Alpha Diversified Fund - Positioning 8/31/2022

Pie chart legend: Absolute Return | L/S Equity | Systematic | Global Macro | Long Biased Equity | Cash

Chart values:
- Cash 1%
- Long Biased Equity 6%
- Global Macro 23%
- Absolute Return 25%
- Systematic 14%
- L/S Equity 31%
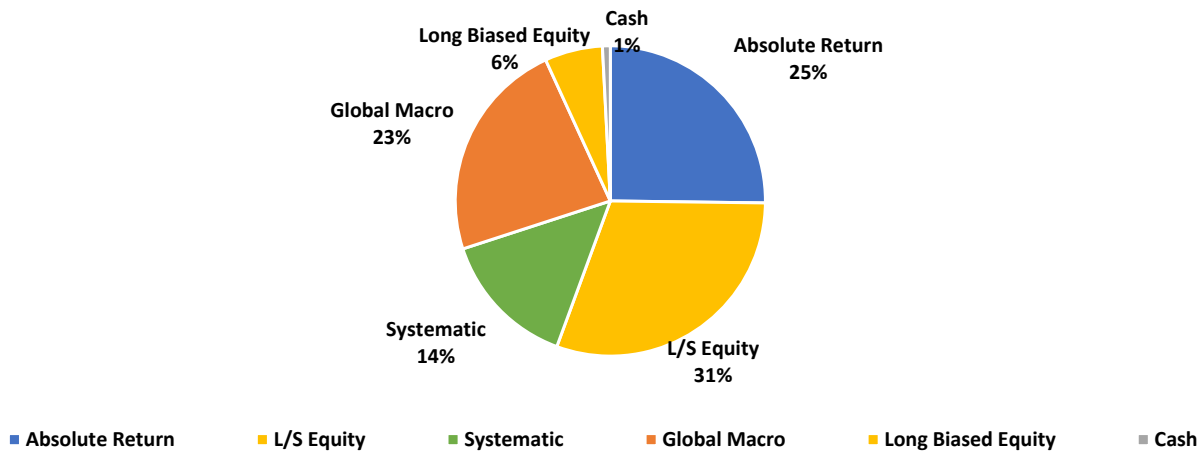
Systematic Discussion

Nasdaq introduced computers to Wall Street in 1971, and since then, systematic investing, also known as quantitative, rule-based, or algorithmic investment strategy, has been on the rise. Investment decisions made by humans in discretionary investing are made by algorithms in systematic investing. Some estimate that up to 90% of security transactions today involve algorithmic decision-making.

Discretionary Investing has been around forever and relies on the skills and knowledge of a fund manager to analyze a relatively limited number of securities with a limited number of indicators to determine companies that show the greatest likelihood of generating profits in the future. The number of stocks and indicators that a fund manager can consider in the discretionary investment approach is relatively limited for practical reasons. The fund manager can easily be overwhelmed by the sheer amount of data associated with each stock, compromising decision-making ability. Trading a large number of markets with this approach can be difficult, and adding additional discretionary traders creates a further challenge in implementing core strategy consistently. In the systematic approach, these challenges are overcome using algorithmic models to analyze a large amount of data and make investment decisions.

In addition to avoidance of investment error due to psychological biases, a systematic approach offers several key benefits, including scalability in investing with a consistent approach twenty-four hours a day across a global portfolio of securities, the implementation of consistent risk management, and the scientific rigor which can be devoted to the continuous development of the core investing approach. There is now a considerable body of theoretical and empirical evidence proving the difficulties a discretionary investor faces in making consistent and reliable forecasts and decisions related to risk allocation. Humans are often prone to irrational behaviors in risk seeking and risk aversion when making decisions under uncertainty. Furthermore, there is now recognition of these psychological biases' effect on financial markets and subsequent opportunities for systematic investors.

The systematic Investing approach can have many advantages over the traditional discretionary method in selecting investments. Since all the decision-making and investment processes are automated in systematic investing, risk monitoring, new information processing, signal generation, and trade execution can be implemented continuously, and an algorithm can monitor and trade several thousand stocks. Many investors embraced systematic investing techniques due to their strong performance in the depth of the global financial crises. Nevertheless, recent awareness of the broader benefits of the approach in all market environments has incited others. The proliferation of data on publicly traded securities allowed systematic investors an information edge over their fundamental counterparts. Calculating factors such as sales growth, earning momentum, price momentum, and other vital indicators across a large universe of stocks provided an opportunity for alpha in this approach.

High-frequency trading, another form of systematic investing in which a large number of equities are traded in fractions of seconds, has produced excess returns for decades. More recently, data from social media, web scraping and other unique sources have provided a further informational edge to systematic investors. Companies like Dataminr are at the forefront of harvesting real-time data from numerous sources, generating signals, and providing valuable information to investors. The latest developments in systematic investing use machine learning models to predict stock movements.

The terms Machine Learning and AI are often used synonymously; however, machine learning is an approach that has been used in the last two decades to develop artificial intelligence. Other AI development methods, such as Fuzzy Logic, have been around for the past sixty years. However, none has been as efficacious as machine learning, which has predominantly been used in the last two decades. Machine learning can be categorized into supervised, unsupervised, and reinforcement learning and is a technique for training a computer model to read, write, see, and sense with high accuracy and mimic human behavior at scale. The application area of machine learning is still in its nascent stage and is evolving fast. An abundance of data and fast computer processors can be credited for the recent advances in machine learning and AI.

Despite all the pros, informational advantages in systematic strategies are prone to dissipation over time. Machine learning models can stale quickly and must be continuously trained using new data. To be successful in any systematic strategy, one must get in early, leverage informational edge, monitor closely, and update constantly. Leibniz, one of Alpha Diversified Fund's portfolio strategies, has precisely done that and has generated constant positive returns in these times of turmoil.

Net Returns, Aug 2019- Aug 2022	Leibniz Intelligence	S&P 500
Total Return	119.26%	41.90%
Annualized Return	29.91%	12.40%

Leibniz leverages a new set of opportunities by systematically trading a highly liquid, cash-efficient strategy that processes large amounts of diverse data using proprietary algorithms. Markets go through phases of low volatile trends, sharp market reversals, trendless periods, mean reversions, and big tail events, followed by swift market recoveries. Leibniz, leveraging proprietary technology, aims to stay ahead by exploiting early opportunities at each phase.

Alpha Diversified Fund leans toward strategies, like the one implemented by Leibniz, that have minimal market exposures, are uncorrelated to big swings in equity markets, and generate significant returns in all market conditions. If you want to learn more about Alpha Diversified Fund and discuss exposure to the systematic investing category, don't hesitate to get in touch with Mark Kress at 415-290-7164 or mkress@alphawealthfund.com.

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