

# Stocks enjoy a breath of fresh air

March 2020

## Research Signals

In a sharp turn of events, US stocks posted three consecutive daily gains last week for the first time since mid-February when the growing coronavirus panic set in. Stocks emerged out of what was the shortest bear market in history even as the weekly report for total number of initial unemployment claims spiked to its highest level on record. We have closely monitored daily factor and style model performance in light of the continued significant day-to-day swings in market returns, and continue our weekly performance **reviews** of daily style exposures in the US, as well as month-to-date results from non-US regions.

- US investors demonstrated renewed interest in analyst outlook last week, with high earnings revisions making a run at the low risk trade's cumulative lead since January, while deep value stocks trailed, moving more in line with the weak cumulative performance associated with high bankruptcy risk firms
- Each of our style models enjoyed positive cumulative spreads in the fourth week of March, led by Price Momentum, though it still trails cumulatively since January, while Historical Growth Model maintained its solid lead
- The risk off trade remained a positive signal and high bankruptcy risk firms were disfavored in both developed and emerging markets, while Developed Pacific saw a strong downturn in small caps at the same time that Emerging Asia saw a rebound to this size segment

## February and March style model and factor returns

We review daily factor and style model performance through 27 March across a representative group of our 400+ US factor library in addition to our style models – Deep Value, Earnings Momentum, Price Momentum, Historical Growth, Relative Value and Value Momentum Analyst II. Performance is based on daily decile return spreads, where the spread is computed as the difference in the equal-weighted return at the top (decile 1) and bottom (decile 10) tails. The universe is our US Large Cap universe, which consists of approximately 1,000 of the largest cap names.

First, from a factor perspective, we focus our results on several factors of interest covering value, momentum, size, risk and short sentiment signals, namely Book-to-Market, TTM EBITDA-to-Enterprise Value, 3-M Revision in FY2 EPS Forecasts, Industry-adjusted 12-Month Relative Price Strength, Natural Logarithm of Market Capitalization, 60-Month Beta, Altman Z-score and Demand Supply Ratio.

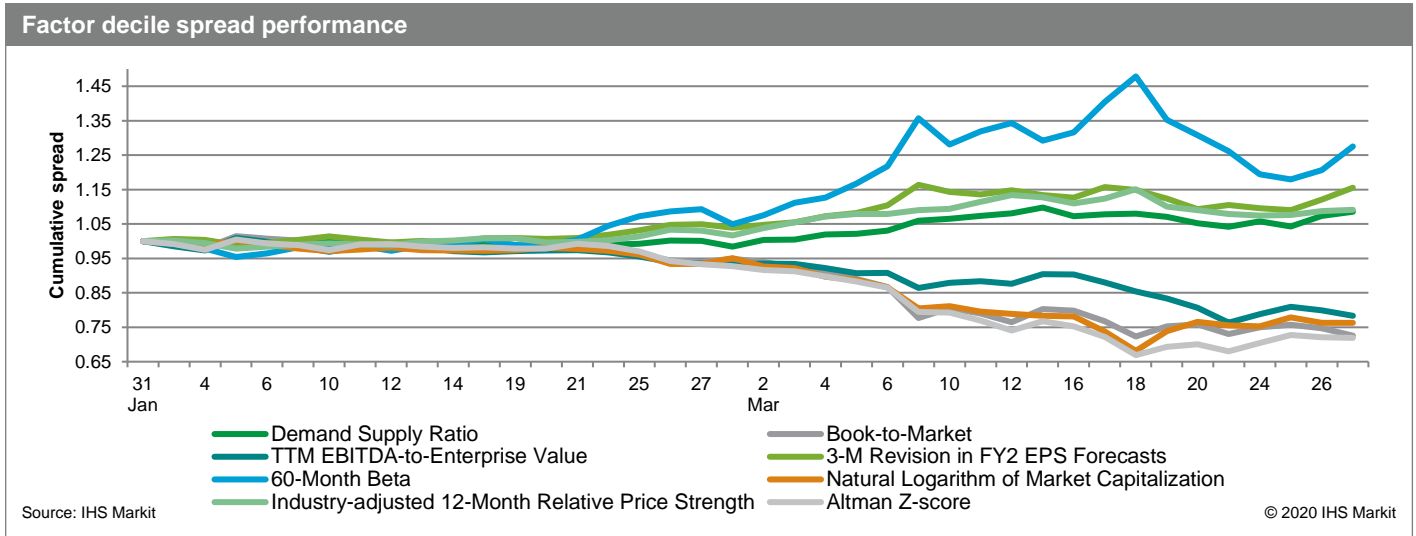
60-Month Beta saw another reversal during the course of the fourth week of March (Figure 1), though in the opposite direction of the prior week, as the early-week slump in performance unwound by the week's end. Since early February, this low risk trade has benefited the most on a cumulative basis, even after coming off its peak on 18 March, while 3-M Revision in FY2 EPS Forecasts also experienced a late-week surge which elevated its cumulative spread above the

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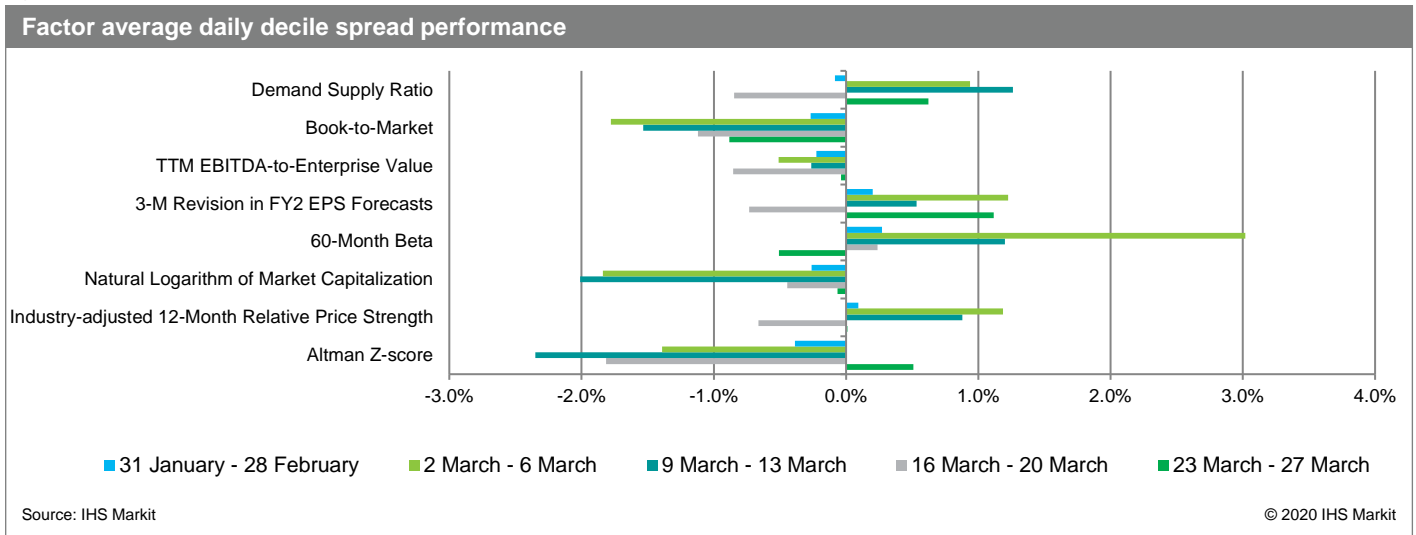
remaining factors. Natural Logarithm of Market Capitalization and, to a lesser extent Altman Z-score, continued their rebound off their weakest cumulative spread on 18 March, though high bankruptcy risk remained the weakest trade since January with a -28.1% cumulative spread. As one of February’s weakest performers, Book-to-Market tried to make up ground last week, but a -2.9% decline on Friday dropped it to a near tie with Altman Z-score for the weakest performer cumulatively.

Figure 1



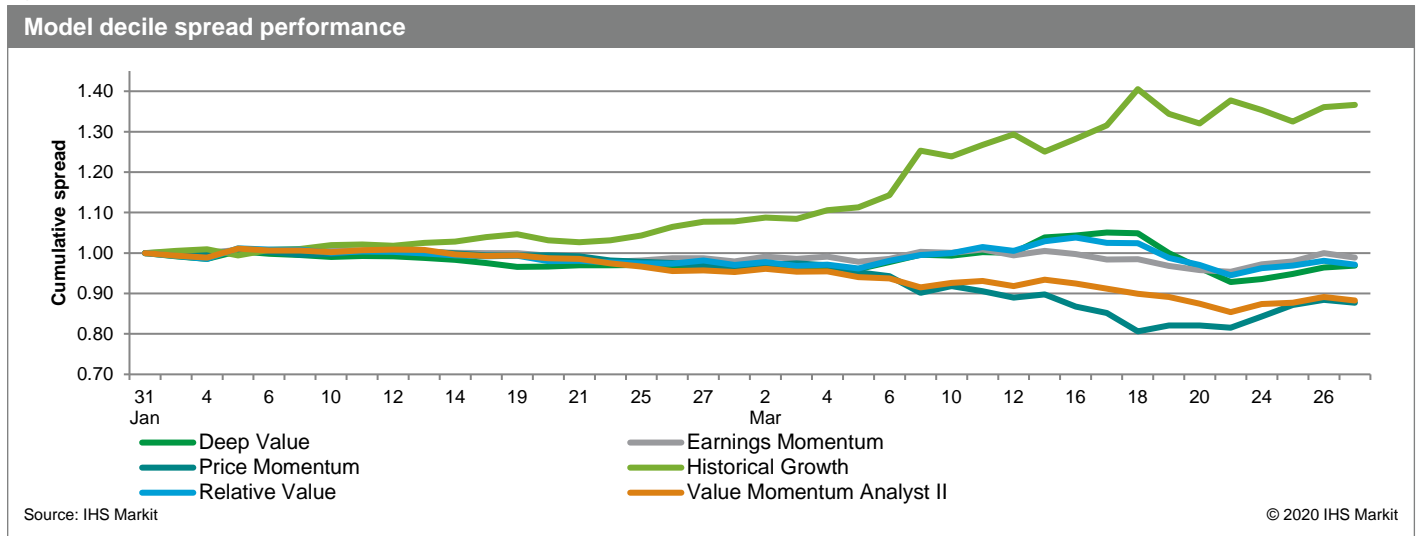
For another perspective, we compare average daily decile spreads in February with those in the first four weeks of March (Figure 2) to provide a more focused view of the extreme behavior between the four periods. From this vantage point, we see the renewed energy in analyst outlook captured by 3-M Revision in FY2 EPS Forecasts’ (1.1%) top average daily spread last week. Book-to-Market (-0.9%) sat at the opposite extreme with the weakest one-week drawdown in average daily performance. Interestingly, 60-Month Beta was the only factor to see a decline in average daily spread last week, while Alman Z-score posted the strongest rebound followed by 3-M Revision in FY2 EPS Forecasts.

Figure 2



Each of our style models enjoyed positive cumulative spreads in the fourth week of March (Figure 3), mostly maintaining their relative positioning on a cumulative basis since January. Historical Growth remained the top performer by a wide margin as the only style to remain in positive territory cumulatively over the full period. However, while still the weakest performer overall, Price Momentum recorded the top weekly cumulative return of 6.8%, followed by Historical Growth (3.5%) and Earnings Momentum (3.2%).

Figure 3



Lastly, to put the factor and model performance results into perspective globally, we look at return spreads and information coefficients for the same set of factors in non-US universes, covering Developed Europe, Developed Pacific, Emerging EMEA and Emerging Asia, through the fourth week of March. The risk off trade remained a key driver in each region, with 60-Month Beta maintaining its substantial lead over other factors, particularly in developed markets. At the same time, investors continued to disfavor high bankruptcy risk firms, with Altman Z-Score a noticeably negative signals across each region, especially in Developed Europe. Developed Pacific saw a strong downturn in small caps, which also lagged in Developed Europe; however, Emerging Asia saw a rebound to this size segment. Finally, Industry-adjusted 12-Month Relative Price Strength was a positive signal in our coverage regions outside the US, while Book-to-Market lagged, with the exception of Developed Pacific.

Table 1

Factor/Model	Developed Europe		Developed Pacific		Emerging EMEA		Emerging Asia	
	Return spread	IC	Return spread	IC	Return spread	IC	Return spread	IC
Altman Z Score	-15.26	-0.28	-6.51	-0.21	-5.28	-0.15	-2.90	-0.08
Industry-adjusted 12-Month Relative Price Strength	3.25	0.10	0.93	0.01	5.05	0.13	4.36	0.16
Natural Logarithm of Market Capitalization	-6.72	-0.10	-15.08	-0.23	0.72	-0.04	4.13	0.15
60-Month Beta	15.12	0.29	11.96	0.24	9.80	0.23	7.07	0.21
3-M Revision in FY2 EPS Forecasts	0.74	0.05	2.27	0.09	0.45	0.02	4.53	0.10
TTM EBITDA-to-Enterprise Value	-6.26	-0.18	1.66	0.08	3.03	0.09	-1.57	-0.01
Book-to-Market	-15.78	-0.28	2.83	0.01	-5.70	-0.16	-2.24	-0.04
Demand Supply Ratio	-3.06	-0.02	-8.83	-0.13	0.26	0.02	4.44	0.18

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