

Dimensional Fund Advisors Harvard Case Solution & Analysis

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DFA's Business Strategy

- Purchasing large blocks of small, illiquid stocks at a discount
- Close relationships with prominent academics, including Fama and French
- Matching a broad based, value-weighted small stock index

Fama-French Findings

1. Stocks with high betas don't always offer higher returns than stocks with low betas
 - Beta is not an accurate measure
 - CAPM model
2. High book-to-market stocks generate higher returns than low book-to-market stocks
3. Small cap stocks outperform large cap stocks

DFA's Success

- Reputation
- Important resource for large funds (trade discounts)
- Avoidance of adverse selection
 - *Earnings announcement*
 - *Negative surprises*
 - *Insider sales*
 - *Higher discounts for unfamiliar sellers*
 - *"Penalty Box"*

DFA's Tax Managed Fund

- Tax exempt institutional clients (e.g., union pension funds, college endowments, government) vs. high net worth individuals
- Capital gains vs. dividend taxes
- 10 basis point premium

Future Strategy

- Proven strategy - approximately \$0 in 1981 to \$35 billion in 2001
- Survived tech bubble
- Allow room for growth in the tax-managed fund

Why fix what isn't broken?



Q & A

