Artificial Intelligence Has Entered the Field of Investing: What are the implications for financial reporting?

The Issue
Technology is rapidly transforming the accessibility of information useful for investing purposes. Much of financial reporting continues to be built on the implicit or explicit assumption of a traditional user. However, it is already clear that a large and increasing portion of the “readership” for this information consists of artificial intelligence (AI) of one kind or another. This evolution has implications for the direction of financial reporting.

The Opportunity — The Use of Innovative Technology to Improve Financial Analysis
Everyone talks about the vast quantity of data available to investors and the proliferation of non-GAAP measures. What is less understood is how investors are using AI to obtain and analyze this information, including financial information, to facilitate investment decision-making.

Historically, investors primarily used financial data found in traditional information sources (e.g., financial statements, regulatory filings) to search for trends. However, investors are now increasingly embracing

WHAT IS “ALTERNATIVE DATA”?
There is no commonly accepted definition of alternative data. It is generally described as data from non-traditional data sources used to support investment decisions.

“We define alternative data as the intersection of big data and investment research. When applied to investment research, alternative data is the collection, cleansing, packaging, modeling and distribution of large structured and unstructured data sources to generate predictive insights and improved investment returns.”

other data to gain an edge in their investment strategy. This is often referred to as “alternative data”. Investors are also now able to access financial information in a new way and analyze it in ways that were not possible previously.

The alternative data landscape includes things like satellite imagery and information from news feeds, web traffic and social media, just to name a few. Of course, use of diverse information sources is not a completely new phenomenon. For example, analysts have been tracking things like the language and tone of executives on earnings calls for a long time. What has changed are the new forms of alternative data which are emerging and the sophisticated tools investors are using to analyze this data.

There is no shortage of technology products available to the investing public that use AI to gather and analyze data from a multitude of different sources to inform investment selections and make predictions. Some products even claim to automatically check the accuracy of facts.

For example, Sentieo offers contextualized search of earnings conference calls using natural language processing. Kensho, recently acquired by S&P Global, uses machine learning and AI to comb through vast amounts of data to find correlations and answers to complex financial questions. RS Metrics provides insights and data based on analysis of satellite imagery.

The market for alternative data in the U.S. is expected to reach $400 million by 2021.

Source: TABB Research Group

The Questions
These technology driven investing developments raise important questions for all stakeholders and participants in the financial reporting process:

For Standard-Setters
What place does periodic GAAP-compliant financial reporting occupy in this new environment? Are our standards keeping pace with the capacities of the new AI-enabled users?

For Regulators
Are we continuing to focus on the right issues? Do the regulations and remedies that worked well in the past continue to achieve the right balance between facilitation of information and protection of investors in the face of escalating technological capability? Do we need a new approach or changes in our current approach to react to the increased use of artificial intelligence for investing purposes?

For Preparers
How well do we understand our real users and the way they access our financial information? Are we overlooking opportunities to create value? Are the key performance measures and other metrics we are reporting well suited to the new environment?
For (Human) Investors
Do we need to change the way we engage with financial reporting? What implications do the greater prevalence of AI in investing carry for our short-term and long-term investing practices? What are the risks associated with the data we are relying on?

Closing Thoughts
The jury is still out on the optimal mix and balance of information needed to inform investment decision-making. Technology has complicated matters. One AI startup stated: “The more inputs you have, the better you can make decisions.” There are others who argue that plying investors with too much data can have the opposite result. Whatever your position, it does not appear that investor thirst for more information will be quenched anytime soon.