Financial Analysts Journal ›
Volume 56, 2000 - Issue 1

PERFORMANCE

Too Many Cooks Spoil the Profits: Investment Club Performance

Brad M. Barber & Terrance Odean

Pages 17-25 | Published online: 02 Jan 2019
Cite this article https://doi.org/10.2469/faj.v56.n1.2326

Abstract

We report our analysis, using account data from a large discount brokerage firm, of the common stock investment performance of 166 investment clubs from February 1991 through … t toward high-bet… lio annually. The aver… nd the performa… erperformed the inde…

The f… nce of inves… vestors Corporat… rket. Are these cl…

We used … stock investm… nuary 1997. We report that the average club earned an annualized geometric mean return of 14.1

percent whereas a market index returned 17.9 percent. In addition, 60 percent of the clubs we analyzed underperformed the index. Not only did the average club fail to beat the market, it failed to match the performance of the average individual investor, who earned 16.4 percent during our sample period.

Two reasons account for the poor performance of investment clubs relative to individual investors—trading costs and investment style. Despite having roughly similar account sizes, the clubs executed smaller trades and held more stocks than did individuals. Thus, their proportionate cost of trading was higher. Trading costs accounted for approximately one-third of the clubs' performance shortfall relative to individuals. The remaining two-thirds of the shortfall was accounted for by investment style. Relative to individuals, the clubs tilted more toward large-cap stocks and growth stocks. During our sample period, large-cap stocks underperformed small-cap stocks by 15 basis points a month and growth stocks underperformed value stocks by 20 basis points a month.

Investment clubs serve many useful functions: They encourage savings; they educate their members about financial matters; they foster friendships and social ties; and they entertain. Unfortunately, their investments do not beat the market.
