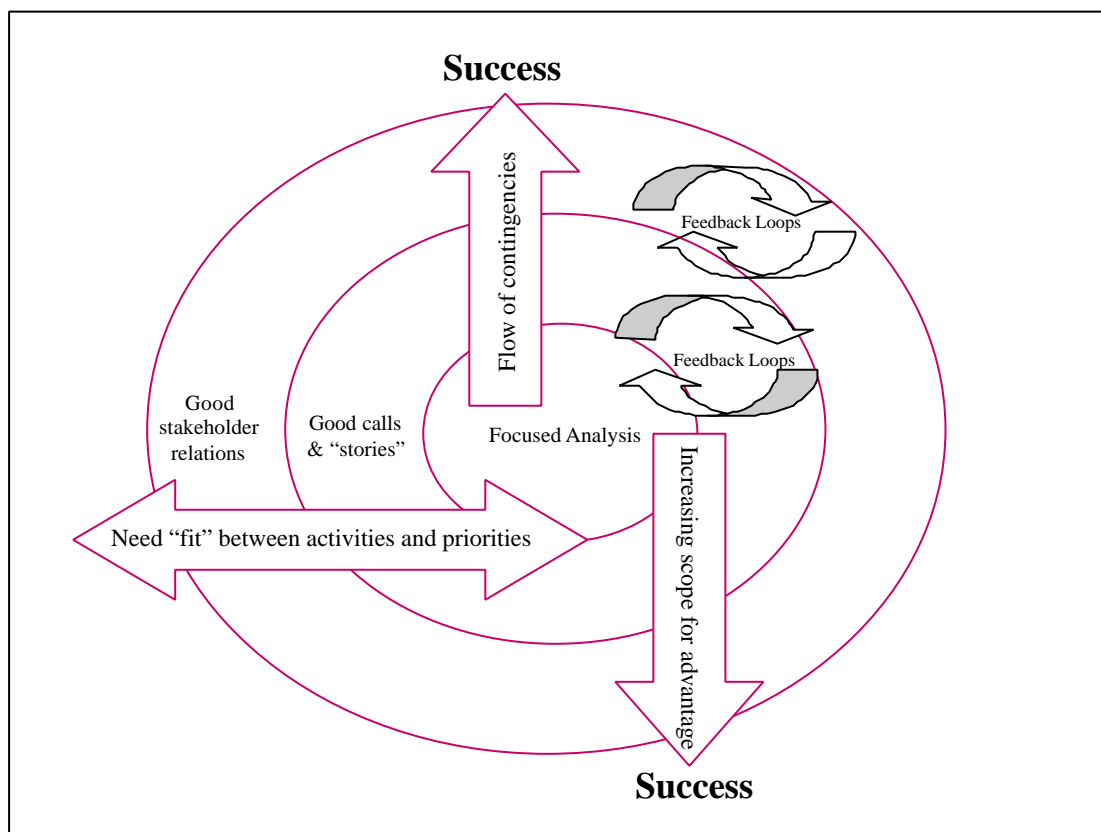
A model of sources of success for analysts is derived below, and implications drawn from it. We next discuss the contribution of this paper to prior literature and then conclude this section with suggestions for practitioners.

Success for equity analysts appears, from Phase One, to depend most strongly on their ability to manage relationships with stakeholder groups, and particularly to manage conflicts of interest between those groups. The important stakeholder groups, as defined by analysts in Phase One, are the equity salespeople and financiers inside the analysts' bank, and, external to the bank, FM clients and the FDs of analysed companies. Successful analysts spend longer than less successful analysts in communicating with those groups most involved in secondary markets; the FMs and equity salespeople. Moreover, the reputational advantage created from high rankings appears to create positive feedback within all the stakeholder groups, thereby establishing an elite of analysts who are almost universally perceived as far better than most.

Analysts' activities and therefore the basis for advantage are best understood in terms of the social network defined by stakeholder groups. Analysts act to bind the interests of the four stakeholder groups. This centrality is explained by analysts' role in distributing analysis that serves the commercial interests of each group. Analysts form the sole group for which commercial incentives coincide to a significant degree with all groups. Moreover, informational analysis and distribution is not merely mechanical; Phase One suggested that it is influenced by perceptions of, for example, trust, reliability, or market knowledge. In short, analysis is coloured by relationships. Those analysts best able to collectively manage, or "serve" the stakeholder groups and relationships are hypothesised to achieve the greatest centrality and therefore success.

We now link the discussion of the analyst's tasks and interactions to a conceptual performance model. Stakeholder relations depend on the nature of communications from analysts. The essence of communication is in "good calls" and engaging "stories" relating to equity valuation. This, in turn, depends on focused analysis (thorough research, based on detailed knowledge) from the analysts. Along with the nested contingencies in each of these "levels", there are feedback loops. For example, good relations with FMs can lead to good feedback to FDs and hence, in reciprocation, fuller comments from FDs, which leads to more "thorough" analysis. In this way, a high ranking for an analyst can be seen as both an outcome and a cause of success. Greatest scope for analysts to succeed is in creating and managing stakeholder relations. An abstract of this performance model is provided in Figure 13 below.

Figure 13: A Performance Model for Brokers' Equity Analysts



Compared with prior studies (c.f. Arnold and Moizer, 1984), the role of the analyst now appears to enlarge and distort. For example, analysis of the economic value or derivation of analysts' recommendations should take account of their use to FMs.

Evidence suggests that FMs take “ideas” more than specific stock recommendations from analysts. The analysis of the economic value of recommendations is, from the FMs’ perspectives, near worthless, as evinced by the virtual absence of such research on their own behalf. In partial support of Barker (1998a), it is difficult from the evidence to see how most (but not all) analysts could be influential in determining equity prices. Analysts’ roles in prior research into stock price volatility or determination (c.f. Bulkley and Harris, 1997) appear overstated.

There is prevalent in virtually all stock market research a view of participants (including analysts) that is, in the terms of Granovetter, (1985) “socially atomised”. This paper suggests that analysts’ roles and actions can be better interpreted as embedded within social networks defined by stakeholder groups; a view more socially-based than, for example, Barker’s (1998a) two-part characterisation. The stakeholder perspective helps explain why analysts face so many allegations of bias. Furthermore, it suggests ways to understand the likely outcome of attempts to legislate against or otherwise control such bias.

The authors argue that this exploratory study has highlighted the importance of social networks in understanding competition amongst analysts. With this realisation we might also suggest that the social network view be extended to analysis of sources of competitive advantage amongst, for example, entire investment banks or venture capital companies. The issues of reputation and influence are similarly material, with DeMarzo et al (1997) a rare attempt to model quantitatively features relevant to equity markets.

The conceptual model of analysts’ roles and influences developed within this paper offers a basis for further examining analysts and each of the four stakeholder groups. The authors argue that it contributes to a more grounded view of the analysts’ role and context, and suggests opportunities to explore behavioural aspects of equity analysis, such as the value of trust to market participants, or social-determinants of investment decision making.

{Note that supporting material to this research, such as the questionnaires or respondents’ details, can be supplied on request.}

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