

Convergence Long/Short Strategies

Q3-2020 Factor Analysis

Factor Research

The following table shows the three top and bottom performing factors within the U.S. Equity market over different time periods. We ranked all 15 factor 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 Reversal	Price Momentum	Sales Growth	Sales Growth	Traditional Value
	Historical Growth	Price Momentum	Historical Growth	Price Momentum	Price Momentum	Price Reversal
	Size	Expected Growth	Expected Growth	Price Reversal	Earnings Momentum	RiskOff
Bottom 3	Traditional Value	Accruals	Accruals	Accruals	Accruals	Size
	Capital Discipline	Traditional Value	Earnings Risk	RiskOn	Traditional Value	Price Momentum
	Accruals	Earnings Risk	Traditional Value	Traditional Value	RiskOn	Expected Growth

As of 09/30/2020. Source: Convergence Investment Partners, Wilshire Analytics.

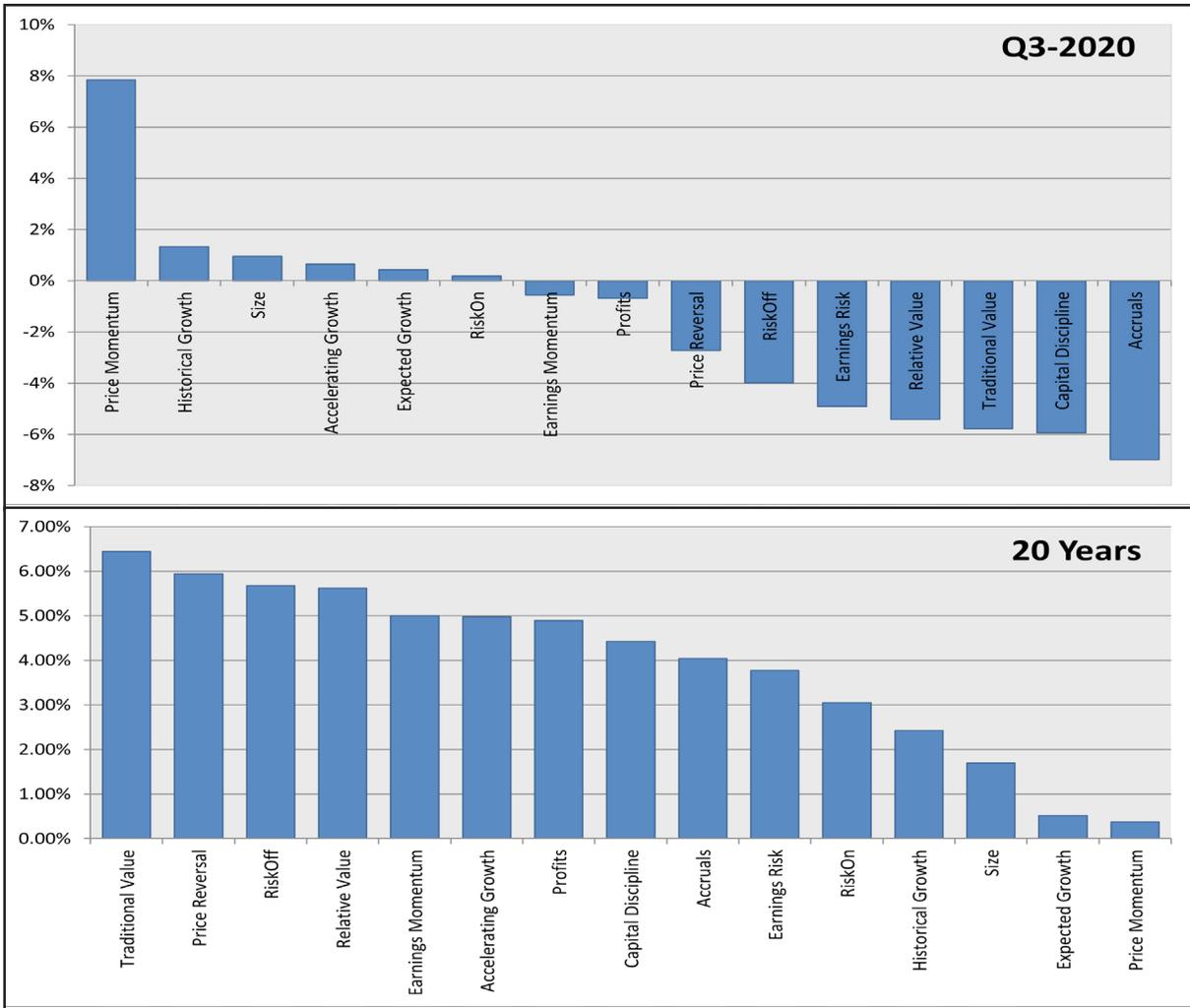
The above table shows that technical factors, such as Price Reversal and Price Momentum, continue to dominate the more recent time periods. Our Price Momentum composite is used for both the long and short ranking process, and includes factors like multi week price movements, percent above 52 week low, and the 4 to 52 week oscillator. Most of these factors are quite straight forward. However, (as is typical in finance) fancy names are applied to make things appear more complex. For example, Investopedia defines an "Oscillator" as:

"...a technical analysis tool that is banded between two extreme values and built with the results from a trend indicator for discovering short-term overbought or oversold conditions. As the value of the oscillator approaches the upper extreme value the asset is deemed to be overbought, and as it approaches the lower extreme it is deemed to be oversold. Oscillators are most advantageous when a clear trend cannot be easily seen in a company's stock such as when it trades horizontally or sideways."

At Convergence, we simply define it as comparing a short-term price with a long-term trend while considering volume. Our 4-to-52 week oscillator seeks to quantify price movement while stripping out short-term price volatility.

The charts below show an analysis of which factors worked in Q3-2020 versus their trailing 20-year returns. These tables show the long-short quintile spread returns (measures going long the highest ranked while being short the lowest ranked stocks within each metric) of all the factor composites we monitor at Convergence Investment Partners. ¹

Factor metrics rewarded by market participants within the US equity markets



As of 09/30/2020. Source: Convergence Investment Partners, Wilshire Analytics. Production Long Q1 - Short Q5.

The third quarter of 2020 was dominated almost exclusively by Price Momentum. Some factors generated significant negative spread in the third quarter, including Accruals, Capital Discipline, Traditional Value and Relative Value. After Price Momentum, there were not many factors that generated a noteworthy positive spread in the quarter. These returns compared to the long-term spread results show how atypical the recent period of performance has been.

¹ These returns are linked monthly spread returns as opposed to the difference between the 3- month long and short holdings.

To better observe thematic changes in factor efficacy, we created the following chart which shows spread returns of 3-month periods over the past 3 years. These are ranked from highest spread return to lowest spread return for each quarter (see the legend below).

	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20
ER	3.96	PM	PM	PM	ER	PR	PM	ER	RON	HG	PR	PM
PT	3.43	AG	AG	AG	SZ	RV	EM	SZ	RV	PM	RV	EM
SZ	2.63	EG	RON	PT	RSK	CD	EG	AG	TV	PT	RON	HG
PM	2.51	ACC	ACC	EM	PT	EM	SZ	PT	RSK	EM	EG	AG
RV	2.37	HG	EG	ER	HG	HG	AG	PR	AG	CD	EM	SZ
TV	1.92	CD	CD	PR	CD	RON	ER	EM	PR	ER	RSK	RON
EM	0.91	EM	RV	CD	EG	EG	HG	CD	SZ	AG	AG	EG
RSK	0.39	ER	HG	HG	TV	ACC	PT	ACC	CD	EG	PM	PT
AG	0.3	PT	PR	EG	RV	AG	PR	RON	EG	ACC	CD	PR
EG	-0.18	RSK	EM	ACC	PR	RSK	CD	RSK	PT	SZ	ACC	ER
HG	-0.38	PR	RSK	RSK	ACC	SZ	RON	PM	HG	PR	HG	RSK
PR	-0.63	SZ	ER	SZ	EM	PT	RSK	TV	EM	RSK	PT	RV
CD	-0.74	RV	PT	RON	PM	PM	RV	HG	ACC	RV	SZ	TV
ACC	-1.6	RON	TV	TV	AG	TV	ACC	RV	ER	TV	TV	CD
RON	-2.03	TV	SZ	RV	RON	ER	TV	EG	PM	RON	ER	ACC

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

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.

FACTOR COMPOSITE RESULTS

Factor Composites (factors) 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 3000 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.