Andreas Krause



Chapter 8.1 Financial analyst access to company information

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Financial analysts should provide the best forecast possible

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Information and forecast

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Information and forecast

Financial analysts obtain a signal of the current value

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Forecast error

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Financial analyst would minimize the forecast error
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• Financial analyst would minimize the forecast error $\Pi_B = E\left[\left(\hat{P} - P\right)^2 \middle| s\right]$ • $\Pi_B = E\left[\left(\hat{P} - E\left[P|s\right]\right)^2\right] + Var\left[P|s\right]$

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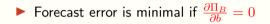
Financial analyst would minimize the forecast error Π_B = E [(P̂ - P)²|s]
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Bayesian learning gives Var [P|s] = 1/(σ²_P + σ²_s)

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Bayesian learning gives Var [P|s] = 1/(π¹/_p + π²/_{σ²})
Π_B = b² + 1/(π¹/_{σ²} + π²/_{σ²})

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• Forecast error is minimal if
$$\frac{\partial \Pi_B}{\partial b} = 0$$
, or $b = -\frac{1}{2} \frac{\partial \sigma_{\varepsilon}^2}{\partial b} \left(\frac{\sigma_P^2}{\sigma_p^2 + \sigma_{\varepsilon}^2} \right)^2$

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Properties of the bias

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Properties of the bias

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Companies prefer positive analyst coverage

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Companies prefer positive analyst coverage and can encourage that by granting more access to information in return for more positive coverage



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- Minimizing their forecast error trades off the biased prediction against access to better information



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