MARKET ANOMALIES

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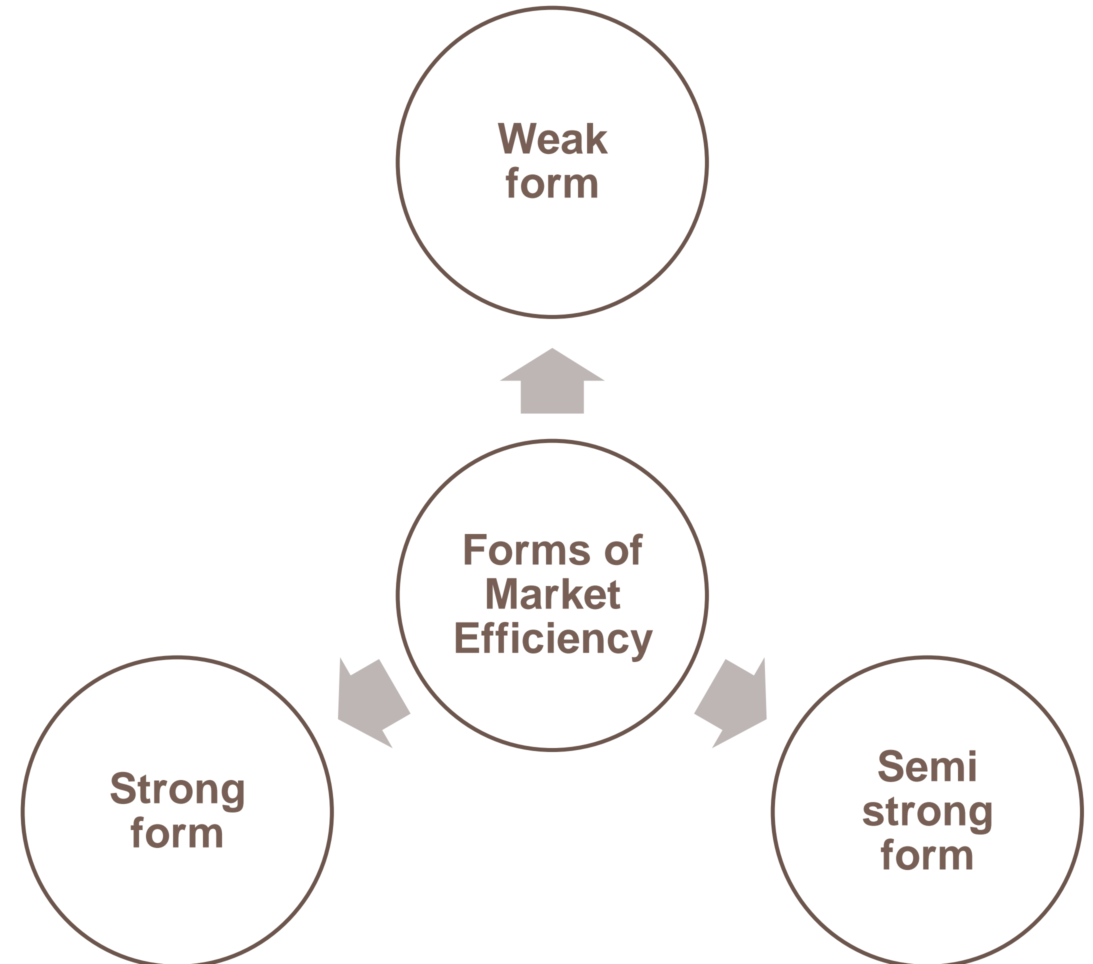
INTRODUCTION

- Fama (1970) stated, “A market in which prices always fully reflect available information is called efficient.”
- Efficient market is the one where available information is quickly translated to prices.
- Anomalies are the unpredictable behaviour observed in the markets which are inconsistent to the existing financial theories.

MARKET EFFICIENCY AND ANOMALIES

- Efficient market hypothesis states that markets are rational and all available news and information are reflected in stock prices. It also states that investors make timely decisions and hence all the available information are automatically reflected in stock prices.
- Fama (1970) defined efficient market as "a market with large numbers of rational profit maximizing individuals actively competing with each other and doing attempts to predict future market values of individual securities, and where all important relevant information is almost freely available to all investors."



FINANCIAL MARKET ANOMALIES

FUNDAMENTAL ANOMALIES

- ***Value anomaly***
- ***Low Price to Book Ratio***
- ***High Dividend Yield***
- ***Low Price to Earnings (P/E)***
- ***Neglected Stocks***

TECHNICAL ANOMALIES

- **Moving Averages**
- **Trading Range Break**

CALENDER ANOMALIES

- ***Effect on the Weekend***
- ***Effect due to Turn-of-the-Month***
- ***Effect due to Turn-of-the-Year / January Effect***

RESEARCH REVIEW ON MARKET ANOMALIES

- Lakonishok et.al, (1988) analysed daily data of returns for a period of 90 years to study the seasonal patterns in rate of returns for Dow Jones Industrial Average and found the evidence of persistent abnormal returns during the turn of the week, month, year and around holidays.
- Hawawini and Keim (1995) examined the predictability of equity returns. Anomalies are the existence of cross- sectional and time series patterns in stock returns which cannot be predicted by extant theory. They focused on the most robust findings of the evidence of predictive returns. They judged robustness in terms of both time and the number of stock markets in which they have been observed.
- Ariel (1987) in his study established that mean stock returns are positive only for days that are immediately before and during the first half of calendar months, and cannot be distinguished from zero for days during the last half of the month. The study claimed that this ‘monthly effect’ is distinct from other calendar anomalies such as the January effect. The study says that this “month effect” can be due to a shift in the mean of the distribution of returns from days in the first half of the month relative to days in the last half.

CONCLUSION

- It can be concluded that the well-known anomalies like size effect, value effect, weekend effect, etc. does not hold for different sample periods. As the literature reveals that size effect and value effect disappear after they have been high lightened. In a similar fashion, the predictive power of weekend effect and dividend effect have become week. The effect of small-firm turn-of-the-year became weaker in the years after it was first documented in the academic literature. The predictive powers of dividend yields or inflation in predicting stock returns have become weak after their documentation.

Thank You

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EXPECTED UTILITY THEORY, AGENCY THEORY AND LIMITS TO ARBITRAGE

Continued…