and fund managers who manage their portfolios actively, on the basis of value investing strategy, can earn above-average returns.

As explained earlier in our literature review, researchers contend that value strategies produced higher returns because they are contrarian to naïve strategies followed by other investors. These naïve strategies include extrapolating past earnings growth too far into the future, thus assuming a trend in stock prices even though the future does not warrant such extrapolation, overreacting to good or bad news, or simply equate a good investment with a well-run company irrespective of price.

An alternative explanation of why value strategies have produced superior returns is that they are fundamentally riskier. That is, investors in value stocks bear higher fundamental risk and their higher average returns are compensation for this risk.

References

1. Bachelier, L. (1900), Theory de la speculation in random character of stock market prices, Ganthier Villars, Paris