



## Factor/Style Investing

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### The Interaction of Value and Momentum Strategies

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Researchers have convincingly demonstrated that value strategies can be used to predict stock returns. For instance, Fama and French showed as much for value strategies based on the ratio of a firm's book value to the market value of its equity. Similarly, Lakonishok, Shleifer and Vishny did the same for value strategies based on a firm's cash-flow-to-price ratio.

Although conflicting explanations have been offered for the success of these strategies, the empirical evidence that they have worked is quite strong.

Researchers have also convincingly demonstrated that momentum strategies have power to predict stock returns. For instance, Jegadeesh and Titman showed that strategies that buy winners and sell losers based on returns over the previous 6 to 12 months generate excess returns. Asness showed that these strategies are effective even after accounting for common value measures. In particular, they are most effective when the definition of momentum excludes returns over the most recent month.

The evidence that momentum strategies work is convincing. As with the value strategies, however, the explanation of why they work is largely incomplete.

For this study, we examined whether value and momentum strategies are independent or related, asking how well value strategies work among stocks that have exhibited both strong momentum (winners) and weak momentum (losers). Similarly, we looked at momentum strategies among only high-value (cheap) or only low-value (expensive) stocks. We found that value works, in general, but that it is particularly strong among loser stocks and quite weak among winner stocks. Momentum also works, in general, but is particularly strong among expensive stocks.

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