Timing the market in specific industries delivers for hedge fund managers

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Hedge fund mangers who time the market ahead of positive and negative news within the manufacturing industry outperform competitors,

research from FIU Business finds.

The study found that timing the market ahead of positive and negative news within specific industries, versus overall market timing, pays off for skilled hedge fund managers —and, ultimately, their investors. The manufacturing sector, specifically, delivered superior industry-specific results.

"As a hedge fund manager, if I'm aware of companies' earnings announcements, it's easier to forecast the future, and I can take positions before earnings come out," said study co-author Mustafa Caglayan, associate professor of finance at FIU Business. "If I do it consistently, I end up with higher returns."

Investors can redeem those higher returns by investing in the best industry-timing hedge funds, he added.

Researchers examined 11,040 hedge funds across 12 industries—including telecommunications, retail, energy, business equipment and durable, as well as non-durable, consumer products —testing if they had the ability to time industry-specific returns and whether this could predict the variation in future returns.

The manufacturing industry was consistently the top performer.

In addition to generating higher returns, the best manufacturing industry-timing hedge funds experience larger inflows of capital and as a result have a higher chance of survival in the following six-to-12-month period. These have the highest return sensitivity to earnings surprises, indicating that fund managers should pay close attention to earnings news in the sector.

"It's easier to forecast earnings surprises and business cycle indicators

for companies in the industry because they are more likely to be persistently in the same earnings direction and maintain similar results over the following months," said Caglayan.

By contrast, researchers didn't find evidence of a positive link between manufacturing industry timing and mutual funds' future performance.

"Hedge funds can move quickly," said Caglayan. "They aren't heavily regulated, don't have concentration requirements and have more flexibility in their portfolio holdings and investment strategies, including the use of short-sell."

Provided by Florida International University

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