Alternative Investing

The Less-Efficient Market Hypothesis

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Market efficiency is a central issue in asset pricing and investment management, but while the level of efficiency is often debated, changes in that level are relatively absent from the discussion. I argue that over the past 30+ years markets have become less informationally efficient in the relative pricing of common stocks, particularly over medium horizons. I offer three hypotheses for why this has occurred, arguing that technologies such as social media are likely the biggest culprit. Looking ahead, investors willing to take the other side of these inefficiencies should rationally be rewarded with higher expected returns, but also greater risks. I conclude with some ideas to make rational, diversifying strategies easier to stick with amid a less-efficient market.

Read the full paper here.