Jacobs Levy Equity Management Center
for Quantitative Financial Research

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2021 Wharton-Jacobs Levy Prize for Quantitative Financial Innovation Remarks
Bruce I. Jacobs, Ph.D., Chair of the Prize Selection Committee, Jacobs Levy Center
Kenneth N. Levy, Advisory Board, Jacobs Levy Center

KEN LEVY:

Thank you, Chris and Craig, for those kind remarks.

In investing, momentum is defined as the tendency of assets that have recently outperformed to continue to outperform. Looks like Newton had it right with his First Law of Motion. As far back as the 18th century, investors seemed to have an inkling of this phenomenon. Famed British economist David Ricardo, who made a fortune speculating on stocks, advised, "cut short your losses, let your profits run." Nineteenth- and early-20th century investment manuals often recommended what we now call momentum strategies.

But momentum never fit neatly into the late-20th-century world of efficient markets and modern portfolio theory. Nonetheless, Narasimhan Jegadeesh and Sheridan Titman, winners of the 2021 Wharton-Jacobs Levy Prize, have shown us how it could be applied systematically by skilled practitioners.

Our distinguished honorees would be the first to tell you that they can't say with certainty what causes momentum or accounts for its persistence. Nevertheless, theories of momentum's origins and persistence abound. One survey of the literature found at least 10 potential explanations. We look forward to hearing Narasimhan's and Sheridan's latest thoughts.

As with any factor, the benefits of momentum can disappear suddenly, and for extended periods. This may point to risk-based explanations. But in a 2011 follow-up to their seminal 1993 paper, Jegadeesh and Titman argue that the magnitude and persistence of momentum returns are too strong to be explained by risk.

Instead, many see momentum as the result of investors being slow to react to new information—to underreact—causing prices to adjust slowly but persistently. An alternative explanation is that investors may overreact to new information, pushing prices up or down. But why do investors underreact or overreact? The list of potential behavioral explanations is a long one, and includes overconfidence, the disposition effect, and cognitive dissonance. In a 2020 *Wall Street Journal* article, Avanidhar Subrahmanyam and Titman offered a more succinct explanation of overconfidence: "Investors tend to have too much confidence in their own ability to evaluate stocks, and too little in the abilities of others."

Whatever you believe explains the momentum effect, we are grateful to our honorees for their meticulous research that gave new life to this factor which allows investors to harness it.

BRUCE JACOBS:

The Wharton-Jacobs Levy Prize for Quantitative Financial Innovation recognizes outstanding quantitative research that has contributed to an important innovation in the practice of finance. The 2021 Wharton-Jacobs Levy Prize recipients, Narasimhan Jegadeesh and Sheridan Titman, are being honored for their work documenting the momentum premium. Robert Shiller called their seminal 1993 paper—"Returns to Buying Winners and Selling Losers: Implications for Stock Market Efficiency" —a "bombshell." It can be summed up with a simple set of instructions: buy stocks that have performed well and sell stocks that have performed poorly.

Jegadeesh and Titman's findings seem to contradict much of what we thought we knew about investing, including the efficient markets hypothesis, the random walk theory, the capital asset pricing model, and even buy-low-sell-high. And yet their model, elegant in its simplicity, describes a factor of unusual strength and robustness. Subsequent studies have shown that momentum has produced return premiums, in and out of sample, in dozens of countries and asset classes for hundreds of years.

And while we're not close to understanding why stock-price momentum persists, that is part of the beauty of our honorees' work. By shining a bright light on classical beliefs about how markets work, they have challenged us, and themselves, to gain a deeper understanding of stock-price behavior so that our theories better reflect market realities. In the meantime, their momentum model has provided skilled practitioners with a tool for improving investor outcomes.

When Ken and I established this biennial award in 2011, it was our hope that over time the recipients would constitute an elite group of scholars and practitioners who have had a transformative impact on finance. Jegadeesh and Titman now join Markowitz, Sharpe, Ross, and Ball and Brown as Prize winners.

We are proud to award the 2021 Wharton-Jacobs Levy Prize for Quantitative Financial Innovation to Narasimhan Jegadeesh and Sheridan Titman in recognition of their groundbreaking accomplishments. Thank you for your contributions and a hearty congratulations to both of you.

Narasimhan and Sheridan, please join us for the presentation of the prize medals.

It is an honor to present each of you with a Wharton-Jacobs Levy Prize Medal.