BSAMC

Bocconi Students Asset Management Club

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LONG-SHORT FUND

Adham Touny	TEAM LEADER
Anthony Smelansky	ANALYST
Ayman Rabdi	ANALYST
Leonardo Bambagioni	ANALYST
Samantha Boucher	ANALYST

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Introduction

The Long-Short Fund was launched in September 2023 and takes an active and innovative approach to managing investments. This report outlines the fund's recent activities and strategic updates, emphasizing its goal of achieving higher risk-adjusted returns while staying dedicated to ethical and sustainable investing.

Additionally, the goal of this report is to summarize the performance of the fund as well as the changes made to reach a higher performance, alongside an analysis of the current macroeconomic environment.

Fund Definition

The main objective of the Long-Short Fund is to obtain higher risk-adjusted returns through a strategy of going long on undervalued securities and short on overvalued ones. The fund targets a 60:40 allocation between long and short positions, respectively. This two-sided approach allows the fund to profit from both upward and downward market movements, taking advantage of inefficiencies in the equity market.

The Long-Short Fund invests primarily in equity markets across developed regions, focusing on industries and companies that show strong growth potential, financial stability, or mispricing opportunities. It follows a thorough selection process to balance the weight of long and short positions, diversifying the portfolio across sectors and geographies such as technology, consumer discretionary, biotechnology, and energy.

The benchmark taken for this fund is the AQR Long-Short Equity Fund. This benchmark was taken because it aligns with the fund's strategic focus on market inefficiencies and delivering absolute return. The AQR Long-Short Equity Fund represents an established and respected industry standard. Therefore, it forms a robust framework for performance evaluation.

Consequently, and in conformity with the dedication of Bocconi Student Asset Management Club to responsible investing, our fund follows rigid ESG criteria. We as a team screen our investments in order to exclude companies engaged in unethical practices. It thereby reflects adherence to principles guiding sustainable, socially responsible investing of its management. To qualify for inclusion in the portfolio, companies must achieve a minimum ESG score of 55/100 according to FactSet. This approach testifies our dedication to ethical portfolio management while making profitable investments.

Portfolio Performance

The fund has shown a strong performance over the reported period, from October 2023 to the present. During this semester we were able to significantly outperform our benchmark index (i.e., AQR Long-Short Equity Fund), achieving a total return of 8.94% compared to 5.57% of the benchmark. The performance of our fund and our benchmark is displayed in the graph below.

Our best performing long positions were 3M (32.8%) and Lockheed Martin (30.08%). 3M saw strong growth due to positive earnings reports, growth in healthcare and safety segments, and strategic restructuring efforts. On the other hand, Lockheed Martin benefited from increased defense spending globally and a increase in demand for military systems. This stock was already part of our portfolio, but due to the new ESG requirement of the fund, this stock has been sold with a large profit.

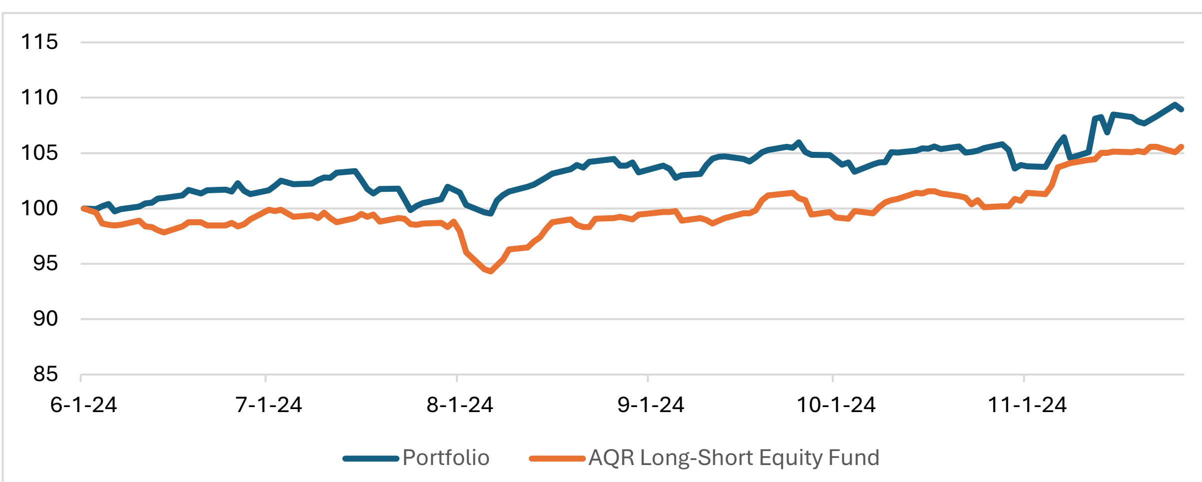
Our best performing short positions were Spirit Airlines (60%) and Beyond Meat (17.1%). Spirit Airlines declined significantly due to rising fuel prices, operational challenges, but most importantly due to the collapse of its merger talks with JetBlue. Beyond Meat's stock fell as competition in the plant-based market grew and demand for its products weakened.

Our worst performing position was Bristol-Myers Squibb Co (-41.9%), which was a short position. The main reason is that the company reported better-than-expected earnings, positive pipeline news, and FDA approvals.

Macroeconomic Analysis

When looking at the macro environment in the second half of 2024, it is evident that many economic changes have changed the market landscape and directly affect the management decisions made for the Long-Short Fund.

As the fund invests focuses on U.S. equities, this macro analysis will focus on the U.S.



Evolution of $100 invested from June 1 to November 26

Monetary Policy: Interest Rates and Inflation

Q3 and Q4 of 2024 have shown the Federal Reserve's long-anticipated interest rate cuts finally coming into action. An initial cut of 50 basis points, followed by another 25 basis point cut brought the base rate in the US to 4.58%. As inflation nears the Fed's target of 2%, investors are pricing in even greater rate cuts for 2025 and these positive expectations are fueling US equity markets.

Political Climate

The most relevant political development in the US has been the recent re-election of Donald Trump. His presidency will bring a completely new wave of economic policies. His administration is pushing for significant tax cuts and deregulation, aiming to stimulate business investment and economic growth. However, these measures have sparked debates about potential inflationary pressures and the long-term impact on the federal deficit. This is especially evident in his protectionist plans that seem to have the potential to easily spiral into full-on trade wars with the likes of China and even some European countries.

Economic Growth and Labor Market

According to projections, the U.S. economy will expand by 2.7% this year and by 2% in 2025 and 2026. With unemployment rates close to all-time lows, the labor market is nevertheless robust. But in several industries, there are worries about a lack of workers. Although it is anticipated that tax cuts and deregulation will increase company investment, some of these benefits may be countered by the possibility of greater inflation.

Financial Markets

Financial markets have experienced a volatile environment in response to the changing economic policies but have maintained their upward trajectory. The stock market has shown resilience. With inflation nearing the Fed's 2% target and interest rates still relatively high, investors are pricing in multiple rate cuts in 2025 and this prospect of cheaper borrowing is fueling the equity market. In addition, the expanding artificial intelligence industry has been acting as rocket fuel for US equity markets. Big tech, particularly Nvidia, has had a breakout year and continues to push their valuations higher and higher. However, a big question remains: Will AI really meet the sky-high expectations placed on it?

Portfolio Updates

Over the semester, the fund refocused on individual equities primarily in tech and biotechnology as well as meeting ESG criteria, closing out positions on Vanguard Total Bond Market Index Fund Admiral Shares (VBTLX) and iShares Core U.S. Aggregate Bond ETF (AGG) to achieve full equity composition. The fund also closed its position on Gold Futures (GC=F) due to macroeconomic conditions driving lowered inflation, having already reaped 50% returns on the position. To meet ESG requirements, the fund sold its share in Lockheed Martin (LMT). Finally, the fund closed its long position on Kraft Heinz (KHC) despite its positive dividend yield due to its discontinuation of Lunchables and lawsuits likely to continue its downwards price trend.

The fund also closed positions in Ebay (EBAY), Hasbro (HAS), and Meta (META) due to low growth prospects and the funds existing overweight in technology. However, we increased its position on Microsoft (MSFT) due to promising strides in AI integration and predictive analytics.

Seeking fast returns and long-term growth, the fund prioritized stocks with immediate anticipated growth prospects and strong fundamentals. Our long positions were diversified across industries including tech, consumer discretionary, biotechnology, and energy.

Long Positions

ASML (ASML): Underlying value due to unique lithography technology that is highly in-demand with growth prospects aligned with AI. Due to double buy ratings, double digit year-on-year growth and dividend growth, ASML was a value buy however this growth is not yet realized.

Sirius XM (SIRI): A bounce-back pick heavily invested in by Berkshire Hathaway, which bought 5.2M shares in October. With market indications of growth and significant undervaluation, recent momentum was strong in ad revenues and podcast acquisitions. We decided on a lower position due to the unattractive leverage ratio and longer-term growth prospects.

Technogym (TGYM.MI): Listed on the MTA, Italian sports equipment manufacturer Technogym showed strong growth potential following its sponsorship of the Paris Olympics. Given its high valuation, we opted for a conservative position.

Palantir (PLTR): One of the biggest winners of the year, Palantir had a strong Q3 performance on EPS and revenues due to strong demand for its AI Platform and US election expectations given the US government is Palantir's largest client.

MercadoLibre (MELI): The Latin American e-commerce and fintech platform experienced tailwinds from network effects and a growing ad business, creating a strong market position amidst geopolitical instability to justify its valuation.

GE Verona (GEV): As a spinoff of parent GE Electric, GE Verona manufactures electric power equipment for nearly 25% of the world's electricity, with nuclear power products heavily invested in by growing AI and big tech customers. With low debt, 7% expected growth, and a backlog driving guaranteed revenues, GE Verona is a steady growth pick.

Uber (UBER): We invested in Uber as a momentum play with growth likely to continue as Uber focuses on high-margin diversified products across Uber One, enterprise, and healthcare offerings. Strong margins, cash flows, market capitalization and relatively good debt make Uber a strong pick.

Short Positions

Beyond Meat (BYND): Poor performance in the past year, high debt, and high competition in the plant-based meat substitutes industry drove our rationale to short Beyond Meat. The company's financials provide a limited runway with no free cash flows, high inventory, and limited market share to grow.

Nikola Corporation (NKLA): Nikola reported disappointing cash burn rates, revenues, EBITDA, and EPS in the third quarter despite increased sales. With outstanding recalled vehicles and an inflated valuation, investment firms dropped their price targets and shareholders are unhappy with dilution concerns.

Spirit Airlines (SAVE): The fund opened its short position in SAVE amidst rising costs, merger turmoil, and lawsuits prior to Spirit declaring bankruptcy. We closed the position shortly after to maximize profits and shift the fund's focus to more active sectors.

Risk Analysis

Diversification Analysis

Industry Exposure

Our portfolio, including only currently open positions, reflects a strategic approach that balances conviction in high-growth sectors with a nuanced understanding of industry-specific dynamics. The significant exposure to Tech and Retail highlights our confidence in their strong growth potential, driven by innovation in technology and resilient consumer demand. These sectors were identified as key drivers of performance, and our long positions are positioned to capitalize on these opportunities.

Our strategy in Pharma, with both long and short positions, showcases a thoughtful and differentiated approach. While the long positions focus on companies with strong pipelines and solid fundamentals, the short positions hedge against firms facing challenges such as regulatory pressures or weaker growth prospects. This dual exposure demonstrates our ability to navigate the complexities within the sector and adapt to varying market conditions.

The high short exposure in the Food sector reflects a strategic expectation of underperformance, likely driven by challenges such as evolving consumer trends, cost pressures, or industry-specific headwinds.

A complete overview of our industry exposure by long and short positions is illustrated in the graph below.

Diversification Ratio and Volatility

The portfolio's current volatility of 50.17% indicates a relatively high level of risk, reflecting exposure to volatile assets or potential leverage in the positions. However, with a diversification ratio of 1.41, the portfolio demonstrates a moderate level of diversification, suggesting that the asset allocation effectively reduces some of the inherent risks through low correlations among holdings. While this level of diversification helps mitigate risk, it also highlights the potential to further enhance the portfolio's risk-adjusted returns by refining the asset mix and seeking additional uncorrelated opportunities. This analysis underlines the importance of continuously evaluating and optimizing the portfolio's composition to achieve a more efficient balance between risk and return.

Risk Metrics

The portfolio's metrics provide a comprehensive insight into the effectiveness of the strategy implemented. With a beta of 0.1736, the portfolio demonstrates low sensitivity to the benchmark, reflecting a deliberate approach to minimize market-related risks and focus on uncorrelated assets. This aligns with the strategic goal of reducing dependence on broader market movements while emphasizing stability.

The daily and annual variance of portfolio returns, measured at 0.0034% and 0.8652%, indicates low return variability, showcasing the stability achieved through careful diversification and a measured allocation to less volatile assets. The annualized Sharpe ratio of 1.40 underscores the strategy's potential to deliver improved performance over the long term, indicating consistent returns relative to risk when viewed from a broader perspective.

The Treynor ratio of 0.00297 and its annualized counterpart of 0.747 illustrate that the portfolio delivers moderate excess returns per unit of market risk. These figures align with the portfolio's low beta and further validate the strategy's focus on controlled market exposure. Meanwhile, the maximum drawdown of -3.72% highlights strong downside risk management, ensuring limited losses even during adverse market conditions.

This analysis suggests that the portfolio strategy successfully achieves its objectives of maintaining stability, managing risks, and delivering moderate risk-adjusted returns. There is potential for optimization by increasing the Sharpe and Treynor ratios to enhance the overall efficiency of the portfolio.

Conclusion

The Long-Short Fund's performance during this reporting period has demonstrated a well-executed strategy marked by strong risk-adjusted returns, outperforming the AQR Long-Short Equity Fund benchmark. The team’s ability to identify high-growth opportunities in technology and biotechnology, while prudently managing underperforming sectors through short positions, underscores a deep understanding of market dynamics and macroeconomic influences. Notable achievements, such as securing substantial gains from 3M and Lockheed Martin and navigating the challenges posed by weaker positions like Bristol-Myers Squibb, reflect the fund's agility and robust decision-making.

Moving forward, the fund's commitment to ethical investing through ESG criteria, coupled with its diversification efforts and focus on low-beta strategies, positions it well to weather market volatility and capitalize on evolving trends like AI integration and shifts in monetary policy. While there is room for optimization in risk metrics and sector allocation, the portfolio's disciplined approach and consistent alignment with its strategic objectives lay a strong foundation for sustained growth and resilience in future market conditions.