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US Election Special: a short update

This is an update of our US Elections Special from October, where we demonstrated how US presidential election years differ from other years in terms of Time Series Momentum (TSMOM*) and CTA performance.

Background

An election year is typically characterized by weak or negative performance during the first three quarters of the year and a significantly stronger performance during the fourth quarter. As of November 25, Evolving F EUR is up 1.30% this far in the fourth quarter and up 2.75% since the start of the year.

A reasonable explanation for why election years differ, is the uncertainty regarding the outcome of the election and thus the future fiscal and monetary policies that prevail up to election night. When that uncertainty is removed, markets may find new or reinforced directions and TSMOM develops.

2020, so far…

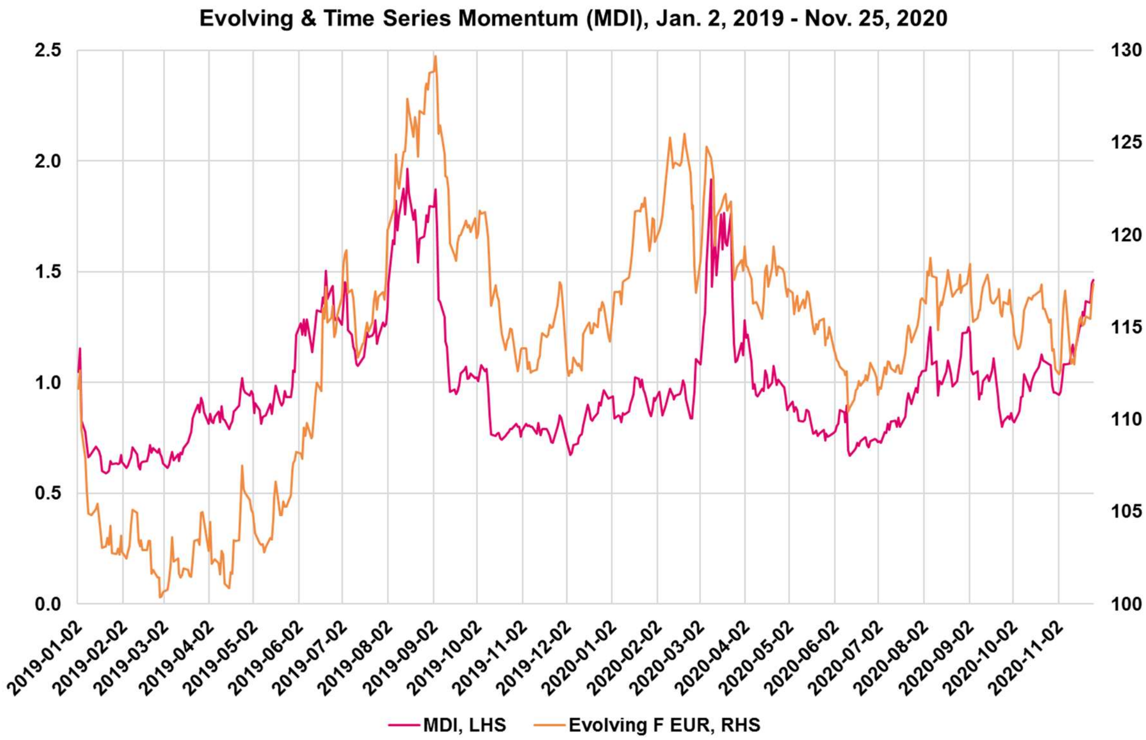
This year, uncertainty lingered longer than usual – most likely due to Trump's refusal to accept the outcome and the cascade of lawsuits claiming election fraud, and the drawn-out counting of ballots. Worries over the Corona virus and a possible stimulus package did not alleviate the uncertainty.

Now, conditions seem to have changed. This is manifested by the recent upticks in TSMOM (measured as RPM's MDI) that have occurred in tune with what seems like Trump's gradual realization of his loss and continued good news regarding vaccines. TSMOM is now mainly driven by energies, various soft commodities and metals, and stock indices.

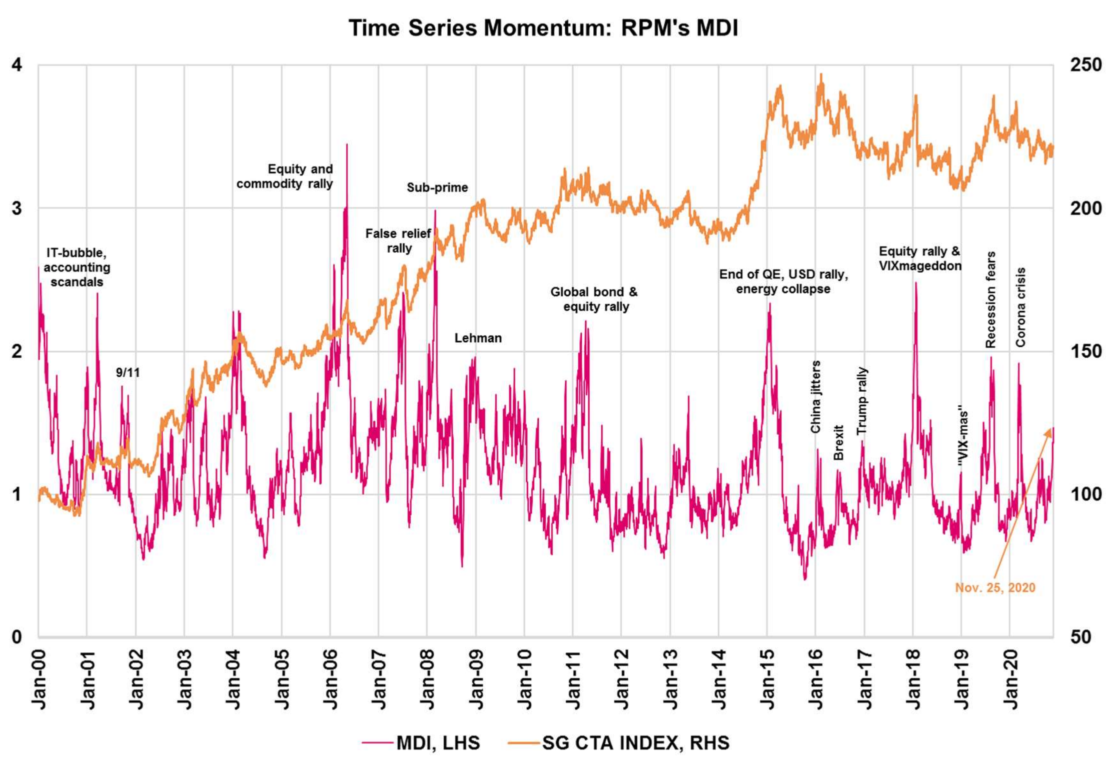
In the absence of any new controversies over the election result and disappointments in the fight against the virus or any other unforeseen event, there are reason to be optimistic for the remainder of the year. Most of our indicators have turned bullish on TSMOM and CTA performance.

****Time Series Momentum (TSMOM) is a risk factor first identified by Moskowitz et. al. in 2011. RPM's method of calculating TSMOM is called MDI and based on the ratio of absolute price move and volatility for a wide array of markets and timeframes. The long-term correlation of MDI and the performance of the SocGen CTA Index is 0.73, calculated on daily observations.***

The graph below illustrates the development of TSMOM and CTA performance in 2019-2020:



For TSMOM and CTA performance in a longer perspective see below:



Outlook

Despite the ongoing "lockdown light" in Europe, equity markets and other risky assets have started to rally largely driven by removed US election uncertainty and breakthroughs with regards to vaccines against coronavirus. The end is in sight! Whereas economic statistics keep surprising on the upside, the outlook for continued recovery has brightened even further. As markets are now pricing in return-to-normal-life by first half of 2021, TSMOM is expected to increase further until year-end which might indicate a favorable environment for CTAs up until year end.

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