

Session 10

Temporal Patterns

Test

1. There is evidence that January is the best month of the year to invest in stocks. One story that has been told to explain this is that tax loss selling at the end of the prior year pushes down the stock prices of the companies where there is such selling and that it is the rebound that creates the January effect. If this were true, which of the following groups of stocks should be the biggest beneficiaries of the January effect?
 - a. Stocks that went down the most in the prior year
 - b. Stocks that went up the most in the prior year
2. There is also evidence that a significant portion of the small cap premium (the excess returns earned by small companies over the market) is generated in the first few days in January. Which of the following stories provides an explanation for the phenomenon?
 - a. Small cap stocks are riskier than large cap companies
 - b. Small cap companies are less liquid than large market cap companies
 - c. Small cap companies are less likely to be held by institutions than large market cap stocks
 - d. Small cap companies are followed by fewer analysts than large market cap companies
 - e. All of the above.
3. Looking at returns across the weekdays, it seems likely that Mondays have been the worst day of the week to invest in stocks over the last few decades. One explanation that is offered for the Monday effect is that companies report a disproportionate amount of bad news after the close of trading on Friday and that the Monday reaction reflects the bad news. If this story holds, which of the following would you expect to see in Monday returns?
 - a. Almost all of the negative return should come from stocks opening lower on Monday than from returns over the course of the day.
 - b. The negative Monday returns should be reversed over the course of the remaining weekdays.
 - c. The Monday return should be most negative for companies that had large positive returns on Friday.
 - d. The Monday return should be most negative for companies that had large negative returns on Friday.
 - e. The Monday return should be more negative for companies that are most liquid.
4. Assume that Monday returns are caused by companies sitting on bad news until after the close of trading on Friday. Is there a strategy that you can use to exploit this tendency to make money?
 - a. Yes
 - b. No

Explain.

5. There is some evidence that the weekend effect has shifted over the last two decades, with Fridays (rather than Mondays) becoming the worst day of the week to invest in US stocks over the last decade.
 - a. True
 - b. FalseIf true, what might explain this shift?