# Meet the academic who has fired up moonshot investing

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Opinion Markets Insight

Arizona professor provides backing for the approach of investors such as Ark and Baillie Gifford

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Hendrik Bessembinder of Arizona State University © WSCOTTPHOTO.COM (c)2018

The accidental high priest of moonshot investing works at a public university in Phoenix, Arizona, a place mostly known for dry heat, golf and allegedly the home of a deep-fried burrito dish known as the chimichanga.

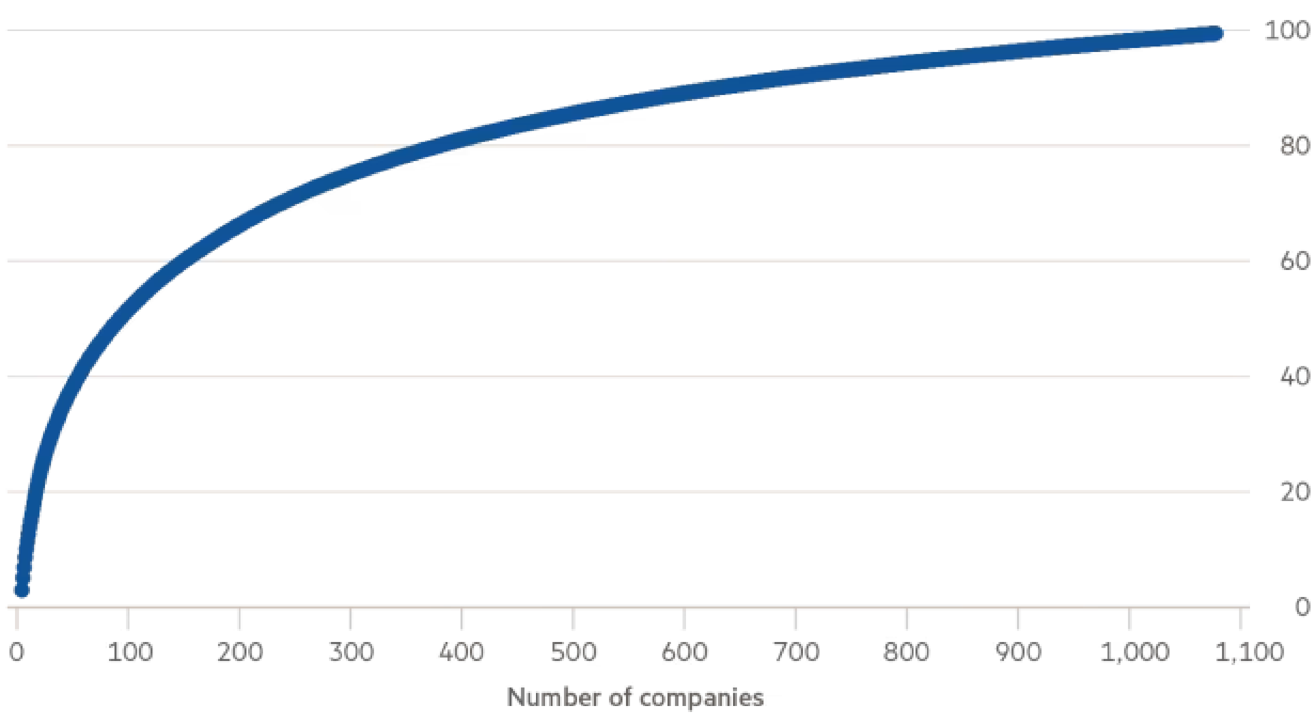
Four years ago Hendrik Bessembinder, a finance professor at Arizona State University, published a paper that showed that despite the equity market's gains over the past century, most stocks are actually duds. In fact, of the roughly 26,000 companies listed between 1926 and 2016, more than half lost money or did worse than simply holding one-month Treasuries. In contrast, about 1,000 stocks — or just 4 per cent of the entire sample — in practice accounted for all the net wealth creation over the period, or almost $35tn.

Until then, Bessembinder's biggest hit had been an undoubtedly gripping paper entitled *Equilibrium Pricing and Optimal Hedging in Electricity Forward Markets*. First published in 1999, it has been downloaded almost 2,500 times and cited 24 times on the research repository SSRN since then. *Do Stocks Outperform Treasury Bills?* has already been downloaded more than 32,000 times and cited in 41 papers. For academia, this is the equivalent of a smash box-office hit.

"It's been an interesting journey," Bessembinder chuckled. "Even the ones that we think of as our best papers, published in a prominent academic journal, have an audience of a few hundred people."

## Only a few companies have dominated historical US stock market returns

Cumulative % of wealth creation of top 1,100 companies




Source: Hendrik Bessembinder


Like every good movie franchise, the paper has had a sequel. In 2019, Bessembinder showed that the skewed nature of stock market returns was even more extreme internationally. About 61 per cent of non-US stocks underperformed Treasury bills in the 1990-2018 period, and less than 1 per cent accounted for the entire $16tn of net wealth creation over the period.

Initially, many seized on this as further evidence of the superiority of passive investing. After all, if so few stocks account for all the market's overall gains, investors should surely just buy the entire haystack rather than scour for a few rare golden needles buried within.

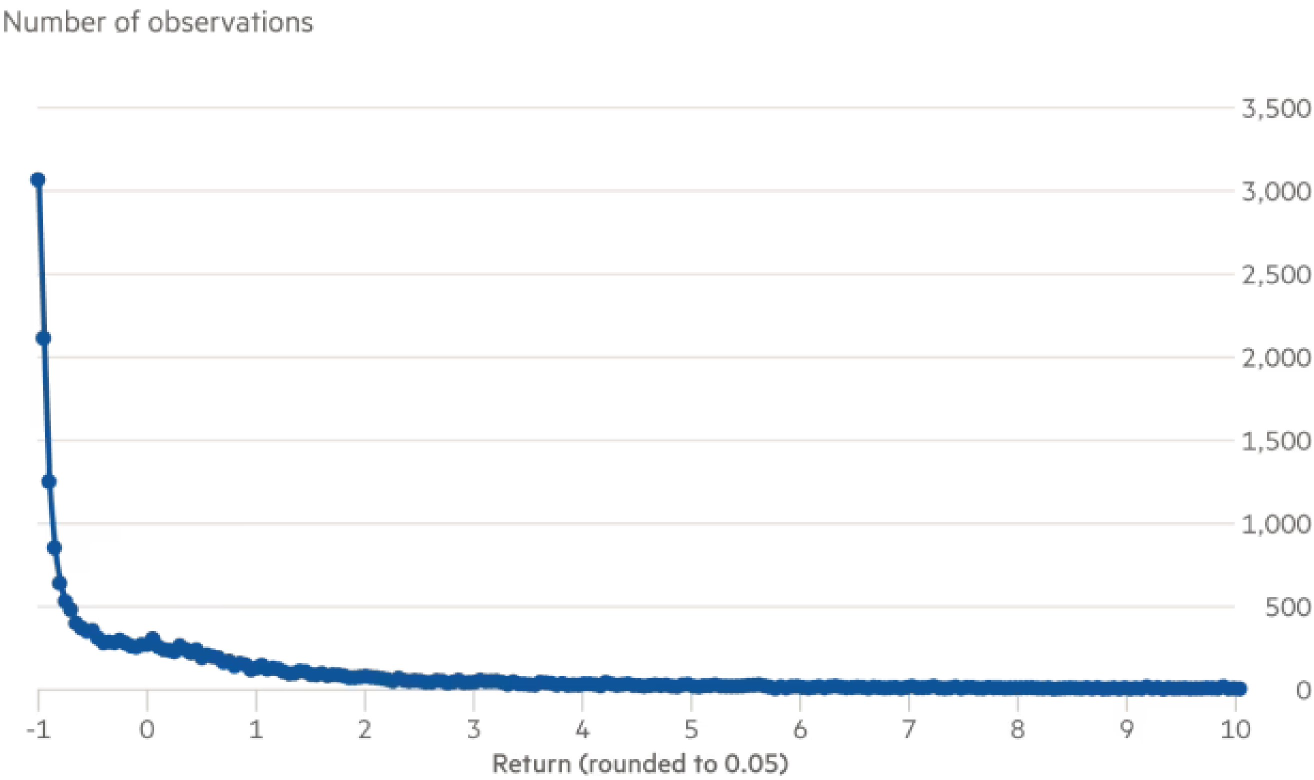
More recently, however, some investors cite Bessembinder's work as evidence that aggressively investing in a narrow clutch of potential corporate superstars — almost whatever the price — is actually the way for active asset management to regain its mojo. After all, his data implies that finding just one of these nascent stock market titans can more than compensate for losses elsewhere.

Bessembinder's influence can be most obviously seen in Baillie Gifford, the money management group that has seized on his work as backing for its big bets on fast-growing, disruptive companies. Baillie Gifford has hired Bessembinder as a consultant, and bankrolled his 2019 global study.

But his subtle reach can also arguably be detected in the approach of Cathie Woods' Ark Invest and Chase Coleman's Tiger Global. The former has caused a stir in the traditional investment world by making outsized, wildly successful bets on hot technology stocks, while the latter's gung-ho investment spree in an array of promising start-ups is now ruffling feathers in Silicon Valley.

"I think I have provided some ammunition for the people who say it's their business to chase moonshots," Bessembinder said. "The skewness shows just how big the pay-offs can be if you're good at this."

## Lifetime buy-and-hold returns




Source: Hendrik Bessembinder
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Historically, so-called "growth" stocks have underperformed in the long run because of our human inclination for optimism, which leads to overpaying for lottery ticket-like stocks. But perhaps what was once a foible might make more sense today. The winner-takes-all dynamic of the modern digital economy arguably means that lottery ticket stocks pay off far more than they have in the past, making what was once a foolhardy strategy a little more rational.

Bessembinder is wary of filtering his findings through the prism of "growth" or "value" investing. But a recent revision on the 2017 paper offers some evidence for those that argue the deepening winner-takes-all dynamic favours growth investing. It found that the concentration of stock market wealth creation is increasing, and is now at an all-time high.

Of course, as every investment prospectus points out, past performance is no guarantee of future returns. The uncomfortable truth is that the investment industry has demonstrated that it is bad at divining stock market starlets. For every fund manager that chances upon one that makes their career, there are hundreds that fizzle out unnoticed. For most people, buying the haystack still makes the most sense. But gung-ho growth investors at least finally have some compelling quantitative data to back their beliefs.

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