

Coleman, Robert D., "Asset Pricing Simultaneity, Three-Factor Model and Cost Analysis", *Indian Journal of Economics and Business*, Vol. 4, No. 1, (June, 2005): 73-94, <<http://www.ijeb.com/journals/index.html>>.

Abstract

We explain the phenomenon of the atheoretic size and value effects in asset pricing, which lack face validity, and thereby resolve contradictory assertions about the theoretical and empirical validity of asset pricing models of return with risk factors that entail price. We show that size-related, value-related and other price-entailing risk factors are not scientifically valid in asset pricing models of return estimated and tested by scientific statistical methods. Analysis shows that the direct cost of these pricing fallacies is hundreds of millions of dollars each year in capital markets worldwide.

Excerpt:

The pioneer and leader in designing and selling financial products based on the Fama-French Three-Factor [FF3F] stock pricing model is Dimensional Fund Advisors Inc. (DFA), a family of index mutual funds that has grown to \$65 billion of assets under management worldwide.

Excerpts from Conclusions:

Any representation, therefore, that scientific studies show that investment strategies and financial products based on either the FF3F model or its risk factors can earn consistent average risk-adjusted expected returns greater than the returns on broad market indexes or conventional market proxies is not true. There can be no possible evidence or proof that FF3F is scientifically valid. FF3F has never been scientifically valid and never will be as long as logically circular econometric simultaneity is not scientifically valid.

It appears, therefore, that the Fama-French Three-Factor stock pricing model is the biggest fatal fallacy in stock market history when measured by each of six major criteria: the number of investors adversely impacted, the total direct cash cost to all investors, the total net realized harm to all persons impacted, the geographical range of residence of the adversely impacted persons worldwide, the duration since the first commercial application of the FF3F model or its price-entailing risk factors, and the number of professionals in academia and the financial-services industry who are involved.