Does Peer-Reviewed Research Help Predict Stock Returns?

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Abstract

Mining 29,000 accounting ratios for t-statistics over 2.0 leads to cross-sectional return predictability similar to the peer review process. For both methods, about 50% of predictability remains after the original sample periods. Predictors supported by peer-reviewed risk explanations or equilibrium models underperform other predictors post-sample, suggesting peer review systematically mislabels mispricing as risk, though only 20% of predictors are labelled as risk. Data mining generates other features of peer review including the rise in returns as original sample periods end and the speed of post-sample decay. It also uncovers themes like investment, issuance, and accruals—decades before they are published.

First posted to arxiv.org: December 2022. E-mails: andrew.y.chen@frb.gov, Alejandro.Lopez-Lira@warrington.ufl.edu, tom.zimmermann@uni-koeln.de. Code: `https://github.com/chenandrewy/flex-mining`. Data: `https://sites.google.com/site/chenandrewy/`. We thank Alec Erb for excellent research assistance. Initial drafts of this paper relied on data provided by Sterling Yan and Lingling Zheng, to whom we are grateful. For helpful comments, we thank discussants: Leland Bybee, Yufeng Han, Theis Jensen, Jeff Pontiff, Shri Santosh, and Yinan Su. For helpful comments we also thank Svetlana Bryzgalova, Charlie Clarke, Mike Cooper, Albert Menkveld, Ben Knox, Emilio Osambela, Dino Palazzo, Matt Ringgenberg, Dacheng Xiu, Lingling Zheng, and seminar participants at Auburn University, Baruch College, Emory University, the Fed Board, Georgetown, Louisiana State, Universitat Pompeu Fabra, University of Kentucky, University of Utah, University of Wisconsin-Milwaukee, and Virginia Tech. The views in this paper are not necessarily those of the Federal Reserve Board or the Federal Reserve System.