UNIVERSITI TEKNOLOGI MARA

EXAMINING THE PERFORMANCE OF DOD AND POD PORTFOLIOS AND DETERMINANTS IN DEVELOPED AND DEVELOPING COUNTRIES

SITI HAJAR NADRAH BINTI MOHAMAD GHOUSE

Thesis submitted in fulfilment of the requirements for the degree of
Doctor of Philosophy

Faculty of Business Management

May 2018

ABSTRACT

Believers of the Efficient Market Hypothesis have argued that it is impossible to make abnormal return since market is efficient. Nevertheless, the contrarian strategists differ to agree. In this setting, this study attempts to examine the ability of Dogs of the Dow (DoD) and Puppies of the Dow (PoD) trading strategies in outperforming the market return. The analyses are done on the DoD and PoD portfolios of 15 individual countries and as well as a group. In addition, this study also investigates determinants (dividend yield, size, gross domestic product and inflation rate) that might affect the returns of these DoD and PoD portfolios. The countries studied are Australia, Hong Kong, Japan, New Zealand, Singapore, South Korea and Taiwan for developed countries and Brazil, Russia, India, China, South Africa, Malaysia, Indonesia and Thailand for developing countries. Yearly data comprising of return, dividend yield, size, gross domestic product and inflation rate are collected from 2000 until 2014. Empirical findings reveal that DoD portfolios outperformed the market in all 15 individual countries studied but the results are only statistically significant in the Russian market. However, when analysis was done as a group, the portfolio returns of DoD beat the market statistically and significantly for developed and developing countries. As for the PoD portfolios, the results indicate that abnormal returns are statistically significant only in share markets of New Zealand, Taiwan and Russia. Similar to the results of DoD portfolios, PoD portfolios also outperformed the share market in the respective countries as a group and these abnormal returns are also statistically significant. The t-test results between the abnormal returns of DoD and PoD portfolios are insignificant, implying that neither DoD nor PoD trading strategies are superior than the other. It is discovered that for the DoD portfolios; dividend yield (in Hong Kong, Singapore, China and Indonesia) size (in Hong Kong, Singapore, South Korea, China, Malaysia and Indonesia) gross domestic product (in Hong Kong, New Zealand, South Korea and India) and inflation rate (in Hong Kong, Taiwan, Malaysia and Thailand) statistically and significantly determine the strategy's portfolio returns. Positive relationships between dividend yields, gross domestic product and portfolio returns are found in those countries whereas size positively influenced the returns in these countries except for Hong Kong. On the other hand, inflation rate is negatively related to the portfolio returns in these countries. In terms of the PoD portfolio returns, findings indicate that dividend yields in Hong Kong and South Africa; size in Hong Kong, South Korea and Malaysia; gross domestic product in Hong Kong, South Korea India and Malaysia; and inflation rate in Hong Kong, New Zealand, Taiwan, South Africa, Malaysia and Thailand statistically and significantly influence the returns. Dividend yield, size and gross domestic product are positively related with PoD portfolio returns whilst inflation rate indicates an inverse relationship. Overall, this study documented that the determinants vary across countries which could be attributed to the nature of individual share markets and companies, individual economic structure, different government and financial regulatory systems.

ACKNOWLEDGEMENT

Syukur, Alhamdulillah. With the mercy of Allah Subhanahu Wata'ala, I succeeded in completing this thesis after so much time and patience throughout the journey of my PhD. Special gratitude is dedicated to the people who

First and foremost, I would like to extend my sincere appreciation to my supervisors, namely Associate Professor Dr Noryati Ahmad and Professor Dr Norhana Salamudin for their supports, advices, motivations, guidance and commitments to my project. These positive qualities enable me to understand my topic deeper.

My special appreciation and thanks also are dedicated to my late father, Mohamad Ghouse bin Abdul Latiff and my mother, Suri binti Sukor as they are the main figures that inspired me to pursue my study at this higher level. Besides that, I also would like to extend my special appreciation and thanks towards my husband, Izzuddin Shah bin Zamani as well as my parents-in-law, Zamani bin Ahmad and Melor binti Shamsudin for always supporting me and my dreams. Not forgotten, my younger sisters, Sarah and Aisyah, my younger brother, Afiq, and my younger brothers-in-law, Azman, Hafiz, Shahfiq and Amir for always supporting me by providing me with much fun and joy throughout the completion of this thesis. The affections and presences of these important people during the passing of my beloved father caused the dispirited me to feel more alive and thus, not to give up.

Finally, I would like to thank my colleagues and friends for supporting me continuously. The lonely journey as a PhD student are filled with joys and hopes due to their willingness in sharing ideas and delivering advices.

TABLE OF CONTENTS

CHAPTER ONE
INTRODUCTION

1.1 BACKGROUND OF STUDY

In 1985, Werner F. M. De Bondt and Richard Thaler introduced the Overreaction Hypothesis whereby the article on this theory is presumed as one of the most influential article written as it was against the norm of investment and in fact, it has been globally tested by investors and practitioners. The basis of this theory is to implement the idea behind contrarian strategy by buying past poor performing shares and selling past good performing shares. This is because, investors tend to overreact to news, informations and rumors that caused price reversal in future, which indirectly enable investors to generate abnormal returns in the share markets (Maheshwari and Dhankar, 2014). Besides the Overreaction Hypothesis, there are also abundant of theories that aim for abnormal returns through the implementation of contrarian factors whereby shares with higher dividend yield is amongst them.

Higher dividend yields mean lower prices and purchasing these shares shows that investors are buying undervalued shares, which contrarian strategy suggests will rise in future. Among the trading strategies that apply this idea are Dogs of the Dow theory and its new version, namely Puppies of the Dow theory in which their basic element is shares with higher dividend yield will provide higher return in future. Introduced by Michael O'Higgins and John Downes in 1991, these trading strategies nevertheless are a little bit contrast to the fundamental contrarian strategy. This is because, Dogs of the Dow theory is focusing solely on the inclusion of ten blue chip shares (market index) with higher dividend yield whereas Puppies of the Dow theory aims for five shares under Dogs of the Dow theory yet with lower prices. Despite of that, these theories incorporate undervalued shares in the portfolios with a faith that the prices of those shares will rise in future, which is similar as specified under basic contrarian strategy. Past study used to mention that portfolio consisted of high-yielding shares did possess lower risks yet it was able to generate higher returns (Carvalhal and Meireles, 2015).