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<input type="checkbox"/>	Licentiate's thesis
<input type="checkbox"/>	Doctor's thesis

Subject	Accounting and Finance	Date	20.8.2009
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		Number of pages	64
Title	Rationality of fundamental indexation: evidence from the Finnish stock market		
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Abstract

In a concept of fundamental indexation the company weights in the stock market indexes are based on simple capitalization-indifferent firm size metrics such as book value, dividends, sales, and cash flow. Previously it has been found that fundamental weighted indexes can consistently provide higher returns and lower volatility than traditional capitalization-weighted equity market reference indexes. In this thesis it is studied, whether it is possible to construct more mean-variance optimal market portfolio using fundamental indexation weights instead of market capitalisation weights in the Finnish stock market.

In order to study the performance of fundamental indexation in the Finnish stock market, fundamental and stock return data are gathered from the April 1991 - March 2008 period. Two categories of fundamental portfolios are created: one to replicate OMX Helsinki index and another to replicate OMX Helsinki Cap index where the weight of a single company restricted to maximum 10 %. In order to compare excess returns and CAPM adjusted returns of fundamental portfolios relative to reference portfolio, a paired two sample for means t-test is applied.

As far as the results of OMX Helsinki index replicating strategy is concerned, the findings seem to be somewhat biased which is very likely to be caused by the very dominating influence of Nokia Corporation to the Finnish stock markets during examination period. As for the results of OMX Helsinki Cap index replicating strategy, they are more favouring toward fundamental indexation in statistical terms. Furthermore, the findings are more robust, and according to t-statistics, excess returns of cash flow and composite indexes, and CAPM-adjusted returns of book, sales, cash flow, and composite indexes are significant on 5 % significance level.

Key words	Fundamental indexation, capitalization-weighting, OMX Helsinki
Further information	