1. Introduction

The important role of analysts in financial markets is undisputed. Analysts are important to a variety of market participants and add value by gathering and summarizing important information from a variety of sources and derive new informational content through their analysis (see Ivkovic and Jegadeesh, 2004). Furthermore, past research indicates that the consensus opinion of analysts affects stock prices and trading volume (see Stickel, 1995; Barber, Lehavy, McNichols, & Trueman, 2001). At the same time, the quality of analysts’ forecasts has been extensively discussed, however the consensus is rather gloomy. Kahneman (2011) states that “Professional investors, including fund managers, fail a basic test of skill: persistent achievement.” At the same time, examining analyst forecasts as a proxy for the overall quality of experts accuracy is partially distorted by analysts being a relatively homogenous group and affected by each other in the form of herding behavior (see DeBondt and Forbes, 1999; Hong, Kubik, & Solomon, 2000).

Thereon, we make use of the Livingston Survey data, in order to evaluate the forecasting ability of individuals from alternative affiliations, namely academic institutions (A), commercial banking (B), government (G) as a combination of the Federal Reserve and governmental institutions, investment banking (I) and non-financial businesses (S). Given the structure of the survey, we can utilize forecast expressed directly towards the S&P 500 and thereby bypass the issue of forecast errors being affected by the quality and availability of firm specific information (Das, Levine, & Sivaramakrishnan, 1998). Furthermore, we overcome the issue of cross-sectional variation in forecasting accuracy caused by jointly evaluating analyst forecasts towards alternative underlying’s (see Jacob et al., 1999; Hong et al., 2000).

Results in this study indicate, in contrast to Kahneman (2011), that professional investors do indeed show persistence, however in the form of under achievement due to an optimism bias. We examine the forecasting performance of professionals, when sorted into categories according to their affiliation, and find a considerable amount of evidence for diverse characteristics. Secondly, by applying zero-month ahead implied returns based on data available since 1992, we mitigate the base date problem and can incorporate short-term forecasts. Finally, we investigate the influence of business and market cycles on the quality of forecast, which yields insight on the drivers for observed differences between affiliations.

The remainder of the paper is organized as follows. In Section 2 we provide an overview on the existing empirical studies concerned with the Livingston Survey. In Section 3 we describe the dataset, paying particular attention to the newly introduced 0-month ahead 6-month ahead forecast. Section 4 provides the methodological groundwork on deriving forecasts by accounting for non-unified response dates and respective forecasting accuracy. Section 5 presents the empirical results, controlling for a possible misspecification of the loss function with respect to rationality tests of Livingston forecasts; and Section 6 concludes.
2. Prior literature

Due to the limited availability of solid survey records, literature analyzing the forecast accuracy of quantitative data outnumbers qualitative ones. Nevertheless, a handful of papers consider questionnaire based, or company related datasets, relying mostly on one of the following sources: the UBS/Gallup poll (see, for instance, Bachetta, Mertens, & van Wincoop, 2009), the Thomson Reuters I/B/E/S analyst recommendation database (see, for instance, Womack, 1996) and, predominantly, the Livingston Survey, which is subject to this study. Maintained since 1990 by the Federal Reserve Bank of Philadelphia, this database emerged in the 1950s, when columnist Joseph A. Livingston started to question decision makers about expected stock market changes. As economists come from a variety of institutions, survey members cover the fields of academia, banking, governmental institutions and non-financial businesses as well. A unique property of this dataset over other surveys is its impressive history, which reduces the likelihood of biased out-of-sample estimations. As the questionnaire is handed out biannually, over 60 years of data is available providing 6 and 12-month ahead estimations of the S&P Composite index. Additionally, the panel is not exposed to member specific serial correlation as participants change annually and rarely reappear.

Literature related to Livingston's dataset has existed since 1980s, predominantly because the sample size reached an adequate extent around that time. While later studies primarily examine predictive power, earlier contributions solely focus on the statistical properties of the Livingston panel. In an initial study, Lakonishok (1980) observes the expectations of survey participants in order to find evidence for the assumptions of the Capital Asset Pricing Model and concludes that the data does not meet the condition of efficiency. Brown and Maital (1981) conduct an analysis on biasedness and completeness of predictions and aim to answer the question of whether the dataset fulfills rational expectations. The authors show that experts’ forecasts are in general unbiased, but cannot confirm the complete use of all relevant and known information. Pearce (1984) reports similar results. Dokko and Edelstein (1989) introduce a new approach to overcome the base date problems of Livingston’s data and find in contrast to earlier studies that forecasts specifically for stock markets are unbiased and rational, i.e. that fulfill the hypothesis of adaptive expectations. Supporting evidence comes from Croushore (1997), which underlines the statistical benefits of the permanently increasing sample size of the panel. Accordingly, tests around the turn of the century became more reliable and the dataset today proves to be a meaningful instrument for measuring the forecasts of economists. Considering the predictive power of experts, De Bondt (1991) applies the methodology of generating returns upon base dates and finds that even naive, i.e. permanently positive, forecasts beat sample participants. Experts are lacking not only magnitude, but also the direction of forecasts. Furthermore, De Bondt (1991) investigates the dataset during bullish and bearish market periods and is unable to determine significant differences. Soederlind (2010) provides a recent study with in-depth analysis of the Livingston Survey. Following the approach of Dokko and Edelstein (1989), his findings also reject the reliable forecasting ability of panel participants. Moreover, it identifies a typical error pattern of experts that goes along with over fitting qualitative predictors. Extending existing research on the Livingston Survey dataset, this paper takes a new turn by dissociating from consensus forecasts and specifically evaluating professionals based on their current affiliation. Additionally, through calculating zero-month ahead returns for the first time, it contributes to the base date problem related to this dataset.

3. Sample

This study relies on Livingston Survey data published by the Federal Reserve Bank of Philadelphia. The survey is conducted twice a year and gathers forecasts regarding various macro-economic variables. In April/October the survey is distributed and panel members are to return their forecasts by the end of May/November. Subsequently, the data becomes publicly available beginning of June/December of the respective year.

We solely focus on forecasts of the S&P Composite index, which are recorded since 1952. Participants report 6 and 12-month forecasts, which are actually forecasts for 7 and 13 months into the future given a 1-month processing period. As of 1992 panel members are additionally requested to provide zero-month forecasts in order to account for this 1-month lag. Thereon, zero-month forecasts refer to estimates of end-of-month index values of the publication month (i.e. 30th June and 31st December). Fig. 1 illustrates the process of collecting the data and deriving forecasts, as discussed in the following section.

We build on forecasts from economists categorized into five alternative affiliations, namely: academic institutions (A), commercial banking (B), government (G) as a combination of the Federal Reserve and governmental institutions, investment banking (I) and non-financial businesses (S). For aggregating individual data, the Fed Philadelphia offers series calculated as means and median values. In contrast to existing literature, we opt for mean values within affiliations in order to account for categories with a reoccurring tendency for extreme values. In line with category forecasts

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1. Alternative variables for which forecast are gathered include: short- and long-term interest rates, CPI and PPI, unemployment rate, GDP and others.
2. Historically panel members where sorted into 10 alternative affiliations, but for a number of categories no sufficient record is available, while others have been discontinued. Moreover, the affiliation of some panel participants is labelled as unknown.
3. Note that aggregated data also includes observations of categories that are not specifically subject to this paper. Not covered affiliations are as follows: consulting, industry trade groups, insurance companies and labour unions. Participants with unknown affiliation are represented as well.

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