'Slow' stock analysts do best, says new study

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Whether it's a rich, creamy risotto gradually stirred to perfection, or the story of the turtle and the hare, there are plenty of examples showing that a slow and steady approach can be the key to success.

Add slow stock analysts to that list. Portfolios that lean on the advice of

analysts who take an average of 20 months to change their recommendations to sell, buy, or hold a company's stock have been found to perform 5 to 10% better than portfolios that follow "fast" analysts—those who change their recommendations an average of every six months.

The recent research from the University of Toronto's Rotman School of Management showed that slow analysts were found to have longer careers, work for top brokerages serving large, institutional investors, have better professional reputations and be more influential in the marketplace. Their recommendations were bolder and tended to "lead the pack," with other, faster speed-style analysts following behind.

Slow analysts didn't get there just by gaining experience, either. Fast analysts typically based their recommendations on quantifiable information accessible to everyone, such as regular earnings announcements. Slow analysts changed their recommendations based on their interpretations of more complicated, softer information, such as news about operations strategy, mergers and acquisitions, and legal matters. This information was also more revealing about underlying firm value.

"Many older analysts are slower because they were slow to begin with and they end up lasting in the profession," says researcher Chay Ornthanalai, an associate professor of finance at the Rotman School. "The fast ones don't last long. They get terminated because they're bad.

"The main message here is, if you're really good, you do not need to update your recommendation that often because your initial recommendation will be correct," says Prof. Ornthanalai.

The study looked at stock recommendations from more than 4,500 analysts between 1996 and 2013. It introduced a method of classifying

the analysts according to the speed of their recommendation changes—fast, slow, or average—the first research to do so. Then, it linked the analysts to information about their careers and industry reputations. Analysts averaged nearly seven years of experience and followed about seven companies each.

Prof. Ornthanalai and his team additionally pored over 2,000 analyst reports to get insight into the rationale for their decisions. These revealed that even though slow analysts changed their recommendations less frequently, they were constantly engaged with assessing a company's value and updating their forecasts.

The research shows that good analysts fulfill a valuable role in the market and economy, even in an age of machine learning, says Prof. Ornthanalai.

"A lot of media have said that you don't need analysts anymore; machines can replace humans," he says. "We show that the human component is still important in interpreting and distilling difficult and especially soft information."

The study represents the last published work of Kent Womack, a much beloved finance professor at the Rotman School who died in 2015. Prof. Womack joined the Rotman School after a period at the Tuck School of Business at Dartmouth, where he built on his experience at Goldman Sachs to become a leading expert on the role of equity analysts and underwriting. He initiated the research, and Prof. Ornthanalai spent several years piecing together Prof. Womack's notes in order to finally publish the study.

The study was co-authored by Profs. Ornthanalai and Womack with Prof. Romain Boulland of ESSEC Business School. It appears in the *Journal of Financial and Quantitative Analysis*.

More information: Romain Boulland et al, Speed and Expertise in Stock Picking: Older, Slower, and Wiser?, *Journal of Financial and Quantitative Analysis* (2022). DOI: 10.1017/S0022109022000199

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