SMART BETA

RISK BASED INVESTMENT SOLUTIONS

GREAT LAKES ADVISORS®
A WINTRUST WEALTH MANAGEMENT COMPANY

OBJECTIVE

The GLA Smart Beta Strategy provides an alternative to market-cap weighting with a risk-based approach to index construction. The strategy seeks to equalize risk contribution of index constituents and to maximize risk diversification while avoiding excessive turnover and portfolio concentration. The approach seeks to provide lower volatility, reduced maximum drawdown, and a higher Sharpe Ratio compared with market capitalization indices over the long-term.

Potential Benchmarks for this strategy:

The default strategy benchmarks are generally the major benchmarks in each market, e.g., S&P 500 for the U.S. fund index. The strategy is benchmark agnostic and can be tailored to specific client goals and preferences.

PORTFOLIO MANAGER

Michael Zhang
Director

Mr. Zhang is the Portfolio Manager of the Smart Beta strategy at GLA. He also leads the efforts on research. Prior to joining Rothschild & Co. Asset Management US, he was a Senior Portfolio Manager at Sensato Investors, a global quantitative hedge fund, managing both Long/Short and Long-Only funds with peak assets of over $2bn.

Michael received a Ph.D., Masters of Engineering, and Bachelor of Science, with minors in Quantitative Finance and Economics, all from the Massachusetts Institute of Technology.

PHILOSOPHY

Our strategy aims to reduce portfolio volatility and maximum drawdown relative to the market capitalization weighted benchmark, without curtailing portfolio performance. Our proprietary risk-based equity strategy analyzes each portfolio constituent’s volatility and cross-correlation on a line-by-line basis.

Traditional Passive Management		Risk-Based	Traditional Active Management	
Equal Weighted	Cap Weighted	Smart Beta	Active Long-Only	Hedge Funds

We focus on two “hidden assets” in the portfolio: volatility and correlation. The methodology used in our proprietary risk engine has evolved from decades of academic and industry research.

We believe that diversification is good, but diversification of risk is even better.

PROCESS

The strategy uses an Equal Risk Contribution (ERC) approach. The key difference is the removal of excess risk from the portfolio:

- We focus not on the allocation of capital, like traditional market-cap strategies, but on the allocation of risk
- Stocks are ranked by their risk contribution
- The riskiest 50% stocks are removed, subject to a buffer rule*, in an effort to remove unrewarded risk
- The remaining stocks are weighted so that each contributes an equal amount of risk to the overall portfolio

The resulting portfolio can be implemented without additional constraints, does not result in security or sector concentration, and does not generate excessive turnover when rebalanced on a quarterly basis. The portfolio also avoids style biases and is highly correlated with the market capitalization weighted index.

On average, our portfolios result in a 30% reduction in volatility, 25% reduction in maximum drawdown, and a 50% improvement in the Sharpe Ratio when compared with market capitalization weighted indices.

Buffer Rule – if an existing holding ranks in the bottom 10% among the 50% highest risk stocks, that stock will continue to be held if already in the portfolio to reduce turnover.*

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