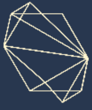


BSAMC

Bocconi Students Asset Management Club

FEBRUARY 2024

EQUITY AND FIXED INCOME FUND

ENNIO LAMARI – TEAM LEADER

CARLO VILLA

PETER IVANOV

ADHAM TOUNY

ELENA CAVALLARO

ETHAN LEVINE

LUDOVICA PERAZZI

Contents

Introduction 2
Fund Description 2
Investment Approach 2
Portfolio Allocation Breakdown 4
Performance 5
Risk management 7
Improvements for the future 8
Conclusion 8
Sources 9

Copyright © 2024 BSAMC | Bocconi Students Asset Management Club

BSAMC
Bocconi Students Asset Management Club

Introduction

The ***primary*** purpose of this report is to analyze the performance of our Equity & Fixed Income Fund over the months of October 2023 to January 2024. To do so, this memo will provide a description of the fund, our investment approach, and how funds have been allocated to reach such performance. The ***secondary*** purpose is to provide improvements for the future using our performance analysis.

Fund Description

As its name indicates, this fund exclusively invests in fixed income securities (debt instruments that pay a fixed rate of interest) and equity (shares). To do so, our team uses Ziggma, a portfolio simulator that allows for the evaluation of trade impacts on portfolio diversification, risk, and yield. It is worth noting that due to the platform's limitations, the fund invests exclusively in Bond ETFs for FI securities and more generally only in US securities assets. Yahoo Finance is also used to make the track of performance easier. In terms of target return, the fund aims to achieve a 9.5% annualized return. This target has been chosen following the establishment of an 80/20 allocation strategy for this particular fund. That is, this fund should aim to be made of 80% of equity and 20% of fixed income securities.

Investment Approach

The last months of 2023 marked a significant phase in the stock market, characterized by a robust performance and a series of critical events that shaped its trajectory. The S&P 500 index showcased a notable trend of growth and fluctuations, influenced by various economic, political, and technological factors. Starting the year at 3892 points, the index experienced a series of ups and downs, reflecting the dynamic nature of the market. Key events later led to the index hitting a high of 4707 points by mid-December.

The market's performance was underpinned by several underlying factors. A key driver was the deceleration in inflation, with developed world inflation dropping from 7-7.5% to 3-3.5%. This reduction, coupled with a decrease in energy prices eased inflationary pressures, contributing to market optimism. Furthermore, the performance of mega-cap tech companies, particularly those in the NASDAQ 100 Index,

Copyright © 2024 BSAMC | Bocconi Students Asset Management Club

significantly bolstered the market. These companies especially benefited from cost-cutting measures and the expanding potential of artificial intelligence (AI).

The economic climate in 2023 was also characterized by steady growth, with the U.S. economy expanding at an average annualized rate of 3.2% in the first three quarters and a projected additional growth of 1.3% in Q4. The job market outperformed expectations, adding to the positive sentiment. These factors, combined with declining inflationary pressures, led to a shift in interest rate expectations, with the Federal Reserve hinting at possible rate cuts. This hint contributed to a general market sentiment that leaned towards a "soft landing" for the economy, steering clear of a recession as the year 2024 approached.

Due to this volatile market environment, we steered away from some industries and investments and focused on others. For example, we avoided investing in oil due to the 10% decline in crude futures in 2023 amid geopolitical turmoil and uncertainties around oil output levels from major producers. This decline led to the lowest year-end levels for oil since 2020. Doubts about OPEC+'s commitment to supply cuts mainly compounded the investment risk. Additionally, geopolitical tensions and conflicts in the Middle East added to the market's volatility, influencing the investment strategy away from oil.

In managing our portfolio, we employed a value investing strategy. Value investing is an investment strategy that involves identifying and purchasing undervalued securities, such as stocks or bonds, based on their intrinsic value. This approach is based on the idea that financial markets can sometimes misprice assets, leading to opportunities for investors to buy these assets at a discount. Key metrics used in value investing include PE ratio to identify overvalued/undervalued companies (as well as PEG ratio to also factor in company’s expected earning growth), D/E to calculate the value of total debt and financial liabilities against total shareholder’s equity, as well as EPS growth which allow us to measure how fast a company is growing (or expected to grow) in terms of its earnings. Moreover, this approach requires the use of various financial statements (Income statement, Cash flow statement, Balance Sheet) to understand the true intrinsic value and financial health of companies.

But why this method? Historically, value investing has outperformed growth investing over the long term. Individuals like Warren Buffet have adopted this strategy. This is because by focusing on stocks that are underappreciated by investors and the market at large, there is potential of

Copyright © 2024 BSAMC | Bocconi Students Asset Management Club

higher returns, far less risks, and lower volatility compared to other methods. Value investing also focuses on long term value creation. While it requires patience, this strategy seeks for holding undervalued stocks for a long period of time with hopes that it will grow over time. However, the main downside is that undervaluation of stock does not equate with sure growth. That is, a lower valuation, although attractive, may not have potential for growth in the long term. Additionally, it may be time consuming to find truly undervalued stocks as it requires investors to analyze various reports and metrics to understand the actual intrinsic value of that company.

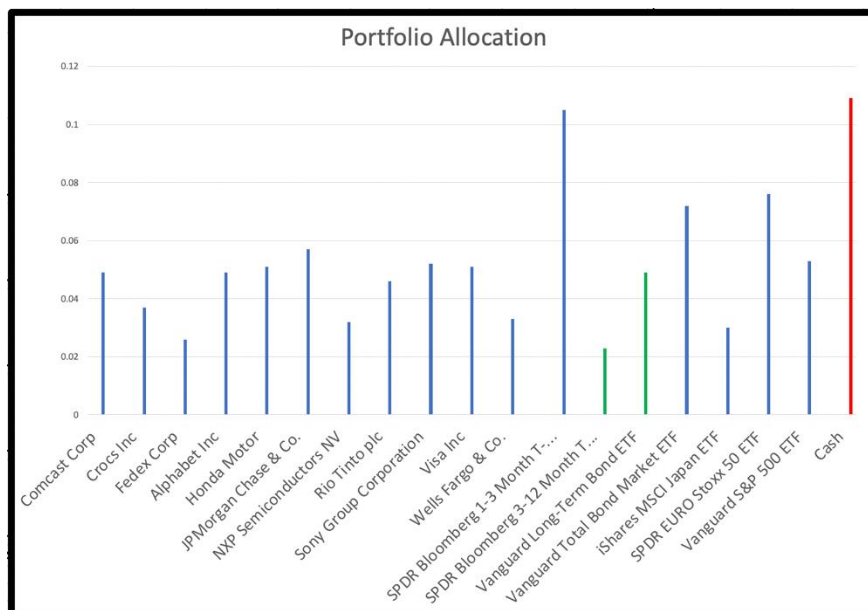
Overall, while value investing had drawbacks, this method is an effective way to gain insights about a company's intrinsic value and does not require the constant monitoring of prices as it focuses on the long term. It is a method that can be used by everyone and does not require extensive resources as most reports and sources are publicly available.

Portfolio Allocation Breakdown

This fund is comprised of 18 total investments. 11 of these investments are securities in the U.S. stock market and the remaining 7 are fixed income. The portfolio's composition is 77.4% invested in equity, 12.1% invested in fixed income and 10.5% held in cash. Throughout October 2023 to January 2024, numerous different transactions have taken place of buying and selling a variety of assets. Each transaction was proposed and defended by an analyst. These stocks were picked in order to maximize expected returns and minimize risks. To reach our benchmark, our team undertook certain risks to outperform the market index. These included stocks that are not as heavily researched and analysed to find under-priced or overpriced securities.

Specifically, our current holdings are: Comcast corp. 4.7%, Crocs inc. 4.0%, Fedex Corp. 2.7%, Alphabet Inc. 4.9%, Honda Motor 4.8%, JPMorgan Chase & Co. 5.6%, NXP Semiconductors NV 3.1%, Rio Tinto plc 4.8%, Sony Group Corporation 5.4%, Visa Inc. 5.0%, Wells Fargo & Co. 3.3%, SPDR Bloomberg 1-3 Month T-Bill ETF 10.5%, SPDR Bloomberg 3-12 Month T-Bill ETF 2.4%, Vanguard Long-Term Bond ETF 5.1%, Vanguard Total Bond Market ETF 7.4%, iShares MSCI Japan ETF 3.0%, SPDR EURO Stoxx 50 ETF7.5%, Vanguard S&P 500 ETF 5.2%.

Copyright © 2024 BSAMC | Bocconi Students Asset Management Club



Performance

In the initial period following its creation (from November 1st to January 15th), our portfolio demonstrated a significant outperformance compared to our benchmark. Notably, we came close to achieving our annual target of 9.5% within just two and a half months, securing an impressive 9.4% return.

It is worth noting that our performance unfolded during a phase of general market growth in both the US and global markets (S&P500: +13.5%). To better evaluate our portfolio performance, we also have to look at its Beta (0.74), which indicates a restrained volatility of our assets compared to the market. This lower

Copyright © 2024 BSAMC | Bocconi Students Asset Management Club

Beta is a result of a substantial allocation to cash, secure investments in T-bonds, and ETF Bonds. In light of these factors, we can conclude our performance went far beyond our expectations.

Among our top-performing stocks were J.P. Morgan Chase & Co (+21%), Sony Group Corporation (+16%), and Wells Fargo & Co (+16%). These outcomes underscore our ability to generate substantial returns by investing in stable, well-established companies while managing risk prudently. Notably, the Betas for the mentioned stocks are 1.01 (SONY), 1.12 (JPM), and 1.18 (WFC).

The only stock incurring a loss in our portfolio is FedEx (-3% since November 10th), representing a modest portion of our capital (less than 3%, considering a standard investment of 5% for each stock).

Shifting focus to fixed-income ETFs, both the Long-Term Bond and Total Bond Market experienced a great price appreciation (7% and 6%, respectively). Besides price growth, it is crucial to consider that these assets are expected to generate significant dividends over the next 12 months: 4.2% and 3.1% for the Long-Term Bond and Total Bond Market, respectively.

Risk management

To achieve the best risk-reward combination possible, we pursued a risk management approach on two levels: the individual security level and the overall portfolio level.

On the individual security level, our approach to managing risk consisted of selecting securities which are undervalued relative to the market based on indicators including the P/E and EV/FCF ratios. Through this approach, our goal was to lower risk without sacrificing returns by investing in securities with relatively low downside and high upside potentials, thereby achieving better risk-adjusted returns than the market.

On the overall portfolio level, we focused on minimizing idiosyncratic risk without compromising the selection criteria applied at the individual security level. To that end, we avoided being too concentrated in one security, industry, or geographical area. Since the platform we used only allowed us to invest in US-traded securities, we invested in ETFs that track indices of non-US markets. Moreover, we invested 5% of our capital in an ETF tracking the S&P 500 to better diversify our US portfolio.

At the time of writing this report, we were invested in 10 different industries in the active part of the portfolio and around 28.5% of our capital was invested in non-US stocks in the active and passive parts combined.

In the end, our risk management approach on both levels allowed us to achieve acceptable returns with a beta of only 0.75.

Copyright © 2024 BSAMC | Bocconi Students Asset Management Club

Improvements for the future

As we have analyzed the performance of our equity and fixed income fund, we have recognized the importance of a clear and cohesive investment strategy. Currently, we are using fundamental analysis, focusing on identifying value stocks with untapped potential and growth stocks with promising trends. However, we are looking into integrating technical analysis to better time our market entries and exits for potential higher returns.

To improve our decision-making process, we could potentially incorporate more quantitative analysis into our evaluations. We could use metrics such as beta to understand volatility, alpha to measure our performance against benchmarks and maybe even discounted cash flow (DCF) calculations to estimate intrinsic values with precision. This planned shift towards a more numbers-oriented approach will provide a solid foundation for our decisions to buy or sell that we have not had thus far, ensuring that each action is backed by data analysis.

Finally, we are looking into developing a structured risk assessment model and establishing clear metrics for identifying favorable stocks. We want to set predetermined thresholds for returns, both positive and negative, for each stock, dictating when to take profits or cut losses.

Conclusion

Over the last semester, the equity and fixed income fund team has achieved a projected yearly return equivalent to that of the target 9.5% return (9.4% as of January 15th). Indeed, diversification and the use of a value investing approach allowed our team to reduce volatility (beta of 0.75) and increase potential return by investing in undervalued companies. Nevertheless, improvements are possible for the future such as the implementation of more quantitative analysis to measure our performance and select our potential investments.

Copyright © 2024 BSAMC | Bocconi Students Asset Management Club

BSAMC
Bocconi Students Asset Management Club

Sources:

TradingView. (2023). *Free Stock Charts, Stock Quotes and Trade Ideas*. TradingView. https://www.tradingview.com

Hayes, A. (2022, January 29). *Value Investing*. Investopedia. https://www.investopedia.com/terms/v/valueinvesting.asp

Www.eidebailly.com. Retrieved February 7, 2024, from https://www.eidebailly.com/insights/articles/2024/1/quarterly-financial-market-update-2023-q4