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Stock return predictability and the adaptive markets hypothesis: Evidence from century-long U.S. data $\hat{\sim} \dagger$

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Abstract

This paper provides strong evidence of time-varying return predictability of the Dow Jones Industrial Average index from 1900 to 2009. Return predictability is found to be driven by changing market conditions, consistent with the implication of the adaptive markets hypothesis. During market crashes, no statistically significant return predictability is observed, but return predictability is associated with a high degree of uncertainty. In times of economic or political crises, stock returns have been highly predictable with a moderate degree of uncertainty in predictability. We find that return predictability has been smaller during economic bubbles than in normal times. We also find evidence that return predictability is associated with stock market volatility and economic fundamentals.

Highlights

— This paper examines return predictability of the US stock market. — A century-long US data has been examined. — The results have been consistent with the adaptive markets hypothesis.



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Keywords

Economic bubbles; Economic crises; Adaptive markets hypothesis; Market efficiency; U.S. stock market

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