Academic Research

Return dispersion and conditional momentum returns:International evidence

Momentum is a pervasive anomaly with high expected returns. However, momentum strategies experience infrequent but large drawdowns. This paper shows that across international equity markets these drawdowns occur simultaneously, suggesting a common driver of momentum drawdowns. Using this result, the authors examine the relationship between the expectation of structural shifts in the economy and momentum returns. Using return dispersion (the cross-sectional standard deviation of returns on 25 portfolios sorted on size and book-to-market ratio) as a proxy for structural shifts, this paper shows that high return dispersion predicts a higher probability of negative momentum returns. Moreover, when return dispersion is in its highest quintile the momentum premium is insignificant from zero across all regions. Using the relationship between momentum and return dispersion, this paper shows that altering the weight an investor places on momentum depending onthe level of return dispersion can improve the Sharpe ratio of a momentum strategy.

Click on the below link to read more about this research:

Academic Research (https://www.sciencedirect.com/science/article/pii/S0927538X16301871)

Important information

For more information please contact

Gary Adamson
Chief Executive Officer –
Platypus Asset Management

Email: gadamson@platypus.com.au

Docherty, P., & Hurst, G. (2018). Return dispersion and conditional momentum returns: International evidence. *Pacific-Basin Finance Journal*, 50, 263-278.