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The Effect of Financial Ratios and Market Hype on Short Term Stock Prices

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Oral Presentation O6.2

THE EFFECT OF FINANCIAL RATIOS AND MARKET HYPE ON SHORT TERM STOCK PRICES

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This paper considers possible sources of short term changes in stock price. By predicting these changes, analysts can learn about the forces that drive the stock market enabling investors to earn greater returns. Studies conducted throughout the twentieth century have provided a conclusive basis for stock market analysis. The concept behind these studies is the use of intrinsic ratios to determine a change in stock price. Unfortunately, few studies have produced truly relevant results. This failure led to the introduction of a new variable into stock market analysis: hype. Hype consists of non-market factors that can affect the price of a stock. This paper makes use of financial ratios and market hype to predict changes in stock price. More specifically, this paper uses the dividend payout ratio, operating cash flow per share, earnings per share, equity per share, and analyst upgrades as indicators of changes in stock price. All of the variables are taken from the quarter immediately prior to the quarter over which the stock price was measured. Those various data are then broken down by industry in an attempt to determine how the ratios affect particular industry sectors. The results show that investors rely primarily on prior earnings information about a company when making their current period investment decisions. Furthermore, retail and restaurant stocks tend to under perform the market as a whole while hype has a significantly positive effect on the financial service and communications sectors. With these significant results, much can be learned about the predictive nature of financial ratios and market hype.