

This article (Financial Times, 1/29/07) refers to the international rankings of business school MBAs. One criterion used in the rankings is the starting salaries of the schools' MBA alumni. To make relevant international comparisons, the FT uses PPP (as discussed in the article below.) I have attached a FT ranking after the article. If you want to explore these rankings further, there is a very cool interactive ranking platform at the FT site. Go to: <http://rankings.ft.com/global-mba-rankings>

## **Global MBA 2007**

### **Purchasing power parity rates: Meaningful comparisons mark the choice of methodology**

By Ursula Milton

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The Financial Times rankings aim to provide a global overview of business education and to publish data which enable comparisons between the best programmes on offer around the world. For this reason, for all its business school rankings, the FT uses purchasing power parity (PPP) conversion rates published by the World Bank – not exchange rates – to convert alumni salary data to US dollar equivalents.

These rates were first used in the 1970s to allow meaningful comparison of economic data, such as gross domestic product, between countries. The rates are used in preference to exchange rates because, as the World Bank states, “market exchange rates are based on short-term factors and are subject to substantial distortions from speculative movements and government interventions”.

However, the PPP approach does have some potential drawbacks. One is the difference that might exist between the consumption profile of an average MBA graduate and that represented by the basket of “standard” consumer goods from which PPP rates for each country are derived.

Leonard Cheng, professor of economics at the Hong Kong University of Science and Technology (HKUST), feels that the supposed higher-spending profile of an MBA graduate could create a PPP conversion problem that is particularly relevant to graduates who are earning and spending their post-MBA salaries in China.

“It is not a secret that upscale and luxurious consumption goods are more expensive in China than in Hong Kong (that is why China tourists come to Hong Kong to buy lots of them), which would be opposite to the relative cost of living of median income earners in Hong Kong and China. Thus, the PPP [...] could be very misleading for measuring the real purchasing power [of MBA graduates in China and Hong Kong].”

In the FT rankings, the average salaries of business schools based in China have been consistently very high. PPP conversion rates also make the average salaries of graduates living and working in South America, Africa and Australasia seem enticing. It is worth noting that the conversion rates for these countries have been relatively stable. The Brazilian real and Australian dollar rates, for example, changed by less than one percentage point between 2004 and 2005.

David Parsley, associate professor of management at the Vanderbilt's Owen Graduate School of Management, makes the point that salaries seem higher in these countries because they genuinely are

much cheaper places to live. His research suggests that the much lower cost of labour in these countries is an important factor in lower prices.

A second HKUST economics professor, Francis Liu, presents another potential problem of using PPP rates to analyse the salaries of MBA graduates: “A large percentage of MBA graduates...work in expensive cities such as Beijing or Shanghai. The PPP data from the World Bank apply to the average cost in the country and therefore are inappropriate for Shanghai or Beijing.”

However, empirical evidence suggests that this pattern of MBA employment – most are working in major centres – holds true for MBA graduates around the world. Therefore, this bias will affect salary conversions for all countries, although it will be particularly strong in large countries in which there is a big discrepancy in the cost of living between regions.

Prof Parsley’s research examines price discrepancies within the US. As might be expected, the purchasing power of MBA graduates who remained in Nashville (the home of Vanderbilt University) after graduating was much greater than that of alumni who moved to cities such as Boston, New York and Los Angeles on similar salaries.

That said, PPP rates are still the best tool for converting and analysing the salary data collected for the rankings. This is particularly true as MBA graduates are an internationally mobile bunch, often working in several countries within the five-year window surveyed by the FT. Nearly a quarter of all respondents report salaries in more than one currency during this brief period of their careers.

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