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Management Insights

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Financial Literacy, Financial Education, and Downstream Financial Behaviors (p. 1861)
Daniel Fernandes, John G. Lynch Jr., Richard G. Netemeyer

Does financial education pay? The financial environment that consumers face today has become dramatically more perilous in just one generation. Baby boomers witnessed during their working careers the advent of exotic mortgage forms, much-expanded credit availability, and new borrowing options such as payday loans and debt consolidation loans. They experienced fivefold increases in bankruptcies in the United States in the last 30 years. In the arena of retirement savings, defined benefit pensions of boomers' parents were replaced by defined contribution retirement systems, simplifying the balance sheets of employers but requiring employees to figure out how much to save, where to invest, and how to make lump-sum payouts last throughout retirement. Policy makers have embraced financial education as a necessary antidote to the increasing complexity of consumers' financial decisions over the last generation. The authors find that interventions to improve financial literacy explain only 0.1% of the variance in financial behaviors studied, with weaker effects in low-income people. Like other education, financial education decays over time; even large interventions with many hours of instruction have negligible effects on behavior 20 months or more from the time of intervention. The insight for management: Knowledge should be imparted only as needed; there is a real but narrower role for "just-in-time" financial education tied to the specific behaviors that it intends to help.

Volume Flexibility in Services: The Costs and Benefits of Flexible Labor Resources (p. 1884)
Saravanan Kesavan, Bradley R. Staats, Wendell Gilland

Does the flexibility of part-time and temporary workers result in improved financial performance? The last 40 years have seen significant changes in how jobs are structured. Although nontraditional labor structures have existed for some time, factors such as increased competition, higher uncertainty, and poor macroeconomic conditions have led to a significant rise in the use of alternative or flexible employment approaches such as part-time workers (permanent, but fewer hours compared to full time) and temporary workers (limited length of employment with variable time). Estimates on the prevalence of part-time and temporary workers find that more than 70% of U.S. organizations use part-time workers, whereas almost 40% use temporary workers, and that approximately 20% of U.S. workers are part-time workers. Organizations can create volume flexibility—the ability to increase capacity up or down to meet demand for a single service—through the use of flexible labor resources. The authors use two years of archival data from 445 stores of a large retailer to study this relationship. They find at low-to-middle concentration of flexible resources, revenues can improve and costs fall, but this pattern reverses for higher concentrations. The insight for management: Although flexible labor resources can create volume flexibility for a firm, it is possible to have too much of a good thing.

Retail Store Density and the Cost of Greenhouse Gas Emissions (p. 1907)
Gérard P. Cachon

What is the greenest configuration of a retail network? The density, size, and location of stores in a retailer's network influence both the retailer's and the consumers' costs. With stores few and far between, consumers must travel a long distance to shop, whereas the travel time is shorter with a dense network of stores. The layout of the retail supply chain is of interest to retailers who have emission reduction targets and to urban planners concerned with sprawl. Are small local shops preferred over large, "big-box" retailers? A model of the retail supply chain is presented that includes operating costs (such as fuel and rent for floor space) as well as a cost for environmental externalities associated with carbon emissions. A focus on exclusively minimizing operating costs may substantially increase emissions (by 67% in one scenario) relative to the minimum level of emissions. The insight for management: A price on carbon is an ineffective mechanism for reducing emissions. The most attractive option is to improve consumer fuel efficiency—doubling the fuel efficiency of cars reduces long-run emissions by approximately one-third, whereas an improvement in truck fuel efficiency has a marginal impact on total emissions.

Giving Feedback to Clients (p. 1926)
Teck-Hua Ho, Catherine Yeung

Is feedback valuable? In a situation with performance-based compensation, how honest is the feedback on services provided? The authors conduct experiments where a service provider does a task for a client, and only upon completion gets feedback on their performance. The service provider's pay is dependent on that feedback. The agent's earnings are proportional to the client's reported happiness, the agent inflates that feedback, and the client reports a higher level of happiness. The authors show that neither the agent nor the client behaves altruistically in their reporting. The client reports being happier because she overestimates her performance and mistakenly believes that the agent's feedback is genuine. The agent stops inflating his feedback when doing so no longer benefits him. The insight for management: An agent behaves opportunistically when providing feedback in order to inflate the client's overconfidence of her own performance.

The Long-Run Role of the Media: Evidence from Initial Public Offerings (p. 1945)
Laura Xiaolei Liu, Ann E. Sherman, Yong Zhang

What is the power of the press on initial public offerings (IPOs)? The unique characteristics of the U.S. IPO process, particularly the strict quiet period regulations, make it possible to explore the effects of media coverage when the coverage does not contain hard information that was previously unknown. The authors show that a simple, objective measure of pre-IPO media coverage is positively related to the stock's long-term value, liquidity, analyst coverage, and institutional investor ownership. They also find that pre-IPO media coverage is negatively related to future expected returns, measured by the implied cost of capital. The insight for management: Media coverage increases awareness of an IPO; if investors consider only stocks with which they have a certain level of familiarity, then having more investors paying attention to the stock effectively shifts out the demand curve for the stock. As a result, stocks that receive more attention should have a higher initial valuation and a resulting lower rate of return.

Compensation and Peer Effects in Competing Sales Teams (p. 1965)
Tat Y. Chan, Jia Li, Lamar Pierce

How do compensation plans affect peer performance among collocated sales teams? The authors use department store sales data to show that compensation systems influence worker incentives to compete with peers within the same firm, which in turn changes the capability of the firm to compete with rivals. Compensation also affects how salespeople impact peers at collocated competing firms, thereby impacting market competition. Moreover, compensation influences how salespeople strategically discount prices in response to peers. The insight for management: Heterogeneity in worker ability enhances firm performance under team-based compensation while hurting individual-based firms; peer interactions are critical considerations in designing sales force incentive plans and broader firm strategy.

Differences in Trading and Pricing Between Stock and Index Options (p. 1985)
Michael Lemmon, Sophie Xiaoyan Ni

Are there differences in trading and pricing between stock and index options? There are differences in the composition of traders with different types of options: Options on stocks are actively traded by individual investors, whereas trades in index options are more often motivated by the hedging demand of sophisticated investors. As it turns out, the individual investor sentiments and past market returns are related to time-series variations in the slope of the implied volatility smile of stock options, but they have little impact on the prices of index options. The pricing impact is more pronounced in options with a higher concentration of unsophisticated investors and those with higher delta hedging costs. The insight for management: The demand for stock options that increases exposure to the underlying stock is positively related to the individual investor sentiments and past market returns, whereas the demand for index options is invariant to these factors.

Balancing Acquisition and Retention Spending for Firms with Limited Capacity (p. 2002)
Anton Ovchinnikov, Béatrice Boulu-Reshef, Phillip E. Pfeifer

How do revenue management and customer relationship management interact in a firm that is concerned with customer retention but faces limited capacity? The authors describe how the firm balances investments in customer acquisition and retention across multiple customer types. They characterize the optimal policy and discuss how the policy changes depending on capacity limitations. They introduce the concept of the value of an incremental customer (VIC), and they show that when capacity is unlimited, VIC equals customer lifetime value (CLV), but when capacity is limited, VIC is much smaller and changes dynamically depending on the number of customers and their mix. As a result, the optimal spending is constant and depends on CLV for the firms with unlimited capacity, but it changes dynamically and is generally unrelated to CLV when capacity is limited. Interestingly, in experiments the authors find some biases in individual behaviors that do not align with optimal behavior. The insight for management: Providing CLV information exacerbates these biases and leads to a loss of net revenue when capacity is limited, but providing information about the marginal costs of acquisition and retention eliminates these biases and increases net revenue.

Crowdsourcing with All-Pay Auctions: A Field Experiment on Taskcn (p. 2020)
Tracy Xiao Liu, Jiang Yang, Lada A. Adamic, Yan Chen

How do crowdsourcing and all-pay auctions interact? Crowdsourcing is the open solicitation of effort on a well-defined task to a community (crowd) to obtain a submitted solution before a deadline. Crowdsoucing has become an increasingly popular choice for tasks such as translation, programming, website design, and open innovation. In an all-pay auction everyone expends effort, but only the winner receives a reward. To explore the effects of different incentives on crowdsourcing participation and submission quality, the authors conduct a randomized field experiment on Taskcn, a large Chinese crowdsourcing site using mechanisms with features of an all-pay auction. In the study, they systematically vary the size of the reward as well as the presence of a soft reserve, or early high-quality submission. The insight for management: A higher reward induces significantly more submissions and submissions of higher quality, but high-quality users are significantly less likely to enter tasks where a high-quality solution has already been submitted, resulting in lower overall quality in subsequent submissions in such soft reserve treatments.

Information Content When Mutual Funds Deviate from Benchmarks (p. 2038)
Hao Jiang, Marno Verbeek, Yu Wang

How does the weighting of stocks in funds affect stock performance? The consensus wisdom of active mutual fund managers, as reflected in their average over- and underweighting decisions, contains valuable information about future stock returns. Analyzing a comprehensive sample of active U.S. equity funds from 1984 to 2008, the authors find that stocks heavily overweighted by active funds outperform their underweighted counterparts by more than 7% per year, after adjustments for their loadings on the market, size, value, and momentum factors. However, this large premium dissipates quickly as the consensus view becomes publicly available. In addition, active mutual funds invest only a small portion of fund assets in high alpha stocks, in accordance with the consensus view that active mutual funds on average fail to outperform passive benchmarks. The insight for management: Overweighted stocks outperform their counterparts until such information becomes publicly available.

Money Talks: Rebate Mechanisms in Reputation System Design (p. 2054)
Lingfang (Ivy) Li, Erte Xiao

Put your money where your mouth is; how does remuneration for feedback affect the efficiency of information? Reputation systems that rely on voluntary feedback from traders are important in creating and sustaining trust in markets. Feedback nevertheless is a public good, and providing it is often costly. The authors study the effect of a seller precommitment mechanism: Sellers have an option to commit by providing a rebate to reduce the buyer's feedback reporting cost before making purchasing decisions. The authors find that the seller's rebate decision has a significant impact on the buyer's purchasing decision via signaling the seller's cooperative type. More importantly, market efficiency under the precommitment mechanism increases with the probability that sellers will provide a rebate. The insight for management: Compared with the no rebate mechanism market, more efficient trades can be achieved when the sellers offer a rebate to the buyers in the market with the rebate mechanism, even when the rebate does not cover the full cost of feedback reporting.

Firm-Level Productivity, Risk, and Return (p. 2073)
Ayşe İmrohoroğlu, Şelale Tüzel

What is the link between firm-level total factor productivity (TFP) and stock returns? The authors estimate firm-level TFP and show that it is strongly related to several firm characteristics such as size, the book-to-market ratio, investment, and hiring rate. Low-productivity firms earn a significant premium over high-productivity firms in the following year, and this premium is countercyclical. The authors show that a production-based asset pricing model calibrated to match the cross section of measured firm-level TFPs can replicate the empirical relationship among TFP, many firm characteristics, and stock returns. The insight for management: The results offer an explanation as to how these firm characteristics rationally predict returns.

Timing Ability of Government Bond Fund Managers: Evidence from Portfolio Holdings (p. 2091)
Jing-Zhi Huang, Ying Wang

What is the evidence surrounding the ability of government bond fund managers? The authors study the ability of government bond fund managers to time the bond market, based on their monthly or quarterly holdings of Treasury securities during the 1997–2006 period. They find that, on average, government bond funds exhibit significantly positive timing ability at the one-month horizon under an unconditional holdings-based timing measure. However, their results indicate that managers' actions based on public information can explain the documented positive timing ability—namely, the average government bond fund has neutral or even slightly negative conditional market timing ability once public information is controlled for. The insight for management: There is evidence that fund managers specializing in treasury securities can better interpret public information than can general government bond fund managers.