

Convergence Long/Short Strategy

Q1-2024 Signal Analysis

Signal Research

The following table shows the top three and bottom three performing signals within the U.S. Equity market over different time periods based on our internally generated research. We ranked all fifteen of Convergence’s main signal composites by quintile spread return to show that what can work over the long term is not always true in the short term (see disclosures for a definition of quintile spread return).

	3 mo	6 mo	12 mo	5 yr	10 yr	20 yr
Top 3	Price Momentum	Price Momentum	Size	Earnings Momentum	Earnings Momentum	Earnings Momentum
	Profits	Accruals	Traditional Value	Risk Off	Risk Off	Traditional Value
	Historical Growth	Historical Growth	Profits	Size	Profits	Price Reversal
Bottom 3	Capital Discipline	Relative Value	Earnings Risk	Earnings Risk	Accruals	Historical Growth
	Relative Value	Earnings Risk	Risk Off	Accruals	Expected Growth	Risk On
	RiskOn	Risk Off	Risk On	Capital Discipline	RiskOn	Expected Growth

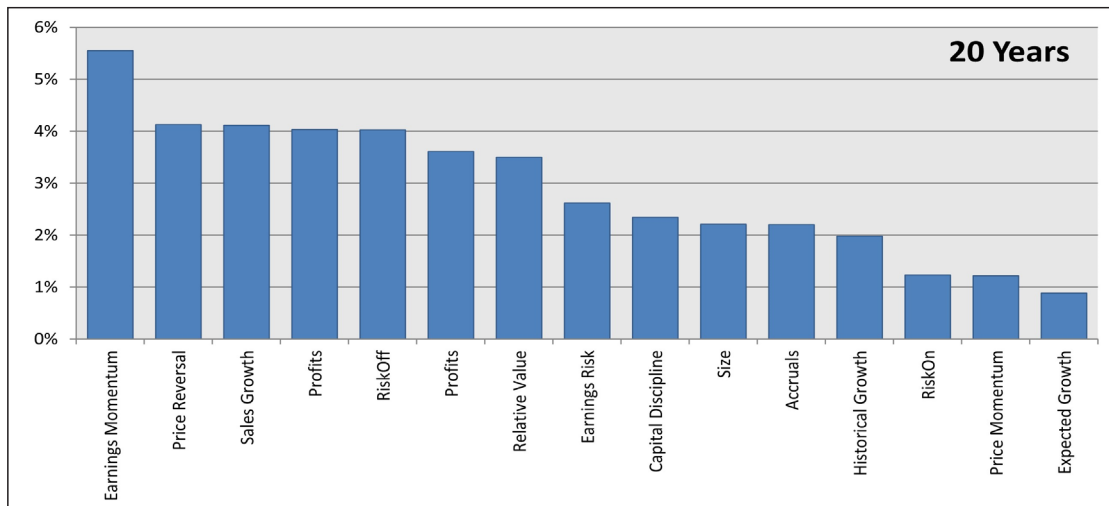
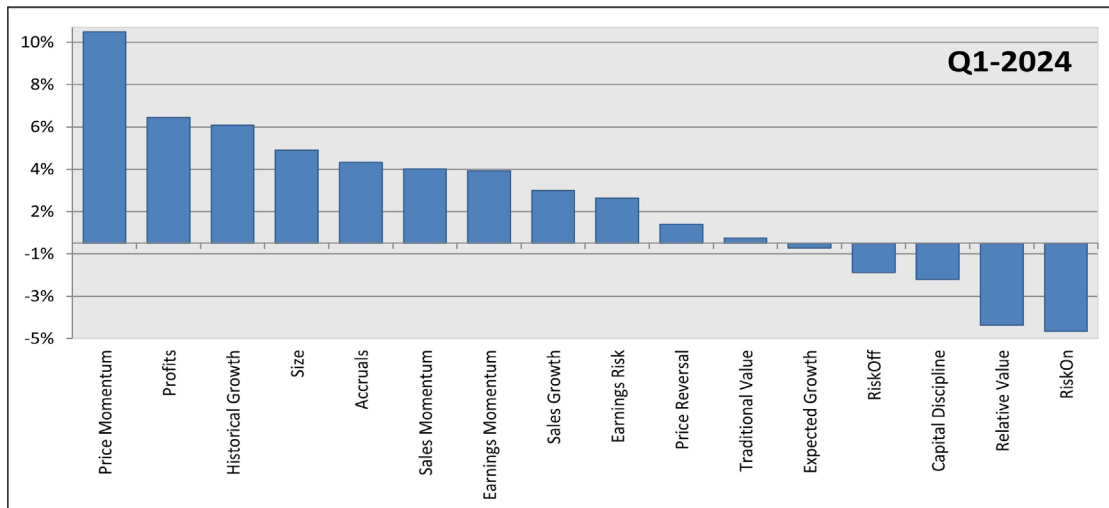
As of 03/31/2024. Source: Convergence Investment Partners, Wilshire Analytics. Production Long Q1 - Short Q5.

Looking at the table above, it seems that what was in favor, stayed in favor for the trailing 3- and 6-month periods. This is shown by the strength of our Price Momentum and the Historical Growth signals. It is interesting to note that unlike typical momentum fueled rallies, this run was driven by fundamentally strong companies with strong and improving profitability and earnings growth. Often momentum runs can be powered by lower quality stocks. These “lower quality” momentum runs would see strong returns from our Risk On and Expected Growth signals and this was not the case for the trailing 3- and 6-month periods.

Moving to the long term, our Earnings Momentum signal has been quite strong. This signal is comprised of consensus earnings estimate factors. The Earnings Momentum signal ranks the Convergence universe of stocks based on the magnitude of absolute earnings surprises, changes in earnings surprises, and earnings estimate revisions.

The charts below show the ranking of how well signals worked in both Q1-2024 and over the last 20 years. These tables show the long-short quintile spread returns of all the signal composites we monitor at Convergence.¹

Factor metrics rewarded by market participants within the US equity markets



As of 03/31/2024. Source: Convergence Investment Partners, Wilshire Analytics. Production Long Q1 - Short Q5.

¹ These returns are linked monthly spread returns and do not represent the difference between long and short holdings for each time period. Not all signals have twenty years of history, therefore, there are more signals presented in the more recent and shorter time periods than are presented in the twenty-year history.

In order to better observe thematic changes in signal efficacy, we created the following chart which shows the spread returns of each signal composite for each calendar quarter of the past three years. These are ranked from highest spread return to lowest spread return for each quarter (see the legend below).

	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24											
RON	2.75	ER	7.41	PT	10.12	RSK	12.66	ER	17.05	SM	5.77	RSK	13.31	HG	3.11	SM	2.91	PT	6.3	RON	3.63	PM	9.99
EM	2.75	PT	6.23	SZ	9.68	SZ	9.25	TV	10.26	AG	3.31	TV	12.75	PT	2.41	HG	1.49	CD	5.91	RV	1.37	PT	5.95
PM	2.1	SZ	6.04	ER	8.96	RON	9.21	PT	9.85	PR	1.94	ER	10.98	PR	1.66	EG	1.27	TV	5.43	PR	1.15	HG	5.57
HG	1.4	TV	5.16	RSK	8.2	RV	8.9	RSK	9.68	EM	1.5	SZ	9.47	CD	0.41	SZ	1.07	ER	5.34	EM	0.75	SZ	4.41
AG	1.27	HG	5.15	RV	7.26	TV	8.56	AG	8	HG	1.27	RV	6.88	EM	0.19	RV	0.64	SZ	3.2	AG	0.35	ACC	3.81
ACC	1.07	SM	4.73	PM	7.12	AG	7.68	EM	7.66	EG	1.11	PT	6.05	RV	0.13	PM	0.31	RV	2.8	TV	0.32	SM	3.51
SZ	1.06	EM	4.64	TV	7.06	ACC	7.11	RV	6.83	PM	1.11	ACC	5.39	SM	-0.33	TV	0.17	RSK	2.58	CD	0.26	EM	3.42
SM	0.71	AG	4.3	HG	6.16	ER	4.84	SZ	5.16	ACC	-0.03	EM	4.57	EG	-0.46	RON	0.03	ACC	1.9	EG	-0.13	AG	2.49
RSK	0.12	RV	4.14	EM	5.86	EM	2.19	PM	5.14	CD	-0.79	RON	3.62	TV	-1.28	PR	-0.49	HG	0.9	SZ	-0.83	ER	2.14
EG	-0.39	RSK	3.61	PR	4.08	CD	2.13	CD	3.65	PT	-2.43	CD	1.89	SZ	-1.94	ACC	-0.52	EM	0.88	RSK	-0.85	PR	0.9
ER	-0.39	PM	2.67	SM	2.74	EG	1.6	ACC	2.98	RV	-2.61	PR	1.66	ACC	-3.24	EM	-0.92	SM	0.56	ACC	-0.92	TV	0.25
CD	-0.51	ACC	1.67	RON	1.04	HG	1.33	RON	0.59	SZ	-3.75	HG	-0.65	AG	-3.24	PT	-1.04	AG	0.29	HG	-1.85	EG	-0.22
PR	-1.34	CD	0.86	EG	0.78	PT	0.19	HG	0.52	RSK	-3.89	EG	-2.12	RON	-3.28	CD	-1.35	PR	-0.29	SM	-2.02	RSK	-1.38
RV	-1.54	EG	-3.38	ACC	0.56	SM	-2.69	PR	0.34	RON	-4.19	AG	-2.65	RSK	-3.32	RSK	-2.57	EG	-0.87	PM	-3.04	CD	-1.71
PT	-1.6	RON	-3.44	AG	-0.33	PM	-4.47	SM	-1.01	ER	-4.55	SM	-4.2	PM	-4.31	AG	-3.14	PM	-1.45	ER	-3.15	RV	-3.87
TV	-2.05	PR	-5.23	CD	-2.49	PR	-4.48	EG	-1.08	TV	-5.12	PM	-5.69	ER	-6.38	ER	-4.27	RON	-3.16	PT	-4.71	RON	-4.15

ACC	Accruals	HG	Historical Growth	RV	Relative Value
AG	Accelerating Growth	PM	Price Momentum	SZ	Size
CD	Capital Discipline	PR	Price Reversal	TV	Traditional Value
EM	Earnings Momentum	PT	Profits	RON	RiskOn
ER	Earnings Risk	RSK	RiskOff	EG	Expected Growth

How is Convergence positioned?

The following table illustrates a few of the many fundamental factors that we utilize to rank a stock's relative attractiveness within our investment process. The values shown for each factor represent the weighted average value of that specific factor in the Convergence Long/Short equity composite portfolio compared to the broader market.

Average Fundamental Statistics of Long & Short Holdings for our Long/Short Equity Strategy:

Category	Factor	Long/Short Equity	Market	Long/Short Equity
		LONG	Russell 3000 Index	SHORT
Value	Price to Earnings	18.7	28.0	146.7
Value	Price to Free Cash Flow	13.7	27.5	-32.7
Value	Free Cash Flow to Enterprise Value	6.1%	3.3%	-1.3%
Profitability	Net Income Improvement	21.4%	12.7%	-10.7%
Profitability	Cash Flow to Sales	24.7%	-84.4%	-59.5%
Capital Discipline	Change in Shares Outstanding	-0.4	-0.1	4.4
Capital Discipline	Dividend Growth (5 yr cumulative)	120.6	78.2	30.6
Quality	Return on Assets (ROA)	12.3%	12.0%	1.0%
Earnings Growth	Consecutive Qtrs Earnings Growth	2.7	1.3	-0.9
Earnings Growth	Short-term Earnings Growth	43.2%	8.7%	-11.4%
Cash Flow Growth	Consecutive Qtrs Cash Flow Growth	2.4	1.3	-0.2

As of 03/31/2024; Source: Wilshire Analytics & Convergence Investment Partners. All values included.

As the table above demonstrates, the Convergence fundamental stock picking methodology leads us toward holdings in the long portfolio with strong cash flow, earnings, profits and other desirable financial characteristics, at reasonable valuations. Over time, companies with these characteristics have tended to reward investors, since these are signs of healthy and growing companies with competitively strong business models. Conversely, the Convergence process also identifies companies with weak or declining fundamentals. Our research has shown that shorting these types of firms is effective in sourcing alpha, i.e., outperformance from this side of the trade. We believe that companies that are consistently profitable and manage their assets effectively are the ones that build wealth in the long run. Although irrational investments have periods of strong performance, we believe the disciplined investor that maintains a high-quality focus will ultimately be rewarded. Please let us know if you would like to discuss our portfolio exposures or any other aspect relative to recent portfolio results.

Thank you for your support!

Disclosures

Past performance is no guarantee of future results. Any investment contains risk including the risk of total loss. There is no guarantee that an investment or strategy will meet its investment objectives

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Source of all factor data: Convergence Investment Partners.

No graph, chart, or formula should in and of itself be used to determine which securities to buy or sell.

SIGNAL COMPOSITE RESULTS

Signal Composites (factors or "signals") are composed of securities in the Russell 3000 Index ranked by Convergence in terms of the identified metrics. Thus, individual stocks appear in multiple Composites. No client portfolios are managed to any one factor and all factor results reflect backtested data. Factor composites are not available for direct investment. Factor composite results are measured in terms of their quintile spread return ("spread return"): the difference between the index-weighted average results of the highest ranked 20% less that of the lowest ranked 20%. Higher positive numbers indicate that the factor was more relevant to / indicative of stocks that performed well. Negative results are similarly indicative of factors that could have made effective shorts. Convergence views most factors on an industry group neutral basis where industry group weights are fixed based on the selection universe/ index weights.

The Russell 3000 Index measures the performance of the largest 3,000 US companies. It is constructed to provide a comprehensive, unbiased, and stable barometer of the broad market and it is reconstituted annually to ensure new and growing equities are reflected. Comparison to any index is for illustrative purposes only and the volatility of the benchmark may be materially different from the volatility of the strategies due to varying degrees of diversification and/or other factors. Index performance returns do not reflect any management fees, transaction costs, or expenses. Indices are unmanaged. You cannot invest directly in an index.