Risk factors shrug off virus concerns

Research Signals

While concerns of a COVID-19 resurgence and the potential for another round of shutdowns cast shadows on the global economic recovery, investors remained optimistic for equities, contributing to outperformance of higher risk names captured by 60-Month Beta and 24-Month Value at Risk across each of our coverage universes (Table 1). Investors put their hopes on vaccine developments and a continuation of the US Federal Reserve’s low rate policy as it shifts to average inflation targeting. The recovery of the global manufacturing sector also gathered pace in August for a second month, following five consecutive declines, with the J.P. Morgan Global Manufacturing PMI rising to a 21-month high.

- US: While positive earnings revisions was a negative signal, outperformance to 2-Year Ahead EPS Growth was particularly pronounced for small caps, posting its highest spread for this cohort since May 2003

- Developed Europe: 60-Month Beta struggled last month as investors sought higher risk names, a trend that has been in place in general since April

- Developed Pacific: Implied Loan Rate, a Short Sentiment indicator measuring the cost of borrowing a stock, was a highly rewarded indicator in markets outside Japan

- Emerging markets: A broad set of styles were represented among the weakest performing factors, including Demand Supply Ratio, 24-Month Value at Risk and Real Earnings Surprise

Contacts

Research Signals · MK-ResearchSignals@ihsmarkit.com
## Global factor quantile return spread performance snapshot, Aug 2020

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<td>-3.58</td>
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<td>-4.20</td>
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<td>Working Capital Accruals</td>
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<td>Average Monthly Trading Volume-to-Market Cap</td>
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<td>60-Month Beta</td>
<td>Liquidity, Risk &amp; Size</td>
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<td>Operating Leverage</td>
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<td>Natural Logarithm of Market Capitalization</td>
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<td>2-Year Ahead EPS Growth</td>
<td>Earnings Momentum</td>
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<td>2.01</td>
<td>0.26</td>
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<tr>
<td>3-M Revision in FY2 EPS Forecasts</td>
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<td>-7.26</td>
<td>-5.33</td>
<td>-2.39</td>
<td>-0.43</td>
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<td>Real Earnings Surprise</td>
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<td>-0.86</td>
<td>1.69</td>
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<td>-6.74</td>
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<td>24-Month Value at Risk</td>
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<td>-4.77</td>
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<td>5-day Industry Relative Return</td>
<td>Price Momentum</td>
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<td>Industry-adjusted 12-month Relative Price Strength</td>
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<td>-2.17</td>
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<td>-0.98</td>
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<td>Rational Decay Alpha</td>
<td>Short Sentiment</td>
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<td>Demand Supply Ratio</td>
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<tr>
<td>Implied Loan Rate</td>
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<td>1.54</td>
<td>4.99</td>
<td>0.66</td>
<td>-1.19</td>
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</table>

Source: IHS Markit
United States

**US Large Cap**

US manufacturing operating conditions gained further ground, accelerating to the strongest since early 2019. The PMI posted 53.1 in August, up from 50.9 in July, reflecting faster increases in output and new orders and the highest degree of confidence in the outlook for output over the coming year since April 2019. With the data indicating that the third quarter could see a strong rebound in production from the steep second quarter decline, coupled with investors’ hopes for COVID-19 vaccines and treatments, equity markets posted their strongest August in decades.

Investors turned once again to corporate fundamentals for guidance, as confirmed by the top performing factors for US large caps in August (Table 2). Quality and value measures which captured this theme include Inventory Turnover Ratio (7.65%) and Cash-to-Price (5.18%). On the other hand, earnings revision metrics were among the weakest performing factors for the month (Table 3). 3-M Revision in FY2 EPS Forecasts (-7.26%), whose performance has been cyclical in nature over the past six months, trailed by the widest margin, though to a much lesser extent than in the early stages of the coronavirus pandemic in April (Figure 1).

<table>
<thead>
<tr>
<th>Factor</th>
<th>Decile spread (%)</th>
<th>Factor group</th>
</tr>
</thead>
<tbody>
<tr>
<td>Inventory Turnover Ratio</td>
<td>7.65</td>
<td>Management Quality</td>
</tr>
<tr>
<td>Natural Logarithm of TTM Sales (USD)</td>
<td>5.28</td>
<td>Liquidity, Risk &amp; Size</td>
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<tr>
<td>Cash-to-Price</td>
<td>5.18</td>
<td>Deep Value</td>
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<tr>
<td>Trailing 12-Month Sales to Invested Capital</td>
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<td>Management Quality</td>
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<tr>
<td>Current Liabilities-to-Price</td>
<td>5.03</td>
<td>Liquidity, Risk &amp; Size</td>
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<tr>
<td>Fixed Assets Turnover Ratio</td>
<td>4.78</td>
<td>Management Quality</td>
</tr>
<tr>
<td>Cyclically Adjusted Earnings-to-Price</td>
<td>4.71</td>
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<td>Working Capital-to-Total Assets</td>
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<td>Management Quality</td>
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<td>Cyclically and Inflation Adjusted Earnings-to-Price</td>
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<td>Deep Value</td>
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<tr>
<td>Normalized Earnings Yield</td>
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<td>Deep Value</td>
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<td>Net Current Assets-to-Price</td>
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<td>Deep Value</td>
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<td>Liquidity Coefficient</td>
<td>4.37</td>
<td>Liquidity, Risk &amp; Size</td>
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<td>Deep Value</td>
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<tr>
<td>Net Operating Asset Turnover</td>
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<td>Management Quality</td>
</tr>
<tr>
<td>2-Year Ahead EPS Growth</td>
<td>4.30</td>
<td>Earnings Momentum</td>
</tr>
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</table>

Source: IHS Markit
Table 3

US Large Cap bottom decile return spread factor performance, Aug 2020

<table>
<thead>
<tr>
<th>Factor</th>
<th>Decile spread (%)</th>
<th>Factor group</th>
</tr>
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<tr>
<td>3-M Revision in FY2 EPS Forecasts</td>
<td>-7.26</td>
<td>Earnings Momentum</td>
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<tr>
<td>Street Revision Confidence</td>
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<td>Earnings Momentum</td>
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<tr>
<td>Time Weighted Earnings Revision</td>
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<td>Earnings Momentum</td>
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<td>Averaged Last 6-M EPS Revisions for FY1</td>
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<td>Earnings Momentum</td>
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<tr>
<td>Volatility-adj 3-yr Projected EPS Growth</td>
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<td>Earnings Momentum</td>
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<td>3-M Revision in FY1 EPS Forecasts</td>
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<td>Earnings Momentum</td>
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<td>Management Quality</td>
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</tbody>
</table>

Source: IHS Markit © 2020 IHS Markit

Figure 1

US Large Cap 3-M Revision in FY2 EPS Forecasts decile return spreads

Source: IHS Markit © 2020 IHS Markit

**US Small Cap**

Small cap factor performance moved more in line with large caps in August on the lists of top (Table 4) and bottom (Table 5) performing factors, with corporate fundamental and earnings revisions measures at the extremes, represented by factors such as Average Collection Period (8.68%) and Street Revision Confidence (-10.23%), respectively. Ironically, another earnings momentum factor, 2-Year Ahead EPS Growth, was the most highly rewarded indicator with a double-digit spread of 11.29% (Figure 2), a level not reached since May 2003.
### Table 4
**US Small Cap top decile return spread factor performance, Aug 2020**

<table>
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<tr>
<th>Factor</th>
<th>Decile spread (%)</th>
<th>Factor group</th>
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<tbody>
<tr>
<td>2-Year Ahead EPS Growth</td>
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<td>Earnings Momentum</td>
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<td>Average Collection Period</td>
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<td>Management Quality</td>
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<td>2-Year Ahead EPS Growth Percentage Change</td>
<td>8.31</td>
<td>Earnings Momentum</td>
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<td>TTM Sales-to-Enterprise Value</td>
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<td>Deep Value</td>
</tr>
<tr>
<td>TTM Sales-to-Price</td>
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<td>Deep Value</td>
</tr>
<tr>
<td>Cyclically and Inflation Adjusted Earnings-to-Price</td>
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<td>Deep Value</td>
</tr>
<tr>
<td>Cyclically Adjusted Earnings-to-Price</td>
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<td>Deep Value</td>
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Source: IHS Markit © 2020 IHS Markit

### Table 5
**US Small Cap bottom decile return spread factor performance, Aug 2020**

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<th>Factor</th>
<th>Decile spread (%)</th>
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Source: IHS Markit © 2020 IHS Markit

### Figure 2
**US Small Cap 2-Year Ahead EPS Growth decile return spreads**

Source: IHS Markit © 2020 IHS Markit
Europe

Modest growth in the eurozone manufacturing economy was sustained in August, following its first growth in 18 months during July. The PMI registered at 51.7 in August, little moved from 51.8 in July, continuing the recovery from the severe COVID-19-related constraints on economic activity. Country level data indicated divergent trends, with Italy, Ireland, the Netherlands, Germany and Austria above the 50.0 no-change mark, while manufacturing performance stagnated in Spain, France and Greece. While business confidence continued to recover, stock market optimism was once again more subdued, on headwinds from a strong euro, trading at levels versus the US dollar not seen since May 2018, making European products less competitive abroad, alongside fears of more COVID-19-related restrictions.

As with US markets, quality and value measures were prevalent among the top performing factors in Developed Europe in August (Table 6), led by TTM Gross Profit to Assets (5.66%) and 5-yr Relative Book-to-Market (3.91%), respectively. At the opposite extreme, 60-Month Beta (-5.25%) was one of the weakest performing factors for the month (Table 7), as investors have sought higher risk shares in general following the initial shock of the COVID-19-induced volatility (Figure 3). Other bottom performing factors include Leading 12 Month Regular Dividend Yield (-4.79%), perhaps an indication of concerns for corporations to reach their current dividend expectations.

Table 6

<table>
<thead>
<tr>
<th>Developed Europe top decile return spread factor performance, Aug 2020</th>
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<tbody>
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<td>Factor</td>
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<td>TTM Gross Profit to Assets</td>
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<tr>
<td>14 Day Relative Strength Index</td>
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<tr>
<td>Natural Logarithm of Market Capitalization (USD)</td>
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<tr>
<td>1-Month Active Return</td>
</tr>
<tr>
<td>5-yr Relative Book-to-Market</td>
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<tr>
<td>5-yr Relative TTM EBITDA-to-Price</td>
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<td>TTM Cash Flow-to-Price</td>
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<tr>
<td>Financial Leverage</td>
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<tr>
<td>TTM EBITDA-to-Price</td>
</tr>
<tr>
<td>3-yr Compound Annual Sales Growth</td>
</tr>
<tr>
<td>Market Leverage</td>
</tr>
<tr>
<td>3-yr Growth in TTM Cash Flow</td>
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<tr>
<td>2-Month Active Return</td>
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<tr>
<td>5-yr Relative TTM Cash Flow-to-Price</td>
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<tr>
<td>5-yr Relative TTM Sales-to-Price</td>
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</table>

Source: IHS Markit

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IHS Markit | Key drivers: Risk factors shrug off virus concerns

Table 7
Developed Europe bottom decile return spread factor performance, Aug 2020

<table>
<thead>
<tr>
<th>Factor</th>
<th>Decile spread (%)</th>
<th>Factor group</th>
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</thead>
<tbody>
<tr>
<td>5-yr Relative Leading 12-Month Earnings Yield</td>
<td>-5.37</td>
<td>Relative Value</td>
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<tr>
<td>60-Month Beta</td>
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<td>Liquidity, Risk &amp; Size</td>
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<td>CV of Prior 90-Day Closing Prices</td>
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<td>Product of Beta and Sigma</td>
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<td>Liquidity, Risk &amp; Size</td>
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<td>Leading 12 Month Regular Dividend Yield</td>
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<td>Dividend Forecast</td>
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<tr>
<td>24-Month Value at Risk</td>
<td>-4.77</td>
<td>Price Momentum</td>
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<td>Leading 12 Month Total Dividend Yield</td>
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<td>Dividend Forecast</td>
</tr>
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<td>1-yr Change in Total Assets</td>
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<td>Leading 1-Year Regular Dividend Payout</td>
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<td>Dividend Forecast</td>
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<td>Stock Return Volatility</td>
<td>-4.36</td>
<td>Liquidity, Risk &amp; Size</td>
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</table>

Source: IHS Markit

Figure 3
Developed Europe 60-Month Beta decile return spreads

Source: IHS Markit

Asia-Pacific

Improvements in manufacturing operating conditions in the two largest Asian economies of China and Japan were seen in August. In China, the headline PMI rose to 53.1 in August, from 52.8 in July, lifted by strong expansions in production and new orders and the first increase in export sales in 2020 to date. In Japan, the manufacturing downturn continued to ease, with the PMI picking up to 47.2 in August, from 45.2 in July, the highest reading since February, supported by softer declines in production and new business. However, stocks fared better in Japan compared with China despite a late month dip on Prime Minister Abe’s announcement that he was resigning.

Momentum metrics were displaced by corporate fundamentals for the top spots of factor performance in developed Pacific markets outside Japan in August (Table 8), including factors such as Net Current Assets-to-Price (5.23%) and Cash Earnings Return On Equity (3.46%). We also highlight Implied Loan Rate (4.99%), a Short Sentiment indicator favoring stocks with low cost to borrow, for which investors rewarded with a 15-percentage point month-on-month swing in performance (Figure 4). Conversely, factors which lagged for the month (Table 9) once again include several risk measures including 24-Month Value at Risk (-7.16%), as investors sought higher risk stocks.
In Japan, price reversal metrics dominated the list of top performing factors (Table 10) in August. 2-Month Active Return (16.85%) led the way, with a spike in spread (Figure 5) to a level not seen since January 2000, indicating that investors shifted to recent underperformers in droves. At the opposite end of the spectrum, 52-Week High (-17.68%) traversed from the top performer in July to the weakest performer in August, joining other Price Momentum measures on the laggard board (Table 11).

Table 8

| Developed Pacific exJapan top decile return spread factor performance, Aug 2020 |
|-------------------------------------------------|----------------|----------------|
| Factor                                          | Decile spread (%) | Factor group    |
| Net Current Assets-to-Price                     | 5.23            | Deep Value      |
| Implied Loan Rate                               | 4.99            | Short Sentiment |
| 60-Month Active Return with 1-Month Lag         | 4.71            | Price Momentum  |
| 5-yr Relative TTM Oper Cash Flow-to-Price       | 4.64            | Relative Value  |
| Ohlson Bankruptcy Score                         | 3.61            | Liquidity, Risk & Size |
| Net Cash to Equity                              | 3.56            | Liquidity, Risk & Size |
| Cash Earnings Return On Equity                  | 3.46            | Management Quality |
| Net Debt Ratio                                  | 3.17            | Management Quality |
| TTM Gross Profit to Assets                      | 3.16            | Management Quality |
| 1-yr Growth in TTM Free Cash Flow               | 3.15            | Historical Growth |
| Yearly TTM Total Sales Growth Rate              | 3.05            | Historical Growth |
| Cash Cycle                                      | 3.05            | Management Quality |
| Assets Turnover Ratio                           | 2.91            | Management Quality |
| TTM Gross Profit Margin                         | 2.88            | Management Quality |
| Comprehensive Debt to Total Assets              | 2.83            | Liquidity, Risk & Size |

Source: IHS Markit © 2020 IHS Markit

Figure 4

Developed Pacific exJapan Implied Loan Rate decile return spreads

Source: IHS Markit © 2020 IHS Markit
Table 9

<table>
<thead>
<tr>
<th>Factor</th>
<th>Decile spread (%)</th>
<th>Factor group</th>
</tr>
</thead>
<tbody>
<tr>
<td>24-Month Value at Risk</td>
<td>-7.16</td>
<td>Price Momentum</td>
</tr>
<tr>
<td>CV of Prior 90-Day Closing Prices</td>
<td>-6.82</td>
<td>Price Momentum</td>
</tr>
<tr>
<td>Forward 12-M EPS-to-Enterprise Value</td>
<td>-6.42</td>
<td>Deep Value</td>
</tr>
<tr>
<td>Predicted Dividend Yield</td>
<td>-6.34</td>
<td>Deep Value</td>
</tr>
<tr>
<td>Earnings Torpedo</td>
<td>-6.29</td>
<td>Earnings Momentum</td>
</tr>
<tr>
<td>Time Weighted Earnings Yield</td>
<td>-5.83</td>
<td>Deep Value</td>
</tr>
<tr>
<td>Forward Return on Equity</td>
<td>-5.60</td>
<td>Management Quality</td>
</tr>
<tr>
<td>Leading 12-Month Mean Earnings Yield</td>
<td>-5.58</td>
<td>Deep Value</td>
</tr>
<tr>
<td>60-Month Beta</td>
<td>-5.49</td>
<td>Liquidity, Risk &amp; Size</td>
</tr>
<tr>
<td>60-Day Residual Risk</td>
<td>-5.38</td>
<td>Liquidity, Risk &amp; Size</td>
</tr>
</tbody>
</table>

Source: IHS Markit © 2020 IHS Markit

Table 10

<table>
<thead>
<tr>
<th>Factor</th>
<th>Decile spread (%)</th>
<th>Factor group</th>
</tr>
</thead>
<tbody>
<tr>
<td>2-Month Active Return</td>
<td>16.85</td>
<td>Price Momentum</td>
</tr>
<tr>
<td>1-Month Active Return</td>
<td>15.53</td>
<td>Price Momentum</td>
</tr>
<tr>
<td>5-yr Relative TTM Sales-to-Price</td>
<td>15.31</td>
<td>Relative Value</td>
</tr>
<tr>
<td>4-week Industry Relative Return</td>
<td>14.57</td>
<td>Price Momentum</td>
</tr>
<tr>
<td>5-yr Relative TTM Dividend Yield</td>
<td>14.16</td>
<td>Relative Value</td>
</tr>
<tr>
<td>5-yr Relative Book-to-Market</td>
<td>14.05</td>
<td>Relative Value</td>
</tr>
<tr>
<td>5-day Industry Relative Return</td>
<td>13.96</td>
<td>Price Momentum</td>
</tr>
<tr>
<td>14 Day Relative Strength Index</td>
<td>12.62</td>
<td>Price Momentum</td>
</tr>
<tr>
<td>Price Above Last 260-day Lowest Trading Price</td>
<td>12.44</td>
<td>Price Momentum</td>
</tr>
<tr>
<td>3-Month Active Return</td>
<td>12.01</td>
<td>Price Momentum</td>
</tr>
<tr>
<td>2-Year Ahead EPS Growth</td>
<td>11.59</td>
<td>Earnings Momentum</td>
</tr>
<tr>
<td>TTM Sales-to-Price</td>
<td>10.37</td>
<td>Deep Value</td>
</tr>
<tr>
<td>US Dollar Value Sensitivity</td>
<td>10.00</td>
<td>Macro</td>
</tr>
<tr>
<td>Oil Prices Sensitivity</td>
<td>9.86</td>
<td>Macro</td>
</tr>
<tr>
<td>60-Month Alpha</td>
<td>9.86</td>
<td>Price Momentum</td>
</tr>
</tbody>
</table>

Source: IHS Markit © 2020 IHS Markit

Figure 5

Japan Standard Cap 2-Month Active Return decile return spreads

Source: IHS Markit © 2020 IHS Markit
Emerging Markets

We round out the report with a review of top (Table 12) and bottom (Table 13) performing factors in emerging markets in August. Valuation measures returned to the leaderboard, accompanied by several quality measures, as captured by Dividends-to-Cash Flow (4.85%) and Leading 12 Month Sales Yield (2.88%), among others. We also draw attention to outperformance for Natural Logarithm of Market Capitalization (USD) (3.42%), as investors favored smaller cap names in four of the last five months (Figure 6). Lastly, factors which lagged for the month represent a broad set of styles including Lending Supply (-6.14%), TTM Gross Profit Margin (-4.32%), 3-M Revision in FY1 EPS Forecasts: Dispersion Relative (-3.84%) and 24-Month Value at Risk (-3.63%).

Table 12

<table>
<thead>
<tr>
<th>Emergent Markets top quintile return spread factor performance, Aug 2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Factor</td>
</tr>
<tr>
<td>Dividends-to-Cash Flow</td>
</tr>
<tr>
<td>Unexpected Change in Accounts Receivable</td>
</tr>
<tr>
<td>Natural Logarithm of Market Capitalization (USD)</td>
</tr>
<tr>
<td>Street Consensus Rating</td>
</tr>
<tr>
<td>Cash Earnings Return On Equity</td>
</tr>
<tr>
<td>Change in QTR Sales vs. Gross Margin</td>
</tr>
<tr>
<td>Leading 12 Month Sales Yield</td>
</tr>
<tr>
<td>US Dollar Value Sensitivity</td>
</tr>
<tr>
<td>Cash &amp; Equivalents-to-Current Liabilities</td>
</tr>
<tr>
<td>1-yr Chg in Acct Receivable as % of Sales</td>
</tr>
<tr>
<td>Dividend Coverage Ratio</td>
</tr>
<tr>
<td>TTM Sales-to-Price</td>
</tr>
<tr>
<td>Time Weighted Sales Yield</td>
</tr>
<tr>
<td>1-yr Change in Total Assets</td>
</tr>
<tr>
<td>Skewness of 90-Day Stock Daily Returns</td>
</tr>
</tbody>
</table>

Source: IHS Markit © 2020 IHS Markit
Table 13
Emerging Markets bottom quintile return spread factor performance, Aug 2020

<table>
<thead>
<tr>
<th>Factor</th>
<th>Decile spread (%)</th>
<th>Factor group</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lending Supply</td>
<td>-6.14</td>
<td>Short Sentiment</td>
</tr>
<tr>
<td>Inventory Value Concentration</td>
<td>-5.93</td>
<td>Short Sentiment</td>
</tr>
<tr>
<td>Yield Curve Slope Sensitivity</td>
<td>-4.46</td>
<td>Macro</td>
</tr>
<tr>
<td>TTM Gross Profit Margin</td>
<td>-4.32</td>
<td>Management Quality</td>
</tr>
<tr>
<td>Net Income per Employee</td>
<td>-3.94</td>
<td>Management Quality</td>
</tr>
<tr>
<td>3-M Revision in FY1 EPS Forecasts: Dispersion Relative</td>
<td>-3.84</td>
<td>Earnings Momentum</td>
</tr>
<tr>
<td>24-Month Value at Risk</td>
<td>-3.63</td>
<td>Price Momentum</td>
</tr>
<tr>
<td>Slope of 66 Week Price Trend Line</td>
<td>-3.55</td>
<td>Price Momentum</td>
</tr>
<tr>
<td>Real Earnings Surprise</td>
<td>-3.48</td>
<td>Earnings Momentum</td>
</tr>
<tr>
<td>Stability of 5-yr TTM Earnings per Share</td>
<td>-3.39</td>
<td>Historical Growth</td>
</tr>
</tbody>
</table>

Source: IHS Markit © 2020 IHS Markit

Figure 6
Emerging Markets Natural Logarithm of Market Capitalization (USD) quintile return spreads

Source: IHS Markit © 2020 IHS Markit