

Strategic Capability Evaluation of the Savana US Equity Strategy



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1.0 Overview: Savana US Equity Portfolio Strategy

Inception Date: 01 Nov 2021.

Funds Under Management: No live strategy- model portfolio analysis.

Strategy Objective: The strategy's objective is to leverage advanced finance and collective intelligence, applied through dedicated research and development, to provide a rate of return (after fees and expenses and before taxes) which exceeds the return of the S&P 500 index.

Data Period Analysed: Period I - Model portfolio – Nov 2021- Aug 2023.

Live- Not Applicable

2.0 Savana Investment approach and Factor Biases – Small Cap Value (refer Exhibit 1-2)

Our fundamental style factor-based analysis of the Savana US Equities portfolio confirms the strategy to be Small and Mid Cap Value. While we observe some drifts on factors over a cyclical period, the secular bias to Small and Mid-Cap Value is very pronounced, persistent and pervasive (e.g., Financials, Consumer Discretionary, Communication Service, Healthcare, Materials sectors). The strategy's economic footprint as measured by style factors is in line with management philosophy and belief – to select deeply undervalued companies and concentrate capital allocations onto the best opportunities. The execution of the strategy to date is also consistent with the team's investment philosophy of seeking opportunities in the segments of the market where significant structural information advantage exists and that can be exploited by its disciplined process.

At a more granular level, some Value factors (measures of cheapness) relatively more significant (statistically) and include:

- Sales to Price
- Free Cash Flow Yield
- Cash Flow Yield

From the analysis of the value factors, Savana's process appears to favor mispriced opportunities based on their cash flow or revenue generation as opposed to PE and Book to Price for instance. This is in contrast to many systematic value managers.

Savana has adopted a flexible approach to Value over Quality, such as it prioritizes Value over Quality. That said, a lot of the anti-Quality portfolio bias relative to the index (example negative tilts to Earnings Growth stability) was driven by the size effect (small-cap bias). This Size bias is also a driver of higher than index volatility of the portfolio returns. The portfolio also exhibits anti-Momentum (Contrarian) attributes which is different to quant-based value or style-neutral managers that tend to emphasize price and earnings momentum in their stock selection models. The strategy has a positive tilt to Dividend Yield and Shareholder Yield (a broader measure of yield), which is important from 2 perspectives. Firstly, its total return in the long run is enhanced by dividends, buybacks and reduction of debt. Secondly, the selection process is not exposed to seek cheap but speculative companies with no payout history.

The current economic factor footprint of the portfolio suggests Savana's portfolio has a very significant alpha upside if the valuation gap (as indicated by a range of valuation ratios) of the portfolio companies converge over time towards market multiple. For instance, on a Sales to Price ratio basis, the portfolio is 10 standard deviations cheaper than the index. A closer look at Exhibit 2 shows that Savana's portfolio is cheap, not just on Sales to Price but also on Free Cash Flow Yield and Cash Flow Yield.

The active risk appetite and depth of valuation advantage of this portfolio means it's more suitable for clients with a higher risk appetite and multi-manager portfolios and who take longer term approach to investing and can afford to ride-out short-term relative index volatility.

3.0 Key Drivers of Alpha – Skill or Luck? (Exhibits 3-5)

Evidence from adjusted Brinson analysis – sources of alpha within sectors and style

Since inception, our holdings-based attribution analysis shows that the strategy generated positive and pronounced skilled-based alpha (a.k.a idiosyncratic alpha). Savana's US strategy generated a cumulative excess return of 39.51% p.a. since inception. In addition, the evidence suggests that Savana is not just a factor or smart-beta manager but also a **skilled stock picker**, which is evident from their consistent outperformance of factor benchmarks. Its strong stock selection was persistent and pronounced even after adjusting for the market, sector and style. This was demonstrated by the style- and market-adjusted returns of the portfolio, which were positive and shows that stocks selection was the primary driver of returns (accounting for 48.40% and 41.17% respectively). The strategy's entire track record is less than a full cycle none the less it demonstrates the positive attributes of a skilled manager when we adjust for style and sector effects (Exhibit 3).

The value add from adjusted stock selection over the analysis period was broad based in the Financials, Consumer Discretionary, Healthcare, Communication Services, and Materials sectors. The weakest stock selection results were evident in the Real Estate, Industrials, and Energy (Exhibit 4). From a cyclical and defensive sector perspective, Savana's process added value across all types of sectors. This broad-based contribution to its success is very encouraging.

When stock selection value-add was assessed across size and style segments, we observed the success was attributed to Mid and Small Value and Mid and Small Growth. Negative results were noted in the Mid-Core segments (Exhibit 4). The constitution of value-add came from diverse names such as Qurate Retail Inc., Zim Integrated Shipping Service, Deutsche Bank and Fossil Group (Exhibit 6).

4.0 Decomposition of risk – Is risk hierarchy aligned with management belief and proclaimed skill? (Exhibits 7-8)

Our foregoing analysis shows that the active risk taken by the portfolio was well rewarded with positive return payoffs. Importantly, portfolio's active risk (index relative) is driven by stock-specific drivers, first and foremost, followed by sector and style factors. This structure of risk hierarchy ensures alignment of risk with Savana's competitive edge (stock picking) as well as mitigation of excessive headwinds and tailwinds on performance from non-skill (systematic factors).

The assessment of the portfolio's active orientation across the dimensions of tracking error and active share classifies Savana's portfolio as a stock-picker with concentrated factor exposure (Exhibit 8). Typically, funds with higher active shares that are managed by skilled managers have a higher propensity to outperform the index and peers over the medium-to-long term. The active orientation of Savana's strategy demonstrates that the portfolio companies are highly leveraged to the underlying manager's stock selection skills, which creates the opportunity to materially outperform in the medium-to-long term. We also observe that both tracking error and active share have been trending higher since the portfolio's inception. This suggests effective identification of opportunities and capturing favorable risk-return profiles, leading to improved risk-adjusted returns.

Drilling deeper into the sources and nature of the active risk drivers, we observed that the risk positioning is in line with the expectations of a stock-picker strategy. That is, stock-specific risk dominates style and sector sourced risks (Exhibit 7).

Further active risk decomposition shows systematic risk was mainly driven by sector and style risk, which in turn were driven by the Communication Service and Energy sectors, and Small Value and Small Growth style segments. So long as it is intended and the team has a positive pay-off attached to these risks over a reasonable time horizon, then the level of risk is not a source of concern. Our style-based attribution of returns shows good value-add from stock selection and sector allocation from the small-cap segment. So, the additional volatility that is sourced from small-cap stocks was well rewarded.

The securities contributing to the risk were Telephone and Data Systems, United States Cellular Corp, Vital Energy Inc., PBF Energy, Crescent Energy Co. and Excelerate Energy which belong to the Energy and Communication Service sector (Exhibit 7).

Overall, our risk analysis of Savana's strategy shows the stock-specific risk dominates sector and style-based risks, which is consistent with the managers claim of 'focus stock picker'. In addition, the return-based attribution shows that majority of the value-add came from good stock picking across sectors and style segments.

5.0 A nuanced Value approach makes Savana's strategy unique (Exhibit 1-2)

Savana's investment strategy stands out with a distinctive combination of attributes that shape its unique approach to exploiting mispriced securities. One outcome of the nuanced approach is a high-yield portfolio relative to the index, based on non-classic value ratios (Dividend Yield and Cash Flow). This characteristic allows the strategy to blend well and compliment classic value peers.

Detailed factor-level analysis of the portfolio shows that the strategy captured a range of Value factors. Free Cash Flow Yield, Cash Flow Yield and Sales to Price factors were the most pronounced, persistent and pervasive. This signals that the portfolio focuses on assets that have strong cash flow generation capabilities relative to their market value. On the yield side, Shareholder Yield (a broad measure of yield including Dividend Yield, Net Debt Paydown Yield and Net Buyback Yield) dominated factor bias.

Overall, Savana's strategy appears to be rooted in the belief that significant information advantages exist in small and midcap segments of the market where significantly undervalued securities can be identified and traded. However, while the strategy exhibits a structural bias towards small and midcaps that are undervalued simply because of the prevalence of smaller companies in the index, it does not necessarily mean that they rule out larger cap. Savana uses consistent processes across the entire stock universe.

References

- “Holding based Active Insights.” Report by Foresight analytics. November 30, 2023.
- “Savana AI US Portfolio Performance Assurance.” Report by Foresight analytics. November 30, 2023
- ‘Capital Raise Pitch deck.’ Pitch Deck by Savana Asset Management. July 31, 2023.

Appendix I- Charts

Exhibit I: Historical country- and sector-adjusted style bias

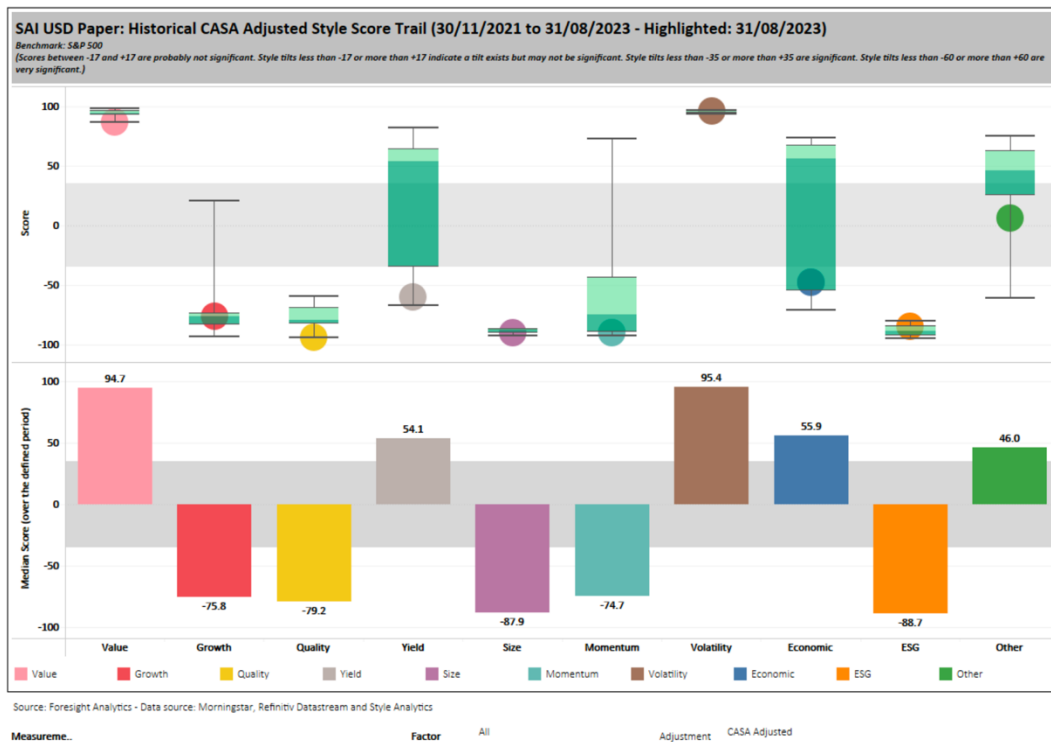
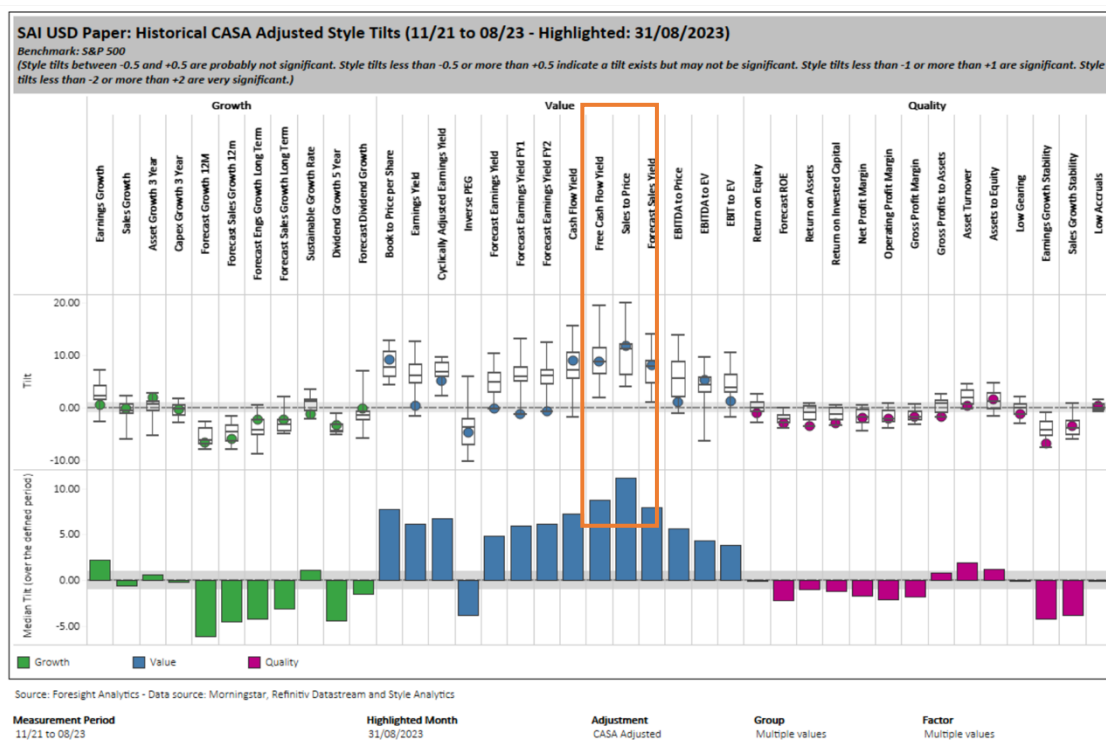


Exhibit 2: Style factor secular and cyclical tilts of the portfolio since inception



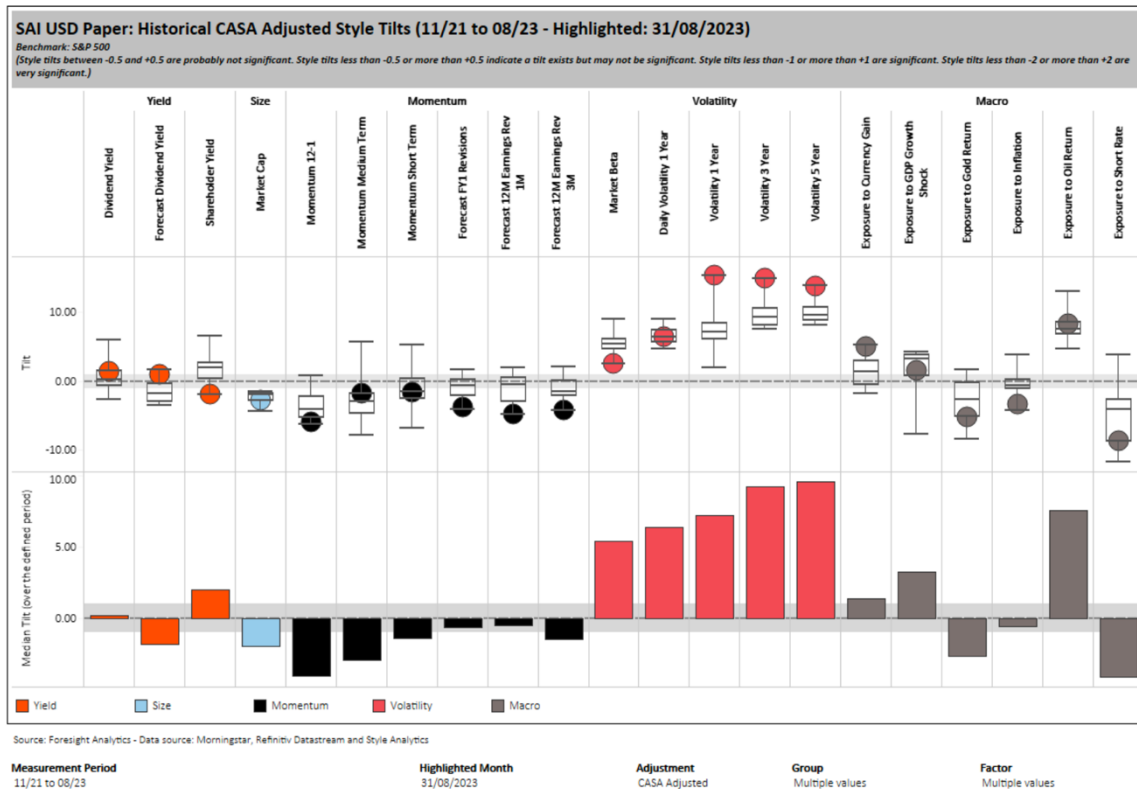


Exhibit 3: Brinson active return attribution since inception

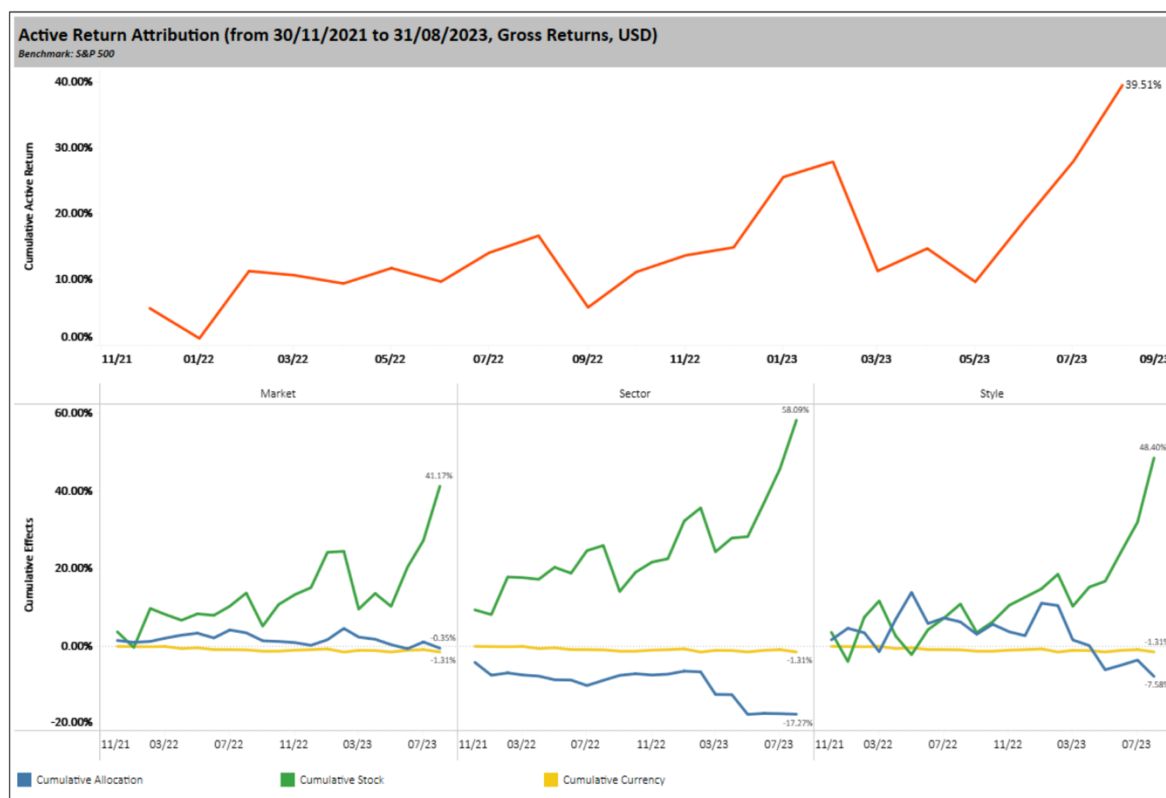


Exhibit 4: Brinson active return attribution since inception- Sector & Style



Exhibit 5: Security Contribution to Active Return

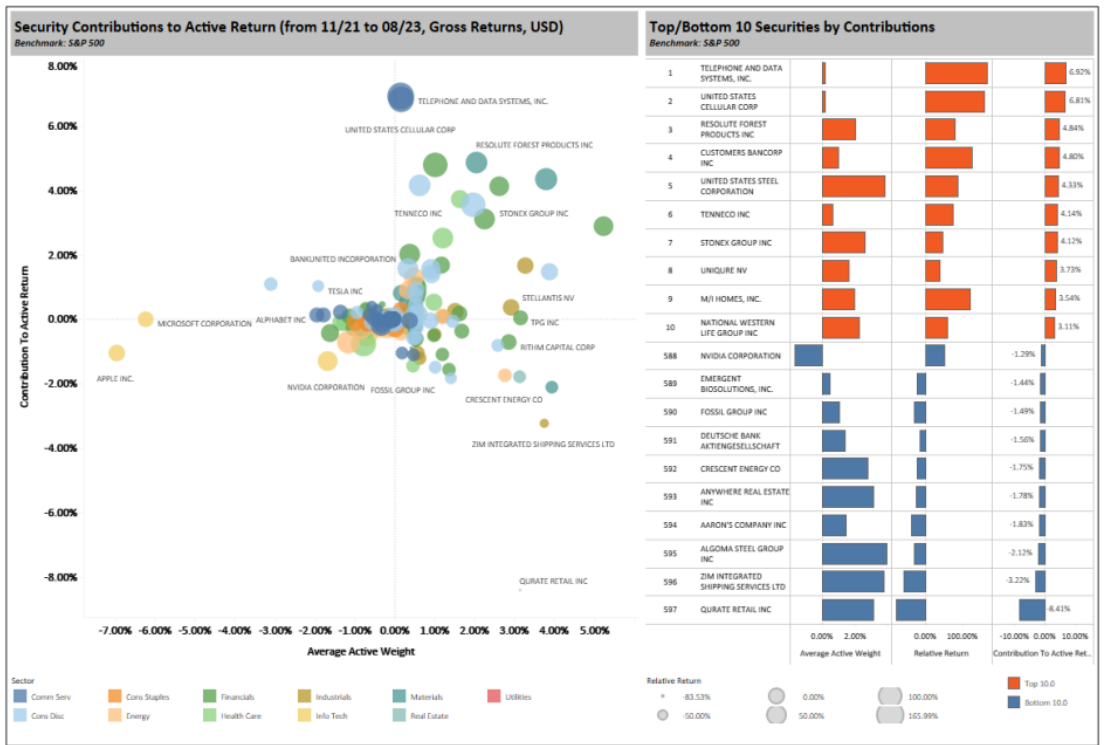
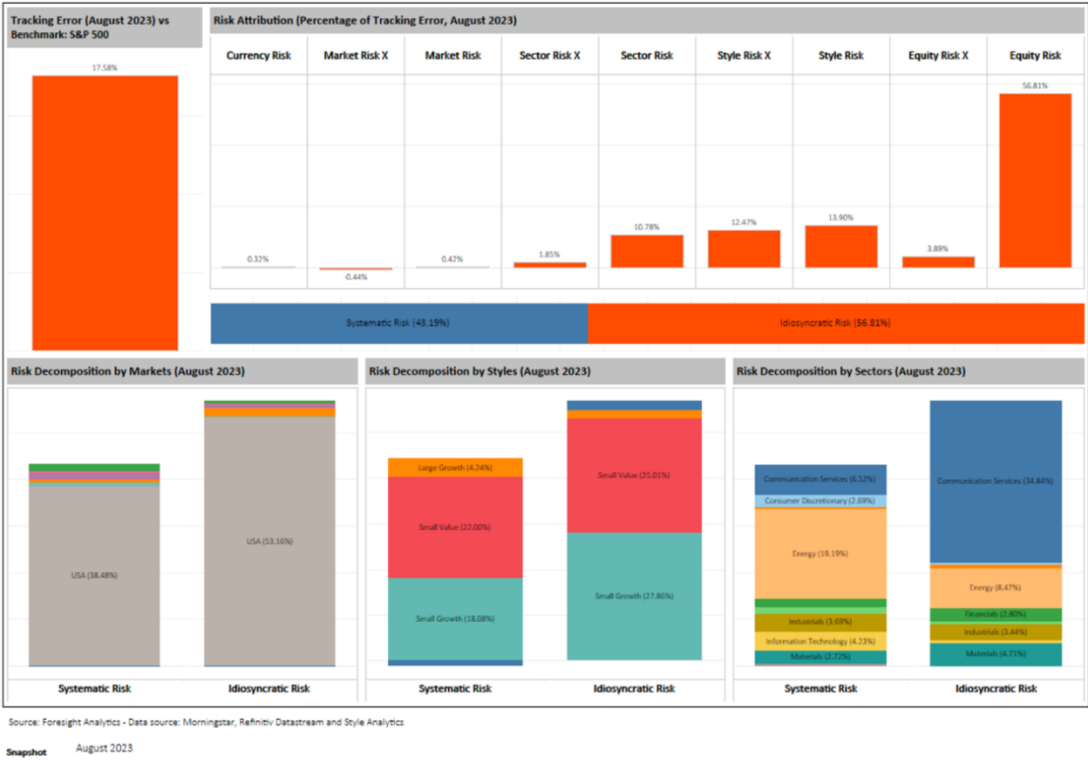


Exhibit 6: Risk attribution as of August 2023.



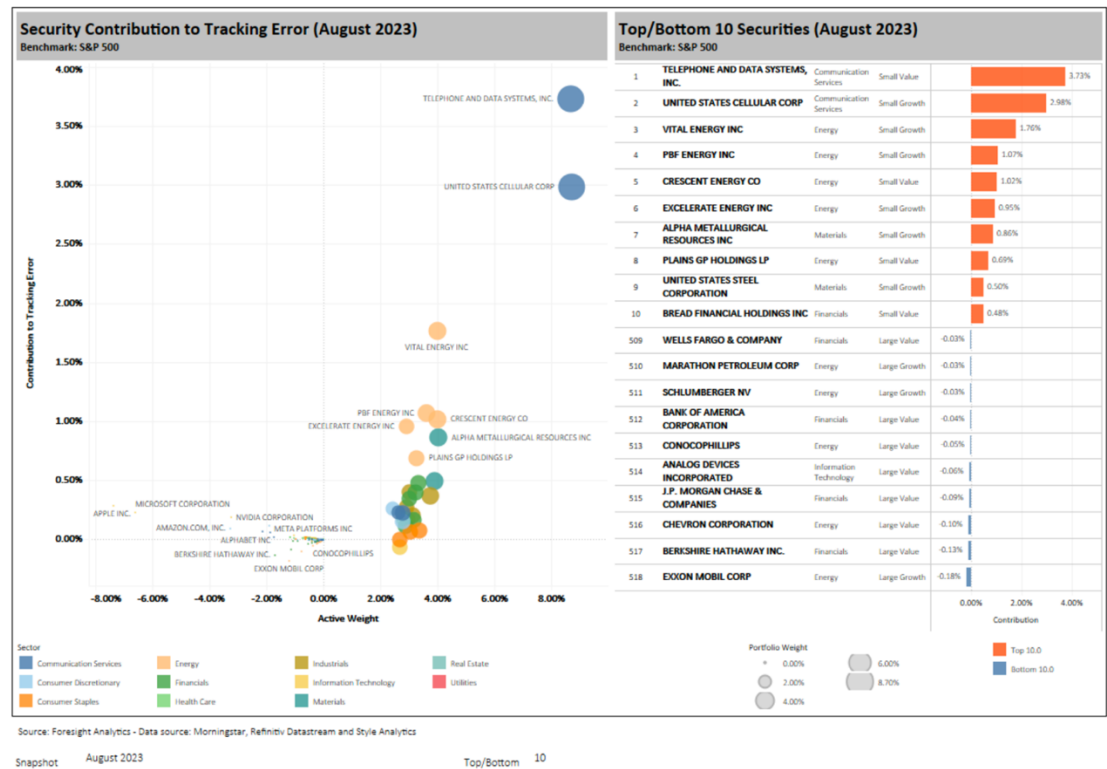
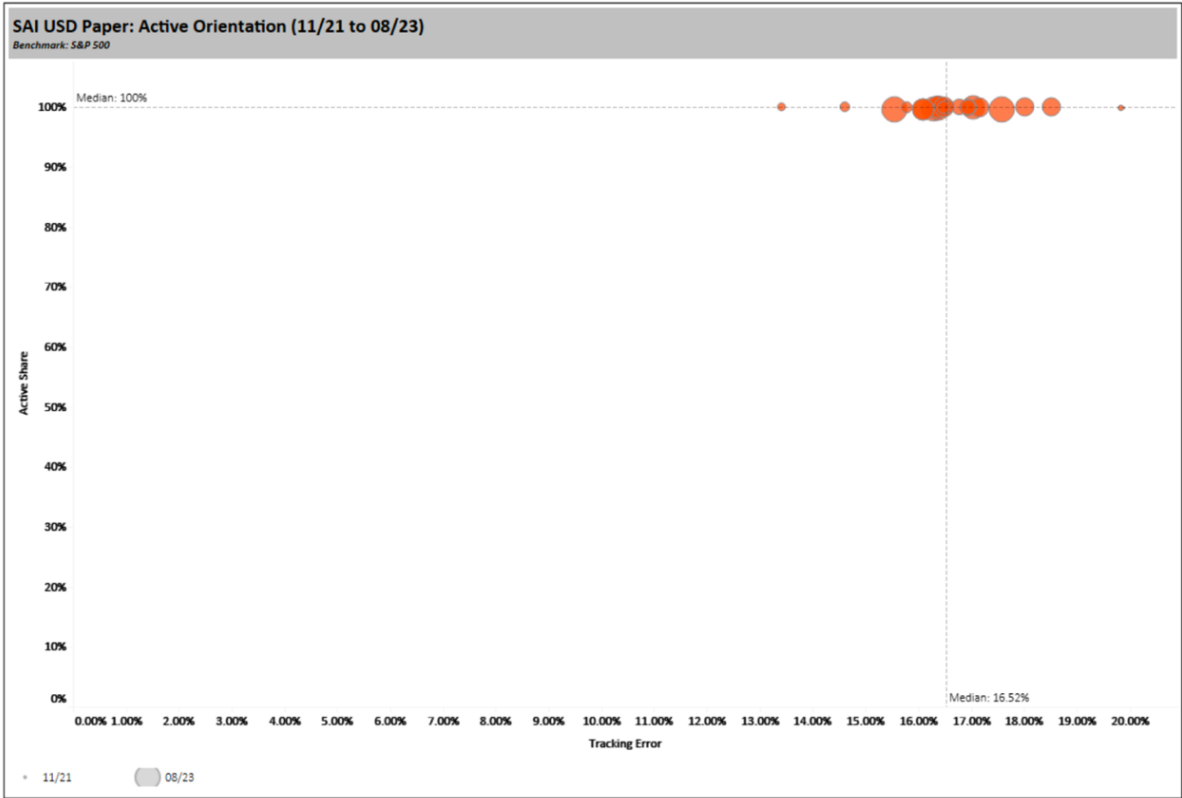


Exhibit 7: Active Orientation



Appendix 2 – Definitions

Term	Definition
Active Share	a measure of the percentage of stock holdings in a fund that differs from the benchmark index.
Active Weight	The difference in allocation of an individual security or portfolio segment between portfolio and the benchmark. For example- if a portfolio allocates 12% in the IT sector, & the benchmark's allocation in IT is 7% then active weight if the IT segment of the portfolio is 5%.
Alpha (Skill Measure)	Alpha is the difference between the fund's expected returns based on its beta and its actual returns. It is sometimes interpreted as the value that a portfolio manager adds, above and beyond a relevant index's risk/reward profile. If a fund returns more than what you'd expect given its beta, it has positive alpha.
Beta	Beta is the sensitivity of the portfolio in relation to the market. A beta of 1.00 implies perfect historical correlation of movement with the market. A higher beta manager will rise and fall more rapidly than the market, whereas a lower beta manager will rise and fall slower. Eg a 1.10 beta portfolio has historically been 10% more volatile than the market.
Book to Price	The ratio of the company's book value (the sum of shareholder's equity plus accumulated retained earnings from the P&L account) to its share price. This factor has been one of the most successful measures of the intrinsic value of company shares.
Cash Flow Yield	Annual cash flow per share divided by the share price. This factor is related to earnings yield but also includes other items, Specifically: depreciation, amortizations & provisions for deferred liabilities. It is intended to capture the cash availability of the company as a multiple of the share price, & offer a value criteria based on the stream of accessible cash earnings.
Correlation	Correlation is a statistical term that measures the extent of linear association of two variables. Correlation coefficients can range from —1 to +1. A coefficient that is —1 means that the manager is perfectly negatively correlated with the index or manager against which it is regressed (move same amount in opposite directions); a coefficient of 0 signifies zero or no correlation, & finally a coefficient of +1 means perfect positive correlation (move the same amount in the same direction).
Cyclically Adjusted Earnings Yield	10-year average of cyclically adjusted annual earnings (adjusted for amortizations of intangibles, extraordinary charges & credits) per share divided by the share price. This factor measures the worth of a company's shares according to the company's ability to support each share with after tax earnings.
Dividend Yield	The annual dividend paid per share divided by the share price. This factor measures the value of company shares according to the stream of dividend income resulting from share ownership.
Drawdown	'A drawdown is the peak-to-trough decline during a specific recorded period of an investment, fund or commodity security. It is usually

	quoted as the percentage between the peak & the subsequent trough. Max drawdown measures the largest single drop from peak to bottom in the value of a portfolio (before a new peak is achieved).
EBITDA to Price	The factor is a measure of a company's core profitability as a multiple of its share price. EBITDA is Earnings Before Interest, Taxes and Depreciation & is calculated by taking the pretax income & adding back interest expense on debt & depreciation, depletion & amortization & subtracting interest capitalized.
Excess Return	Excess returns are investment returns from a security or portfolio that exceed the riskless rate on a security generally perceived to be risk-free, such as a CD or a government issued bond. It can also entail returns excess of the market or give benchmark.
Free Cash Flow Yield	Annual cash flow per share minus capital expenditure per share divided by the share price. Free Cash Flow is the amount of money available to the company after paying out for the maintenance & renewal of fixed assets.
Factor Sensitivity	Is the magnitude of a fund's reaction to changes in underlying factors. It accounts for all factors that impact a given instrument in a negative or positive way.
Forecast Dividend Yield	The consensus 1 year forecast annual dividend per share, divided by the share price.
Growth Style	Growth investing is a style of investment strategy focused on capital appreciation. Those who follow this style invest in companies that exhibit signs of above-average growth, even if the share price appears expensive in terms of metrics such as price-to-earnings or price-to-book ratios.
Idiosyncratic Alpha	Idiosyncratic alpha is the unexplained component of a fund's return in excess of the benchmark that can be attributed to stock picking skill after the return is adjusted to systematic risk factors.
Idiosyncratic Risk	Idiosyncratic risk, also referred to as unsystematic risk, is the risk that is endemic to a particular asset such as a stock & not a whole investment portfolio. It is the risk which affects a very diminutive number of assets & can be almost eradicated through diversification.
Market factor	This factor aims to capture the premium from taking systematic risk originating from macroeconomic factors.
Momentum factor	In finance, momentum is the empirically observed tendency for rising asset prices to rise further & falling prices to keep falling. The premium of this factor is calculated as the return difference between a portfolio of top 30% stocks and a portfolio of bottom 30% stocks by their 11 month (excludes the most recent month) cumulative returns.
Peer Share	To calculate peer share, the benchmark is replaced by a peer. It is, therefore, the percentage difference between a fund & its peer in stock holdings.
Size factor	This factor assesses the excess return of a portfolio of small stocks over the return of a portfolio of large stocks. It is based on the small cap anomaly that says smaller firms (In terms of market capitalization) tend to outperform larger companies over the longer run.
Sales to Price	Net Sales per share divided by the share price. This factor measures the worth of a company's shares according to the annual sales volume

	supporting the company business. The item is considered by many analysts to be less susceptible to manipulation than other valuation criteria; It is, However, a less comprehensive measure of a company's range of activities.
Sales to EV	Net Sales per share divided by enterprise value. Enterprise value is defined as "market capitalization + total debt + preferred stock – cash & cash equivalents".
Systematic Risk	Systematic risk is the risk inherent to the entire market or market segment. Systematic risk, also known as undiversifiable risk, "volatility," or "market risk," affects the overall market, not just a particular stock or industry. This type of risk is both unpredictable & impossible to completely avoid. It cannot be mitigated through diversification, only through hedging or by using the correct asset allocation strategy.
Tracking Error	A measure of the amount of active risk that is being taken by a manager. This statistic is computed by subtracting the return of a specified benchmark or index from the manager's return for each period & then calculating the standard deviation of those differences. A higher tracking error indicates a higher level of risk - not necessarily a higher level of return - being taken relative to the specified benchmark. Tracking error only accounts for deviations away from the benchmark but does not signal in which directions these deviations occur (positive or negative).
Value Factor	The value factor aims to capture the premium between the return of a portfolio of stocks with high book-to-market ratio over return of a portfolio of stocks with low book-to-market ratio.

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