SOCIOPOLITICAL DYNAMICS IN RELATIONS BETWEEN TOP MANAGERS AND SECURITY ANALYSTS: FAVOR RENDERING, RECIPROCITY, AND ANALYST STOCK RECOMMENDATIONS

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We examine how the disclosure of negative firm information may prompt top executives to render personal and professional favors for security analysts, who may reciprocate by rating firms relatively positively. We further examine how negative ratings may prompt executive negative reciprocity toward an analyst and how such retaliation may deter other analysts’ negative ratings. Because analyst recommendations influence investor behavior, firm reputation, and access to capital, our theory and supportive findings suggest that corporate leaders enhance and perpetuate external support for their firms via social influence processes that develop and maintain social exchange relations with a key type of external constituent.

A primary responsibility of top executives is to maintain the support of key external constituents for their firms (Hambrick, Finkelstein, & Mooney, 2005; Mintzberg, 1973, 1983). Yet, the academic literature on corporate governance and strategic leadership has devoted surprisingly little attention to the behavioral mechanisms by which executives influence external constituents. Most research in this literature has examined how executives exert influence over internal constituents of a firm, such as corporate board members, in the process of formulating or implementing strategy (for reviews, see Cannella, Finkelstein, and Hambrick [2005], Carpenter, Gelekanycz, and Sanders [2004], Hillman and Dalziel [2003]). Nevertheless, two theoretical perspectives in organization studies have posited behavioral mechanisms by which firms can exert control over external constituents. Resource dependence theory suggests how leaders use formal mechanisms such as board appointments to co-opt external constituents into supporting their firms (Pfeffer & Salancik, 1978). Empirical research has shown, however, that appointing an external constituent to the board can result in “infiltration” rather than cooptation, whereby the constituent uses their board position to exert influence over the firm rather than vice versa (Mizruchi & Stearns, 1988: 206; 1994). This scenario has become especially likely in recent years, as boards are increasingly expected to exert independent control over management decision making and behavior (Johnson, Daily, & Ellstrand, 1996; Carpenter, Gelekanycz et al., 2004).

More recently, theory and research on symbolic management has shown that leaders sometimes influence constituent decision making and behavior by engaging in public actions or communications that lend the appearance of conformity to institutional logics or prevailing norms of corporate conduct. For example, Elsbach (1994) showed that leaders effectively manage constituent impressions of their organizations following controversial events by issuing public statements that acknowledge the controversy while highlighting the adoption of legitimate structures and procedures that give the appearance of resolving stakeholder concerns about the organizations. And Westphal and Zajac (1998; Zajac & Westphal, 2004) provided evidence that corporate leaders attract investors to their firms by formally adopting executive incentive plans or other policies that appear to demonstrate or ensure leaders’ commitment to shareholder interests, while issuing public statements that align these policies with prevailing institutional logics of corporate governance (also Carter, 2006; Certo, 2003; Fiss & Zajac, 2004; Porac, Wade, & Pollock, 1999; Stevens, Steensma, Harrison, & Cochran, 2005; Zott & Huy, 2005).

Although this research has advanced understanding of how corporate leaders influence the decision making and behavior of external constituents, it has not addressed what may be a primary source of influence in leader-constituent relations.
The larger literature on power and social influence suggests two general mechanisms by which leaders can gain and maintain support from external constituents (Bowles, 1987; Edelman, 1977; Pfeffer, 1981). Leaders can garner external support by engaging in public actions and communications that symbolically demonstrate their commitment to constituent interests, and on a more private level they can also enhance or maintain constituent support by engaging in social influence processes, such as favor rendering, that develop or maintain social exchange relations with individual constituents. Although research on power and influence in government and other settings suggests that both influence mechanisms can be effective in maintaining constituent support (Bowles, 1987; Edelman, 1977; Pfeffer, 1981), the organizational literature on leader-constituent relations has generally focused on public symbolic management to the exclusion of private social influence and exchange processes. More specifically, this literature has devoted little attention to how leaders garner external support for their organization by engaging in individual-level social influence processes that develop or maintain social exchange relations with key constituents of the firm. In the present study, we address this gap in the literature by examining social influence and reciprocity in relations between top executives and a key external constituent of firms; namely, security analysts.

Security analysts guide investor behavior by interpreting and disseminating information about corporate finances, strategic decisions, and industry trends, and by rendering summary judgments about the firms that they follow (Hayward & Boeker, 1998; Jensen, 2004; Rao, Greve, & Davis, 2001; Zuckerman, 2000). Those judgments include recommendations about whether to buy, hold, or sell particular securities. There is extensive evidence that analysts’ stock recommendations have a material impact on trading behavior and stock market valuations (e.g., Ho, 1995; Ryan & Taffler, 2000; Womack, 1996). Changes in stock market valuations, in turn, influence a firm’s capacity to raise capital and affect its general reputation, ultimately influencing its corporate strategy (e.g., acquisition strategies) and compensation policies (e.g., level of executive compensation) and impacting the reputation and career prospects of the firm’s top executives (Fombrun, 1996; Hayward & Boeker, 1998; Kuperman, 2003). Given the wide-ranging impact of their judgments, security analysts are an important external constituent of a firm. Thus, we focus in this study on relations between top executives and security analysts. In particular, we draw from theory and research on interpersonal influence, reciprocity, and social exchange to suggest (1) how the disclosure of negative firm information may prompt top executives to engage in social influence tactics directed toward security analysts, in the form of personal and professional favor rendering, and (2) how such favor rendering may prompt analysts to reciprocate by issuing relatively positive ratings of the firm. We also extend our theoretical framework to consider how a relatively negative analyst rating may prompt executives to engage in negative reciprocity or retaliation against the analyst, and how such negative reciprocity may deter other analysts from issuing relatively negative ratings about the firm in the future. We test our theoretical perspective with a unique data set that combines large-sample survey data on manager-analyst relations with archival data on analyst stock recommendations. Given that analyst reports have a significant influence on the behavior of investors and other members of the financial community toward a focal firm, including bankers, debt holders, and ratings agencies, our theory ultimately suggests how corporate leaders can enhance and perpetuate external support for their firms by engaging in social influence processes that develop and maintain social exchange relations with a key external constituent of the firms.

This study also contributes to the literatures on financial market behavior and corporate control. Normative theories of corporate governance and strategy suggest that security analysts’ stock recommendations have the potential to serve a critical role in corporate control (Fama & Jensen, 1983; Rao et al., 2001; Wright et al., 2002). By issuing negative recommendations in response to poor performance or to strategic actions that advance the interests of top executives rather than shareholders, analysts can steer capital and other resources away from “underperforming” firms, limiting the ability of those firms to pursue strategies that harm shareholder interests and deterring executives from engaging in such strategies. More generally, by rendering accurate and objective evaluations of the firms that they cover, security analysts have the potential to play an important role in maintaining the allocative efficiency of financial markets (Jensen, 2004; Zuckerman, 2000).

There is growing evidence, however, that analysts systematically “underadjust” their earnings forecasts and stock recommendations in response to negative firm information (Amir & Ganzach, 1998; Chopra, 1998). Explanations for this “stickiness” of stock recommendations in the face of negative information have focused primarily on cognitive factors such as overconfidence bias and the tendency to ignore disconfirming evidence (Hong &
Kubik, 2003: 314). Very little theory has addressed how social or political factors could contribute to overly positive analyst reports. Prior work has not examined how and when top managers may actively cultivate social relations with security analysts or how the interpersonal influence behavior of executives could contribute to positivity bias in analyst reports. This gap in theory and research is surprising, given that the normative literature on investor relations strongly advises top managers to develop relationships with analysts (e.g., Conger, 2004; Dolphin, 2004). In the present study, we begin to address this gap in the literature by developing a sociopolitical perspective on manager-analyst relations. Given that analyst recommendations have a significant influence on investor behavior, firm reputation, and access to capital, an implication of our theory is that microsocial factors in manager-analyst relationships, by reducing the objectivity of analysts’ reports, may ultimately have negative consequences for the allocative efficiency of financial markets and the quality of corporate control.

**SOCIAL INFLUENCE AND RECIPROCITY IN MANAGER-ANALYST RELATIONS**

Contemporary perspectives on social exchange suggest that reciprocity has both a normative and instrumental basis. The norm of reciprocity is a nearly universal code of moral conduct. As Gouldner (1960: 161) stated, quoting Westermarck, “To requite a benefit is probably everywhere ... regarded as a duty” (Ekeh, 1974; Molm, 2003). There is growing evidence from research in evolutionary psychology that humans are evolutionarily programmed to reciprocate favors (Fehr, Fischbacher, & Gachter, 2002; Friedman & Singh, 2004; Hoffman, McCabe, & Smith, 1998). Experimental research has shown that receiving favors induces a psychological state of indebtedness that most people find aversive, and which prompts a “heightened alertness and sensitivity to opportunities for its reduction” (Greenberg, 1980: 1; Uehara, 1995). The norm of reciprocity includes the obligation to accept favors when they are offered, as well as the obligation to repay them, so that social exchange can be initiated by unsolicited favors (Befu, 1980; Cialdini, 2001). The norm is flexible in that the things exchanged can be different in form and function and need only be roughly equivalent in value (Ashforth, 1993). The perceived obligation to reciprocate favors is thought to be particularly strong in dyadic exchange (Ekeh, 1974).

The instrumental motive for reciprocity is to increase the probability of receiving further favors in the future. Social exchange theorists have long argued that reciprocity is, in part, an act of reinforcement (Blau, 1964; Deckop, Cirke, & Andersson, 2003; Homans, 1958). According to Blau, “‘Social exchange’ refers to voluntary actions of individuals that . . . discharge obligations by reciprocating benefits in the interest of receiving further benefits, [such that] exchange processes utilize, as it were, the self-interests of individuals” (1964: 91). Although most individuals subscribe to the norm of reciprocity, there is evidence that a significant minority do not (Fehr & Gachter, 2000), and thus instrumental motives for reciprocity, such as the prospect of receiving more favors in the future, can increase the likelihood of social exchange (Ashforth, 1993). As a result, social exchange tends to be more pervasive in repeated interactions (Axelrod, 1984; Fehr et al., 2002; Sethi & Somanathan, 2003). There is also evidence from the literature on ingratiation and social exchange that positive affect toward the favor-doer motivates reciprocity: people tend to feel gratitude and liking toward those who have benefited them (Flynn, 2004; Lawler & Yoon, 1993). As Ekeh (1974) and other theorists have suggested, there are two separate traditions within the larger literature on social exchange (see also Molm, 2003). The first tradition allows for instrumental motives as an impetus for favor rendering and reciprocity, and contrasts social exchange with economic forms of exchange (e.g., Blau, 1964; Greenberg, 1980; Homans, 1958; Molm, 1997, 2003). According to Blau (1964), Molm (2003), and others, in economic exchange the contributions of each party are explicitly negotiated, and typically specified in a formal contract (cf. Deckop et al., 2003; Heath, 1976). In social exchange, “The expectation of reciprocity at a future time is left implicit” (Flynn, 2004: 739), as repayment is not assured by a contract (Blau, 1964: 95). Blau (1964) and Homans (1958) believed that reciprocity results primarily from individual self-interest, and only secondarily from generalized moral norms, but many of their followers have argued that norms and self-interest combine to prompt reciprocation of favors (e.g., Deckop et al., 2003; Greenberg, 1980; Molm, 2003). Empirical research in evolutionary biology and experimental economics has bolstered this view.

In the second tradition, which emerged primarily from anthropology, contributions to the exchange relationship are purely symbolic and function mainly to preserve group or societal solidarity (e.g., Mauss, 1954). In this study, we adopt the former perspective on social exchange. It should be acknowledged, however, that our theoretical analysis does not capture all aspects of social exchange discussed by Blau (1964). In particular, it does not capture the potential for social exchange relationships in organizational settings to develop over time into personal relationships characterized by interpersonal trust.
1993; Wayne & Kacmar, 1991; Wortman & Linsenmeier, 1977). As a result, people derive satisfaction from helping their benefactors, and they tend to be biased in the benefactors’ favor, which can lead them to allocate more rewards and benefits to their benefactors in the future (Barry & Fulmer, 2004; Liden & Mitchell, 1988; Yukl & Tracey, 1992). However, although instrumental motives and positive affect have been shown to increase the frequency of reciprocity, there is substantial evidence that most people reciprocate favors even in the absence of positive affect and without any expectation of receiving further benefits (as in one-shot exchanges between strangers) (Hoffman et al., 1998; Perugini et al., 2003; Webster, Smith, Rhodes, & Whatley, 1999). In fact, people are often willing to reciprocate favors from those whom they actively dislike (Cialdini, 2001), despite significant cost to themselves (Fehr & Gachter, 2000; Friedman & Singh, 2004).

Thus, the norm of reciprocity provides a “starting mechanism” in social exchange, as it reduces the risk of performing favors for another person without a contractual guarantee that reciprocal services will be rendered (Axelrod, 1984; Blau, 1964; Gouldner, 1960; Molm, 2003). As a result, social influence theory suggests that while the norm of reciprocity serves vital societal functions, it can also be manipulated or “exploited by [those] who recognize it as a weapon of influence” (Brass & Burkhardt, 1993; Cialdini, 2001: 22). Individuals can exploit the reciprocity norm to their advantage by rendering favors for those who have the power to benefit or harm them. Research on ingratiation in organizational behavior has provided empirical evidence that doing personal favors for powerful actors can lead to a wide range of beneficial outcomes, including more positive performance evaluations, higher compensation, recommendations for promotions, and prestigious appointments (e.g., Kipnis & Schmidt, 1988; Vonk, 2002; Westphal & Stern, 2006; Yukl & Tracey, 1992). Favor rendering directed at powerful actors is particularly effective in avoiding harmful actions (Cialdini, 2001; Gouldner, 1960) such as firings, demotions, or pay cuts (Westphal, 1998). As Molm (2003) and others have suggested, the norm of reciprocity dictates not only that people should look for opportunities to help those who have helped them, but also that they should be especially motivated to avoid taking actions that would actually harm their benefactors (when given the opportunity to do so, whether in the short term or longer term).

In the present context, we expected that by rendering favors for security analysts who followed their companies, top executives would increase the likelihood of relatively favorable treatment when the analysts rendered judgments about their firms. Top executives can perform a range of personal and professional favors for security analysts by drawing on their social contacts, status, knowledge, and personal experience. For instance, our preliminary interviews indicated that CEOs and CFOs sometimes help analysts acquire critical information about recent developments in an industry environment by putting them in contact with personnel of buyer and supplier firms, or by personally relaying valuable information gleaned from industry contacts. They may also offer to meet with an analyst’s clients, as such meetings are highly valued by institutional investors and reflect well on the analyst. Executives may perform personal favors for analysts such as recommending them for jobs, helping them gain entry to a private social club or other exclusive organization, or giving advice on a career matter. The receipt of such favors should induce a feeling of indebtedness toward the executives and motivate efforts to reciprocate. Given that favor rendering is especially effective in deterring harmful actions toward the favor-doer, an analyst who has received favors from an executive should be particularly averse to taking actions that would materially harm the executive’s interests, such as issuing a more negative recommendation on the executive’s firm. As noted above, stock downgrades tend to hurt market valuation and hinder access to capital, ultimately threatening the executive’s employment security, compensation, wealth, and reputation. Thus, social exchange theory would suggest that analysts should be more reluctant to downgrade a firm’s stock when they have received favors from the firm’s top executives.

Social influence tactics tend to be most effective when the decision-making process by which benefits are allocated is relatively complex or ambiguous, and thus difficult to monitor (Liden & Mitchell, 1988; Pfeffer, 1981). Analyst stock recommendations are typically based on complex, subjective assessments of a firm’s prospects (Jensen, 2004; Kuperman, 2003; Schipper, 1991), which should make it easier for analysts to rationalize positive ratings in the face of relatively negative information about the firm (Hayward & Boeker, 1998). To the extent that analysts are influenced by executive favors in issuing stock ratings, their recommendations should tend to be less predictive of future firm performance, which might be expected to hurt their career prospects. As noted above, however, the norm of reciprocity prompts most people to return favors despite material costs to themselves. And social exchange in this context in-
volves repeated interactions: analysts may reciprocate favors to positively reinforce executives' generosity and increase the likelihood of receiving more favors in the future. The professional and personal favors noted above may be critically valuable to an analyst's career. Thus, instrumental motives should supplement feelings of indebtedness and positive affect to perpetuate a mutually beneficial social exchange relationship between analysts and executives.

The Release of Negative Firm Information and Executive Favor Rendering toward Analysts

Top executives may be especially prone to render favors for security analysts in response to the release of negative or controversial information about their company. Social exchange theory suggests that the greater the instrumentality or utility to an actor of exchange with another actor, the greater the likelihood the first actor will render favors for the second (Blau, 1964; Molm, 2003). There is also considerable empirical evidence that the subjective expected utility of a social influence tactic predicts the extent to which people will use that tactic in their relations with powerful actors (Barry & Watson, 1996; Jones & Pittman, 1982; Porter, Allen, & Angle, 1981). Social influence from favor rendering should be particularly valuable in the face of negative information about an executive's firm. The release of such information has the potential to be a triggering event that prompts analysts to consider changing their recommendation. As noted above, there is evidence that favor rendering is particularly effective in deterring others from taking actions that harm the interests of the focal actor. And there is evidence that analyst downgrades have a stronger effect on trading behavior than upgrades (e.g., Frankel, Kothari, & Weber, 2006; Hirst, Koonce, & Simko, 1995; Womack, 1996). Thus, the release of negative information about a firm should increase the subjective expected utility of executive favor rendering toward security analysts.

In this study we examine how two kinds of firm announcements may influence executive favor rendering toward analysts: the announcement of earnings that are below consensus forecasts, sometimes referred to as a “negative earnings surprise” (Matsumoto, 2002), and the announcement of unrelated acquisitions. The consensus forecast for a particular firm is the average quarterly earnings forecast among all analysts who cover the firm, and an earnings surprise is the difference between the consensus forecast and the actual quarterly earnings reported by the company. Given that negative earnings surprises should tend to lower analysts' expectations regarding future firm performance, such announcements should tend to increase the risk that analysts will downgrade the firm's stock. Thus, our theoretical perspective suggests the following hypothesis:

Hypothesis 1a. The more reported earnings are below consensus forecasts, the greater the extent to which top executives render favors to security analysts who cover their firm.

We also examine the effect on executive favor rendering of announcing diversifying corporate acquisitions. The prevailing view among academic researchers and members of the financial community is that unrelated or diversifying acquisitions tend to have negative implications for shareholder interests. Negative sentiment regarding diversification has been attributed to the spread of an “agency logic” or “shareholder-value conception” of corporate strategy and governance that occurred from the mid 1980s through the 1990s (Davis, Diekmann, & Tinsley, 1994; Zajac & Westphal, 2004; Zorn, 2004). From an agency perspective, although a primary purpose of corporate diversification is to reduce firm risk by operating in diverse business environments, shareholders can diversify firm-specific risk more efficiently through portfolio diversification. Moreover, diversification is thought to conflict with the prevailing mandate to focus on “core competencies.” The agency logic attributes diversification (and diversifying acquisitions) to managerial self-interest: managers are thought to diversify in order to increase their compensation and status and reduce their employment risk (Sanders, 2001). Davis et al. (1994) documented how the spread of agency perspectives on corporate control contributed to a predominantly negative view of diversifying acquisitions among members of the financial community. This view remained the conventional wisdom on such acquisitions through the time period of our study (Klein et al., 2001; Zajac & Westphal, 2004; Zorn, 2004).

Thus, the announcement of a diversifying acquisition should tend to make security analysts more pessimistic about the performance prospects of an acquiring firm, triggering them to consider a change in their recommendation concerning the firm’s stock. Accordingly, our theoretical perspective suggests the following hypothesis:

Hypothesis 1b. The announcement of diversifying corporate acquisitions increases the extent to which top executives render favors to security analysts who cover their firm.

A subjective expected utility perspective on social influence further suggests that people should
tend to direct their influence attempts toward actors whom they perceive to be relatively powerful (i.e., those who have the greatest ability to procure benefits for them or impose costs on them) (Tedeschi, Schlenker, & Lindskold, 1972). In the present context, top executives may tend to concentrate their favor rendering on analysts who they expect will have the greatest influence on investor behavior. There is evidence from the finance and accounting literatures that two analyst characteristics represent strong indicators of an analyst’s influence on investors: selection as a member of the “All-America Research Team” by the magazine Institutional Investor, and the size of the analyst’s firm. Each year, Institutional Investor surveys large institutional money managers to determine who the managers believe are the best analysts. The results of the survey are published each fall, with the top three finishers in each industry designated as “first team,” “second team,” and “third team” All-Americans. Designation as an All-America analyst is an important source of status in the financial community (Hayward & Boeker, 1998; Hong et al., 2000). All-America analysts tend to serve as opinion leaders in the market: other analysts are influenced by their reports, and institutional investors pay greater attention to their recommendations (see Stickel, 1995).

Prior research in accounting (Clement & Tse, 2003; Mikhail, Walther, & Willis, 2004) has also shown that investors respond more strongly to the recommendation changes and earnings forecasts revisions of analysts who work at large brokerage firms, possibly because analysts who work for large firms have access to larger sales forces through which to distribute their ideas (Stickel, 1995). Qualitative evidence from our field interviews suggested that top executives recognize All-America status and firm size as primary determinants of an analyst’s influence on the market. Thus, executives should perceive greater value in rendering favors for analysts who have these characteristics. Accordingly, a subjective expected utility perspective on social influence suggests the following additional hypotheses:

**Hypothesis 2a.** The positive relationship between reported earnings below consensus forecasts and the extent to which top executives grant favors to security analysts who cover their firm is greater for analysts who have All-America status or are employed by relatively large brokerage firms.

**Hypothesis 2b.** The positive relationship between announcing a diversifying corporate acquisition and the extent to which top executives grant favors to security analysts who cover their firm is greater for analysts who have All-America status or are employed by relatively large brokerage firms.

### Reciprocity in Relations between Executives and Analysts

**Executive favor rendering and subsequent analyst recommendations.** Our theoretical perspective leads to the expectation that executives can decrease the likelihood that their firm’s stock will be downgraded following the disclosure of negative information about the firm by rendering personal and professional favors for security analysts who cover the firm. Drawing from theory and research on social exchange and interpersonal influence, we have argued that executive favor rendering directed at security analysts should engender a feeling of indebtedness and positive affect toward an executive, which should deter analysts from downgrading the executive’s firm in response to negative information. We also suggested that instrumental motives may further deter analysts from downgrading a company after receiving favors from the firm’s top executives, as analysts seek to positively reinforce the executives’ generosity and increase the likelihood of receiving more favors in the future. We also noted that social influence tactics tend to be particularly effective when the decision-making process by which judgments are rendered is relatively complex or ambiguous and analysts face considerable uncertainty in determining whether and when negative firm information is sufficient to warrant a downgrade. Thus, our theory suggests the following set of hypotheses:

**Hypothesis 3a.** The extent to which top executives of a firm grant favors to a security analyst who covers the firm negatively moderates the effect of reported earnings below consensus forecasts on the likelihood that the analyst subsequently downgrades the firm’s stock.

**Hypothesis 3b.** The extent to which top executives of a firm grant favors to a security analyst who covers the firm negatively moderates the effect of announcing a diversifying corporate acquisition on the likelihood that the analyst subsequently downgrades the firm’s stock.

**Negative reciprocity and deterrence.** Although the norm of reciprocity encourages cooperative behavior in response to favors, it also compels negative reciprocity or retaliation in response to harmful acts (Fehr & Gachter, 2000; Gouldner, 1960; Homans, 1958; Molm, 1997; Westphal & Zajac,
There is experimental evidence that most people reciprocate injurious acts to a greater extent than would be predicted by economic self-interest (see Fehr & Gachter, 2000 for a review). In part, negative reciprocity may reflect a purely cognitive motivation to maintain balance or equity in social relationships (Greenberg, 1980; Molm, 1997; Westphal & Zajac, 1997). However, there is growing evidence that most people exhibit a “punitive sentiment” in response to defection from social exchange relationships (Carpenter, Matthews, & Ong’ong’a, 2004: 415). This research has provided empirical confirmation of earlier claims by exchange theorists that emotional factors mediate negative reciprocity (Homans, 1958; Gouldner, 1960; Ekeh, 1974). Recent research in evolutionary psychology further suggests that this punitive sentiment may be “hardwired into our motivational circuitry” (Carpenter, Matthews et al., 2004: 415) in such a way that humans are evolutionarily predisposed to react negatively to injurious behavior (Friedman & Singh, 2004). In fact, the motivation to punish harmful actions may be even stronger and more reliable than the motivation to reward helpful behavior (Charness & Rabin, 2000; Fehr & Gachter, 2000; Offerman, 1999).

At the same time, this literature suggests that although most people reflexively reciprocate injurious acts by exchange partners, a minority retaliate only if there is an instrumental benefit in doing so (Fehr & Gachter, 2000). In social contexts that extend beyond purely dyadic interactions, an instrumental benefit in retaliation derives from the deterrent value of punitive behavior. Specifically, in such contexts individuals benefit from cultivating a reputation for retaliating against noncooperation by exchange partners (Ekeh, 1974; Figueredo, Tai, McNeil, & Guillen, 2004; Molm, 1997). Such a reputation should induce higher levels of cooperation by third parties who witness or learn about the punishment. Thus, negative reciprocity is an important form of social influence over other exchange partners: it serves as a credible threat that an actor will punish similarly negative acts in the future, thus deterring other social exchange partners from engaging in noncooperative behavior with the focal actor (Abbink & Irlenbusch, 2000; Axelrod, 1984; Blau, 1964; Ekeh, 1974; Friedman & Singh, 2004; Heath, 1976; Molm, 1997). The reputational benefit of negative reciprocity is thought to be a primary reason for the success of “tit for tat” as a strategy of social behavior, and a critical mechanism by which high levels of cooperation can be sustained in a population (Axelrod, 1984; Fehr et al., 2002; Sethi & Somanathan, 2003).

Thus, although relations between top executives and security analysts may provide a context for positive reciprocity, they may also provide a context for negative reciprocity or retaliation. In particular, top executives may negatively reciprocate toward analysts who downgrade their firms’ stock. Given that downgrades have a variety of negative consequences for firms and their leaders—damaging firm reputation, market value, and access to capital, and harming the reputation and career prospects of the firm’s leaders—they have the potential to incite retaliatory behavior by top executives, and there is some empirical evidence supporting such behavior (see Chen & Matsumoto, 2006). This evidence is consistent with contemporary theory and research on reciprocity, which would suggest that executives may be predisposed to respond in a punitive manner to downgrades. Moreover, a punitive response to downgrades should also have the instrumental benefit of deterring other analysts who witness the punishment or become aware of it through other means from downgrading the focal firm’s stock in response to the disclosure of negative information about the firm. Thus, in response to downgrades, executives may be motivated to engage in negative reciprocity that involves not only a reduction in favors for the offending analyst, but also a reduction in access to top executives. Managers may respond by limiting or cutting off personal communication with the analyst, thus making it more difficult for the analyst to obtain timely and relevant information about the firm. There is considerable evidence that security analysts highly value frequent, timely access to top executives (Kuperman, 2003; Lang & Lundholm, 1993; Lees, 1981). Such access is perceived to be valuable in generating timely, insightful, and accurate company reports, and it enhances an analyst’s stature with his or her clients (Mayew, 2008). Accordingly, the withdrawal of personal access to top executives is likely to be highly aversive to most analysts. Thus, executives may retaliate against analysts who downgrade their firms’ stock by rendering fewer personal or professional favors to them, and by reducing their personal access. Moreover, theory and research on the deterrence value of negative reciprocity, discussed above, would indicate that such retaliatory behavior should be effective in deterring other analysts who witness the punishment or become aware of it through other means from downgrading the focal firm’s stock in response to the disclosure of negative information about the firm. This suggests the following hypotheses:

Hypothesis 4a. Security analysts who downgrade a company’s stock subsequently receive
fewer favors from top executives at the downgraded firm.

Hypothesis 4b. Security analysts who downgrade a company’s stock subsequently receive less personal access to top executives at that firm.

Hypothesis 5a. An analyst covering a particular firm who is aware of another analyst’s loss of executive favors or personal access to top executives after downgrading the firm is subsequently less likely to downgrade the firm in response to reported earnings that are below consensus forecasts.

Hypothesis 5b. An analyst covering a particular firm who is aware of another analyst’s loss of executive favors or personal access to top executives after downgrading the firm is subsequently less likely to downgrade the firm in response to the announcement of a diversifying corporate acquisition.

METHODS

Sample and Data

The population for this study included analyst-manager dyads at U.S. public companies with more than $100 million in sales, as listed in the Forbes and Reference USA indexes. We conducted a series of surveys of analysts and managers in this population. The first survey was sent in 2001 to a random sample of 1,000 “sell-side” analysts who covered at least one firm in the population. Questions in this survey were used to test hypotheses concerning earnings announcements (that is, as discussed further below, respondents answered questions about favor rendering since the most recent earnings announcement). The second survey was sent in 2002 to a random sample of 2,500 analysts who covered firms in the population. We used questions in this survey to test hypotheses concerning the announcement of diversifying corporate acquisitions. The third survey was sent in the following year to a random sample of 1,000 sell-side analysts who covered firms in the population. Questions in this survey tested the effects of analyst downgrades on favor rendering and executive access. To assess interrater reliability, we sent a separate survey to CEOs, CFOs, and investment relations officers (IROs) at firms in the population for which analysts had assessed favor rendering by top managers.

We conducted a qualitative pretest of the survey instrument that involved in-depth interviews with 18 current or former top executives, security analysts, and investment managers. Each interview was approximately 20 to 40 minutes in length. We used feedback from the interviews to refine the wording of the survey questions and instructions and to improve the overall presentation of the survey. Survey questions about executive favors were only part of the larger questionnaire. Most of the survey questions were about personal and professional helping behaviors toward fellow analysts or executives (for example, the frequency with which analysts provide advice to each other). Thus, most of the survey items were about behaviors with manifestly positive connotations. The cover letter and instructions also reinforced this theme by highlighting the potential benefits to firms and their employees of personal and professional helping behavior. We also followed a variety of other survey procedures that have been shown to elicit relatively high response rates among executives (Greer, Chuchinprakam, & Seshadri, 2000; Westphal & Stern, 2006). For example, the survey was endorsed by a well-known corporate executive, and the cover letter highlighted that the questionnaire was part of an ongoing series of surveys on corporate leadership in which hundreds of leaders had participated. Response rates for the analyst surveys ranged from 40 percent to 42 percent, and response rates for the manager surveys ranged from 38 percent to 42 percent. We tested for nonresponse bias using the Kolmogorov-Smirnov two-sample test, which determines whether the distribution of a given variable is different for respondents and nonrespondents. Results showed that respondents are not significantly different from nonrespondents on any of the continuous-scale archival variables included in the study. For categorical variables, we used difference-in-proportions tests, which also showed no significant differences between respondents and nonrespondents. For instance, there were no significant differences in the size of analysts’ employers or the portion of analysts with All-America status, and there were no significant differences in the reported earnings or sales of responding managers’ employers. \( P \)-values ranged from .22 to .87.

We obtained data on analyst recommendations, earnings forecasts, and earnings announcements from the IBES database. Data on the All-America status of analysts and the size of their employers were obtained from Institutional Investor and IBES, respectively. We collected data on firm performance, size, and industry from Compustat. We obtained acquisition data from Compustat and the Securities Data Corporation, and we searched full-text articles from the Wall Street Journal and the New York Times for announcements of stock repur-
chases and joint ventures during the period of study.

Measures

Favor rendering. We used multi-item survey measures to gauge the extent to which top executives granted favors to individual security analysts who cover their firms. The analyst surveys included questions about favor rendering at up to three firms in our population (i.e., large and mid-sized U.S. companies) that were covered by a focal analyst. We developed and refined scale items using feedback from the pretest interviews. The three analyst surveys included questions about favor rendering by top executives at a particular firm that had occurred (1) since the firm’s most recent earnings announcement, (2) since the analyst’s most recent recommendation regarding the focal firm, (3) since the announcement of a diversifying corporate acquisition but prior to the analyst’s next stock recommendation, with the date of the acquisition announcement specified in the survey (if the firm made such an announcement), and (4) in the prior six months. We used a variety of response formats to minimize response bias (DeVellis, 1991) (see the Appendix for survey scales). Some items had a five-point Likert-type response format (e.g., “To what extent has this executive done personal or professional favors for you since [date of announcement]?”). Other items were intended to elicit an “agree”/“disagree” response (e.g., “This executive has done a number of favors for me since [date of announcement]?”). A series of questions also asked respondents to indicate how many times executives had performed specific favors for them. Respondents were also asked to list any other favors granted by the executive. Using responses to these questions, we calculated the number of favors granted to the focal analyst by executives at the focal firm over the relevant time period. We conducted factor analysis on this count variable and the other survey items—including indicators of personal access discussed below—using the principal factor method with promax rotation. The favor-rendering items loaded on one factor, with loadings above .5 on the same factor and less than .2 on other factors. Cronbach’s coefficient alpha for the scale was .88, indicating acceptable interitem reliability.

We also examined interrater reliability by comparing analyst and executive responses to the favor-rendering items in both surveys. We used the weighted kappa coefficient, which corrects for correlation between ratings that would be expected by chance and weights agreement by the degree of convergence between raters. Values above .75 are generally interpreted as indicating excellent agreement beyond chance, and values between .4 and .75 are taken to indicate fair to good agreement (Fleiss, 1981). In this case, kappas were above .75 for all but two survey items, and all items were above .6, suggesting a relatively high level of interrater agreement. The overall kappa for the scale was .84, and the intraclass correlation coefficient (ICC) was .91, which further indicates a high level of agreement. Reliability was also high for the subsample of dyads in which analysts reported that at least one favor had been rendered (overall $\kappa = .80$; $ICC = .89$). Survey responses indicated that it was rare for analysts to receive favors from more than one executive at the same firm. Thus, we developed a single measure of favor rendering while controlling for the executive’s title.

Personal access to top executives. We also used a multi-item survey measure to gauge analysts’ personal access to top executives (see the Appendix). The questions asked about executive access since an analyst’s most recent recommendation regarding a focal firm. Some items asked analysts to assess the general level of personal access to executives at the focal firm, and others asked them to indicate whether they had been denied access to executives in specific ways. Respondents were also asked to list any specific instances in which they were denied access to an executive. A parallel set of questions asked about executive access during the earlier six-month period. Using these data, we calculated the number of instances in which analysts were denied personal access to executives at the focal firm (i.e., subsequent to the most recent recommendation and in the previous six months). Factor analysis showed that the count variable and the other survey items loaded on one factor as expected. Cronbach’s alpha was acceptably high (.93). We assessed interrater reliability with a separate set of questions in the executive survey gauging the extent to which a focal executive granted personal access to an analyst. The factor score for this scale was strongly correlated with the access measure derived from the analyst survey ($r = .64$), providing evidence of interrater agreement.

Awareness of another analyst’s loss of favors or executive access. We used a survey scale to determine whether analysts were aware of another instance in which an analyst had lost executive favors or personal access to top executives after downgrading a focal firm’s stock (see the Appendix). We expected that analysts would rarely know about more than one such case in a recent time period, given that downgrades are relatively rare events, and our pretest interviews confirmed this
expectation. Thus, the survey scale includes a series of “yes” or “no” questions, such as “Are you aware of an instance in the last two years in which another analyst who covers [the focal firm] had difficulty gaining access to top executives of the firm after downgrading their stock?” “Have you heard of a case during the last two years in which another analyst who covers [the focal firm] received fewer favors from executives after downgrading the firm?” and “In the past two years have you seen or heard of an instance in which an analyst seemed to get blacklisted by [this firm’s] executives after issuing a downgrade?” Reliability for the scale was acceptably high, and we found a negative correlation between this measure and the level of executive access and favors granted to other analysts who covered the same firm and who had downgraded the firm in the past three years, as reported by executive respondents ($r = –.62$). This analysis provided evidence for the accuracy of analysts’ assessments of their colleagues’ access to executives, thus further supporting the validity of the awareness measure.

**Reported earnings and announcements of diversifying corporate acquisitions.** We measured the extent to which reported earnings were below consensus forecasts as the difference between the most recently reported earnings and the median earnings for the same period forecast by all analysts who covered a focal firm for whom data were available. Following many prior studies, we coded acquisitions as “diversifying” when the primary two-digit SIC code of the acquiring firm did not match that of the acquired firm (Fowler & Schmidt, 1989; Krishnan & Miller, 1997; Kroll, Wright, Toombs, & Leavell, 1997). Our survey data provided some additional evidence for the validity of this measure. We asked each responding analyst to assess the relatedness of up to three acquisitions that were made by companies that they covered. Analysts assessed relatedness of acquisitions on a four-point scale, and acquisitions that we had coded as “unrelated” on the basis of SIC code were rated as “not at all related” or “more unrelated than related” in 93 percent of the cases. We created a dichotomous variable coded 1 if a focal firm announced such an acquisition in the prior year and 0 otherwise.

**All-America status and size of analyst’s employer.** There are three levels of All-America status, ranging from First-Team All-America to Third-Team All-America. In the primary analyses, we used a categorical variable that distinguished between these levels (1 = “first team,” 2 = “second team,” and 3 = “third team”). Moreover, the results were robust to alternative operationalizations of this variable, including a dichotomous variable coded 1 if an analyst was nominated to any of the three levels and 0 otherwise. We operationalized the size of the analyst’s employer as the total number of analysts employed at the firm. The hypothesized results were also robust to alternative measures of this construct, including total revenues.

**Downgrades.** To test Hypotheses 4a and 4b, regarding the effect of downgrades on subsequent favor rendering and executive access, respectively, we created a dichotomous variable coded 1 if a focal analyst’s most recent stock recommendation involved a downward change from the previous recommendation. In the primary analyses, we divided stock recommendations into three basic categories: buy, hold, and sell. In supplementary analyses, we used five categories: strong buy, buy, strong sell, sell, and hold; the hypothesized results were not substantively different from those presented below. To test hypotheses regarding the effects of favor rendering on subsequent downgrades, we developed a dichotomous measure coded 1 if a focal analyst downgraded a focal firm’s stock during the 12 months after the survey. In separate analyses, we measured downgrades over alternative time periods (18 months and two years), and found the hypothesized results were qualitatively unchanged.

**Control variables.** We controlled for aspects of an executive-analyst relationship that could affect analyst stock recommendations, executive access, or favor rendering. First, the general level of social interaction between executives and analysts could influence the extent to which either party treats the other favorably. Thus, we included a survey measure gauging the level of social interaction between the focal analyst and executive. Items asked about social interaction during the time period for which favor rendering was assessed. These scales showed acceptable interitem and intrarater reliability ($\alpha = .87–.91, \kappa = .78–.80$). We also included a survey measure of friendship between the executive and the analyst (cf. Burt, 1992). Although our pretest interviews suggested that friendship ties between executives and analysts are not common, such ties could nevertheless influence executive favor rendering and analyst stock ratings. There was a high level of intrarater agreement (92%) between executives and analysts about the status of their relationship as friends versus acquaintances or strangers.

We also controlled for efforts by managers to promote or “sell” their firms to analysts (Kuperman, 2003). Communication of this kind could be correlated with executive favor rendering, although there is little evidence for a positive association between favor rendering and self-promotion in the
social influence literature (Westphal & Stern, 2006). In fact, there is some evidence for a negative correlation between these constructs, perhaps because they represent alternative influence strategies, in which case self-promotion could act as a suppressor variable in the relationship between favor rendering and analyst stock ratings. In any event, as a precaution, we included a survey measure that gauged efforts by managers to promote their firms to analysts (selling behavior). The scale includes questions about persuasion attempts relating to firm strategy, governance, and future firm performance (e.g., “To what extent have managers of the firm sought to persuade you that the firm’s strategy is sound?”; “To what extent have managers tried to convince you that the firm’s performance prospects are good?”; “To what extent have managers sought to persuade you that the firm is well-governed?”). The survey items asked about selling behavior during the time period for which favor rendering was assessed. These scales had acceptable reliability (α = .84–.87, κ = .75–.76). Moreover, we controlled for position of the focal executive (CEO, CFO, or other), as the value of professional favors or personal access could depend on the executive’s position. Analysts could also be influenced by impression management in press releases. Thus, we controlled for the number of positive statements about the firm in press releases issued by the company over the time period for which favor rendering was measured. This measure was based on content analyses of the press releases performed by three independent coders with varying backgrounds and yielded high inter-rater reliability (ICC = .88). The results were robust to different recording units (sentence or paragraph).

Given that market-based measures of firm performance could influence analyst recommendations and favor rendering independently of reported earnings (Miller & Sedor, 2005), we controlled for the industry-adjusted market-to-book value of the focal firm in the prior year (the hypothesized results were unchanged by use of total stock returns). We included a control for firm size. Having access to top management at large firms could be valuable to analysts, as large firms can provide potentially larger underwriting fees, and underwriting fees are one of the most lucrative revenue sources for investment banks (Bradshaw, Richardson, & Sloan, 2003). Thus, firm size could influence analyst recommendations. We controlled for industry by including dummy variables for the N = 1 two-digit SIC codes in the sample, given that industry conditions are known to have a strong influence on stock ratings (Boni & Womack, 2004) (to conserve space, coefficients for these variables are not reported). In addition, we controlled for other firm announcements (in the survey year or the prior year) that have the potential to influence stock recommendations, including stock repurchases, large joint ventures, or related acquisitions (Clement, Frankel, & Miller, 2003).

Moreover, we controlled for the prior level of the dependent variable in models of favor rendering and executive access, measured over the prior six months, using separate scales in the analyst surveys. Another control variable indicated the time period for which favor rendering and executive access were assessed, in months (e.g., the number of months since a firm’s most recent earnings announcement). We also controlled for a focal analyst’s prior rating of a focal firm in estimating downgrades (1, “buy”; 2, “hold”; 3, “sell”). In separate analyses, we controlled for the analyst’s prior rating in models of favor rendering and personal access and found the hypothesized results were unchanged. Finally, in models of favor rendering and executive access, we included a control for the number of other analysts who covered the same firm. Executives are less dependent on the positive assessment of a single analyst to the extent that many other analysts cover their firm. Given evidence for mimetic behavior in analyst decision making (Rao et al., 2001), in separate models of downgrades we controlled for the portion of other analysts covering a focal firm who issued a downgrade during a relevant time period. The hypothesized results were nearly identical to those reported below.

Analysis

The unit of analysis in this study was the analyst-manager dyad. We estimated favor rendering and personal access to top executives using multiple regression analysis, and we estimated downgrades using logistic regression analysis. Since each analyst reported on executive favor rendering and executive access at up to three firms, and different analysts could report on favor rendering and access at the same firm, our sample included multiple dyadic combinations that involved the same analyst or the same firm. As a result, residuals for dyads involving the same analyst or firm could be correlated. Thus, we estimated robust standard errors to correct for nonindependence of observations. Since we controlled for prior levels of the dependent variable in models of favor rendering and access, we effectively examined change in these variables (e.g., change in favor rendering subsequent to a downgrade) (Allison, 1990). In the primary analyses we estimated separate models for
the three analyst survey samples described above (n = 986, 2,612, and 997 for the 2001, 2002, and 2003 surveys, respectively). In supplemental analyses, we estimated one set of models for the combined sample (N = 4,595), and the hypothesized results were qualitatively unchanged.

The error terms from models of favor rendering could be correlated with those from models of personal access. Thus, we estimated separate models of favor rendering and personal access using Zellner’s seemingly unrelated regression (Greene, 1993). The results were nearly identical to those of the multiple regression models because, with the exception of one control variable, the independent variables are the same across both sets of models.

RESULTS

Table 1 displays descriptive statistics and correlation coefficients. Table 2 includes the results of multiple regression analyses of executive favor rendering directed toward security analysts. The results of model 1 provide support for Hypothesis 1a: the lower the reported earnings relative to consensus forecasts, the greater the extent to which top executives subsequently grant favors to security analysts who cover their firm. Hypothesis 1b is confirmed by model 3: announcement of a diversifying corporate acquisition significantly increases the tendency for top executives to grant favors to security analysts who cover their firm. The hypothesized interactions between reported earnings and indicators of analyst influence on investor behavior are tested in model 2. The results generally provide support for these hypothesized interactions. Specifically, the effect of reported earnings on favor rendering is greater to the extent that a focal analyst (1) has All-America status or (2) is employed by a relatively large brokerage firm, in keeping with Hypothesis 2a. There is mixed support for Hypothesis 2b, which posited interactions between the announcement of diversifying acquisitions and indicators of analyst influence on investor behavior. Consistently with this hypothesis, the effect of announcing a diversifying corporate acquisition on favor rendering is significantly greater to the extent that a focal analyst has All-America status. The interaction between announcing a diversifying acquisition and the size of the analyst’s employer is not significant.

Table 4 provides the results of logit regression analyses of downgrades. Models 2 and 4 confirm the hypothesized effects of favor rendering on downgrades. As shown in model 2, the greater the extent to which an executive of a particular firm grants favors to a security analyst who covers the firm, the weaker (i.e., less positive) the effect of reported earnings that are below consensus forecasts on the likelihood that the analyst will subsequently downgrade the firm’s stock. Similarly, as shown in model 2, favor rendering interacts with announcement of a diversifying acquisition to predict downgrades. Specifically, the greater the extent to which an executive of a particular firm grants favors to a security analyst who covers the firm, the weaker (i.e., less positive) the effect of announcing a diversifying corporate acquisition on the likelihood that the analyst will subsequently downgrade the firm’s stock. Graphical displays of the interactions confirmed our interpretation of the regression results (available from the authors on request). The simple effects of the interaction models indicated that negative earnings surprises and announcement of a diversifying acquisition have positive effects on the likelihood of a downgrade at relatively low levels of executive favor rendering (e.g., less than one standard deviation below the mean), but the effects of these variables are not statistically significant at relatively high levels of favor rendering (e.g., above the median). The magnitude of these effects is considerable: rendering two personal favors for an analyst after the release of relatively low reported earnings (one standard deviation below the mean) reduces the likelihood that the analyst will issue a downgrade by 51 percent; rendering two favors for an analyst after one’s firm announces a diversifying acquisition reduces the likelihood that the analyst will downgrade the firm by 65 percent.

Hypothesis 4a, which predicted that security analysts who downgrade a company’s stock will subsequently receive fewer favors from top executives at the downgraded firm, is tested in model 5 of Table 2. Results are consistent with the hypothesis: analysts who downgrade a firm’s stock subsequently receive significantly fewer favors from executives of that firm. Hypothesis 4b predicted that security analysts who downgrade a company’s stock will subsequently receive less personal access to top executives at that firm. As shown in model 1 of Table 3, this prediction is also confirmed: analysts who downgrade a firm’s stock subsequently receive significantly less personal access to top executives at that firm.

Hypothesis 5a predicted an interaction between reported earnings and awareness of another analyst’s loss of executive favors or access to executives after issuing a downgrade on the likelihood of subsequently downgrading the focal firm’s stock. As shown in model 4 of Table 4, the hypothesized interaction is highly significant. Analysts are less likely to downgrade a firm’s stock in response to
| Independent Variables                                      | Mean | s.d. | 1    | 2    | 3    | 4    | 5    | 6    | 7    | 8    | 9    | 10   | 11   | 12   | 13   | 14   | 15   | 16   | 17   | 18   | 19   |
|-----------------------------------------------------------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|
| 1. Announcement of diversifying acquisition                | 0.05 | 0.22 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 2. Reported earnings vs. forecastsb                        | 0.06 | 0.83 | -0.05|      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 3. Size of analyst’s employer                              | 305.35| 263.99| 0.03 | 0.01 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 4. Friendship tie between executive and analyst            | 0.13 | 0.34 | 0.02 | 0.03 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 5. Executive selling behavior                              | 0.00 | 0.92 | 0.21 | 0.24 | 0.08 | 0.11 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 6. Social interaction between executive and analyst        | 0.00 | 0.92 | 0.12 | 0.17 | 0.06 | 0.16 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 7. Prior downgrade of focal firm by analyst                | 0.12 | 0.33 | 0.04 | 0.06 | 0.04 | 0.14 | 0.06 | 0.09 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 8. Number of other analysts covering firm                  | 8.73 | 9.02 | 0.02 | 0.02 | 0.03 | 0.05 | 0.04 | 0.03 | 0.04 | 0.14 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 9. Focal firm salesc                                       | 2.91 | 8.08 | 0.18 | 0.04 | 0.05 | 0.02 | 0.06 | 0.02 | 0.01 | 0.26 |      |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 10. Investment relations officer                          | 0.13 | 0.34 | 0.02 | 0.02 | 0.04 | 0.08 | 0.04 | 0.07 | 0.01 | 0.05 | 0.14 |      |      |      |      |      |      |      |      |      |      |      |      |      |
| 11. Chief financial officer                               | 0.45 | 0.50 | 0.01 | 0.03 | 0.02 | 0.02 | 0.04 | 0.03 | 0.01 | 0.04 | 0.09 | 0.35 |      |      |      |      |      |      |      |      |      |      |      |      |
| 12. Other announcements by focal firm                     | 0.23 | 0.42 | 0.06 | 0.09 | 0.01 | 0.03 | 0.02 | 0.07 | 0.21 | 0.03 | 0.02 | 0.06 |      |      |      |      |      |      |      |      |      |      |      |      |
| 13. Time period for which favor rendering assessed        | 2.71 | 2.68 | 0.00 | 0.01 | 0.00 | 0.00 | 0.01 | 0.01 | 0.02 | 0.00 | 0.01 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 14. Focal firm market-to-book value                       | 0.53 | 0.53 | 0.22 | 0.02 | 0.01 | 0.01 | 0.06 | 0.11 | 0.05 | 0.06 | 0.01 | 0.03 | 0.00 |      |      |      |      |      |      |      |      |      |      |      |
| 15. All-America status                                    | 0.22 | 0.68 | 0.21 | 0.08 | 0.12 | 0.06 | 0.02 | 0.15 | 0.02 | 0.09 | 0.02 | 0.02 | 0.03 | 0.05 |      |      |      |      |      |      |      |      |      |
| 16. Positive statements in press releases                 | 2.38 | 4.51 | 0.01 | 0.01 | 0.01 | 0.01 | 0.06 | 0.01 | 0.04 | 0.12 | 0.05 | 0.01 | 0.04 | 0.12 | 0.07 | 0.00 |      |      |      |      |      |      |      |
| 17. Awareness of another analyst’s loss of favors or executive access | 0.00 | 0.99 | 0.01 | 0.00 | 0.04 | 0.02 | 0.00 | 0.03 | 0.01 | 0.10 | 0.00 | 0.02 | 0.01 | 0.07 | 0.01 |      |      |      |      |      |      |      |      |
| 18. Favor rendering                                       | 0.00 | 0.97 | 0.32 | 0.12 | 0.13 | 0.18 | 0.14 | 0.30 | 0.12 | 0.07 | 0.27 | 0.03 | 0.07 | 0.22 | 0.10 | 0.19 | 0.02 | 0.01 |      |      |      |      |
| 19. Personal access to top executives                     | 0.00 | 0.98 | 0.20 | 0.04 | 0.04 | 0.21 | 0.16 | 0.35 | 0.32 | 0.05 | 0.08 | 0.08 | 0.07 | 0.02 | 0.08 | 0.11 | 0.03 | 0.01 | 0.05 |      |      |      |
| 20. Downgrade                                             | 0.14 | 0.35 | 0.14 | 0.06 | 0.09 | 0.07 | 0.04 | 0.16 | 0.04 | 0.19 | 0.26 | 0.17 | 0.01 | 0.23 | 0.01 | 0.02 | 0.13 | 0.15 | -0.06|      |      |      |

\(^a\) n = 986.

\(^b\) This variable is inverted so that higher values indicate lower earnings relative to forecasts.

\(^c\) In billions of dollars.
<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Model 1&lt;sup&gt;b&lt;/sup&gt;</th>
<th>Model 2&lt;sup&gt;b&lt;/sup&gt;</th>
<th>Model 3&lt;sup&gt;c&lt;/sup&gt;</th>
<th>Model 4&lt;sup&gt;c&lt;/sup&gt;</th>
<th>Model 5&lt;sup&gt;d&lt;/sup&gt;</th>
<th>Model 6&lt;sup&gt;d&lt;/sup&gt;</th>
</tr>
</thead>
<tbody>
<tr>
<td>Announcement of diversifying acquisition</td>
<td>0.954*** (0.107)</td>
<td>0.749*** (0.129)</td>
<td>0.581*** (0.064)</td>
<td>0.517*** (0.067)</td>
<td>0.599*** (0.080)</td>
<td>0.500*** (0.085)</td>
</tr>
<tr>
<td>Reported earnings vs. forecasts&lt;sup&gt;e&lt;/sup&gt;</td>
<td>0.166*** (0.026)</td>
<td>0.133*** (0.029)</td>
<td>0.082*** (0.018)</td>
<td>0.072*** (0.021)</td>
<td>0.088*** (0.014)</td>
<td>0.060*** (0.015)</td>
</tr>
<tr>
<td>Prior downgrade of focal firm by analyst</td>
<td>-0.436*** (0.066)</td>
<td>-0.434*** (0.066)</td>
<td>-0.463*** (0.053)</td>
<td>-0.462*** (0.053)</td>
<td>-0.601*** (0.062)</td>
<td>-0.520*** (0.062)</td>
</tr>
<tr>
<td>Announcement of diversifying acquisition × All-America status of analyst</td>
<td>4.063*** (0.822)</td>
<td>0.832*** (0.186)</td>
<td>1.880*** (0.577)</td>
<td>0.601*** (0.062)</td>
<td>0.0004 (0.003)</td>
<td>0.0004 (0.003)</td>
</tr>
<tr>
<td>Reported earnings vs. forecasts&lt;sup&gt;e&lt;/sup&gt; × size of analyst’s employer</td>
<td>0.676*** (0.123)</td>
<td>0.077*** (0.012)</td>
<td>0.291*** (0.056)</td>
<td>0.0002** (0.0001)</td>
<td>0.0002** (0.0001)</td>
<td>0.0002*** (0.0001)</td>
</tr>
<tr>
<td>Size of analyst’s employer</td>
<td>0.0002** (0.0001)</td>
<td>0.0002* (0.0001)</td>
<td>0.0002** (0.0001)</td>
<td>0.0003** (0.0001)</td>
<td>0.0003** (0.0001)</td>
<td>0.0003** (0.0001)</td>
</tr>
<tr>
<td>All-America status of analyst</td>
<td>0.091 (0.071)</td>
<td>0.092 (0.071)</td>
<td>0.062 (0.043)</td>
<td>0.053 (0.043)</td>
<td>0.063 (0.055)</td>
<td>0.065 (0.055)</td>
</tr>
<tr>
<td>Executive selling behavior</td>
<td>-0.601* (0.026)</td>
<td>-0.060* (0.026)</td>
<td>-0.046* (0.017)</td>
<td>-0.046* (0.017)</td>
<td>-0.025 (0.024)</td>
<td>-0.018 (0.024)</td>
</tr>
<tr>
<td>Social interaction between executive and analyst</td>
<td>0.065* (0.029)</td>
<td>0.065* (0.029)</td>
<td>0.033* (0.016)</td>
<td>0.032* (0.016)</td>
<td>0.052* (0.025)</td>
<td>0.048 (0.025)</td>
</tr>
<tr>
<td>Number of other analysts covering firm</td>
<td>-0.007** (0.003)</td>
<td>-0.007** (0.003)</td>
<td>-0.004** (0.002)</td>
<td>-0.004* (0.002)</td>
<td>-0.004* (0.002)</td>
<td>-0.004* (0.002)</td>
</tr>
<tr>
<td>Focal firm sales</td>
<td>-0.007* (0.003)</td>
<td>-0.007* (0.003)</td>
<td>-0.002 (0.002)</td>
<td>-0.002 (0.002)</td>
<td>-0.003 (0.002)</td>
<td>-0.003 (0.002)</td>
</tr>
<tr>
<td>Investment relations officer</td>
<td>-0.313*** (0.096)</td>
<td>-0.315*** (0.096)</td>
<td>-0.129** (0.051)</td>
<td>-0.129** (0.051)</td>
<td>-0.214** (0.069)</td>
<td>-0.217** (0.068)</td>
</tr>
<tr>
<td>Chief financial officer</td>
<td>-0.056 (0.065)</td>
<td>-0.056 (0.065)</td>
<td>0.028 (0.046)</td>
<td>0.027 (0.046)</td>
<td>0.075 (0.058)</td>
<td>0.085 (0.058)</td>
</tr>
<tr>
<td>Other announcements by focal firm</td>
<td>-0.124* (0.055)</td>
<td>-0.124* (0.055)</td>
<td>-0.064 (0.037)</td>
<td>-0.064 (0.037)</td>
<td>-0.074 (0.052)</td>
<td>-0.073 (0.052)</td>
</tr>
<tr>
<td>Time period for which favor rendering assessed</td>
<td>0.016** (0.006)</td>
<td>0.016** (0.006)</td>
<td>0.013*** (0.004)</td>
<td>0.013*** (0.004)</td>
<td>0.019*** (0.006)</td>
<td>0.019*** (0.006)</td>
</tr>
<tr>
<td>Focal firm market-to-book value</td>
<td>-0.101* (0.045)</td>
<td>-0.101* (0.046)</td>
<td>-0.086** (0.029)</td>
<td>-0.086** (0.029)</td>
<td>-0.107* (0.047)</td>
<td>-0.110* (0.047)</td>
</tr>
<tr>
<td>All-America status of analyst</td>
<td>0.117*** (0.039)</td>
<td>0.101* (0.041)</td>
<td>0.092*** (0.027)</td>
<td>0.081*** (0.026)</td>
<td>0.112* (0.048)</td>
<td>0.098* (0.047)</td>
</tr>
<tr>
<td>Positive statements in press releases</td>
<td>0.002 (0.004)</td>
<td>0.002 (0.004)</td>
<td>0.001 (0.003)</td>
<td>0.002 (0.004)</td>
<td>0.003 (0.005)</td>
<td>0.003 (0.005)</td>
</tr>
<tr>
<td>Prior favor rendering</td>
<td>0.136*** (0.017)</td>
<td>0.136*** (0.017)</td>
<td>0.110*** (0.011)</td>
<td>0.109** (0.011)</td>
<td>0.130*** (0.018)</td>
<td>0.129*** (0.018)</td>
</tr>
<tr>
<td>Constant</td>
<td>-0.187 (0.197)</td>
<td>-0.199 (0.197)</td>
<td>0.244* (0.104)</td>
<td>0.239* (0.104)</td>
<td>0.391* (0.164)</td>
<td>0.359* (0.163)</td>
</tr>
<tr>
<td>F</td>
<td>46.83***</td>
<td>55.02***</td>
<td>64.42***</td>
<td>80.54***</td>
<td>61.34***</td>
<td>81.12***</td>
</tr>
<tr>
<td>R²</td>
<td>.42</td>
<td>.48</td>
<td>.25</td>
<td>.33</td>
<td>.45</td>
<td>.53</td>
</tr>
<tr>
<td>n</td>
<td>986</td>
<td>986</td>
<td>2612</td>
<td>2612</td>
<td>997</td>
<td>997</td>
</tr>
</tbody>
</table>

<sup>a</sup> Standard errors are in parentheses. Values shown bold indicate hypothesized results.
<sup>b</sup> Sample based on 2001 survey. Favor rendering assessed since most recent earnings announcement.
<sup>c</sup> Sample based on 2002 survey. Favor rendering assessed since announcement of diversifying acquisition (or most recent six-month period for firms not making an announcement).
<sup>d</sup> Sample based on 2003 survey. Favor rendering assessed since most recent stock recommendation by analyst.
<sup>e</sup> Inverted so that higher values indicate lower earnings relative to forecasts.

* p ≤ .05
** p ≤ .01
*** p ≤ .001

T-tests are one-tailed for hypothesized effects, two-tailed for control variables.
TABLE 3
Results of Multiple Regression Analysis of Personal Access to Top Executives

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Model 1b</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prior downgrade of focal firm by analyst</td>
<td>-0.432*** (0.082)</td>
</tr>
<tr>
<td>Announcement of diversifying acquisition</td>
<td>0.181 (0.108)</td>
</tr>
<tr>
<td>Reported earnings vs. forecasts</td>
<td>0.080* (0.039)</td>
</tr>
<tr>
<td>Size of analyst’s employer</td>
<td>0.0002 (0.001)</td>
</tr>
<tr>
<td>Friendship tie between executive and analyst</td>
<td>0.071 (0.072)</td>
</tr>
<tr>
<td>Executive selling behavior</td>
<td>0.083* (0.035)</td>
</tr>
<tr>
<td>Social interaction between executive and analyst</td>
<td>0.074* (0.037)</td>
</tr>
<tr>
<td>Number of other analysts covering firm</td>
<td>-0.007* (0.003)</td>
</tr>
<tr>
<td>Focal firm sales</td>
<td>-0.004 (0.002)</td>
</tr>
<tr>
<td>Investment Relations Officer</td>
<td>0.107 (0.109)</td>
</tr>
<tr>
<td>Chief financial officer</td>
<td>0.129 (0.073)</td>
</tr>
<tr>
<td>Other announcements by focal firm</td>
<td>0.129 (0.072)</td>
</tr>
<tr>
<td>Time period for which favor rendering assessed</td>
<td>0.004 (0.007)</td>
</tr>
<tr>
<td>Focal firm market-to-book value</td>
<td>-0.142* (0.066)</td>
</tr>
<tr>
<td>All-America status of analyst</td>
<td>0.129* (0.062)</td>
</tr>
<tr>
<td>Positive statements in press releases</td>
<td>0.007 (0.007)</td>
</tr>
<tr>
<td>Prior access</td>
<td>0.078*** (0.024)</td>
</tr>
<tr>
<td>Constant</td>
<td>0.026 (0.235)</td>
</tr>
<tr>
<td>(F)</td>
<td>15.50***</td>
</tr>
<tr>
<td>(R^2)</td>
<td>.19</td>
</tr>
<tr>
<td>(n)</td>
<td>997</td>
</tr>
</tbody>
</table>

\(^a\) Standard errors are in parentheses. The value shown bold is a hypothesized result.

\(^b\) Sample based on 2003 survey. Favor rendering assessed since most recent stock recommendation by analyst.

\(^c\) Inverted so that higher values indicate lower earnings relative to forecasts.

\(* p \leq .05\)

\(*** p \leq .001\)

T-tests are one-tailed for hypothesized effects, two-tailed for control variables.

relatively low earnings, to the extent that they are aware of another analyst’s loss of favors or access after issuing a downgrade. The interaction between announcement of a diversifying acquisition and awareness of another analyst’s loss of favors or personal access on subsequent downgrades is also significant; thus, Hypothesis 5b is also supported. Again, graphical displays of the interaction effects confirmed our interpretation of the regression results (available from the authors on request).

As discussed above, each survey was designed to test a specific antecedent of favor rendering and personal access to executives. Thus, for instance, the effect of reported earnings on favor rendering was tested most precisely via data from the 2001 survey, which measured executive favors rendered since the most recent earnings announcement. Nevertheless, measures of favor rendering and access to executives that are based on survey data from other years provide some indication of the robustness of the results to different time periods. Thus, it is notable that each of the significant effects discussed above remained significant when we used measures of favor rendering or personal access that were based on survey data from another year. As shown in Table 2, for instance, the relationship between reported earnings and executive favor rendering is strongly significant, when measures of favor rendering from all three surveys are used.

In separate analyses, we examined whether the hypothesized effects of executive favor rendering and awareness of another analyst’s loss of favors or access were contingent on an analyst’s initial recommendation for a firm. Specifically, using multinomial logit regression, we examined whether these effects held for downgrades from (1) buy to hold and (2) hold to sell. The hypothesized effects were statistically significant for both types of downgrade.

**DISCUSSION**

Overall, the results provided strong support for our theoretical perspective on manager-analyst relations. The first set of results indicated that the announcement of relatively low corporate earnings or diversifying corporate acquisitions increased the propensity for corporate executives to render personal and professional favors to security analysts who cover their firm. Additional results suggested that such announcements were especially likely to prompt executives to render favors to analysts who are believed to exert disproportionate influence over investor behavior, as indicated by their All-America status or employment by relatively large brokerage firms. These findings support our socio-political perspective on manager-analyst relations, which draws from the literature on power and politics to suggest that the subjective expected utility of an influence tactic should predict the extent to which people will use that tactic in their relations with powerful actors. In keeping with this perspective, the findings appear to indicate that the release of negative or controversial information about a firm, which might otherwise cause analysts to consider downgrading the firm’s stock, increases the tendency for executives to engage in social influence behavior with relatively powerful analysts, where influence behavior takes the form of personal and professional favor rendering. In effect, the results suggest that executives initiate or escalate social exchange with powerful analysts to neutralize the
Further results provided evidence that such influence attempts tend to succeed: executive favor rendering significantly reduced the propensity for analysts to downgrade a firm’s stock in response to the announcement of relatively low earnings or diversifying acquisitions. Thus, it appears that analysts tend to reciprocate executive favors by maintaining their stock recommendation for the executive’s firm despite the release of negative or controversial information about the firm. A third set of results provided further evidence for reciprocity in manager-analyst relations. In particular, the findings suggested that analysts who downgrade a firm’s stock elicit negative reciprocity from the firm’s executives, in the form of diminished favor rendering and reduced personal access to top executives.

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Model 1</th>
<th>Model 2</th>
<th>Model 3</th>
<th>Model 4</th>
</tr>
</thead>
<tbody>
<tr>
<td>Announcement of diversifying acquisition × favor rendering</td>
<td>−2.64** (0.765)</td>
<td>−0.906 (0.774)</td>
<td>−0.714*** (0.201)</td>
<td>−0.421** (0.170)</td>
</tr>
<tr>
<td>Announcement of diversifying acquisition × awareness of another analyst’s loss of favors or access</td>
<td></td>
<td></td>
<td>−0.284* (0.140)</td>
<td>−0.182** (0.071)</td>
</tr>
<tr>
<td>Reported earnings vs. forecasts × favor rendering</td>
<td></td>
<td></td>
<td>−0.156 (0.135)</td>
<td>−0.301* (0.137)</td>
</tr>
<tr>
<td>Reported earnings vs. forecasts × awareness of another analyst’s loss of favors or access</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Favor rendering | −0.649* (0.272) | −0.556* (0.272) | −0.484*** (0.145) | −0.326* (0.142) |
Announcement of diversifying acquisition | 1.561 (0.844) | 2.286* (0.907) | 0.658* (0.306) | 1.089*** (0.306) |
Reported earnings vs. forecasts | 0.288 (0.150) | 0.281** (0.102) | 0.001* (0.003) | 0.001* (0.003) |
Size of analyst’s employer | 0.0003 (0.001) | 0.0002 (0.001) | 0.001* (0.0003) | 0.001* (0.0003) |
Friendship tie between executive and analyst | −0.879 (0.505) | −0.867 (0.507) | −0.403* (0.199) | −0.405* (0.198) |
Executive selling behavior | −0.257 (0.206) | −0.225 (0.206) | −0.124 (0.094) | −0.130 (0.094) |
Social interaction between executive and analyst | 0.156 (0.188) | 0.138 (0.190) | 0.172 (0.096) | 0.168 (0.096) |
Number of other analysts covering firm | −0.0001 (0.013) | −0.003 (0.013) | 0.0001 (0.010) | 0.0001 (0.010) |
Prior recommendation on focal firm by analyst | 0.685** (0.243) | 0.694* (0.246) | 0.533* (0.176) | 0.556** (0.174) |
Focal firm sales | −0.005 (0.013) | −0.005 (0.013) | −0.013 (0.008) | −0.012 (0.008) |
Investment relations officer | 2.261** (0.734) | 2.280** (0.715) | 2.758*** (0.469) | 2.749*** (0.468) |
Chief financial officer | 2.085*** (0.499) | 1.990*** (0.505) | 1.650*** (0.227) | 1.662*** (0.226) |
Other announcements by focal firm | −0.916* (0.380) | −0.898* (0.380) | −0.433* (0.202) | −0.422* (0.202) |
Time period for which favor rendering assessed | −0.019 (0.041) | −0.021 (0.041) | −0.028 (0.023) | −0.028 (0.023) |
Focal firm market-to-book value | −0.945** (0.302) | −0.946** (0.303) | −0.695*** (0.156) | −0.690*** (0.155) |
All-America status of analyst | 0.004 (0.220) | −0.007 (0.240) | −0.319 (0.350) | −0.288 (0.351) |
Positive statements in press releases | −0.033 (0.041) | −0.030 (0.041) | −0.014 (0.017) | −0.013 (0.017) |
Personal access to top executives | −0.385 (0.204) | −0.296 (0.196) | −0.125 (0.099) | −0.141 (0.085) |
Awareness of another analyst’s loss of favors or executive access | −0.329* (0.135) | −0.301* (0.137) | −0.294** (0.094) | −0.235* (0.095) |
Constant | 1.403 (1.024) | 1.368 (1.036) | 0.454 (0.522) | 0.476 (0.517) |

Wald χ² | 123.95*** | 165.10*** | 183.06*** | 237.45*** |
Incremental χ² | 41.15*** | 54.39*** |

* p < .05
** p < .01
*** p < .001

T-tests are one-tailed for hypothesized effects, two-tailed for control variables.

Effect of negative or controversial information about their firms on analyst stock recommendations.

Further results provided evidence that such influence attempts tend to succeed: executive favor rendering significantly reduced the propensity for analysts to downgrade a firm’s stock in response to the announcement of relatively low earnings or diversifying acquisitions. Thus, it appears that analysts tend to reciprocate executive favors by maintaining their stock recommendation for the executive’s firm despite the release of negative or controversial information about the firm. A third set of results provided further evidence for reciprocity in manager-analyst relations. In particular, the findings suggested that analysts who downgrade a firm’s stock elicit negative reciprocity from the firm’s executives, in the form of diminished favor rendering and reduced personal access to top executives.
executives at the downgraded firm. A fourth set of results provided evidence that negative reciprocity in response to downgrades can influence subsequent analyst behavior: analysts who were aware of another analyst’s loss of favors or access to executives after downgrading a focal firm were less likely to subsequently downgrade the firm in response to the disclosure of relatively low earnings or a diversifying acquisition. This result is consistent with the social exchange literature, which suggests that retaliation against an injurious act serves as a credible threat to punish similar such acts in the future, thus deterring other exchange partners from engaging in noncooperative behavior.

Overview

In short, our findings provide multifaceted evidence for social influence and reciprocity in relations between top executives and the analysts who cover their firms, thus supporting a sociopolitical perspective on manager-analyst relations. The results suggest that (1) top executives use favor rendering as a social influence tactic in their relations with security analysts, and (2) such favor rendering elicits positive reciprocity from analysts in the form of more positive stock recommendations, while (3) negative analyst recommendations elicit negative reciprocity from executives, and (4) negative reciprocity in turn deters noncooperative behavior (i.e., negative recommendations) by other analysts. From a methodological standpoint, our empirical analysis is based on a unique data set comprised of original survey data on favor rendering and personal access to executives collected from a large sample of security analysts and top executives. We obtained a fairly high response rate and provided evidence of interrater reliability of our survey measures, while controlling for a range of social and organizational factors that could be correlated with the independent and dependent variables of interest. Moreover, although our study was conducted in a field setting, it provides a relatively strong test of reciprocity between social actors by positing and testing dynamic relationships.

Contributions

Our theory and supportive results contribute to an understanding of how corporate leaders influence the behavior of external constituents toward their firms. A growing literature in organization theory and strategic management has examined the behavioral mechanisms by which leaders influence the actions of key external constituents toward their organizations. Research on organizational influence external constituents through overt, public actions and communications such as symbolic changes in corporate governance or impression management in press releases. Although this literature has provided impressive evidence that corporate leaders can garner support from external constituents though symbolic action, it has devoted little attention to how leaders, on a more private level, may enhance or maintain constituent support by engaging in social influence processes that develop or maintain social exchange relations with individual constituents of their firms. Yet, the larger literature on power and influence in organizations, government, and other settings suggests that both public symbolic management and private interpersonal influence and exchange processes are important means of constituent support (Bowles, 1987; Edelman, 1977; Pfeffer, 1981). Our study begins to address this gap in the literature by examining the determinants and consequences of social influence and reciprocity in relations between top executives and a key external constituent of firms: security analysts. Given that analyst reports are known to have a significant influence on the behavior of investors and other members of the financial community toward focal firms, our theory and supportive findings ultimately address how corporate leaders can build and perpetuate external support for their firms by engaging in social influence processes that foster and maintain social exchange with a key external constituent of the firms.

Our study builds on recent research by Westphal and Bednar (2007), which showed that interpersonal influence behavior by executives toward representatives of institutional investors can reduce the likelihood of changes in corporate governance and strategy that would tend to harm executive interests. The present findings complement that study by suggesting how executive influence behavior can actually affect an external constituent’s assessment of a firm, while also examining influence behavior toward a different constituent (i.e., security analysts). Moreover, Westphal and Bednar (2007) did not consider the potential for negative reciprocity in relations between executives and constituents or the influence of retaliation on third parties. Taken together, these studies raise the possibility that executives simultaneously exercise interpersonal influence over different constituents through separate channels, so that the total impact of such behavior on constituent opinion and decision making could be substantially greater than is suggested by the current findings alone.

Our theory and results also contribute to the literatures on financial market behavior and corpo-
rate control. As noted above, prior research has documented a systematic tendency for analysts to underadjust their stock recommendations and earnings forecasts in response to negative firm information, resulting in overly positive stock ratings and overly optimistic forecasts (Chopra, 1998; Francis & Philbrick, 1993; Hong & Kubik, 2003). Extant theories attribute this positivity bias primarily to cognitive factors such as the tendency to discount or ignore disconfirming evidence. Our study provides a social explanation for this phenomenon. Specifically, our theoretical argument suggested how social influence and reciprocity in manager-analyst relations could dampen the effect of negative firm information on analyst stock ratings, and our results confirmed this thesis for a large sample of analysts and managers at large and midsized U.S. firms. Accordingly, our findings have important implications for corporate control and the efficiency of capital markets. Security analysts, by issuing negative recommendations in response to poor firm performance or strategic actions that appear to serve management interests at the expense of shareholders, can direct capital and other resources away from underperforming firms and self-interested managers toward more productive uses. In this way, analysts can serve an important role in controlling agency costs and maintaining the allocative efficiency of financial markets (Jensen, 2004; Wright et al., 2002; Zuckerman, 2000). An implication of our findings is that microsocial factors in manager-analyst relationships, by reducing the objectivity of security analysts’ stock recommendations, may ultimately compromise corporate control and financial market efficiency. Moreover, our findings indicated that managers tend to concentrate their favor rendering on analysts who have the most influence on market behavior, thus strengthening the link between managers’ social influence behavior and market (in)efficiency. Thus, our theory and findings contribute to the larger behavioral literature on financial markets, which has focused mainly on how cognitive and institutional factors limit market efficiency. This literature has not systematically examined the impact of microsocial factors, such as social influence and reciprocity in manager-analyst relationships, on the allocative efficiency of financial markets.

Our theory and findings also have implications for organizational research on social capital and embeddedness. This literature has tended to treat social network ties as exogenous and devoted little attention to the behavioral mechanisms by which social ties are actively cultivated (cf. Adler & Kwon, 2002; Brass, Galaskiewicz, Greve, & Wenpin, 2004; Geletkanycz, Boyd, & Finkelstein, 2001). Our study suggests that social influence behavior (i.e., favor rendering), by drawing powerful others into a social exchange relationship, may be an important mechanism by which leaders build and maintain their social capital. Our theory and supportive results also address how negative reciprocity or retaliation in response to injurious behavior can help maintain positive social ties with third parties, by deterring those other actors from engaging in noncooperative behavior (i.e., issuing more negative firm reports in response to negative information about a firm).

It might be suggested that rendering favors to analysts contains elements of bribery. According to relatively broad definitions of the term, bribery involves the provision of money or favors in order to influence the judgment or conduct of someone in a position of trust (Weber & Getz, 2004). On the other hand, bribery is also often defined as involving criminal behavior, and otherwise generally connotes such behavior (Jain, 2001; Kingston, 2007). Moreover, many definitions state that bribery refers especially to illicit payments made to a public official, and most empirical research on bribery has examined the corruption of public officials (typically in developing nations) (Jain, 2001; Weber & Getz, 2004). Thus, the relevance of empirical research on bribery to the social influence processes examined in this study is questionable. Nevertheless, it is interesting to note several parallels between theoretical assertions and findings about the determinants and consequences of bribery and our perspective on executive favor rendering directed toward analysts. Several authors have asserted that the subjective expected utility of bribing public officials predicts the likelihood and extent of such behavior (for a review, see Jain [2001]). Moreover, some have suggested that bribery is especially common where the decision-making process by which public officials allocate benefits appears complex or ambiguous to outsiders. Similarly, our theory suggested that complexity and subjectivity in the decision-making process by which analysts render recommendations may enhance the subjective expected utility of executive favor rendering. Also, political economists have suggested that bribery often has distortionary and disincentive effects that compromise social welfare, and we have suggested that executive favor rendering directed to analysts may have negative welfare effects by compromising the allocative efficiency of capital markets.

It might be suggested that analysts have incentives to render “accurate” judgments about the firms that they cover and that these incentives should diminish the effects of executive favor ren-
dering on their recommendations. Although not denying this possibility, we would suggest that a number of factors are likely to diminish the extent to which economic incentives reduce analysts’ receptiveness to social influence from top executives. There is mixed evidence as to whether the correlation between stock recommendations and subsequent firm performance is a strong predictor of analysts’ career advancement (Mikhail, Walther, & Willis, 1999), and analysts face considerable uncertainty in determining whether and when negative firm information is sufficient to warrant a downgrade. Further, our theory and findings suggest that executives focus their favor rendering on relatively influential analysts whose recommendations tend to have a significant influence on the market value of the firms that they cover (Stickel, 1995). In effect, the stock recommendations of highly influential analysts are to some extent self-fulfilling (Clement & Tse, 2003), so that if analysts were rewarded according to the predictive value of their recommendations (i.e., the extent to which their recommendations predict subsequent market returns), they would not necessarily be penalized for maintaining their current stock recommendation in the face of negative or controversial information about a firm.

In addition, and perhaps most importantly, the theoretical mechanisms by which executive favor rendering is posited to influence analyst behavior should operate despite economic incentives for analysts to render accurate judgments. Because of the norm of reciprocity, when most people receive favors from another person, they feel socially and psychologically obligated to reciprocate despite economic incentives to the contrary. Thus, in response to an executive’s favor rendering, analysts should tend to feel appreciable cognitive dissonance about taking actions (e.g., downgrades) that not only fail to reciprocate benefits, but that also actively harm the executive’s interests. Moreover, the literature on ingratiation has shown that favor rendering induces positive affect for the favor-doer, which independently increases the likelihood of favorable treatment despite contrary economic incentives (Yukl & Tracey, 1992). Our theory also suggested that there is an instrumental motive for reciprocity: analysts may reciprocate favors in order to reinforce the executive’s generosity and increase the likelihood of receiving more favors in the future (Blau, 1964). When these mechanisms are considered together, it seems quite plausible that favor rendering by an executive would tend to deter analysts from taking actions that would harm the executive’s interests, such as downgrading the executive’s firm, despite countervailing incentives to render accurate judgments about the firm, which may not be strong in any case.

It might be suggested that executives initially respond to a downgrade by rendering more favors for the offending analyst, and only retaliate if the analyst fails to respond to such positive treatment. However, if an executive were to respond to a downgrade with more favors, if only for a period of time, it would positively reinforce the issuance of downgrades, providing an incentive for other analysts to issue more negative reports of the focal executive’s firm. Moreover, social exchange theory suggests that emotional factors partially mediate negative reciprocity (Ekeh, 1974; Gouldner, 1960; Homans, 1958), and there is compelling empirical evidence for this proposition. There is growing evidence that most people exhibit a punitive sentiment in response to noncooperative behavior by social exchange partners, even in situations where instrumental benefits from negative reciprocity are absent. Such a sentiment also reduces the likelihood that executives will respond to a downgrade by rendering more favors to the offending analyst. Moreover, our results suggest that executives tend to respond initially to downgrades by issuing fewer favors and granting less personal access to the issuing analyst (i.e., executives respond in this way during the period subsequent to the downgrade and prior to the analyst’s next report, which is the first opportunity for the analyst to upgrade the stock back to the initial recommendation).

**Limitations and Future Research**

Our findings do not necessarily generalize to the most recent time period. It is possible that regulations adopted early in the decade have reduced the effect of favor rendering on analyst recommendations in more recent years. The October 2000 Securities and Exchange Commission Regulation Fair Disclosure (FD) provides that when a firm’s senior officer, or any other employee or agent who regularly communicates with security holders, discloses material nonpublic information to securities market professionals or holders of the company’s securities, the firm must make public disclosure of that information. Although this regulation does not directly affect executive favor rendering directed toward analysts, it may have indirectly influenced such behavior by altering the climate of executive-analyst relations. However, most of our results are based on data from the post–Regulation FD period; although the primary tests of Hypotheses 1a and 2a, regarding the effects of reported earnings on favor rendering, are based on data from the pre–Regulation FD period, all other hypothesis tests are based
on data from the post–Regulation FD period. Nevertheless, further research is needed on executive-analyst relations in the most recent time period.

Our analyses do not necessarily capture the full impact of executive favor rendering on analyst behavior. It is possible that executives provide favors for analysts on an ongoing basis as a kind of insurance against negative events. Although separate analyses indicated that past favor rendering did not influence the likelihood of downgrades in response to negative earnings surprises or diversifying acquisitions independently of subsequent favor rendering—perhaps because such past behavior was less salient to analysts than executives’ more recent actions—past favor rendering could still influence analyst behavior in other ways. For instance, journalists sometimes ask analysts to comment on the significance of apparent crises such as widespread product failures or alleged ethical violations by key personnel. In such cases, there may not be time to render favors between an event and the request for comment, and thus past favor rendering may be valuable in affecting an analyst’s comment (or willingness to comment) about the event in the media. Alternatively, executives might be more likely to engage in analyst favor rendering in response to events (e.g., diversifying acquisitions) that receive an initially negative investor reaction. Thus, future research should examine whether such announcements have an especially strong effect on executive favor rendering.

Future studies could follow our theoretical and empirical approach by examining microsocial processes that mediate relations between managers and other constituents of firms, including members of the press, labor representatives, government officials, and managers of alliance partners. We need a better understanding of how social influence tactics, reciprocity, and other social processes are used to successfully manage these relationships. There is also a shortage of research on negative social dynamics in manager-constituent relationships. Moreover, future studies might examine how social influence behavior toward key external constituents affects executive-level outcomes such as CEO compensation or dismissal (cf. Westphal & Bednar, 2007), or firm-level outcomes such as free cash flow. In effect, though prior research has examined how internal political dynamics affect such outcomes (e.g., Finkelstein & Hambrick, 1989; Shen & Cannella, 2002), there has been little consideration of how political dynamics in relations with external constituents affect agency costs within a firm. One might also examine how executives vary their social influence strategies according to the particular characteristics and behavior of individual analysts. For instance, executives might notice individual differences in analysts’ propensity to issue downgrades in response to negative firm information and adjust their level of favor rendering accordingly. Finally, future studies could examine how symbolic management or other relatively overt, public forms of constituent management combine with the microsocial processes examined in this study to affect important firm-level outcomes. There would be value in developing a larger theory of manager-constituent relations that integrates perspectives on interpersonal influence with symbolic management and impression management perspectives.

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**APPENDIX**

**Survey Scales**

**Favor Rendering**

1. To what extent has this executive done personal or professional favors for you since [date of announcement]? (not at all . . . to some extent . . . very much so)
2. To what extent has this executive made an effort to do favors for you since [date of announcement]? (not at all . . . to some extent . . . very much so)
3. This executive has done a number of favors for me since [date of announcement]. (strongly disagree . . . neither agree nor disagree . . . strongly agree)
4. This executive has made an effort to do personal favors for me since [date of announcement]. (strongly disagree . . . neither agree nor disagree . . . strongly agree)
5. Please indicate how many times this executive has performed the following favors for you since [date of announcement]:
   (a) Put you in contact with a top manager at another firm
   (b) Recommended you for a position at another company
   (c) Provided you with advice on a personal matter
   (d) Provided you with advice on a career matter
6. Please list any other favors that this executive has done for you since [date of announcement] and on how many occasions:
   Favor: ____________________________ Number of times: ____________________________
   Favor: ____________________________ Number of times: ____________________________
   Favor: ____________________________ Number of times: ____________________________

**Personal Access to Top Executives**

1. To what extent have you had personal access to this executive since [date of recommendation]? (not at all . . . to some extent . . . very much so)
2. I have had considerable personal access to this executive since [date of recommendation]. (strongly disagree . . . neither agree nor disagree . . . strongly agree)
3. To what extent has this executive made him/herself available to you since [date of recommendation]? (not at all . . . to some extent . . . very much so)
4. How many times has this executive failed to return your phone call since [date of recommendation]?
5. How many times has this executive ignored your question in a conference call since [date of recommendation]?
6. Please list any other instances in which you were denied access to this executive since [date of recommendation]:
   1. ____________________________
   2. ____________________________
   3. ____________________________
Awareness of Another Analyst’s Loss of Favors or Executive Access

1. Are you aware of an instance in the last two years in which another analyst who covers [focal firm] had difficulty gaining access to top executives of the firm after downgrading their stock?
2. Have you heard of a case during the last two years in which another analyst who covers [focal firm] received fewer favors from executives after downgrading the firm?
3. In the past two years have you seen or heard of an instance in which an analyst seemed to get blacklisted by [this firm’s] executives after issuing a downgrade?
4. In the past two years have you seen or heard of an instance in which an analyst was unable to get access to [this firm’s] top executives after downgrading their stock?
5. Are you aware of an instance during the last two years in which an analyst who covers [focal firm] stopping receiving favors from executives after downgrading the firm?

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