A New Anomaly: The Cross-Sectional Profitability of Technical Analysis

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Abstract

The paper applies a moving average strategy of technical analysis to portfolios sorted by volatility. It finds that the investment timing portfolios based on the moving average strategy outperform the buy-and-hold strategy substantially. For high volatility portfolios, the abnormal returns, relative to the CAPM and the Fama-French three-factor models, are high, and higher than those from the well-known momentum strategy. The abnormal returns remain high even after accounting for transaction costs. Although both the moving average and the momentum strategies are trend-following methods, their performances are surprisingly uncorrelated and behave different over the business cycles, and has different exposures over default and liquidity risk.