Commissioned Research
No More Biased Than Research From Other Sources.

A common perception in the market is that commissioned research is invariably biased towards the subject company, largely due to the fact that the companies are paying a direct fee for the research, and the corollary is that the researchers must follow the company line.

This raises the question, 'is commissioned research biased?', and if so 'is it any more biased than that from other sources of company research, such as broking houses?'

My conclusion, as discussed below, is that commissioned research is no more biased than, or has no more potential to be more biased than, research from other sources.

In discussing this, I am solely concentrating on the junior to mid-size resources sector, where a "buy" recommendation is generally taken as a "speculative buy" i.e. one with significant risk and downside potential, and where there are very few "sell" recommendations.

If commissioned research is more biased from that written by other research providers, e.g. broking houses, it cannot be due to remuneration – brokers will only write research to help generate income or the potential to earn future income – they are not philanthropists. Brokers income is generated either indirectly (e.g. due to increased brokerage via more trades in a stock for which research has been published, attracting new clients due to making good picks or via using it to attract a company's fund raising business for which fees are received), or directly when research is part of an ongoing corporate mandate with the company.

The latter case is the most similar to the commissioned research model – indeed some brokers will write commissioned research and the fact that it is commissioned will only be seen in the disclaimer at the back. Furthermore, brokers may hold significant positions in stocks and thus it is in their best interests to support those stocks, with writing positive research one way of achieving this. Any potential difference then must come in how a stock is chosen and how the research is written.

When prudently researched and written, with the best interests of the potential investor in mind, commissioned research (and any other research for that matter) is fair, and no more biased than that from other sources.

Invariably, there is a filtering of clients before a decision is made whether to write up a company (or when selecting companies to approach for potential write up), and thus poor quality stocks are able to be eliminated if the analyst does not like it, or would feel uncomfortable in providing a positive recommendation.

Importantly, good research reports will always discuss the key risks in a company, thus enabling investors to assess whether it meets their investment criteria– the reports should not simply be "advertising brochures" for the company and need to reflect the analyst's thoughts and conclusions.

It is critical to remember that analysts (for those providers with the appropriate AFSL) are making a recommendation to investors and potential investors on what to do with THEIR money – it is the investors' interests that need to be held paramount. This last point is actually enshrined in legislation – the needs of the investor do need to come first. It is important that, for a report to be unbiased, the analyst retains a significant degree of independence in picking and writing up companies – this applies equally to independent commissioned work and analysts in broking houses.

There is the risk, in the case of commissioned work, for any stock to be written up just to get the fee, and in the case of broking firms 'house stocks' may be promoted with minimal consideration of the merits of the company. Where this happens there is of course the risk of considerable bias, with the needs of the research provider and researched company taking precedence over the interests of the investors.

It is the analysts' name that is on the research, and if we want to develop or keep a professional reputation it is paramount to provide high quality, unbiased research.

As a background to readers, there are three key stakeholders in the business of providing commissioned and non-commissioned research

1) *Most importantly, the investors and potential investors, whose interests are paramount*

2) *The company commissioning the work*

3) *The firm and/or analyst writing the research*

All three parties have their own interests, and are looking for some gain from their actions – this is not a altruistic business we are in.

Investors and potential investors are there for one reason – to make money, or to put it more genteelly to "achieve a return on their investment". They often rely on research (and analysts) to make an informed opinion.

The company is naturally looking to attract new investors (and to retain existing ones), and in the process increase its share price and market capitalisation. In the case of the junior resource sector this is vital for attracting new capital to carry out their core business of mineral exploration and development without overly diluting existing holders. A company has a number of options when doing this, which brings us to the third stakeholder, the research providers.

Resources companies commonly use research as a marketing tool, with the two key research providers being those providing commissioned research (e.g. Breakaway Research) and those providing non-commissioned research (e.g. broking houses, or the broking/ research arms of banks and other AFSL holders). Both research providers are remunerated for this work, albeit by different mechanisms.

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