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The Risky Business of Hiring Stars

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Research Setting & Data Set

- 1,052 star stock analysts who worked for 78 investment banks in the United States from 1988 through 1996
  - ✓ Star = *Institutional Investor* ranking
    - Ranked analysts generate more accurate and more frequent forecasts, and their reports have a bigger impact on stock prices
    - In 1996, less than 5% of all the analysts in the United States were ranked analysts
  - ✓ Why focus on star analysts?
    - Stock analysts suffer few distractions when they change companies
    - Most companies and executives believe that the performance of analysts, especially that of stars, depends on their talent

Impact of Move on Star's Performance

- The star's performance fell sharply and stayed well below his old achievement levels
  - ✓ Stars that moved significantly underperformed stars that stayed in the year after the move
  - ✓ Performance didn't climb back to that of non-movers even five years later
- Stars that moved don't stay with their new firms for long
  - ✓ Turnover rate of stars that moved in the past was significantly greater (36% within 36 months, another 29% in the next 24 months) than for star that didn't

Impact of Star Move on Hiring Firm

- Each time the firms announced that they had hired a star
  - ✓ Stock prices of the investment banks we studied fell by 0.74%, on average
  - ✓ Investors lost an average of $24 million
  - ✓ Why?
    - Winner's curse
    - Performance of star hires declined post-move
    - Performance of other professionals in the group hiring the star declines
    - Star's recruitment was a signal of the hiring company's weakness

Drivers of Star Performance

- An analyst's performance is driven by:
  - ✓ the analyst's ability *and*
  - ✓ the platform the firm provides the star
- Platform matters:
  - ✓ Performance drop was most pronounced and extended over five years after a star analyst moved from bulge bracket to smaller firm
  - ✓ When stars hopped between companies with similar capabilities, their performance dipped for only two years
  - ✓ The performance of analysts who migrated from smaller to bigger firms did not dip significantly
  - ✓ Stars who brought with them teams of research analysts, salespeople, and traders performed better than stars who moved solo

How Firms Grow Stars

- Three approaches:
  - ✓ Hire people, don't do much to develop or retain them, but focus on retaining the high-level stars developed and brought in from outside
  - ✓ Recruit smart people and develop some into stars, knowing that they may be lost to rivals
  - ✓ Recruit bright people, develop them into stars, and do everything possible to retain them
- The third approach:
  - ✓ leads most frequently to long-term success
  - ✓ develops more stars, faster
    - Example: Between 1988 and 1996, Sanford Bernstein made a star out of one in five analysts; Merrill Lynch's rate was one in 30; it took analysts at Merrill Lynch 12 years, on average, to climb to star status; at Sanford Bernstein it took 4 years

The Challenge of Hiring Stars

- Should companies ever hire stars?
- From 1988 to 1996, only three of the 24 investment banks we studied in depth were able to integrate star analysts into their organizations
- Stars are hired to:
  - ✓ Enter new businesses (37%)
  - ✓ Strengthen existing research teams (17%)
    - Performance declined most acutely
  - ✓ Replace star analysts who had left (27%)
  - ✓ Replace non-star analysts who had left (20%)
  - ✓ Performance did not decline

- On balance, the war for talent is won not by hiring stars but by systematically growing them