

ON SECTOR-BASED RESEARCH, MACHINE LEARNING AND ECONOMIC SLOWDOWN

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On the last “Behind the Markets” podcast, Liqian Ren and I were joined by Kelvin Zhang and Peter Boockvar. In the first half of the podcast, Zhang, a partner at AlphaLetters, LLC, discussed sector-based research and the rise of alternative data. Boockvar, the CIO and portfolio manager at Bleakley Advisory Group, followed with a macro-focused discussion and explained his more defensive and [bearish](#) outlook on 2019.

A New Approach

Zhang leads research and product development at AlphaLetters, a quantitative research group that provides stock selection and asset allocation services to money managers. With many of the theories and much of the research in the quantitative field coming from academia, Zhang described AlphaLetters’ unique ability to bridge the gap between academic research and the fund managers who implement ideas.

Zhang said that new alternative data sets are improving quantitative trading strategies—particularly for sector-based work. The more traditional way of analyzing data sets—for example, via trading metrics such as price and [volume](#)—has become a less reliable form of seeking [alpha](#). Zhang explained that with data mining, users can influence a data set to agree with their theory if they are able to manipulate it long enough. These alternative data sets provide a more intuitive and less exploited way of conducting analysis. Examples of data sets can range from looking at the spending trends of a 10-million-person sample of credit card users to using satellite imagery to observe parking lots outside of brick-and-mortar retail chains. Zhang believes this promising form of research will lead to the continuation of increasing trends in “[quantamental](#)” investing, machine learning, alternative indexing and [ESG](#) (environmental, social and governance) factors.

Zhang has also spent a great deal of his time researching foreign exchange (FX) alpha strategies because they can be an effective way to reduce costs, increase returns and lower risk. Again citing academic work, he noted the struggle with FX to be the lack of a centralized exchange and how this has led to interesting findings on the relationships between price swings and trading volumes.

Inflection Point

Boockvar is the CIO at Bleakley Advisory Group, a conventional wealth manager, where he manages a global macro multiasset strategy. Boockvar believes the market currently sits at an inflection point; as the growth scare, rate hikes and trade tensions have faded and the relief rally has run its course, the fundamentals of the market will decide the market’s direction from here. The slowdown in earnings growth in the United States and slowed growth in Europe could start to weigh on the market. In the [S&P 500](#), a level of 2,800 has proven to be a level of resistance recently, and it will be interesting to see if it is able to break through.

Boockvar prefers to hold more dry powder in his portfolios today because this provides more options to invest in attractive situations that could arise.

Boockvar likes gold and silver as a hedge against the weakening U.S. dollar—in addition to emerging market assets and

emerging market local currency bonds.

There is reason for concern in bonds beyond the flat [yield curve](#) because the European Central Bank) and the Bank of Japan may eventually try to get their rates out of negative territory, pressuring global yields, including U.S. yields, higher.

Boockvar warned listeners that the central banks will not be able to bail out the economy in the next downturn as much as they have in the past because there is less room for rate cuts. The [Federal Reserve \(Fed\)](#) wanted to get the [Federal Funds Rate](#) above 3%, and a 200 [basis point](#) drop will not provide much relief during the next recession. This smaller room for error will force investors to pay close attention to valuations going forward.

To listen to our full conversation with Boockvar and Zhang, go [here](#).

For standardized performance and the most recent month-end performance click [here](#) NOTE, this material is intended for electronic use only. Individuals who intend to print and physically deliver to an investor must print the monthly performance report to accompany this blog.

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DEFINITIONS

Bear market : A sustained downturn in market prices, increasing the chances of negative portfolio returns.

Average daily volume : Average dollar amount traded over the course of a single trading day.

Alpha : Can be discussed as both risk-adjusted excess return relative to a specific benchmark, or absolute excess return relative to a benchmark. It is sometimes more generally referred to as excess returns in general.

Quantamental : A portmanteau of the words “quantitative” and “fundamental.” Refers to an investing strategy that is predicated on both quantitative and fundamental research and analysis.

ESG : An acronym for environmental, social and governance, ESG standards quantify the degree to which a company is socially responsible.

S&P 500 Index : Market capitalization-weighted benchmark of 500 stocks selected by the Standard and Poor’s Index Committee designed to represent the performance of the leading industries in the United States economy.

Curve : Refers to the yield curve. Positioning on the yield curve is important to investors, especially during non-parallel shifts.

Federal Reserve : The Federal Reserve System is the central banking system of the United States.

Federal Funds Rate : The rate that banks that are members of the Federal Reserve system charge on overnight loans to one another. The Federal Open Market Committee sets this rate. Also referred to as the “policy rate” of the U.S. Federal Reserve.

Basis point : 1/100th of 1 percent.