

## Valuable signals in crowded short trades

Although unusual terminology, factor crowdedness, provides quantifiable clarity into which factors short sellers are targeting. Assigning sentiment to strategy, factor crowding presents investors with exclusive insights and trading signals.

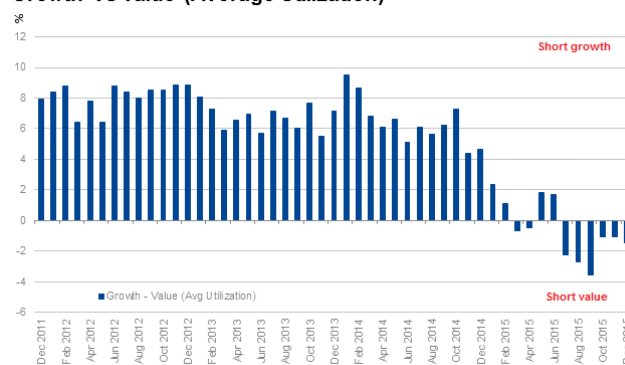
- Short sellers shift from growth to value in a trend last seen during financial crisis
- Trend reversal sees short demand across value stocks more than double by utilisation
- Stock selection overlaid with utilisation enhances growth and value returns as well as risk profiles

To access the full research report on Factor Crowdedness, [please contact us](#).

Factor Crowdedness refers to the difference of utilisation\* levels between groups of stocks that contain or exhibit certain qualities or factors. Factor Crowdedness surfaces the thematic sentiments of short sellers, providing actionable information to both the short, long and neutral investor. Even after accounting for borrowing costs, since July 2014 a long short strategy across value stocks ranked by utilisation has delivered returns of 50% on an annual basis.

Gauging for 'crowdedness' using utilisation levels is possible by leveraging two distinct data sets; Markit [Research Signals](#) and [Securities Finance data](#). Post September 2014 across a universe of 1000 large cap US companies, short sellers who were previously crowded around growth stocks began to shift towards value stocks. This reversal is similar to the trend that played out during the financial crisis.

Growth vs Value (Average Utilization)

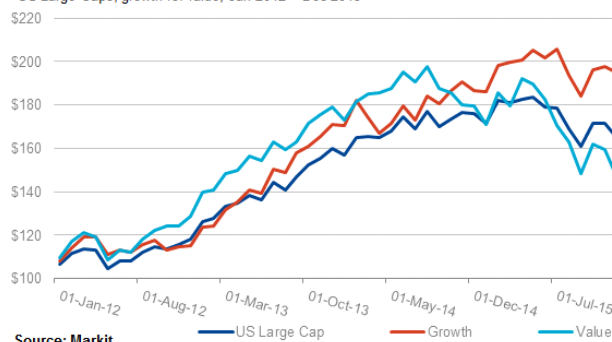


Source: Markit

Assessing cumulative returns across the entire universe of stocks reveals that growth has outperformed the universe with value significantly underperforming since 2014, adding further credibility to Factor Crowdedness. Increased utilisation levels in value stocks during this time indeed underperformed. Currently across value stocks, utilisation levels remain high.

Cumulative total returns

US Large Caps, growth vs. value, Jan 2012 – Dec 2015



Source: Markit

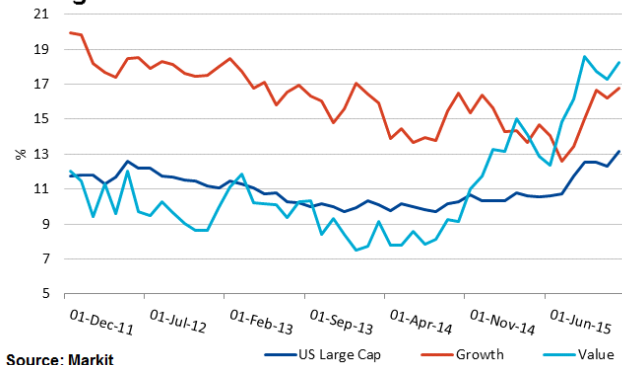
The four factors recently analysed include; Book to Market, Price Momentum, Beta and Realised Volatility. The test period was conducted with monthly data from December 2011 to 2015. In general, growth stocks (ranked by the Book to Market factor), high momentum, high beta and volatile stocks carried higher utilisation levels than the universe during this time frame.

Rank		2012	2013	2014	2015
<b>US Large Cap</b>		<b>12%</b>	<b>11%</b>	<b>10%</b>	<b>11%</b>
Book to Market	Low (Growth)	18%	17%	15%	15%
	High (Value)	10%	10%	9%	15%
Price Momentum	Low	8%	7%	6%	6%
	High	21%	19%	17%	21%
Beta	Low	11%	10%	10%	7%
	High	15%	12%	12%	16%
Realized Volatility	Low	9%	8%	7%	6%
	High	25%	22%	22%	26%

Table 1: Average Utilization by factors, US Large Caps, Dec 2011 – Dec 2015

The sharp rise in average utilisation in value stocks shown below (in blue) quickly overtook both the average of the universe and growth stocks in 2015. Average utilisation across value stocks more than doubled between September 2015 and the end of 2015.

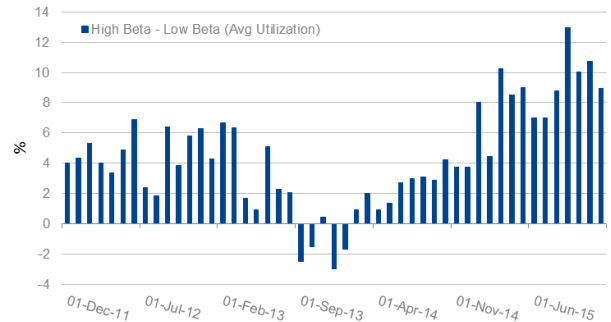
**Average utilization**



Source: Markit

Since 2013 and up to the end of 2015, short sellers have almost consistently increased exposure to high beta stocks. Considering the recent market selloff in 2016 this indicates that these were timely shifts, pre-empting recent market movements.

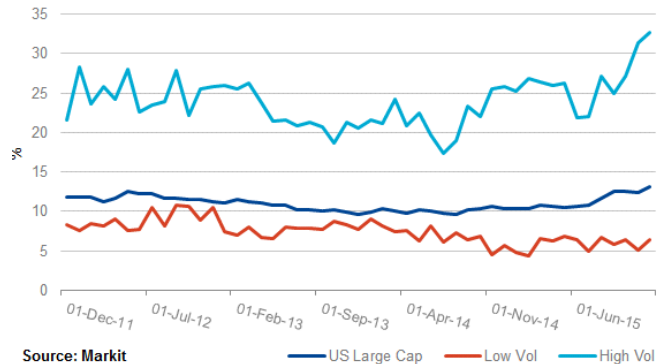
**High Beta vs Low Beta (Average Utilization)**



Source: Markit

Short sellers additionally increased positions in stocks with higher levels of volatility and the average difference in utilisation between the least and most volatile stocks reaching the highest levels seen in over five years.

**Average utilization**



Source: Markit

Filtering growth stocks by low utilisation returns over the test period are enhanced. The same is true for value stocks however, additionally, with a long, short strategy, long value stocks with low utilisation and short value stocks with high utilisation can achieve a higher Sharpe ratio than buying all value stocks. In other words, a market neutral strategy within the value universe, using utilisation pays even more than the value universe overall.

**\*Utilisation** specifically measures how much stock is sold short out of the total available in securities lending pools, and provides clarity on supply and demand dynamics.

\*To receive more information on **Securities Finance, Research Signals, Exchange Traded Products, Dividend Forecasting** or our Short Squeeze model please **contact us**

To read this article on our commentary website please click **here**.

### **Relte Stephen Schutte**

Analyst

Markit

Tel: +44 207 064 6447

Email: [relte.schutte@markit.com](mailto:relte.schutte@markit.com)

For further information, please visit [www.markit.com](http://www.markit.com)

The intellectual property rights to this report provided herein is owned by Markit Group limited. Any unauthorised use, including but not limited to copying, distributing, transmitting or otherwise of any data appearing is not permitted without Markit's prior consent. Markit shall not have any liability, duty or obligation for or relating to the content or information ("data") contained herein, any errors, inaccuracies, omission or delays in the data, or for any actions taken in reliance thereon. In no event shall Markit be liable for any special, incidental, consequential damages, arising out of the use of the data. Markit is a trademark owned by the Markit group.

This report does not constitute nor shall it be construed as an offer by Markit to buy or sell any particular security, financial instrument or financial service. The analysis provided in this report is of a general and impersonal nature. This report shall not be construed as providing investment advice that is adapted to or appropriate for any particular investment strategy or portfolio. This report does not and shall not be construed as providing any recommendations as to whether it is appropriate for any person or entity to "buy", "sell" or "hold" a particular investment.