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Satrix SmartCore™

Overview | May 2022

Overview

This document provides a high level description of the **SmartCore™** multi-factor fund's methodology and performance. Multi-factor funds are known by many names, including factor, smart beta and quantitative investment funds. This document sets out to demystify what this means and what it can offer investors.

Factor investing in a nutshell

Factors are features of companies that have shown to make them more likely to outperform peers. This is the same as using measurable height & muscular features to pick players for a basketball team.

Similarly, certain company level features have shown to deliver outperformance over time. **The key** is to objectively define & quantify what these attractive features are. Examples include:

- **Good Value** (based on some comparable price ratio, e.g. Share Price / Book Value);
- **Good Quality** (strong balance sheet, -cash-flow & management style);
- **Strong earnings & price Momentum** (where the market is realising a company's potential).

In fact, we apply multi-factor principles to many facets in our lives:

When buying a house – you consider multiple factors:

- The **Quality** of the house
- Price **Momentum** of other houses in the area
- Its **Value**: whether it is well priced or not

Any one of these attributes alone does not tell us whether a house is a good investment. We need to consider the location, quality of furnishings, price growth in area, safety of area, etc.

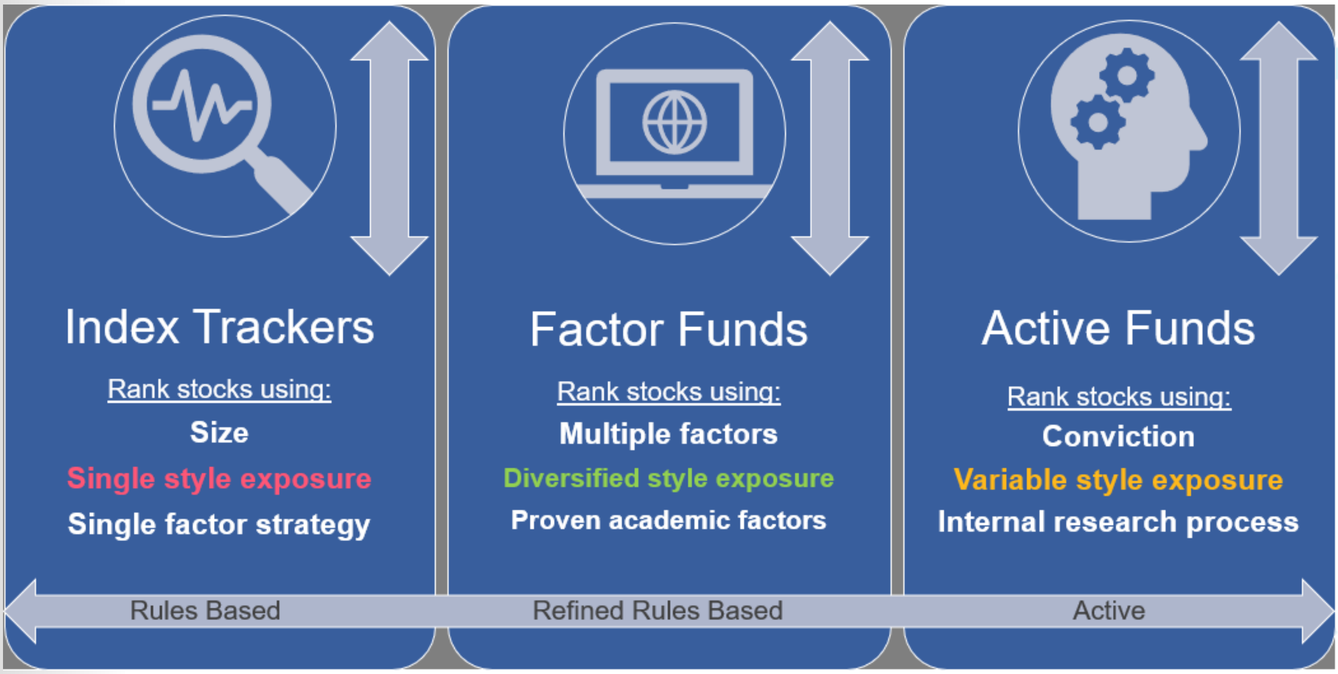
This is factor investing.

Is factor investing a fringe / exotic strategy?

Factor investing is not a fringe or exotic investment strategy at all. Ordinary cap-weighted indexes like the FTSE / JSE Top 40 Index or the S&P 500 Index are in fact all **factor strategies** – the difference is that only a single factor is used: *Size.* The larger the company, the larger its weight in the S&P 500 Index. Simple, intuitive and easy to understand - but still a factor strategy.

Factor strategies, like **Satrix SmartCore™**, expand on these well-known cap-weighted strategies by considering company features proven to be associated with outperforming companies over time (like quantifying good value, strong fundamentals, positive momentum and various other attributes).

> The **active-vs-passive** debate should really be an **active-vs-rules based** debate



From this figure note that both index trackers, or traditional *passive* strategies like the S&P 500 Index, and factor funds, like Satrix SmartCore™, **explicitly** target company factors (such as size, value, quality and momentum features). Active managers in turn target factors **implicitly**, with the focus more on finding individual winners.

Active managers also consider similar factors, but with the added subjectivity that allow them to find the *X-factor.* Factor strategies can then be combined with active managers in a portfolio - allowing investors to have the best of both rules-based and X-factor seeking active managers.

Why Satrix SmartCore™?

Since inception, SmartCore™ has managed to comfortably outperform its benchmark, the FTSE / JSE Capped SWIX. It also managed to outperform the active industry retail median, and achieved top decile performance over the past year. In addition to its stellar performance, it managed to provide clients with the highest aggregate exposure to the Quality, Value and Momentum factor composite.[1]

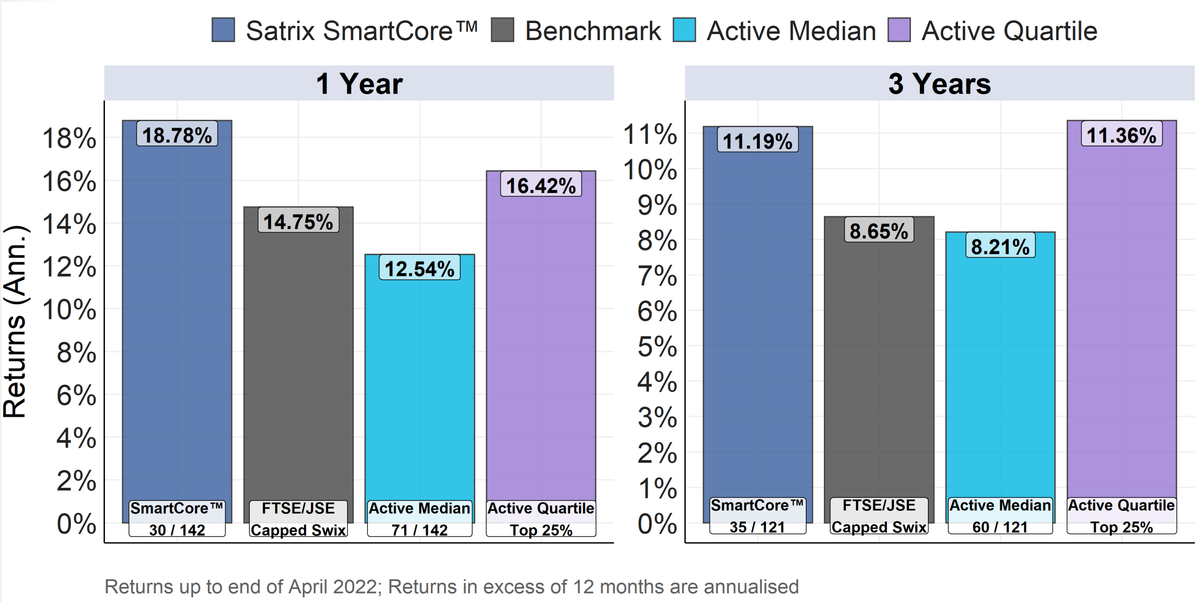


Figure 1: Source: (ASISA) South African Equity General

Why Satrix?

Satrix has been a leader & pioneer in the local factor investing landscape for more than a decade. We offer a wide selection of single factor solutions, including our Satrix Momentum, Satrix Dividend, Satrix Quality, Satrix Value, RAFI 40 & Equal weighted indices.

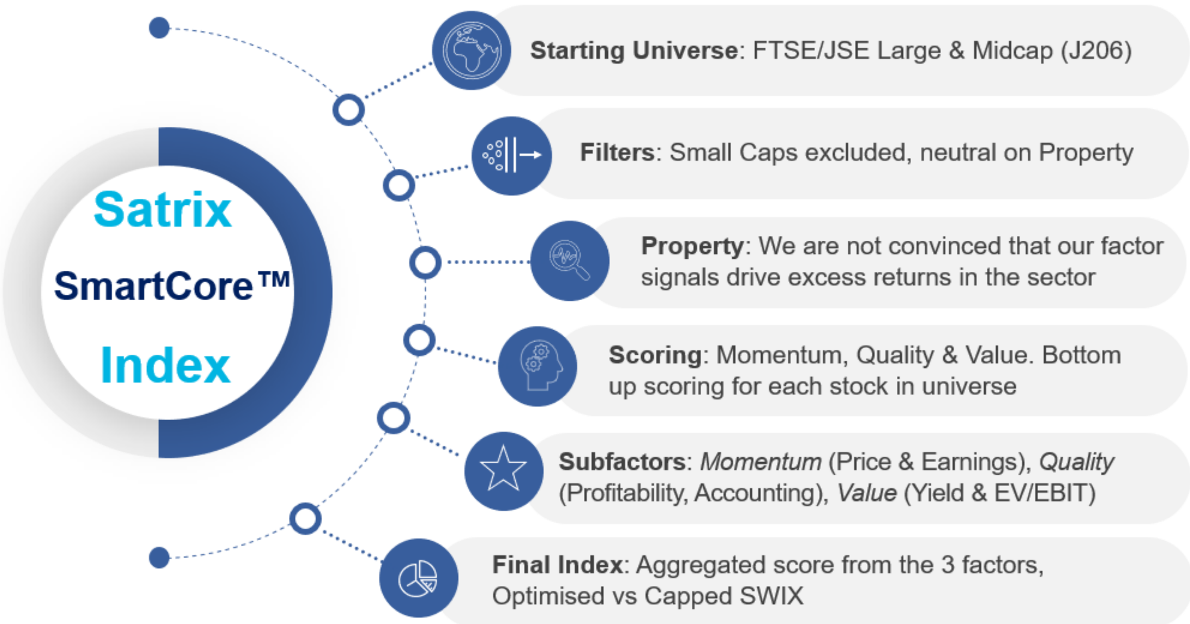
In **SmartCore™**, we offer an attractive multi-factor solution that delivers the potential for enhanced performance within an explicit risk budget. The process of identifying likely outperforming stocks is simplified using a consistent, proven & transparent rules-based framework.

> With **SmartCore™**, investors still get the benefit of low fees and efficiency they have come to expect from Satrix index tracking solutions. The only difference - it considers more than just size.

[1] Our research is based on data from Morningstar as of end of December 2021. We base our analysis on factor information for the mid- and large cap locally listed equities.

SmartCore™ methodology

SmartCore™ is Satrix's flagship equity strategy within our broader factor offering. It offers our clients the best of both: **passive transparency** and **active outperformance** potential. The methodology used to construct the SmartCore™ portfolio is summarised below. As the diagram below shows, the final portfolio remains aware of the benchmark, while diversification is ensured through the use of sector and individual stock capping limits.



Conclusion

For years there's been a popular & polarising debate around *Active* vs *Passive* strategies.

- *Passive* promises low fees & transparency and has shown to be hard to beat;
- *Active* promises outperformance potential, but higher fees are seldom justified with consistent outperformance.

We argue that the active-passive debate is misplaced, and should rather be framed as *active* vs *rules-based.*

From this perspective, factor funds offer an improved rules-based alternative to traditional passive strategies by considering more than just size in construction.

The Satrix SmartCore™ multi-factor solution provides a consistent framework to capture the Quality, Value and Momentum factor premiums on offer - and has proven to deliver value to our clients.

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