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# Estimating risk-return relations with analysts price targets\*

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## Abstract

Asset pricing tests often replace ex ante return expectation with ex post realization. The large deviation between the two drastically weakens the power of these tests. This paper proposes to use analysts consensus price target for a stock as the market expectation of the stock's future price to directly construct the stock's expected excess return. Analyzing the expected excess return behavior both over time and across different stocks shows that classic asset pricing theory works much better on ex ante return expectations than on ex post realizations. The analysis also provides new insights on the pricing of common equity risk factors.

*JEL Classification:* C13; C51; G12

*Keywords:* Risk-return relation; Equity risk premium; Analysts price targets

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