EQUITIES

Investing in the Asset-Growth Anomaly Across the Globe

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Several studies have show that slow-growing companies return more to stock-market investors than fast-growing companies, based on the growth in the book value of companies' assets. In this paper, we explore how investors can capture the excess returns associated with this "asset-growth effect."

We confirm that the asset-growth effect is present in international markets with strong predictive power coming from the straightforward two-year total asset growth measurement. We also confirm that the effect persists across time, in different subsample periods, and is present among both large and small firms. We also show that the asset-growth effect meaningfully affects a firm's performance for up to three years.

We further provide insight into the risk associated with the asset-growth effect; in particular whether the effect can be attributable to a market mispricing or to some systematic market risks, such as governance or market accessibility. Overall, we believe that our results tend to favor the mispricing explanation over that of systematic risk, perhaps because investors overreact to transient asset-growth rates only to be disappointed when growth and stock returns revert to a more normal level.

Harvesting these returns is another matter, however. Using a host of proxies for arbitrage costs and arbitrage risks, we find that the effect is more prevalent among small and illiquid stocks with greater idiosyncratic volatility. These arbitrage costs reduce the opportunity to extract excess returns.

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