

Factor Diversified Balanced Portfolio with High Active Share

We are often asked whether a diversified portfolio with a high number of stocks can beat the benchmark and generate alpha, and does a high number of stocks reflect a lack of conviction? This note attempts to address some of these commonly asked questions.

The pre-requisite for any manager to generate alpha or outperform the benchmark is to have an active share. Active Share is the measure of the percentage of security holdings in a manager's portfolio that differs from the benchmark. A low Active Share score indicates that a portfolio manager is closely replicating the Benchmark (engaging in a passive investment strategy). A high Active Share score suggests that a portfolio's holdings diverge from the benchmark. As a result, managers with reasonably high Active Share have a higher potential to outperform the benchmark.

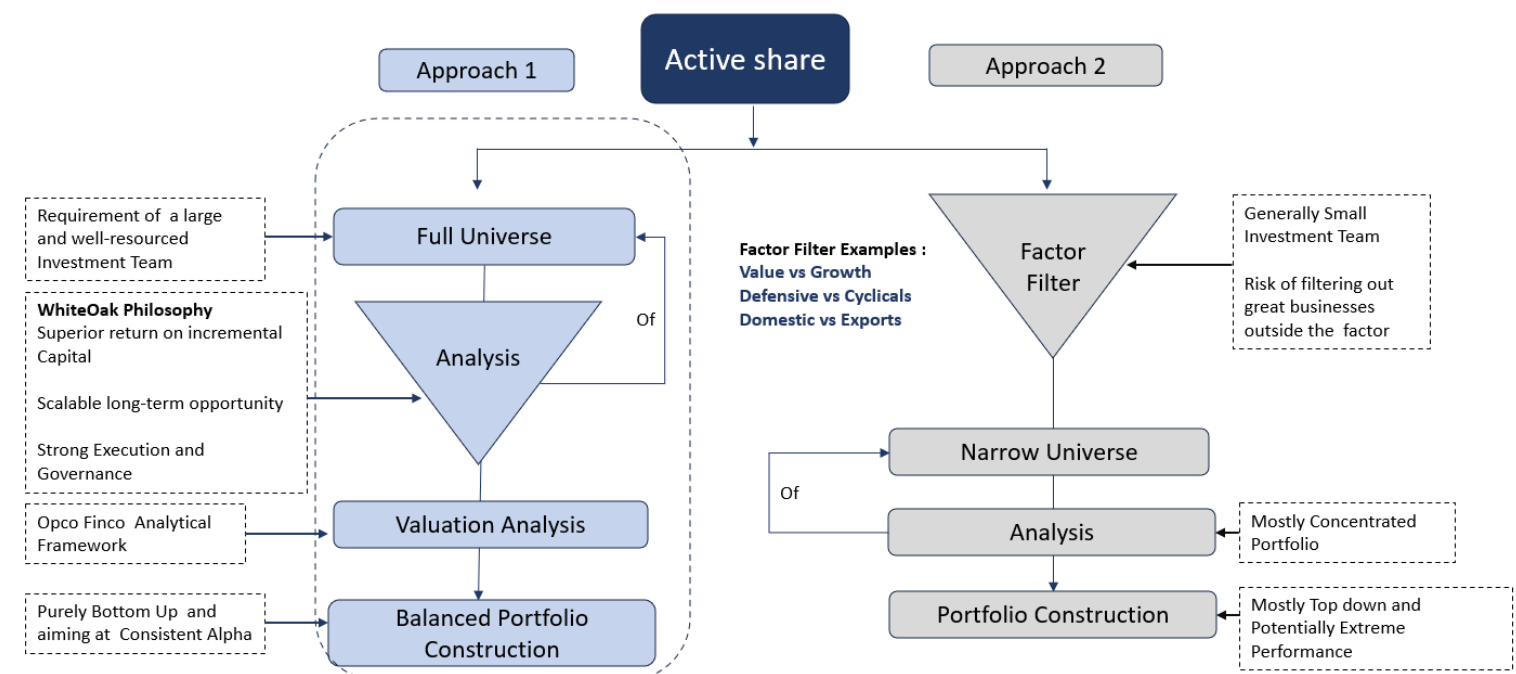
Active positions can be attained either by taking top-down bets or via bottom-up stock selection. A top-down bet entails concentrated exposure along various factors such as growth/value, large/small & mid, defensives/cyclicals, exporters/domestic, etc. Factor performance inherently tends to be volatile and thus the performance of such a portfolio will also be volatile and is likely to swing between extremes.

However, higher active weights generated through bottom-up stock selection is likely to ensure that not only is the alpha generation strong but also consistent and not overwhelmed by factor performance over any reasonable time-period. This has been the case with White Oak's portfolio which has generated peer group leading performance since its inception with lower risk. However, as a caveat, we might choose to tolerate some of these factor risks but only if such risks are more than commensurately compensated by the increased potential for superior stock selection returns.

	Pure Indexing	Factor Neutral	Factor diversified (Balanced Portfolio)	Concentrated Factor bets	Concentrated Stock Picker
Description	Portfolio similar to Benchmark	No Active Factor Bets	Bottom-Up Stock Picking and a Balanced Portfolio Construction Approach	Targeted factor bets along Growth / Value, Large / SMID, Quality / Momentum, Thematic etc	Targeted individual stock bets
Active Risk (Volatility of Alpha)	Zero	Low	Medium	High	Highest
Active Share (Measure of the percentage of security holdings in a portfolio that differs from the benchmark)	Zero	Low	High	High	Highest

A higher active share may also introduce active risk, if the portfolio is constructed based on a narrow strategy such as concentrated top-down factor bets. Conversely, a manager can pursue a higher Active Share without necessarily increasing active risk by following a Balanced Portfolio Construction Approach.

How WhiteOak's approach to create Active Share is different?



As the table below illustrates, White Oak strategy has historically had a high active share even in each of market cap buckets.

Portfolio Component Compared ->	Entire Portfolio	Large Cap Portion of the Portfolio	Mid Cap Portion of the Portfolio	Small Cap Portion of the Portfolio
Index, the Portfolio component compared with ->	S&P BSE 500	S&P BSE 100	S&P BSE Midcap 150	S&P BSE Small Cap 250
Calendar Year	Active Share			
2019	79.6%	78.9%	90.7%	90.2%
2020	65.4%	60.9%	89.1%	88.2%
2021	65.6%	60.4%	85.2%	82.7%
2022	67.3%	63.9%	89.3%	82.7%

Source : WhiteOak

High Active Share in each Market Cap Bucket

Do Number of Stocks in a Portfolio Matter for Alpha Generation ?

- The primary goal of investing is to generate the highest returns or outperformance. Metrics such as 'number of holdings', 'turnover', 'concentration, focus or diversification' are by-products of the investment approach chosen to achieve this goal. Amount of risk taken to generate that outperformance is also an accompanying consequence that must be paid heed to, even if it is not the primary goal.
- At White Oak, we believe that larger number of names provides greater flexibility to generate alpha with possible risk mitigation. To select a large number of stocks is a luxury which we can afford by virtue of our well-resourced. Concentrated portfolios reduce the investible universe which is sub-optimal compared to the much larger universe of companies that we are able to select from.
- For markets like India, the small caps are typically less well-researched and hence more inefficient, thereby providing a more fertile ground for stock picking and strong alpha generation potential. **Moreover, having a well-diversified portfolio allows one to build granular positions as well.** For example, in 2018, our team invested in a specialty chemicals manufacturer when the company's market cap was ~Rs 3,000 crore. Since then, its market cap is up 7x. At the time of the initial investment, it had a weight of ~1% in the portfolio. However, if one is managing a 15-20 name portfolio, there would have been no flexibility to invest 1% in a single name. A 5% holding in 1 stock, as compared to a 1% holding in 5 stocks, where all are expected to compound at a higher CAGR than the broader market, the latter one has an equal potential return with much lesser risk.
- A large number of stocks, to some extent, is a by-product of our balanced portfolio construction approach. We seek to maintain a balanced portfolio reflecting the stock selection capabilities and views of the team rather than being driven by non-stock specific macro factors such as market timing, sector, currency, or other such factor exposures. To a certain manageable extent, we may tolerate some of these factor risks (for example, higher allocation to mid-cap stocks), but only if such risks are more than commensurately compensated by the increased potential for superior stock selection returns. This balanced approach fits exceptionally well with our bottom-up philosophy and process and aligns the portfolio risks to the same.

Granular Positions Can Help Generate Sizeable Alpha

A commonly asked question is how do stocks with 0.5% or 0.6% weightage add to overall performance of the portfolio. There are two things to keep in mind:

- If a stock has 0.5% weight in the Pioneers portfolio it doesn't have to remain there. As corporate performance plays out, as market capitalization and liquidity and breadth of holding rises, nothing stops WhiteOak team from increasing allocation over the years. There was a point in time a specialty chemical manufacturer or a midcap IT company may have been under 0.5% to 1% allocation of the portfolio but ultimately they did go to 3-5% of the portfolio; we still own the chemical company and have exited the IT name quoted above.
- A stock with 0.5% weight may be perceived to add negligible % points to the overall return but if that stock is not part of the benchmark or has much lower weight in the benchmark, what matters is how much alpha it adds. Let us say a stock is 3% of benchmark and 5% of our portfolio a 100% move in the stock will add 2% to alpha; 2% active position in a single stock imparts high active risk and at the same time such a large move is improbable for a large index stock in any year. But if a stock has 0.1% weight in benchmark and 0.75% weight in our portfolio a 100% move will add 0.65% to the alpha, statistically more probable for a portfolio with high number of well researched small and midcap allocations and at lower active risk.

In the table alongside, we have highlighted some of the portfolio stocks which were among the top contributors during the respective calendar years and their weights. As can be seen, we have had positions where the weight of the stock has ranged from <1% to between 5-7%, yet they were the top contributors to the alpha.

Stocks with low exposure may not contribute significantly to overall performance to begin with but contribute significantly to outperformance at all times.

	Total Return	Contribution to Alpha	Min Weight (%)	Max Weight (%)	Port. Ending Weight (%)
CY 2018 (Portfolio Return : 1.3% Alpha : 3.12%)					
Vinati Organics	66.5%	0.9%	0.8	1.9	1.3
Fine Organic Industries	52.7%	0.7%	0.6	2.3	1.3
Mahindra Logistics	18.3%	0.6%	0.7	2.8	0.7
Garware Technical Fibres	19.2%	0.4%	0.5	1.8	1.6
Aarti Industries	31.3%	0.3%	0.2	1.4	1.2
CY 2019 (Portfolio Return : 13.3% Alpha : 4.34%)					
AstraZeneca Pharma	61.2%	1.0%	0.8	3.0	1.2
Coforge	39.2%	1.0%	0.5	7.3	1.8
Dr. Lal PathLabs	59.2%	0.7%	1.0	2.4	1.5
Mindtree	5.4%	0.4%	0.1	7.0	0.0
Trent	27.4%	0.2%	1.0	3.2	3.1
CY 2020 (Portfolio Return : 34.9% Alpha : 16.51%)					
Coforge	72.5%	2.0%	0.3	5.7	4.6
Ipsa Laboratories	92.2%	1.9%	0.9	6.4	0.0
Muthoot Finance	55.8%	1.4%	0.5	3.7	0.0
JB Chemicals & Pharma	83.9%	1.3%	0.7	2.0	0.0
Avenue Supermarts	50.3%	0.9%	0.5	2.7	0.6
CY 2021 (Portfolio Return : 34.4% Alpha : 2.81%)					
Persistent Systems	226.6%	2.5%	1.0	4.2	4.2
Intellect Design Arena	135.6%	1.8%	0.9	3.8	1.9
L&T Technology Services.	141.0%	0.7%	0.9	1.6	1.6
Titan	61.3%	0.6%	0.9	3.8	3.8
CAMS	49.5%	0.4%	0.1	1.8	1.1

Source : White Oak. Year 2018 details are of India Acorn Fund. Year 2019, 2020, 2021 details are for White Oak India Pioneers Equity PMS

White Oak India Pioneers Equity Portfolio Performance

The Portfolio has **outperformed the benchmark by 3.2% CAGR** as of June 30, 2023 since its inception.

Performance (%)	June 2023	3 Months	6 Months	1 Year	3 Year	CYTD 2023	CY 2022	CY 2021	CY 2020	CY 2019	Since Inception	
											CAGR	Absolute
Portfolio	4.6	15.0	7.9	22.6	23.7	7.9	-6.6	34.4	34.9	13.3	17.6	116.1
S&P BSE 500 TRI	4.3	13.2	6.8	24.0	26.4	6.8	4.8	31.6	18.4	9.0	14.4	89.8
Excess Returns (%)	0.3	1.8	1.1	-1.3	-2.6	1.1	-11.4	2.8	16.5	4.3	3.2	26.4

Source: WhiteOak Capital. Inception Date: 27 September 2018. All indices are Net Total Return in INR. Partial 2018 : Performance shown since 27 September 2018 as client monies were managed from this date. Performance is net of all fees and expenses. Performance related information provided herein is not verified by SEBI. Past performance is not a reliable indicator of future results. Returns less than one Year are Absolute Return and more than one year are CAGR. Please note that performance of your portfolio may vary from that of other investors and that generated by the Investment Approach across all investors because of 1) the timing of inflows and outflows of funds; and 2) differences in the portfolio composition because of restrictions and other constraints. Performance relative to other Portfolio Managers within the selected Strategy : [Click Here](#)

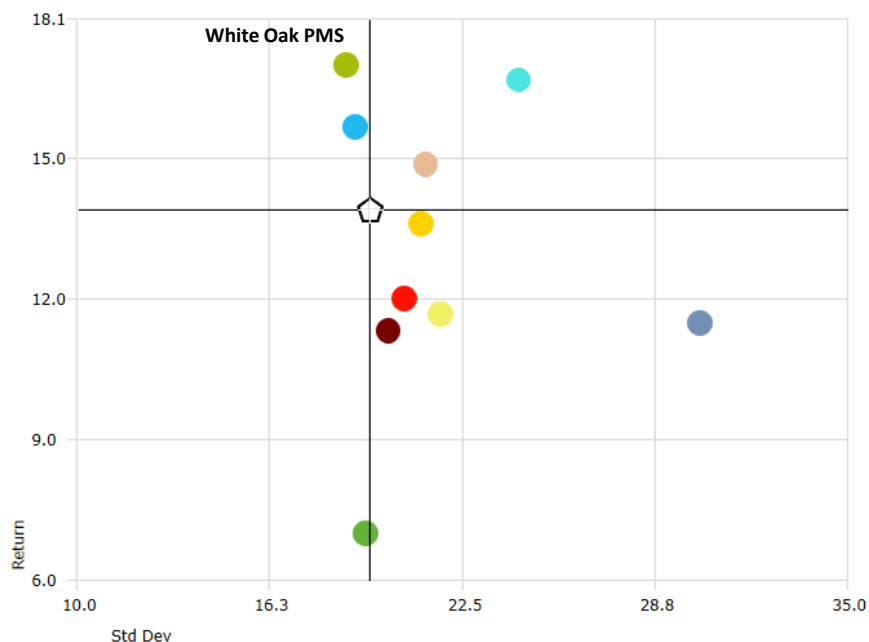
Investing in the stock markets can be a rollercoaster ride, and with so much at stake, making informed investment decisions is essential. One way to do that is by evaluating the performance of the portfolio relative to the risks it has undertaken.

The chart below highlights the Return – Standard Deviation mapping of White Oak PMS vs its Peers. The White Oak PMS has delivered a higher return relative to the underlying risk. We have also highlighted the number of stocks for the competition, which signifies that White Oak PMS delivered industry leading performance despite holding a higher number of stocks relative to its peers.

Risk-Reward - Since WOI Pioneers Eq PMS Inception

Time Period: 01-10-2018 to 31-05-2023

Currency: Indian Rupee Calculation Benchmark: S&P BSE 500 India TR INR



The numbers in the brackets denote the Number of stocks in the Portfolio

- Portfolio 1 (25)
- Portfolio 2 (31)
- Portfolio 4 (24)
- White Oak PMS (67)
- Portfolio 6 (38)
- Portfolio 5 (24)
- Portfolio 9 (18)
- Portfolio 10 (22)
- Portfolio 7 (12)
- Portfolio 8 (25)
- ◇ S&P BSE 500 India TR INR

Since 30 September 2018, Chart Calculation Source : Morningstar. Peer Group source: PMS Bazaar. Peer Group includes benchmark and Flexicap portfolios with AUM over INR 1,950 Cr and three years of investment horizon. Data is till 31 May 2023. The numbers in the brackets denote the Number of stocks in the Portfolios

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