ORS Case Study
External Alpha
Alternative Alphas

powered by SherpaFunds Technology

ALTERNATIVE ALPHA SOURCES:

THREE SOURCES OF ADDED ALPHA THAT CAN COMPLEMENT TRADITIONAL FUNDAMENTAL ANALYSIS IN ASSET MANAGEMENT

1. (BIG) DATA

RAW DATA THAT TRACKS ECONOMIC OR SOCIAL ACTIVITY OR RESOURCES

2. INTELLIGENCE-ADDED DATA

CURATED, EDITED AND 'INFERRED' OPINIONS BASED ON DATA. INTELLIGENCE ADDED BY NON ASSET-MANAGEMENT EXPERTS WHO COVER TO ASPECTS OF ECONOMIC OR SOCIAL ACTIVITY.

3. SPEED-RELATED, SEEING TRADING SIGNALS FIRST

TECH DRIVEN SIGNALS BASED ON BETTER CONNECTIVITY

High capital cost, arms race, not considered any further here

Applying Data Sources to Asset Management, Confidence, Risk and Process

Challenge

- How to get confident that the data-driven inferences (which translate into risk positions) will work?

- With traditional alpha, a CIO can quiz the PMs & analysts about opinions and generate a qualitative confidence around any single idea
  - ‘soft point-confidence’ that says “this analysis is ‘right- enough’ to justify taking a position”

- With data-driven signals, this must be replaced with a more rigorous approach which gives broad confidence about a portfolio of ideas, not narrow confidence on any single idea
  - a ‘hard statistical-confidence’ about the risks that you are taking in the portfolio

Solution, the rigorous approach

- Use Sherpa’s ORS process. It gives you ‘*more of the risk you want and less of the risk you don’t want*’. You define what risk you want in the portfolio.
- The ORS process **manages risk ex-ante** to match risks with business objectives & constraints whilst capturing the value in the Alternative Alpha source

(Big) Data

- There are more & more Data sources, (remote sensing, retail PoS & comms tracking)
- Typically designed for purposes other than Asset Management
  - Consumer/promotion/marketing analytics
- Drawing market-tradeable inferences from these un-curated large data sets is tough
  - Use A.I. (really regression, PCA, optimisation, same tech as ORS)
  - Caveat: Data has to be pre-screened/cleaned/ matched up/ combined
    - Q: is that correct approach on non-standardised data sets
    - Q: are underlying data methods coherent? Expertise on the subject matter?
- Big Data is generally available, not unique to you
  - So your analysis has to be unique
- Data likely to get cheaper, but less relevant and more noisy (impact of regulations)
- Data vendors not keen to be pinned down to exclusivity
  - Add something to their product, to get better access (?)

BIG DATA II

- Providers of Big Data:
  - Large players here: Nielsen, IRI, various ad-tech co's
  - Niche players who have the data but aren't selling it (yet)

- Contrast: Quant driven portfolios based on Financial data vs. based on other 'Big' data:
  - Financial data: we have a well-understood model for translating a higher P/E ratio into a stock price expectation
  - Non-Financial data: we don't have that model

- Big Data is hard to mine for Alpha Generation ideas (open questions)
  - I have no thesis, I am looking for a pattern
    - Hard Q: What is the new trend in fashion? How will that impact store sales?
- But easy to query for thesis verification (closed questions)
  - My thesis is that people are buying more red than blue & this will lead to a performance uptick in red dye makers
    - Easy Q: Are people buying more Red than Blue?

INTELLIGENCE

- 2 types of 'Expertise' that has collected and analysed data & has drawn inferences

1. Financial targeted intelligence (External Financial Analyst)

        - Sometimes 'free' (broadcast data from sell-side analysts)
        - Sometimes subscribed data from a provider (MIFID driven)

    - Directly market relevant
    - Hard to understand the process in many cases

        - Makes it hard to have long term confidence

2. Industrial targeted intelligence

        - Specialised Management Consulting intelligence
        - Aimed at specific users, non-leveraged, constrained by real world time effects

INTELLIGENCE II

2. Industrial targeted intelligence contd.

   - Analysis performed for fee usually to answer specific Qs with sector expertise
   - The original client reports are confidential
   - But sensitivity models and market/regulatory impacts are available
   - Models calibrated to real client data, makes them better than Financial Analysts

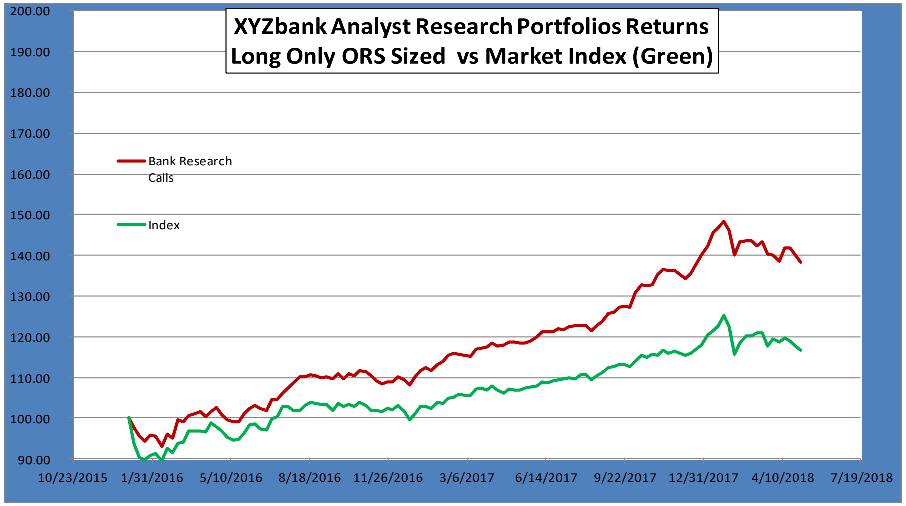
- Repeatability, needs data gathering to be robust/central to the expert thesis
  - It should be a real consulting firm, not one man & a dog!
- Application: needs Markets-Analyst Qs to create asset scores & see value in the intelligence
  - So it's an Active Engagement with the Consultancy
  - Analysts take themes and ask Q's
  - Consultants' answers used in Analyst Scoring models

INTELLIGENCE EXAMPLES

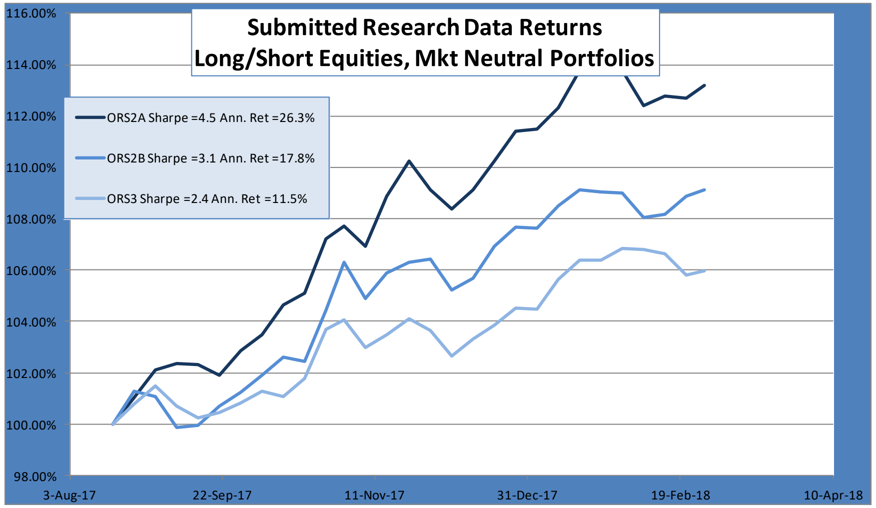
- Financial Intelligence
  - Easy to source, but hard to get confidence
  - How to get confidence on other peoples analysis?
    - Treat data as statistically valid, not ‘point’ valid
    - Add ex-ante risk management (ORS) to mitigate unwanted risks

- 2 examples below:

‘Ignored’ Sell-Side Analysts’ Calls



Polled Analyst Calls



You never know which call is right/wrong, so you build an ex-ante risk-managed portfolio of calls

INDUSTRIAL INTELLIGENCE SOURCE REAL WORLD EXAMPLES

1. Healthcare Consultancy
   - Deep knowledge of Regulatory, Scientific and Commercial aspects of healthcare
   - Example: A project uncovers that new regulatory uncertainty is appearing
   - Analyst Q's lead to inference that other companies are very exposed to this & stock prices will drop. As the uncertainty gets resolved the prices will rise.

2. Industrial Supply Chain Consultancy
   - Deep knowledge of true costs of businesses and their supply chains
   - Commissioned to improve purchasing, leads to very accurate models of costs
   - Example: Consultancy builds /calibrates models to show true cost impact of moving a supplier to regional from global
   - Analyst Q's point out that same model shows Brexit means most UK retail will struggle to cope with GBP devaluation

- In neither case was identifying stock movers the original project. The consultancies calibrate their models to fulfil the project which allows Fund Analysts to ask deeper Q's.
- Gain risk confidence: use portfolio construction process to remove unwanted risks.

OVERALL

- Alternative Alpha Sources exist & have value
- Select the opportunity set on which to apply the Alpha to maximise
  - Liquidity
  - Dispersion
  - Story
- Industrial alpha is priced for industrial consumption, not leveraged use, so is useful
- Financial alpha is sometime overlooked or mispriced (free)
- Combining internal analyst Qs with external expertise leads to a repeatable, scalable, unique set of Alpha
- Statistical techniques, like the ORS process for portfolio construction, allow you to have less conviction in any given position
- Ex-ante risk-management is essential to get equivalent confidence in a portfolio relative to your internal alpha, and to avoid unwanted risks

SUMMARY: TYPES OF DATA AND STRATEGIES TO USE IT

	Raw (Big) Data	Intelligence-Added Data
Rare	Build your own Sensor/ data capture engine Lock in a supplier through adding value Monetise quickly before your tech is overtaken Apply with ex-ante risk management	Select Intelligence provider (Consultant) with process & models that are used to answer different (non stock-price) Q's. Markets analysts then perform markets focused Q&A Apply with ex-ante risk management
Widely Avail-able	To create Alpha: You need a better analysis engine, or understanding of the data protocols, to get unique Alpha from the data. To verify a Thesis: much easier to ask 'closed' Q's of this data: is this really happening in the real world?	Standard published Financial Research Question the longevity Cheap, and often overlooked Apply with ex-ante risk management

Let us Show you how Sherpa can Help Your Portfolio

Contact the Sherpa team below and let us…

- Share how funds like yours use ORS to maximize returns from alternative Alphas

- Go into more detail on the ORS philosophy and methodology

- Demonstrate how the ORS process can help you on a Portfolio of your own data

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