



Nothing Has Changed/Everything Has Changed

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Everything Has Changed, Nothing Has Changed

“The four most dangerous words in investing are 'This time it's different'”

-Sir John Templeton

“Models work when they are appropriate for the particular circumstance, but some of the best investment judgments over time have come when people recognized that models derived in other periods were broken or not directly relevant”

- Abby Joseph Cohen

Which is it?

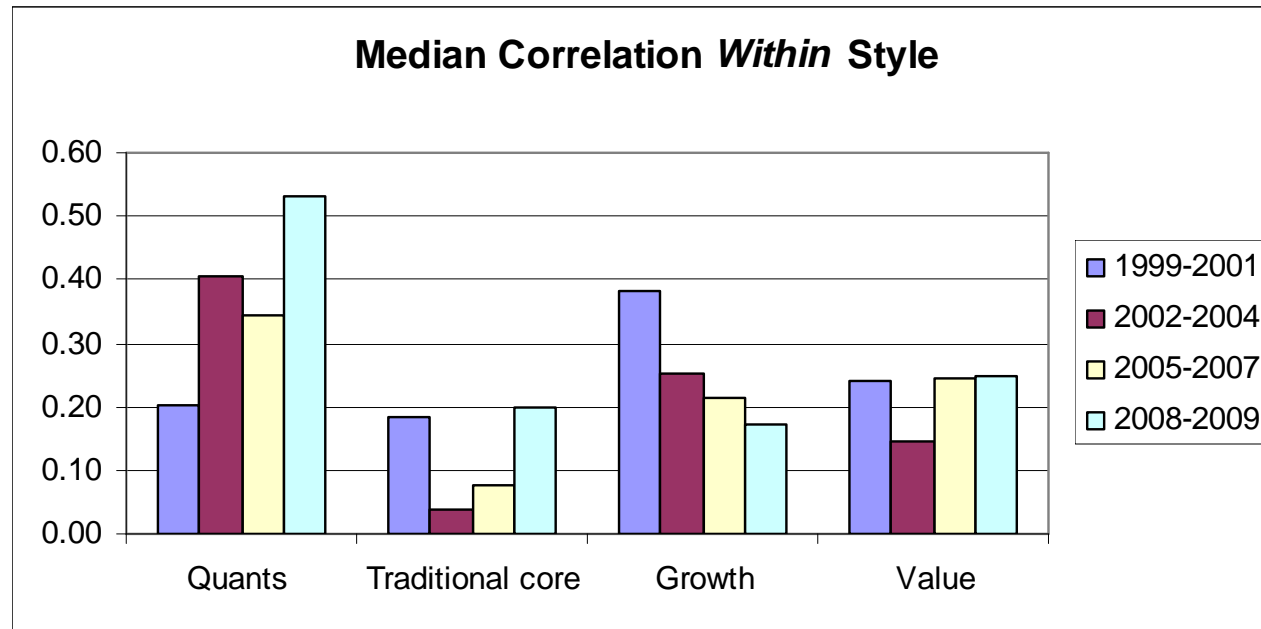
Everything has changed

- Correlations of quant managers have risen
- Common factors' volatility and magnitude has increased
- Increased market volatility after an unusually calm period
- Worst Recession in 75 years
- Asset owners are more fearful of quant

Nothing has changed

- Factor volatility has always been variable
- Models have typically done poorly at market/economic turning points
- Investment styles have always drifted in and out of favor; quant is no exception
- Quant managers still provide a strong diversification benefit

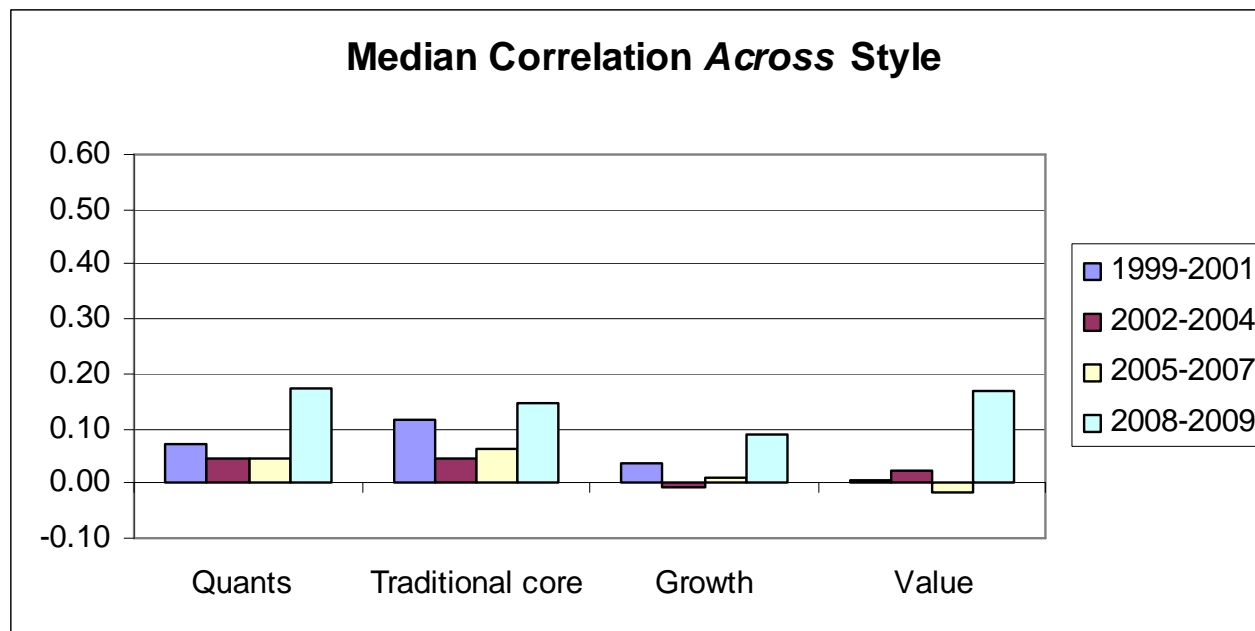
Everything Has Changed: Quant Manager Excess Returns Have Become More Highly Correlated



Quants: 17 well-known quantitative core managers benchmarked to S&P 500. Core, growth and value: based on screen for Active, Fundamental, Tracking Error 3-6, AUM>\$750m as of December 2008 but includes defunct strategies, benched to the S&P 500, Russell 1000 Growth and Russell 1000 Value, respectively. 41 managers fell into the core category, 70 into Growth and 74 into Value. Source: eVestment Alliance.

Everything Has Changed (But Not Just For Quants):

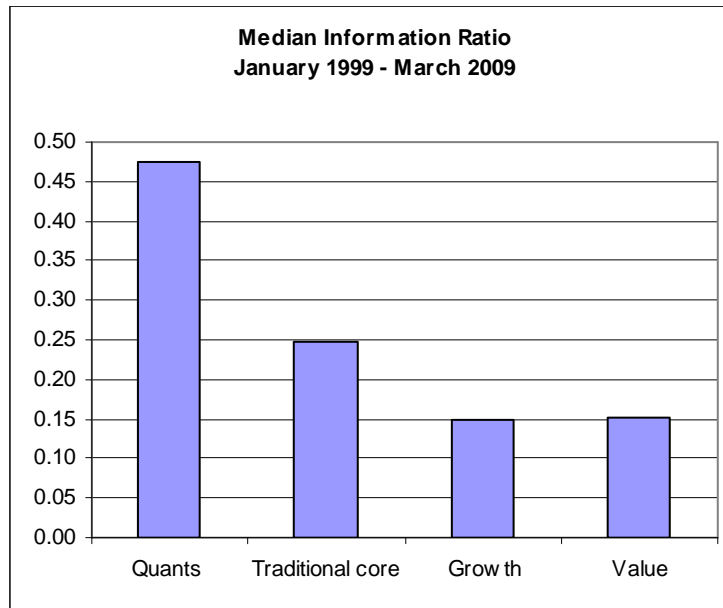
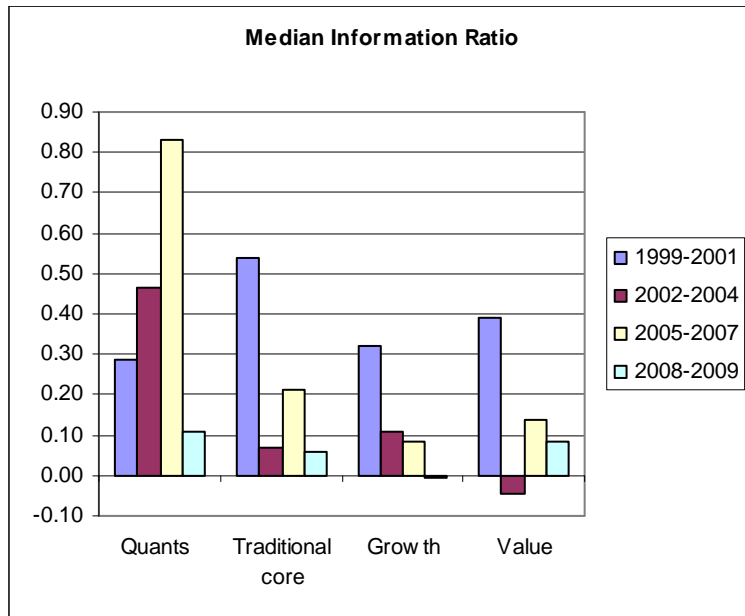
Correlations have increased for all categories of managers, although they remain low
Quants still provide diversification benefit



Correlations are between one style and all the other (e.g, “quant” means quant managers versus traditional core, growth and value managers.) Source: eVestment Alliance.

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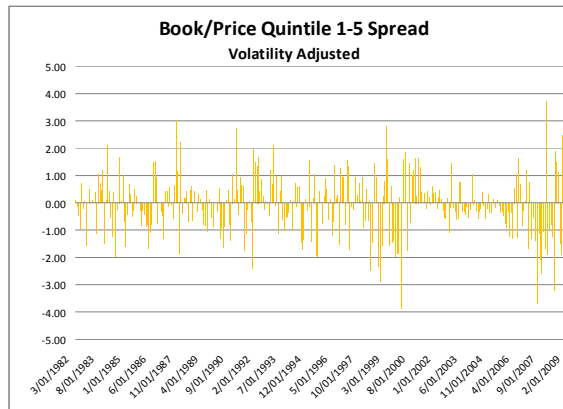
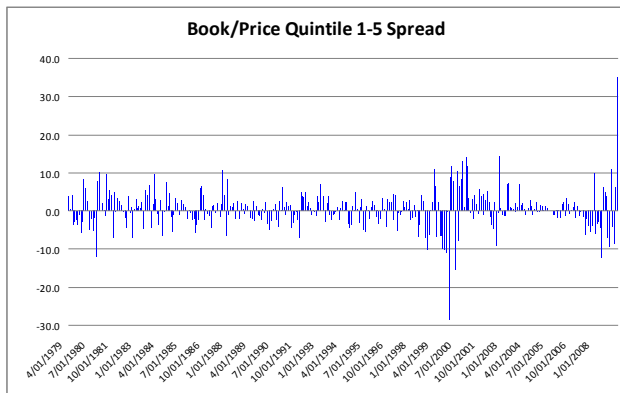
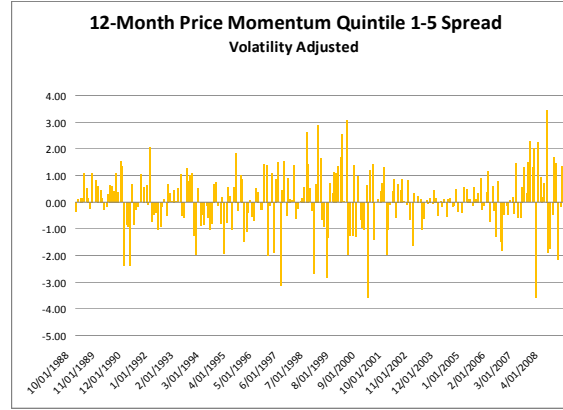
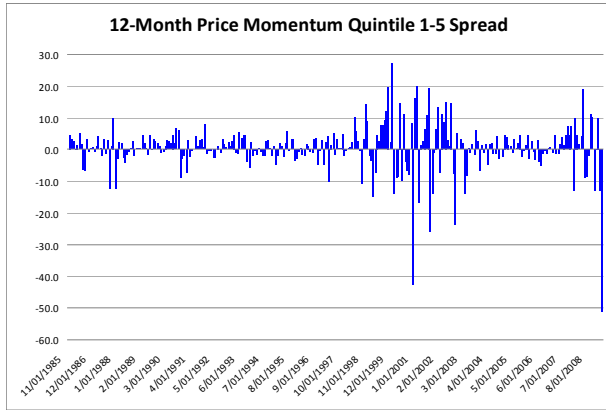
Average Information Ratios Have Fallen Across the Board
And Longer Term Results Still Favor Quants



IR = realized active returns/realized active risk over each time period. Manager returns had to be reported for the full period in order to be included, but didn't need to be reported for any other subperiod. Thus, full period returns have more survivor bias. Source: eVestment Alliance.

Nothing Has Changed:

We've seen models behave poorly before, but infrequently and with smaller magnitude



Universe = Russell 1000. Source: FactSet and AIP Research

Nothing Has Changed:

Statistically, the recent period is very similar to earlier periods

	P-Values	
	Momentum	Book/Price
Equal Periods	0.64	0.76
Last 5 Years vs. Earlier	0.59	0.91
Since Jan. 2007 vs. Earlier	0.68	0.71

Universe = Russell 1000. Source: FactSet and AIP Research

Everything Has Changed:

Yet March 2009 was one of the worst months ever for Quant excess returns

- Quants' average rank in March 2009, relative to their own history, fell in the 8th percentile. None did well.
- April 2003, the prior "turnaround" market, percentile averaged 16 relative to history up to that point. These ranks were worse than in August or November 2007.
- Coming out of the 2003 "turnaround", quant performance was substantially better than the past, and substantially better than other styles'.
- Traditional managers have beaten quants recently, but will they continue to?

Nothing Has Changed/Everything Has Changed: Conclusions

- **High volatility means high magnitude of returns, bigger swings from period to period**
- **Recent poor performance is more likely related to perception of economic/market turn rather than another quant “meltdown”**
- **Quants are more highly correlated than in the past: Are they becoming more similar to each other?**
- **Correlations within each style category and across styles remain low; the benefits of diversification are still apparent**
- **Even with the poor recent period, quants have produced better results over the longer term than other styles**