Analyst Forecast Accuracy and Firm Layers in Affiliated Business Groups: Local and Foreign Analysts

Chen, Yu-Ju; Chin, Chen-Lung

Abstract

Business groups are an important organizational form in many countries. Business groups typically take the form of a pyramid structure, and thus provide incentives for controlling owners to expropriate wealth from other members (referred to as tunneling). Thus, business groups and its members tend to have lower information transparency. This paper argues that the layer in which a firm is located within a business group is a key determinant of analyst forecast accuracy. We find that firms located in a lower layer have lower analyst forecast accuracy within an affiliated group. Secondly, we document that local analysts' information advantage over foreign analysts increases moving from higher layers to lower layers within a business group. Finally, we find that the local analysts' advantage is driven by expatriate analysts. Our results remain qualitatively unchanged after controlling for agency problems, proxied by the divergence between voting and cash flow rights of controlling owners.