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Campbell Harvey (Duke): Half the financial products are false! (/e/35657807c235e8L/)

HALF THE FINANCIAL PRODUCTS ARE FALSE!



00:26:22

My guest today is Professor Campbell Harvey from Duke University.

Mr Harvey is Professor of Finance at the Fuqua School of Business, Duke University. He served as President of the American Finance Association in 2016.

Prof Harvey received the 2016 and 2015 Best Paper Awards from The Journal of Portfolio Management for his research on distinguishing luck from skill. He has also received eight Graham and Dodd Awards/Scrolls for excellence in financial writing from the CFA Institute. He has published over 125 scholarly articles on topics spanning investment finance, emerging markets, corporate finance, behavioral finance, financial econometrics and computer science.

Our conversation covers a wide range of topics. For the convenience of the listeners, I have split our conversation into 2 parts. The current episode is the first part, in which we mainly talked about how to distinguish luck from skill in financial investment.

I have asked Prof Harvey some interesting questions, such as:

1) You mentioned that in the field of physics, scientists apply much tougher standard to quantify significance in any finding. For example, they need a 5 sigma significance to declare a discovery.

Why do you think the same standard is not applied in finance, that we are happy with a2-sigma significance?

2) What about Buffett's theory of all the coin flipping champions come from the same Graham-Doddsville village?

In that famous letter, he mentioned a few names such as Walter Schloss, Tom Knapp, and of course himself who are all successful active managers. I am not sure that these managers will be able to pass a test of 5 sigmas mentioned in your paper.

Therefore is it a reasonable strategy for investors to bet on style and reputation, given the realistic constraint that it is very difficult to tell luck from skill, and most empirical research in finance is likely to be false anyway?

3) You concluded in your paper that: Most of the empirical research in finance, whether published in academic journals or put into production as an active trading strategy by an investment manager, is likely false. Half the financial products that companies are selling to clients are false.

Then what shall we investors do?

I hope you enjoy the conversation. Our contact: info@woodsfordcapital.com

Reference:

Evaluating Trading Strategies (<https://ssrn.com/abstract=2474755>)

Backtesting (<https://ssrn.com/abstract=2345489>)

The Cross-Section of Expected Returns (<https://ssrn.com/abstract=2249314>)

Lucky Factors (<https://ssrn.com/abstract=2528780>)

Detecting Repeatable Performance (<https://ssrn.com/abstract=2691658>)

Decreasing Returns to Scale, Fund Flows, and Performance (<https://ssrn.com/abstract=2990737>)

The Scientific Outlook in Financial Economics (<https://ssrn.com/abstract=2893930>)

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