

## AlphaScreens: the might of momentum

11 February 2022

### Revamped UK screens plus US momentum

*We've given our earnings upgrade momentum screens a facelift. Apart from slight tweaks, the market-beating methodology is the same, but we're now screening from different large-cap, mid-cap and small-cap indices. We've also added a US screen that highlights the best S&P 500 momentum stocks. Results this month are somewhat reflective of asset allocators' preferred trades in an environment of rising inflation and central banks turning hawkish on rates.*

- We're now basing the starting universe for our UK Alpha screens on the Numis index family – the aim is to give results that better fit into a remit of identifying large-cap, mid-cap and small-cap shares.
- Main market and Aim shares will be grouped according to market capitalisation (which affects the momentum ranking in each size grouping and gives more useful results). We will also be using indices that exclude investment trusts, although we continue to cover ITs extensively in the Alpha investment trust report.
- We've temporarily eased the year one earnings upgrade momentum tests to allow for the effect the pandemic has had on how forecasts have changed.
- Leading larger companies reflect the improved performance and a bullish view of the prospects for oil & gas, resources and energy companies. Banks also score well, as although they will face loan impairments if higher interest rates cause a recession, those higher rates will make lending more profitable to individuals and businesses that remain solvent.
- Small companies are grouped together in our version of Numis' NSCI plus Aim index. This includes all main market companies that were in the bottom 10 per cent in size by market capitalisation and Aim companies that are below that size cut-off. This gives a much better appreciation of the opportunity set for UK-listed small companies. Three companies pass all the tests.
- We've also screened the S&P 500 for earnings upgrade stocks stateside. We're including only companies that pass 7/7 tests this month and the results reflect the surge in positive sentiment towards the energy sector.

James Norrington

## Building on great expectations

Momentum shares, those that have seen the biggest share price gains in a recent period, have frequently been observed to outperform in the subsequent period. Whether that's down to initial underreaction to good news (Jegadeesh and Titman), or simply animal spirits, it's a well attested to phenomenon.

Yet there are drawbacks: when momentum fails, it has done horribly. Peak-to-trough drawdowns (high to low mark-to-market losses) have been as much as 50 per cent. Few investors have nerves stern enough to ride out that sort of drop and keep faith with the intensive trading to maintain the strategy.

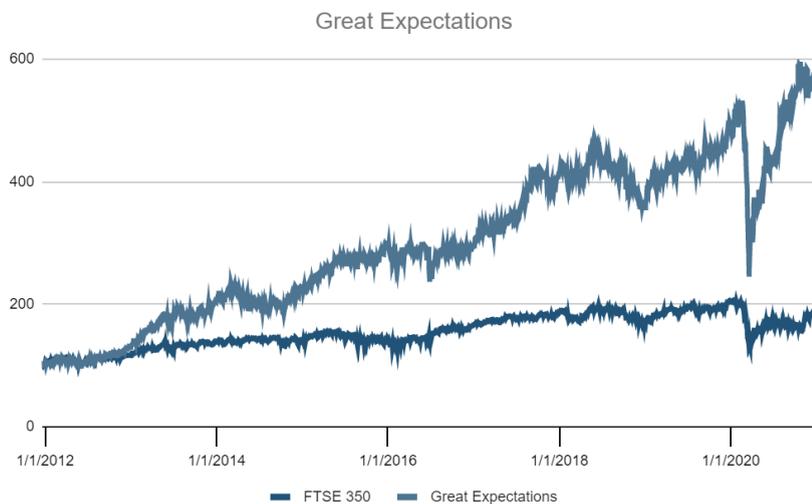
On a practical level, charges for churning between momentum stocks on a quarterly, or even half-yearly, basis would rack up costs. So, even when momentum works, charges seriously eat into the return premium.

## Shifting the focus to earnings

Being selective about individual momentum stocks is difficult and it reintroduces the element of decision making (with all the mental short-cuts and cognitive biases that entails), which a mechanical strategy like momentum should eliminate. Moving the emphasis from pure share price momentum to optimism about profitability and analysts' upgrade cycles is by no means a flawless approach, but it certainly provides a more useful starting point in terms of idea generation for individual shares.

Over time the Investors' Chronicle methodology of looking not only at earnings forecast momentum, but also at the momentum in the pattern of analysts' upgrades, has proved hugely successful. Fewer companies meet the criteria of forecast upgrades and the momentum in the sentiment behind the upgrades (the latter factor being a compulsory test in our screen), so it's a system that can be followed more easily. Although, as some pretty horrendous losses at times demonstrate, the screens are best employed as a source of potential ideas, not as a strategy to be followed exactly.

Performance statistics for the "Great Expectations" screen Investors' Chronicle has run for years against the FTSE All-Share index, demonstrate the potential of the system, but note the shocking falls in early 2020 when the coronavirus pandemic hit.



Source: Refinitiv, Investors' Chronicle

## Methodology and some tweaks to allow for the pandemic

- **Earnings upgrade momentum:** EPS upgrades over the past 12 months of at least 10 per cent for both the next financial year (in normal years, this test must be passed for the current financial year, too – see below).
- **Earnings momentum:** Forecast EPS growth of at least 10 per cent in the current financial year and next financial year.
- **Price momentum:** Studies have found that the longer price momentum has persisted the more likely it is to be 'stale' and set to reverse. The Alpha momentum screen tests for strong share price performance over four different periods, which helps check price momentum remains fresh. Companies are tested whether they are in the top quartile of shares based on trailing 12-month share price momentum and whether they are above the index median for trailing six-month, three-month and one-month share price momentum.

Companies must pass the earnings upgrade momentum test(s). Those that do are listed by the total number of tests they pass – out of seven (eight in normal years) – and within that a combined ranking score of earnings upgrade and three-month share price momentum.

The core test for our Great Expectations screen is for analysts to have upgraded their view of a company's earnings outlook in the last year. Before the pandemic, this test had to be passed for the current and next financial years. Thanks to the exceptional rebounds expected for the current year (with businesses reopening after lockdowns), momentum in upgrades is a given. Therefore, for the next 12 months, we are dropping one of the tests – we're only

interested if analysts are getting more excited about the prospects for profits growing in the following year, a measure of sentiment less likely to appear distorted by the restart. This is also a test that shows up the companies analysts are expecting to do well in the more inflationary environment.

## New indices, a tighter set of ideas

The Alpha earnings momentum screens have run the Great Expectations tests against the FTSE All-Share index (for 'large-cap' companies); the FTSE All Small Companies index (for main market 'small cap' companies); and the FTSE Aim All-Share index for the junior market. Where this has fallen down in the past is that a lot of the companies in the FTSE All-Share index are mid-to-small caps, so few genuine large-caps were appearing on the momentum ranking tests (especially price tests) that were comparing the medians and percentiles for an index containing many small companies.

Going forward, we're switching to screening in an equities universe inspired by the Numis family of UK indices. The aim is to give investors a true overview of the genuine large-cap; mid-cap and small-cap companies that are exciting analysts and the markets.

We will also be excluding investment trusts from results. The purpose of these screens is to highlight individual companies that are worth investigating further. Including closed-end funds in the universe skews the results and distracts from that objective. Investment trusts are given their own, far more detailed, analysis in the regular Alpha Investment Trust report.

## Breakdown of the Numis indices we have been inspired by:

**Numis Large-Cap** index (excluding investment companies/trusts): This includes the top 80 per cent of companies by market capitalisation that are listed on the UK main market. The lower size cut-off for 2022 is **£4.12bn** market cap.

**Numis Mid-Cap** index (excluding investment companies/trusts): This includes the 15 per cent of UK main market listed companies below the top 80 per cent but above the bottom five per cent by market capitalisation. The upper size cut-off is **£4.12bn** and the lower cut-off is **£880mn** market cap.

**NSCI** (Numis Small Companies Index), version excluding investment trusts: This includes the bottom 10 per cent of the UK main market by market capitalisation

(so there is overlap with the Numis Mid Cap index). The upper size cut-off is **£1.64bn** market cap.

**NSCI plus Aim**, version excluding investment trusts: This adds all Aim companies below the **£1.64bn** market cap cut-off to the NSCI.

## How the AlphaScreens will be guided by the Numis indices

The Numis index family is rebalanced at the end of the calendar year, but we will be taking elements of their methodology to update the universe of companies we look at every time we run the screens. Our cut-off points will move around and our screens will capture the impact of mergers and acquisitions, de-listings and initial public offerings on the UK equity universe throughout the year.

**Large Cap** – This will copy and refresh the Numis Large-Cap (excl ITs) index methodology. Top 80 per cent of main market companies by size.

**Mid Cap** – This will copy and refresh the Numis Mid-Cap (excl ITs) index methodology, plus we will add in the Aim-listed companies that are within the size parameters of the main market index. Bottom 20 per cent (excluding bottom five per cent) of main market companies; plus all Aim companies that also have a market cap within this size range.

**Small Cap** – This will copy and refresh the NSCI plus Aim (excl ITs) index methodology. Bottom 10 per cent of main market companies and all Aim companies that also have a market cap below the cut-off size.

## Performance tracking

Clearly, we won't be able to claim the back-tested performance of the Investors' Chronicle Great Expectations screen, which is based on all the companies in the FTSE All-Share. The deconstructed performance of momentum shares selected from that universe will be attributable to a different set of size and beta factors to the ones we will be exposed to.

Back-testing in general is a very dangerous tool. One needs to guard against survivorship bias in an index and look-ahead bias (factoring in data that although it relates to a period, wouldn't have been known at the time). Therefore this is year zero for the performance tracking of the screens. Finally,

it is worth reiterating the purpose is to flag ideas. What the screens do not do is generate off-the-shelf portfolios.

## American adventure

One no-brainer addition to the Alpha screens is to add American companies to the mix. We've run our methodology against the S&P 500 and there are so many companies ranking well on the criteria we are only showing those that get full marks.

## February 2022 results

### Large-cap momentum shares (passing at least 6 out of 7 tests)

Name	Share price Ticker (last close)	Mkt cap (£mn)	Fwd 12-mth PE	Trailing 12-mth DY	Next yr 12-mth EPS upgrade	Fwd EPS growth current FY	Fwd EPS growth next FY	3-mth share price mom	Net cash (£mn)	Tests passed (out of 7)	Tests failed
Airtel Africa	AAF	144 5412	10.1	2.3%	90%	101.0%	25.3%	10%	-1427.1	7	na
Glencore	GLEN	421 55533	7.4	2.7%	118%	305.4%	8.8%	18%	-27710.6	6	/>10% EPSgrth FY+2/
Anglo American	AAL	3600 48170	9.2	4.9%	41%	194.3%	-23.8%	32%	-1139.0	6	/>10% EPSgrth FY+2/
BP	BP	411 80514	7.2	3.8%	48%	21.8%	-4.7%	18%	-36417.7	6	/>10% EPSgrth FY+2/
HSBC	HSBA	562 113879	11.4	2.8%	20%	100.4%	-5.6%	30%	-	6	/>10% EPSgrth FY+2/
Shell	SHEL	2019 154137	8.3	3.2%	42%	33.4%	-2.4%	20%	-43247.1	6	/>10% EPSgrth FY+2/
Barclays	BARC	209 34963	7.6	1.4%	29%	257.6%	-19.7%	8%	-	6	/>10% EPSgrth FY+2/
Lloyds Banking	LLOY	53 37934	8.5	2.3%	30%	511.7%	-22.0%	8%	-	6	/>10% EPSgrth FY+2/
Centrica	CNA	79 4649	9.8	0.0%	22%	-46.7%	128.1%	24%	-5845.0	6	/>10% EPSgrth FY+1/

Source: FactSet, 11 February 2022

### UK mid-cap momentum shares (passing at least 6 out of 7 tests)

Name	Share price Ticker (last close)	Mkt cap (£mn)	Fwd 12-mth PE	Trailing 12-mth DY	Next year 12-mth EPS upgrade	Fwd EPS growth cur FY	Fwd EPS growth next FY	3-mth share price mom	Net cash (£mn)	Tests passed (out of 7)	Tests failed
Investec	INVP	454 3160	8.2	4.1%	23%	98.2%	13.7%	30%	-	7	na
Watches of Switzerland	WOSG	1318 3158	25.2	0.0%	52%	78.8%	28.9%	5%	-112.7	7	na
Beazley	BEZ	487 2968	10.4	0.0%	23%	23.8%	17.5%	20%	-	7	na
Drax	DRX	643 2565	9.9	2.8%	48%	-4.9%	125.7%	19%	-1018.2	6	/>10% EPSgrth FY+1/
OSB	OSB	569 2553	7.5	2.5%	20%	33.2%	-2.7%	14%	-	6	/>10% EPSgrth FY+2/
TBC Bank	TBCG	1582 873	4.6	2.2%	37%	173.2%	-0.4%	1%	-	6	/>10% EPSgrth FY+2/
Computacenter	CCC	2776 3169	17.8	2.0%	22%	22.0%	1.1%	2%	-1276.4	6	/>10% EPSgrth FY+2/
Biffa	BIFF	356 1087	15.4	0.6%	31%	156.5%	19.5%	-9%	-317.0	6	/3mthMom/
Marshalls	MSLH	691 1382	21.5	1.3%	12%	235.3%	11.6%	-5%	-53.5	6	/1yrMom/
Spire Healthcare	SPI	240 963	32.3	0.0%	47%	-	53590.4%	1%	-147.6	6	/>10% EPSgrth FY+1/

Source: FactSet, 11 February 2022

## UK main market and Aim small-cap momentum shares (passing at least 6 out of 7 tests)

Name	Ticker	Share price (last close)	Mkt cap (£mn)	Fwd 12-mth PE	Trailing 12-mth DY	Next year 12-mth EPS upgrade	Fwd EPS gwth cur FY	Fwd EPS gwth next FY	3-mth share price mom	Net cash (£mn)	Tests passed (out of 7)	Tests failed
DWF	DWF	118	384	10.4	3.8%	11%	35.0%	17.4%	10%	-126.2	7	na
Frenkel Topping	FEN	80	91	17.8	1.7%	19%	146.0%	41.9%	3%	-	7	na
Galliford Try	GFRD	190	211	12.0	2.5%	10%	49.3%	18.3%	-2%	-276.5	7	na
PetroTal Corp.	PTAL	39	333	3.3	0.0%	168%	-	86.5%	59%	-36.2	6	>10% EPSgrth FY+1/
Lookers	LOOK	101	396	9.3	0.0%	43%	494.4%	-38.4%	64%	-804.8	6	>10% EPSgrth FY+2/
Serica Energy	SQZ	255	686	3.3	1.4%	354%	2392.2%	9.3%	36%	-6.1	6	>10% EPSgrth FY+2/
Savannah Energy	SAVE	28	348	5.2	0.0%	198%	-	330.6%	44%	-108.1	6	>10% EPSgrth FY+1/
John Menzies	MNZS	478	439	13.2	0.0%	42%	-	71.0%	58%	-221.8	6	>10% EPSgrth FY+1/
iEnergizer Ltd	IBPO	372	707	12.5	4.4%	78%	32.3%	22.8%	42%	11.0	6	/1yrMom/
Equals	EQLS	80	143	20.8	0.0%	90%	-	39.4%	20%	-6.0	6	>10% EPSgrth FY+1/
Pendragon	PDG	22	312	6.8	0.0%	55%	673.1%	-29.2%	18%	-913.6	6	>10% EPSgrth FY+2/
Capital Ltd	CAPD	96	182	8.3	0.0%	32%	-16.8%	10.2%	20%	-	6	>10% EPSgrth FY+1/
Lok'nStore	LOK	1010	303	30.6	1.5%	85%	200.0%	-1.5%	11%	2.2	6	>10% EPSgrth FY+2/
Atalaya Mining	ATYM	432	605	5.8	6.8%	113%	312.0%	-6.4%	9%	-76.5	6	>10% EPSgrth FY+2/
M&C Saatchi	SAA	178	217	17.3	0.0%	46%	450.0%	20.0%	9%	-101.1	6	/1mthMom/
Gulf Keystone Petroleum	GKP	221	473	3.1	11.5%	158%	-	64.6%	6%	57.6	6	>10% EPSgrth FY+1/
Sanderson Design	SDG	187	133	13.2	0.4%	67%	69.4%	6.8%	9%	-8.0	6	>10% EPSgrth FY+2/
Colefax	CFX	705	56	12.9	0.0%	20%	52.1%	-26.1%	9%	-3.0	6	>10% EPSgrth FY+2/
Secure Trust Bank	STB	1335	249	6.6	4.8%	11%	178.3%	-19.0%	6%	-	6	>10% EPSgrth FY+2/
Keystone Law	KEYS	825	258	37.9	1.8%	16%	48.8%	-6.3%	8%	-8.0	6	>10% EPSgrth FY+2/
Alpha Fin. Mkts Consulting	AFM	405	455	21.0	1.9%	13%	23.0%	11.5%	14%	4.5	6	/1mthMom/
James Cropper	CRPR	1425	136	22.5	0.2%	16%	165.9%	52.5%	6%	-16.8	6	/1yrMom/
Anexo	ANX	149	172	7.6	1.0%	12%	49.4%	16.3%	8%	-40.9	6	/1yrMom/
Wilmington	WIL	240	210	14.2	2.5%	22%	18.4%	8.7%	5%	-54.0	6	>10% EPSgrth FY+2/
M.P. Evans Group PLC	MPE	830	454	13.0	3.3%	49%	216.5%	-26.3%	-1%	-32.3	6	>10% EPSgrth FY+2/
Next Fifteen Comm.	NFC	1200	1114	20.2	0.9%	25%	38.8%	4.8%	0%	-84.9	6	>10% EPSgrth FY+2/
HSS Hire	HSS	18	123	7.4	0.0%	751%	-	260.9%	-4%	-10.1	6	>10% EPSgrth FY+1/
Bank of Georgia	BGEO	1558	735	4.3	2.2%	26%	156.9%	6.6%	-3%	-	6	>10% EPSgrth FY+2/
SigmaRoc	SRC	92	587	13.8	0.0%	34%	20.4%	32.9%	-4%	-23.4	6	/1mthMom/
Epwin	EPWN	106	153	11.3	2.6%	22%	90.1%	22.8%	-5%	-65.9	6	/1yrMom/
Marlowe	MRL	910	872	19.5	0.0%	31%	47.8%	32.9%	-4%	-37.4	6	/1mthMom/
Hurricane Energy	HUR	5	99	2.5	0.0%	49%	-	200.0%	10%	68.3	6	>10% EPSgrth FY+1/
Record	REC	77	153	15.5	3.8%	11%	57.5%	18.1%	-2%	-	6	/6mthMom/
Tullow Oil	TLW	52	742	3.6	0.0%	383%	-	62.1%	14%	-2635.7	6	>10% EPSgrth FY+1/
Brickability	BRCK	101	302	10.9	2.0%	35%	47.5%	14.9%	-7%	-32.1	6	/3mthMom/
Marshalls	MSLH	691	1382	21.5	1.3%	12%	235.3%	11.6%	-5%	-53.5	6	/1yrMom/
Biffa	BIFF	356	1087	15.4	0.6%	31%	156.5%	19.5%	-9%	-317.0	6	/3mthMom/
Midwich	MIDW	600	532	19.8	1.1%	17%	127.0%	17.4%	-9%	-124.7	6	/3mthMom/

Source: FactSet, 11 February 2022

## US large-cap momentum shares (passing all 7 tests)

Name	Ticker (all US)	Share price \$ (last close)	Mkt cap (\$mn)	Fwd 12-mth PE	Trailing 12-mth DY	Next yr 12-mth EPS upgrade	Fwd EPS gwth cur FY	Fwd EPS gwth next FY	3-mth share price mom	Net cash (\$mn)	Tests passed (out of 7)	Tests failed	GICS sector
Mosaic	MOS	45.92	17402	6.2	0.5%	356%	494.3%	55.7%	27%	-2564.4	7	na	Materials
CF Industries	CF	73.76	15820	7.0	1.6%	530%	285.5%	99.4%	17%	-223.0	7	na	Materials
EOG Resources	EOG	112.66	65916	10.7	1.4%	163%	494.4%	22.6%	19%	-66.6	7	na	Energy
Diamondback Energy	FANG	130.42	23629	7.3	1.2%	135%	261.6%	63.5%	22%	-1128.0	7	na	Energy
Pioneer Natural Resources	PXD	222.12	54227	10.4	1.0%	123%	509.2%	69.6%	22%	-277.0	7	na	Energy
Halliburton	HAL	32.41	29123	17.8	0.6%	44%	62.9%	33.6%	36%	-1262.0	7	na	Energy
Hess Corporation	HES	92.4	28619	17.7	1.1%	111%	133.9%	19.3%	13%	-351.0	7	na	Energy
Schlumberger NV	SLB	39.17	54970	19.2	1.3%	30%	53.3%	33.4%	20%	-7220.0	7	na	Energy
Charles Schwab Corp.	SCHW	92.85	167939	23.6	0.8%	48%	17.8%	26.2%	15%	-	7	na	Financials
Signature Bank	SBNY	343.96	19821	17.1	0.7%	72%	29.6%	28.8%	9%	-	7	na	Financials
Marriott Int'l, Inc. Class A	MAR	174.68	56890	32.1	0.0%	25%	1518.1%	81.0%	9%	-4875.0	7	na	Consumer Dis.
Ameriprise Financial	AMP	315.9	35033	12.1	1.4%	23%	12.9%	15.3%	4%	-	7	na	Financials
Hilton Worldwide	HLT	154.2	42979	36.3	0.0%	15%	2048.6%	90.5%	5%	832.0	7	na	Consumer Dis.
Juniper Networks	JNPR	34.56	11238	17.2	2.3%	14%	13.9%	12.9%	9%	-638.5	7	na	Information Tech
Arthur J. Gallagher & Co.	AJG	158.81	33105	25.8	1.2%	19%	10.8%	13.3%	-1%	-	7	na	Financials
ONEOK	OKE	63.02	28103	16.5	5.9%	23%	140.2%	11.1%	0%	-820.1	7	na	Energy
Bank of New York Mellon Corp.	BK	63.47	52415	13.0	2.0%	11%	15.0%	21.2%	7%	-	7	na	Financials
State Street Corp.	STT	101.39	37107	11.6	2.2%	13%	14.5%	22.5%	4%	-	7	na	Financials
Hartford Fin. Services	HIG	72.96	24832	10.5	2.0%	15%	11.0%	16.3%	1%	-	7	na	Financials
IQVIA	IQV	250.43	47842	24.4	0.0%	11%	38.9%	13.5%	-1%	-2656.0	7	na	Health Care
Sealed Air Corp.	SEE	64.38	9538	15.4	1.1%	12%	11.7%	16.3%	1%	-818.7	7	na	Materials

Source: FactSet, 11 February 2022

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