Active Large-Cap Equity

Creating a Superior Sector Strategy

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What is Right Way to Evaluate Sectors?

- **Individual** performance?
  - *"Rank" by performance statistics (i.e. Sharpe Ratio, etc.)*

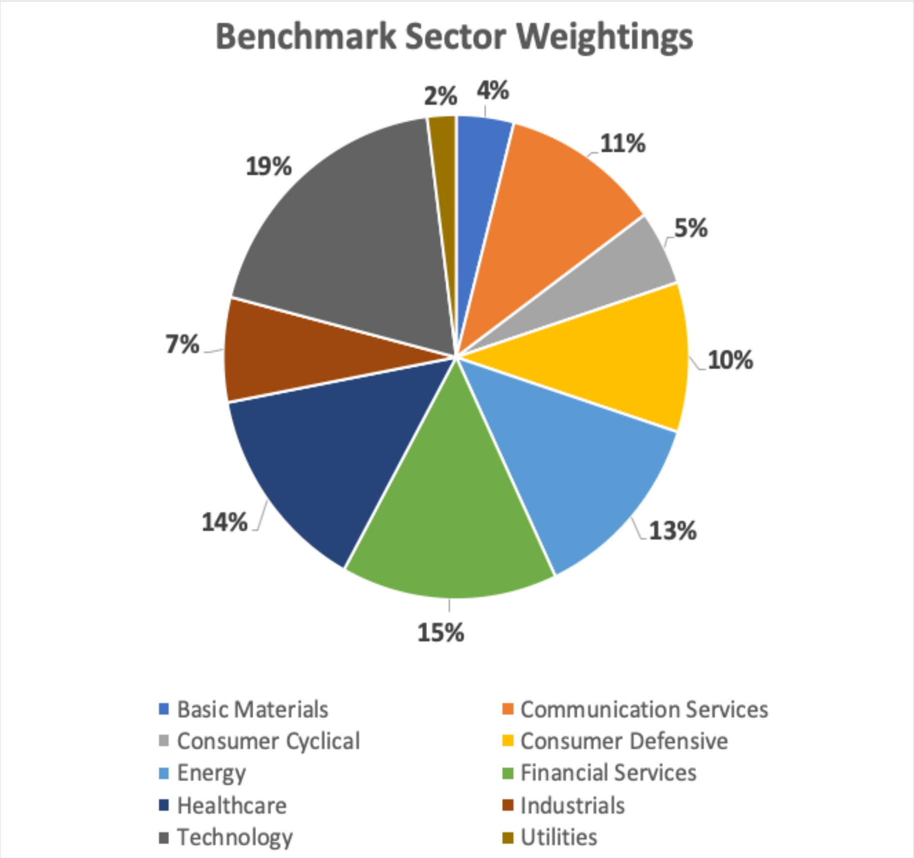
Or…

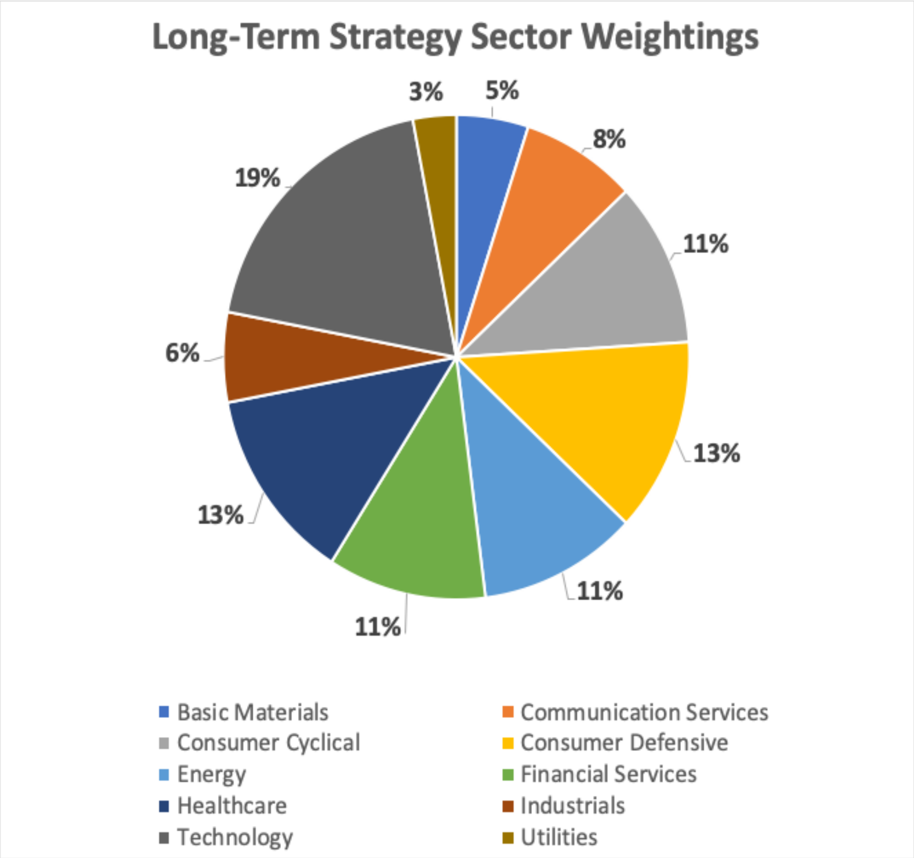
- How they contribute to the **portfolio**?
  - *Balanced contribution to return and risk?*
  - *Any "weak links?"*

Key Insight:

It's all about the CONTEXT in which you measure risk

Compare Benchmark and Portfolio

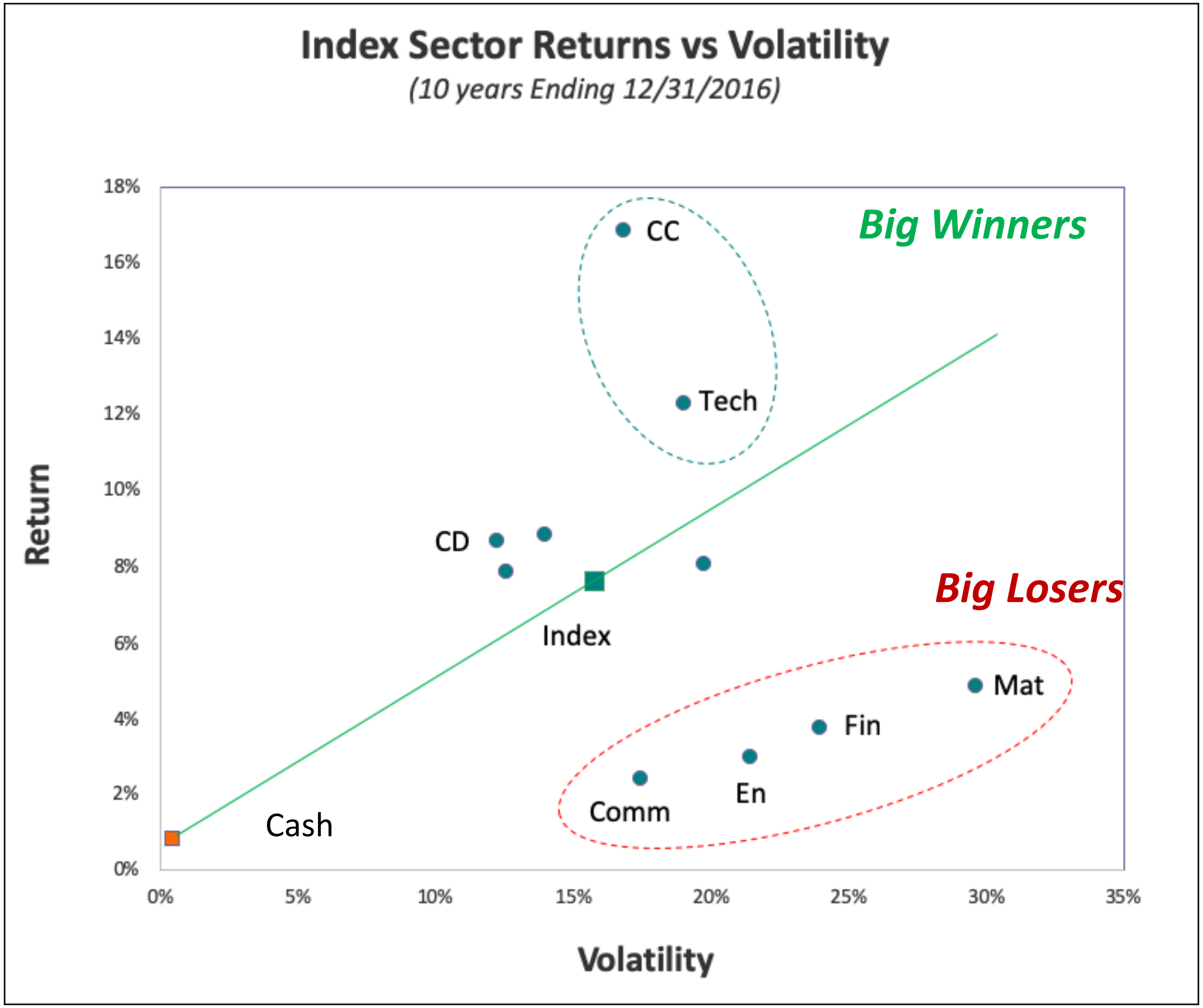




Strategic Portfolio Sector Weightings:

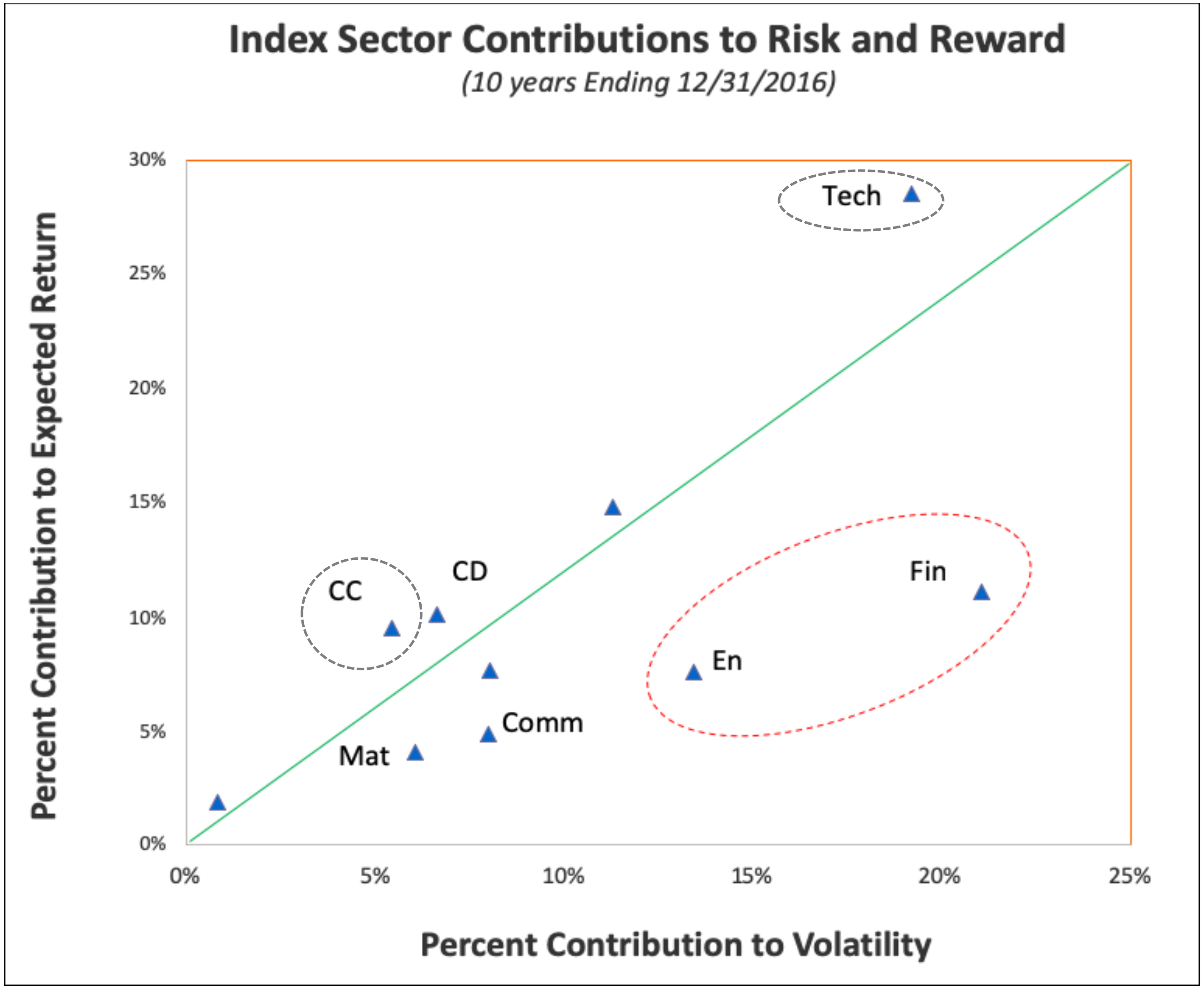
- *Permanent bias relative to index*
- *"Modest but Meaningful" active weights*

Traditional View of Sectors:
In Isolation



Really?

Holistic View of Sectors:
Within Portfolio

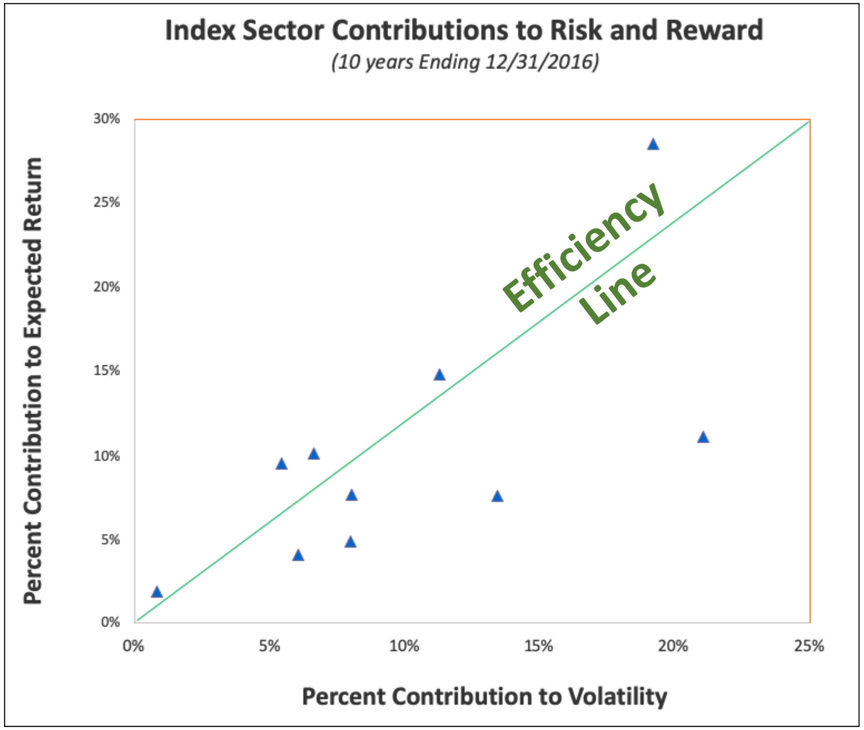


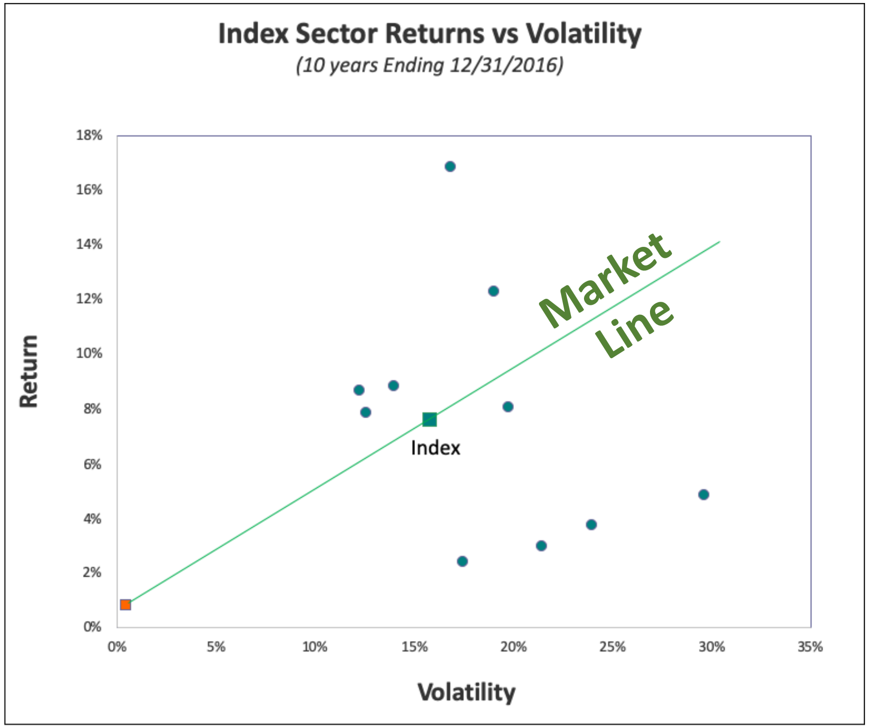
2 Losers
Not 4…

CC and Tech
Switch ranking

Portfolio View vs Isolation View

Measure Risk in the proper Context





<u>Insights and Decisions</u>

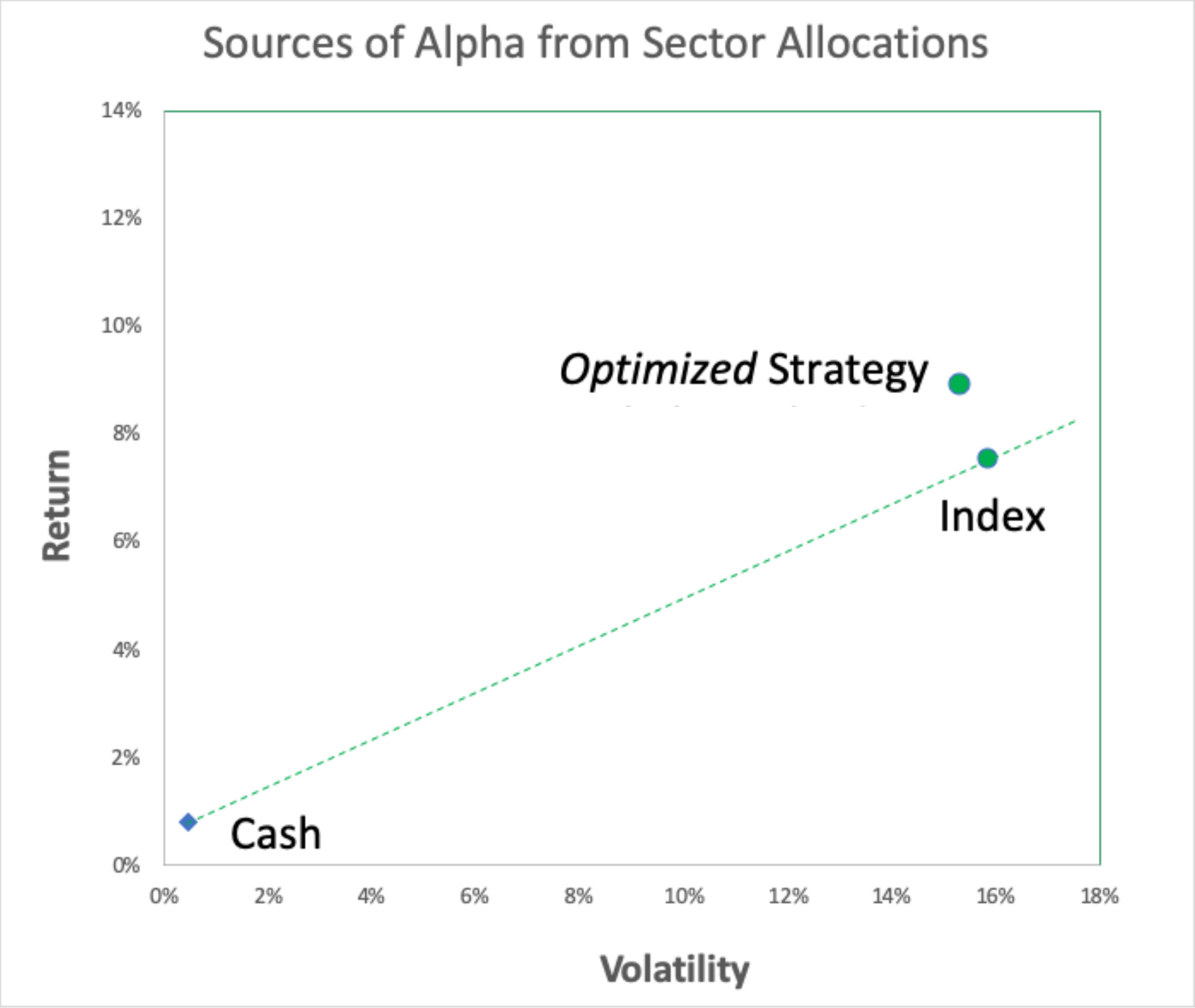
- *What contributed to success?*
- *Where are opportunities for improvement?*

Focus on Sector Correlations

(This is ignored in Indexes)

Sector Correlations	**Average**	**Index Weighting**	**Strategy Weighting**	
Basic Materials	**0.63**	4%	5%	
Communication Services	**0.66**	11%	8%	
Consumer Cyclical	**0.68**	5%	11%	
Consumer Defensive	**0.66**	10%	13%	
Energy	**0.64**	13%	11%	
Financial Services	**0.72**	**15%**	**11%**	*Key Underweight*
Healthcare	**0.66**	14%	13%	
Industrials	**0.73**	**7%**	**6%**	*Key Underweight*
Technology	**0.68**	19%	19%	
Utilities	**0.49**	**2%**	**3%**	*Key Overweight*

Benefits of Strategic Sector Strategy



Validates fact:
Cap-weighted
indexes are
inefficient

Evaluate Active Results

Decide on Market Risk

Investment Decisions	Total Return	Volatility
Cash	0.80%	0.46%
Benchmark	7.55%	15.82%
Strategy	8.93%	15.29%

Exploit Benchmark Inefficiency

- Excess return from Strategic Sector Allocations: **138 bps**
- Contribution to Portfolio Tracking Error : **35 bps**
- Information Ratio of Sector Allocation Decision: **3.94**
  (Astoundingly High)

Strategic Portfolio Sector Weightings:

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Want to Generate Alpha via Portfolio Efficiency?

We can help!

Please contact us for a consultation

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