

Copyright is owned by the Author of the thesis. Permission is given for a copy to be downloaded by an individual for the purpose of research and private study only. The thesis may not be reproduced elsewhere without the permission of the Author.

110.899 Thesis

Presented in partial fulfilment of the requirements for MBS degree

**Mandatory Recognition of Externalities, Price Elasticity and the Market
Value of Firms**

Name: John Mead

Student ID: 03400816

School of Accountancy

Massey University

2009

Mandatory Recognition of Externalities, Price Elasticity and the Market Value of Firms

ABSTRACT

The scene for environmental performance and disclosures is changing rapidly from that of a voluntary state to one where both are being mandated. One such regulatory initiative is that of the European Union Emissions Trading Scheme (EU ETS), under which all firms within certain industries have to comply with similar environmental performance and disclosure requirements. The imposition of such requirements can have both adverse and beneficial effects on firm value. The purpose of this study is to examine how EU ETS membership affects the market value of European firms. Using a sample of 1,985 firm-year observations from Great Britain, France, Germany, Spain and Italy, I find that joining the EU ETS has a positive impact on firm value, and this impact is larger for firms with high price elasticity of demand (PED). These findings suggest that a regulated environmental performance and environmental disclosure setting is likely to reduce uncertainties pertaining to externalities, in particular, for firms which are unable to shift their externality costs to their consumers.

ACKNOWLEDGEMENTS

This paper has benefited from presentations at Massey University. I appreciate helpful comments and suggestions from Asheq Rahman and Steve Courtenay, (supervisors), and Paul Dunmore, Jill Hooks, Michael Bradbury, Natasja Steenkamp, Nicholas Smith, Helen Bishop, and Warwick Stent. I also wish to thank Andrew Brown for technical support.

TABLE OF CONTENTS

	Page
Abstract	1
Acknowledgements	2
Table of contents	3
List of tables	4
Introduction	5
Background	8
Literature review	16
Hypotheses	24
Sample selection and variable measurement	30
Results	34
Discussion	45
Conclusions, limitations & future research	49
References	53
Appendix 1	71
Appendix 2	75

LIST OF TABLES

	Page
Table 1: Sample details	59
Table 2: Carbon allowances	60
Table 3: Descriptive statistics for all countries	61
Table 4: Descriptive statistics all industries	63
Table 5: T Tests	64
Table 6: Correlations merged	65
Table 7: Regressions H1	66
Table 8: Regressions H2	67
Table 9: Regressions H3a	68
Table 10: Regressions H3b	69
Table 11: Regressions industry sectors	70