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An Empirical Validation of a Behavioral Finance Model:

The 52-week High as a Benchmark for an Index

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Abstract

Purpose: This study investigates the impact of a stock's 52-week high price on investor behavior and subsequent stock returns, specifically examining how varying levels of the market index influence this relationship. The research challenges the weak-form efficient market hypothesis.

Design/Methodology/Approach: A panel data analysis is employed, using data from the NASDAQ National Market. The study follows the methodology of Chang (2011), extending it with the inclusion of market index conditions. The analysis includes firm characteristics (size, book-to-market, price-to-earnings ratios) and trade volume and examines the effects of past high prices over different time horizons (5, 20, and 60 days).

Findings: The study confirms a significant positive relationship between a stock's 52-week high and its return. Importantly, this effect is amplified when the market index is relatively lower than its average, contrasting previous studies. Firm characteristics also significantly influence investors' decisions.

Research Limitations/Implications: The study is limited to the NASDAQ market. Thus, generalizability to other markets should be done cautiously. Further studies can explore different markets and additional behavioral factors influencing investment decisions.

Practical Implications: The results suggest that investors can potentially generate abnormal returns by considering the 52-week high benchmark within different market conditions, contradicting the weak form of the efficient market hypothesis.

Originality/Value: This study uniquely highlights the moderating effect of the market index level on the relationship between a stock's 52-week high and its return, providing evidence that the relationship is amplified during periods of lower index values, which contradicts previous findings in different markets.

Keywords: 52-Week High, Behavioral Finance, Market Index, Momentum Trading, Efficient Market Hypothesis (EMH)

JEL Classifications: G11, G12, G14

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