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July 10, 2006

Letters to the Editor
The Wall Street Journal
200 Liberty Street
New York, NY 10281
Email: wsj.ltrs@wsj.com

Dear Editor:

This is in response to the commentary article in *WSJ.com* entitled "The 'Noisy Market' Hypothesis" by Jeremy J. Siegel, page A14, June 14, 2006. Mr. Siegel is a professor of financial economics at Wharton School, University of Pennsylvania, and he failed to disclose that he is a member of the board of directors of Wisdom Tree Investments Inc.

Mr. Siegel refers to Robert Arnott as the author of new research (see citation below), which allegedly demonstrates that sales, dividends and other so-called fundamental factors of firm value can be used to weight the stocks in broad-based indexes and offer investors better returns and lower volatility than capitalization-weighted indexes. This alleged revolution heralded by Mr. Siegel is old wine in a new bottle. It is part of the grand design in price-, shares- and dividends-related return factors initiated by Fama, Fisher, Jensen and Roll in 1969.

Mr. Siegel says that Eugene Fama from the University of Chicago and Kenneth French from Dartmouth College Tuck School built a very successful investment firm [Dimensional Fund Advisors Inc] based on segmenting the universe of stocks into size- and value-based style sectors to sell to institutional and high-net-worth individual investors. The most relevant research on this topic by Messrs. Fama and French is their 1993 article in the *Journal of Financial Economics* (see full citation below).

The cited article by Arnott, Hsu and Moore, and more than twenty published articles by Fama and French on this topic are a fatal fallacy and a hoax in the sense that the authors knew or had reason to know that their research was neither logically valid nor scientifically valid. This concealed, undisclosed, fatal fallacy is a form of vicious circular reasoning and a failure to algebraically isolate the unknown, due to something in introductory econometrics known as circular simultaneity.

This irremediable, material, fatal fallacy is explained by me in two published articles in 2005 and 2006 in scientific economics journals (see citations below). The cited articles

authored by Arnott, Hsu and Moore and by Fama and French, and the stock equity index funds they designed for Research Affiliates and for Dimensional Fund Advisors, are not scientific; rather they are pseudoscience in the sense of serious deviation from generally accepted, standard, scientific, research methodological practice, and they are junk science in the sense of acknowledged non-scientific motivations and multiple, major, financial conflicts of interests. There is no scientific reason to expect these investment products to earn higher expected risk-adjusted returns compared to the market average. The underlying causal, inferential, econometric models of expected total return for stock-portfolio pricing are logically meaningless, non-interpretable, indeterminate, destabilizing in the sense of moving prices away from fundamental fair values, irrational, inefficient, and economically wasteful.

As a master, mass manipulator once wrote: "Even though the facts which prove this to be so may be brought clearly to their minds, they will still doubt and waver and will continue to think that there may be some other explanation."

The efficient markets hypothesis of the rationalists is not a theory. The alleged new paradigm and huge paradigm shift called the 'noisy market' hypothesis of Mr. Siegel and the behavioralists is not a theory. The Noisy Markets Hypothesis (NMH) is the behavioral finance analogue of the Efficient Markets Hypothesis (EMH). Both hypotheses have comparable theoretical foundation, which is none, and comparable ideological foundation, which is much. The NMH is claimed to explain the alleged size and value anomalies, which have been demonstrated to be instantiations of econometric circular simultaneity.

Mr. Siegel alleges that dividend-weighted indexes had better risk and return characteristics than capitalization-weighted indexes in each industrial sector and each country that he analyzed. Yet no citation to his research paper is provided.

Mr. Siegel appears to be not merely enabling, not merely aiding and abetting, but actively perpetuating the biggest hoax in stock market history as measured by each of six major criteria. A conservative estimate of harm to investors alone is more than $1 billion each year, and a more realistic estimate is $4 to $5 billion each year and growing. This vast, wide-ranging, long-running hoax is a Piltdown man of the economics sciences and a contagion spreading worldwide. Academic entrepreneurs involved in this hoax may earn some good will if they do not stonewall and cover-up their part in it, as have Messrs. Fama and French, but rather cooperate in good faith with full disclosure in the interests of fair, open discussion of this important matter.

Sincerely,

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REFERENCES

Arnott, Robert D., Jason C. Hsu and Philip Moore, 2005, “Fundamental Indexation”, *Financial Analysts Journal* 61:2 (March/April), 83-99. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=713865.

Coleman, Robert D., 2005, “Asset Pricing Simultaneities: Phases and Patterns”, *Annals of Economics and Finance* 7:1 (May), 49-76. http://www.aeconf.net/Articles/May2006/aef070103.pdf

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Fama, Eugene F. and Kenneth R. French, 1993, “Common Risk Factors in the Returns on Stocks and Bonds”, *Journal of Finance Economics* 31:1, 3-56. http://www.nes.ru/~agoriaev/Papers/Fama-French%205%20factors%20for%20stocks%20and%20vonds%20JFE93.pdf

----- Original Message -----
From: B C
To: wsj.ltrs@wsj.com
Sent: Monday, July 10, 2006 8:19 AM
Subject: Letter to the Editor

Letters to the Editor
The Wall Street Journal
200 Liberty Street
New York, NY 10281
Email: wsj.ltrs@wsj.com

Dear Editor:

Attached is a letter in response to the *WSJ.com* commentary article entitled "The 'Noisy Market' Hypothesis" by Jeremy J. Siegel, page A14, June 14, 2006.

Supporting information is included in two other attached documents: Comments on "The 'Noisy Market' Hypothesis"; and a copy of the embargoed one-page summary of a research paper in review since late May, 2006, entitled "Demise of an Investment Revolution and Its New Paradigms".

I trust that this letter will not be considered to be overly technical for the readers of *The Wall Street Journal*.

Sincerely,

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Attachments (3): Letter to WSJC Editor 10Jul2006 A.doc
LetterWSJCeditor2006B.pdf
DemiseSummary.pdf