HQAM

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CORPORATE EXCELLENCE INSIGHTS

We are a specialized provider of systematic Quality Investment Solutions and one of the few providers of Quality equity investment strategies worldwide. Corporate Excellence Insight is our monthly publication that includes a brief update on markets and our thoughts about major trends that are impacting the investment management industry.

MARKET UPDATE: TECH COMPANIES LEADING GROWTH

Technology shares surged on stellar profit at Amazon.com Inc. and Alphabet Inc., propelling the U.S. market to record levels. Europe lagged behind as the region continues to wrestle with Brexit negotiation impasses and the potential secession of Catalonia.

$357.50

COSTS TO MAKE THE IPHONE X

The iPhone X smartphone costs $357.50 to make and sells for $999, giving Apple a gross margin of 64%, according to TechInsights, a firm that tears down technology devices and analyzes the parts inside.

10x

EXPECTED ONLINE PAYMENT INDUSTRY GROWTH IN INDIA BY 2020

Online payment industry is pegged to grow ten-fold to $500 billion by 2020. PayPal and Google this year launched domestic online payment operations in India, a market already dominated by China's Alibaba-backed PayTM.

0.005%

PERCENT OF GDP - SHARING ECONOMY SIZE IN JAPAN

Japan has missed the boat when it comes to expanding its sharing-economy sector. Miles behind the U.S. and China, Japan's sharing economy is also smaller than that of other developed economies such as the U.K. and France.

MONTHLY TOPIC: ALTERNATIVE DATA

Technology is transforming investment management just like any other industry during the last few years and, to stay up-to-date, asset managers should increasingly put focus on enhancing their investment processes with data-driven solutions that could substantially improve their results.

Rapid development of cloud-based computing capacity together with machine learning techniques has made it possible to collect, store, process and learn from vast amounts of data, getting actionable insights into development of companies' business trends.

Consumer brands are changing their business models to advertise and sell their goods online and investing heavily in digital marketing and consumer interaction through social media platforms. They promote their products on Instagram, Facebook and Twitter – platforms on which activity can be easily tracked.

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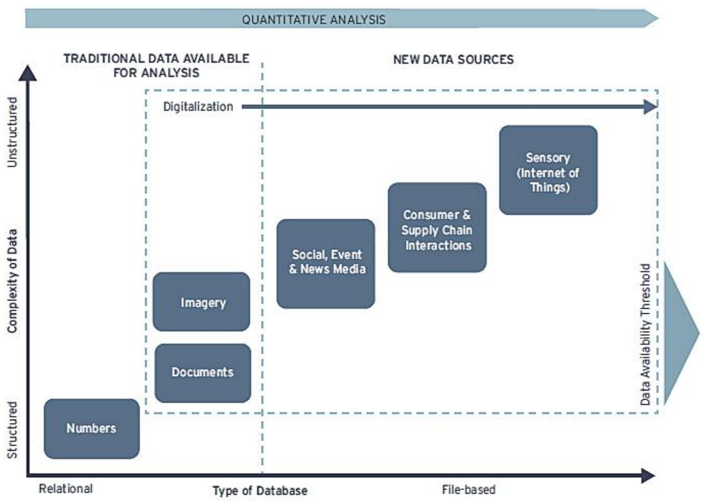
THE SEARCH FOR NEW ALPHA SOURCES

On January 26th, 2017 healthcare giant Johnson & Johnson announced the acquisition of Actelion in a $30 billion all-cash deal – exciting news for the Swiss biotech company's investors, whose stock rose 44 percent six weeks before the publication. But a certain group of hedge funds were particularly happy – Och-Ziff Capital Management, Eton Park Capital Management and Elliott Management, which built substantial stakes in the company based on a rather unusual source of information – tracking the arrivals of the J&J Gulfstream corporate jet at Basel airport, where Actelion headquarters is located.

That is just a one example how money managers losing assets to passive funds are trying to build up an informational advantage to deliver above benchmark returns. An increasing number of investment houses are establishing sizable quant teams managing exponentially rising amounts of data to make better investment decisions.

Data Revolution

The topic started to gain traction in 2015 when Blackrock (link), Citigroup (link) and Goldman Sachs (link) published the first papers outlining frameworks to adjust the investment industry in this new environment. All of them came to the conclusion that traditional sources for analysis - annual reports, company presentations, management meetings and Bloomberg - should be complimented with alternative data from social media, aggregated search results, newsflow sentiment and satellite imagery (or even flight traffic as in the example above), which will become an integral part of the future investment process (see chart below). Rapid development of cloud-based computing capacity together with machine learning techniques made it possible to collect, store, process and learn from vast amounts of data, getting actionable insights into the development of companies' business trends.



Source: Citi Business Advisory Services

Figure 1: Emerging Approach to Data Analysis

Tectonic shift in retail

Amazon, the great disruptor, is putting a tremendous pressure on traditional retail business models – more and more people are less keen on spending their valuable time visiting department stores in search of the items they need to buy. This fact was the major contributor to rising sales of Amazon, Asos, Zalando and other digital platforms. And the stock market is surely responding – Amazon's market value now is bigger than most brick and mortar retailers put together.

Online retail sales growth has been extreme during the last five years almost doubling in size and reaching 14% of total in UK, 13% in US and 12% in Germany. But top position is clearly occupied by China with 16% share with purchases hitting $1 trillion in 2017 due to success of giants like Alibaba and JD.com.

Consumer brands are responding by changing their business models to advertise and sell their goods online, investing heavily in digital marketing and consumer interaction through social media platforms. They team up with celebrities with millions of followers to promote their products on Instagram, Facebook and Twitter – platforms on which activity can be easily tracked.

Use cases and our results

Puma, long-time stock market underperformer, has made a smart move in December 2014 – it signed Rihanna as its new creative director. Why was it a game changer? Rihanna is among the most followed celebrities on social media platforms – 81 million fans on Facebook and 82 million on Twitter. And as the new collection has hit the market end of 2015 – aggregated search activity for Puma exploded and stock price followed.

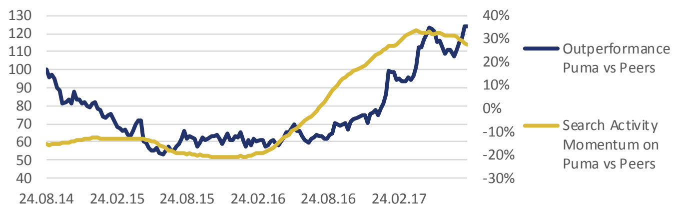


Figure 2: Facebook Fan Engagement vs 1Y Performance (Source: HQAM, Reuters)

Another important metric to follow is how companies engage with its customers online. When a person likes a brand on Facebook – it's already a sign of loyalty, but also their interaction with a page (likes, comments and re-shares) can tell you a lot about the quality of their digital strategy. Just look at the chart below – there is a clear correlation between the engagement (in % of total audience) and 1-year stock performance, one company that clearly stands out is boohoo.com – UK e-commerce phenomenon.

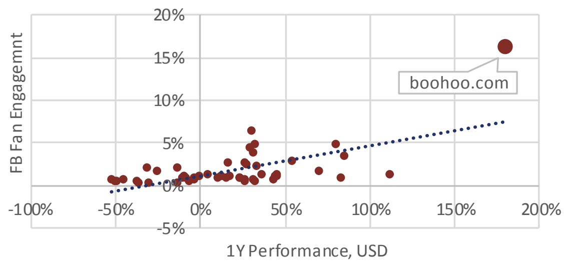


Figure 3: Facebook Fan Engagement vs 1Y Performance (Source: HQAM, Reuters)

HQAM is convinced that this source of information cannot be ignored. Rather it could be a valuable input in addition to a traditional fundamental-based anaylsis. Therefore we have devoted substantial resources to systematically collect and analyze data from multiple alternative sources and combine them in our proprietary platform Astutex. And the results are convincing - companies having biggest momentum in popularity are delivering above average returns generating consistent alpha over the period of last ten years. The chart below demonstrates active return of different quintiles (Q5 being the best and Q1 – the worst) depending on magnitude of the trend.

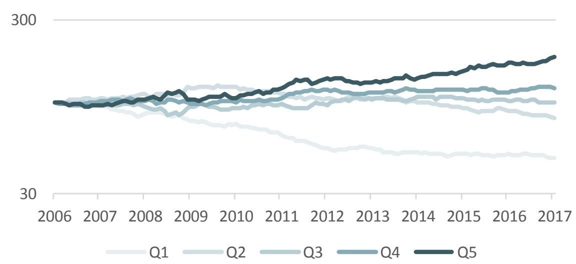


Figure 4: Cumulative Active Return (Source: HQAM, Reuters)