

> Thursday, October 27th, 2022

14:30 - 16:00

ACCOUNTING



EMPOWERING CHANGEMAKERS FOR A BETTER SOCIETY

‘THE MANAGERIAL PERCEPTION OF UNCERTAINTY AND COST ELASTICITY’ BY REUVEN LEHAVY – MICHIGAN STATE UNIVERSITY



ABSTRACT

Extensive theoretical research demonstrates the important role of uncertainty in shaping a firm’s cost elasticity. We contribute to this literature by analyzing the inherent tension between the effects of uncertainty about unit contribution margin (CM) and volume on cost elasticity. First, we use the occurrence of words implying uncertainty in forward-looking statements in the Management Discussion and Analysis section of 10-K filings to measure managerial perceptions of overall, unit CM, and volume uncertainty. Doing so, we find a significantly positive (negative) association between the uncertainty about unit CM (volume) and cost elasticity. Examining these results further, we find the negative association between volume uncertainty and cost elasticity remains negative for manufacturing firms but turns positive for firms in the healthcare sector. We further find a significant negative relation between volume uncertainty and cost elasticity for firms with work-in-process inventory, low financial risk, or unconcentrated industry affiliation. Our empirical evidence supports the theoretical argument that managerial perceptions of uncertainty and its components influence resource allocation decisions, and suggests that any analysis of the relation between uncertainty and a firm’s cost elasticity should specify the type of uncertainty as well as the firm and industry characteristics.