Diversified Firms and Analysts’ Earnings Forecasts: The Role of Management Guidance at the Segment Level

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October 31, 2018

Acknowledgements

We thank Marco Fasan (JIAR conference discussant), Wolfgang Schultz (editor), Alessandro Ghio, Mark Clatworthy, Giorgio Gotti, Ole-Kristian Hope, Michel Magnan, Andreea Moraru-Arfire, Linda Myers, Bernard Raffournier, Donna Street, Jason A. Voss, Holly Yang (EAA discussant), participants at the HEC Montréal and University of Bristol research workshops, EAA 2015 Glasgow, AMIS 2016 Bucharest, AAA 2016 New York, EUFIN 2018 Stockholm, and JIAR 2018 Venice for valuable comments. We thank Anna Cherkas, Xiao Sun, and Lio Tong for excellent research assistance. This paper is based on the third chapter of Rucsandra’s dissertation at ESSEC Business School. Part of this work was supported by the Concordia University FRDP start-up grant.
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Abstract

Using a unique, manually-collected dataset, we are the first to analyze the role that management guidance about segments plays for financial analysts’ earnings forecasts of diversified firms. About half of the diversified European firms in the sample provide segment-level guidance (SLG), with considerable variation in precision and disaggregation. We find that (1) analyst earnings forecast errors are smaller, and (2) the magnitude of disagreement between individual forecasts and the average forecast is lower for the firms that provide SLG, beyond the effect of group-level guidance. The results hold in matched samples and within-firm analyses around SLG initiation. We further show that the results are stronger in situations characterized by higher information asymmetry, but not in situations characterized by operational complexity. Overall, the results imply that SLG mitigates to some extent the difficult task that financial analysts face when valuing diversified companies.

Keywords

Management guidance; Segment disclosure; Financial analysts; Analyst earnings forecasts; Corporate diversification