Stock market liberalization, investment banks, and analyst forecast quality:

Evidence from a quasi-natural experiment in China

Baolei Qi
School of Management, Xi'an Jiaotong University, China
baoleiqi@xjtu.edu.cn

Donghui Liu
School of Management, Xi'an Jiaotong University, China
3124108132@stu.xjtu.edu.cn

Zeyu Sun*
Bay Area International Business School, Beijing Normal University, China
zeyusun666@bnu.edu.cn

Declarations of interest: None
JEL codes: G18 G24 M40

*Corresponding author: associate professor, #18 Jinfeng Road, Tangjiawan, Zhuhai City, Guangdong Province, China, 519087.

We acknowledge the support from National Natural Science Foundation of China (72172116).

Stock market liberalization, investment banks, and analyst forecast quality: Evidence from a quasi-natural experiment in China

Capitalizing on a quasi-natural experiment in China where certain investment banks become investible to the global market across different periods, we explore the role that stock market liberalization plays in shaping local analysts' incentives to provide high quality forecasts. In a staggered difference-in-differences research design to improve identification, we find that analysts affiliated with liberalized banks (i.e., pilot analysts) significantly reduce the errors and bias in their earnings forecasts from the pre-liberalization period to the post-liberalization period, relative to non-pilot analysts whose employers remain under strict capital controls during the same timeframe. Consistent with expectations, this result is concentrated among local investment banks that are smaller, have higher existing institutional ownership, and have stronger tournament incentives. Additionally, we identify three specific changes in analysts' forecasting practices following market liberalization. Our analysis provides insight on the importance of financial globalization to the institutional environment of a country's capital market.

Keywords: stock market liberalization, investment banks, analyst forecast quality

JEL Classification: G18; G24; M40