Fourteen years of darts on Wall Street lead Malkiel to reassert stock theory

By DEBORAH AROTSKY
STAFF WRITER
Published: Wednesday, May 8th, 2002

Journalists are not monkeys, but they are pretty close. For the last 14 years, Wall Street Journal reporters have thrown darts at NASDAQ stock listings, choosing stocks to compete against the picks of professional investors.

The test is an extension of University economics professor Burton Malkiel GS '64's book "A Random Walk Down Wall Street."

The book states, "A blindfolded monkey throwing darts at a newspaper's financial pages could select a portfolio that would do just as well as one carefully selected by the experts."

The Journal accorded Malkiel the honor of throwing the first dart and, 142 contests later, the experiment concluded last month. Originally it was scheduled to last only one month.

"They thought it would be cute to have this contest," Malkiel said. "I got a kick out of it."

"This wasn't really a serious contest," he added.

Georgette Jasen, the Journal reporter who covered the story, agreed.

"This was not a scientific experiment by any means," she said. "The point was to get new investment ideas out there and to have a little fun with it. It's not a real test of the efficient market."

With an average 10.2-percent profit to the dart throwers' 3.5-percent profit, the experts won.

However, Malkiel does not believe the contests were conclusive.

"There's a publicity effect," he said, explaining that, by advertising the stocks that the experts picked, the Journal influenced the market.
"Because the Journal talks about the experts' picks and the experts describe why they picked certain stocks, the stocks get publicity boost," Malkiel said.

He added that, when he recalculated the returns from experts' stocks using the value from the day before the article was released instead of the day of, the experts do not fare any better than the dart throwers.

"Any advantage of experts completely goes away," Malkiel said. "It was good journalism, but it wasn't an appropriate test," he said.

People love to hear about what the experts think of various stocks, he said.

Since the book first came out in 1973, the advent of information systems have altered the nature of information exchange in the business world.

Yet Malkiel argues that his theory remains true today.

Malkiel said this is because of the efficiency of the marketplace — which means the current price of a stock reflects everything that is known about a company.

A valuable stock has a high price, while the price of a less valuable stock is much lower. Therefore, he said, the investor will make just as much investing in either one.

Malkiel also said that darts were not the best method of testing his theory.

"I don't literally mean that you ought to throw darts," he said.

The correct analogy, he said, would be to throw a towel and buy multiple stocks on the market.

"I believe in [my theory] even more strongly today than when I first wrote the book," he said. "What is absolutely clear is that regularly index funds do better than about two-thirds of active managers, and the active managers who beat the index in one period are not the same as those who beat it in next."

Recent events such as the collapse of Enron have caused some to question Malkiel's theory. Once the seventh largest company in the United States, Enron became involved in complicated transactions without disclosing to its investors the risks involved. Nor were its accounting firms reporting the situation correctly.

But instead of making Malkiel doubt his faith in the efficient economy, the Enron situation only gives him more evidence for his theory.

"Enron makes me very skeptical about the ability of the investment professionals to beat the market," he said.

He explained that it was not necessarily true that somebody who does the homework could avoid such a situation.

"In the long run, it leads to more transparency," he said, because it serves as a warning to other companies.
"As people react, chief financial officers will be less likely to engage in very complicated arrangements where there is even the appearance of subterfuge, because the market will punish these companies now."

**Original URL:** http://www.dailyprincetonian.com/2002/05/08/5144/