

## Analyzing the Analysts

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Analyzing the industry analysts has become a popular indoor sport in CRM and beyond. Ever since the scandals involving a few financial analysts kiting stocks for their investment bank employers, there has been an attempt to upgrade the standards by which financial analysts are judged and to apply those standards to industry analysts as well. CRM Magazine has an interesting piece by Jason Compton in the November issue that analyzes the analysts and tries to figure out what makes a good one and why we need them.

And why not? There have been enough apparently questionable activities by some industry analysts performing projects for vendors — so called white papers for hire — to make average consumers want to change the atmosphere. My only issue with all the attention is that we might be applying the wrong fix. The rules for analyst behavior when examining a company's financial position and its prospects might not be the optimal rules of engagement in the industry analyst realm. Here are my observations based on my career as an industry analyst.

### IS IT A PRACTICE OR A JOB?

I doubt you can answer the larger questions about the analyst community until you settle on the fundamental questions of the job description and who pays, here's why.

The work of an industry analyst is a practice and there is a big difference between a job and a practice. In a practice one is supposed to take all that one knows from experience and learning and apply it to unique situations for the benefit of a client. For example, lawyers and doctors use everything they have learned

within their professions and apply it for the exclusive good of clients and patients.

They say a law client is entitled to the best efforts and most aggressive application of a lawyer's ability on behalf of the client. A lawyer's belief in the client's guilt or innocence should not enter into the mindset of the lawyer. Maybe that's why so many of us have problems with attorneys — until we need one. Perhaps the medical model is better. At graduation from medical school new doctors still repeat Hippocrates' oath to "First, do no harm."

But practices evolve as knowledge and learning push back the frontiers of ignorance. Performing a dental extraction without anesthesia today might be considered malpractice but until about 1846, when the anesthetic properties of nitrous oxide and then ether were discovered, it was common practice. That, to me is the big difference — in a practice your thinking evolves as you know more. And nobody accuses you of "flip-flopping."

Doctors and lawyers are not the only people who practice a profession. Accountants and tax advisors can also be classified that way.

### INDUSTRY ANALYSIS IS A PRACTICE

Just about everyone I know, myself included, regards what industry analysts do as a practice. Believing that history repeats itself, but never exactly, we take what we've learned about our subject matter and try to apply it to what might happen next. We are sometimes wrong but the key is that if we are wrong, our intentions are good — i.e. first do no harm.

We also use the tools of survey and statistical analysis to test our hypotheses and to share our

findings with the world. Analysis is the best way to know if our theories are off the mark and what needs to be changed in our thinking. Alternatively, it's what reinforces our point of view and makes it tenable.

That approach enables us to look at new technologies and new markets with eyes wide open. And looking at what is new and hard to figure out is a critical part of what we do.

Unlike financial analysts who deal mostly with established (but not necessarily mature) companies and markets, industry analysts tend to be on hand closer to the birth of a category or an idea.

### FINANCIAL ANALYSIS IS A JOB

I have a great deal of respect for my financial analyst cousins. They take a great deal of information about the economy, a sector, and a company and along with some basic assumptions about the future, like GAAP standards, weave it into credible prognostications about individual company performance.

But at the end of the day, financial analysis is a job not a practice. As a financial analyst you have one loyalty — to the company that employs you — and your primary job is to be right in retrospect within narrow tolerances and if you are wrong, to err on the side of caution. You can forecast 10 percent growth when the numbers really tell you it's more like 14 percent and no one will be mad. That's because there is a fundamental difference in the audience for your work.

### WHO PAYS?

Like it or not, no analysis of either the financial or industry type gets done unless someone is willing to pay for it. Financial analyst firms have a built in audience — investors — who need their financial recommendations to make investment decisions. As we have seen the financial analysis system breaks down when the companies that are the subjects, become

the clients and start demanding certain coverage.

The question of who pays is at the heart of the controversy about industry analysts and it is a wonderful "Catch-22" for the industry. No one with a mortgage to pay is going to research and write about an obscure new technology or business solution in an unproven market. In fact, it is hard for emerging vendors to get coverage by many analyst firms when markets are just emerging because there is little or no market for such information. So if there is going to be any third party validation of these emerging companies, more often than not, they have to pay for it themselves.

But paying an analyst firm to cover a company need not be the conflict of interest it sometimes appears. Many credible analysts make a living at uncovering new companies and new markets and maintain their integrity at the same time. The key is in transparency and expectation setting.

### A PATH FORWARD

Industry analysts ought to be able to tell their readers who paid for their analysis but at the same time they need to be — and most are — firm about how they work and what a vendor can expect from a research project. I do not think there needs to be some industry watch dog group that oversees what analysts do because I believe it would be counter productive. It would have a chilling effect on research and no one would win in that situation. There is no perfect solution to this issue and different analyst firms each work a bit differently so perhaps the best approach for end users is to do their homework and seek out multiple sources. And always remember this is a market place like any other and the rules of engagement haven't changed much since the Romans wrote the primary rule that we still quote in their native tongue, *caveat emptor*.





## About the Author



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Denis Pombriant is a well known thought leader in CRM and he is the founder and managing principal of the Beagle Research Group, a CRM market research firm and consultancy. In 2003, CRM Magazine named Pombriant one of the most influential executives in the CRM industry. Pombriant's latest white paper, "The New Garage" discusses the emerging new enterprise software industry business model.

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## About Beagle Research Group

Beagle Research Group is a consulting and market research organization focused on emerging companies and technologies that will have an important impact on the way business is conducted in the years ahead. Our work is based on professional standards of quantitative and qualitative research which informs all of our publications.

This document was researched and written by Beagle Research Group.

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