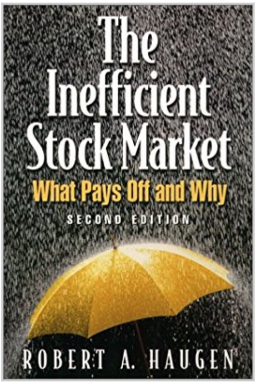

The Inefficient Stock Market

By Robert A. Haugen

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Sparked with wit and humor, this clever and insightful book provides clear evidence that the stock market is inefficient. In the author's view, models based on rational economic behavior cannot explain important aspects of market behavior. The book tackles important issues in today's financial market in a highly conversational and entertaining manner that will appeal to most readers. Chapter topics include: estimating expected return with the theories of modern finance, estimating portfolio risk and expected return with ad hoc factor models, payoffs to the five families, predicting future stock returns with the expected-return factor model, super stocks and stupid stocks, the international results, the topography of the stock market, the positive payoffs to cheapness and profitability, the negative payoff to risk, and the forces behind the technical payoffs to price-history. For anyone who wants to learn more about today's financial markets.

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Editorial Review

From the Back Cover
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About the Author

Robert A. Haugen is Emeritus Professor of Finance at the University of California, Irvine. Professor Haugen has held endowed chairs at the University of Wisconsin, the University of Illinois, and the University of California. He is the author of more than 50 articles in the leading journals in finance and 13 books, including *The Incredible January Effect*, *The New Finance*, *Beast on Wall Street*, and *Modern Investment Theory*. He serves as Managing Partner to Haugen Custom Financial Systems, which licenses portfolio management software to 25 pension funds, endowments, and institutional and high-net-worth money managers. Visit Robert Haugen's Web site at: ***www.bobhaugen.com*** .

Factor models have been widely employed in the investments business for decades. Quantitatively oriented managers have used them to control the month-to-month variation in the *differences* between the returns to their stock portfolios and the returns to the stock indices to which they are benchmarked. These models employ a wide variety of ad hoc factors that have been shown to be effective in predicting the risk of a stock portfolio.

Factor models have also been widely discussed in academic finance. Finance professors have long searched for the factors that account for the extent to which returns are correlated stock to stock. The professors have correctly concluded that the correlations can be *explained* by a few factors, such as unexpected changes in industrial production, inflation, or interest rates. This is not to say that these few factors can match the success of the wide variety of ad hoc factors used in the business for *forecasting* risk.

The professors have also used factor models to explain why stocks have differential expected returns. These models are theoretical in nature, and are derived under the assumption that pricing in the stock market is efficient and rational. If it is not, a wide variety of ad hoc factors may be useful in explaining and predicting expected stock returns.

Until recently, ad hoc factor models have not been employed to predict the expected return to stock portfolios. Surprisingly, the factor models are much more powerful in predicting expected return than they are in predicting risk. The purpose of this book is to demonstrate and explain the nature of this power.

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