The New York Times ON THE WEB

Wednesday, March 25, 2009
Visitors per Month: 15,086,201
http://economix.blogs.nytimes.com/2009/03/25/dont-blame-us/

Economix

Explaining the Science of Everyday Life

Don’t Blame Us

BY CATHERINE RAMPELL

The media — especially as embodied by Jim Cramer — has been accused of starting, perpetuating or inflating bubbles. A new study looks at the dotcom bubble of the late 1990s and declares otherwise.

The study — by Utpal Bhattacharya, Neal Galpin, Rina Ray and Xiaoyun Yu — is forthcoming from the Journal of Financial and Quantitative Analysis. In the study, the authors examined news articles released from 1996 to 2000 on 458 Internet initial public offerings and 458 non-Internet public offerings. Each of the 171,488 relevant news items was classified as good news, neutral news or bad news.

Not surprisingly, the news coverage of dotcom initial offerings was more positive than that of non-dotcom initial offerings during the bubble, and more negative compared to non-Internet counterparts during the bust. The paper finds, though, that the actual effect this coverage had on stock prices was tiny after the first couple days:

After controlling for lagged abnormal returns, market capitalization, contemporary market trading conditions, and contemporary and past news, we find that net news today is positively related to today’s and tomorrow’s risk-adjusted returns. However, the net news effect dies out after these two trading days for both Internet and non-Internet I.P.O.s. We find that the effect of today’s net news on today’s risk-adjusted return is lower for Internet I.P.O.s than for non-Internet I.P.O.s during both the bubble and post-bubble periods. The effect of today’s net news on tomorrow’s risk-adjusted return is also lower for internet I.P.O.s, especially during the bubble period. In addition, since net news on average is positive during the bubble period and is negative post-bubble, this implies today’s good (bad) news matters less for today’s and tomorrow’s risk-adjusted returns for Internet I.P.O.s during the bubble (post-bubble) period. Our results are robust to whether we risk-adjust individual stocks, or whether we risk-adjust a portfolio consisting of either Internet or non-Internet stocks.

In the end, the authors say:

[M]edia coverage was not a significant factor in the Internet bubble. The media explains only 2.9% of the difference in between Internet and non-Internet firm returns from January 1, 1997 to March 24, 2000 (the day the Nasdaq peaked). This is because the market downplayed media sentiment: though today's net news affected today's and tomorrow's risk-adjusted returns for both groups of I.P.O.s, the effect was lower for Internet I.P.O.s, especially in the bubble period.

O.K., this doesn't totally let the media off the hook — especially since the research looked only at news coverage of I.P.O.'s, not stories about the wisdom of investing in dotcoms in general. But it's still an interesting complement to the debate about how much responsibility (or blame) journalists should take for "irrational exuberance" directed toward dotcoms, housing or anything else: Yes, the media basically behaved badly, but its bad behavior did not appear to have much influence.

Find the citation and abstract here, and an ungated earlier draft of the paper here.