Case 3:
Final Portfolio Review

Long-Only U.S. Equity Strategy

Client Name: UTIMCO

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Contents

Client, Mandate, Constraints

CLIENT:

UTIMCO

University of Texas / Texas A&M Investment Management Company

OBJECTIVE

- Generate risk-adjusted excess return relative to the S&P 500

GOAL

- Provide active return while maintaining controlled benchmark deviation

CONSTRAINTS:

- Long-only U.S. equities
- Benchmark: S&P 500
- Target tracking error: 5–20%
- Diversified sector exposure
- Liquid securities only

STOP-OUT RULE

Tracking error exceeds 20%, persistent underperformance relative to benchmark, or concentration risk exceeds internal limits

Strategy Overview

Investment Philosophy: Growth at a reasonable price (GARP)

Portfolio construction balances:

- Growth exposure
- Valuation discipline
- Sector diversification
- Risk management

Differentiation vs. Benchmark

Strategy intentionally deviates from S&P 500 weights while maintaining broad market exposure.

Goal:
Generate alpha without excessive volatility.

Macro Environment

Markets experienced volatility driven by:

- Uncertainty surrounding interest rate path
- Mixed inflation signals
- Geopolitical tensions impacting global energy supply
- Uneven performance across technology sectors

Observed trends:

- AI-related semiconductor demand remained strong
- Energy companies benefited from supply constraints
- Defensive consumer firms demonstrated resilience

Implication:

Diversified exposure improved stability.

Portfolio Construction Process

Security Selection Criteria

Companies selected based on:

- Exposure to structural growth trends (AI semiconductor demand via AVGO, TSM)
- Stable cash flow characteristics to reduce downside volatility (PG)
- Sensitivity to macroeconomic drivers including interest rates and commodity prices (JPM, COP)
- Strong profitability metrics relative to sector peers
- Diversification across industries responding differently to economic conditions

Portfolio Structure

- Balanced exposure across growth, defensive, and macro-sensitive sectors
- Reduced concentration in highly volatile technology sub-sectors
- Adjusted position sizes to manage contribution to tracking error
- Included defensive consumer exposure to stabilize returns during market drawdowns
- Allocated to energy sector to diversify equity market sensitivity

Key Investment Examples

Semiconductor Growth Exposure

AVGO (Broadcom)

- Core supplier of custom chips and networking solutions to major data centers
- Operating margins consistently above 60% with strong free cash flow
- Valuation elevated but justified by earnings visibility and long-term customer commitments

Global Semiconductor Demand

TSM (Taiwan Semiconductor)

- Manufactures chips for every major designer: Apple, NVIDIA, AMD
- Revenue grew 36% in 2025 with expanding margins
- 30% revenue growth guided for 2026; ~27x P/E supported by earnings trajectory

Energy Exposure

COP (ConocoPhillips)

- Direct oil price exposure backed by one of the strongest balance sheets in the energy sector.
- Delivered strong returns while technology holdings underperformed

Diversification and Stability Contributors

Defensive Consumer Exposure
Procter & Gamble (PG)

- Products sit in every home and get repurchased regardless of market conditions
- Generates a remarkably consistent earnings profile through economic cycles
- Provides stability in a technology-heavy portfolio, cushioning against market downturns

Financial Sector Exposure
JPMorgan Chase & Co (JPM)

- Built on decades of disciplined management across multiple revenue streams: consumer lending, investment banking, asset management, and trading
- When rates are high, they earn more on loans. Trading and advisory businesses pick up when markets are active
- Delivers steady returns that technology holdings alone cannot provide

Portfolio Characteristics vs. Benchmark

Portfolio Tilts	Result:
01 Focused on companies with direct exposure to growing AI demand	Captured AI-driven sector momentum while maintaining valuation discipline
02 Added energy exposure through companies positioned to benefit from supply constraints	Provided diversification with energy companies delivering strong returns during periods of supply tightening.
03 Added defensive consumer exposure through high-quality recession-resistant staples	Reduced portfolio volatility during market downturns while maintaining steady returns contribution

Performance Summary:

Evaluation Period:

Jan 20 – Apr 3, 2026

Portfolio continuously outperformed benchmark during a declining market environment.

7.2%

Tracking Error

Cumulative Return

−1.71%

Our portfolio

−4.90%

S&P500

0.82

Beta

+3.19%

Active Return

Risk Metrics

7.2%

Tracking Error

- Portfolio deviated from the S&P 500 enough to create active
- Strategy was different from the benchmark without being extreme

0.82

Beta

- Portfolio moved in the same direction as the market, but with less volatility
- Portfolio maintained equity exposure but avoided excessive sensitivity to market downturns

0.44

Information Ratio

- For every unit of risk taken relative to the benchmark, the portfolio generated 0.44 units of excess return

CAPM Interpretation

Regression results indicate:

- Portfolio returns partially explained by market exposure
- Positive alpha suggests value added through security selection
- Beta below 1 indicates slightly defensive positioning

Conclusion:

Portfolio construction decisions contributed to relative outperformance.

Stress Period Analysis

During the trading period:

- Equity markets declined significantly, likely driven by geopolitical events such as war in the Middle East, interest rate uncertainty, and technology volatility
- Portfolio drawdown was smaller than benchmark drawdown
- Diversification across technology, financials, energy, and consumer sectors

Conclusion:

Outcome aligns with mandate of achieving risk-adjusted excess return, showing downside protection.

Lessons Learned

Lessons:

- Sector diversification improves downside protection
- Position sizing significantly impacts tracking error and risk exposure
- Macroeconomic awareness improves portfolio balance
- Active strategies require patience and longer evaluation periods

Conclusion:

Active strategies require disciplined rebalancing.

Final Recommendation

Strategy demonstrated:

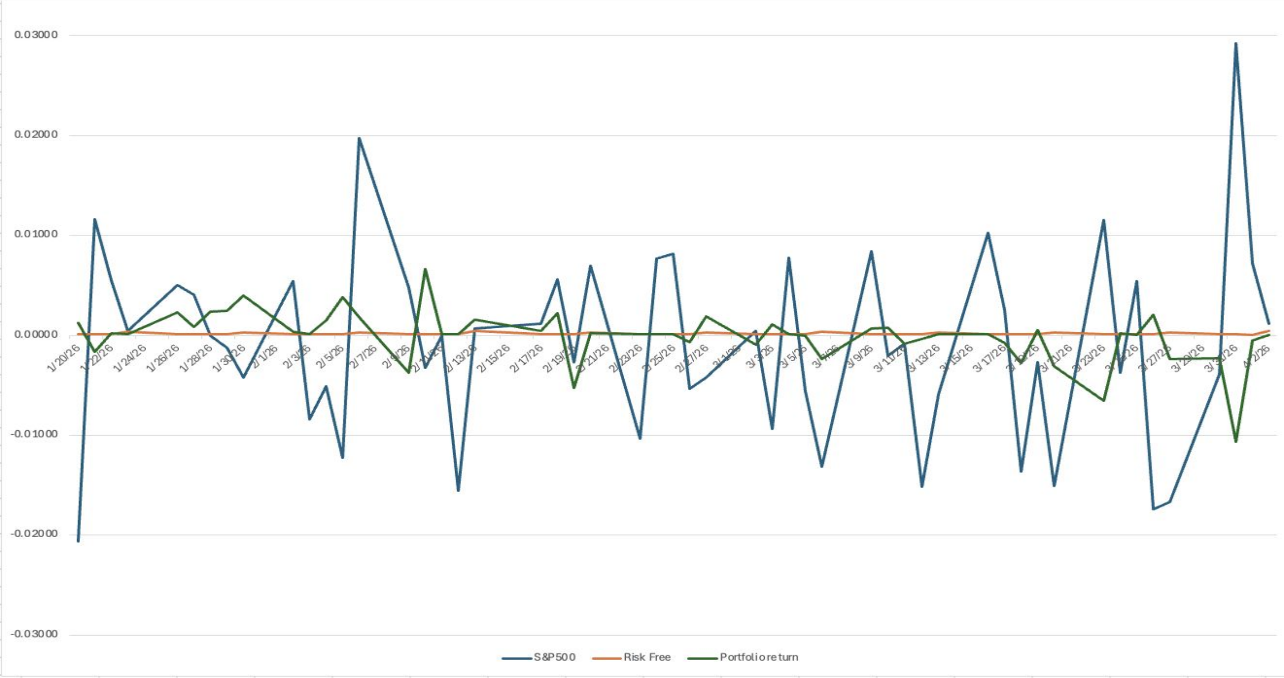
- Positive active return
- Controlled tracking error and market exposure
- Consistent investment philosophy

Further improvements:

- Extend evaluation period to assess consistency of alpha generation
- Continue monitoring sector exposures and concentration risk

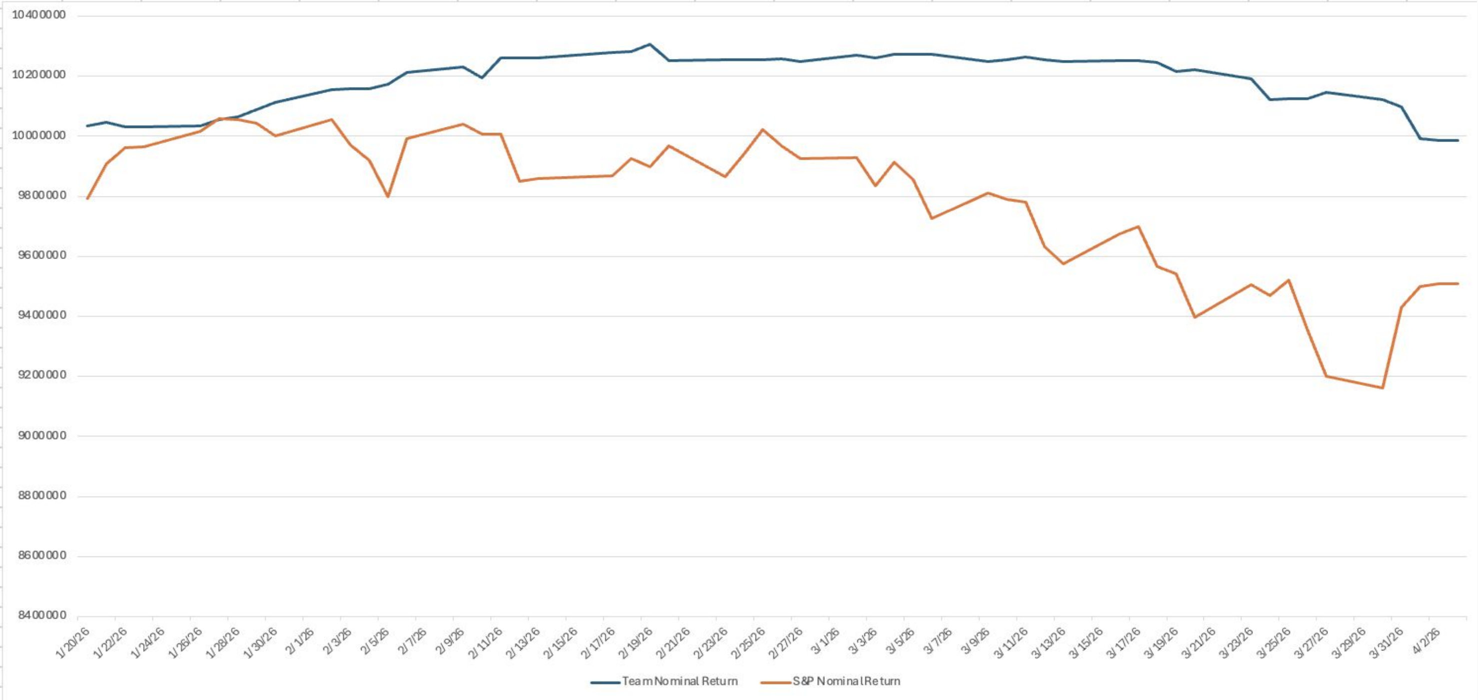
Appendix

Portfolio vs. S&P500 Performance



Demonstrates the higher volatility of the S&P 500 as compared to our portfolio, when looking at daily returns.

Portfolio vs. S&P500 Performance



Demonstrates our total nominal outperformance of the S&P consistently over the course of the evaluation.