Systematic Equity Switzerland

Introduction – Factor investing to enhance return

Leading academic studies have found that it is possible to identify distinct factors which can systematically generate higher risk-adjusted returns. Based on economic theories these factors are also expected to be profitable in the future. The return anomalies are explained by a semi-efficient reaction to news which respectively causes an over- or under-reaction to the information.

The sources of outperformance are called factors and can be referred to styles such as value, momentum, growth or quality. Strategic allocation towards such factors is called factor investing.

Factor investing is based on a rational investment and has come into the spotlight by a new dynamic from index providers often titled as “smart-beta” investments.

Rational for multi-factor approaches

Successful active equity strategies can often be explained by exposures to a set of well-documented factors. After taking these factor exposures into account, active returns can eventually be explained entirely. This has led to the construction of single factor-indices (size, value, quality, dividend, etc.).

But even if the factors to which these indices are exposed to are well rewarded in the long run, they often encounter prolonged periods of underperformance. Hence the reward of exposure to individual factors has been shown to vary over time.

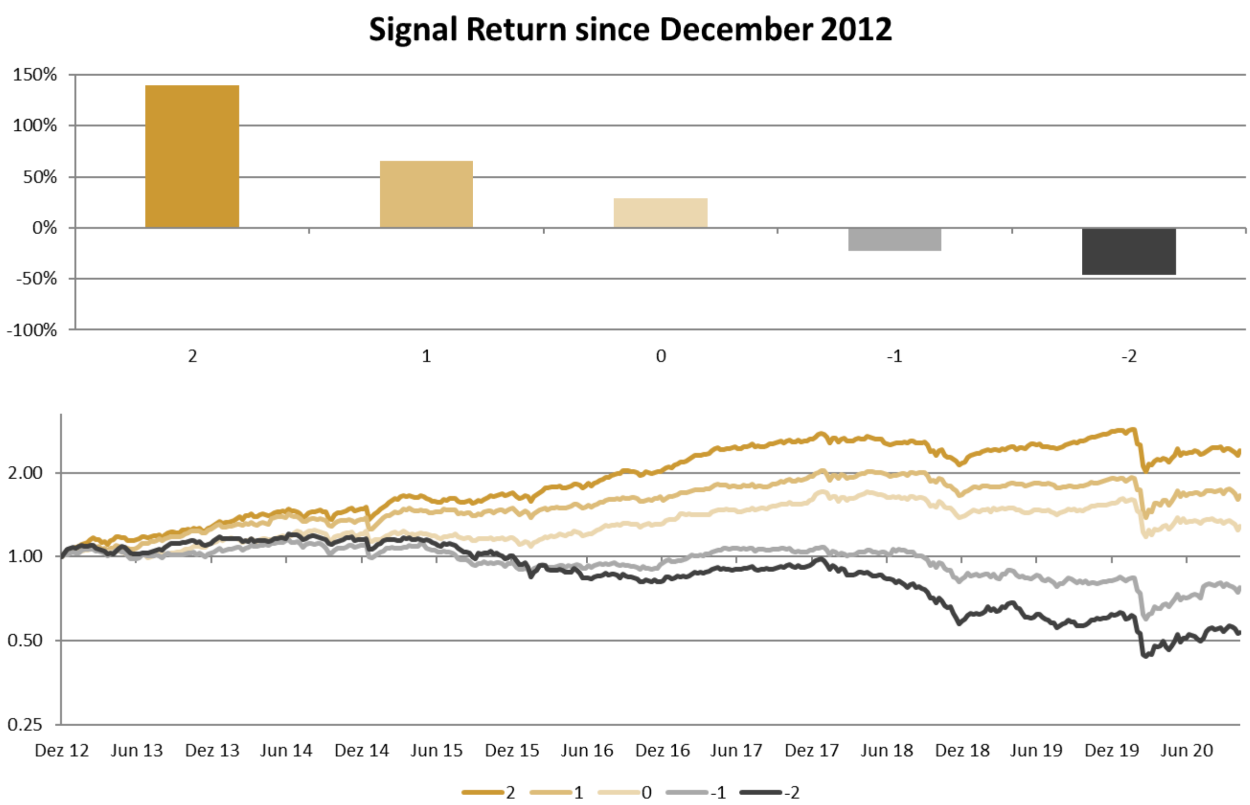
Assuming that the returns of distinct factors are not correlated, allocation across distinct factors permits to diversify the sources of outperformance thus smoothing their performance across market cycles.

In addition investors gain due to allocations being made across factors in terms of implementation as certain transactions can be eliminated or reduced through crossing effects.

Multi-Factor Investing in Swiss Equities

A multi-factor approach was developed in 2006 and enhanced in 2012 for the Swiss equity market, with the aim of benefitting from well documented factor premia.

The stock selection algorithm rests on a combination of distinct factors, which can identify temporary market imbalances. The correlation between the imbalances and the factors are historically analysed and verified.

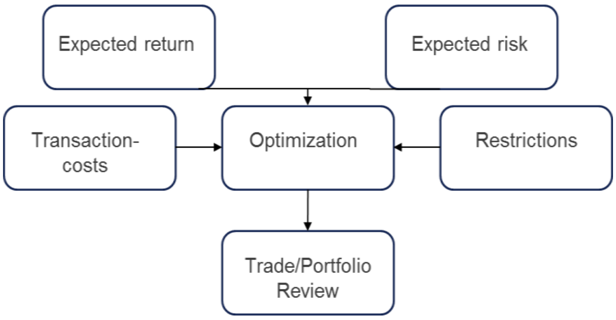


The Graph shows the cumulative return and the indexed development of equities according to their respective scores. All calculations and scores are based on out-of-sample data from December 2012 until October 2020.

Systematic and risk-controlled implementation

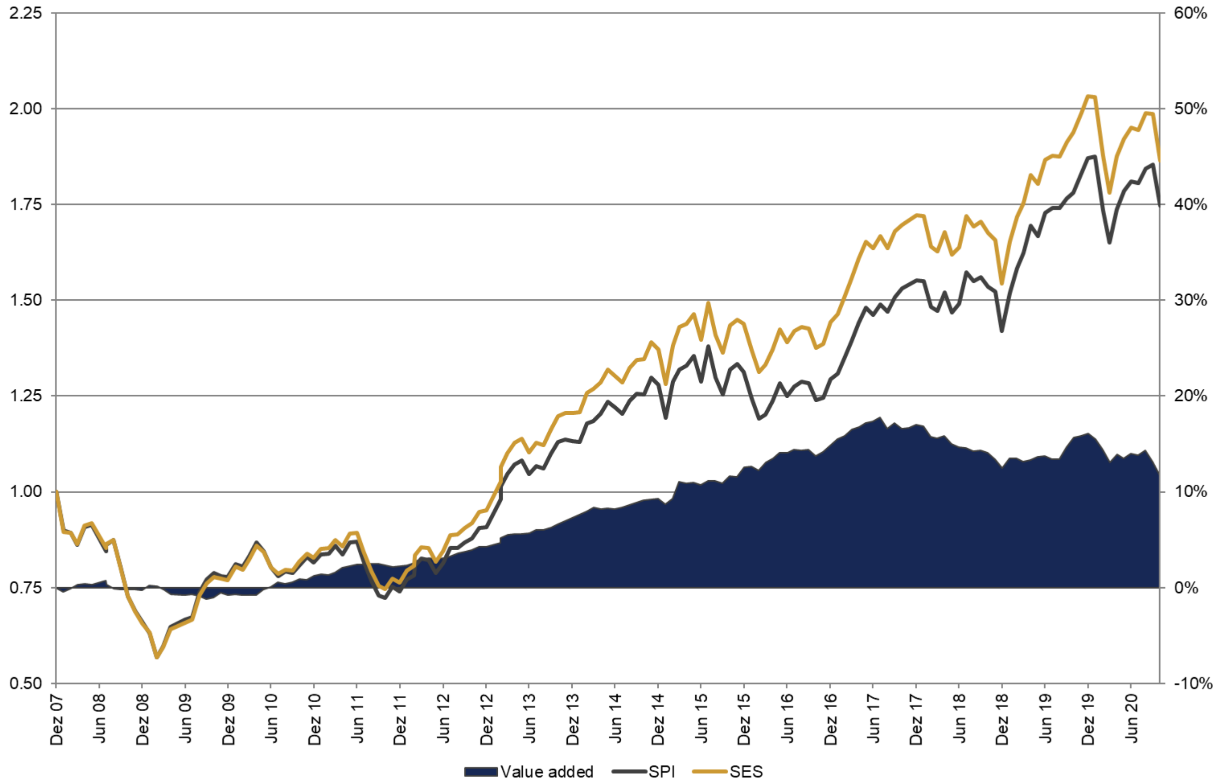
Systematic Equity Switzerland benefits from exposures to different factors, without changing the risk profile.
To construct portfolios a risk model is used, which takes the following factors into account:

- the expected return
- the expected risk
- the transaction costs
- and the liquidity.



Performance record

Since its successful implementation, via a stratified sampling, the „Systematic Equity Switzerland" strategy has achieved performances within expectations:



The Graph shows the cumulative return and excess return of the strategy since implementation after all transaction costs, before fixed fees.

Optimum between active and passive concepts

The systematic, risk-controlled strategy of Systematic Equity Switzerland aims to represent an optimum between active and passive concepts.

The risk-return-profile of a passive strategy can be improved through an elaborate systematic as well as a stringent risk control.

In the case of Systematic Equity Switzerland this is achieved through an optimized risk replication of the index and an active stock selection based on a multi-factor approach, which deviates from the strict replication of the index. Considering various factors, a risk-optimized portfolio is constructed, which generates higher expected returns with the same expected risks as the index.

Summary

AlphaStream has developed a multi-factor approach for the Swiss equity market, with the aim of consistently assigning scores to each individual company within the universe.

The approach is based on well documented factor premia that can be referred to styles such as value, momentum, growth or quality.

The selection algorithm rests on a combination of distinct factors, which if combined efficiently have shown to systematically generate higher risk-adjusted returns.

The intention of AlphaStream-Score is to provide an objective view based on a rigorous methodology which:

- enables investors to quickly asses a company’s category
- might help generate new investment ideas
- makes it easier to evaluate current positions

The scores are based on academic theories and empirical evidence and have been implemented successfully for more than ten years.

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