**Analysts Unfavorable Recommendation Initiations**

Joshua Livnat

jlivnat@stern.nyu.edu

New York University

Quantitative Management Associates

Kate Suslava

ks063@bucknell.edu

Bucknell University

Yakun Wang

wangyakun@cuhk.edu.cn

Chinese University of Hongkong, Shenzhen

Li Zhang

lizhang@business.rutgers.edu

Rutgers University

Chen Zhao

zhaochen@swufe.edu.cn

Southwestern University of Finance and Economics

**Abstract**

We observe that analyst unfavorable initiations of coverage (hold/sell/strong sell) amount to half of all analyst initiations. This result is surprising given that analyst recommendations are documented to be overly optimistic in the prior literature. Why would financial analysts initiate unfavorable coverage? First, we find that analysts are more likely to initiate coverage with reserved recommendations when their reports include more discussions about firm uncertainty, suggesting that analysts are dissuaded from issuing favorable forecasts when they perceive the firm's future prospects to be more uncertain. Second, we find that analysts gain credibility from investors after they begin coverage with unfavorable recommendations. Specifically, the market reaction to subsequent upgrading recommendations is significantly stronger after analysts initiate unfavorable coverage than when favorable coverage was initiated. These two forces explain why there exist so many unfavorable initiations of coverage.

**Key words**: analyst recommendations, coverage initiation, uncertainty, stock market reaction

**JEL classification:** G10, G14, G17, G24