Researcher Examined Over 400 Stock Market Strategies, Here Are The Top 1%
Academics have hunted for ways to beat the market for decades. Unfortunately there’s a problem with all those years of investigation. It’s rooted in statistics when a large number of ideas are tried. A detailed analysis determines that just four factors out of four hundred might offer the best chance of beating the market over time.

**Data Mining**

In recent years two things have grown exponentially for financial researchers. These are computing power and stock-market datasets. When academics were doing manually intensive and slow analysis decades ago, finding a stock market anomaly that had perhaps a 1 in 50 chance of randomly occurring was actually rare and impressive.

However, now academics can run 50 tests while they have lunch. As many more relationships and ideas are tested, so more apparent opportunities will be found, but maybe they aren’t quite a good as they appear.

**False Positives**

The bad news is that a lot of these could be false positives. When you’re testing hundreds of ideas, something having a one in a hundred chance of being random is, in fact, routine. In fact, if you’re testing a thousand ideas, then you’ll often find one that’s a one in the thousand. It’s similar argument to how if you give enough monkeys enough typewriters, then...
one will eventually write Shakespeare. But that will just be dumb luck.

That’s why Campbell Harvey and Yan Liu in their paper *A Census of the Factor Zoo* look to find the handful of investment approaches that really rise to the top. That means current research that really aces statistical tests, or older research that has good statistical results for the time.

Taking this approach shows that four anomalies are notably robust, based on statistical testing. These are value, momentum, durable consumption goods and long-run volatility.

Of course, that doesn’t necessarily mean that other factors fail, but that we can’t be as sure of their merits based on statistics alone. From another direction, even these four, look good based on past data, but that could all change in future, and some suggest that maybe it already has.

**The Winners**

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**What This Means**

To put these four strategies in simple terms, value means buying stocks that appear less expensive than others. This based on their financial reporting such as stocks with low price to book values. In essence, owning cheap stocks. Momentum means buying stocks that have risen more than average in recent months. Durable consumption goods means buying companies that make durable goods like cars and home appliances, since they can show better risk-adjusted returns over the economic cycle. Long-
run volatility means that stocks that have less extreme price movements tend to show better risk-adjusted performance.

It should be noted that statistical testing is not the only appropriate test for investment strategies. Sometimes too much back-testing can be a problem. Strategies that can be explained and hold up over different countries, market segments and time periods might also be said to be more robust. Nonetheless, setting a high statistical bar can be a powerful way to highlight better strategies.

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