



188 Views | 121 CrossRef citations to date | 6 Altmetric

PORTFOLIO MANAGEMENT

Capturing the Value Premium in the United Kingdom

Elroy Dimson, Stefan Nagel & Garrett Quigley

Pages 35-45 | Published online: 02 Jan 2019

🗨️ Cite this article 🔗 <https://doi.org/10.2469/faj.v59.n6.2573>

Sample our Law journals, sign in here to start your FREE access for 14 days

References

🗨️ Citations

Metrics

Reprints & Permissions

Read this article

Share

Abstract

Using a new data set of accounting information merged with share price data, we found a strong relationship between the value premium and the market. This relationship existed among stocks in the United Kingdom, the United States, and Japan. We investigate the challenges. We show that the value strategies have been successful in the past, but they may not be so in the future. We can be sure that the value premium will continue to exist, but its accuracy in the future is uncertain. We value stocks based on their value, not on their price. We favor of value investing. We investigate the challenges. We show that the value strategies have been successful in the past, but they may not be so in the future. We can be sure that the value premium will continue to exist, but its accuracy in the future is uncertain. We value stocks based on their value, not on their price. We favor of value investing.

We Care About Your Privacy

We and our 912 partners store and access personal data, like browsing data or unique identifiers, on your device. Selecting I Accept enables tracking technologies to support the purposes shown under we and our partners process data to provide. Selecting Reject All or withdrawing your consent will disable them. If trackers are disabled, some content and ads you see may not be as relevant to you. You can resurface this menu to change your choices or withdraw consent at any time by clicking the Show Purposes link on the bottom of the webpage. Your choices will have effect within our Website. For more details, refer to our Privacy Policy. [Here](#)

We and our partners process data to provide:

Use precise geolocation data. Actively scan device

I Accept

Reject All

Show Purposes

Using book value of equity to market value of equity (BE/ME) as the measure of value, we found a strong value premium in the United Kingdom for the 1955–2001 period. The return spread we found between our high-BE/ME and low-BE/ME portfolios (averaged across large- and small-cap stocks) is about 0.5 percent a month. The value premium was particularly strong among small-cap stocks, and it was surprisingly stable until the mid-1970s. In recent years, the spread between high-BE/ME and low-BE/ME stocks has been highly volatile. We also show that returns on value strategies based on dividend yield move closely with returns on BE/ME strategies. The premium earned by dividend yield strategies is smaller, but the results suggest that dividend yield may be a useful auxiliary measure of value when BE/ME data deliver doubtful results.

Although the historical returns seem impressive, implementation of strategies designed to capture the value premium is potentially costly, particularly within the small-cap segment. Stocks migrating in and out of the small-cap value universe, dividends, and delistings—all give rise to trading needs, even for a passive manager. We found rebalancing-induced portfolio turnover for a passive small-cap value strategy to be approximately 40 percent a year. In a high-trading-cost environment, this mechanical trading strategy could easily cut several percentage points off annual performance.

We show that high trading costs are an important concern in the U.K. market. Even today, the equity market for small-cap value stocks in the United Kingdom is

substantially less liquid than the U.S. market. Small-cap value stocks are often held by institutional investors who demand high liquidity to meet their needs. Patient investors, however, may be able to achieve better returns by using a less patient manager.

Rebalancing is a dominant feature of small-cap value strategies designed to capture the value premium. Trading needs are high because of the high turnover induced by rebalancing. For example, using a flexible trading strategy that can benefit from a high trading cost environment may be a good idea. High trading costs can thus be a source of substantial competitive advantage for small-cap value managers.

Furthermore, small-cap value stocks in the United Kingdom may be most suitable for the managers who are less subject to daily inflows and outflows and the trading needs they cause.

Finally, the concerns our results raise for the U.K. equity market may be even more relevant for other non-U.S. markets, where liquidity is likely to be even lower than in the United Kingdom.

We appreciate contributions from Paul Marsh and Mike Staunton and the comments of James Davis, Ken French, and Rex Sinquefield.

 Financial Analysts Journal: Invested in Research, Shaping the Future. Click to find out more
Related research 

People also read

Recommended articles

Cited by
121



Information for

- Authors
- R&D professionals
- Editors
- Librarians
- Societies

Opportunities

- Reprints and e-prints
- Advertising solutions
- Accelerated publication
- Corporate access solutions

Open access

- Overview
- Open journals
- Open Select
- Dove Medical Press
- F1000Research

Help and information

- Help and contact
- Newsroom
- All journals
- Books

Keep up to date

Register to receive personalised research and resources by email

 Sign me up



Copyright © 2024

Accessibility

Registered in England
5 Howick Place

Wiley and John Wiley & Francis Group
are trademarks of John Wiley & Sons, Inc.
or its affiliated companies.

