

TWO ESSAYS ON TOURNAMENT THEORY

Michael Robert Melton, Ph.D.

University of Nebraska, 1999

Adviser: Thomas S. Zorn

This study empirically examines the implications of tournament theory in two very different contexts. In the first essay, we examine whether or not there are incentive effects in professional golf tournaments. In the second essay, we examine whether or not the behavior of mutual fund managers is characterized by tournament-like behavior.

Using data from the 1994 and 1995 Senior Professional golf Association Tours, the first essay tests the effectiveness of rank-order tournaments in motivating effort in an explicitly designed tournament. Previous research using data from golf tournaments has contradictory findings on the effect of prize money on incentives. Ehrenberg and Bognanno conclude that the tournament prize money does influence players' performance. Orzag concludes that the level of tournament total prize money has an insignificant effect on players' performance. In order to resolve the conflicts from previous tests, the Senior PGA Tour is chosen for its unique format where players are not eliminated from the tournament before completion. This format eliminates any survival bias. The findings of this study are consistent with the hypothesis that the level and structure of prizes in Senior PGA tournaments influence players' performance.

Empirical investigation of the tournament model has not been limited to the realm of sports. In fact, much research has been devoted to determining whether or not mutual fund managers behave as if they were in a tournament. Previous research find that funds defined as "growth oriented" exhibit tournament-like behavior. In the second essay, we examine whether other categories exhibit tournament-like behavior. This study concludes that tournament-like

behavior is not as prevalent in other categories of the mutual fund industry. The motives for investing in those may be different. For example, investors may choose International or Global funds for diversification. Other investors may choose to invest in Sector funds because they are optimistic about a particular sector. Such motives may make investors less sensitive to ordinal rankings. In either case the evidence indicates that these funds do not appear to exhibit tournament-like behavior.