Touro College Accounting and Business Society Journal

Spring 2002

Aaron Twersky, President

Rachel Spitezki, Vice President

Zev Brachfeld, Editor-in-Chief

Table Of Contents

Foreword by the Dean of Students

Dean Robert Goldschmidt 4

Foreword by the Dean of Undergraduate Business

Dean Barry Bressler 5

Foreword by the President of the TAB Society

Aaron Twersky 6

British Financial Markets

By: Marian Klein 8

How Color Affects Marketing

By: Channa Leichtling 22

Strategies in Options Trading

By: Sarah Karfunkel 32

Economic Perspectives on Affirmative Action

By: Dena Stern 40

Innovative Marketing Tools

By: Sheldon Abraham 48

The Federal Reserve System

By: Rachel Spitezki 63

The Knowing-Doing Gap

By: Aaron Twersky 74

The Ins and Outs of a Marketing Plan

By: Chaya Brook 83

The United States Currency and Its Financial System

By: Ester Weiss 100

Getting Technical

By: Zev Brachfeld 108

Introduction to Options

By: Joel Bodner 117

Income Inequality and Its Repercussions for Us

By: Rochie Saks 130

Microsoft: An Economic Analysis

By: Chana Grossberger 141

The Financial Outlook for the United States and the World at Large

By: Fraidy Zelmanovicz 160

Culture and Ethnicity in Consumer Decision Making

By: Yitzie Pretter 167

TOURO COLLEGE

Office of the Dean of Students

1602 Avenue J
Brooklyn, N.Y. 11230
(718) 252-7800, Ext. 234
Fax: (718) 253-9455

Manhattan Office:
27-33 West 23rd Street
New York, N.Y. 10010-4202
Tel (212) 463-0400 Ext. 419

From the Desk of the Dean of Students

Our philosophy at Touro College always has been to encourage students to excel in their academic pursuits and to motivate them to broaden their educational experiences beyond the confines of the typical classroom. Under the guidance of a spirited cohort of student leaders, academic societies and clubs have developed and grown, covering such fields as business, computer science, the natural sciences, political science and speech language pathology.

The Spring 2002 ***Touro College Accounting and Business Society Journal*** presents a wide spectrum of student scholarly articles, selected from an initial pool of more than three-dozen submissions. The TAB Journal, sponsored by the largest and oldest student organization at the college's Flatbush Campus, provides a wonderful opportunity for students to hone their research and writing skills as they prepare for graduate school and professional careers.

It is appropriate to recognize the student leaders whose initiative, determination and hard work have been instrumental in producing the Spring 2002 edition of The TAB Journal. Aaron Twersky, an economics major, President of the Touro College Accounting and Business Society, worked tirelessly over the past several months to bring the journal to fruition. He was ably assisted by Zev Brachfeld (Flatbush Men's Division), Editor-in-Chief, and Rachel Spitezki (Flatbush Women's Division), Vice President of the TAB Society.

I congratulate the students whose articles have been published in this journal. I encourage you to continue developing your talents. Remember, as you enter the world of business, that individual achievement must be coupled with community service.

Finally, I wish to express my appreciation to President Bernard Lander and the Board of Trustees for encouraging and supporting the publication of student scholarly journals.

Sincerely Yours,

Robert Goldschmidt

Dean Robert Goldschmidt
February 2002

TOURO COLLEGE

Barry Bressler, Ph.D.
Dean, Business School

1602 Avenue J
Brooklyn, N.Y. 11230
(718) 252-7800
Fax: (718) 253-9455

From the Desk of the Dean of the Business School

Much attention has been given in recent years to the assessment of the educational process. How can we be assured that students who complete the requirements of an academic program have received quality training and superior preparation for their future career? One of the most convincing ways of establishing quality outcomes is for students to demonstrate that they can take the theories, principles and techniques which have been taught to them and apply them to diverse real life applications.

It is particularly gratifying therefore to see students of the Touro Business School produce a journal which contains high quality papers in the broad fields of business, i.e., accounting, finance, management, marketing, economics and management information systems. The scope of the topics is impressive ranging from financial markets and options trading to marketing strategies, management actions, and economics of the Microsoft case and analysis of affirmative action policies. Even more significant is the fact that the student authors did not simply restate principles, theories and facts that they were required to master in the courses they took. They demonstrated that they could apply the theories to a myriad of applied topics, problems and issues.

I want to commend the members of the Touro College Accounting and Business Society (TAB) in general and the authors of these articles in particular. They all have bright futures ahead of them. We are especially indebted to those who in addition to their scholarly skills exhibited leadership and were able to see the project through. These include Aaron Twersky, Zev Brachfeld and Rachel Spitezki. Their unwavering dedication and professional work is noted and will stand them in good stead. We expect to see great things from them in the years to come.

Sincerely Yours,

Barry Bressler, Ph.D.
Dean, Business School

From the Desk of the President of the Touro College Accounting and Business Society

I am pleased to present the Touro College Accounting and Business Society Journal for the spring 2002 semester. The TAB Society (as it is identified throughout college) is the largest and most prominent society among student organizations in Touro College. Its membership consists of students majoring in accounting, business administration, economics, finance, management, and marketing.

The TAB Journal represents one of the many activities initiated by the TAB Society, which strives to serve the campus and the community as a preeminent business intellectual resource, both in and out of the classroom. Through appealing academic courses and dynamic extra curricular activities – lectures, publications, and conferences – the society provides an invaluable forum in which to engage in business issues and civilization.

This journal is presented to you by the junior and senior class of students majoring in the fields mentioned above. Featuring the research and arduous labor of those students involved in the publication of this journal, the fruits of their labor result in a wonderfully diverse and compelling collection of first-rate academic articles and opinion pieces sure to please readers of all backgrounds, levels, and interests. Topics that include the Federal Reserve System and an economic analysis of Microsoft, to technical analysis, options trading, and the economic effects of Affirmative Action.

I would certainly be amiss if I neglected to acknowledge the efforts of several individuals to whom I profess great appreciation.

Firstly, I would like to thank my Vice President, Rachel Spitezki, and Editor-in-Chief, Zev Brachfeld, for their dedication and enthusiasm on behalf of the society and its journal. They solicited submissions, selected items for inclusion, edited the material, and did all the work necessary leading to a camera-ready copy for the printer. Thank you for your precision and diligence.

Secondly, I would like to thank, on behalf of the entire student body, all the professors and instructors of the Touro College Business Department. It was only through their well prepared lectures and lessons that we have been able to come to the point at which we stand today.

Lastly, I would like to thank our Dean of Students, Robert Goldschmidt, and Dean of Undergraduate Business, Barry Bressler, for their undivided attention and devotion in allowing the TAB Society to accomplish its goals and objectives. Their consideration and constant support and advice to the society mirror their boundless dedication to each and every student at Touro College.

Enjoy the Spring 2002 edition of the Touro College Accounting and Business Society Journal.

Sincerely,
Aaron Twersky
President, Touro College
Accounting and Business Society
February 2002

British Financial Markets

By: Marian Klein

Although much is known and published about financial markets in the United States, investors know and understand less about overseas markets. Numerous financial markets, similar to those in the United States, exist in foreign countries. Although many of these markets tend to be relatively small and insignificant, some markets, like those in the United Kingdom, are perhaps as influential as their equivalent American markets.

For centuries, London has been celebrated as an international financial center. Despite Britain's weakened economic and political strength since the 1940's (Baughn 4), it still continues to be an influential and powerful financial market. This is mostly due to its unrivaled variety of services and degree of financial expertise. In this article, I will present four financial markets in the United Kingdom and will explain the framework, procedures, and regulations in those markets as well as the similarities and differences between these markets and those in the United States.

Equity Market

There are two main kinds of equity: preference shares and ordinary shares. Preference shares bear a fixed rate of interest, and some, called participating preference shares, also receive a fluctuating amount of the profits of the company. The shares have a preference over the ordinary shares in that the interest on them must be distributed first before any dividends are distributed to the ordinary shareholders. Unlike the preference shares, the income from the ordinary shares is not fixed in any way. Instead, the shareholders are entitled to whatever share of the profits the directors of the company decide to distribute. (Revel 43, 44)

In addition to traditional equity, gilt-edged securities, those backed by the British government, are also listed on the London Stock Exchange. Likewise, securities backed by local U.K. authorities and securities issued by international organizations like the

World Bank are also listed. However, these securities make up less than 20% of the stock market, while it is the company securities that make up the greater part of the market (Revel 58). As of 1995, the London Stock Exchange listed 2,078 domestic companies and 462 foreign companies (Levich 528). London is the center for trading foreign stocks, and until recently, more foreign stocks were listed in London than in the United States (Levich 528).

The London International Stock Exchange (ISE) is similar to all other stock markets in that it can be divided into two main sections: the primary market and the secondary market. The former raises new financial claims while the latter is involved in the buying and selling of the "second hand" - or already existing - financial claims. The secondary market is the largest market in the United Kingdom. One of its functions is to help the primary market in pricing the new issues. An active secondary market with semi-strong efficient markets will lead to the accurate pricing of new securities where share prices correctly reflect the company's prospects. (Pawley 203, 204)

The ISE has three tiers: the main market (the Official List) with over 200 domestic companies; the Unlisted Securities Market (USM) that allows for the entrance of smaller companies into the market; and the OTC - the over-the-counter market. The OTC market is an informal market that consists of trading in small business shares by a group of brokers and licensed dealers to the public. (Pawley 205)

The London Stock Exchange differs from all other stock exchanges in one main feature - the jobber system. A jobber is a dealer who acts as a chief in all dealings and is instrumental in evening out dramatic fluctuations in price. London is unique in enforcing an adamant separation between jobbers and brokers and in forbidding direct dealings between brokers. (Revel 62)

In 1989, the ISE accounted for approximately thirty percent of European domestic equity capitalization, the largest proportion of any European country. The ISE has also shown a tremendous amount of growth in terms of market capitalization. In 1984, U.S. markets had 54% of the total equity market capitalization, while the United Kingdom had

only 15%. This spread however has significantly decreased, and by 1995 the U.K. had 22% of the market, while the U.S. had 39% (Levich 526).

Most major equity markets allow foreign companies to trade their stocks locally. Nevertheless, each company must satisfy some sort of requirement that is demanded from them by the domestic government. In the United States, each listed company, whether domestic or foreign, must satisfy the demands of the Securities and Exchange Commission (SEC). Because SEC rules are much stricter than those demanded in foreign markets, foreign companies wishing to be listed in the United States must often release more information than they are accustomed to doing at home.

The Securities and Investments Board (SIB) regulates international stock exchanges. The SIB must recognize the exchange in order to allow the transfer of securities. If an exchange is accredited, it becomes known as a Recognized Investment Exchange (RIE). The Securities Association (TSA) allows firms to deal in gilts, domestic and foreign equities, fixed interest stocks, options, and international bonds. (Pawley 226)

The Financial Services Act of 1986 prohibited market manipulation, insider trading, and investment fraud. The act protects investors from these problems and assists in bolstering investor confidence. Insider trading has been illegal in the United Kingdom since 1980 when the Companies Act was passed. (Pawley 227) Similar to the United States, investors are required to maintain an adequate amount of margin to protect against large falls in share prices. The greater the risk and the more volatile the shares, the larger the capital requirement.

Most of Europe permits open markets by practicing reciprocity. This means that foreign companies do not have to restate their accounting reports into local GAAP (Generally Accepted Accounting Principles) before their shares may be listed on their markets. The London Stock Exchange practices a modified form of reciprocity where it reserves the right to request additional accounting information in individual cases. (Levich 558) Although London is stricter in this sense than other European markets, it is still not as strict as the United States that requires all firms to report their accounting statements in U.S. GAAP. This policy, mandated by the SEC, protects investors from

potentially misleading and confusing foreign accounting statements, hence decreasing investor risk. Furthermore, companies whose securities are quoted on the stock exchange are expected to create a prospectus that complies with the legislation of the securities market. Because the companies must formulate their goals and potential weaknesses, investors – both domestic and foreign – will have a greater knowledge of the investment profits or losses that they might be risking.

Two other characteristics of the equity market in Britain that are different from those in the United States are transaction costs and the settlement period. Transaction costs vary considerably between countries. The United States tax of .0033% is one of the lowest in the world. The United Kingdom has a considerably larger tax of .5%, yet that is still below the average of .64% in non-U.S. markets. The settlement period is the amount of time it takes to make/receive payments and to obtain/deliver the securities. A shorter settlement period is an attraction for sellers since it allows for a more rapid means of raising cash. Conversely, a longer settlement period is a deterrent to investment. Before 1995, the United States had a settlement date of T+5 days, but since then has switched to T+3. It takes longer in the U.K. to deliver securities, with a settlement date of T+5 days. Before 1995 however, the United Kingdom's settlement date was T+10 days. While Britain's settlement period is faster than those in the developing markets, it is nevertheless behind most of Europe whose settlement date is T+3 days. (Levich 529, 531)

Like the United States, the equity market in the United Kingdom has evolved with technology. The SEAQ-International (SEAQ-I) began in the London Stock Exchange in 1986. It is a screen-based, NASDAQ-style system, where designated market makers distribute quotes and execute trades (Levich 557). As of 1991, a computerized paperless system called TAURUS (Transfer and Automated Registration of Uncertified Stock) was implemented in the ISE. This system carried the ISE from a paper-based system to an electronical one, eliminating the need for share certificates and transfer forms. Additionally, TAURUS solved the problem of a backlog of unsettled trades that at times exceeded five billion pounds. (Pawley 220)

The Financial Times Index is an index computed by the *Financial Times* to measure U.K. Stock Exchange prices in the London Stock Exchange. The *Financial Times* publishes several indexes in cooperation with the Institute of Actuaries, Faculty of Actuaries, and the Stock Exchange. The indexes include the FT 300-share index (of the 30 leading shares), the Industrial Ordinary shares index, the 500-share index (of the 500 leading shares), and the All-Share index. (Walmsley 91)

Bond Market

In Britain, the central government, local authorities, and numerous companies issue bonds. Those issued by the government and authorities are usually called "stock", while those issued by a company are called "debentures" or "loan stocks" (Revel 40).

There are two main classes of bonds - perpetual bonds and redeemable bonds. Only local authorities might issue perpetual bonds, while the government can issue an undated stock that has no final date by which it must be redeemed. Other types of stocks traded are dated - they carry a date of redemption. Redeemable bonds usually have a range of dates within which they may be redeemed. The borrower cannot redeem the bond before the first date, but must redeem it before the last date. It would thus be preferable for the borrower to have a range of redemption dates since he then has a greater probability of selecting a relatively cheap moment at which to redeem the stock and to replace it with another stock. On the other hand, lenders will prefer a narrower range of redemption dates. (Revel 40-42)

Gilt-edged securities, commonly referred to as gilts, are sterling denominated British government bonds issued by the Treasury. They are issued to fund the PSBR - the United Kingdom's Public Sector Borrowing Requirements. Gilts are fully guaranteed as to interest and principle by the government. There are four categories of gilts -

1. Short - whose maturity is up to five years
2. Medium - from five to fifteen years
3. Long - greater than fifteen years
4. Undated - also called irredeemables since there is no repayment date.

The size of a gilt issue is usually about one billion pounds. Nevertheless, the minimum denomination in the secondary market is fifty to a hundred pounds, while the maximum is one thousand to fifty thousand. (McLintock 170)

Like US Treasuries, gilts pay a semi-annual coupon and their prices are calculated in 1/32 of a percentage point, rather than in 0.01 points as in most other markets. The majority of gilts are standard fixed-rate bonds. Nevertheless, other popular gilts include convertible gilts, created in the 1970's, and floating-rate gilts that originated in 1994. The floating-rate gilt market is a growing market whose issues are used for hedging purposes. Convertible gilts have more than one potential maturity date. In some cases the government has the option of an early redemption, while in other cases, the investor has the opportunity of choosing the maturity date. For example, if the investor buys a short-dated gilt he later has the option of converting into in a longer-dated paper. (Essex 143,144)

In 1986, the Bank of England undertook the reformation of the gilt market. Before that time gilts were bought and sold wholesale on the floor of the London Stock Exchange by jobbers and brokers who acted as intermediaries between the jobbers and the investors. The Bank of England believed the system took advantage of investors and so the Bank appointed primary dealers, who replaced the jobbers, and salespeople who were to advise investors. The dealers are called GEMMs – gilt-edged market makers. The GEMMs anonymously trade with each other using a screen-based service provided by inter-dealer brokers (IDB). (Essex 138)

Other types of bonds include debenture bonds, unsecured loan stock, straight debt, and convertibles. A debenture bond is secured against assets or revenues, while an unsecured loan stock is unsecured and ranks behind the debenture bond. It nevertheless ranks before the shareholders in the order of creditor claims. This definition is contrasted to that in the United States where a bond is usually secured while a debenture is not. A straight debt, often called a straight bond, is a fixed income bond with a fixed maturity date at which the full principal is repaid. A convertible bond carries a fixed interest rate

but provides the holder with the option to convert the bond into shares of the issuing company's stock at a predetermined rate of conversion. (McLintock 177)

Another type of bond is the Eurobond, which is denominated in a particular currency and is usually issued simultaneously in the capital markets of several nations. The Eurobond market is an international market for bonds that are not registered in any country since there is no international authority with whom to register. Eurobonds are issued in a different currency than the domestic currency of the country in which the bond is being sold. The U.S. Dollar and the Deutschemark are the predominant currencies used in the Eurobond market (Baughn 13).

The Eurobond market provides an alternative for borrowers who wish to obtain new sources of funds and avoid the regulation and expense of floating the bond in the domestic market. Eurobonds are negotiable, long-term debt instruments issued by borrowers with high credit ratings. Since the borrower is able to quickly raise the necessary funds with a minimum amount of expenses, the borrower will usually pay a higher interest rate. Additionally, the investor will demand a higher return since there are fewer safeguards in the unregulated Eurobond market. (Baughn 12)

Some characteristics that influence the price of a bond include:

1. Degrees of risk associated with the issuer. The government bonds have the least amount of risk of default followed by the local authorities and then the issuing company. Thus there will be price differentials between the three classes of issuers.
2. The size of the bond issue also places additional risk on the bond. A larger issue of stock is traded daily on the stock exchange and therefore has greater liquidity. Conversely, smaller issues from a local authority or company bond are less frequently traded and thus a seller might not easily find a purchaser in the narrower market. (Revel 42)

The United Kingdom has benefited from the longest period of political stability, enabling the country to claim that it has never defaulted on a government loan for the past three hundred. Nevertheless, since World War II, the bond market has been damaged due

to Britain's policy of relying on inflation in order to reduce the national debt. Due to this method, few small investors have purchased government bonds until the 1990's when the Bank of England began to reform the bond market. (Essex 123) It is quite possible that it is because of this that Britain's bond market, though sizeable, is nevertheless inferior to the bond markets in Germany, Switzerland, and the United States.

Foreign Exchange Market

Foreign exchange markets, the world's largest markets, are markets within which participants buy and sell different currencies. Most of the trading takes place in only a few currencies, such as the U.S. dollar, Japanese yen, German mark, and British pound sterling. As of 1986, London had a greater percent of the foreign exchange market, with about 45% of the market, while New York and Tokyo each had 25% of the market (McLintock 19). Participants in the market include importers, who pay for goods in foreign currencies; exporters, who may have foreign currency sales; brokers, who match buying and selling orders; and commercial banks, which borrow in multiple currencies.

The foreign exchange markets are among the oldest in existence. Their foundations are rooted in trade transactions and cross-border finance. The primary need for the purchase of foreign currency arises from business transactions between residents and foreign countries. This necessitates the requirement to make payments in foreign currency. Foreign exchange markets are markets that convert issues of foreign money for local units. Thus, banks that deal in foreign currency provide the perfect means to meet customer claims.

The major players in the foreign exchange market are the banks that make up the interbank market. In London, over 45% of the transactions undertaken by the banks are inter-bank deals (McLintock 23). Banks participate in the market for three basic reasons. First, banks need to service customer requirements. Second, banks have their own financial transactions that involve foreign currencies. They must meet their own internal requirements for current transactions or for hedging future transactions. Finally, banks use the foreign exchange market to trade amongst themselves. (Baughn 333)

Other dominant players in the foreign exchange market are the central banks, which play a major role in intervention. According to the Bretton Woods Agreement of 1944, central banks were obligated to intervene in the foreign exchange markets at fixed levels in order to preserve the established parities of their currencies against other major currencies. This obligation is now overlooked since most currencies are allowed to float freely against other currencies. Nevertheless, many central banks have retained the option to intervene in the markets to influence the level of the exchange rates for their currencies. (Baughn 335)

The foreign exchange has two markets – the wholesale market and the retail market. In the wholesale market, banks in different centers deal with each other through brokers, while in the retail market, customers approach their banks for foreign exchange that come in the form of travelers' checks or bank-notes. (Revel 51)

The foreign exchange process usually works in the following fashion. Either banks trade between themselves or, for a fee, a broker brings two banks together to transact a deal. A foreign exchange broker brings together professional buyers and sellers of foreign exchange. There are hundreds of banks active in the international foreign exchange market. Since it is time-consuming for each bank to search for the best available price in the market, foreign exchange broker firms have been established. When approached by a bank with an order to buy or sell, the broker will contact other banks and will try to find a counter party.

All foreign currency transactions have the same characteristics - the exchange of two currencies at an agreed exchange rate, the deal date, and value date. The deal date is the date at which the transaction is agreed, while the value date is the date on which the physical exchange occurs. (McLintock 20)

Exchange rates are rates for different currencies and their individual demand and supply determine them. Factors affecting the rates include interest rates, inflation, and the balance of payments position. Rates are quoted in terms of the spot rate – the current rate. The United Kingdom uses the indirect quote that expresses the rate per unit of the home currency. All other countries, however, use the direct quote, which defines the rate per

unit of foreign currency. In addition, forward rates are also used for future dates. Quotes include one, three, or six month forwards. (McLintock 20)

Since World War II and the Bretton Woods Agreement, the dollar has become the world's primary trading and financial currency, thereby fulfilling the role of the world's primary reserve currency. Thus, the majority of foreign exchange trading involves the trading of individual currencies against the dollar. The central banks have traditionally kept the bulk of their foreign exchange reserves in dollars. Due to the historic role of the United Kingdom as a major financial center and trading country, sterling has remained an important international currency even after its decline as the dominant currency of the world's international trading markets. Therefore, the British pound sterling still continues to be actively traded in all the major financial centers. (Baughn 337)

One common foreign exchange transaction is the spot foreign exchange contract. This contract is the foreign exchange transaction undertaken at the current rate of exchange – the spot rate. The transaction is used to convert a sum in one currency into an equivalent sum in another currency. It is usually undertaken by banks for the purpose of inter-bank transactions to increase or decrease the balances of foreign currency in the banks. In addition, the transaction may be used by a corporation or by a broker who has to meet foreign currency obligations. The physical exchange of the currencies takes place on the second working day from the deal date. This is the most common transaction on the foreign exchange markets, representing about 70% of all transactions. (McLintock 23)

Another type of foreign exchange activity is a financial transaction. It has the unique characteristic of almost always involving a swap, which is the simultaneous purchase and sale of the same foreign currency for two different dates in time. (This is also known as a straddle to commodity traders.) This type of transaction is performed for the sake of increased marginal yields. (Baughn 327) However, since rates move at a fast pace, only sophisticated and informed investors should execute such types of financial transactions in order to avoid excessive losses.

No actual physical market exists for foreign exchange. Instead, the markets are unstructured and dealers and brokers transact over phone or computers. The foreign exchange market is a 24-hour market, since one trading center is open while the other is closed. Since business hours overlap around the world, it is not unusual for traders to work around the clock.

The wholesale market is handled exclusively through telephones and tele-printers, with direct telephone lines established between brokers and the main banks in London, and tele-printer links between smaller banks in London and overseas banks. Deals are usually concluded within a matter of seconds and are confirmed by the exchange of written notes. The latest technological advance in communications is the Reuters Money Dealing Service, which provides a high-speed computerized telex system. The new system enables member banks to communicate with each other over computer terminals at high speed (Baughn 336).

Futures Market

A futures contract refers to a deal in a commodity or financial instrument that is made today for settlement at some future date. An organized futures market requires some kind of standard contract and a clearinghouse through which payments are made. Futures, like equities, require margin from investors as a check on their solvency. The chief center of futures trading is the U.S. Commodities. Instruments traded include copper, silver, gold, live hogs, and pork bellies. Financial instrument futures include U.S. Treasury bills and bonds, Eurodollar deposits, and stock index futures. In London, futures are traded on the London Metal Exchange (LME), the Baltic Exchange, and the London International Financial Futures Exchange (LIFFE). The list of commodities includes metals, rubber, cocoa, coffee, sugar, grain, and soybean oil. Included in the financial instruments traded are sterling interest rate contracts, gilts, Eurodollar deposits, foreign currencies, and the Stock Exchange Index. (Walsmely 100)

The London Metal Exchange (LME) is a major world center of metals trading. The LME trades copper, silver, tin, lead, and zinc. It also organizes warehouse facilities

for physical storage of metal. In contrast to the LME is the London Commodity Exchange, which is a company responsible for the provision of services to the 'soft' (non-metal) commodity markets in London. Its members consist of the market associations of the cocoa, coffee, petroleum, rubber, sugar, and wool markets. (Walmsley 132)

The primary function of the Baltic Exchange in London is the matching of cargoes to ships and vice versa by a shipbroker. The Exchange, first established in 1744 under the name of Virginia and Baltic Coffee House, provides the only regulated shipping market in the world. It is comprised of an international membership of 1500 individuals who represent over 670 companies virtually covering the entire shipping spectrum. Ship owners, brokers, and commodity traders make up the core sector of the network. (Baltic Exchange 1) The Baltic International Freight Futures and Options Exchange (BIFFEX) is operated by the London Commodity Exchange and it offers ship owners, charterers, traders, and brokers a means of protecting themselves against the risks of dry bulk carrier freight rates. Risk control using futures trading is called hedging, which is taking a position in a futures market as a substitute for a forward cash transaction. If a charterer who has sold a commodity forward is afraid that freight rates will rise, he will protect himself against a potential loss in profit by buying BIFFEX futures contracts. If freight rates do rise the loss incurred will be offset by a profit on the futures contract. (Baltic Exchange 18, 19)

The object of the London International Financial Futures Exchange (LIFFE) is to provide facilities to enter into contracts for hedging due to possible changes in interest rates, foreign currency rates of exchange, the price of government bonds, the price of equity shares, and the price of agricultural and soft commodities (LIFFE Rules: Section 1.3.1). LIFFE began trading financial futures contracts for sterling, deutschemarks, and yen against the dollar in 1982. It also began trading 20-year gilt-edged stock, and 3-month time deposits in dollars and sterling (Walmsley 132). Under the Financial Services Act of 1986, the Exchange must ensure proper investor protection and must attempt to maintain a fair and orderly market (LIFFE Rules: Section 1.4.1). In order to trade on the

Exchange a member must hold a permit issued by the Exchange, obtain a lease of a permit from a member, or be granted a trading license (LIFFE Rules: Section 3.9.1).

The Financial Times Stock Exchange Index (FTSE) is an index of U.K. Stock Exchange prices produced jointly by the Stock Exchange and the *Financial Times*. The Index is continuously updated, minute-by-minute, to form the basis of futures trading on LIFFE. In 1984, LIFFE introduced a contract based on FTSE. (Walmsley 91)

It is common practice for the futures market exchange to be organized so that every contract traded on the floor of the exchange is executed with the clearinghouse as counter party. The clearinghouse on LIFFE is the International Commodities Clearing House, which is a London company that operates a clearing system for contracts traded between members of LIFFE and the London commodity markets, as well as for the Sydney Futures Exchange, the Australian Options Market, and the Hong Kong Commodity Exchange. The International Commodities Clearing House was formerly known as the London Produce Clearing House. It is now owned by the major British clearing banks and the Standard Chartered Bank Ltd. (Walmsley 117)

The United Terminal Sugar Market Association administers the London Terminal Sugar Market. The association provides standard contracts and clearing facilities for the market via its alliance with International Commodities Clearing House and the London Commodity Exchange. It is interesting to note that since the switch of the main sugar contract from sterling to U.S. dollars, trading volume in the London market has declined, with business being transferred to New York instead. (Walmsley 211)

In conclusion, this article has presented four financial markets in Britain. Although this paper has shown that the country has an expansive infrastructure of financial markets and London is at the center of many of these markets, other countries, such as the United States, are becoming increasingly financially dominant. And while Britain is well recognized for its long-standing tradition of financial prominence, it cannot rely only on past merit. The United Kingdom must begin to challenge the United States and win back some of its lost standing.

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How Color Affects Marketing

By: Channa Leichtling

Touching, tasting, smelling, hearing, and seeing, are the five senses that we use in order to perceive the world we live in. Of these five senses, sight is the one we use the most. Ninety percent of what we know of the world is through our vision. The National Bureau of Standards estimates that the human eye can see 10 million different colors. For centuries, people believed that our eyes were merely receivers. Sir Isaac Newton (1642-1727) claims that our eyes were "visual equipment", and that the brain, emotions, and experiences have no connection to our perception of color what so ever. (Miller, p.1-2)

One hundred years after Sir Isaac Newton died, a German poet by the name of Johann Wolfgang Von Goethe (1749- 1832) began to argue Newton's theory. He claimed that the eye, brain, emotions, and experiences do, in fact, have a connection to our perception of color. Von Goethe's views were not appreciated until one hundred years after his death. (Miller p.2)

Von Goethe's theory is the basis of many research studies done on color today. Many of these recent studies have come to prove that color is not only something we perceive but it also affects the way we feel. (Miller, p.2) An illustration of Wolfgang's theory can be demonstrated in the example of a cloudy day. Cloudy days make colors dull, gray, and monotonous. As a result we tend to feel depressed and sluggish. Working in a dark, gloomy room often leaves us with the same depressed feeling. A bright sunny day, however, will make us feel happy and energetic. We are aware of color from the time we are infants, well before we can recognize shape or form. This awareness stays with us through out our lives. (Danger, p.5)

Almost everyone is affected by color. No two people have exactly the same reaction to a particular color, though there are certain generalities. (Wollard) How can color effect us? Here is a list of how the following colors may affect you.

Red: Red can make you feel excited, full of energy, and alive. Red can actually increase

your heart rate. (Burtoff)

Yellow: The effects of yellow can vary. Yellow can either make you feel cheerful, optimistic, "sunny", or it can make you feel irritated. According to some studies, babies in yellow nurseries seem to cry longer. (Burtoff)

Green: Green is the color of nature. Therefore it leaves us feeling rested and at peace. Green has actually been shown to lower blood pressure, which is one of the reasons why so may hospitals have green walls. (Burtoff)

Blue: Blue makes you feel calm and cool. (Burtoff) Blue is actually the most popular color in America. (Piirto)

Purple: Purple comforts, assures, and spiritualizes. (Jerdee)

Brown: Brown stabilizes, secures, and symbolizes the "down to earth" attitude, as a result of its earthly color. People may feel more like confiding to someone dressed in brown. (Jerdee)

Orange: Orange cheers, and commands, which are why many warning signs are orange. It commands us not to, for an example, walk in a certain hazardous area. (Jerdee)

Black: Black makes you feel sophisticated when it is worn; it forces, disciplines, authorizes, strengthens, and encourages independence. (Jerdee)

White: White can make you feel absolutely quiet, and gives the feeling of cleanliness. (Jerdee)

As a result of the psychological effects color has on human beings, the use of color has become an important marketing tool. Because colors affect our moods, those trying to sell us something agonize over the color of the product, or packaging or even the colors of the atmosphere in which the product is sold. Color is not the only factor that is important when trying to sell a product, but it is the color that attracts the customer, and if the wrong color is used the product won't sell. In fact color is ranked among the top three considerations in the purchase decision. (Cooper)

With many products such as clothes and cars the "color of choice" relies largely on historical sales trends. Research had been conducted to find out which colors certain genders or age groups tend to buy. Each year Cooper Marketing Group conducts a nation

wide “color preference study”, and sells the results to manufacturers and retailers of clothing, major automakers, and home furnishings. This study consists of 400,000 people who are apart of the “Market Fact Consumer Mail Panel.” The panelists represent a cross- section of the U.S. population. They are asked several different questions on their opinion about certain colors. Some of the questions are, “Which color car would you buy?” “What color clothes are you most likely to wear?” “Would you wear a trendy color as soon as it comes out, or do you wait for your friend to wear it first?” Respondents are also required to give basic information about themselves such as age, where they live, and yearly income. This information can help retailers chose the correct color for whatever product they want to sell. “Most research will show differences between the wants and needs of men vs. women and the young vs. the old: We’ve carried it to all other demographic levels as well” said Cooper Marketing Group.

Cooper Marketing developed “color lifestyle” groups. The “color lifestyle” places consumers in three different groups according to the effect color has on the products they buy: Color Forward consumer, Color Prudent consumer and Color Loyal consumer.

The Color Forward group is the consumer that likes to be the first to try a “new” color and is willing to spend more money for it. This type tends to consist of women under the age of 30 or over 50, or men under 30; city dwellers; impulse buyers and people who make less then 35,000 per year.

The Color Prudent group will buy a new color only after seeing a friend try it. They often put quality ahead of color. When choosing a product they tend to be men or women from the ages of 30-50; suburban; careful shoppers; and people who make more then 50,000 a year.

The Color Loyal group is the consumer who stays with the “safe” colors such as blue, gray, and black, rather then fashionable colors. Color Loyal people tend to be men over 60, suburban or rural; people who dislike shopping; and may fall anywhere in the income bracket. (Triplett)

When manufactures and retailers are deciding on what color they wish to make their product, they should first take into account what “group” they are catering to, and

then act accordingly. If, for an example, someone was to manufacture a line of clothes geared toward middle aged women, and distributed the clothes in stores that are predominately located in rural areas, it would be wise to steer clear of colors that attract the Color Forward consumer. The wise decision would to be to choose the colors of their product that would appeal to the Color Prudent consumer.

Cooper Marketing has also concluded that the Color Forward group represents a small, but highly influential segment of consumers. Color Prudent shoppers are the bulk of the market. Color Loyalists are a small but predictable group because that they buy the same color each year. (Triplett) It is important for companies to get the Cooper Marketing results annually, for yesterdays "in" color could be in today's trash bin.

The constant change in popular color trends can sometimes be linked to events happening at a particular time. The metallic fabrics in the disco era can be attributed in part to the publicity generated by the national tour of the King Tut exhibition. In the 1980's black was a very popular color. Credit for this can be given to the "Star Wars" Villain, Darth Vader. Green was another popular color in the 1980's. One reason was in order to increase attention to the environmental and the ecological issues at the end of the 1980's. (Piirto)

When a retailer is dwelling upon which color to promote, economic consideration is very important. When the economy is up, people are more willing to spend money on trendy colors. If the color they bought will only last one season, it won't bother them. However, when the economy is down, or there is a recession, people tend to be stingier. Consumers cannot afford to buy trendy colors that will only last one season. They are more apt to stick to more classic colors, such as blue, gray, and black, so that they will feel they are getting more for their money. (Cooper)

Even when advertising, picking the right color is crucial. One year, a certain car company advertised an older women stepping out of a teal colored luxury car. This advertisement was not successful. The Cooper Marketing group explains, that it was because "teal" was found to be a color that younger aged people were attracted to. Furthermore younger age groups tend to buy small, sporty cars, not large luxury cars.

(Triplett)

Choosing the "perfect color" is difficult, but it is better to have some color in an advertisement than none at all. In the fall of 1998, the Newspaper National Network ran an ad in both *People Magazine* and a newspaper without color print. They put the same ad in another newspaper with color print. Response to the *People Magazine* ad and the one newspaper ad was only six percent. But the newspaper ad, with color scored 21 percent higher. "Color has enough stopping power to give a weak advertisement legs" Says Bob Watson, VP of marketing and media at the NNN. (Davids)

Just as the color of a product must be carefully chosen, the color of the atmosphere in which the product is sold, must also be chosen wisely. The color bright orange, for example, is usually associated with affordability, which is why stores such as Home Depot, Wal-Mart, and the roof of Howard Johnson have a color theme of orange. Orange tells us that these stores are affordable, or cheap. (Cahan) If someone wanted to open a classy, expensive boutique, the color orange would be inappropriate. Restaurants should use red tablecloths, because red stimulates appetite, but should avoid the color blue because it tends to suppress appetite. (Color matters) Therefore it is no coincidence that most fast food restaurants utilize the red and yellow colors because it stimulates appetite and purchases. (Wollard)

B.J. Eichorn, president of BJ's Lifecode Merchandising, was asked to analyze two bowling alleys. She found that the clientele for each bowling alley was very different. The people in one bowling alley were mainly working-class people, who were serious league bowlers. The customers at the other bowling alley were mainly upper class, and bowled only for pleasure, relaxation, and exercise. Eichhorn redecorated the first alley with energetic triangles and southwestern color theme consisting of colors such as peach and green. She redecorated the second alley with "Art Deco" curves, and she used a more complex color scheme, which is usually favored by upper class groups. After she redecorated, both alleys saw an increase in revenue. Eichhorn comments that "We need to design based on the lifestyles of the target market, not the preferences of designers" (Piirto)

Companies often become interested in the color of the interior of their offices because it is believed its appropriate use will make people work harder. Red, orange, and yellow may be the colors they choose, because they tend to stimulate and excite. Others may choose colors such as pale - greens, light yellows, and off whites because these colors offer a more soothing environment, and allow for workers to focus on their projects. (Wollard)

When deciding the colors to use in helping create the best atmosphere, the shade chosen can make all the difference. The brighter shade of a given color can have a very different effect than a darker shade of the same color. The Seattle, Washington jail changed the color of their prison cell walls from bright pink, to a darker "Pepto- Bismol" pink. The darker pink was shown to reduce aggression among inmates. (Wollard)

Our response to color also depends on who we are and what our culture tells us certain colors should mean. In China, a red door symbolizes hospitality and good luck. In old Europe, doctors often wore red capes to show that help was on the way. (Wollard) In the Unites States, we use the phrase "green with envy", while in many other countries such as Japan, Italy, and Turkey, yellow is associated with envy. (Piirto) In the United States, black is generally worn at funerals, making black a color associated with mourning. However, in Japan white is the color of mourning. (Danger, p.5) In the Middle East, women wear black clothing as a sign of modesty. African American women are more likely to wear gold and silver; Hispanic are likely to prefer bright-red, orange and fuchsia; and Caucasian women favor blues, and pinks. The color of product packaging can be different from culture to culture. In Honk Kong, for example, gold type on a label signifies high quality, white and black lettering on white labeling generally conveys a generic or inferior quality. (Gimba)

Children tend to respond more directly to colors than adults. For the majority of children, the color of a food product is far more important than its actual taste. Dave Siegal, general manager of Small Talk, a research firm in Cincinnati, Ohio, explains, "Kids are far more visual then adults." For example, since 1991, Siegal states, "Kids love neon colors, the green and yellow top the list. When we ask kids for ideas on new

products, they shout, 'make it green!'" Siegal attributes the popularity of neon green to Nickelodeon's (a popular children's television show on cable) brand colors that are neon green and orange. (Piirto)

Siegal did another study on a board game called "Perfect Wedding". The target audience for this game was girls from the ages 5-7. Studies showed that most of the girls hated the new board game. Siegal did some research and found out why "Perfect Wedding" was a failure. The pictures on the box showed a brunette bride, an engagement ring, and a picture of a cake- top bridal couple. The problem was that the cake-top groom's hair looked gray in the picture. The groom's hair was made into a youthful black, and then sales picked up. "Kids have such sharp visual acuity, they see things no adult would notice." Siegal also pointed out that any color parents consider revolting is another color that seems to appeal to young children. Siegal found this out while working on colors for Gummy Worms. "Kids love slime and vomit green, anything that repels their parents." (Piirto)

When deciding on the right color for your product, naming that color can have a marked effect on the success of the product. "Renaming 'off-white' to 'antique silk' doubled business for a paint company," said Bob Cooper, a principal of the Cooper Marketing Group in Oak Park, Illinois. "If we name something 'sulfur' that is a real downer." Leatrice Eiseman, a color-design specialist in Seabeck Washington, and the director of the New Jersey based Patone Color Institute, says, "To give a color a name gives it romance…. If you tell someone you just painted your living room '36485', will they rush to the store for a can of that color paint? Not as quickly as if you tell them that this is 'Angel Wing Pink." (Frost)

Under the 1994 Trademark act, the U.S. Supreme Court declared that because color is so important to a product, it could actually be a legal defensible trademark. A trademark is a symbol used to identify goods with a particular producer or seller. It is used to distinguish them from goods produced or sold by others. The case *Qualitex Co. vs. Jacobson*, will show how this law may come into action. Dry-clean pads manufactured by Qualitex were made in the green-gold color scheme that identified these

pads as products of Qualitex. Jacobson, a competitor, began marketing press pads of a similar color. Qualitex then registered its green- gold color as a trademark with the Patent and the Trademark office, and then sued Jacobson for using colors scheme they patented. The Federal Appeals court in California rejected the lawsuit, claiming that a color cannot be trademarked. Many federal courts debated the issue. The U.S. Supreme Court finally decided that color schemes could, in fact, qualify to be a registered trademark. This patented color scheme, however, may only be protected by the statutes of the Trademark Law for a set period of time. After this time period has elapsed, another company may patent this particular color scheme. (Rogers)

Registering colors as trademarks is not an easy thing. It requires significant market penetration. The company must be able to prove that the color they chose is distinctive in relation to their product. The color of certain products, as used in medication, cannot be trademarked at all. The color-coding of pills is usually done to identify their chemical composition, not as a potential trademark. (Rogers) Though there are many guidelines that a business must follow in order to register a color as a trademark, the fact that a color can be registered as a trademark at all is another proof of how important color is to a product.

The right color can't always be predicted. Sometimes choosing the right color for your product can only come about through a trial and error basis. Back in the 1950's Proctor & Gamble, the manufacturer of "Cheer" detergent were deciding on the color of the "flecks" in the detergent. Proctor & Gamble tested three different colors of flecks: red, blue, and yellow. They produced many boxes of this detergent with either red, blue, or yellow flecks. Consumer reports stated that people complained that the detergent with the yellow flecks didn't get clothes clean enough. Others claimed that the red flecks actually damaged their clothes. Blue flecks were singled out for their ability to "get clothes cleaner". Nan Powell, research director for Cheskin & Masten Image Net, says "The color offered no advantage or disadvantage in cleaning ability. However, it was the blue flecks that helped make Cheer detergent one the longest-lived brands on the market". (Piirto)

It has become clear to me that the uses and choices of color have significant impact in a wide variety of circumstances. The success and failure of a product can often be attributed to the "appropriate" color choices. Societal behavior and tradition can result in wide variations in the "interpretation" of colors. The quality of life is often described in terms of associated colors. We live in a colorful world, and we need to understand the impact it has on our lives.

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Strategies in Options Trading

By: Sarah Karfunkel

Covered Call Writing:

Investors use two strategies involving stock options to offset risk: (1) covered call writing and (2) protective puts. The strategy of choice for an investor is dependent upon the extent of the expected stock or stock market decline. Many investors view options as highly speculative, risky investments. However, there are several options strategies that are conservative. One such strategy is covered call writing. Investors write covered calls for the following two reasons:

1. Realize additional income on the underlying common stock by earning premium income
2. Provide a measure of a downside protection (limited to the amount of the premium) against small declines in the price of the stock

Covered call writing usually is considered to be a more conservative strategy than the outright purchase of common stock, because the investor's downside risk is reduced by the amount of the premium received for selling the call.

The covered call writer either buys common stock and simultaneously sells an equivalent number of call options against the shares purchased (commonly called a "buy write"), or sells calls against common stock that is already owned. Its characteristics can be summarized as follows:

- The sale of the option provides immediate cash flow.
- Losses are reduced by the amount of the premium in the event of a downward movement in the price of the common stock.
- It provides a good return even if the underlying common stock is called away (exercised).

A covered call writer owns the underlying common stock but is willing to forgo a price increase in excess of the option stock price in return for the premium.

A writer should be prepared to deliver the common stock shares, if assigned, at any time during the life of the option. Assignment is the act of exercise against a seller, which is executed on a random basis or in accordance with procedures established by the Options Clearing Corporation and brokerage firms. To avoid losing the stock, an investor may cancel the obligation at any time by executing a closing transaction. A closing transaction is performed by buying a call in the same series (option with identical terms).

A good strategy is to sell out of the money calls (strike price> current price) with about two months until expiration. The current expiration month should be avoided because option prices decline as they get closer to expiration. Also, far out of the money calls should be avoided because the sale will produce minimal proceeds.

Uncovered Call Writing:

Uncovered (naked) call writing differs from covered call writing in that the investor does not own the shares of the common stock represented by the option. Further, the potential loss of uncovered call writing is unlimited, whereas covered call writing is a more conservative strategy. An investor who writes an uncovered call option has the objective to earn a return from the writing transaction without investing in the underlying shares of stock. An uncovered call writer must deposit and maintain enough margin (cash and/ or securities on deposit) with the broker to guarantee that the stock can be purchased for delivery if the call is exercised.

Writing uncovered calls can be profitable during periods of declining or generally stable prices, but investors who are considering this strategy should be aware of the significant risks involved. If the market price of the underlying common stock sharply increases, the call could be exercised. To satisfy the delivery obligation, the writer would have to acquire stock in the market for substantially more than the strike price of the option. This action could result in a new loss. Therefore, only investors who have studied the options market closely and are financially able to afford the risk should undertake uncovered call writing.

To explain, an investor who writes an XYZ October 40 call for a premium of $4

receives $400 ($4 x 100) in premium income. If the stock price remains at or below $40, the calls will not be exercised. However, if the stock price rises to $55 ($1,500 loss), the investor will be assigned and will incur a loss of $1,100 ($1,500 loss on covering the call assignment less the $400 premium). An uncovered call writer may cancel the obligation at any time prior to being assigned by executing a closing purchase transaction (buying a call in the same series). Note that an assignment is the receipt of an exercise notice against a seller that provides an obligation to sell the underlying security at the specified strike price.

Protective Puts:

A protective put is the simultaneous purchase of a stock and a put option or the purchase of a put related to a stock already owned by the investor. Whereas covered call writing provides a partial hedge against a decline in stock prices, protective puts can provide almost complete protection. If the stock value declines, the price of the put increases, especially when the put is in the money.

A protective put results in unlimited profit potential. The price of protection against loss while retaining the upside potential is the put option's premium. The investor will pay a premium (the cost of the put) to insure against a loss in the stock position. Because the put option is a right to sell at a predetermined price, the purchase of the put predetermines the maximum risk of the stock. This limit on risk occurs because a put entitles the investor to sell the underlying shares at the exercise price of the put at any time through the expiration of the option, despite how much the price of the common stock declines. The investor continues to receive any dividends paid during the period on stock owned. For common stocks that pay substantial dividends, this dividend revenue can substantially reduce the cost of purchasing puts.

The cost of protection can be measured in terms of annualized percent of investment. For example, consider a 6-month XYZ put with a premium of $4 when the stock is trading at $50. The premium of $4 represents 8 percent of the $50 cost of XYZ. Because the 8 percent premium protects the investor for only six months, the annualized

cost of protection is 16 percent. The 16 percent annual cost is the price the investor is willing to pay to benefit from any advance in the stock of XYZ while limiting the risk of loss.

The protective put strategy is most effective when the investor feels the price of the stock is vulnerable on the downside. In employing this strategy, the investor probably should stick to the put with a strike price closest to the existing price of the common stock. In addition, it is advisable to purchase a put with at least three months remaining to expiration. This strategy permits the stock sufficient time to make an upward move.

Writing Put Options:

The seller (or writer) of a put option is obligated to purchase the underlying stock (normally 100 shares per put option) at the strike price upon receipt of an exercise notice. In return for assuming this risk, the investor is paid a premium at the time the put is written. As a put writer, the investor must be prepared to buy the underlying stock at any time during the life of the option. Investors can write covered or uncovered put options.

Covered Put Writing- a put writer is considered to be covered when (a) there exists a corresponding short position or (b) cash deposits or cash equivalents equal to the exercise value of the option are held with a broker. Recall that a short sale is the sale of a security that is not owned with the intention of repurchasing it later at a lower price. The investor borrows the stock from another investor through a broker and sells it in the market. Subsequently, the investor repurchases the stock and returns it to the broker. To ensure that the short position is covered, the broker requires the posting of collateral.

A covered put writer's profit potential is limited to the premium received and the difference between the strike price of the put and the original price of the stock shorted. The potential loss of this position is substantial: the price of the stock may increase significantly above the original price of the stock shorted. In this case, the short position will generate losses offset only by the premium received. The covered put writing strategy is not used frequently because uncovered put writing offers the same risk and rewards with generally higher premiums.

Uncovered Put Writing- a put writer is considered to be uncovered if (a) there is no corresponding short stock position or (b) no deposits of cash or cash equivalents equal to the exercise value of the put exist. An investor unwilling to purchase stock at the current price might write put options, hoping to acquire the stock at a lower price and meanwhile, receive premium income. If the put is exercised, the cost of the common stock will be the exercise price less the premium.

Straddles:

A straddle is the simultaneous purchase of a put and a call on the same stock, with the identical strike price and expiration month. Typically, the buyer of straddle anticipates a substantial movement in a stock but is uncertain what the direction will be. Because the investor is betting on an extraordinary stock movement, the odds of losing are good. Hence, this strategy is risky and should be undertaken only by experience options traders.

The buyer of a straddle risks losing only the amount of the premium. The maximum loss occurs only if the price of the stock on the expiration date of the options is exactly equal to the strike price. Although it is difficult to lose the entire premium paid for a straddle, it also can be difficult to make a profit. Either the put or the call side of a straddle is almost certain to expire worthless. As a result, the stock has to move substantially for a profit to be made.

EXAMPLE:

Suppose that an investor purchases both a put and call on a stock, paying $5 for the call and $4 for the put, for a total of $9. Also suppose that the underlying stock's price is $60 and that the strike price of the options is $60. If the price of the stock rises above $69 or drops below $51, the investor will make a profit. Only if the stock expires at the strike price of $60 will the investor lose the entire investment. The investor loses only part of the investment at any other price between $51 and $69.

The investor earns a profit if the stock sells at a price exceeding $69 or drops to

less than $51. If the stock rises to $75 and the investor exercises the call at $60, the investor's profit is $6 ($15 minus $9 premium). Alternatively, if the stock drops to $43 per share and the investor exercises his/her put a $60, the profit is $8 ($17 minus $9 premium). Thus, the investor is assured of a profit only if the stock moves by more than $9 in either direction.

One of the most profitable strategies options traders can undertake is straddle writing. This option maneuver involves the issuance of both a put and call on the same underlying stock when the exercise price and the expiration date of the put and the call are identical. Conservative investors who write straddles use a covered writing strategy. In other words, straddles are backed by stock ownership in the event the call portion of the straddle is exercised. In addition, they have sufficient funds to pay for any shares they could be forced to buy as a result of the puts being exercised.

In a flat or unchanging market, time works against the straddle buyer and in favor of the straddle writer. The straddle writer's profits rise as maturity approaches because of the decay in time value. The significant weakness of covered straddle writing is that the price of the stock may decline sharply. Every dollar that the stock declines below the strike price reduces the value of the investor's position by one dollar on the stock owned and one dollar on the stock that will be sold by the owner of the put side of the straddle. Using this example, the writer of the straddle will earn a profit as long as the price of the stock involved stays between $51 and $69.

Spread:

A spread is the purchase and sale of options on the same underlying stock. The options may be either at the same exercise price with different expiration months, or at different exercise prices with the same or different expiration months. This sophisticated strategy is aimed at reducing the risk associated with a simple long (opening buy) or short (opening sale) transaction, and should be used only by experienced trader.

There are two basic types of spreads: (1) bull and (2) bear. A bull spread involves the purchase of an option with a lower strike price, and the concurrent sale of an option

with a higher strike price. In a bear spread, the option with a lower strike price is sold, and the option with a higher strike price is bought. A bull spread is most profitable when the underlying stock's value increases, whereas a bear spread is most profitable when the underlying stock's value falls. The simplest way to execute a bull spread is to purchase an at the money call option and sell an out of the money call option; both options have the same time to maturity but different exercise prices. The lower priced option is purchased in the hope that the underlying stock will increase in value between the time of purchase and expiration. If that happens, the long in the money option will increase in value at a faster rate than the higher, short position. For an investor who is confident what the market is going to rise substantially, purchasing calls would be a better strategy. However, a bull spread is less risky than a simple long position because the cost of the long position is reduced by the amount received from the sale of the call option.

EXAMPLE:

A trader buys one October 40 XYZ put and sells one October 35 XYZ put when the underlying stock is $41 per share. If the stock drops to $37, the October 40 put purchased will rise point for point with the drop on the underlying stock, because it is in the money. The put sold will not increase in value to the same extent, because it is still out of the money. The trader could close this portion at a profit.

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Economic Perspectives on Affirmative Action

By: Dena Stern

Affirmative Action is a very controversial topic. According to some, it's the best thing since sliced bread! It eliminates discrimination, increases the minority-working ratio, thereby creating equal opportunity for all. However, there are many who protest, claiming quite the contrary. These representatives believe that Affirmative Action creates *reverse* discrimination, violates principles of compensatory justice, while leaving us with an economically inefficient work force. Therefore, according to this point of view, Affirmative Action is detrimental and flawed! We are now in a situation where thorough research must play the role in determining which argument holds the most water, and whether or not Affirmative Action is truly an asset to our economy.

Let us begin by familiarizing as to what Affirmative Action entails. Affirmative Action can be defined as policies that attempt to eliminate group based disadvantages, and the inequalities historically resulting from them. So in principle, at least, affirmative action can be distinguished from other anti-discrimination measures by requiring pro-active steps (hence the term "affirmative") to erase differences between women and men, minorities and non-minorities. This was in contrast to the laws that only prevent employers from taking steps that are detrimental to minorities in the work market, such as refusing to employ them. As a matter of fact, studies show that between 1974- 1980, once the policy was well established, employment for women and minorities rose – while employment for white males declined by about 5-10%. Also, the percentage of black males and females rose significantly representing both professional and managerial occupations. We see the argument for pro affirmative action is the increase in professional services to disadvantaged population. Al Gore was quoted, "…the way to lift up the nation isn't by pulling the weakest down; rather, we need to expand opportunities to everyone who wants."

Some opinions hold that affirmative action is a means of remediation for past discrimination and historical injustice. In his book Justice and Reparations, Howard

McGary states, “African-Americans are entitled to receive preferential treatment in employment and college admissions as reparations for slavery and institutional discrimination.” So too, affirmative action helps correct *current* institutionalized discrimination.

From an Educational point of view, universities have implemented affirmative action admission procedures and financial assistance programs to assist women and minority candidates. Universities feel that affirmative action increases diversity, and these assorted environments offer many benefits to the students. When young people are placed in racially and ethnically diverse classrooms, exposed to classes that deal with cultural differences, they blossom intellectually when long held beliefs and ideas are challenged. College students who experience the most racial and ethnic diversity in classrooms and in interaction on campus become better learners and more effective citizens, according to an analysis conducted at the University of Michigan. So according to the previous arguments, Affirmative Action policies can only aid the various institutions, establishments, and organizations.

According to the aforementioned, Affirmative Action is a step forward since the establishment of Equal Employment Opportunity legislations. However, we have critics who disagree. They believe that a generation ago we did it properly when the civil rights laws were passed to prohibit discrimination. This idea of “Affirmative Action” is in essence, special interests hijacking the civil rights movement. They claim that instead of equality, government started imposing quotas, preferences, and set-asides that are a focus on minorities and women to have a place in society.

This is why many believe that Affirmative Action is actually reverse discrimination. Lisa Newton explains how affirmative action violates the principle of equal protection of laws. Turning tables on previously favored groups is as unjust as the original discrimination. That is why Proposition 209, The California Civil Rights Initiative was enacted, it restates the historic Civil Rights Act and proclaims simply and clearly: "The state shall not discriminate against, or grant preferential treatment to, *any individual or group*, on the basis of race, sex, color, ethnicity or national origin in the

operation of public employment, public education, or public contracting.” Reverse discrimination based on race or gender is wrong, “and two wrongs don't make a right”.

It has been estimated that almost two thirds of the population are entitled to preferential treatment under Affirmative Action, while the other third are not. Therefore, unsurprisingly reverse discrimination cases have received increased attention over the last several years. This reflects pressure to modify the force of existing Affirmative Action Plans. The number of race-based discrimination charges filed with the EEOC by white males increased from just over 1,200 in 1990 to about 1,400 in 1993-1994, an average of about 4.4% of all race-based complaints. The number of gender-based discrimination charges filed by white males increased from just over 3,000 to almost 4,400 over the same period, an average of almost 18% of all gender-based EEOC complaints.

As noted by Kauffman in Affirmative Action and the White Male in America, a number of recent court cases have found that affirmative action plans impermissibly infringe upon the rights of protected class non-members with respect to organizational practices including selection, promotion, and reductions in force. This includes Hayes vs. North State Law Enforcement Officers Association 1993; promotion of black officers ahead of higher ranking white officers pursuant to outdated and unjustified quotas in court-ordered consent decree held improper.

Another example, Britton v. South Bend Community School Corporation 1987; white teachers impermissibly laid off over less senior black teachers. These cases should make further sense of the trends in reverse discrimination cases, and illustrate the importance of utilization analyses in helping organizational practitioners "comprehend the razor's edge that they must walk between affirmative action and reverse discrimination," Robinson said in Reverse Discrimination Employment Litigation: Defining the Limits of Preferential Promotion.

In reference to education, today, while Affirmative Action rules stay in place, students are being rejected from public universities because of the need to fill certain quotas of minorities thereby discriminating against the white males. In addition to this argument, Florida Governor Jeb Bush announced his plan to eliminate Affirmative

Action from all state universities because he feels its actually harming intended beneficiaries. He states that you can promote opportunity and diversity in higher education without using unfair and legally suspect racial preferences.

Students should be proud of their accomplishments, and confident that achievement, not skin color or ethnic background, is the measure of merit in their university. Students, as well as workers, need to know that they are there because they deserve to be, not because of legally binding issues to employ or accept a certain percentage of them. Shelby Steele in the New York Harper Perennial argues "Affirmative Action stigmatizes its intended beneficiaries by implying that they are less competent and can't compete as equals with others." Many critics claim that eliminating Affirmative Action will boost the self-confidence of minorities. This effects whether businesses will find themselves in economically inefficient situations. For example, since blacks know they are needed to fill these quotas, it reduces their incentives to achieve and accumulate human capital by systematically lowering the standards of admission or employment expected of them

So too, affirmative action violates the principle of merit. Michael Walter, writer of Spheres of Justice claims that the most meritorious candidate has the right to the position; whereas this race-based affirmative action plan opens opportunities to minorities and women at the expense of the least advantaged white man. White job applicants are turned away because their race does not meet some "goals" or "quotas", set by Affirmative Action. Jobs, university admissions, or a contract, ought not to be based on race or sex. The government must judge all people equally, without discrimination.

Another critic, Barry Gross, author of Morality in Practice, states how Affirmative Action violates principles of compensatory justice in three ways. Firstly, Affirmative Action benefits individuals who have not suffered discrimination. We should only help those who need to be helped. We are individuals; not every white person is advantaged and not every "minority" is disadvantaged. Affirmative Action was enacted to provide opportunity through removing discrimination. It is unjust that an unharmed, unthreatened

minority will get the position due to his birthplace, where as a qualified white male is at a disadvantage regardless of any negative experiences he or she may have suffered.

Secondly, it burdens individuals who have never engaged in discriminatory acts. Should innocent, honest, and moral companies have to deal with all these rules and regulations while they follow the proper guidelines and procedures that insure their success?

Lastly, Affirmative Action fails to adjust the size and type of compensation to the specific discriminatory harms each individual suffered. There is no proof that the individuals who initiated Affirmative Action are actually being helped. These are imperative issues that require immediate attention.

The only honest and effective way to address inequality of opportunity is by ensuring that everyone is provided with equal tools to compete in our society. Then let them succeed on a fair, color-blind, race-blind, gender-blind basis. It is a clear myth that "minorities" and women cannot compete without special preferences- this cannot perpetuate!! We must instead move forward by returning to the fundamentals of our democracy: individual achievement, equal opportunity, and zero tolerance for discrimination against or for any individual. Our government should base its policies on fairness not favoritism.

Since the Civil Rights Restoration Act of 1991, it is not surprising that Affirmative Action is the topic of debate. Also expected, is that instead of focusing on the legal issues, everyone has questions on the cost and efficiency of this policy as well as concerns for the possible show of reverse discrimination. It makes perfect sense, many argue, that the policy contributed to the decline of the U.S. economy by both lowering the average productivity of the workers through the hiring of under qualified minorities, and by increasing the cost of doing business with the rigid burden of fulfilling government requirements.

Though there is a lot to criticize on the fairness and efficiency problems of Affirmative Action, these arguments lie on weak foundations, argue researchers Margaret Simms, Harry Holzer, and David Neumark. Their studies present three perspectives on

Affirmative Action issues, and challenge many of the criticisms raised. First, in The Economic Cost of Discrimination Against Black Americans, Andrew Brimmer states how there's a loss to our economy because blacks are not being given the jobs or education, for them to work up to their potential. In 1993 the disparate treatment of blacks cost the economy over $240 billion dollars, 3.8% of GDP (Gross Domestic Product), and has grown over time. Brimmer's analysis shows that this is due to the fact that instead of being given jobs that exceed their potential, blacks and minorities are over- qualified for the jobs they actually hold. This is a major critique that needs to be implemented in the public discussions on this issue.

Second, Cecilia Conrad wrote a book on the Economic Cost of Affirmative Action, after doing a thorough analysis on public and private expenditures. She concludes that direct costs of enforcing Affirmative Action are pretty small relative to the costs of doing business. She also found that the impact on the productivity appears to be minimal.

Studies by Badgett and Hartmann review the effectiveness of equal employment opportunity policies. One approach the researchers use to measure equal employment/ Affirmative Action activity is by comparing firms that are subject to high standards of federal review (like contractors) and those firms that are not. The companies with a lot of supervision are more likely to be very careful on their representations. In other cases, wages, employment, and occupational status of minority groups and women are reviewed to compare the differences before and after the policy was enforced. There is much evidence that shows that there is only a small gain in wages and employment since the policy was adopted. However, there is a significant gain of colored workers as well as women in a range of blue-collar and white-collar occupations.

Furthermore, there is no evidence that shows that the gain of employment is at the expense of good quality workers. This argument has been going around, but it is all based on assumption, and is no clear-cut evidence whatsoever. In fact, studies have shown that Affirmative Action has had some positive effects on the employment position of protected classes while at the same time limited negative effects on the workers and firm productivity. However, the studies find that there aren't many measurable benefits to the

individuals. For example, Badgett and Hartmann point to the continued differentiation between the unemployment rates of blacks and whites. They also point out the significant occupational disparities. This makes the point clear to us, that although affirmative action can reduce some forms of discrimination, according to their argument, it does not necessarily eliminate institutional or systematic discrimination.

A review of the evidence would lead one to conclude that while affirmative action can be an effective policy tool, its impact is really related to how it's enforced. It doesn't have the power to overcome economic forces, nor can this tool eliminate all racial and gender disparities…though some think it helps (while others are adamant about being against it!) Affirmative action is a strategy to promote equity in American society. It seems clear from the last remarks that it is the best idea we have right now…but I still feel, considering the lack of *extensive* research in this area, that there is plenty of room to disagree.

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Innovative Marketing Tools

By: Sheldon Abraham

The Company Newsletter

Does anyone actually read the monthly mailings many companies distribute? Very likely, they do not read advertising pieces, even though they know your company and may even be a loyal customer.

Advertising mailers may not be the best way to cultivate your customer base. Why not replace those slick flyers with a company newsletter? A newsletter can serve many purposes, the most important of which should be customer service. Advertising may be included, but it should not be the primary content of the piece. In fact, even company information should not be the primary content.

The main focus of a successful newsletter should be the customer - content should be relevant to your customers' interests. It should contain articles about how to save money, save time, preserve their health and safety, or improve their lifestyle. Ideally, your product or service addresses these universal needs in some way, so providing information (other than product information) will still promote your product.

For instance, suppose your business is computer sales and repair. Your newsletter might contain user maintenance tips - a "Tip Of The Month" feature, or glossary installments to define computer terms. Perhaps an article about the history of computer technology, or the future of the computer industry. You might include a short review of popular software, computer-related books, or web sites. Be creative with topics - "Teaching Your Child Computer Skills", "How Computer Games Improve Concentration", "Home Banking Tips", etc.

The more interactive your newsletter, the better it is! Include a question-and-answer section, or "Letters To The Editor". Contests are appropriate in some cases - a trivia question, with a drawing for a useful prize.

If your business is a golf shop, you can use the same ideas above, with a slant toward golf, rather than computers. Even a barbershop could use these ideas - with grooming related issues.

Your company newsletter will help you to develop a relationship with your customers and prospects. If you have a company web site, an online newsletter will keep your costs down by eliminating printing and distribution costs, PLUS - it will increase traffic by providing dynamic content.

Although publishing a newsletter is a marketing tactic, it should be 95% customer oriented. It may be appropriate to include a coupon or other promotional information, but "We-Best" content should be kept to a minimum.

Trade Shows

Trade shows aren't the right marketing venue for everyone, but for some the right shows perform like nothing else. Chief among the advantages is the chance to present your case face to face to more qualified prospects per hour than with any other marketing medium. After all, once you arrive at the show venue, there's no additional traveling. Potential buyers are swarming up and down the aisles - or, for smart exhibitors, stopping by the booth by prior arrangement.

Why else are they beneficial? One main goal is overcoming the "never heard of you guys" sales barrier. Sales representatives say that a company has to be known for people to listen to their presentations. And such awareness comes cheaper by the trade show than by advertising. Afterwards, you would know a certain show was worthwhile because the reps got responses like, “Yeah, we saw you at the Atlanta show. Come on in.”

According to Steve Miller, author of "How to Get the Most Out of Trade Shows," the shows also make it easy to scope out your competition in a natural setting or cost-effectively test-market a new product. "Instead of putting together an expensive market research project, I used to take prototypes of products to shows to see how many actual

orders I could get," he says. "If something was a winner to buyers at a trade show, it was a good bet that it would be a winner in the marketplace."

Knowing your goals and wisely choosing which shows to exhibit at are essential elements of trade show success, says Julia O'Connor, president of Trade Show Training, Inc. "There should be a good industry fit," notes O'Connor, "and don't exhibit only because the show's in Hawaii, Paris or near Aunt Ida. However, if it's a good show and has lower travel costs, that's a consideration for a 'maybe' fit."

Steve Miller adds that too many firms attend with wildly unrealistic sales projections by extrapolating from the expected show traffic to their expected return on investment. Ignore the total number of attendees and go by how many contacts an hour those working the booth can make on average. Then, of those they talk with, how many will eventually buy and how much will they spend with the company over time? Compare that total with the cost of exhibiting, Miller suggests, and you've got a better estimate of return on your trade- show investment.

Show Tips

Trade Shows can be critical to a sales person's success. Some are giant productions with thousands of attendees and hundreds of vendors. Many are much smaller affairs that a sales person has to deal with on his own. Here are a few tips to remember about shows.

Who is at the show? Make sure the show is appropriate for your product line.

Plan in advance.

1. See if you can get an early registration list and do a quick mailing just before the show.
2. Who is speaking and what about? See if any speakers are using your products or will be mentioning your products in their presentation.
3. Promote the show among your current clients. Let them know you will be there and what the program is about.

4. Prepare fliers for specific products that relate to specific parts of the agenda. (If an author is speaking, a flier about his book, for example.)
5. A table cloth and banner are an inexpensive way to look professional. Make sure you have all the appropriate products for display.
During the show.
6. This is show business. Make it is a real production. Lights, balloons, candy, gifts, give-aways, drama, some enthusiasm are critical to success.
7. Distribute the fliers at the venue to which they relate before the program begins.
8. Do not sit down behind the table. Stand it front of it or even to one side.
9. Have chairs available for software demonstrations.
10. Have order forms handy on a clipboard so it is easy to get signatures.
11. Have fun. It is a self-fulfilling prophecy. If you look like your having fun, you will talk to more people, you will then sell more stuff and make more money, then you will really be having fun.
12. Aggressively collect business cards and other lead information. Make notes for further follow-up.
13. Don't forget the other vendors. Many are potential clients, all of them have information you might find useful. Be friendly, ask questions.
14. Use a show discount to close business right now. A 20% discount is enough to force an immediate decision. Take advantage of it and close the business now.
After the Show
15. Get a list of attendees and do a follow-up mailing.
16. Critique yourself on your performance. What could you do better next time?

Small Favors

There was a study done in the late sixties on college students and their attitudes towards policemen. The student’s attitudes toward the police were measured and then they were broken up into three groups. All three groups were asked to write an essay in

praise of the police in spite of their personal feelings. One group was paid $10 for their essay, the second group was paid 25 cents and the third group was not paid anything.

Several weeks later, the attitudes of all three groups were again polled to see if there was any change in the way they felt about policemen. The group that was not paid and the group that was paid $10 showed no change in attitude. The group that was paid 25 cents was remarkably pro police.

The explanation of the phenomena is simple. Those who were paid $10 to write an essay in favor of the police, knew why they wrote the essay. Those who were not paid knew they wrote the essay, because they were asked to. The group that was paid 25 cents were psychologically confused, they didn't do it for the money, they didn't really do it because they were asked, they must have done it because they had a positive attitude about the police. Their attitudes followed their behavior.

This same phenomenon is being played out every day all over America. Every time an insurance agent hands out a ball point pen, or a real estate agent gives away a calendar, attitudes are changed. They are changed much more profoundly with a small gift than a large one.

Getting Publicity

When you have a business of any kind, publicity is very important. If your business is new and has limited funds for advertising, what do you do? Make some noise. Generate some interest. Since you have a draft of your marketing plan with word-of-mouth, as the first line of marketing your new business or product, talk it up!

Next look for some local advertising if you have that type of business or product. It is important to understand that the publications your potential customers read, whether they are glossy magazines or daily newspapers, need to fill their pages every day or week or month with interesting information. You can be that interesting information!

First write down the details of what you would like the public to know about your product or service, anything you would like to publicize. For the local newspapers, this should be just an outline with an intriguing headline, one that will make an editor want to

learn more about your service or product or event. Try to write simple paragraphs with very few words. This will become your "press release" so to speak. You see what a typical press release looks like by going onto the Internet and searching under "press releases." Almost all major companies have them listed on their publicity pages. These samples will give you an idea of what kinds of points are important to highlight about your business or product to grab attention.

Your press release does not need to be very detailed and don't use technical descriptions; instead use words that simply tell the facts about your product or service. It should, however; contain enough information to get the attention of an editor, usually the business editor. Make sure that along with the information about your business or product you include your contact information.

Your local newspapers are generally the easiest to contact. Send your press release giving the details you want to make known. The editor may send a reporter to interview you, send a photographer to the event you want covered; or at the very least, have someone call you. The papers do need sufficient notice, though, so if you have something important coming up, an event or a seasonal product, make sure you give enough notice.

It's a little tougher to get noticed by a major magazine. Sometimes a local story will be noticed by a larger publication and they will contact you. Since so many newspaper articles are now on the Internet, it will help you get expanded coverage. Look for a magazine in your field and do the same thing as for the local papers. Send a short press release, following the directions given either in the magazine itself or on their Web site. It may take some time, but they will contact you if you have a unique product or service that fits into the kind of material they publish.

Free Information

How do your clients come to hire you? Shopping begins when someone has a need, narrows the field to several top candidates and selects a provider who seems to fit the bill. Discovery involves folks not fully conscious of a need, who encounter someone

about whom they get excited. "This person can help me! " they think, and they get in touch to become a client.

When you're discovered rather than shopped, price takes a back seat to the client's excitement. And the relationship with the client tends to go more smoothly. Dennis Vogel, the "Small Biz Thriving" Wizard at Wz.com, gave a name for this process that explains why providing lots of information produces congenial clients. The information that you provide about your business facilitates a "compatibility check." Without you having to spend hours on the phone screening potential clients, what you've written serves as a magnet for those who like how you see and do things.

Writing isn't the only medium that helps attract the right clients. Psychotherapists who have appeared on radio or TV say that those who get in touch after their media appearance don't need a free sample session to feel comfortable becoming a client. Public speaking also allows those in the audience to get a feel for compatibility. On the Web, video clips could play this role.

When asked for examples of "compatibility checks," Vogel's list includes these examples:

* Movie previews show the most exciting or funniest parts of movies.
* Some stores allow customers to look through or partially read books or magazines before deciding whether or not to buy them.
* Martial arts demonstrations at county fairs show people what they can learn if they take lessons.

Joe and Maria Gracia of Milwaukee, Wisconsin, have a Web site, givetogetmarketing.com, where they make it plain that they recommend that clients give information or something of value to prospects. Anybody who doesn't agree with their beliefs probably won't hire them because of incompatibility.

* Free product samples, say of shampoo, can let you know if you like the way the shampoo smells and lathers up.
* A medical clinic has videotapes available for prospective patients, telling them, "Imagine getting to your doctor before your first appointment."

The free information that facilitates a compatibility check, Vogel points out, is beneficial not only to the recipient. By aiding the process of discovery, it helps ensure the good match that keeps the provider happy too.

Getting Visibility by Sponsoring Events

My husband runs marathons, and we've both been involved in running clubs in the city, so when I saw that a certain bank was sponsoring the Chicago Marathon, I opened an account there. I was impressed with their community involvement and support of the running community," says Chicagoan Sharon Bond. Her statement illustrates perfectly why businesses help fund special events in exchange for recognition as a sponsor.

Bond's story also has another chapter, however. "This particular bank did not have its internal systems in order, and I had one disastrous experience after another with my account. I finally closed it after a year of frustration," she says. "The sponsorship was nice, but don't promise what you can't deliver!"

Sponsorships are a time-honored method of winning favor with the public by associating the name of your business with an event. When strategically selected and intelligently executed, event sponsorships help persuade your target market to do business with you. Like every marketing technique, however, sponsorships sometimes waste your money or, as with Bond's bank, trigger a backlash.

Most businesses don't have a specific goal when they sponsor an event, just a vague idea that it will bring them tons of new business. Since sponsorship usually costs anywhere from five hundred to several thousand dollars, you should first make sure that the audience for your product or service will be attending, and that sponsoring something for that audience fits your plans for growth.

Don Debalak, author of “Infiltration Marketing”, cites as an excellent match a hobby store in Minneapolis, where he lives, that sponsored special events for local Cub Scout groups. As a faulty choice he recalls the time a hardware store sponsored a community dance, not realizing that the dance was for teenagers - not their clientele.

"If a group is worth sponsoring, then nurture those relationships and become active in the organization. Show up at the event," Debelak suggests. "Get a booth. Run a contest there. Give things away. Do a survey. Give out prizes. Present a workshop. Merely sending over a check gets you only a portion of the benefit possible from sponsoring events."

Besides showing up at the event, getting involved with attendees in some way and collecting names, Debelak urges businesses to band together with other sponsors and send joint mailings to encourage people to come to the event. "That way, all the sponsors benefit from increased attendance and also get exposure to people who don't go to the event," he says.

Be proactive in seeking out events to sponsor, instead of just responding to solicitations from salespeople. By watching calendar listings in the local newspapers or in trade magazines, you can identify annual events reaching your target market that you could explore sponsoring the following year. Above all, consider a sponsorship a shrewd investment that gives you access to a slice of the public with whom you form a warm, profitable and enduring relationship.

Headlines that Sell

Skilled copywriters spend a disproportionate amount of time crafting the top line of an ad because that's what accounts for most of its impact. Here are some of the time-tested formulas on which they rely.

1. Make a promise. "Print labels with your PC in just 2 seconds." "Eliminate stale website content!" "Wherever you are, we'll get them to your door." By simply stating the result that the product or service achieves, these headlines from Dymo, Screaming Media and MapQuest, respectively, earn the notice of those experiencing the problem and interested in the promise.

2. Single out the folks you're appealing to. Often this takes the form of a question: "Growing pains?" "Reinventing the wheel with every document?" "Heard enough 'Be Your Own Boss' hype?" The latter two, for Hotpaper.com and eWork Exchange, work

better because they're more specific. You'd know just from each headline whether or not the ad deserves a read from you. The first example, from UUNET Small Business Plus, requires guesswork or further reading to be sure what the ad is about. Remember, people decide in less than five seconds whether or not they're going to give your message conscious scrutiny.

3. Present a testimonial. Words from some real, identified person shown in a photo carry weight. An ad for NetLedger consists completely of remarks from Tom Coughlan, president of Open Door Technologies. Readers have such regard for testimonials that even quotes coming from a photographic model standing in for a typical buyer gain attention, as with Interland's "I got my Web site for $19.95 a month," illustrated by an unnamed mechanic hefting a tire on his shoulder.

4. Deliver news. Lead off with something resembling a news headline. "Kelly's Karwash now handles RV's too." "New herbal remedy banishes fungus toe-nails fast." "Driveup dry cleaner simplifies life for Nashville working moms." Even when a publication insists on an accompanying tag, "Advertisement," news-format ads get high readership.

5. Tell a story. Auto manufacturers such as Saturn and Volvo often narrate a true tale about a particular owner saved by their car's special safety features. Sometimes, though, the story is much sketchier, told through a headline such as "What a difference a day makes" (for a plastic surgeon) with before-and-after photos of a woman's chin or bustline.

6. Offer a "how to." "How to make a mailing simple," reads the header for an eLetter ad. "How to lose weight fast." "How to buy the car of your dreams - and get it delivered next week." These all deliver the core message cleanly and efficiently.

If you're wondering why wildly creative headlines aren’t recommended, it's because award-winning ad copy does not necessarily sell. Unless you're trying to earn the notice of the advertising community, investors or journalists who write about cool ads, you're better off earning plain ordinary rewards, like new customers walking through your front door, your phone ringing off the hook. Forget the risks of cute stuff. Strong, functional headlines get the job done!

Testing and Tracking Ads

How can you know which marketing media and messages are producing the best results? It's easy when every ad includes a call to action and a tracking method. In contrast to "we exist" advertising, which supposedly spreads and reinforces awareness of your company, invite your reader, listener or viewer to take some specific action. "Call now to receive your free sample." "Register at our Web site for a chance to win." "Bring in this coupon for a 10 percent discount."

Combine this with a tracking method and you'll be able to tally responses and compare results from different versions of graphic images, ad copy, ad media, timing and so on. These tracking methods enable you to know which variations had which effect:

* Multiple phone numbers. A real-estate expert who sells home-study courses uses one toll-free reply number for each magazine in which he is running classified ads. His monthly phone bills then automatically reveal which magazine prompted the greatest number of calls.
* Extension numbers. You can require callers to punch in or state an extension number, each keyed to a different ad location, a different headline and so on.
* Someone to ask for. Version A of the ad says "Ask for Melanie Weaver," while version B says "Ask for Ken White." You needn't have a Melanie or Ken working for you. The operator jots down which person was mentioned and replies, "Melanie (or Ken) isn't in today. May I help you?"
* A discount code. To take advantage of an offered discount, the customer must provide a numerical or verbal code. For phone or Internet sales, the buyer reads back or types in the number. For mail order or retail shops, the buyer needs the coupon that contains the code.
* "Mention this ad." For radio and TV ads, use this method instead of the code. Someone gets a free imprinted T-shirt, mouse pad or hat if they come in and ask for it. The number of the amount of people who ask indicates the effectiveness of the station that aired the corresponding ad.

* A special URL. Print ads or e-mail ads with a call to action can send respondents to a Web page set aside just for that version of the promotion. Newspapers and magazines can deliver your ad with what's called a "split run" - half the subscribers get an ad keyed to URL A, and the other half get a version keyed to URL B. Convenient!
* An address variation. Check with your post office before implementing this. In many situations you can add a suite or box number to a street address to reveal which ad version prompted the order or inquiry.

Tests often reveal surprising results. For example, in one test, black-and-white ads attracted more orders than the same ads in color, because those readers associated black-and-white layouts with news. Little factors sometimes have a disproportionate effect. Advertising great John Caples once found that simply changing the word "repair" to "fix" increased response 20 percent!

Location, location, location...

It would be funny to think of someone introducing a new swim product in Anchorage, Alaska, or presenting a revolutionary heater to residents of Tucson, Arizona in the summer; yet when someone has a great idea they are often so caught up in the process they forget who the end users will be or what impact the product or service will have on their intended market.

There are many factors to be considered when you are either starting a new business or even trying to introduce a new product - and where you are located is one of them.

There were news stories recently about where the best cities in the country are to start a new business and the story show how important it is for people to consider their surroundings when starting out. Not your physical surroundings but your surroundings in relation to the product and/or service you plan to offer.

If your business is service oriented is there sufficient growth in your area to sustain another service? Keeping up with trends in certain areas will help you answer this

question. If you read that a large factory or housing development is coming to your town, for instance, it might be a good time to get your new business started.

If you have a product intended for children and young families, do you live in an area with young families; or, do you have a marketing plan showing how you will get your product to those people who will use it? If your business will utilize outside contractors, will they be available in your area? And do you live in an area where those contractors will readily be able to travel to meetings without much of a problem or expense? If the nearest airport were 250 miles away it certainly would not be convenient.

If your business requires a website and technical expertise is there a source for finding this expertise? In the northeast it is very difficult and expensive, though not impossible, to find good technical people. This factor is a consideration for new companies. If you were located in a college town or near a university and there was a good supply of help, it would not be a factor.

If your business depends on lots of tourists and you live in Fargo, North Dakota, I would say you are in the wrong business. Not that Fargo isn't a wonderful place to visit; it certainly is. But if your business was located in Orlando, Florida instead and you catered to tourists, it would more likely be a success.

On the other hand, there are always opportunities for entrepreneurs who are creative. For instance, if you live in a small town that typically has a strong tourist business in the summer and you have the space, you could open a miniature golf course, for instance, or rent summer play items like tubes or canoes if you live by a river, and could almost make your year's wages just in the summer.

The trick is to find a problem that needs to be solved or a niche market and keep in mind your location and the market you are trying to serve.

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The Federal Reserve System

By: Rachel Spitezki

The Federal Reserve, the central bank in the Unites States was founded by Congress in 1913, to provide the nation with a safer, more flexible and stable monetary system. Over the years, it's role in banking and the economy has expanded.

Today the Federal Reserve's duties fall into four general areas:

- Conducting the nation's monetary policy by influencing the money and credit conditions in the economy in pursuit of full employment and stable prices.
- Supervising and regulating banking institutions to ensure the safety of the nation's banking and financial system and protecting the credit rights of the consumers.
- Maintaining the stability of the financial system and containing systemic risk that may arise in financial markets.
- Providing certain financial services to the U.S government, to the public, to financial institutions, and to foreign official institutions, including playing a major role in operating the nation's payments system (Brauddus 5-7).

Background of the Federal Reserve

Before Congress created the Federal Reserve System, periodic financial panics had plagued the nation. These panics had contributed to many bank failures, business bankruptcies, and general economic downturns. A particularly severe crisis in 1907 prompted Congress to establish the National Monetary Commission, which put forth proposals to create an institution that would counter financial disruptions of these kinds. After considerable debates, Congress passed the Federal Reserve Act, which President Woodrow Wilson signed into law on December 23, 1913. The act stated that its purpose

was “to provide for the establishment of Federal reserve banks, to furnish an elastic currency, to afford means of rediscounting commercial paper, to establish a more effective supervision of banking in the United States, and for other purposes”.

Structure Of The System

The Federal Reserve System has a structure designed by Congress to give it a broad perspective on the economy and on economic activity in all parts of the nation. It is a federal system, composed basically of a central, governmental agency—the Board of Governors —in Washington, D.C., and twelve regional Federal Reserve Banks located in major cities throughout the nation. These components share responsibility for supervising and regulating certain financial institutions and activities; for providing banking services to depository institutions and to the federal government; and for ensuring that consumers receive adequate information and fair treatment in their business with the banking system.

A major component of the System is the Federal Open Market Committee (FOMC), which is made up of the Board of Governors, the president of the Federal Reserve Bank of New York, and presidents of four other Federal Reserve Banks, who serve on a rotating basis. The FOMC oversees open market operations, which is the main tool used by the Federal Reserve to influence money market conditions and the growth of money and credit (Clifford 21).

Two other groups play roles in the way the Federal Reserve System works: depository institutions, through which the tools of monetary policy operate, and advisory committees, which make recommendations to the Board of Governors and to the Reserve Banks regarding the System’s responsibilities (Mayer 26).

Board of Governors

The Board of Governors of the Federal Reserve System was established as a federal government agency. It is made up of seven members appointed by the President of the United States and confirmed by the U.S. Senate. The full term for a Board member is fourteen years; the appointments are staggered so that one term expires on January 31

of each even-numbered year. After serving a full term, a Board member may not be reappointed. If a member leaves the Board before his or her term expires, however, the person appointed and confirmed to serve the remainder of the term may later be reappointed to a full term (Woodward 25-29).

The Chairman and the Vice-Chairman of the Board are also appointed by the President and confirmed by the Senate. The nominees to these posts must already be members of the Board or must be simultaneously appointed to the Board. The terms for these positions are four years.

The Board of Governors is supported by a Washington staff numbering about 1,700. The Board's responsibilities require thorough analysis of domestic and international financial and economic developments. The Board carries out those responsibilities in conjunction with other components of the Federal Reserve System. It also supervises and regulates the operations of the Federal Reserve Bank and their Branches and the activities of various banking organizations, exercises broad responsibility in the nation's payments system, and administers most of the nation's laws regarding consumer credit protection (Groseclose 33-34).

The Federal Reserve System conducts monetary policy using 3 major tools:

- Open market operations—the buying and selling of U.S. government (mainly Treasury) securities in the open market to influence the level of reserves in the depository system.
- Reserve requirements—requirements regarding the amount of funds that commercial banks and other depository institutions must hold in reserve against deposits.
- The discount rate—the interest rate charged commercial banks and other depository institutions when they borrow reserves from a regional Federal Reserve Bank.

Policy regarding open market operations is established by the FOMC. However, the Board of Governors has sole authority over changes in reserve requirements, and it must also approve any change in the discount rate initiated by a Federal Reserve Bank (Thoren 13).

The Federal Reserve also plays a major role in the supervision and regulation of the U.S. banking system. Banking supervision—the examination of institutions for safety and soundness and for compliance with law—is shared with the Office of the Comptroller of the Currency, which supervises national banks, and the Federal Deposit Insurance Corporation, which supervises state banks that are not members of the Federal Reserve System. The Board's supervisory responsibilities extend to the roughly 1,000 state banks that are members of the Federal Reserve System, all bank holding companies, the foreign activities of member banks, the U.S. activities of foreign banks, and Edge Act and agreement corporations (institutions that engage in a foreign banking business).

Some regulations issued by the Board apply to the entire banking industry, whereas others apply only to member banks, that is, state banks that have chosen to join the Federal Reserve System and national banks, which by law are automatically members of the System. The Board also issues regulations to carry out major federal laws governing consumer credit protection, such as Truth in Lending, Equal Credit Opportunity, and Home Mortgage Disclosure; many of these regulations apply to various lenders outside the banking industry as well as to banks (42).

Members of the Board of Governors are in continual contact with other policymakers in government. They frequently testify before congressional committees on the economy, monetary policy, banking supervision and regulation, consumer credit protection, financial markets, and other matters. Under the Humphrey–Hawkins Act, the Board of Governors must submit a report on the economy and the conduct of monetary policy to Congress by February 20 and July 20 of each year. The Chairman of the Board of Governors is called to testify on the report before the Senate Committee on Banking,

Housing, and Urban Affairs, and the House Committee on Banking, Finance, and Urban Affairs (Groseclose 44).

The Board has regular contact with members of the President's Council of Economic Advisers and other key economic officials. The Chairman meets from time to time with the President of the United States and has regular meetings with the Secretary of the Treasury (53-54).

The Chairman has formal responsibilities in the international area as well. For example, he is the alternate U.S. member of the Board of Governors of the International Monetary Fund. He is a member of the board of the Bank for International Settlements (BIS). The chairman is also a member, along with the heads of other relevant U.S. agencies and departments, of the National Advisory Council on International Monetary and Financial Policies. He is also a member of U.S. delegations to key international meetings, such as those of the finance ministers and central bank governors of the seven largest industrial countries—the Group of Seven, or G-7.He, other Board members, and Board staff members share many international responsibilities, including representing the Federal Reserve at meetings at the BIS in Basle and at the Organization for Economic Co-operation and Development in Paris (Johnson 7).

One member of the Board of Governors serves as the System’s representative to the Federal Financial Institutions Examination Council (FFIEC), which is responsible for coordinating, at the federal level, examinations of depository institutions and related policies. The FFIEC has representatives also from the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision.

The Board publishes detailed statistics and other information about the System’s activities and the economy in publications such as the monthly Federal Reserve Bulletin, special announcements of Board actions, and separate statistical releases. Through the

Federal Reserve Regulatory Service, it provides materials relating to its regulatory and supervisory functions (Greider 64).

Federal Reserve Banks

A network of twelve Federal Reserve Banks and their twenty-five branches carries out a variety of System functions. It includes operating a nationwide payments system, distributing the nation's currency and coins, supervising and regulating member banks and bank holding companies, and serving as banker for the U.S. Treasury. A letter and a number identify each Reserve District. All U.S. currency carries the letter and number designation of the Reserve Bank that first put it into circulation. Besides carrying out functions for the System as a whole, such as administering nationwide banking and credit policies, each Reserve Bank acts as a depository for the banks in its own District and fulfills other District responsibilities (Mayor 78).

The Board of Governors exercises broad authority over the operations and activities of the Federal Reserve Banks and their Branches. This authority includes oversight of the Reserve Banks' services to banks and other depository institutions and of their examination and supervision of various banking institutions (84).

Each Federal Reserve Bank must submit its annual budget to the Board of Governors for approval. The Reserve Banks are the operating arms of the central banking system, and they combine both public and private elements in their makeup and organization. As part of the Federal Reserve System, the Banks are subject to oversight by Congress; and like the Board members, Reserve Bank presidents may testify before congressional committees. Each Reserve Bank has a staff of full-time officers and employees that manages and operates it. Each Reserve Bank has its own board of nine directors chosen from outside the Bank as provided by law (Moore 95-97).

Boards of directors of the Reserve Banks and Branches provide the Federal Reserve System with a wealth of information on economic conditions in virtually every corner of the nation. The FOMC and the Board of Governors in reaching major decisions

about monetary policy use this information. Information from directors and other sources gathered by the Reserve Banks is also shared with the public in a special report—informally called the Beige Book, which is issued about two weeks before each meeting of the FOMC. In addition, every two weeks, the board of each Bank must recommend to the Board of Governors a discount rate for its Bank; a recommendation for a change cannot take effect unless the Board of Governors approves it (Thoren 48).

The income of the Federal Reserve System is derived primarily from the interest on U.S. government securities that it has acquired through open market operations. Other major sources of income are the interest on foreign currency investments held by the System; interest on loans to depository institutions (the rate on which is the so-called discount rate); and fees received for services provided to depository institutions, such as check clearing, funds transfers, and auto-mated clearinghouse operations.

After it pays its expenses, the Federal Reserve turns the rest of its earnings over to the U.S. Treasury. About 95 percent of the Reserve Banks' net earnings have been paid into the Treasury since the Federal Reserve System began operations in 1914. (Income and expenses of the Federal Reserve Banks from 1914 to the present are included in the Annual Report of the Board of Governors.) If a Reserve Bank were liquidated for any reason, all proceeds after the payment of bills would also be turned over to the Treasury (Humprey 149).

The Board of Governors audits the Reserve Banks every year; and its staff periodically reviews operations in key functional areas. The Reserve Banks, like the Board, are subject to audit by the GAO, but certain functions, such as transactions with foreign central banks and open market operations, are excluded from the audits (Brauddus 65).

Each Reserve Bank has an internal auditor who is responsible to the Bank's board of directors (67-68).

Federal Open Market Committee

The FOMC is charged under law with overseeing open market operations, the principal tool of national monetary policy. These operations influence the amount of reserves available to depository institutions. The FOMC also sets ranges for the growth of the monetary aggregates and directs operations undertaken by the Federal Reserve in foreign exchange markets (Griffin 72).

The FOMC is composed of the seven members of the Board of Governors and five of the twelve Reserve Bank presidents. The president of the Federal Reserve Bank of New York is a permanent member; the other presidents serve one-year terms on a rotating basis. All the presidents participate in FOMC discussions, contributing to the Committee's assessment of the economy and of policy options, but only the five presidents who are members of the Committee vote on policy decisions. The FOMC under law determines its own internal organization and by tradition elects the Chairman of the Board of Governors as its chairman, and the president of the Federal Reserve Bank of New York as it’s vice chairman. Formal meetings are held eight times each year in Washington (76).

Member Banks

The nation’s banks can be divided into three types - according to which governmental body charters them and whether or not they are members of the Federal Reserve System. Those chartered by the federal government (through the Office of the Comptroller of the Currency in the Department of the Treasury) are national banks; by law, they are members of the Federal Reserve System. Banks chartered by the states are divided into those that are members of the Federal Reserve System (state member banks) and those that are state non-member banks (Benston 85).

State banks are not required to join the Federal Reserve System, but they may elect to become members if they meet the standards set by the Board of Governors. At the end of 1993, 4,338 banks were members of the Federal Reserve System, 3360

national banks, and 978 state banks—out of 11,212 commercial banks nationwide (Moore 187).

Member banks must subscribe to stock in their regional Federal Reserve Bank in an amount equal to 3 percent of their capital and surplus. The holding of this stock, however, does not carry with it the control and financial interest conveyed to holders of common stock in for-profit organizations: It is merely a legal obligation that goes along with membership, and the stock may not be sold or pledged as collateral for loans (Gause 90).

Advisory Committees

The Federal Reserve System uses advisory and working committees in carrying out its varied responsibilities. Three of these committees advise the Board of Governors directly:

- ***Federal Advisory Council***. The Federal Reserve Act established the council, which consists of one member—traditionally a commercial banker—from each Federal Reserve District. The council is required by law to meet four times each year with the Board of Governors in Washington, D.C., to discuss economic and banking matters.

- ***Consumer Advisory Council***. This statutory council, which has thirty members, meets with the Board three times a year on matters concerning consumers and the consumer credit protection laws administered by the Board. The council consists of academics, legal specialists in consumer matters, and members representing the interests of consumers and the financial industry.

- ***Thrift Institutions Advisory Council.*** After the passage of the Depository Institutions Deregulation and Monetary Control Act of 1980, which extended to thrift institutions the Federal Reserve's reserve requirements and access to the discount window, the Board of Governors established this council to obtain

information and opinions on the needs and problems of thrift institutions. The council is made up of representatives of savings and loan associations, savings banks, and credit unions (Greider 98).

At last, the Federal Reserve Banks also use advisory committees. Perhaps the most important are the committees (one for each Reserve Bank) that advise the Banks on matters of agriculture and small business. Two representatives of each committee meet once a year in Washington, D.C., with the Board of Governors.

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The Knowing – Doing Gap

By: Aaron Twersky

Background

Approximately a year ago, as I was sitting in one of my initial Management classes, I recall listening to one of the students in class answer a question that the professor had posed to the class. I have long forgotten the question, but it was his answer that remained with me - not what it was, but how it was. His solution to the professor's dilemma went on, and on, never making much practical sense. He spoke with a forced eloquence, using all the latest -seemingly unrelated to the topic - buzzwords he could muster. All, in my opinion, just to sound articulate, polished and that he knew it all. As I listened to his comments, I wondered about a few things: Whom is this guy trying to deceive? Why? Would he, in a real-life management scenario actually carryout any of his verbose and over-complicated solution? I began to wonder as well if all managers do this? Could this student's situation reveal a much bigger, more serious problem managers face? These are some of the issues that will be discussed in this paper.

Purpose of Study

This article will include some of the problems which occur in the Management world whose symptoms I described above: talk substituting for action, over-complicated talk and the knowledge of what you have to do but never actually doing it. These problems, if not dealt with, can tear at the heart of a company, as they can unnecessarily slow, and possibly remove altogether, the decision making process a company requires to achieve its goals. This can in turn disappoint customers and shareholders, who will in-turn take their business elsewhere.

Scope of Study

I will deal specifically with what has come to be known as the *knowing-doing gap*

and the *smart-talk trap*. Jeffery Pfeffer and Robert Sutton coined these terms in an article they wrote for the Harvard Business Review (May 1999). They subsequently wrote a book about these phenomenon which they describe as: "How smart companies turn knowledge into action", or don't. The implications of this problem, if it indeed does exist, may be quite serious.

Methodology

Research for this paper was done using websites and many management books as reference. As I am a full time student, I was unable to bring any personal examples, and was therefore forced to include case studies and statistics from other sources to prove the points made within the paper.

Analysis

Pfeffer and Sutton give as a definition for the knowing doing gap: "It is not the inertia of indifference or ignorance, but of knowing too much and doing too little." An example:

> Faced with a worrisomely slow time-to-market for its new products, a large furniture company conducted a careful benchmarking study. The results were clear: a project-based organizational structure would help solve the problem. But more than a year later, the company had not instituted a single change. Senior executives, although uniformly supportive of the idea of restructuring the organization, were still discussing it in meetings that ended with...decisions to have more meetings. (Pfeffer and Sutton, 1999)

This problem can be seen at all walks of life. A child can get a scolding from his/her parents for poor performance on a report card, and a semester later, receive the same rebuke for doing it again. Nothing changed. A child and a company are very different; the "management" of both varies as well. To pinpoint the reason for this inertia in the child is the topic for a different paper, though the problems with the company can be any one of a few, such as: the over-abundance of information, complacency, a natural human inertia,

letting talk substitute for action, and the smart-talk trap.

There is too much information in our society. Hundreds upon hundreds of books, journals, and articles are published each year, which deal with general management concepts, and specific management problem solving. Every weekend is another seminar; every Tom, Dick, and Harry is a consultant. And that is just external information. Within, a company may have piles of reports, status checks, satisfaction surveys, and a variety of other tools the company may have as their internal analysis. Confronted with all this information and all this know-how, managers may be prone to consider: “Hey great, let’s just wait until the numbers, statistics, and graphs tell us what to do!” waiting and never actually doing anything. They feel that the information they need is just a study away and instead of applying their findings, they anxiously wait for the next good-idea, or indicator to guide them. An abundance of know-how and ready-made solutions is an excellent characteristic for a company to acquire, but only to complement an entrepreneurial spirit, not to supplement it.

Complacency can also be the cause of increasing the “gap” among managers. Many are comfortable in the jobs they do, do not mind the routine, and are wary of *rocking the boat* with a new idea, or innovation. Who knows? If it is their idea, or rather helping another's idea come to life, they run the risk of having to be personally involved! They are paid well enough and receive admirable benefits to leave well enough alone. A fear of criticism can also make managers complacent. A 1994 poll of 2,400 employed adults by Princeton Survey Research Associates found that one in six workers claims to have withheld a suggestion about improving work efficiency “out of fear that it would cost someone their job.” (Pfeffer 2000) What about your own job? How much more so would that fear be projected into complacency!

A human inertia. This one is similar to complacency, but is more a human condition than a manager-specific one. The Merriam-Webster Dictionary defines inertia as “a property of matter, whereby it remains at rest or continues, in uniform motion unless acted upon by some outside force.” There is a basic physical propensity to pay no attention to and disregard that which requires an extra modicum of unnecessary effort.

This propensity exists in the business world as well.

Allowing talk to substitute for action. This is expressed brilliantly in a poem by T.S. Eliot in the “Hollow Men” as quoted by Pfeffer and Sutton (May, 99), which illustrates this point: "Between the conception /And the creation / Falls the shadow." This "shadow" is all the empty words that separate the idea from the action. It includes the proposals ignored, the deadlines missed, and the like. Talk is easy, there's very little risk involved. But just talk, as we know, is cheap.

Lastly, but I feel most importantly, is what is known as the smart-talk trap, the phenomenon where people speak too often and in an overly complex manner. Why do they do that? What’s wrong with it? We shall see.

One cause for this smart-talking trend lies in our schooling. We are taught that class participation is an essential part of the grade. And that each word contributed during class brings us one step closer to meriting an A. Sound like an A, get an A. Use whatever buzzwords it takes. Another problem is that classroom problems, which are usually taken from real-life management quandaries, are being solved with the mere words contained in a students answer. “What would you do if...?”, “Well, I would....”, you “would”, won't make a manager, I “did” will. Real-life problems require real-life solutions.

Even after school, people in their jobs see talking as a positive thing. The more someone says, the more that person must know, and the more important that person is to our company. Pfeffer and Sutton quote Bernard Bass, in his book: “Bass and Stogdill's Handbook of Leadership” who calls this the “blabbermouth” theory of leadership. The theory states that people who talk longer and more often - regardless of the quality of their comments - are more likely to emerge as leaders of new groups, to be identified as leaders by observers of the group, to be viewed as influential by both group members and outsiders, and to have greater influence on group decisions. We have all been at meetings and have conceded to the speaker with the extensive vocabulary and the intimidating manner - even if we know he or she is wrong - since we are afraid to acknowledge that we know better, and assume that anyone with the confidence to use such a vocabulary must know what they are talking about.

Besides for looking good, talking smart pays, as well. When executives have to decide who to hire, fire, promote, assign, and the like, on what is their decision based? In a massive and global company, how can one really know the individual actions of a candidate? It can be very difficult. Therefore, they rely on how the person sounds and presents himself. As a result, why bother with doing the work; just make sure you sound like you do it. All of the above are reasons why managers may find themselves talking the talk, but not walking the walk. Thus, a knowing-doing gap occurs.

It is very hard to blame people for their smart-talk. It's almost Darwinian Survival of the Fittest; to do well, you've got to talk. But there can be negative aspects as well. Over-complexity can make you miss the point. For example, take a scenario from The Managers Bible:

> A large Company drew up plans for a spectacular new die-casting plant to make parts for its new outboard motor. Management wanted the finest fully automated die-casting plant in the country. The chief industrial engineer was given the job of touring the country to find the ultimate in automation. When he came back, he said that full automation was indeed workable, but that the knottiest problem was devising an automatic conveyer system for carting off metal scrap from the die-casting machines. Studies then showed that it would be possible to automate the scrap handling, but it would require an additional investment of $180,000. However, there was a happy ending. The final solution to the scrap disposal problem: one man with a wheelbarrow. (Heyel, 1981)

The story is almost comical, but what we see is, keeping it simple is often the most intelligent way to go. It is understandable as well, where the problem of over-complexity in proposals is based. It is the attitude that if a plan is simple, then everyone must be doing it, even our competition, so we must devise something innovative and unique to compete. They are wrong inasmuch as the plan need not be more unique than the competition's; it just needs to be properly implemented.

Recommendation

There can be no one-step solution to the possible problems highlighted here. Their causes can be too many and often difficult to pinpoint. In regard to the smart-talk trap, the solution cannot be to refrain from including one's insights and remaining mute, or to tone down what you do say. The aim though, is that, talk is cheap when unaccompanied by action. Here are a few solutions and ways to close this breach and to thwart such a situation before it occurs.

Start at the beginning. Business schools and undergraduate business programs should focus on the "how", not "why". They should not let the class revolve around only hypothetical scenarios and theoretical resolutions but should be more skills-oriented. Instead of a professor lecturing on what is the best way to interview, the professor should rather make the student take part in a role-play. Compel the student to give an interview. Then the student would be forced to implement the theoretical into practice. Possibly another exercise should be for the student to establish a business and use what he/she has learned in class to maintain it running smoothly and profitable. A project of this scope would certainly overcome the limitations of the classroom setting, and would promote the attitude of "getting it done."

To avoid the problem of all talk and no action, a company can implement certain rules and regulations that would deal with the proposals and ideas of its staff. For example, a company can avoid unfulfilled commitments, by taking action against the employee who made that empty commitment. Cut his/her pay. Take a vacation day away. On the other hand, reward the prompt fulfillment of promises with bonuses and additional incentives. This will have a two-fold positive result: it will encourage people to propose innovative ideas in the first place, and assure that those ideas come to fruition.

Leadership must set an example. The leaders of a company must have a first-hand knowledge of what their company does, day to day. This sounds effortless, but I can assure you that the chairman of AT&T does not know the inner workings of a phone. There is less likelihood that leaders familiar with the workings of the company will be deceived by smart-talk. They will know what the employee is proposing and the possibility of it coming to fruition, or if it is just unfilled pledges proposed simply to

impress. Another positive characteristic of managers is that they be “doers.” They should be seen in situations of action, so that workers can learn from example how precisely a company is run. Companies must overlook (the attitude of) “‘What *can* we do to achieve peak business performance?' but rather think, 'What *must* we do to achieve peak business performance?’” (Redwood, Goldwasser, Street, 1999). A company must ingrain in its culture a concentration on do, do, do, from the upper echelons of management to the lowest level of maintenance.

A company’s purpose is to maximize shareholders wealth. These content attitudes can be the undoing for this function, if not ameliorated. Companies require a constant flow of innovative ideas and solutions to stay afloat amongst the competition. Ideas alone are not enough. Without action, companies will by no means solve their problems. Words cannot be deposited in the bank. Leaders must not only discuss and postulate what the implications of these problems might be, but to diagnose if their company does indeed suffer from these tribulations and what they will *do* to solve them.

Conclusion

I bent the truth. In the Background to this paper, I blamed this problem on a student in one of my past management classes. That anonymous student was me. I remember pondering as I delivered that management soliloquy: “What am I saying?”, “Is the teacher believing this?”. It was not until I witnessed it again in another class, with another student, that I began to really begin to think that there could be a broader problem. Had I not done this research, I am not sure that I would have been able to avoid a knowing-doing gap, or a smart-talk trap of my own. I might have become one who would value his words more than his actions. Having examined this issue thoroughly, I now realize that these ills are real, and must be dealt with in order to insure a company’s survival. Being cognizant of these points is the optimal way to combat these issues.

It is my personal piece of advice, that the best way for solving these problems are to simply publicize the concepts which I have discussed. Realizing their existence and making people aware, is the first way to induce a change. I have. No longer will I just say

or propose without asking myself if I would indeed carry out that which I am suggesting. Awareness and a little introspection will then allow managerial candidates to be able to become the manager that companies need - the knowing *and* doing ones.

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The Ins and Outs of a Marketing Plan

By: Chaya Brook

Marketing plays a vital role in successful business ventures. How well the plan you develop markets your business, along with the management and financial management plans, will ultimately determine your degree of success or failure. The key elements of a successful marketing plan are to 1) know your customers -- their likes, dislikes and expectations, and 2) to know your competitors -- their strengths and weaknesses. By identifying these factors, you can develop a marketing strategy that will allow you to arouse and fulfill customers needs, better understand competitors and identify changes in the marketplace that can affect your bottom line.

The purpose of the marketing plan is to define your market, i.e., identify your customers and competitors, to outline a strategy for attracting and keeping customers and to identify and anticipate change. Your business will not succeed simply because you want it to succeed. It takes careful planning and a thorough understanding of the marketplace to develop a strategy that will ensure success. This plan is extremely important for the success of your business because it sets down your ideas, so the business is focused.

Understanding the Marketplace

Generally, the first and most important step in understanding the market is to study it through market research. In the case of a franchise, the franchiser has developed a marketing program, so you will need to review the program he or she has provided. Look over the plan to determine what product/service you will offer and write a description of it. Even though a franchiser has described your product or service, it is a good idea to develop and write your own description because this process helps you to know your product or service--a key variable in any successful marketing plan. When describing your products or services, outline what you feel are its unique aspects, and explain how or why these aspects will appeal to customers. Emphasize the special

features that you feel are its selling points. These features are what you will use to convince customers to purchase your product or service.

Next go over sales projections, determining if there is a demand for the product or service. In the case of a franchise, the franchiser will have developed the projections. Study this data to see how he or she arrived at these projections. This will help you to better understand how the marketplace operates relative to your product/service, and it can help you develop the skills necessary to identify and anticipate changes in the marketplace. Generally, a growing market is more desirable. Not only is there great sales potential, but it is usually easier to enter and build sales in a growing marketplace than it is to supplant competition in flattening or shrinking marketplaces.

For a very small firm, however, a large market can be a double-edged sword. On the positive side, of course, there is the potential for huge sales. Negatively, though, larger firms with established access to marketing channels and better financing may be tempted to enter such an attractive marketplace. Firms already involved in the particular industry may devote considerable resources to defending or increasing their current market share.

Start your own file on marketplace trends. Periodically review your data, looking for shifts in the market. If changes are occurring, you should modify the marketing plan to coincide with these changes. In franchise operations, it is customary for the franchiser to update the marketing plan periodically to reflect changes in the marketplace and to keep the marketing program current.

<u>A marketing plan should answer these questions</u>:

* Is this product or service in constant demand?
* What kind of appeal does this product have?
* How many competitors provide the same product or service?
* What is the customers basic need?
* Can you create a demand for your service or product?
* Can you effectively compete in price, quality and delivery?

* If a franchise, will the franchiser price the product or service to give you the projected profit?

Review your program to ensure that it answers these questions. If your plan doesn't answer the questions, it will need to be modified, or you will need to devise a strategy that will provide a means for answering them. When you are satisfied that you understand the program, how the market operates and how to identify market shifts and trends, start writing the marketing section of your business plan.

Even if you adopt a marketing program that has been developed elsewhere, it is your responsibility to promote your product or service by cultivating the marketplace, i.e., attracting and keeping customers. You can accomplish this aim by knowing your market, your customers, your competitors and your product/ service. Don't rely solely on the program provided by a franchiser or others, gather and assess your own data using the techniques outlined in your plan. By gathering and analyzing this information, you will be better able to determine if your program is in line with your competitors, if it is in line with industry averages and what adjustments you can make to improve your overall competitiveness.

Market Segmentation

Almost all markets have some major and distinctive segments. Even if a market isn't currently segmented, it probably carries that potential. And, in the case of large national markets, it would be almost impossible for a small firm to be competitive unless the market were segmented.

Segmentation can come about in many ways. Often several types of segmentation are evident. Almost all markets can be segmented by price and quality points. So price and quality issues may not form the most clear and precise definition of segmentation within a marketplace. Reasons for strong segmentation are most often found through an examination of product use and the benefits consumers derive from product use.

For example, the personal automotive car market may be thought of as being divided into station wagons, sedans, pickup trucks, mini-vans, and sports cars. Price and

quality may further divide each of these segmented categories. With the luxury sedan segment, for instance, a change in the pricing or quality of pickup trucks would have no competitive impact because the potential consumer for a luxury sedan isn't weighing a decision between purchasing a sedan or a pickup. However, if mid-price sedans are dramatically upgraded in quality, they may become competition for the luxury sedan market. This happened in the luxury car market in the early 1990s. Offerings from Infiniti and Lexus caught the attention of consumers who had previously only considered the more expensive cars manufactured by Mercedes, BMW, and Jaguar.

Market Research

Strategies for Researching the Market

Researching your market is perhaps the easiest way to assess it. Market research does not have to be costly, nor does it have to be a complex process. It can be as simple and as easy as surveying a cross-section of your consumers (focus group) to get their opinions about the product or service you will be offering, or conducting a telephone or mail survey. The disadvantage of using the telephone or mail survey method is that the individuals you contact may not be interested in responding to a survey. Other market research techniques include analyzing demographic data, such as population growth/decline rate, age range, sex, income/educational level; brainstorming with family and friends, and focus group interviews. Whatever method you use, your focus should be on gathering enough information to determine who your potential customers are--their needs, wants and expectations; if there is a demand for your product or service; who your competitors are, and how well they are doing.

Market research should answer questions such as:

* Who are your customers and potential customers?
* What kind of people are they?
* Where do they live?
* Can and will they buy the product or service you are offering?
* Are you offering the kinds of goods or services they want -- at the best place, the best

time and best amounts?

* Are your prices consistent with what the buyers view as the products' values?
* Are you applying the promotional programs in a way that will bring about success?
* What do customers think of your franchise?
* Who are your competitors?
* If a franchise, how does your operation compare with the competition?

While there are some disadvantages to market research—it may be a costly and time-consuming process, there exist built-in biases that may distort information, it ignores answers or lets arrogance or hostility cut off communications at some point in the marketing process--the advantages, however, outweigh the disadvantages. Don't forego this process or stop halfway because you are not getting the desired results. This may be an indication that you are going into the wrong business or that there isn't a market for your product or service. Don't be discouraged. You simply may need to modify your original plan.

A few of the benefits of market research are outlined below.

* Learning who your customers are and what they want.
* Learning how to reach your customer and how frequently you should try to communicate with them.
* Learning which appeals are most effective and which ones aren't.
* Learning the relative successes of different marketing strategies in relation to their return on investment.

While market research may appear to be a tedious, time-consuming process, it is necessary if you want to be successful. Think of market research as simply a method of finding out what catches customers' attention by observing their actions and drawing conclusions from what you see, and as an organized way of finding objective answers to questions every business owner and manager must answer in order to succeed. Market research focuses and organizes marketing information, ensuring that it is timely and that it provides what you need to:

* Reduce business risks.

* Spot problems and potential problems in your current market.
* Identify and profit from sales opportunities.
* Get basic facts about your markets to help you make better decisions and set up plans of action.

If viewed from this standpoint, market research is an invaluable tool that can save you time, effort and money.

What Does A Marketing Plan Contain?

Many first-time business owners think that by simply placing an ad in a local newspaper or a commercial on a radio or a television station, customers will automatically flock to purchase their product or service. This is true to a certain extent. Some people are likely to learn about your product or service and try it, just out of curiosity. But hundreds, even thousands, of other potential customers may never learn of your business. Just think of the money you'll lose, simply because you didn't develop an adequate marketing program!

Marketing is an essential part of business operations. And, it oftentimes determines how successful your business will be. What you as a potential business owner must do is maintain a thorough understanding of the marketing program, and use it to extract advantages from the marketplace. Go over the strategies and techniques until you understand how to apply them to get the results you desire. Remember, your aim is not only to attract and keep a steady group of loyal customers, but also to expand your customer base by identifying and attracting, new customers and to reduce risks by anticipating market shifts that can affect your bottom line.

To help you accomplish this aim, your marketing plan should include strategies typical of any marketing plan. The plan should especially include what marketeers dub as the 4 P's of Marketing - PRODUCT/SERVICE, PRICE, PLACE AND PROMOTION. Make certain your plan contains the strategies listed below, then determine how these strategies are applied. Include a brief explanation for each strategy in your plan.

* Describe the target market by:

- age
- sex
- profession/career
- income level
- educational level
- residence

Identify and describe your customers (target market) by their age, sex, income/educational levels, profession/career and residence. Know your customers better than you know anyone--their likes, dislikes, and expectations. Since you will have limited resources target only those customers who are more likely to purchase your product or service. As your franchise grows and your customer base expands, then, you may need to consider modifying this section of the marketing plan to include other customers.

* Identify Competition

- market research data
- demand for product or service
- nearest direct and indirect competitors
- strengths and weaknesses of competitors
- assessment of how competitors businesses are doing
- description of the unique features of your product or service
- similarities and dissimilarities between your product or service and competitor's
- pricing strategy for and comparison of yours and the competition's.

Identify the five nearest direct competitors and the indirect competitors. Start a file on each identifying their weaknesses and strengths. Keep files on their advertising and promotional materials and their pricing strategies. Review these files periodically determining when and how often they advertise, sponsor promotions and offer sales.

* Describe Product/Service

Try to describe the benefits of your goods or services from your customer's perspective. Emphasize its special features--i.e., the selling points. Successful business

owners know or at least have an idea of what their customers what or expect from them. This type of anticipation can be helpful in building customer satisfaction and loyalty.

* Develop Marketing Budget

- advertising and promotional plan
- costs allocated for advertising and promotions
- advertising and promotional materials
- list of advertising media to be used.

Operating an effective marketing plan requires money, so you will have to allocate funds from your operating budget to cover advertising, promotional and all other costs associated with marketing. Develop a marketing budget based on the cost for the media you will use, and the cost for collecting research data and monitoring shifts in the marketplace.

* Describe Location (Place)

- description of the location
- advantages and disadvantages of location.

Again, try to describe the location of your business from the customer's perspective. Describe its assets -- i.e., the convenience, whether or not public transportation is accessible, the safety aspects--street lighting, well lit parking lot or facility, decor, etc. Your location should be built around your customers, it should be accessible and should provide a sense of security. An advantage of purchasing a franchise isthat the franchiser oftentimes assists in site selection and decorating.

* Develop Pricing strategy

- pricing techniques and brief description of these techniques
- retail costing and pricing
- competitive position
- pricing below competition
- pricing above competition
- price lining
- multiple pricing

- service costs and pricing (for service businesses only)
- service components
- material costs
- labor costs
- overhead costs

Although your pricing strategy may be based on the strategy devised by others, you should study this plan and the strategies used by competitors. That way you will acquire a thorough understanding of how to price your product or service, and you can determine if your prices are in line with competitors, and if they are in line with industry averages and what adjustments you can make to bring them in line. The key to success is to have a well-planned strategy, to establish your policies and to constantly monitor prices and operating costs to ensure profits. Keep abreast of changes in the marketplace because these changes can affect your bottom line.

* Develop an effective Promotional Strategy

- advertising media
- print media (newspaper, magazine, classified ads, Yellow Pages advertising, brochure)
- radio
- television
- networking
- business cards
- tee shirts, hats, buttons, pens.

Develop a promotional strategy that uses various media for promoting your business. Monitor the different media identifying those that most effectively promote your business. Concentrate on developing material for these formats that clearly identifies your goods or services, its location and price.

Since financial institutions weigh the soundness of your marketing plan when deciding whether your business is a good risk for their money, it is important that you

prepare and present credible market data that shows there is a need in the community for your business and that demonstrates your ability to compete successfully.

Advantages and Disadvantages of a Marketing Plan

A well-written, comprehensive marketing plan is the focal point of all business ventures because it describes how you plan to attract and retain customers--the most crucial aspect of a business. And why are customers so important? The answer is simple. They ultimately are the means by which you will generate the income needed for daily operations, to repay debts and to turn a profit. In essence, the customers are your lifeline and the marketing plan is the pipeline that allows you access to them -- i.e., to fulfill their needs and expectations.

The marketing plan is essential to any successful business. It is the heart of the business, the basis from which all other operational and management plans are derived. Marketing offers you a wealth of information that if applied correctly virtually can ensure your success. Therefore, it is important to develop a comprehensive, effective marketing plan.

An effective marketing plan will certainly boost your sales and increase your profit margins, which is the goal of every business owner. It is a milepost down the road to success and, as such, care and time should be put into its development. You must be able to convince customers that you have the best product or service for them at the best possible price. If you cannot convince potential customers of this, then you are wasting your time and money. This is where the marketing plan comes into play, and this is why it is so important.

There are numerous advantages you can extract from the marketplace if you know how. The marketing plan is an excellent tool for identifying and developing strategies for extracting these advantages. A few of the advantages are outlined below.

The plan:

* Identifies needs and wants of consumers.

* Determines demand for product or service.

* Aids in design of products/services that fulfill consumers needs.
* Outlines measures for generating the cash for daily operation, to repay debts and to turn a profit.
* Identifies competitors and analyzes your firm's competitive advantage.
* Identifies new product/service areas.
* Identifies new and/or potential customers.
* Allows for test to see if strategies are giving the desired results.

<u>Some of the disadvantages of the market plan are:</u>

* Identifies weaknesses in your business skills.
* Leads to faulty marketing decisions based on improperly analyzed data.
* Creates unrealistic financial projections if information is interpreted incorrectly.
* Identifies weaknesses in your overall business plan.

The marketing plan offers numerous advantages; however, as you can see, there can be drawbacks. Remember, however, the advantages outweigh the drawbacks, so it is advisable to seek professional assistance when you are developing the marketing section of your business plan. It will be worth the investment.

Developing An Effective Marketing Strategy

An advantage of purchasing a franchise is that the franchiser provides the marketing plan. While this saves you the time and energy it takes putting together a marketing program, it doesn't however, ensure that you will attract customers to your franchise. How well your advertisements and promotions draw customers will ultimately determine how effective your marketing strategy is.

While a reputable franchiser will not sell you a franchise in a territory where there is not a market, or where the market is declining, it is your responsibility to cultivate your designated market. Whether you are independent or a franchise, one of the easiest ways to do this is through advertising and promotions. Remember, the aim of the advertising and promotional strategy is to create awareness of your product or service, to arouse

customers' needs and expectations to the point of consumption, and to create a loyal stream of satisfied customers who will continue to patronize your business.

Effective Advertising and Promotions Techniques

Perhaps, the first step in developing an effective advertising and promotional strategy is to understand the difference between the two concepts. Most people think that advertising and promotions are one in the same; there is, however, a distinction between the two. While both advertising and promotions use the different media formats - print, radio and television - as a way of conveying a message, promotion encompasses much more. It is the method of advertising and it can entail community involvement. This could mean sponsoring a Boy or Girl Scout troop, allowing non-profit organizations to use your facility, such as, letting the high school drama club use your parking lot for a car wash fund raiser, sending an underprivileged child to day camp or involvement in any type of positive community activity that will bring attention to your business.

While advertising is a way of keeping your business is the public's eye, promotions are a way of signaling that you are concerned and committed to the welfare of the community and its residents. This commitment may be one of the most effective techniques for building customer loyalty. People tend to be more supportive of businesses and organizations that give something to the community rather than those that just take from the community, never giving anything in return.

Now, let's look at how to develop an effective advertising program and promotional program for your business.

The Key to a Successful Advertising and Promotional Plan

Advertising

Advertising plays an important role in successful business ventures. It entails identifying and selecting the media that provide the greatest amount of exposure for your business and developing effective, yet appropriate materials for each medium. It is more than running an ad in a local newspaper, on a radio or television station or just simply

hanging a sign outside your business and waiting for the customers to purchase your product or service. It requires that you know the selling points of your product or service, and that you develop literature that can arouse the customers' consciousness levels to the point that they are curious enough to investigate it, and then raises their need or desire levels to the point that they are willing to purchase it.

Advertising keeps your product or service in the public's eye by creating a sense of awareness. Yet this awareness alone will not ensure the success of your business. Thus, advertising not only has to be effective, it also has to be a continuous process.

When developing an effective advertising strategy for a franchise, review the national advertising materials the franchiser has developed, and determine if they can be applied regionally or locally. If they can, select the media that will provide the greatest amount of exposure and the most effective means for promoting your franchise. If the national materials are inappropriate, you may need to modify or develop your own materials. Remember, however, that you may have to get the franchiser’s approval to use these materials. As a courtesy, regardless of the advertising policies in the franchise agreement, allow the franchiser to review these materials.

Once you are satisfied with the advertising materials, select the media that will best market your business. Since advertising can be costly, try to use a medium that is cost effective, yet will effectively market your business. If this is not possible, then be prepared to spend what is necessary to promote your business effectively - the outcome will be worth the investment.

It may be a good idea to mix the different media formats that you use. For example, design a brochure that describes your product or service, emphasizing its selling points (special features). Place copies of the brochure in strategic locations of your business to use as customer handouts. Or, devise a customer survey. The survey should focus on whether customers like the product or service, the quality of the product/service, ways to improve it, the quality of service provided by staff--their friendliness and courtesy. Place the survey with a self-addressed, stamped envelope near the check-out counter and ask customers to mail in or return the survey when they come back. Review

their comments with staff and implement those suggestions that are practical, cost efficient and can improve the overall quality of service your business provides.

Other media formats to use are:

* Newspaper, radio or television ads (newspaper advertising is the least expensive and television advertising is the most expensive of these formats).
* Business cards.
* Classified ads in the local newspaper.
* Direct marketing.
* Telemarketing (this format can be expensive).
* Yellow Pages advertising.
* Sampling - mailing or distributing free samples of your product or a flyer about your service to the public.
* Advertising in community-based magazines or newspapers.

Whatever media format you use, be willing to invest the money needed to develop an effective ad campaign.

Promotions

As discussed earlier, promotion entails more than just selecting the media format to market your business. It can, and oftentimes does, encompass community involvement. This involvement can range from sponsoring a Boy or Girl Scout troop to hosting a charity ball for senior citizens, or allowing non-profit organizations to use your facilities. Your approach to promoting your business should encompass more than creating a sense of awareness about your business. It should include a commitment to community involvement--the desire to give something back to the community and its residents. An excellent way to foster this type of involvement is to meet with community leaders to find out how you can help, and what events are forthcoming that could or will require your assistance. Keep in mind that community leaders can be an excellent networking tool, especially if they feel your involvement is genuine.

Examples of community programs you can sponsor or take part in are:

* Sponsor a Boy or Girl Scout troop for summer camp

* Sponsor a underprivileged child in day camp
* Host and sponsor a charity ball for senior citizens
* Sponsor cooperative education for high school and/or college students
* Volunteer as a tutor for at-risk (those likely to drop out or fail in school) students
* Sponsor a fundraiser for the homeless, or day care tuition assistance for children of single-parent households
* Offer summer employment to local high school, middle school and college students
* Become active in the local chapters of the Big Bothers or Big Sisters organizations.
* Volunteer in a local literacy program.

<u>Other inexpensive ways of promoting your business that doesn't encompass community involvement are:</u>

* Employee tee shirts, hats, aprons or jackets with the name of your business and logo.
* Ball point pens with the name, telephone number and logo of your business.
* Balloons with the name, telephone number and logo of your business
* Free samples
* A door prize for the 100th or 1,000th customer to enter your business.

While it is impossible for you to participate in every event or program in the community, you should at least get involved in one or two activities, even if it's only on a part-time basis. People tend to be more supportive of businesses, organizations or individuals who give something to the community. And, this is the image you especially want to project in your promotional activities.

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The United States Currency and its Financial System

By: Ester Weiss

John Kenneth Galbraith, U.S. economist said the following about money:

"Money is a singular thing. It ranks with love as a man's great source of joy, and with death as his greatest source of anxiety. Over all history it has oppressed nearly all people in one of two ways: either it has been abundant and very unreliable, or reliable and very scarce."

I believe history has proven, since the genesis of our nation, that money has been able to "oppress" even men that have been bestowed with the most prestigious titles our country can offer, the presidency of the United States of America. A president's popularity is primarily dependent on the stability of money and the condition of the economy during his years in office.

Why should money be the primary determinant of the success of a presidency? Money is what makes the financial system work, it is a measure of wealth, a medium of exchange - it can be used to purchase goods and services, it is acceptable to repay debts. Creating and transferring money are integral parts of the capital formation process. However, too much money in an economy is associated with unsustainable economic growth and rapidly rising prices. On the other hand, too little money in an economy is associated with poor economic performance and sometimes recession. I find this idea legitimized by the presidency of Jimmy Carter. Carter is considered one of the worst presidents to have served our country, despite his striding in human rights and relatively good foreign policy: tremendous economic instability and exorbitant inflationary percentages, will forever tarnish his presidency in the eyes of the American people. Ernest Hemingway summed it up by saying: "The first panacea for a mismanaged nation is inflation of the currency, the second is war. Both bring a temporary prosperity, both bring a permanent ruin. Both are the refuge of political and economic opportunists."

Therefore, it is so important for our nation to have broad based economic objectives, mechanisms for achieving these objectives, and a system of checks and

balances to ensure that policy makers will operate in the best interests of the citizens of the United States. National economic policy should focus on achieving economic growth, high employment, price stability, and a balance in international payments or transactions.

In the following report I will conduct an in depth analysis of a number of economic policies initiated and adapted by various presidents and delineate their levels of success, accomplishment and acceptance among our countries citizens.

The Great Depression and Herbert Hoover's Trickle Down Policy.

Herbert Hoover had been a millionaire businessman and a successful public official before he became president. He entered the White house at a time of great prosperity in the United States. Americans expected him to lead them on to even better days. In the election campaign, Hoover spoke hopefully about increasing prosperity. He observed, *" The slogan of progress is changing from the full dinner pail to the full garage,"* and during his inauguration he remarked, *"Ours is a land rich in resources…in no nation are the fruits of accomplishment more secure."* Then, seven months after he took office, the stock market crashed and the Great Depression began. The United States had been building up to a crash for a long time. The economy was weakened by widespread buying on credit. Thousands of people had borrowed money to pay for stocks. Stock prices soared to record heights. By the end of 1929 the crash had caused losses estimated at $40 billion. The values of stocks listed on the New York Stock Exchange had dropped 40 percent. Fortunes had been wiped out. By 1932, more than 12 million Americans were out of work. Factories closed and many banks failed. Thousands of people lost their homes because they could not keep up their mortgage payments. Many families lived in clumps of shacks known as *"Hoovervilles."*

In February 1931, Hoover declared, *"I am willing to pledge myself that if the time should ever come that the voluntary agencies of the country together with the local and state government are unable to find resources with which to prevent hunger and suffering in my country, I will ask the aid of every resource of the federal government…but I have faith in the American people that such a day would never come."* Herbert Hoover was

wrong, that infamous day did arrive and when it did Hoover did not *"ask the aid of every resource of the federal government."*

Americans asked the president to help them, but the federal government had never created jobs to help people, housed the homeless, or fed the starving. Hoover wasn't willing to start such novel programs. He sincerely believed that the nation's lawmakers and officials should not interfere in the lives of its citizens. Hoover felt that such interference would cause people to lose their freedom and their ability to help themselves, two qualities that had made the nation great.

He believed that Charles Darwin's theory of *"rugged individualism"* is the foundation of American life. Hoover felt the government should assist citizens by helping them rise above their poverty using their own capabilities. This policy can clearly be seen by the fact that he endorsed a $45 million appropriation to feed the livestock of Arkansas farmers, during the 1930 drought but rejected a grant of $25 million for food for the farmers and their families.

Hoover allowed businesses to borrow money with great ease and he urged business executives to keep up production, prices and wages, which he thought would lead to a corporate revival and decrease the downsizing trend. He operated on the theory that as businesses recovered, the economic benefits would "trickle down" to the people in the form of jobs and wages

I believe, that the fact that Hoover was a self-made millionaire led him to believe that every person could do the same, which fueled his beliefs in rugged individualism. Hoover remarked in one of his speeches, *"Victory over this depression and over difficulties will be won by the resolution of our people to fight their own battles in their own communities by stimulating their ingenuity to solve their own problems, by taking new courage to be masters of their own destiny in the struggle for life. This is not the easy way, but it is the American way."*

Franklin Delano Roosevelt's New Deal

The American people were so disappointed with Hoover that by the time the 1933

elections rolled around, the Democratic candidate FDR, won by one of the most considerable landslides U.S. history had ever known. FDR's approach to economics was a more people oriented one than that of Hoover.

In FDR's acceptance speech to the 1932 Democratic Convention, he said, "*Those millions shall not hope in vain. I pledge you – I pledge myself to a new deal for the American people*." This was the introduction of Roosevelt's famous economic and social reform, the New Deal.

Roosevelt's New Deal Program aided the lower class, poor and needy citizens directly. The objectives of the program were relief for suffering people, recovery of the economy to rebuild itself and reform movements to insure our country against future depression. FDR firmly believed that the government must try to protect its citizens from personal disaster. His goal was that *"no American would be allowed to perish through neglect or indifference."*

President Roosevelt believed in taking action to reform the economy. He once told his cabinet members, *"Take a method and try it. If it fails try another, but above all try something!"* His many programs and agencies prove his willingness for action to solve the problems of the depression. He promoted The Federal Emergency Relief Act to provide money and employment for the poverty stricken, homeless, and unemployed. He initiated The National Industry Recovery Act, which set standard regulations for corporations and industries. FDR's most well known program is one that remains at the center of presidential debates till today, and is the cause of much controversy, his Social Security Act. The Social Security Act is an entitlement program, which at its inception provided pension for the elderly, unemployed, and handicapped. (It has long been revised over the years). These programs and many more prove his conviction to the American people, and his strong desire to assist those affected by the depression.

F.D.R. believed in the Prime Pumping Method. He thought the government should distribute money to the poor on the premise that their spending will cause business to flourish and ultimately raise the economy. He believed in lifting the morale of the people and he tried to imbue the public with feelings of optimism and security.

President Roosevelt's economic policy is reflected in the words he spoke at the 1936 Democratic presidential nominations, *"Governments can err; Presidents do make mistakes....but better the occasional faults of a Government that lives in a spirit of charity than the consistent omissions of a Government frozen in the ice of its own indifference."*

Ronald Reagan's Supply Side Economics

President Reagan once remarked, *"In this present crisis government is not the solution to our problem --- government is the problem."* Reagan inherited a weak economy --- one if the nation's most pressing problems at that time. He blamed the government for causing inflation and economic crisis by spending excessive amounts of money on various social programs. Reagan aimed at reducing government interference in the private people. He called his domestic agenda the New Federalism.

Reagan believed that the states and local governments are closer to the people and therefore can know their needs and better provide programs to assist them. He gave the federal welfare, food stamps, job training, and education programs to the states in exchange for money to finance the programs. Reagan's economic policy was referred to as "Supply-Side Economics*"* or *"Reaganomics."* He claimed that many of the economic problems were caused by extremely high taxes. High taxes prevented people from investing money in productive businesses. Reagan proposed a large tax cut for wealthy individuals and corporations so they can use their savings to invest in more businesses. This would cause the businesses to hire more workers, which results in an increase of supply and ultimately lead to a decline of inflation and economic problems. Supply-siders said the general population would eventually prosper as the new growth *"trickled down"* in the form of new employment. These ideas were similar to those used during Hoover's Administration. Supply-siders theorized the increased employment would expand demand (consumer spending power). Congress supported the basic plan.

Though Reagan created a large income tax cut, he increased other taxes, especially social security. This raised taxes for most individuals. He also spent a great

deal of money on the military, which created a tremendous deficit and a recession in 1991.

Reagan's economic policy was one of not involving the federal government in programs for specific causes. His policy was reflected when he told a group of Cuban American's in Miami that no special programs were needed for Hispanics or other depressed groups, because *"a rising tide lifts all boats."* Although some critics denounced Reagan's domestic agenda and economic policies, his personal popularity remained high.

Analysis of the 3 most Controversial Economic Policies.

Presidents are entitled to their beliefs and independence in the economic policies they seek. However, I feel that it is essential for a president to accept failure and move on. Hoover and Roosevelt, both initiated fine economic policies, but what made Roosevelt a phenomenal president and Hoover an awful one, was the fact that when Roosevelt realized his theories weren't taking off the way he thought they would, he revamped his policies. Hoover on the other hand could not admit failure, and stuck by his policies despite the fact that they were unsuccessful.

The economic policies of the president's had different effects on different people. Roosevelt's economic policies were beneficial to the poor and detrimental to the rich. The wealthy conservatives hated Roosevelt and his policies. They would not say his name. They referred to him as *"that man."* Hoover was disliked by the poor because he favored the rich and did not help the underprivileged. They blamed Hoover for the depression. As the economy declined in the 1980's many people compared Hoover and Reagan. In September 1982, House Speaker Tip O'Neill called Reagan *"Hoover with a smile."*

I found it interesting to note, that although Roosevelt's economic policies greatly differed from those of Reagan and Hoover, the end results in all methods was to theoretically benefit all classes. In Hoover's trickle down policy and in Reaganomics, the money was given to businesses on the assumption they would make new investments and

expand their businesses. The expansion would lead to new jobs and an increase in production. The increased production would cause more jobs to be available and therefore cause the unemployed to earn more money. The more money in circulation leads to an increase in demand for goods. Roosevelt's, "Prime Pumping" has the same basic components. This policy, however, starts from the lower class. The government gives the unemployed money, which causes more capital to be in circulation and increases the demand for goods. This leads to investment expansion, which causes new jobs and profits to be made. Theoretically, the ending result in all three cases is the same, but the main difference exists; which class does the government view as the catalyst, and give the money to first.

A president's economic policies are further influenced by the party to which he belongs. Mario Cuomo once remarked at the 1984 Democratic National Convention, *"I have always felt that the difference between Democrats and Republicans has always been measured in courage and confidence. The Republicans believe the wagon train will not make it to the frontier unless some of our old, some of our young and some of our weak are left behind by the side of the trail. The democrats believe, that we can make it all the way with the whole family intact. I feel Franklin Roosevelt proved that to our nation."*

Being a member of the Democratic party, I agree with Mario Cuomo when he said, *"We believe in encouraging the talented, but we believe that while survival of the fittest may be a good working description of the process of evolution, a government of humans should elevate itself to a higher order, one which fills the gap left by chance or a wisdom we don't understand."*

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Getting Technical

By: Zev Brachfeld

"There are two times in a man's life when he should not speculate: when he can't afford it, and when he can." *Mark Twain, 1897*

With the recent boom in technology, in particular the Internet, many new and inexperienced investors have jumped on the Wall Street bandwagon. Trading from their home PC's, these investors helped push the stock markets up through all of 1999, and part of 2000. The Dow Jones Industrial Average gained about 25% between January 1999, and it's high of 11,908 on January 14, 2000, while the NASDAQ Composite Index rose a whopping 120% in the same time period. These indices rose so rapidly because of speculation and forecasts of unreachable future earnings set for the technology sector by Wall Street analysts. Since then, we have seen these same indices lose up to 50% of their value. Institutional investors realized that the performance expected of the emerging Internet companies was unattainable, and sold their positions in the "dot-com" companies. Many beginner investors, not knowing the rules and guidelines of investing smartly and safely got badly burned and lost money when the institutional investors left the tech sector. Had they set goals and boundaries when they invested they could have avoided huge losses, and maybe even have walked away with a profit.

In this report, I will attempt to explain some smart and efficient strategies that I have researched and studied. I chose these specific strategies because they are simple, easy to research, and proven successful over many decades.

The first rule of successful investing is to leave your emotions at the door. William J. O'Neil, the founder of Investors' Business Daily, once remarked, "In my experience, the only way is to establish buying and selling rules derived from historical

research- rules based on how the market *actually* works, not on personal opinions and preconceived ideas."

When an investor gets emotionally involved in his or her investments, it usually ends up as a losing proposition. People do not think rationally when their money is involved. Instead of holding on to a particular security that is pointing in a higher direction, they sell on gut feeling, missing out on great profits. On the other hand, when people feel attached to a particular company, for whatever reason, they will hold on to its stock and suffer such great losses, that it doesn't pay to sell the stock anymore. These are examples of emotional involvement that can be, and usually is very dangerous. Your feelings have an immediate impact on your account equity. You may have a brilliant trading system, but if you feel frightened, arrogant, or upset, your account is sure to suffer.

The way to conquer these feelings is to get educated. Great thinkers have always said, "Education conquers fear." This report will strive to do just that- educate the new and inexperienced players in the market.

There are many different strategies and methods used extensively to determine if a stock should be purchased, and if it is acquired, what price should be paid for it. Most methods usually fall into one of two categories: **fundamental analysis**, and **technical analysis**. In very broad terms, *investors* (long-term), both private and institutional, use fundamental analysis as their basis for stock purchases. Short-term *traders* generally use technical analysis.

Fundamental analysis is the study of a specific company's financial health and future growth potential. It includes such statistics as a stock's annual growth rate, five-year, one-year, or quarterly earnings records, and P/E (price to earnings) ratios. In general, it is for the not-so-intrepid investors who want to have stability and long-term growth from their investments. They do not follow their portfolio on a day-to-day basis, but rather on a long-term basis, which can span many years, and sometimes even decades.

The factors used to determine the health of a company focuses on economic, industry, and company statistics. The typical approach to analyzing a company involves four basic steps:

1. Determine the condition of the general economy.
2. Determine the condition of the industry.
3. Determine the condition of the company.
4. Determine the value of the company's stock.

- **Economic Analysis**

  The economy is studied to determine if overall conditions are good for the stock market. Is inflation a concern? Are interest rates likely to rise or fall? Are consumers spending? Is the trade balance favorable? Is the money supply expanding or contracting? These are just some of the questions that the fundamental analyst would ask to determine if economic conditions are right for the stock market.

- **Industry Analysis**

  The company's industry obviously influences the outlook for the company. Even the best stocks can post mediocre returns if they are in an industry that is struggling. It is often said that a weak stock in a strong industry is preferable to a strong stock in a weak industry.

- **Company Analysis**

Examining the company's financial statements is crucial to fundamental analysis. There are a number of items to look for in these statements. Some of the main items include:

> Net Profit Margin: A company's profitability ratio calculated by dividing net income by total sales. For example, a net profit margin of 30% indicates that $0.30 of every dollar in sales is realized in profits.

> Price/Earnings Ratio: Shows how much an investor must pay to "buy" $1 of the companies earnings. It is calculated by dividing the securities current price by the previous four quarters earnings per share (EPS). For example, if a stock's current price is $20 and the EPS for the last four quarters was $2, the P/E ratio is 10. This means that you must pay $10 to buy $1 of the company's earnings. Of course, investor expectations of the company's future performance play a heavy role in determining a company's current P/E ratio.

>Debt Ratio: A company's debt ratio is a leverage ratio calculated by dividing total liabilities by total assets. This ratio measures the extent to which total assets have been financed with debt. For example, a debt ratio of 40% indicates that 40% of the company's assets have been financed with borrowed funds. Debt is a double-edged sword; during times of economic stress or rising interest rates, companies with a high debt ratio can experience financial problems. However, during good times, debt can enhance profitability by financing growth at a lower cost.

After determining the condition and outlook of the economy, the industry, and the company, the fundamental analyst is prepared to determine if the company's stock is overvalued, undervalued, or correctly valued.

Fundamental analysis is employed by investors that are in for the long haul. The problem with this method is illustrated by the following anecdote told by an avowed technician, Ed Seykota. "One evening, while having dinner with a fundamentalist, I accidentally knocked a sharp knife off the edge of the table. He watched the knife swirl through the air, as it came to rest with the pointed end sticking into his shoe. 'Why didn't

you move your foot?' I exclaimed. 'I was waiting for it to come back up' he replied." Holding onto a stock for the long term can put an investor at a disadvantage for if the value falls, it may never come back up again.

Short-term traders use a different method, which if utilized correctly, can be very profitable even in a down market. Welcome to the world of Technical Analysis.

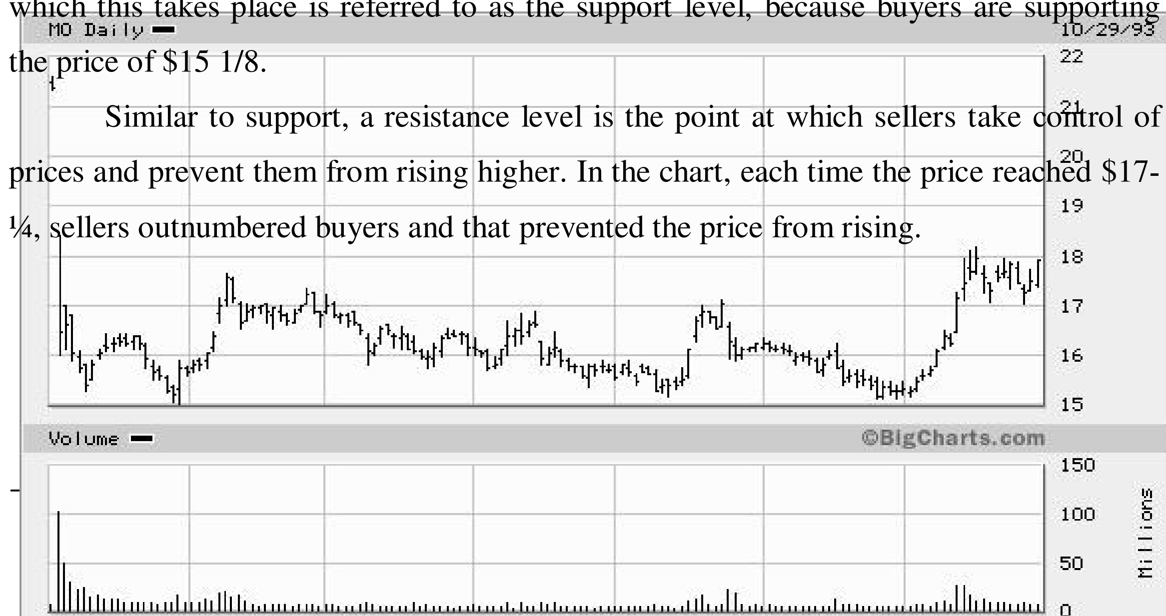
Technical analysis can be defined simply as the study of individual securities and the overall market based on supply and demand. Technicians record, usually in chart form, historical price, and volume activity and deduce from that pictured history the probable future trend of price.

The study of a company's charts is the primary method for doing technical research. Many different sophisticated techniques are used in this field, but I will cover only the most basic ones, which I have employed successfully.

The first things to learn about studying charts are the terms **support** and **resistance.** The best way to understand these terms is to think of security prices as the result of a head-to-head battle between a "bull" (the buyer) and a "bear" (the seller). The bulls push stock prices higher, while the bears push the price lower. The direction the price moves actually reveals who is winning the battle.

Using this analogy, the price action in the following chart of the Phillip Morris Company can be explained in terms of support. During the period shown, each time the price fell to the $15 1/8 level, the bulls took control and prevented the price from falling further. That means that at the price of $15 1/8, buyers felt that investing in Phillip Morris was worthwhile, and sellers were not willing to sell for less than that price. The price at which this takes place is referred to as the support level, because buyers are supporting the price of $15 1/8.

Similar to support, a resistance level is the point at which sellers take control of prices and prevent them from rising higher. In the chart, each time the price reached $17-¼, sellers outnumbered buyers and that prevented the price from rising.



The price at which the trade takes place is the price at which the bull and bear agree to do business. It represents the consensus of their expectations. The bulls think prices will proceed higher and the bears think the prices will move lower. Support levels indicate the price where the majority of investors believe that prices will move up, and resistance levels indicate the price at which the majority of investors feel prices will move down.

When does the price of a particular security ever break out of its range between resistance and support levels? This takes place when investor expectations change. When expectations do change, they often do so abruptly. In the following chart of the Hasbro Corporation, when the price rose above the resistance level of $9 (**breakout point**), it did so decisively. In addition, the breakout was accompanied by a significant increase in volume.

Once investors accepted that Hasbro could trade above $9, more investors were willing to buy in at higher levels, causing both price and volume to increase. Similarly, sellers who would previously have sold when prices approached $9 also began to expect prices to move higher, and were no longer willing to sell.

The time to buy a particular stock is right *after* it breaks the resistance point on higher than average volume. The effectiveness of this method can sometimes reap huge returns in very short periods like in the following chart of the UroMed Corporation. In early February 2000 the volume started rising. This meant investors were beginning to show some interest. A few days later there was a very sharp rise in volume, in addition to a breakout past the previous resistance point. The stock, which broke out at around $3.00, reached a high of almost $15.00 in a very short period, potentially returning roughly 500%! Of course, no one could have known how high it would end up going. So when would have been the right time to sell?

There is no one right answer to that question. Some experts suggest that a cap should be set on how much one expects to profit from a particular security. When it reaches that level the investor should sell without any hesitation. The same theory would hold true were the stock not to advance to the positive side. Every investor should set a loss limit on every trade, so as not to be burned by a sharp and sudden drop. William J. O'Neil, the founder of Investors' Business Daily, always says "If the nasty bear market

has taught us anything about investing, it was this: *always* sell if your stock falls 7%-8% from your buy point."

Another way of knowing when to sell is to watch the volume level after the breakout. When the price decreases on a drop in volume, it usually means interest in the stock is subsiding.

The methods discussed are not foolproof ways of winning on Wall Street, for no one knows what is going to happen in the future. However, it has been proven that implementing these techniques correctly over a long period will bring a nice return on an investment.

If these strategies are so successful why don't all investors use them? Voltaire answered this a long time ago when he said; "Common sense is not so common."

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Introduction to Options

By: Joel Bodner

The financial markets have undergone tremendous change in the last twenty years, including the introduction of a variety of financial instruments. None has been more exciting to investors than the expansion and growth of the options and futures markets. Both markets have captured the imagination of investors and dramatically altered the investment arena.

The growth of these markets has stunned even the most optimistic observers. Although the history of options extends back several centuries, it was not until 1973 that standardized, exchange-listed, and government-regulated option became available on the Chicago Board Options Exchange (CBOE). By the early 1980s, the daily volume of trading in stock options had reached the point where the number of shares underlying the options frequently exceeded the daily volume of shares traded on the New York Stock Exchange (NYSE). The bull market of the 1990s caused a surge in options trading. In the period from 1992-1998, the number of contracts traded increased by a jolting 400 percent to 400 million contracts. The new world of options trading, once considered too risky for most individuals, is now widely embraced. Although professional investors are still active traders, the current boom is largely the result of heightened trading by individual investors.

Options:

A stock option is a contract that gives to its holders the right, but not the obligation, to buy or sell shares of the underlying security at a specified price on or before a given date. After this date, the option expires. Therefore, options contracts specify three conditions:

1. Property to be delivered
2. Price of the property
3. Specified period during which the right held by the buyer can be exercised

Options can be a versatile investment vehicle for investors who understand their risks and limitations. Strategies are not limited to buying, selling, and staying out of the market. Options allow investors to tailor their positions to individual situations and be as conservative or as speculative as they wish. An investor can reap the following benefits from options:

- Protection of stock holdings from a decline in market price.
- Increased income against current stock holdings
- Purchase of stock at a lower price
- Benefit to an investor from a big market move without knowing the direction of the move
- Benefit to an investor from the rise or fall of a stock without the cost of actually buying or selling the stock

Since the creation of the Chicago Board Options Exchange (CBOE) in 1973, trading volume in stock options has grown remarkably. The listed option has become a practical investment vehicle for institutions and individuals seeking financial profit or protection. The CBOE is the world's largest options exchange. Options also are traded on the American Stock Exchange (AMEX), the Pacific Exchange (PCX), and the Philadelphia Stock Exchange (PHLX). Options are not limited to common stock. They are written on bonds, currencies, foreign exchanges, specific industries, and various indexes. The CBOE trades options on listed and over-the-counter stocks and on Standard & Poor's 100 and 500 market indexes. Russell 2000 Index, and NASDAQ 100 Index, on U.S. Treasury bonds and notes, on long-term and short-term interest rates, and on the Dow Jones Industrial Average (DJIA). In 1999, the CBOE listed more than 1,200 options on the stock of foreign and domestic companies, 41 index options, 171 equity LEAPS, and 11 index LEAPS.

Options traded on exchanges such as the CBOE are similar in many respects to common stock.

- Options are listed securities

- Orders to buy and sell options are conducted through brokers in the same manner as orders to buy and sell stock. Similar to common stock, orders on listed options are auctioned on the trading floor of a national exchange.
- Price, volume, and other information about options are instantly available.

The following are some crucial differences between common stocks and options:

- There is no fixed number of options. The number of available options depends upon the number of buyers and sellers
- There are no certificates as evidence of ownership. Printed statements prepared by the involved brokerage firms indicate ownership of options.
- An option is a wasting asset. If it is not sold or exercised before expiration, it becomes worthless and the holder loses the full amount paid for the option.

Options Terminology:

The options market has a language all its own. Some of the more important terms include:

- **Options writer**- an option writer is the seller or issuer of an options contract. For example, if the buyer exercises an ABC call option, the options writer must deliver the required number of shares of ABC common stock. The options writer is sometimes called the options seller. A covered options means that the writer owns the underlying security. A naked option occurs when the writer does not own the underlying security.
- **Options buyer** or **holder**- the options buyer is the investor who obtains the right specified in the options contracts. For example, the buyer of an ABC call or put has the right, but not only the obligation, to purchase or sell, respectively, shares of ABC Corporation common stock at a specified price within a specified period.
- **Strike** (exercise) **price**- the price at which the holder can sell to or buy from the writer the item underlying the option. For example, an ABC 50 call option gives the holder the right to purchase 100 shares of ABC stock at a price of $50 per

share. On the other hand, an ABC 40 put option gives the holder the right to sell 100 shares of ABC common stock at a price of $40 per share.

- **Expiration date**- the expiration date is the last date on which the holder can exercise an option. If an option has not been exercised before expiration, it ceases to exist and is worthless. Options expire on the Saturday following the third Friday of the month in which they can be exercised.
- **Premium**- the premium is the price that the buyer of an option pays and the writer of the option receives. Premiums vary in response to such variables as the relationship between the strike price and the current market value of the underlying security, the volatility of the underlying security, and the amount of time remaining until expiration, the current interest rates, and the effect of supply and demand in the options market. Option premiums are a nonrefundable payment from the options buyer to the options writer for the rights conveyed by the option.
- **Out of the money option-** a call option is out of the money when the strike price is greater than the market price of the underlying interest. A put option is out of the money when the strike price is lower than the market price of the underlying interest. Premiums are lower when options are out of the money.
- **In the money options**- a call option is in the money when the strike price is less than the market price of the underlying interest. A put option is in the money when the strike price is greater than the market price of the underlying interest.
- **At the money options-** options are at the money when the common stock price is equal to the strike price.

Call Options:

A call option gives its holder the right to buy a specified number of shares of the underlying stock at the strike price between the date of purchase and the option's expiration date. It must be emphasized that an option gives an investor the right to purchase, but not the obligation to do so. A single call option gives the holder the right to

buy 100 shares. For example, an investor who bought an XYZ October 40 call option would have the right, but not the obligation, to buy 100 shares of XYZ common stock at a cost of $40 per share at any time before the option expires in October.

EXAMPLE:

Suppose an investor buys an XYZ 40 call option when the price of the stock is $40 and pays a premium of $2. A premium or price of $2 means that the option will cost $200 (an option contract is based upon 100 shares). If the price of XYZ stock climbs to $45 before expiration and the premium rises to $6, an investor has two choices in disposing of the option:

1. The option can be exercised and the underlying XYZ common stock can be bought for the total cost of $4,200 ($40 X 100 plus the $200 premium). The shares can then be sold for $4,500, yielding a net profit of $300.
2. The option contract can be sold for $600, earning a profit of $400 ($600-$200 premium). Here, the Investor makes a profit of 33 1/3 percent (200/600), whereas the profit on an outright purchase given the same price would be only 12 ½ percent [$45-$40)/ $40].

An option does not have to be exercised to result in a profit. Like common stock, options are regularly bought and sold on the exchanges. Whether it is more advantageous to exercise or sell a profitable option is influenced by whether an investor desires to own the common stock. In making the decision to exercise the option or to sell the option, the investor must consider premium levels, commissions, and taxes. Unless the investor wants the stock, it is generally better to reap the profit by selling the option itself.

Of course, stock prices often do not move in the direction anticipated or desired. Using the previous example, assume that XYZ common stock were to fall to $35 and the option premium dropped to ¾ ($75 total). The investor could sell the option to partially offset the $200 premium, and the loss would be $125. If one did not act, and the option expired worthless, the loss would be the total amount of the premium paid- $200. This

loss would be less than if the 100 shares had been purchased outright. An outright purchase would have produced a loss of $500 ($4,000 less $3,500).

The examples illustrate the two main advantages of options:

1. Leverage. A somewhat smaller investment controls a larger investment with corresponding greater profit potential.
2. Limited and defined risk. Despite how much XYZ stock falls, the maximum risk exposure is limited to the premium. In our example, the maximum loss that could be incurred on this option is the premium of $200.

Put Option:

A put option gives the holder the right to sell a specified number of shares of the underlying common stock at a predetermined price (strike price) on or before the expiration date of the contract. Buying an XYZ October 40 put gives an investor the right to sell 100 shares of XYZ stock at $40 per share at any time before the option expires in October.

EXAMPLE:

Assume that an investor buys an XYZ October 40 put at a premium of $2 (or $200) when the price of the underlying common shares is $40 per share. If the price of XYZ stock falls to $35 before October and the premium rises to $6, there are two choices in disposing of these in the money (the strike price is greater than the market price) put options:

1. One hundred shares of XYZ stock can be purchased at $35 per share. Then, the put options can be exercised to sell the XYZ at $40 per share. This action produces a profit of $300 ($500 profit on the common stock minus the $200 option premium).
2. The put option contract can be sold, producing a profit of $400 ($600 premium received less the $200 premium paid).

As discussed previously, an option does not have to be exercised to realize profit. It is generally a better strategy to sell an option than to exercise it. Sales of options usually involve lower transaction costs than do exercising options.

If XYZ stock had climbed to $45 before expiration and the premium fell to $1, the option would be out of the money. The investor could continue to hold the option, hoping the price will drop, or sell it for $100. A sale for $100 would mean a $100 loss ($200 less $100). It is often a good strategy to sell an option at a loss rather than wait for the price of the stock to change in the investor's favor. The time value of an option rapidly shrinks toward zero, starting about six weeks before expiration.

Short Sales vs. Put Options:

An investor who anticipates declining stock prices can purchase put options or sell stock short. A short sale is the sale of a common stock that is not owned with the intention of repurchasing it later at a lower price. The investor borrows the stock from another investor through a broker and sells it on the market. Usually, a broker has other clients who own the security and are willing to loan shares.

An important aspect of a short sale order is that an investor does not receive the proceeds of the order at the time the trade is executed. In a short sale, the money is kept by the brokerage firm until the short is covered; that is, until the security is purchased and returned to the lender. Also, to ensure that the short position will be covered, the broker requires the posting of collateral. Most short selling is done through margin accounts, in which case short sellers are required to have in their account the required percentage of the stock's price (currently 50 percent).

The objectives of the put option purchaser are the same as those of the short seller. They are both trying to make a profit from anticipated declines in stock prices. Unlike the short seller, however, the put buyer faces a maximum loss defined by the amount of the premium. A short seller has no limit on the loss that can be sustained. In addition, the short seller faces margin requirements and additional restrictions not applied to the put buyer. On the other hand, the option's limited life span constrains the put

buyer. With, options, an investor can be correct in anticipating a future price change, but still lose money because the price change did not occur within the limited period of the life of the option.

Valuation of Call Options:

Six factors determine the value of an American-style call option. An American-style call option is one that may be exercised at any time before the expiration date, whereas a European style option may be exercised only on the expiration date. Premiums are determined by the relationship to the following factors:

1. Stock price- the call's price rises when the price of the stock rises, and falls when the price of the stock falls. The relationship is based upon the fact that an option represents a leveraged position in the underlying stock. A relatively small initial premium gains control of a larger asset with significant profit potential. A call option has intrinsic value (the amount by which an option is in the money) if the stock price is greater than the strike price. At a given strike price, the price of the common stock determines whether the option is in the money (stock price > strike price) and therefore has intrinsic value, or out of the money (stock price < strike price) and has only time value (the option's premium above any intrinsic value.)
2. Cash dividends- the value of a call option is inversely related to the dividends paid on the common stock. Consider what happens on the ex-dividend date. On this date, stockholders are not eligible to receive the dividend and the market price on the opening sale is reduced by the amount of the dividend. Because the stock's price declines by the amount of the dividend, the call option price should drop in a corresponding fashion.
3. Stock price volatility- a positive relationship exists between the volatility of the underlying stock and the value of the call option. Volatile stocks have greater movement, which increases the likelihood that at some time before the option expires, it will be in the money. If the call option is in the money at expiration, it will be profitable for the holder to exercise the option.

4. Time to maturity- a major determinant of the value of an option is its time to maturity. The longer the period to maturity, the greater the value of the option. The longer the time frame, the greater the chance that options will gain intrinsic value. This relationship is why longer-term call options on a given common stock and exercise price will have higher prices than shorter-term options.
5. Strike price- the call option price is higher when the strike price is lower, and vice-versa. Out of the money call options have lower premiums because they have lower intrinsic values. As call options go in the money, their intrinsic values increase and the premiums rise. For example, consider a common stock trading at $60 per share. A call option with a strike price of $50 has a greater value than a call option with a strike price of $55. The $50 option is in the money by $10, whereas the $55 option is in the money by only $5.
6. Interest Rates- the final factor is the positive relationship between the market interest rate and the value of a call option. Higher interest rates generally produce higher call option prices, whereas lower interest rates result in lower call option prices. In effect, a call option buyer's leveraged position is being financed by a loan from a call option writer. The call option writer defers the benefits of converting the stock to cash by enabling the options buyer to leverage a position in the common stock. Higher interest rates mean that the opportunity cost of entering the agreement with the options buyer is greater for the options seller. Therefore, an options writer will demand a higher call option premium to compensate for the inability to take advantage of the higher interest rates.

Intrinsic Value and Time Value

The value of an option consists of two components: intrinsic value and time value. Intrinsic value reflects the amount by which an option is in the money. For example, when the market price of ABC stock is $56 per share, an ABC 50 call option has an intrinsic value of $6. If the underlying sock declines to $52, the intrinsic value of the call

option is only $2. However, if the price of the underlying stock drops to $50 or less, the call option lacks intrinsic value.

Time value is the value a call option has in addition to its intrinsic value. The premium reflects what the buyer is willing to pay for an option in anticipation of price increases of the underlying stock before expiration. For example, when the market price of ABC common stock is $50 per share, an ABC 50 call option may command a premium of $2. This premium is entirely time value; it reflects the hope that the underlying security will rise sufficiently to enable the holder to sell or exercise the option. The time value of an option typically decreases as the call option approaches expiration and eventually becomes worthless. Just before the call option's expiration date, its premium is either zero or equal to its intrinsic value. At this point, its time value is zero, and the option price or premium is solely determined by its intrinsic value. The components of the premium may be expressed by the following formula:

Option Premium = Intrinsic Value + Time Value

This formula applies to both put and call options. For in the money options, the time value is amount in excess of intrinsic value. For at the money and out of the money options, the time value is equal to the option premium.

Valuation of Put Options:

Like all items traded in a competitive economy, the supply and demand for an option determines the price or premium of the option. During periods of rising stock prices, the demand for calls grows stronger and call premiums tend to rise. During periods of declining or stable prices, call premiums tend to be lower. Alternatively, strong stock prices tend to reduce the demand for puts, and put premiums tend to decline, whereas weak stock prices generally increase the demand for puts, exerting upward pressure on put premiums.

Although this analysis provides a general reason for changes in premiums, more specific factors can be defined that primarily account for changes in put option prices. The factors are the same as the factors that affect call option prices. They include the following:

1. Stock price- the value of a put option rises when the price of the stock falls, and falls when the price of the stock rises. At a given strike price, the price of the stock determines whether the option is in the money and has intrinsic value or if it is out of the money and has only time value. Because a put option grants the right to sell shares at the strike price, this right becomes less valuable to the owner as the stock price rises and the put option loses intrinsic value. If the price of the underlying common stock declines, the put option gains intrinsic value.
2. Cash dividends- the put option's value increases when the underlying common stock pays cash dividends. A stock's price should decline by the amount of the cash dividend on the ex-dividend date. The ex-dividend date begins the period during which purchasers of the stock cannot receive the next quarterly dividend. The dividend goes to the seller.
3. Stock price volatility- the more volatile the underlying stock, the higher the price of the put option. The greater the volatility of the stock price, the greater the potential for the option to gain intrinsic value. Volatility is nondirectional in that the fluctuation could be up or down. Consequently, when higher volatility is expected, premiums on both puts and calls rise.
4. Time to maturity- a significant factor in determining the premium of a put option is the time to maturity. The longer the time to maturity, the greater the value of the option. Longer term put options command higher premiums. The put option's time value slowly declines until about six weeks before expiration. After that, the dissipation of time value accelerates.
5. Strike (exercise) price- the value of a put option is greater when the strike price is higher, and smaller when the strike price is lower. This relationship exists because put options gain intrinsic value as strike prices increase. For example, assume a

stock sells for $50. A put option with a strike price of $60 has a higher value than an option with a strike price of $55. The first put is in the money by $10, whereas the second put is in the money by only $5.

6. Interest Rates- put option prices rise when interest rates fall, and fall when interest rates rise. One way to explain this relationship is to use the present value argument. The premium on the put option reflects the present value of the strike price. The higher the interest rate, the lower the present value of the strike price and the lower the intrinsic value of the option. Lower intrinsic values translate into lower premiums. Alternatively, lower interest rates increase the present value of the strike price, which increases intrinsic value. A higher intrinsic value results in higher premiums.

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Income Inequality and its Repercussions for Us

By: Rochie Saks

Income inequality as an economic concept is central to the distribution of our nation's wealth and to the personal wealth and poverty levels of all individuals. But does it affect us in a real way in our day-to-day lives? What is the difference between income inequality and an absolute state of poverty? Is the income level at which we live, in our control, or a product of our surroundings? Have these factors affected us in positive ways, i.e. are we richer now than our ancestors of 100 years ago?

The controversy of income inequality in modern-day America is a great one. There are convincing arguments for both ends of the spectrum: Some say that income inequality is the main cause of our nation's problems, while others believe that it is largely insignificant. Harvard and Berkeley Universities conducted a study to investigate this issue. They wanted to discover if social issues like crime, welfare, and poor education as well as the phenomenon of higher death rates are connected to income inequality or if they are associated with a lower standard of living. The universities learned that income inequality is directly correlated, and not the lower living standard.

It is well known, especially among health professionals, that the poor have higher death rates and more health problems than the rich. In a 1986 study, researchers found that poor white men had 6.7 times the death rate of rich white men and poor black men had 5.4 times the death rate of rich black men. With results such as these typifying all studies done on the subject, the question must be asked. Why, in a society where science, technology, safety, public education, and prosperity are all growing, are poorer people still living in such a lower state of health and mortality?

The most obvious answer is that the poorer sections of society cannot afford the health care richer people can. Especially preventative health care, as this naturally takes a lower place on the list of financial priorities for a poor person. There are, however, a myriad of additional causes of the health problems of the poor. Their residences and

places of employment are in more toxic environments and they eat lesser quality foods. They are exposed to greater dangers and risks and cannot afford the comforts and safety features that make safer living easier. They have stronger forms of stress involved in their basic survival; and are less educated about the things that would help them live longer and healthier.

The above view is that which is taken by the mainstream members of society; however, there are those who interpret the situation differently. Conservatives point out that correlation is not causation, and say that it is possible that the people who suffer from these health and social problems will by nature earn lower incomes. Poverty does not cause poor health, poor health causes poverty. This means that people who have poor health are less productive as workers and are therefore paid less. Another possibility is that external factors may cause both the poor health and the poverty. For example, the same lack of education that keeps the poor uninformed in health matters also prevents theirs chances to obtain the best paying jobs. Laziness, substance abuse, and other moral shortcomings could also have a depressing effect on both incomes and health.

When trying to determine which opinion is the correct one, it is important to remember that the second two views attribute the cause to the individual, and not to the general social economic situation. Consider the enormous jump made in life expectancies and living standards over the past two hundred years. It would be highly bizarre to a credit this to a sudden change in individual human morals, habits and work ethics. This upward trend demands a social explanation; it is not the result of isolated individual behavior. Human nature has not changed, society has. Societies as a whole, as well as its institutions, ranging from scientific to economic to political systems, have been affected by the progresses made in the past two centuries. It is far more reasonable to state that these changes took place as a result of advances in social causes and social programs, and not due to individual personality alterations.

If poverty is indeed essentially a murderer, then the issue of income inequality needs to be looked upon differently. A society that allows high levels of inequality is in essence killing its own citizens. Conservatives defend their position by saying that the

living standards of the poor have continually risen, so if the rich are growing richer by comparison it should be insignificant. They base their claim on the idea that we do not live in a zero-sum economy, and that a poor person with a smaller portion will benefit if proportionally everything grows. Two important issues are necessary to examine relative to this concept: that of relative poverty and absolute poverty.

Relative poverty introduces the idea that a person is poor relative to others, i.e. how large is his slice of the economic pie. Absolute poverty measures the actual size of the slice itself, not compared to anything else. Income inequality refers to the relative difference between the growth of the income levels of rich and poor people. To better determine where the real cause lies, it is necessary to take a closer look at how income inequality is linked to health and other social problems.

In 1996, Harvard and Berkeley conducted independent studies that examined income inequality in all 50 states. Both studies found that states with higher income inequality share the following social problems: Higher death rates for all age groups, higher rates of homicide, higher rates of violent crime, higher costs per person for police protection, higher rates of incarceration, higher rates of unemployment, a higher percentage of people receiving governmental income assistance, a higher percentage of high school dropouts, less state funding spent per person on education, resulting in poorer educational performance, higher infant mortality rates, higher rate of heart disease, higher cancer rates, a greater percentage of people without medical insurance, babies born with low birth weight, the population unable to work because of disabilities. A higher proportion of the population using tobacco, a higher proportion of the population being sedentary, higher costs per person for medical care. The correlation between income inequality and mortality rates was significant as well.

In both studies, the researches also looked to see if the average or median income of each state was a tool in predicting its mortality rate, however, they were not. Income inequality in each state proved to be meaningful though, even after accounting for such factors as smoking and drinking rates, household size, and household income. The latter factors are especially important, as they show a connection with relative poverty in

addition to absolute poverty. Dr. George Kaplan, the lead researcher of the Berkeley study, says: “People might assume that states with higher income inequality have more poor people, and we know that poor people have higher death rates. [But] the evidence in these two studies suggests that the increased death rates in those states are not due simply to their having more poor people. Income inequality seems to be increasing mortality rates among non-poor people as well, and we are investigating that possibility.” Kaplan went on to say that “this effect on health wasn’t just happening to poor people; middle class people were affected too. When we accounted for income differences, there was still a strong relationship between income inequality and mortality rates.”

A practical example of the above would be the following scenario. Picture a perfect society where everyone makes $50,000 a year and is guaranteed a life expectancy of 75 years. Now add income inequality to this equal society, so that it proportionally grows and shrinks. Whereas beforehand 100% of the population earned $50,000 a year each, now one third make $35,000, one third make $50,000 and one third make $65,000 yearly. One would imagine that the mortality rate should remain 75 years, as the lower poorer rate would be balanced by the new, higher richer rate. However, that is not the case. The poor do lose years off of their expected life span, but so do the middle class. The new life expectancy will be around 72 years of age. These figures are supported by both the Harvard and Berkeley studies and European nations. The European countries proved that with higher taxes and better-funded social programs to help alleviate poverty, the income inequality gap lessened and the mortality rate was more equal.

The question must be asked, however: Why do the above numbers work as they do? What causes the income inequality gap to have the devastating effects it does? According to the liberal point of view, in an interdependent society, the weakening of one section weakens the whole society. This would explain why states with greater inequality have greater health and social problems among both the poor and middle classes. Dr. Kaplan suggests, “Income inequality affects all segments of the population because it affects rates of violence and disability, as well as public spending on police protection, education, welfare and health care.” It is also probable that the average statistic in states

with greater inequality drops because losses among the poor are not fully compensated with gains among the rich. For example, there comes a point at which acquiring more money will not affect one's health. If an affluent individual already has a top-quality health care plan, he will not benefit health wise from his salary increase. However the poor person who lost the money will likely have to cut his level of health care, or may have to stop his health care plan altogether, which will negatively affect his mortality. It is interesting to note that the fact that higher death rates affect the middle classes is proof that the social and health problems are not the cause of the lower income, as some conservatives say. In fact, the lower income is the cause of the health problems.

In addition, historical data does not evidence the idea that low incomes are the result of people suffering from health problems or personalities that are criminal, addictive, lazy, or hostile to education. Proof of this claim is that the changes in income inequality are too rapid, too drastic and too localized to be attributed to character changes and social habits in people, especially when they are the same people.

For example, between 1980 and 1990 the index of income inequality showed a major increase. Can one really say that the personalities and morals of the poor considerably worsened in one decade? To believe such a thing would be absurd. It is therefore necessary to attribute the incredible economic changes to the rapidly changing economic policy of that time.

During the 1980's President Reagan greatly reduced the top tax rate for personal income from 70 to 28 percent, allowing income to remain among the wealthy. In 1983, payroll taxes were raised on the working poor. And even more, between 1980 and 1993, family welfare payments were reduced from $350 to $261 per month, which resulted in a 25% decrease. These are obvious reasons as to the growing income inequality during the 1980s.

It is now obvious that income inequality is detrimental to society, and that poverty has far-reaching effects that extend beyond the individual who is experiencing it. But how can this be changed? What can be done about poverty in America, a civilized country? There are those who believe that economic growth can reduce poverty. Michael

Roemer and Mary Kay Gugerty conducted extensive research for the Harvard Institute for International Development to examine this idea and to answer these age-old questions.

In their study, Roemer and Gugerty analyzed the relationship between economic growth and poverty alleviation. They were successful in proving that "economic growth is positively associated with reductions in poverty, and that openness and sound macroeconomic management are associated with higher growth and therefore with reductions in poverty." The effective strategies for reducing poverty are outlined in their research, with the main emphasis being on strong economic growth. It is highly difficult for growth to occur without a reduction in poverty, as the two go hand in hand. But what is poverty? How is it defined and measured?

The common welfare approach toward the measurement of poverty as used by economists, assumes both that individuals know what is best for them and that monetary measures of consumption or income can serve as an indicator of well-being. Using this approach, the analyst defines a poverty line as a level of income, and all those under that line are considered poor. Under an alternative non-welfarist approach, standards of nutritional or other basic human needs are defined by the observer, who then estimates the income level needed to satisfy those needs. That required level of income becomes the poverty line. In either case, poverty means living below the level of a preset standard.

An interesting idea to examine is that of what it means to be poor relative to the times in which one lives. It is said that the twentieth century has been, above all, the century of increasing material wealth. The growth in the wealth of the industrial economies over the twentieth century has been unprecedented compared with all other economies and all previous eras. America's population today have standards of material comfort that greatly exceed what the richest of previous centuries could only dream about. This intense rise of standards is, according to J. Bradford DeLong, "the most important characteristic of twentieth century economic history…is also surprisingly difficult to grasp."

The comforts that have become so basic to us and to the way we live did not even

exist a century ago. Computers, cars, telephones, wireless technology, VCRs, DVDs, washing machines, dishwashers, vacuum cleaners, and countless additional technologies give the regular American citizen a degree of material wealth. The advent of mass production makes such products truly accessible. The chasm between our standard now and that of 100 years ago is so great that it is hard to just imagine what it really means.

DeLong illustrates the difference between the costs of products in 1895 and 1997, relative to hours needed to work to earn the commodity. For example, a bicycle in 1895 cost $65 if ordered from the Montgomery Ward catalog. The actual dollar price of the bike has only doubled in the past 100 years, however if one measures the real price, i.e. the labor needed to produce the item, it is easy to see how the price has dropped.

In 1895, it took around 260 hours of the average American worker's labor to amass enough money to buy a one-speed bicycle. Today the average American can buy a one-speed bike for less than the value of one day's work. In terms of labor power, bicycles have become 36 times cheaper over the century. On the bicycle standard – measuring wealth by counting up how many bicycles it can buy – Americans today are 36 times richer than they were in 1895. Other commodities would paint a different picture. An office chair with cushions is only 12 ½ times cheaper, while a Steinway piano or accordion is only twice as cheap.

In answer to the question of how much wealthier are we today than our counterparts of a century ago, it depends on which set of commodities we view as central and important. If one values personal services, such as having a butler to answer your door and polish your silver, then you would find very little difference between now and then. An hour of a butler's time cost the same as the average worker in 1895; the same is true in 2001. So regarding personal services, Americans are no richer now than we were 100 years ago.

However, regarding the ability to buy mass-produced goods, such as bicycles, we are far better off than you would have been a century ago. Were one to average out all the commodities produced in 1895 as opposed to those made now, one would find that the average productivity multiplication is about eightfold: an average worker today could buy

with one hour's work the average bundle of things that and average worker of a century took eight hours to earn.

From these results, one could think that the answer is that we are eight times richer today than our ancestors were 100 years ago. But it is not that simple. The calculations done above are intrinsically flawed. This is due to the fact that two identical items are not being compared. Commodities produced now were not even invented yet in 1895. So essentially apples are being compared to oranges.

Think about the automobile. In our times, cars are the primary mode of transportation. It replaced the horse and buggy and traction-driven cable car, and it greatly expanded the area that is local and accessible. With a horse, a shopping trip to a store six miles away would become an all-day affair. With a car you can be done in 45 minutes.

The automobile therefore makes a local area denser – one can live in a certain area and have a much wider selection of available services and goods. One can live in the suburbs and work in the city, while both areas are local to him. For example, 100 years ago only 100,000 people lived within ½ hour of downtown Boston. The car has made it possible for 3 million people to live within ½ of downtown Boston. Automobiles have therefore made living in Boston an option for thirty times as many people.

The Atlantic Monthly of 1901 contains a short and anonymous article by a college professor complaining about his low salary – which was about five times the productivity of the average worker in 1901, and gave him the same place in the relative income distribution as a salary of $330,000 a year would today. He could not afford an appropriate house within walking distance of campus. He did not have the spare income to keep a horse. So he rode a bicycle – an uncomfortable alternative in New England winters falls and springs. He spent as large a share of his income on bicycles for his family as someone would on a standard economy sized car today.

The jump in our quality of living because we now know how to make cars is omitted entirely in the simple calculation above that suggested an eightfold multiplication of material wealth.

Another example of why this calculation is flawed is the following. In Looking Backward, Edward Bellamy's turn of the last century utopian novel, the narrator – thrown forward in time from 1895 to 2000 hears the question "Would you like to hear some music?" He expects his host to play the piano, which was a social accomplishment of upper class women around 1900.

To listen to music on demand at that time, you had to have an instrument and someone who was trained to play. The average worker would have spent some 2400 hours working to support such an extravagance. This multiplies out to over a year's work to listen to music at one's whim. In contrast, today all one needs is a CD player or radio and he can listen to whatever his heart desires. The actual cost of a Steinway piano has fallen in price form 2400 average worker hours a century ago to 1100 worker hours today. But if what you value is the ability to hear music in your home at your leisure, then the price dropped from 2400 hours to about 5.

So when we calculate the increase of wealth over the past century, do we count the drop in real time production and acquiring hours or do we count the increase in capability? To figure this, we must analyze what is gained by the increase in capability and try to measure its worth. When one makes the common calculation to see how much they would earn 100 years prior if they were at the same income level as they are now, it is tempting to say that inflation has gone sky high and we have much less purchasing power relative to our income level than did our counterparts of 100 years ago.

However, the crucial aspect that most people forget is that the people who lived 100 years ago were limited to what the technology of their time could offer them. They didn't have the option of purchasing a washing machine, for such machinery simply did not yet exist. Vaccines and medicines that are taken for granted now were not in existence then. Neither was a simple, every day part of life like the telephone available. When these factors are taken into consideration, it almost seems preposterous to try to measure wealth. For no matter how many dollars our ancestors had, they simply did not have access to the items that any middle class American can take for granted today.

Due to our fantastic economic and technological growth, the quality of living is

better than it has ever been, for all people at all income levels. In truth, Americans care less about the gap between the rich and the poor, and more about getting ahead. Every person wants to be successful, and his own wealth relative to Bill Gates' wealth is not even a determining factor. America is by-and-large a middle class nation, and most Americans want it to stay that way. No one wants a society that is completely split into haves and have-nots. This is the flaw with an emphasis on inequality, that it somehow allows the poor to feel that the rich are responsible for their plight. It is mostly a moral self-indulgence. Reducing inequality only matters if we reduce poverty.

In conclusion, income inequality is definitely a problem in America today, causing much of the social breakdown. However, the standard of living is higher and therefore, the population as a whole is better off. If people concentrate on growing economically and striving higher, they can succeed in our society.

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Microsoft: An Economic Analysis

By: Chana Grossberger

Microsoft is the company everybody "loves to hate". Although no one is forced to use Microsoft's products, most people do so. This paper is being written in Microsoft Word, on a computer running Microsoft Windows ME. This is not due to the absence of other, possibly better, options. Many secretaries claim that WordPerfect is superior to Microsoft Word, and some computer experts claim that Linux is better then Windows. Nevertheless, most people choose to use Microsoft products because it is easier, and usually safer, to go along with the crowd. The widespread use of Microsoft products gives those products the advantage of compatibility between its users. The dominance of the PC software industry by Microsoft is not necessarily illegal. If, in fact, they achieved this dominance by producing better software, or even by using superior marketing techniques, they could be considered a legal monopoly. Only if they used illegal, anti-competitive, methods would their monopoly be illegal.

The confrontation between the government and Microsoft, which has been ongoing since 1993, and has received enormous publicity, has tempted commentators to draw comparisons between Microsoft's chairman and the nineteenth century's most famous monopolist, John D. Rockefeller.

In the late 1800s, businesses began to gain market dominance by forming anti-competitive agreements. These relationships were called trusts. Trusts cut prices drastically in order to drive competitors out of business. Among their other anti-competitive techniques were: buying out competitors; forcing customers to sign long-term contracts and forcing customers to buy unwanted products in order to receive other goods.

In March 1881, The *Atlantic* ran a lengthy piece of reporting by the muckraking journalist Henry Demarest Lloyd, titled "Story of a Great Monopoly." The article's significance is incontestable. Chernow and other historians cite it as one of the earliest pieces of progressive muckraking to be published in a national, well-respected magazine,

and as the first exposé of the Standard Oil trust to be taken seriously. The issue helped bring antitrust legislation to the forefront of national debate, foretold the passage of the Interstate Commerce Act of 1887 and the Sherman Antitrust Act of 1890.

Lloyd built his argument around Standard Oil's collusive manipulation of the railroads, then the lifeblood of the nation's transportation system and thus of the economy. He wrote:

> Their great business capacity would have insured the managers of the Standard [Oil Company] success, but the means by which they achieved monopoly was by conspiracy with the railroads.... The Standard killed its rivals, in brief, by getting the great trunk lines to refuse to give them transportation. [The railroad baron] Vanderbilt is reported to have said that there was but one man -- Rockefeller -- who could dictate to him. Whether or not Vanderbilt said it, Rockefeller did it. The Standard has done everything with the Pennsylvania legislature, except refine it.

Summing up the position in which Standard Oil stood with regard to its competitors and the railroads, Lloyd pointedly observed, "America has the proud satisfaction of having furnished the world with the greatest, wisest, and meanest monopoly known to history." He argued that the oil and railroad trust "must be confronted by a power greater than itself," and that "there is but one such power" -- the federal government. Lloyd's conclusion has a somewhat exaggerated, anti-business view:

> In less than the ordinary span of a lifetime, our railroads have brought upon us the worst labor disturbance, the greatest of monopolies, and the most formidable combination of money and brains that ever overshadowed a state. The time has come to face the fact that the forces of capital and industry have outgrown the forces of our government.... Our strong men are engaged in a headlong fight for fortune, power, precedence, and success. Americans as they are, they ride over the people like Juggernaut to gain their ends. The moralists have preached to them since the world began, and have failed. The common people, the nation, must take them in hand.... The nation is the engine of the people. They must use it for their

industrial life, as they used it in 1861 for their political life. The States have failed. The United States must succeed, or the people will perish.

Congress passed the Sherman Anti-Trust Act in 1890, and this is the source of all American anti monopoly laws. The law forbids every contract, scheme, deal, and conspiracy to restrain trade. It also forbids conspiracies to secure monopoly of a given industry. The ideas were new and had to wait before they could achieve some efficiency. The Standard reorganized once more, in a holding in the Standard Oil Company, which now coordinated the whole machine, that is 70 companies and 23 refineries controlling 84% of the crude oil refined in the US in 1899. Ten years later, international competition and the struggle of the independents lowered this percentage to 14%. Theodore Roosevelt committed himself in 1901 to a strong war against monopolies, launching the federal government in 1906 in a lawsuit against the Standard because of discriminatory practices on the market, abuse of power and excessive control on the American oil industry.

In 1911, the Supreme Court found the Standard Oil in violation of the 1890 Sherman Antitrust Act because of excessive restrictions to trade, and its practice of buying out the small independent refiners or that of lowering the price in a given region to force bankruptcy of competitors. The court ordered the Standard Oil Company to dismantle 33 of its most important affiliates. From these affiliates came Exxon, Mobil, Chevron, and American.

This is a landmark ruling in the economic history of the USA, and is the basis for a new doctrine in American antitrust policy, called the rule of reason. Because of a need for more solid juridical basis, the Clayton Antitrust Act in 1914, which explicitly condemns commercial practices like price discrimination, exclusive commercial relations, and the buying out of competitors and the incestuous boards, was passed.

In 1914, Congress passed two more laws that further protected the competitive marketplace. The Clayton Antitrust Act outlawed the following: trusts formed by two companies with interlinking boards of directors; fixing prices in agreement with other businesses offering competing products; making agreements with other businesses to control the supply, and therefore the price, of a product, and abusing power to gain or

maintain a monopoly. Soon after, Congress established the Federal Trade Commission to enforce antitrust laws.

The Federal Trade Commission and the Antitrust Division of the Department of Justice enforce antitrust laws. The FTC has the power to stop companies temporarily from employing suspected anti-competitive practices, while the Justice Department probes and prosecutes businesses. When the U.S. government establishes in court that a company has been involved in antitrust activities, it can break up the monopoly into well-defined components and/or force businesses to tell customers about competitors.

Although the government was now armed with two broad laws and an agency to enforce them, their track record against large corporations was not very good. In 1920, the government accused the U.S. Steel Company of anti-trust violations, but the court ruled that U.S. Steel had not done anything illegal. An attempt to break up IBM in 1982 was also unsuccessful. The government's first success following the U.S. Steel case came in 1983, when AT&T was broken into one long-distance company and seven "baby bell" local phone companies.

Microsoft had its beginnings in 1975, when Paul Allen and Bill Gates, two later to be college dropouts, wrote the BASIC interpreter, for the Altair 8800, while they were undergraduates at Harvard. Bill Gates first used the name "Micro-soft" in a letter to Paul Allen in November of 1975. In 1981, when IBM was developing the IBM Personal Computer, they were looking for someone to write the operating system. Most of the microcomputers in use at the time used an operating system called CP/M, written by Digital Research. IBM wanted them to write the new operating system for their new 16-bit PC, but the president of Digital Research was in the Far East on a business trip. IBM did not want to wait, so they approached Bill Gates and asked him to do the job. He copied most of CP/M, added a few new features and that became MS DOS. By 1991, Microsoft's operating systems were used by 93 percent of the world's personal computers.

In 1993, during the Bush administration, the Federal Trade Commission began its investigation of Microsoft's market power in the sale of operating systems for personal computers. That investigation was later taken over by the Department of Justice and

pursued vigorously by Clinton appointee Anne Bingaman, then head of the Antitrust Division. After an extensive inquiry, DOJ uncovered one practice it considered worth challenging: Microsoft's licensing of its Windows software for multi-year periods on a "per processor" basis.

To help prevent software piracy, Microsoft insisted that computer makers pay a royalty to Microsoft for each computer they shipped, whether or not Windows was installed as the operating system. DOJ was not persuaded by Microsoft's contention that physical machines can more easily and reliably be counted than intangible copies of computer software. Nor was DOJ convinced that customers might actually favor long-term contracts to guard against unpredictable price increases and other uncertainties. Instead, the controversy centered on this loaded and, ultimately, unanswerable question: To what extent did Microsoft take advantage of its dominant market position to dictate "unfair" licensing terms.

The DOJ rejected the possibility that Windows became the industry standard because PC makers thought it was a "superior" product, an assessment that needed to take into account the entire array of product features, not only technical features but also ease of use, quality, price, service, and contract terms. It did not matter that consumers shared that view or that there were no barriers to entry that would prevent a competitor from displacing Windows as the market leader.

DOJ threatened costly and extended litigation, which Microsoft opted to avoid by signing a consent decree in 1994. The decree prohibited Microsoft from using "per processor" licenses, shortened the initial term of each license from two years to one, and implemented other technical changes, one of which, would become the subject of DOJ's second attack.

After a five-year investigation costing millions of dollars, the Antitrust Division found little that could be characterized as anti-competitive. But that did not stop the government. Not only did DOJ subsequently file an antitrust suit that prompted Microsoft to cancel its planned acquisition of Intuit, manufacturer of a popular personal finance program, but the Department also threatened to halt the release of Windows 95,

Microsoft's upgraded operating system. Antitrust Division head Bingaman was reportedly concerned about the link between Windows 95 and the Microsoft Network (MSN), an Internet service provider intended to compete against America Online (AOL), CompuServe, and others. Whenever a user started a Windows 95 system, an MSN icon appeared; then one click of the mouse connected the user with the MSN service. That packaging, according to DOJ, gave MSN an unsporting edge over its online rivals.

However, a few more mouse clicks enabled any Windows 95 user to bring up an AOL or CompuServe icon, which would appear automatically afterwards, at the same time as the MSN icon. Evidently content with its discovery that MSN's edge could be neutralized, the Antitrust Division abandoned its threat to block Windows 95. In retrospect, however, Bingaman's concern was unfounded. MSN now loses an estimated $200 million annually providing service to fewer than 3 million customers. In contrast, AOL has 9 million subscribers and will add nearly 3 million more with its acquisition of CompuServe's consumer business. Although rivals complained that bundling MSN software with Windows 95 would overwhelm competition, Microsoft's did not capture the Internet Service Provider market.

In 1995, the Antitrust Division, headed by Joel Klein, raised the bundling issue again, this time objecting that Windows 95 and Internet Explorer are two separate products, not one integrated product. The whole case depends on that distinction. The 1995 consent decree that Microsoft signed forbids any tie-in between Windows 95 and a separate software product. Is the Internet Explorer a "separate" product, as Klein claims? Or are the two products "integrated," as Microsoft claims? The 1994 consent decree provides specifically that the prohibition on tying separate software products "shall not be construed to prohibit Microsoft from developing integrated software products." Because DOJ denies that Windows 95 and Internet Explorer are "integrated," Klein proposed to fine the company $1 million a day until the two products are unbundled.

In its defense, Microsoft maintained that Windows 95 couldn't perform several crucial tasks -- like word processing, imaging, and drawing -- unless all Explorer files are installed. Furthermore, states the company, the control panel, which operates devices

such as modems and printers, will not work without Explorer, nor will many other products developed by other companies for Windows machines. DOJ responded that Microsoft did not have to make Windows dependent upon the browser and could easily have allowed computer manufacturers to "uninstall" Explorer without compromising the operating system.

In December of 1997, U.S. District Judge Thomas Penfield Jackson issued a preliminary injunction forcing Microsoft to stop, at least temporarily, requiring manufacturers who sell Windows 95, or any successor, to install Microsoft's Internet Explorer.

In its initial response to the preliminary injunction, Microsoft offered PC maker's two versions of Windows 95 without the browser. One version excluded all of the browser files. As a result, it did not work. A second version dated back to 1995, before Microsoft bundled Internet Explorer with Windows; it worked, but did not include more recent enhancements. As one would expect, DOJ was not happy with the company's response. Accusing Microsoft of a "naked attempt to defeat the purpose of the court's order," DOJ asked, once again, for a contempt citation and a $1 million-a-day fine.

Microsoft replied that its offer of a dysfunctional or an obsolete system complied with the letter of the judge's order. According to the company, "Microsoft has done precisely what the DOJ requested and what the court ordered [but] now that the DOJ understands the implications of its prior position, it wants to play by a new set of rules." While hearings proceeded on the second contempt petition, DOJ was now willing to go along with the removal of Explorer's icon from the Windows desktop, an alternative that leaves most of the Explorer program still on the system. And Judge Jackson indicated that he too would be agreeable to that solution, since he discovered, on his own, that a court employee was able to uninstall the browser in only 90 seconds.

To avoid a possible contempt citation, Microsoft agreed to comply with the preliminary injunction by offering computer makers two new options: (1) use the Windows 95 "uninstall" function to remove the Internet Explorer icon but leave related software in the operating system, thereby making Explorer harder, but not impossible, to

access; or (2) remove both the icon and most of the related software, thereby making Explorer inaccessible to the ordinary user, but without impairing other features of the operating system. This agreement seemed to satisfy everyone, but the DOJ continued to look for illegal activities by Microsoft.

On May 18, 1998, the United States Department of Justice, and the Attorneys General of 20 States and the District of Columbia sued Microsoft. The main allegations were:

1. Microsoft illegally monopolized the market for operating systems ("DOS's") for Personal Computers ("PCs") under paragraph 2 of the Sherman Antitrust Act.
2. Microsoft had anti-competitive contractual arrangements with various vendors of related goods, such as with computer manufacturers ("OEMs") and Internet Service Providers ("ISP's"), and had taken other actions to preserve and enhance its monopoly; that these contractual arrangements and other actions were illegal under paragraph 2 of the Sherman Antitrust Act.
3. Microsoft illegally attempted to monopolize the market for Internet browsers, but failed to succeed, an act that is illegal under paragraph 2 of the Sherman Antitrust Act.
4. Microsoft bundled anti-competitively its Internet browser, IE, the Microsoft Internet browser, with its Windows operating systems; that this is illegal under paragraph 1 of the Sherman Antitrust Act.

The Department of Justice's accusations were based on their interpretation of Microsoft's intent. Microsoft's efforts to establish Internet Explorer as the dominant web browser were seen as being aimed at eliminating the use of Java. Sun Microsystems had developed a computer programming language named Java, designed so that programs written in it would run on any computer, regardless of the operating system. The Java language is very important for the development of feature-rich Web publishing. Microsoft wanted to create a special Java language for Windows. Its version wouldn't run on non-Microsoft operating systems, eliminating the possibility of the same software running on different computers. This would permit Microsoft to exercise the same type of

proprietary control over MS Java applications that it did over other Windows applications.

Microsoft, a firm known for its aggressive anti-piracy campaigns, spent tens of millions of dollars to develop and promote the Microsoft Internet Explorer, which it gave away. By controlling the browser market, and by destroying Java's promise as a cross-platform language, Microsoft would be in a position to transform the Internet radically by moving toward a new set of Microsoft-owned or Microsoft-controlled standards for Internet publishing and electronic commerce.

Microsoft's defense was based on six arguments.

First, Microsoft argued that the law was on its side since the Court of Appeals had ruled on June 23, 1998 that Microsoft could legally add new features and functions to Windows. Therefore Microsoft argued that it was legal to add Internet Explorer's functionality to Windows, and it had done nothing wrong by integrating Internet Explorer in Windows.

Second, Microsoft argued that it was just competing hard against Netscape and that it did not commit any anti-competitive acts.

Third, Microsoft argued that it did not have monopoly power in the operating systems market.

Fourth, Microsoft argued that competition in the software field was intense and that a new competitor could replace its leadership position at any time. Although this seems to have been a deeply held belief of Microsoft's management, as revealed by the internal e-mails, its economics expert witness failed to convincingly present Microsoft's view of reality to the court.

Fifth, Microsoft argued that it is a leader in software innovation and that it has enhanced rather than hindered the innovation process.

Sixth, Microsoft argued that consumers have benefited from its actions rather than been harmed by them. Microsoft claimed that consumers benefited from its low pricing of the operating system, the free distribution of its Internet browser, and from its enhancement and acceleration of the innovation process. Microsoft also argued, rather

ineffectively, that consumers benefit from the standardization that its large market shares brought to the operating systems market.

The U.S. District Court handed down its "findings of fact" in November 1999, and "conclusions of law" in April 2000. In these rulings the court found for the plaintiffs (U.S. Department of Justice and 19 States) in almost all the allegations against Microsoft. In particular, Judge Penfield Jackson found that the relevant antitrust market is the PC operating systems market for Intel-compatible computers, and that Microsoft has a monopoly in this market "where it enjoys a large and stable market share." Microsoft's monopoly is protected by the "applications barrier to entry," which the judge defines as the availability of an abundance of applications running Windows. Microsoft used its monopoly power in the PC operating systems market to exclude rivals and harm competitors. Microsoft limited the innovation process and therefore their actions harmed consumers. Various Microsoft contracts had anti-competitive implications, but Microsoft was not guilty of anti-competitive exclusive dealing contracts hindering the distribution of Netscape Navigator.

The definition of a market for antitrust purposes is crucial for the determination of illegal activity. Traditionally, an antitrust market definition is based on considering what products can be substituted for the product in question. DOJ proposed, and the District Court Judge agreed, that the relevant antitrust market was the market for operating systems for personal computers that are based on an Intel-compatible Central Processing Unit ("CPU"). In this respect, the judge took a narrow and static view of the market. It is clear that consumers demand applications services from personal computers and would be willing to switch their purchases to non-Intel-compatible PCs if these computers were offered with similar applications as Intel-based PCs and at attractive prices. Thus, non-Intel-compatible computers, operating systems, and software are substitutes for Intel-compatible computers, operating systems, and software.

If one takes a static view and considers the software applications written for each computer and operating system as given and unchanging, as the judge did, then there is no close substitute for Windows that can run as many applications as Windows does. In

this static view, all substitutes for Windows are much less valuable because they can run so few applications compared to Windows. In a more dynamic view, if new software applications can be written for an operating system, an operating system can easily have close substitutes.

A crucial theory of DOJ's and the District Court's argument on monopolization was that there are significant barriers to entry in the market for operating systems for personal computers. Barriers to entry are costs that new suppliers incur but are not incurred by suppliers already in the field. Software has a very large fixed cost and a very low (almost zero) marginal cost. The fixed cost required to create an operating system could create a barrier to entry to the extent that it is already spent by the incumbent(s), while it has to be paid now by an entrant. However, this barrier to entry is not very significant, given the size of the market.

The main barrier to entry could be created by the abundance of applications that run on Windows. It is estimated that Windows runs 70,000 applications, while the Macintosh and the Linux operating systems run far fewer applications. Currently, there are also applications that run on servers connected with the World Wide Web and are essentially independent of the operating system (Windows, Mac, Linux, etc.) of the client. The number of applications that can be run on an operating system can be thought of as a quality index. To judge whether barriers to entry exist, one has to examine if, in the relevant time frame, the entrants are facing higher costs than the incumbent(s).

It is clear that, early in its history, Microsoft understood the importance of having a large selection of applications for its operating systems. To encourage other companies to write applications for Windows, Microsoft built various "tools" into Windows to make it easy for other programs to work with it. For example, Windows and other operating systems include programming code that makes it easy for an application to print to any of a large number of printers. Since this function is available in the operating system, applications developers do not have to write their own programming code to accomplish this function. It follows that applications are now cheaper and quicker to write. Thus, increasing the number of applications available for an operating system, although it may

have a purely competitive justification, both increases the cost of entry in the operating systems market, and creates the potential for anti-competitive exploitation.

On the other hand, to the extent that the incumbent is currently spending resources to attract applications to its operating system, the difference between the costs faced by the incumbent and a potential entrant is reduced, and therefore barriers to entry are reduced. Thus, the existence, extent, and importance of an "applications barrier to entry" depends on an empirical examination of the extent to which Microsoft spends resources in the current time frame to attract applications to Windows, and the extent to which Microsoft has already sunk such costs in past time periods. Such an examination was not performed by the District Court.

The judge ruled that Microsoft has monopoly power in the Operating System market for Intel-compatible PCs. It is generally understood that a firm has monopoly power when it has the sustained ability to control price or exclude competitors. The existence of significant barriers to entry and the very high market share of Microsoft in the operating systems market gave impression that Microsoft had monopoly power. But there was also a very strong indication to the contrary. Microsoft priced its operating system to Original Equipment Manufacturers ("OEMs") at an average price of $40-60, a ridiculously low price compared to the static monopoly price. Microsoft's economic witness showed that they could have charged $1,800, a large multiple of Microsoft's actual price. At first glance, it seems that Microsoft could not possibly have monopoly power in OS's when its OS price is about 3% of the monopoly price.

Understanding and explaining the very low price of Windows is important for understanding what Microsoft's competitive position was and how Microsoft thought of it. Plaintiffs failed to explain Microsoft's pricing by either assuming it away or giving unrealistic explanations. First, the government claimed that pricing significantly above marginal cost was evidence of monopoly power, and that the discrepancy between actual and theoretical monopoly price did not matter. But, any software is priced significantly above marginal cost since marginal cost is zero, and the government has not yet sued other software manufacturers on these grounds.

Second, the government's economic witnesses claimed that Microsoft could not have charged $1,800 for Windows as they had claimed but they did not offer a reasonable estimate of what they could have charged. Third, the government claimed that large market elasticity and revenues from related products were sufficient to justify Microsoft's low price.

Why was the price of Windows low? For the early periods of each operating system, one expects that Microsoft would charge a low price so that independent software developers as well as users accept the operating system and the bandwagon gets rolling. This theory does not explain why Microsoft did not increase the prices of each generation of operating systems as each one matured. It also does not explain why Microsoft did not increase significantly its price of Windows as it doubled its market share in the past four years.

Microsoft's strategy can be said to be anti-competitive based on a theory that Microsoft priced Windows low to hook consumers and generate network effects, while it planned to increase the price "in the future." This theory is particularly unlikely because Microsoft dominates the PC desktop market and has doubled its market share in recent years without increasing the price for Windows while expanding its features. How long will Microsoft wait until it increases the price of Windows? Some even claim that in a network industry, a firm can practice predation without ever increasing the price, but just benefiting in the future from the network effects. But such a strategy is indistinguishable from a truly competitive strategy and benefits the consumers.

A number of other theories have been proposed to explain Microsoft's pricing. Some claim that the fact that software lasts forever limits Windows pricing. It is true that once Windows runs on an overwhelming market share of PCs, the substitute for a new Windows computer is an old Windows computer. The fact that computers and software are both durable makes this true. But very rapid technological change has prompted consumers to buy new computers much faster than traditional obsolescence rates would imply. Even doubling the price of Windows to OEMs would not have implied a significant change to the final price of the combined computer and operating system. So,

durability of software and durability of computers is unlikely to explain the huge difference between the actual price and the static monopoly price.

Others claim that the low price is forced by the ability of pirating software. If that were the case, it would have prompted Microsoft to cut its much higher prices of MS-Office and other software, since pirating takes the same effort and has the same costs for pirates regardless of the type of software being pirated. Furthermore, the control that Microsoft can exert on piracy of the operating system is much greater than on piracy of applications. Therefore, although piracy could have been more of a problem if the OS software was much more expensive, it is unlikely that the price of Windows is low because of piracy considerations.

Finally some claim that Microsoft kept the price of Windows low because that allowed Microsoft to charge more for complementary goods that it produces, such as the Microsoft Office suite. There are three reasons that make this argument unlikely to be correct. First, Microsoft also produces its most popular products, including the Microsoft Office suite, for the Mac. If Microsoft kept the price of Windows low so that is sold MS-Office for Windows at a high price, then the price of MS-Office for Macs should have been lower than the price of MS-Office for Windows, which is factually incorrect.

As stated before, the District Court ruled that Microsoft had monopoly power in the operating systems market. Judge Jackson further ruled that the Internet browser market was separate from the market for operating systems, and that technological and contractual tying of Internet Explorer with Windows raised prices and hurt consumers. The judge ruled that consumers do not want Internet Explorer even free of charge because it burdens the OS with memory and overhead requirements, and it consumes a significant amount of hard disk space. Microsoft claimed that IE was giving crucial functionality to its operating system and had every right to include it in Windows under the terms of the 1995 consent decree, which allowed addition of functions and features to Windows.

But why did Microsoft produce a browser and why did it then give it away? That is, does it make sense from a competitive point of view that Microsoft was giving away the browser at no charge, or was it an anti-competitive act?

The Court's answer to this question, given by judge Jackson in the "Findings of Law" is as follows:

> The fact that Microsoft ostensibly priced Internet Explorer at zero does not detract from the conclusion that consumers were forced to pay, one way or another, for the browser along with Windows. Despite Microsoft's assertion that the Internet Explorer technologies are not "purchased" since they are included in a single royalty price paid by OEMs for Windows 98, it is nevertheless clear that licensees, including consumers, are forced to take, and pay for, the entire package of software and that any value to be ascribed to Internet Explorer is built into this single price.

The obvious problem with this statement is that Microsoft also produced versions of IE for Windows 3.1 (which it had sold years previously and for which it received no additional sales revenue), for the Macintosh (where Microsoft has no stake in the operating system), and for the HPUX and Solaris versions of Unix. All versions of IE are free. So the claim that Microsoft recovers some payment for IE in its license fee for Windows makes no objective sense. IE is free, and the only thing that this or the previous Microsoft II case is about is the packaging used by Microsoft to give away free stuff. In the previous case, the DOJ asked the judge to force Microsoft to give IE away on a CD separate from the pre-installed Windows system. Whether packaging amounts to "tying" is unclear.

In order to understand Microsoft's strategy in selling Windows at a low price, and in giving away Internet Explorer for free, it is necessary to review the relationship between the operating system and the applications software. Microsoft's monopoly in operating systems is protected by the "applications barrier": Consumers want an operating system that has the most applications (word processing, etc.), and applications writers go to the system with the most consumers. This is the "chicken-and-egg" problem

that makes it impossible for competitive operating systems to thrive. But Netscape's browser, which first made access to the Internet easy, also has the capacity to run applications, such as those written in Java, so that if it were used widely enough, neither consumers nor applications writers would care what operating system underlay the browser, and Microsoft's monopoly would gradually erode.

The core of the case was Microsoft's attack on Netscape's browser by, among other tactics, incorporating its own browser into its operating system, thus making it inconvenient and expensive to use Netscape's browser as well. Computer manufacturers had no choice but to take Microsoft's browser; Netscape, having no operating system, could not effectively respond. Microsoft's internal communications made clear that the object of incorporating its own browser in the operating system was entirely predatory, to "cut off Netscape's air supply," and not, as claimed at trial, to increase efficiency or respond to consumer desires. Indeed, Microsoft executives were clear that on the merits, their browser was unlikely to win against Netscape's.

That Netscape, as a company, survived Microsoft's assault is irrelevant. The issue is the destruction of Netscape's threat to the applications barrier that protects Microsoft's monopoly. The browser war is over. Microsoft, having a monopoly of operating systems, did not have to increase its rate of output, and its marginal costs were negligible. Microsoft continued to make profits on the joint product of operating system and browser, while Netscape, lacking an operating system, had to offer its only product, the browser, free, which is certainly below any cost you care to name. It is illogical to say that Netscape was not hurt because it was free to offer its browser for nothing. That is freedom to lose money forever. Some have argued that the tie-in between Windows and Internet Explorer did not result in any profits to Microsoft. However, the tie-in did drive Netscape's browser from the market, and to Microsoft that was worth a great deal.

It is clear that although Microsoft's strategy does not fit the old "robber baron" pattern of monopolies, nevertheless Microsoft is taking full advantage of their dominant position. They are not giving away Internet Explorer due to altruistic motives. They want to continue to dominate the operating system market, and through it control the PC

software industry. Not all Microsoft products are inexpensive. Microsoft's Visual Studio, the programming system used for professional Windows programming, costs more than $1400. Even an upgrade to Office 2000 is more than $250. As Microsoft strengthens its grip on the software market they are raising their prices.

Ralph Nader was only slightly exaggerating when he wrote an article titled "*The Microsoft Menace*" with the subtitle "*Why I'm leading a crusade to stop its drive for cyberspace hegemony*". As he says:

> Microsoft is aggressively seeking to shape the future of personal computing, Internet publishing, and electronic commerce. It has achieved a dominant position in the computer industry already and is poised to extend its reach.

Although the court ruled that Microsoft had violated the anti-trust laws, and ordered the breakup of Microsoft, no one expects that to actually happen. Microsoft immediately appealed the ruling. Since the Bush administration is much more pro-business than the Clinton administration was, Microsoft is expected to survive as a single company, and will probably continue to dominate the PC software market for the foreseeable future.

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The Financial Outlook for the United States and the World at Large

By: Fraidy Zelmanovicz

On November 26, 2001, the National Bureau of Economic Research declared the United States was officially in a recession. The Bureau stated the recession started in March and was exacerbated by the events of September 11th. In addition to the physical and psychological damage, the terrorist attacks of September 11th also inflicted blows on a weak world economy already on the brink of recession. The world now wonders about the magnitude, effect, and duration of the current downturn.

This recession, the tenth since World War II, ended the longest uninterrupted expansion in American history. The flying 90s have ended and the world suffers its first recession in two decades.

There are a number of definitions of a recession. The International Monetary Fund ("IMF") defines 2.5 percent annual growth rate as the breaking point between economic progress and decline (or is it stagnation?). The US barometer for defining a recession is two quarters of consecutive decline in gross domestic product ("GDP"). The indicators reviewed to determine if a recession is approaching are: employment; personal income, minus government transfer payments like welfare; industrial production; and manufacturing and trade sales.

When the economy is doing poorly, the number of individuals unemployed rises sharply. The lack of employment makes those who are jobless have less discretionary income. During a stagnant economy, less is manufactured. This leads to a decrease in trade since there are fewer items to be exchanged.

The malaise in America has spread throughout the world. Many have been, and will continue to be, affected by the weak economy in the United States. This is due to the fact that the world has become a more integrated place in recent years. New technological innovations develop interdependence between nations.

"One by one, every major country is tipping into a rare and possibly lethal recession," said Stephen Roach, chief global economist at Morgan Stanley. "It is far-reaching and deep, and much of that has to do with the fact that we've become much more interconnected." (Kahn, A5). The interdependence among countries is clear in the following examples: After the September 11th attack on New York City, European reinsurance companies which provide insurance to insurers suffered heavily. Tourism and air travel dropped all over the world. Countries like Germany and Japan are sensitive to swings in auto sales in the American market, while the decline in technology sales led to layoffs in Taiwanese semiconductor companies.

Val Koromzay, director of country studies for the O.E.C.D., says that, "It's clear that the global trade has become an extremely powerful transmission channel… We are only beginning to understand the degree to which economies have become synchronized" (Kahn, A5). The US recession impacts cross-border trade and investment, which have increased for decades. Many are now reacting to the global situation by reviewing merger plans. Because businesses are cutting their investments abroad, capital flows to emerging markets are (or have or will depending on your point) decline.

East Asian economies shrank in the second half of 2001, led by Japan's deepening economic crisis. Japan, a country going through a deflationary period, pushed official short-term rates almost to zero, and now has few monetary policy tools to battle its economic woes. Mexico and Canada followed the United States into recession, and their troubles have spread to Argentina and Brazil (Kahn, A5). The Canadian currency suffers from an association with the U.S. given that 85% of Canada's exports head south of the border (Mccarthy, C14).

Argentina's bond market is on the verge of default, and their problems continue to worsen. Argentina now staggers under a $132 billion burden of foreign debt. Billions of dollars of international bailout funds haven't been enough to keep South America's second largest economy from heading for a default on its bonds (Lifsher, A14).

The bonds of Russia and Ecuador have rallied because their prices had become so low that the risk of buying them was reduced (Fuerbringer, BU8). Ecuador adopted the dollar and the shift has given Ecuador the highest 2001 economic growth rate in Latin America. Inflation, which had been over 90% a year, has fallen dramatically (Lifsher, A14). "A country, post default, has a more attractive debt profile," said Matthew Ryan, emerging market debt portfolio manager, and owner of Russian and Ecuadorian debt. "But the country still must be taking steps to address the problems that got them into trouble in the first place (Fuerbringer, BU8).

Ever since communism collapsed the Russian economy has been in a stupor. The Russians, who thought the demise of Soviet rule would bring prosperity to a land long stunted by mis-governance, were dismayed. After the Soviet Union fell apart, crime and corruption became rampant. But, now, during President Putin's term, Russia is getting out of its slump. This is due in part to the rise in oil prices. Russia has become an important world energy producer. This increases consumer confidence in the Russian economy.

Germany's economy is also worsening and is coming closer to a recession. Germany accounts for one-third of the economic output of the 12-country Euro zone, but its growth has lagged behind the rest of Europe for a long time. Because it depends so heavily on exports of automobiles and industrial machinery the country has been hit especially hard by slumping growth around the world (Andrews, C2). Germany's problems are radiating out to its neighbors. Germany, France, Italy and Portugal have less room for budget slippage than other Euro-zone countries at a time of slowing growth because they hadn't built a large enough fiscal cushion during good times (Oyama, A13).

In the Netherlands, one of Europe's fastest growing economies in recent years, economic output shrank. Italian growth was almost negligible, and business confidence in France has dropped to the lowest level in eight years.

In America, consumer confidence is low and unemployment is high, which has led to a sharp decrease in spending. In an effort to increase spending, airlines and hotels

are offering deep discounts; carmakers are offering interest free loans; department stores are offering products at reduced costs due to the surplus of goods that aren't selling. The extent of the price decreases, and the oversupply of products causing them, suggests that the economic recovery is unlikely to be a robust one. Accounting for nearly two-thirds of the GDP, consumer spending has been an important buffer preventing the economy's slide into a full-blown recession.

The United States could suffer an extended period of declining prices, known as deflation, which could deepen the recession. In a deflationary economy, such as now prevails in Japan, wages drop, and people and businesses struggle to pay off debts, which effectively become larger as the value of money decreases. During a deflationary period, people begin to save money instead of spending it because they are worried about layoffs, salary cuts, and debt payments that are due. Also, there is a decrease in spending because they expect the prices of many products to fall in the months ahead.

In an attempt to stabilize the economy, The Federal Reserve has aggressively reduced interest rates. Rate cuts have been lowered ten times since January 1, 2001. They have lowered interest rates to the point that they are practically giving away free money.

A member of the Federal Reserve said that it should not shy away from continuing to ease monetary policy aggressively just because its benchmark interest rate is beginning to approach zero (Stevenson, C3). In the event that the economy does not recover or encounters an unexpected shock like another terrorist attack, rates may have to be lowered for an again this year. Also, the Fed has to keep in mind the possibility of deflation, a general decline in prices, a development that would require rapid rate reductions.

If not for the rate cuts many transactions would not have occurred. Some of which are, car dealers would have been unable to offer zero interest loans. Home sales and home construction, as well, owe their strength to 30-year mortgages because as mortgage rates fell, families that already owned homes refinanced them and pocketed the savings from the lower monthly payments. Or they took out low interest home

equity loans and paid off high interest credit card debt (Uchitelle, BU4).

There are those who believe that the rate cuts are not enough to reverse the decline in the economy, and they argue that the government must move quickly to make up for the shortfall through a combination of public spending, subsidies and tax cuts. Congress is trying to pass a stimulus package that will attempt to pull the economy out of the economic downturn.

Given the contentious philosophical differences between the two parties, the content of the stimulus package won't please everyone. Republicans are pressing for a bill that will provide tax relief for corporations while Democrats want a plan that would expand unemployment benefits and subsidize health insurance premiums for laid off workers.

It is clear that the only solution for the economy is for the federal government to switch tactics by moving from a budget surpluses to budget deficits. Support for this approach is beginning to broaden beyond its usual liberal base. Advocates say that the most important thing right now is to direct money to those who will spend it, mainly through more unemployment benefits, increased number of grants to the states, more military spending and bigger outlays for public works projects i.e., school repair and highway maintenance (Uchitelle, C4). By doing the aforementioned, more money will be in circulation, which would boost the economy. This approach resembles Keynes's reasoning, in which he states that, for the purpose of economic stimulus, the form of spending isn't very important. Most of the money spent would find its way quickly into the GDP.

Whatever the fiscal stimulus, it should not be a long-term package. Rather it should be temporary, fading out as the economy revives. The advocates want to include carefully aimed tax cuts in their plans; for example, they want to offer a tax benefit for companies that increases investment, but only if they do so quickly. "You want something that has a substantial kick in the next six months and is nearly entirely gone in twelve months," said Robert Greenstein, executive director of the Center on Budget and Policy Priorities. "You can always extend the stimulus if something goes wrong"

(Uchitelle, C4).

Paul Volcker, a former chairman of the Federal Reserve, states, “My view is that the federal government should spend a lot of money, and it will… Tax cuts do not make a lot of sense either as tax policy or as short run stimulus. They are doubly damned.” He feels that tax cuts are too uncertain. A tax break may not persuade a family to increase its spending if it is already deeply in debt. However, if the government would provide jobs to the citizens, then that is more effective than tax cuts, and a family will be less wary about spending money (Uchitelle, C4).

A tax holiday was also suggested which would give workers and employers a one month break from the 6.2 percent payroll tax that each pays into the Social Security Trust Fund. Self-employed people would get to keep the entire 12.4 percent for a month. The holiday proposal would essentially replace rebate checks for lower income workers.

Increased unemployment benefits would add more spending in a short time. So would subsidized health insurance premiums for unemployed workers who had lost company paid benefits. Due to the many layoffs that have occurred because of the slowing economy, there are many in need of unemployment benefits and likewise are unable to pay for health insurance. Government assistance is necessary for the unemployed in order for survival.

The terrorist attacks did not cause the nation’s economic problems, but they might have been enough to make the difference between a pronounced slowdown and a formal recession. Before the attack, the United States economy was doing poorly but the situation may have been too mild to qualify as a recession. However, the terrorism attacks turned the bad situation into an even worse one. The recession in America will not just affect America but will spread throughout the world because of the interdependence among countries.

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Culture and Ethnicity in Consumer Decision Making

By: Yitzie Pretter

One of the most important aspects of doing business with people from various cultures and ethnicities is understanding the differences in their values and the differences in their consumer needs. Since marketing is based upon satisfying the needs of the customers, successful marketers need to become aware of these cultural differences and target their products and services accordingly.

Cultural and ethnic differences can be seen in a variety of circumstances, such as language, religion, food preferences, color, nonverbal communications, and societal manners and customs. People are generally proud of their specific language. Therefore, marketers must take care to avoid blunders in this area.[1] They need to avoid mistranslation, misunderstanding slang or idioms in the native language, and incorrect use of a dialect. For example, Exxon's Japanese brand name, "Esso," means "stalled car" when pronounced phonetically in Japanese. This obviously turned off potential Exxon consumers. And when Budweiser advertisers used the Spanish translation for "the King of Beer" they didn't realize that beer is a feminine noun – so that Budweiser Beer could not be the King, but must be the Queen of Beers. The advertising campaign had to be re-tailored to better fit the Spanish culture.[2]

In contrast, smart marketers can sometimes use cultural differences to their advantage. With regard to religious cultural differences, for example, Polaroid was able to successfully market their instant cameras in Saudi Arabia by emphasizing to Arab male consumers of Islamic traditions that through instant photography they were able to photograph their wives and daughters in the privacy of their homes, without exposing them to strangers working in the processing lab. [3]

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[1] David Ricks, Blunders in International Business, Cambidge, MA: Blackwell Publishers, 1983.
[2] Huberto Valencia, "Point of View: Avoiding Hispanic Market Blunders." Journal of Advertising Research, 23 (December/January 1984): 19-22.
[3] Paul A. Herbig, Handbook of Cross-Cultural Marketing. NY: Haworth Press (1998).

Next to language, food preference is the most culture-sensitive topic. For example, the instant drink, Tang, was difficult to market in France because the French drink little orange juice, and almost none at breakfast. Instead, Tang changed their strategy to market the drink as a refreshment, good at any time. Similarly, when General Foods introduced Jello to Great Britain in the American style, the British were not interested in the powdered form. As a result, General Foods now sells Jello in its jelled form.

Even such a simple factor as color can have different implications for people of different cultures. Blue is considered by Americans to be the most masculine of colors. However, in France and Britain, it is red. While Americans consider pink very feminine, most of the world considers yellow to be the most feminine color. In China and Japan, the color gray is associated with cheap products. In contrast, in the US gray is associated with greater expense, high quality, and dependability. Color is therefore another cultural factor that must be considered by marketers seeking to influence consumer decision-making.[4]

Nonverbal communications include facial expressions, eye contact, gestures, body movements, posture, physical appearance, space, and touch. The meanings of nonverbal communications vary from culture to culture. When advertisers market products, they need to keep in mind the cultural differences. For example, the Japanese often use silence to project a favorable impression. They frequently say little and can even occasionally close their eyes while others are speaking, to help them concentrate. To many Americans, Japanese politeness can come across as phony. However, to the Japanese, an American's directness and loudness can appear as a lack of self-control. So advertisements that portray the main actors as brash and in-your-face can repel Japanese consumers, who will associate American over-aggressiveness with the product or service advertised and decide to turn it down.

Another point for marketers to consider is that people living in different countries have different life experiences. Marketing decisions are based on the priorities they have

set for themselves, according to their individual cultural perspectives. For example, cigarette consumers in wealthy countries such as the US are willing to pay extra money to have their cigarettes filter-tipped. They are more aware of the health risks related to smoking and are willing to pay more for the filter tip. However, in poor countries, where the life expectancy is rarely more than 40 years, threats of cancer may seem less real and can be more easily ignored. For such consumers, the extra cost is not worthwhile.

Just like there are cultural differences between countries, the American society as well cannot be treated as one whole. It is really made up of many ethnic subcultures, each with its own distinct set of values and norms. Culture is defined as "the values, ideas, artifacts, and other meaningful symbols that help individuals communicate, interpret, and evaluate as members of society." [5] Ethnicity is similarly defined as "pertaining to a social group within a cultural and social system that claims or is accorded special status on the basis of complex, often variable traits, including religion linguistics, ancestral or physical characteristics."[6] Both these factors are important in considering consumer decision-making.

Marketers are learning that they cannot treat Hispanics, Asians, and African-Americans as one large cultural melting pot, for their cultural backgrounds are not the same. These three populations have a combined buying power of over a trillion dollars. In addition, the number of different ethnic populations is rapidly growing, because of the continuing stream of immigrants from Russia, Poland, and the Middle East.

In the past, ethnic marketing was practiced by a handful of black and Hispanic-owned companies, focusing on the fields of health and beauty aids and food. But more recently, companies such as Soft Sheen Products and Goya Foods have been joined by others, such as Procter and Gamble and Sara Lee. The reason is that recent US Census reports have shown the growing number of minorities. Lafayette Jones, executive vice president of Segmented Marketing Services Inc., a consulting firm that specializes in

[4] Lawrence Jacobs, Charlie Keown, Reginald Worthley, and Kyung-Il Ghymn, "Cross-cultural Colour Comparisons: Global Marketers Beware." International Marketing Review, 8/3 (1991):21-30.
[5] James F. Engel, Martin R. Warshaw, and Thomas C. Kinnear, Promotional Strategy: Managing the marketing communications process.

ethnic marketing, calls the data from the US census, "a wake-up call for marketers." Gary Berman, president of Market Segment Research, a firm specializing in ethnic market research, said, "it should come as no surprise that at least half of all Fortune 500 companies have launched some ethnic marketing initiatives." [7] For example, leading retailers, including J. C. Penny, Montgomery Ward, and Sears, Roebuck and Company have announced plans to sell merchandise specifically targeted to black and Hispanic consumers.

An example of these recent advances can be found in the field of telecommunications. New immigrants spend a large proportion of their funds on international long distance calls. In some cases, they spend as much as 50% of their income calling their country of origin. Because of this, AT&T, MCI, Sprint, and GTE have found an opportunity for ethnic marketing. A new player in the field, Telefonos de Mexico (Telmex), teamed up with Sprint to form Telmex-Sprint Communications. They are targeting the Mexican-American or Latino and Hispanic communities throughout the US.

The Hispanic market now totals nearly 30 million people in the United States, comprising more than 11% of the total population. By 2050, Hispanics are expected to make up almost a quarter of the population. The Hispanic segment is already larger than the entire population of Canada, with the spending power of over $350 billion, making it a worthwhile community for marketers to consider.

The Hispanic market is the easiest segment of the population to define, because of the common Spanish language. Even though Asian-Americans share the same race, they do not all share the same language. Chinese, Japanese, and Koreans do not speak the same language. Even within the Chinese-American market, the language spoken will vary according to the individual's place of origin (e.g., Mainland China, Hong Kong, or Taiwan).

[6] "Telecom Marketing Opportunities to Ethnic Groups: Segmenting Consumer Markets by Ethnicity, Age, Income and Household Buying Patterns." The Insight Research Corporation. (1999).
[7] Michal J. McDermott, "The Ethnic Market Offers Many Opportunities." (2001).

Jose Pina, manager of the Hispanic Division of Acosta Sales and Marketing noted, "Hispanics want to feel 'culturally welcomed' in your store." He explained that this can be accomplished by using cultural icons and symbols, bright colors, bilingual signs, and hiring Hispanic employees. He added, "Retailers who want to reach foreign-born Hispanics should emphasize branded items from the homeland and de-emphasize US brands, emphasize bulk foods, recognize traditional religious holidays, and offer bilingual point-of-sale materials."[8]

The Asian-American consumer population is fast-growing as well, with a market of 10.5 million. On a yearly basis, Asian-Americans constitute the largest group of immigrants to the United States, with an annual purchasing power of $101 billion. With an average age of 30.1 years, this market is younger than the general market and has the highest average household income in the country. Because of the Asian preference for multi-general households, they also have a larger than average household size. Asians are known to adapt easily to new technology and to be willing to spend their above-average income on this technology. AT&T has made use of this information and geared promotional advertising for high-tech services to the Asian community.

The African American population has a purchasing power of $450 billion and continues to spend more than their white counterparts on luxury items such as cars, clothing, and home furnishings. Many marketers have come to realize that they can target this market over the Internet. So such websites as www.netnoir.com and www.afronet.com are at the forefront of attracting hundreds of thousands of African Americans.[9]

It is not that simple to correctly target ethnic markets. Special attention must be paid to make sure that the products or services being promoted are true to the culture they mean to attract. For example, Mattel Inc. produced black Barbie dolls that, except for their skin color, were identical to their white Barbie dolls. But consumers were dissatisfied with this half-hearted measure. This prompted Olmec Corporation, a New

[8] "Produce Marketing Associates Fresh Summit 2000 Workshop Summary: Reaching Ethnic Consumers. Produce Marketing Association.

York-based black-owned company, to introduce Imani, a Barbie-type doll with authentic African-American feature. This product was an instant hit with black consumers.

Major cultural festivals and holidays present unique opportunities for marketers to target consumers. During this time of year, wise marketers welcome the chance to approach consumers at cultural events in their own communities and demonstrate that their patronage is appreciated. As Saul Gitlin, director of Strategic Marketing Services of Kang & Lee Advertising Inc. said, "Acknowledging cultural events and holidays is a way to build a bond, a way to show commitment and a way to recognize their diverse lifestyles."

The important holidays in the Asian market include Asian Lunar New Year, which is celebrated by the Chinese, Korean, and Vietnamese communities, and the Moon festival, celebrated by Chinese and Koreans. Christmas and January 6, Los Tres Reyes, are important holidays that unite all the Hispanic communities. For African-Americans, Kwanzaa, the period of time between Christmas and New Years is especially important. Important also is Martin Luther Kings' birthday in January and the month of February, Black History Month.

Howard Buford, the president of Prime Access Inc., multicultural marketing firm specializing in advertising and direct marketing suggests that during February, "if a retailer is selling clothes, now is the time to bring out the prints with the African influence." He explained that many minority consumers feel as though they are members of "out groups." They do not feel included in mainstream advertising. Therefore, when a marketer does something that is clearly aimed for them, it strengthens the consumer-marketer relationship. "It tells them you're thinking about them, that they're important. It's not just a matter of including them in ads."

Indeed, with regard to advertising, marketers must take care not to seem as though they are exploiting cultural differences just to make money. They have to be cautious not to reinforce the idea of segregation and market segmentation in a negative way. Cynical consumers may see targeted marketing as bids to win them over for the financial profit

[9] Lisa Skriloff and Dawn Cornitcher, "Multicultural Marketing: A Marketing Imperative." Multicultural

alone. As AT&T spokesman Burke Stinson observed, "When you're advertising to special markets, the only way it works is if the company does not appear to be paying lip service."[10]

Research had pointed to the importance of targeted advertising. It has indicated, for example, that advertising in Spanish is more effective in Hispanic audiences. According to a study by the Roslow Research Group, bilingual Hispanics found English-language ads 38% less effective than Spanish-language ads in terms of ad recall. In addition, they found English-language ads 70% less persuasive and 27% less effective than Spanish-language ads in giving over their main message. So it is worthwhile to figure out advertising strategies that will both be sensitive to the community and effective in its message.

The trick is also to figure out a way to fit in with the consumers' lifestyle. For example, Verizon recognized that African-Americans frequently use the Internet and therefore teamed up with BET.com, the Internet arm of Viacom's BET Holdings, to offer financial incentives to African-American Internet users who also use Verizon services.

In conclusion, culture and ethnicity play a major role in consumer decision-making and the concepts discussed above must be included in all marketing strategies.

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