ABSTRACTS

1. MODELING MARKET BUBBLES, RISK AVERSION, AND EFFICIENT MARKETS: A ROLE FOR THE EFFICIENT MARKET HYPOTHESIS AND BEHAVIORAL MODELS

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ABSTRACT

Recent attention in financial markets has centered on the preponderance of 'market bubbles.' In fact, some studies have questioned the notion of market rationality and the theorized efficient market hypothesis in light of these valuation bubbles. We investigate several factors which might generate market bubbles in a market comprised of risk averse and rationally behaving market participants. To do so, we model algebraically simple market structures including binomially distributed asset values in a two-period model. Even in this simple financial environment, we find rational behavior that generates valuation bubbles. Finally, we discuss several empirical market scenarios where we find our model offers intuition regarding the outcomes in these markets.

Keywords: *Efficient Market Hypothesis, Risk Aversion, Market Bubbles*

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2. VALUATION AND LONG-RUN GROWTH RATES

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ABSTRACT

We use financial analyst-based long-run earnings growth measures to examine excess firm values associated with single- and multi-segment firms. We explicitly examine the relationship of expected long-run growth rates and the diversification discount. Our results indicate that long-run earnings growth rates for the individual segments of multi-segment firms are lower than corresponding growth rates for single segment firms. Further, this difference in forecasted growth plays a major role in explaining the diversification discount of multi-segment firms. We conclude that these lower growth rates are consistent with improperly functioning internal capital markets.

Keywords: *Growth Rates, Valuation, Analyst Estimates, Diversification Discount*

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3. IMPACT OF ECONOMIC LIBERALIZATION ON MANUFACTURER'S SERVICES – CASE STUDY OF AN INDIAN AUTOMOBILE COMPANY

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ABSTRACT

The economic liberalization process, initiated in 1991, has had significant effect on the automobile and the auto component industry in India. The industry is now becoming globally competitive and the policies of economic liberalization have led to capability building of the domestic industry. While the impact of liberalization on the manufacturing and the service sectors in India has been studied, there has also been a similar change in the service component of manufacturing companies. This paper presents a case *study detailing the experience of an Indian automobile manufacturing company which wanted to improve the effectiveness of its display at the Indian Auto Expo and also its efficiency. While the case description highlights the efficiency gains achieved through better planning it also brings to light how a company which prospered during the control regime of the past is adjusting to the changing realities of the market and improving not only the quality of its 'product' but also the service component of the product.*

Keywords: *economic liberalization, automobile industry, optimization, personnel scheduling, first-hour principle*

4. STATE FISCAL POLICY VARIABLES AND NET SMALL BUSINESS FORMATION

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ABSTRACT

We examine the net addition of small businesses across states in response to specific state fiscal policy variables. We find small business creation is tied to individual state spending patterns in education and welfare and the percentage of state revenue from personal and corporate income tax. We examine whether these variables are consistent across different business types. We focus on capital asset intensive small business versus service-related small businesses, finding that for capital asset intensive businesses, the tax revenue pattern is significant, whereas for service-oriented business spending patterns have a much larger impact on small business net formation.

Keywords: *state fiscal policy; entrepreneurship; small business formation*

5. INFORMATION COMPONENTS, SPREAD AND SERIAL CORRELATION IN STOCK RETURNS

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ABSTRACT

This paper develops a model of stock prices to analyze the serial correlation and the autocorrelation in short-term stock returns. The paper provides an asymmetric information approach, and takes into account the trading mechanism and the specific and common components of information. A main point of the study is that the model used to examine serial correlation in stock returns depends crucially on the returns measurement period. Additionally, the study supports the idea that the time series properties of returns are different between individual stocks and portfolios, and that we can achieve a better understanding of the process of portfolio returns beginning by the individual stock returns level.

This paper proposes a market microstructure model to analyze stock prices and the autocorrelation of price changes. The different versions of this model are appropriate to different time periods ranging from the single trading period to one or two days. The development of the model predicts that the autocorrelation of stock returns is the sum of two terms. The spread is the source of a negative term, while the gradual incorporation of common information generates a positive term. In the case of daily stock returns, the model predicts that, taking into account the sign, the autocovariance can be positive, negative or approximately zero, depending on the absolute values of the two terms.

Keywords: *Financial Markets, Market Microstructure, Serial Correlation*

6. GOODWILL VALUATION AND EARNINGS MANAGEMENT

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ABSTRACT

The FASB recently proposed to adopt the economic entity theory for the consolidation of goodwill and non-controlling interests. The proposed economic entity theory recognized the fair value of the acquired company as a whole, not just the parent portion. This paper shows that companies allocate less amount to goodwill in the consolidation process can have results close to the abolished pooling-of-interests method and get better performance indicators. Goodwill does not necessarily suggest better earnings as indicated by the goodwill definition. It will be more consistent with the accounting policy for Research and Development (R&D) cost to immediately expense it right after the business combination. Such consistency not only provides better quality of accounting information but also reduces earnings management opportunities.

Keywords: *Earnings Management, Exposure Draft, Big Bath, Goodwill Impairment Loss*

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7. THE MATCHING PRINCIPLE IN THE ISLAMIC ACCOUNTING THOUGHT

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ABSTRACT

The main objective of this paper is to study one important accounting principle from Islamic point of view; this is the "Matching Principle". Illustrating this principle in the Islamic accounting thought would clarify how this pioneer thought was comprehensive in achieving not only its accounting objectives but also its economic and social objectives by constructing and adjusting some social systems, such as Zakah; and to contribute to the efforts made for the standardisation of the accounting bases used by Islamic banks. Such a standardisation would help in providing useful information to users of financial reports of Islamic banks.

Keywords: *matching principle, Islamic accounting thought*

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8. CEO AND CFO FINANCIAL STATEMENT CERTIFICATIONS UNDER THE SARBANES-OXLEY ACT: AN EXAMINATION OF PERCEIVED FRAUD DETERRENCE

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ABSTRACT

In an attempt to restore confidence in the financial reporting process, the Sarbanes-Oxley Act of 2002 requires public companies' CEOs and CFOs to certify the truthfulness, fairness, and completeness of their companies' financial statements. Survey data suggests, however, that investors may not view top management as trustworthy, raising concerns about the certifications' ability to increase confidence. Recognizing that the certifications' greatest strength may lie in their deterrence quality, this paper explores how nonprofessional investors perceive their effectiveness in preventing fraudulent financial reporting. It finds that when compared to other potential deterrents, namely alternative internal audit reporting structures, investors view the certifications as providing a moderate level of fraud protection.

These results suggest that the certifications may play an important role in creating the perception of reliable, transparent financial disclosures.

Keywords*: Sarbanes-Oxley Act, Financial Statement Certifications, Fraudulent Financial Reporting, Fraud Deterrence*

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9. DOES FUND SIZE STILL MATTER? AN ANALYSIS OF FUNDS SIZE, EXPENSES AND PERFORMANCE IN VOLATILE 2000

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ABSTRACT

This analysis updates the findings of Indro et al with 2000 data to determine if the size of a mutual fund influences the expenses and performance of the fund. In addition, the year 2000 was examined as a year of a volatile down movement in the markets. This provides insight into the nimbleness of different sized funds during severe market conditions. The question is addressed using a sample of Small, Medium and Large Cap Value, Blend and Growth funds. The results indicate that there are economies of scale in mutual fund management. That is as assets under management increase, fund expenses drop. However, these increased economies of scale do not necessarily translate into higher returns over short holding periods during volatile markets. As funds are pooled by investment style the negative relationship between returns and size becomes more dominant. Further evidence indicates that during volatile declining markets, there is a liquidity effect where diseconomies of scale start occurring.

Keywords: *Investments, Mutual Fund, Diversification, Fund Management, Asset Management, Portfolio Management*

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10. FURTHER EXAMINATION OF THE RELATIONSHIP BETWEEN PETROLEUM FUTURES PRICES

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ABSTRACT

This study investigated the relationships between crude oil, unleaded gasoline and heating oil futures prices. The study finds that these three futures price series are cointegrated and share one common stochastic trend. This article also shows that the crude oil variable is weakly exogenous and the common stochastic trend shared by the three price series is the crude oil variable. Furthermore, the study shows that heating oil and unleaded gasoline futures prices adjust to clear deviations from long-term equilibrium relationship. Finally, this study finds that there is a short-term bi-directional Granger Causality between crude oil and unleaded gasoline futures prices but there is only one way Granger causality between crude oil (unleaded gasoline) and heating oil.

Keywords: *Petroleum Futures, Cointegration, Error correction Model*

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11. REGULATION, INTERNAL CONTROLS AND COSTS IN FINANCIAL REPORTING

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ABSTRACT

From 1933 through 1995 financial restatements did not represent a significant issue in securities regulation. In 1995, Tort reform altered the regulatory landscape for accountants. Predictably, there was a change in accounting practice. This paper reviews the history of the resulting turbulent period and the financial scandals surfacing in 2001 and 2002. The period, from 1995 to 2002 is a particularly significant period in securities litigation. We present some financial data on the undesirable impact of tort reform on the financial reporting of revenues. The data suggest that the revenue distortions were not limited to a few corporations run by criminals, but involved a widespread breakdown of reporting standards. The paper then examines the congressional response as embodied in certain sections of the Sarbanes-Oxley Act. Of particular interest are the increased cost arising from internal control and disclosure requirement of that act.

Keywords: *Sarbanes-Oxley Act, Securities regulation, Internal controls, financial reporting, securities litigation, Tort reform Act of 1995, White collar crime, accounting standards*

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12. ON THE OSCILLATING PRICE ELASTICITY

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ABSTRACT

The purpose of this paper is to expand the price elasticity theory developed by Greenhut, Hwang, and Ohta (1974) by including a general cost condition for a profit-maximizing monopolist, cartel, or price leader. The theory is more generalized than the conventional second-order condition as it includes nonconverging price elasticity. Due to structural changes and the income effect in crude oil and other markets, the price elasticity of demand is oscillating and is away from reaching its theoretical limit.

Keywords: *Price elasticity; crude oil market*

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13. THE PERFORMANCE OF TAXABLE BOND FUNDS RELATIVE TO BENCHMARKS AND PEER GROUPS

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ABSTRACT

Proponents of an all-index funds strategy of investing elucidate how investors are consistent losers (mediocre total returns) in the active versus passive investment management competition and debate. This research study uncovers evidence of outperformance by a subset of taxable bond mutual funds over multiple time periods and measured against various benchmarks. Since historical investment performance is not necessarily extrapolative, a blended approach is advocated as an appealing, discretionary option in constructing portfolios.

Keywords*: Mutual Funds, Bond Mutual Funds, Passive Investing, Active Investing*

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14. RISK-ADJUSTED VALUE INVESTMENTS

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ABSTRACT

This paper provides important investment implications for value investors. The value investment based on earnings yield (E/P) appears to be the most reliable regardless of performance measures and time periods. In making the value investment decisions, the impact of additional systematic risk factors on portfolio performance seems to be material. The business cycle is another important factor that influences the performance of the value investment. The value investment is more valuable than the growth during the contraction period, while the latter generates higher return than the former during the expansion period.

Keywords: *Value Investments; Traditional Performance Measures; Three-Factor Adjusted Performance Measure; Contraction Period; Expansion Period*

15. A CRITICAL EVALUATION ABOUT THE STOCK MESSAGE BOARD

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Feng-Shun (Leo) Bin, University of Illinois at Springfield, Springfield, Illinois, USA

ABSTRACT

As an important online source, message boards are widely used by stock investors to share investment information and knowledge. Information system users and investors have been researching various projects related to stock message boards from different perspectives. However, existing research of stock message boards is mainly descriptive. This study provides a prototype critical evaluation of the effectiveness of using a representative public stock message board to support course learning in business college program, therefore providing class students with an open learning-sharing environment.

Keywords: *Stock Message Boards, Knowledge Management; Collaborative Learning*

16. CHANGES IN CREDIT TERMS AND CLIENTELE EFFECTS ON THE CASH DISCOUNT RATE IN CREDIT POLICY

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ABSTRACT

Suppliers may be trading off among various credit terms or, alternatively, they may be simultaneously setting all the credit terms higher or lower to promote sales. In this paper we show that all major credit terms are established simultaneously higher or lower by a typical supplier. Secondly, an empirical investigation of clientele effects on the cash discount rate is presented. In this regard, we test whether the buyer's firm size, credit quality, variable product demand, utilization and demand for trade credit and cash discounts (all of which could proxy for the buyer's cash discount elasticity of demand) and the buyer's industry (which could proxy for the product price elasticity of demand) affect the size of the cash discount rate offered. Our empirical results show that financial managers take clientele effects into consideration when establishing trade credit policies.

Keywords: *cash discount, elasticity, trade credit*

17. AN EXAMINATION OF LONG-TERM WEALTH EFFECTS OF UNETHICAL BUSINESS BEHAVIOR

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D. Michael Long, University of Tennessee-Chattanooga, Chattanooga, TN, USA
Kathleen G. Long, University of Tennessee-Chattanooga, Chattanooga, TN, USA

ABSTRACT

This paper examines the long term wealth effects of firms' unethical conduct involving bribery, illegal payments, employee discrimination, environmental pollution, and insider trading. Firm performance is compared to industry performance over the 5-years before and 5+ years following the announcement of ethical violations. The results show no significant difference in performance before unethical behavior. However, there is a significant underperformance for firms after the announcement of ethical violations relative to their industry as a whole. This finding suggests that ethical business behavior is compatible with a firm's long term goal of shareholder wealth maximization.

Keywords: *Wealth effects, business ethics*

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18. IMPROVING JUDGMENTAL BUSINESS FORECASTS UNDER SEVERE ORGANIZATIONAL CONSTRAINTS

Matthew G. Nagler, Lehman College - City University of New York, Bronx, New York, USA

ABSTRACT

The paper offers a case study in business forecast improvement under conditions of limited data and resources. The practitioner's objective was to forecast annual revenue for a medium-sized company based on salespersons' judgmental predictions of success with respect to open sales opportunities. Unavailability of historic forecasts and matching actuals for revenue and its components rendered the standard optimal linear correction procedure for reducing forecast bias infeasible, while lack of organizational cooperation ruled out other popular techniques for forecast improvement, including Delphi and Estimate-Talk-Estimate. A feasible correction method using available data and based on behavioral analysis of the sales team and their prediction processes generated substantial improvement in forecast accuracy relative to no correction.

Keywords: *Judgmental Forecasts; Adjusting Forecasts; Bias; Behavioral Analysis; Organizational Behavior*

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19. DERIVATIVES AND MARKET VALUATION: AN EMPIRICAL INVESTIGATION OF THE IMPACT OF SFAS DISCLOSURE REQUIREMENTS

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ABSTRACT

This study examines the impact of incorporating information pertaining to derivatives on the market value of bank stocks. The explanatory power of the model formulated and used was expected to increase after such incorporation. The study finds that recent requirements for increased disclosures pertaining to off-balance sheet items could prove useful for investors/analysts, when information about derivatives is also considered. For a better understanding of the dependent variable (market value of bank stock), it is imperative that in the evaluation process, one must jointly considered information about both the independent on-balance sheet variables (book value of equity, net loan loss provisions, loan charge-offs, and the valuation portion of the *reserves for loan loss) and off-balance sheet financial instruments (derivative exposure), especially when such information is publicly available. It was found that at least at present and as modeled in this study, the market seems to be calmly and favorably viewing increased derivative exposures in large commercial banks in the United States. These findings should help future researchers to critically evaluate the implications of future disclosures of derivatives instruments which will be effective September 2006.*

Keywords: *Derivatives, banks, disclosure, off-balance sheet items*

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20. FUEL PRICE HEDGING IN THE AIRLINE INDUSTRY

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ABSTRACT

The cost of fuel represents the second highest operating expense airlines must contend with, second only to labor. Rising jet fuel prices over the past several years have put constant pressure on airlines to maintain positive cash flows and have pushed Delta airlines and Northwest airlines into bankruptcy. There is an ongoing discussion in the literature about the usefulness of hedging for nonfinancial firms like the airlines as well as the source of added value from hedging. Some argue that hedging is not a core competency of airlines and that as long as competitors are not hedged; it will be a level playing field. United, Northwest and ATA do not hedge at all, while other airlines are engaged in some limited hedging. In this paper we use recent data to test the model developed by Froot et. al. (1993) and Allayanis and Weston (2001) to test if hedging adds value to an airline.

Keywords: *Fuel Hedging, Airlines, Financial constraints, Derivatives*

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21. WEALTH EFFECTS OF WATER TRANSPORTATION INDUSTRY MERGERS AND ACQUISITIONS

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Rostyslav Pavlovskyy, Berislav Agro Industrial Company, Kherson, UKRAINE
Krishna G. Mantripragada, Ball State University, Muncie, Indiana USA

ABSTRACT

We study wealth effects of Water Transportation Industry Mergers and Acquisitions on the abnormal returns to merging/acquiring and merged/acquired firms of a sample of 35 and 5 events respectively for the shipping companies, listed on U.S. Stock Exchanges for the period 1995 – 2003. Daily Average Residuals (AVRs) obtained using the market model on the daily Center for Research in Security Prices (CRSP) data show that the stocks of merging/acquiring companies provide high and statistically significant AVRs on day +1 from the announcement day. Merged/acquired companies experience statistically significant negative AVRs on the announcement day. It implies that the market reacts to the merger or acquisition announcement in a way which decreases the shareholders' value of target firms in question. The results run counter to the near-unanimous findings from prior event studies. Cumulative Average Residuals (CARs) over selected intervals further confirm that shareholders of merging/acquiring firms experience positive wealth effects, while shareholders of merged/acquired firms, on the contrary, are negatively affected by the stock market reaction to the merger announcement.

Keywords: *Wealth Effects of Mergers, Maritime Industry Mergers, Water Transport Industry Merger Effects*

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22. THE CAUSALITY OF OIL PRICE SHOCKS TO CHANGES IN FISCAL AND MONETARY POLICY

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ABSTRACT

Fluctuations in oil prices impose on the U.S. economy enormous pressure and induce changes in productive resource allocation, modifications in consumer behavior, and reactions in terms of monetary and fiscal policy to attempt to mitigate potentially unwanted effects. However, changes in public policy typically manifest effects beyond their intended scope, and it is further not clear that policy changes successfully offset the effects of oil price fluctuations. This essay employs a series of vector autoregressive models to test the dynamic relations among oil prices, public policies and macroeconomic performance.

Keywords*: Oil Prices, Fiscal Policy, Monetary Policy, Economic Growth, Vector Autoregression*

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23. STOCK PRICING DISCOVERY – THE CASE OF THE DEAD DOG

Frank S. Smith, University of Central Arkansas, Conway, Arkansas, USA

ABSTRACT

This paper introduces a classroom game that provides practice using the concept of price discovery by allowing students to trade a fictitious stock where market and unique inside information are available. Five teams with detailed expertise are given area unique information to evaluate, along with overall "market" informational events. By varying the depth and usefulness of information, students can see how a stock price responds to differing information by the specific bidding parties. The impact of various backgrounds, from dog breeders to cancer researchers to waste disposal workers, allows for both specific informational price discovery as well as noise trading. This game can be conducted in a 50-minute class with no outside costs except for making copies of the rules and events.

Keywords*: Price Discovery, Teaching Game, Classroom Pedagogy*

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24. DETERMINANTS OF PRICE-EARNING RATIO

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ABSTRACT

Relative P/E-ratio valuation plays an important role among investment research analysts and advisors. The P/E ratio relates to the price paid to current earnings. Due to its simple computation for various stocks and also making comparisons between various stocks, it is widely accepted. The research question being addressed is to find out the determinants that differentiates P/E ratio of one company from the other in a specified time period and over a period of time. A P/E-ratio valuation model can be viewed as a technically simple model, using company's earnings as its value driver, and typically being dependent on having access to stock market data for comparable companies.

This analysis is concerned with the importance of differences, pertaining to valuation of relevant variables (measures of profitability and capital growth), between the companies. P/E ratio also acts as a proxy to risk and growth of a firm and is much likely to reflect market moods and perceptions.

Keywords: *Price Earning Ratio, payout ratio, beta, size of the company (Total Asset), growth, productivity ratio (Sales/Networth), net profit margin (NP/Sales)*

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25. SOCIAL SECURITY: WHAT IS IT REALLY, AND IS PRIVATIZATION A BETTER ALTERNATIVE?

Jason T. White, Northwest Missouri State University
J. Patrick McLaughlin, Northwest Missouri State University

ABSTRACT

Social Security is commonly referred to as the 'third rail' of American politics due to its popular support and venerability. Do we really need to privatize our Social Security system to make it "better?" We explain the historical reasons for the financial structure our current system of Social Security. We assert that the program is not meant to be a "replace-all" retirement income program, but rather a "safety-net" for persons who do not have, for whatever reason, any other way to provide retirement, disability or survivors income for themselves, and we study the issue of Social Security privatization.

Keywords: *Social Security, Privatization, Retirement, Trust Fund, Pay-as-you-go, Advance Funding*

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26. AN EXAMINATION OF MANAGERS' EFFORT ON PRODUCT QUALITY: AN EXPECTANCY THEORY PERSPECTIVE

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Karl, J. Wang, University of Mississippi, Oxford, MS, USA

ABSTRACT

This study is to examine the effects of economic incentive and performance measure responsiveness on managers' effort to improve product quality based on expectancy theory. The strategic control systems differ from traditional controls which focus on short-term, financial measures of performance. Strategic controls emphasize both financial and non-financial measures that support firms' mission. One strategic choice is the integration of quality improvement into the strategic plan. Unlike previous researches, this study uses expectancy theory to examine two aspects of strategic control systems (1) the use of performance-based incentives, (2) the responsiveness of performance measures to managers' efforts, and their influences on production managers' effects to improve quality. The results support the notion that appropriate performance measures and rewards for improvement of quality increase managers' efforts to achieve product quality goals.

Keywords: *Strategic Control Systems; Product Quality; Economic Incentive; Performance measure; Expectancy Theory*
