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Financial

ECONOMIC TRENDS

Do Brokers' Picks Matter?

Yes, but less than you might think

If you're a stock market investor who relies on a broker for advice, it seems to make perfect sense to choose a brokerage whose recent recommendations have been winners. But would such a strategy pay off big in the long run?

Not according to Brad M. Barber of the University of California at Davis, and **Reuven Lehavy** and Brett M. Trueman at the University of California at Berkeley. Analyzing the recommendations of some 100 brokerages from 1987 to 1996, they found that people who each year bought the stocks recommended by the top fifth of brokers with the best performance in the prior year would have averaged 4.3% a year more on their portfolios over the decade than those following the advice of the fifth with the poorest prior returns.

After adjusting for market risk, company size, book-to-market value, and other factors that research has shown tend to strongly affect long-term stock returns, however, they found no significant difference between the returns of the best and worst brokers. In other words, it was the weighting of various portfolios that generated higher returns, rather than any persistent unusual stock-picking abilities of specific brokerages.

The researchers add that this doesn't mean that brokerage advice isn't valuable. "Stocks that are favored by a consensus of brokerage firms," notes Trueman, "still tend to do significantly better than stocks in general disfavor."

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