Do they stay or do they go? Entrepreneurial moves of top analysts

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Does individual performance affect entrepreneurial mobility within the investment banking sector or are company retention policies to blame?

Every year Institutional Investor magazine publishes an all-star list of the world's best research analysts. This influential ranking carries so much clout that making the list can mean hundreds of thousands of dollars in extra pay. Gaining a star ranking is also a surefire guarantee that headhunters will soon be beating a path to your door. Indeed, there are few other professions where professional performances are rated so publicly and so specifically by outsiders.

Given this, Boris Groysberg and Ashish Nanda of Harvard Business School and Julia Prats of IESE felt that research analysts would make an ideal specimen to study in trying to observe mobility patterns and entrepreneurial initiative among those ranked as stars (high performers) and those not.

Researching the researchers

In their paper, "Does Individual Performance Affect Entrepreneurial Mobility? Empirical Evidence from the Financial Analysis Market," the authors focus on sell-side analysts. These analysts are employed by brokerage houses to follow companies in a particular sector or specialty and to generate information such as earnings forecasts, stock recommendations and company reports. This information is used by those on the buy-side, such as money management firms and mutual, hedge and pension funds.

Previous research has found that analysts in *Institutional Investor's* "All-America" rankings tend to supply more accurate earnings forecasts than other analysts and make recommendations that don't just follow the pack. Therefore, the authors of this study decided to focus on nine issues of Institutional Investor magazine's "All-America Research Team" listings, between 1988 and 1996, to identify equity analysts who had made the grade. They then homed in on only those star analysts working at the 24 top U.S. investment banking firms, which accounted for 3,408 ranked analysts.

Next, using an investment research directory, they identified 6,123 unranked analysts also belonging to the same 24 firms, making a combined sample of 9,531 names.

On average, an analyst in the sample had 7.62 years of experience, had worked at the same firm for 5.27 years and had held 1.59 jobs. Just over three-quarters of the analysts were men.

Once again, with a rich amount of data quite readily available, the authors tracked turnover among these analysts over the same nine years and were able to identify for each year whether they had stayed with their original firm, moved into entrepreneurship, moved to competitors within the research industry or moved to companies outside the research industry.

During this period, they identified 1,718 total moves and an annual turnover rate of 18.6 percent.

Of the analysts who moved, 45 became entrepreneurs and 1,673 represented other turnover - that is, they either moved to competitors, moved to buy-side, ended up joining the firms they had been covering for years, or in some cases were laid off, retired or died.

Of the moves to entrepreneurship, star analysts accounted for 28 of the 45 moves to strike out on their own. Forty-four launched money management firms, hedge funds or research and advisory companies. One analyst, who also had a star rating, started an airline.

"All new ventures were established in the areas in which analysts specialized, suggesting that analysts attempt to leverage sector-specific skills in their entrepreneurial ventures," the authors observe.

While the percentage of star analysts who actually went on to become entrepreneurs is small, the authors believe it can be argued that research analysts are using the understanding of the various issues that they have gained to make contributions elsewhere.

The authors also note that moves by some firms to allow their analysts to operate as independent franchises within the same company may help to retain them, and this, too, may account for the small percentage of entrepreneurial analysts who choose to jump ship.

The authors went on to analyze their data against a wide range of variables at different levels, such as those impacting individual analysts, their firms or their sector, plus relevant macroeconomic conditions.

They specifically focused on the probability of star and non-star analysts becoming entrepreneurs, their likelihood of leaving their firm for other reasons, and the effect of "stardom" on new firm survival.

The stars go solo or stay

Previous studies have found that the lure of wealth increases the probability of someone becoming an entrepreneur, but the authors disagree.

"We believe that the decision (to become) an entrepreneur in a talent-based occupation is closer to the idea of mastering the environment instead of triggered by the comfort of a wealthy position. New ventures in a professional setting do not require great investment; (they) require a great deal of personal confidence and client/market understanding," they write.

The authors found that star analysts are indeed more likely than non-star analysts to become entrepreneurs and that their ventures were more likely to survive.

Interestingly, they also found that in looking at staff turnover for reasons other than a move to entrepreneurship, star analysts are less likely than their non-star counterparts to leave.

"Established all-star performers are more likely to stay with their firms or choose entrepreneurship," they say.

The authors point out that in light of these findings, companies and their human resources experts might need to rethink their approach to retaining their elite staff.

"Whereas firms try to minimize turnover to competitors, at the same time, they might be maximizing entrepreneurial turnover. To our knowledge, no study has been able to establish what mobility is more damaging to the firm," they warn.