

Are Trend Strategies Dead?



Many investors have asked us this question given the lackluster, and frankly disappointing, performance of many of their Trend managers prior to 2019.

Industry observers have opined on this as well, and they sometimes attribute disappointing performance to things like: too much capital in the strategy, lower levels of overall market volatility, the effects of quantitative easing, and myriad other reasons.

With little specificity around the answers, we decided to conduct some research and draw our own conclusions.

Our Process

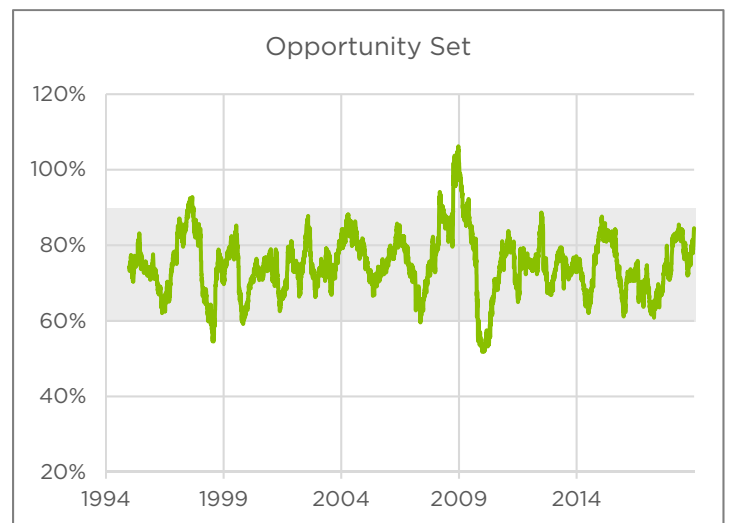
- We started with a simple trend strategy that we felt was generally representative of the industry, and applied it to 25 years of price data across equity indices, interest rates, currencies and commodities.⁽¹⁾
- We then developed a novel method of identifying the “opportunity set” this model is responding to and representative of what one would identify as dominant trends when reviewing price data with the benefit of hindsight.
- This allowed us to decompose performance into two components:
 - A hindsight-informed raw opportunity set that is not fully capturable in practice
 - A capture metric that quantifies over a specified time window what percentage of this opportunity set could be captured
- From this we sought to answer two questions:
 - How has the trend opportunity set evolved over time?
 - How has a simple trend strategy’s ability to capture this opportunity set been diminished in the last several years?

Our Findings

Our conclusions are reassuring. The Trend opportunity set has been relatively consistent throughout the past 25 years. With perfect hindsight, the opportunity on an annual basis has ranged from 60% to 90% per annum for a strategy with a target vol of 10%. See **Chart 1**.

Obviously we cannot trade with perfect hindsight and through time. Even the best Trend strategies are by definition late to enter a trend and exit once a peak or trough has passed. Said differently, we only expect a strategy to capture a small percentage of the opportunity set.

Chart 1



(1) Simple trend strategy performance based on hypothetical results. Please see last page for more information.



Our Findings (continued)

On average based upon the implementation we chose, this percentage was in the low teens.

That said, the simple strategy, albeit designed with some benefit of history, was profitable 21 of 25 years, and every year since 2012. See **Table 2**.

Its average return was 8.1% for a portfolio that was run with a 10% annual vol, a compelling IR for a strategy that has zero correlation to the equity markets and is highly liquid.

Our study also shows that the capture rate varies through time and that the recent rate of capture has been low. See **Chart 3**. This would be consistent with lower return in the space. However, the recent period of low capture, and lower returns, is not at all remarkable when viewed over a 25-year period.

Chart 3

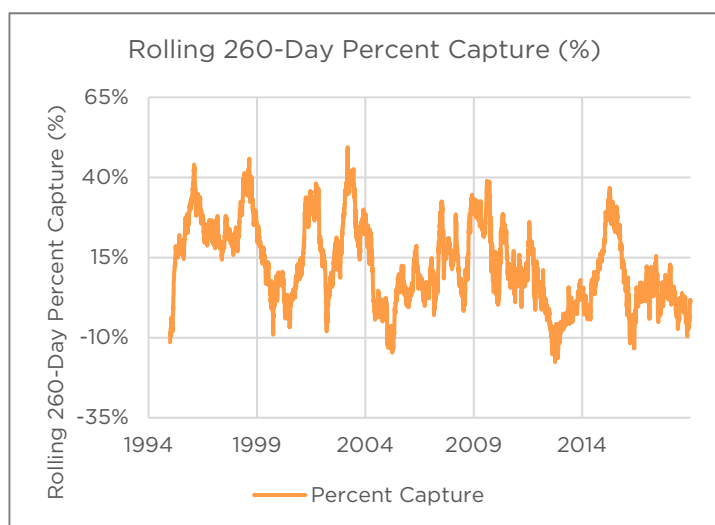


Table 2

Year	Strategy Return ⁽¹⁾
1994	-9.0%
1995	25.0%
1996	16.7%
1997	15.6%
1998	18.0%
1999	6.0%
2000	6.4%
2001	12.4%
2002	19.2%
2003	19.0%
2004	-1.8%
2005	-0.9%
2006	6.6%
2007	9.1%
2008	31.9%
2009	4.2%
2010	8.3%
2011	3.8%
2012	-6.4%
2013	2.7%
2014	13.7%
2015	3.6%
2016	6.4%
2017	2.2%
2018	0.7%
Ann. Total Return	8.1%

Despite the recent move to de-allocate to Trend strategies, we believe they continue to offer value in portfolio construction and have the potential to generate good returns while providing diversification to long equities. Nothing in our study would indicate to us that trend strategies are “dead”!

If you would like to learn more, please reach out to Neal Howe to schedule a call with our team to learn more about the study.

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