

Do Jim Cramer's *Mad Money* Recommendations Have the Same Impact in a Bear Market as in a Bull Market?

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Abstract

Many empirical studies of investment advisory services find statistically significant abnormal returns at the time of their public availability. Jim Cramer's *Mad Money* recommendations are one example of investment advice that has been studied in the recent past. This study is an extension of Neumann and Kenny's (2007) work published earlier concerning Jim Cramer's *Mad Money* stock picks. Earlier Neumann and Kenny (2007) found market reactions to Jim Cramer's stock recommendations using 2005 data. In this study, Jim Cramer's recommendations are examined again but utilizing more recent data occurring during a bear market rather than the previous examinations during bull markets. Specifically, this research questions whether viewers continue to follow Jim Cramer's *Mad Money* stock suggestions in a bear market and whether the mentioned stocks still experience significant abnormal returns during part of the bear market of 2008. The analysis of stock returns and trading volume reveals statistical evidence of response to his buy recommendations.

I. Introduction

Today there is a proliferation of investment advice available to novice investors. Televised programs and internet sites are readily available to investors as sources of information on which to make investment selections. The question becomes which sources, if any, can provide useful information to investors. It is of interest to study these sources of information to determine whether investors are using the information and how reliable and useful the information. This allows an examination of the impact on asset prices, the existence of market volatility, and the efficiency of the market.

In this study, the stock buy recommendations made by Jim Cramer on his nightly CNBC *Mad Money* program are analyzed. Mr. Cramer's show is unlike other programs and comes into question as to whether it is for entertainment or news. Serwer (1998) has described him as "a man who blurs the line between creating business news and covering it." When Mr. Cramer first began his *Mad Money* show after a market bubble burst, he stated his show would "help people avoid the kind of misguided bets that left them with worthless stock" (Gasparino, 2005). He indicated *Mad Money* would "be looking out for people by beating the system" (Gasparino, 2005). Apt (2009) notes that Mr. Cramer's *Mad Money* program has become the most widely watched broadcast for CNBC with 380,000 viewers and that websites are devoted entirely to discussions of his selections.

Several studies have analyzed investment advice from various media. Beginning with print media, there are many publications available today from which investors seek investment advice. Ho and Harris (1998) find significant abnormal returns in their event windows around brokerage stock rating reports, with downgrades prompting stronger reactions than upgrades. In studies of newspaper or magazine columns, Mathur and Waheed (1995) find significant abnormal returns and trading volume in event periods around recommendations contained in the "Inside Wall Street" column from *BusinessWeek*. Several authors who look at "Heard on the Street" in the *Wall Street Journal* find significant market reactions around the day of publication,

including Liu, Smith, and Syed (1990), Beneish (1991), Liu, Smith, and Syed (1992), Bauman, Datta, and Iskandar-Datta (1995), and Sarkar and Jordan (2000). The *Wall Street Journal's* previously conducted dartboard contests also produced abnormal returns on announcement days exceeding 3% as documented by Pruitt, Van Ness and Van Ness (2000), Albert and Smaby (1996), Metcalf and Malkiel (1994), and Barber and Loeffler (1993). Most of this abnormal return was seen at the market's opening prices after the dartboard column had been printed in the morning editions.

There have also been several studies analyzing advice from television and internet media, the same outlets for Mr. Cramer's recommendations. Hirschey, Richardson, and Scholz (2000) use 21 "foolish" buy recommendations to detect significant positive abnormal returns and volume on the day after the buy announcements were made. The conclusions in Dewally (2003) contradict this internet finding in observing no information passage through the newsgroup sites and no perceptible stock market reaction to the recommendations posted to them. Research into recommendations made during weekly broadcasts of Louis Rukeyser's *Wall Street Week* generally document stronger reactions to buy recommendations than sells with buy recommendations eliciting positive price and volume reactions (Beltz and Jennings, 1997; Pari, 1987; Griffin, Jones and Zmijewski, 1995).

More recent research has included examinations of Mr. Cramer and his *Mad Money* recommendations. Karniouchina, Moore and Cooney (2009) examined *Mad Money* from a marketing perspective. The 2009 study used buy recommendations during the time period November 2005 through July 2007. Although their article focused on the communication being employed by Jim Cramer in *Mad Money* being similar to advertising, they utilized event study methodology in other *Mad Money* studies and found buy recommendations resulted in significant abnormal returns of .50% on the day following the recommendation. They also find evidence of investors learning over time with tracking the success of Jim Cramer's performance on recommending the same stocks.

Bolster and Trahan (2009) examined Cramer's recommendations on *Mad Money*. Their event study incorporated data from July 2005 through December 2007. Abnormal positive returns for buy recommendations were found on average of 1.94% for day 1 after the recommendation was made. They examined the time period prior to the recommendations and suggest Cramer recommends stocks to buy that already have "momentum." Results for sell recommendations were found to be significant as well with an abnormal return on average of -0.71%. Further analysis beyond the event study which incorporated risk found Cramer's recommendations, however, have a zero alpha.

Lim and Rosario (2008) found abnormal returns for the recommendations suggested by Jim Cramer on the day after his picks. In their examination of recommendations from June 2005 to December 2006, the authors found Cramer recommends stocks which already have a positive momentum. His recommendations for small-capitalization stocks were found to be more accurate generating longer-term (six month) positive returns.

Engelberg, Sasseville, and Williams (2007) also looked at Cramer's buy recommendations. Their research using buy recommendations between November 16, 2005 and

June 23, 2006 found the recommended buy stocks experienced a price increase of 2.86% on average on the day after their recommendation.

The research that this paper extends is from Neumann and Kenny (2007). Neumann and Kenny found buy recommendations by Jim Cramer during July through September 2005 resulted in statistically significant abnormal and raw returns, as well as trading volume increases, on both the day 0 air dates of buy recommendations and the day +1 trading day, with the day +1 effects being stronger as expected. Almost all of the average raw return on day +1 is captured in the difference between the day 0 close price and the day +1 opening price. They also documented evidence that their smaller sample of the show's sell recommendations coincided with negative abnormal returns and trading volume increases in the (0,+1) event window. Finally, their study analyzed the short-term impacts around *Mad Money* recommendations. While their results showed that short-sale portfolios based on *Mad Money* buy recommendations produced risk and mean-adjusted abnormal returns over a nearly one-month horizon after the positions were established, these returns were only available to professional investors with enough capital to establish and maintain the simultaneous day-specific portfolios. Their results send a message to individual investors with limited capital to be cautious about short-term trading on *Mad Money* recommendations. Not only has the price of recommended buy stocks already moved by the next day's open, but they show that strategies aimed at exploiting next day price moves are not profitable in the aggregate.

The previous research concerning Mr. Cramer's *Mad Money* recommendations has all utilized data during bull market trends. This paper looks at Mr. Cramer's selections during a bear market trend to see whether similar impacts are seen for his buy recommendations.

II. Data and Methodology

Mad Money stock recommendations covering shows aired nightly between September 2008 through December 2008 were obtained from TheStreet.com. During the pre-production phase of *Mad Money*, Mr. Cramer selects which stock he will discuss during the evening's show. Only those firms that Mr. Cramer selected were originally considered for inclusion in the study. The firms suggested by viewer call-in are not included.

During the three months under consideration, Mr. Cramer made 187 recommendations on self-selected stocks. Companies which were mentioned more than once were taken out of the sample. This left 126 companies which were recommended once for which a total of 106 were buy recommendations and 20 were sell. Mr. Cramer suggests selling stocks on which he previously has made a buy recommendation. The sell recommendations were not considered in this study, consistent with Karniouchina, Moore and Cooney (2009). Additionally, in Neumann and Kenny (2007) results were not as significant for sell recommendations. From this group of 126 buy recommendations, 20 were randomly selected to be included in this study.

The companies included in the study shared some similar characteristics. Sixteen of the twenty companies are listed on the New York Stock Exchange. The other four stocks are NASDAQ stocks. Two firms did not have market capitalization data but of the other eighteen, only five had market capitalizations less than one billion dollars. The average market capitalization for the eighteen firms for which there was data was \$31.03 billion. The full list of

the sample of 20 firms is given in Table I.

The standard event study methodology outlined by Brown and Warner (1980, 1985) and used by many of the studies cited previously is used. Opening prices, closing prices and volume data for the sample are taken from www.financeyahoo.com. The daily returns were calculated using closing prices (P):

$$R_{i,t} = \frac{P_t - P_{t-1}}{P_{t-1}}$$

Event day 0 is the date of airing of a show. Since *Mad Money* is initially televised in the evenings at 6pm (Eastern time), it is expected to see any reaction to a particular show on event day +1. In Neumann and Kenny (2007) abnormal returns were determined in three ways, relative to a market model prediction, to the CRSP value-weighted index, and to a stock's recent historical mean. The results were not significantly different using the three approaches, so this study uses only the stock's recent historical mean to calculate the abnormal returns. The abnormal return is then:

$$AR_{i,eventday(t)} = R_{i,t} - \bar{R}_i.$$

Stock return means are estimated using daily returns from six months preceding the event.

The difference between the closing price on the day of a recommendation and the following day's open price is calculated: $Open P_1 - Close P_0$. In Neumann and Kenny (2007), it was found that most of the abnormal return for event day one was captured in the close to open price difference. The average of this price differential is calculated for the six months prior to the event day. The abnormal price difference is then determined by: $(Open P_1 - Close P_0) - \text{Average of } (Open P_1 - Close P_0)$.

The abnormal volume was examined last. In Neumann and Kenny (2007), it was found that abnormal trading volume occurred at the event. The average volume was calculated for the month preceding the event. The abnormal volume is then determined by: $Volume_t - \text{one month average volume preceding event}$.

III. Results

Tables II and III report results of the event analysis of the *Mad Money* buy recommendations becoming public. As shown in table II, there is evidence at the 3% confidence level that these returns are significantly different from zero during the first trading day after a buy recommendation has aired. The raw return on day +1 is 2.62%. The results also document a positive mean-adjusted abnormal return of 2.84% which is statistically significant at the 2% level. Comparing this to the results obtained by Neumann and Kenny (2007) during a bull market, the results are similar. In the current study during a bear market, the difference is that day zero does not have statistically significant raw or mean-adjusted abnormal returns.

The average open price₁ – close price₀ is \$0.51 for the buy recommended stocks. When the mean-adjusted abnormal price change was calculated, the average value was found to be

\$0.46 indicating the opening price on event day +1 compared to day 0’s closing price was \$0.46 higher than would be expected based on the prior month’s average. This value is statistically significant at the .56% level.

Table IV present results of abnormal trading volume using the same estimation period parameters and benchmarks we employed in analyzing event day returns. As seen in the table, the average abnormal trading volume is significantly greater on day +1. This value is statistically significant at the 4% level. This result is consistent with the findings in the bull market study.

IV. Conclusion

The evidence presented here suggests that the stock recommended by Mr. Cramer as “buys” during *Mad Money* do experience price and volume changes after his recommendation. The results of this study during a bear market are consistent with those found during a bull market. There are statistically significant abnormal and raw returns, as well as trading volume increases on day +1 trading day. However, since almost all of the average raw return on day +1 is captured in the difference between the day 0 close price and the day +1 opening price, a change likely induced by the weight of pending buy orders placed before the market opens, the average investor is likely unable to benefit from this effect and, further, the aggregate impact is to increase the cost of acting on these recommendations for all investors. The price of recommended buy stocks has already moved by the next day’s open. As time passes, subsequent research can examine the long-term performance of stocks recommended through this venue.

Table I: Sample of “Mad Money” Stock Buy Recommendations

Company	Market	Market Cap
Clean Energy Fuels	NASDAQ	\$ 1,230,000,000
BB&T Corporation	NYSE	\$ 22,000,000,000
Darden Restaurants Inc	NYSE	\$ 6,100,000,000
Boeing Company	NYSE	\$ 51,410,000,000
Ethan Allen Interiors	NYSE	\$ 579,190,000
McCormick & Co.	NYSE	\$ 5,170,000,000
Lender Processing Services	NYSE	\$ 3,910,000,000
KBR Inc. Common Stock	NYSE	\$ 3,450,000,000
Family Dollar Stores	NYSE	\$ 4,960,000,000
Pepsico Inc.	NYSE	\$ 104,490,000,000
Archer Daniels Midland	NYSE	\$ 18,690,000,000
Advanced Micro Devices	NYSE	\$ 6,120,000,000
Hewlett-Packard	NYSE	\$ 123,090,000,000
Atlas Pipeline Partners	NYSE	\$ 691,610,000
Salesforce.com Inc	NYSE	\$ 9,670,000,000
Owens Corning Inc	NYSE	N/A
Fortune Brands Inc	NYSE	\$ 7,430,000,000
Great Plains Energy	NYSE	\$ 2,570,000,000
Wisconsin Energy Corp.	NYSE	\$ 591,000,000,000
Costco Wholesale Corp/	NASDAQ	\$ 26,700,000,000
Schering Plough corp.	NYSE	N/A
Hovnanian Enterprises	NYSE	\$ 346,490,000
Legg Mason	NYSE	\$ 4,780,000,000
Rockwell Collins	NYSE	\$ 9,900,000,000
Goodrich Corp.	NYSE	\$ 8,940,000,000
Hexcel Corp.	NYSE	\$ 1,350,000,000
Precision Castparts	NYSE	\$ 17,250,000,000
Sprit Aero Systems Holding	NYSE	\$ 3,150,000,000
Alamo Group	NYSE	\$ 218,480,000
Petsmart	NASDAQ	\$ 3,720,000,000
Hartford Financial Services	NYSE	\$ 10,470,000,000
Lincoln National Corp.	NYSE	\$ 8,690,000,000
Principal Financial group	NYSE	\$ 8,750,000,000
Prudential Financial	NYSE	\$ 26,950,000,000
DCP Midstream Partners	NYSE	\$ 1,110,000,000
Williams Pipeline Partners	NYSE	\$ 696,750,000
Broad.com Corp.	NASDAQ	\$ 16,690,000,000
National Semiconductor	NYSE	\$ 3,460,000,000
Texas instruments	NYSE	\$ 30,250,000,000
E.I du Pont de Nemours	NYSE	\$ 33,320,000,000

Table II: Raw Returns for “Mad Money” BUY Recommendations. Event day 0 is the show air date and event day +1 is the next trading day. Figures in parentheses are t scores. * is significant at 2.6% level.

Event Day(s)	Raw Returns
-1	1.94% (1.553)
0	-1.18% (-.9837)
1	2.62% (2.0765*)
2	1.02% (1.2259)
3	-.11% (-0.0881)

Table III: Mean-Adjusted Abnormal Returns for “Mad Money” BUY Recommendations. Event day 0 is the show air date and event day +1 is the next trading day. Figures in parentheses are t scores. ** is significant at 1.97% level.

Event Day(s)	Mean-Adjusted Abnormal Returns
0	-.96% (-.8169)
1	2.84% (2.2117**)
2	1.25% (1.4783)
3	0.11% (.0947)

Table IV: Abnormal Volume Means for “Mad Money” BUY recommendations. Event day 0 is the show air date and event day +1 is the next trading day. Figures in parentheses are t scores. *** indicates significance at the 3.92% level.

	Abnormal Volume Mean
Day 0	343,149 shares (.5549)
Day +1	1,874,214 shares (1.8601***)
Day +2	1,037,579 shares (1.4018)
Day +3	842,014 shares (1.0541)
Day +4	492,529 shares (.5884)

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