

RESEARCH & ANALYTICS

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QSG Boosts Decision Support for Portfolio Managers

NEW YORK — Institutional investment managers researching securities and looking for an industry-specific model that is capable of collecting and handling multiple data points may find just such a tool in QSG, an offering from Quantitative Services Group LLC (QSG).

QSG taps a broad array of data from multiple sources, says Andrew Bertolotti, Managing Director at Quotient Investors LLC, a registered investment advisory firm launched in March 2008, after being developed through a program by CalPERS, the California public employees pension fund, which also invests through Quotient. “We look at the utility industry, utility stocks, and develop a quantitatively based model to forecast price movements within the utility industry,” says Bertolotti. “I use data from different vendors, including QSG, to get information on utility companies,” he adds. “Then internally I formulate my model for the utility industry. We follow a total of 56 industries in the US equity market and I use QSG data to help me analyze each of these industries in the US equity market.”

QSG goes beyond widely used Compustat and IBIS financial data, notes Bertolotti. “What was appealing was that QSG was willing to look at some other data providers,” he says. “They then started looking at sectors through this specific data. For example, they look at the REIT market and look at data specific to REITs, such as vacancy rates and locations — things that are not typically looked at by these more popular databases. That was an interesting direction because I look at industry-specific modeling.”

Madison Square Investors, a unit of New York Life Investments

Management, manages REITs and needed a quantitative model for real-estate securities. “We did not have the capacity to build one,” says Carolic Burroughs, Portfolio Manager at Madison Square Investors. “QSG’s business strategy gathers data from several essential data sources, looks at the properties that the REIT holds and assesses their quality and marketability — where they are located, how those particular markets are doing and what the local economies are in those markets. Those are things that most REIT managers do manually.”

For example, QSG could collect data from multiple real-estate markets throughout the US and assess what each market should look like, aggregating all the information and rating individual REITs based on those local factors, according to Burroughs. “Net asset value [NAV] calculations are based on multiple assumptions,” she says. “There’s always a wide range of what these values are. In other words, a confidence interval is very wide. When I back-tested QSG’s data, I found it had a fair amount of predictability. This is not something you would find in a traditional equity market stock selection model.”

Within QSG’s Virtual Research Analyst product, Madison Square Investors could obtain overall model results for a REIT model, factor-specific results (for eight factors) and sub-factor specific results. “QSG’s website provides the functionality to construct and back-test a custom model, using any of these components,” says Burroughs. “This is beneficial in the short term because it can help investors to identify what the stock market is currently rewarding. In the long run, this type of analysis helps adjust the weights and/or factors in the model such that it keeps up

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in different market regimes.” Valuations of real-estate securities depend on the fundamentals of the real-estate market as much as company-specific fundamentals, she adds.

“REITs are very interesting stocks,” says Burroughs. “Sometimes they move with the stock market, sometimes they move with the real-estate market. Sometimes when you know the real-estate market is dominating you can look at the factors and see which are more specific to real-estate, pull those out and use them to tell you what the market is rewarding at this particular point in time. There’s the ability to analyze the data quite extensively or not. There may be firms that just use the overall score and that’s all, and there may be firms that look at the components and sub-components and use it differently.”

QSG, based in Naperville, Ill., near Chicago, was founded in 2001, and offers five separate research and modeling products: QSG Edge, a daily ranking service; Pre-Trade Analyst; Factor Analyst; Virtual Research Analyst and T-Cost Pro, which analyzes the cumulative impact of a series of transactions in a stock.

“As long as data has been available, investment professionals have sought to use historic data to come up with strategies that will outperform the market,” say Tim Sargent, President and Chief Executive Officer of QSG. “One of the challenges of using historical data is the assumptions that have to be made to be able to do that. One of the largest assumptions made in any back testing is the assumption that you would have been able to achieve the prices in the market on the day you set pricing for performance purposes. The problems encountered in that kind of testing is that everyone recognizes that’s not quite right — that if you actually go to

market and make a demand for liquidity you’re going to change the prices. A big question is how much.”

QSG developed its products by addressing the difficulty of making stock-specific cost considerations in back-testing. “We used almost eight years’ worth of research,” says Sargent. “We reached the point where we’re comfortable that we can forecast the impact or footprint you create when you establish a position in a particular stock. What’s novel about what we created is the ability to take that perspective and work it back in time through this back-testing.”

QSG begins with a few critical factors for a stock — its classification, volume and volatility, according to Dan Bukowski, Director of Research, QSG. “Is it a deep value stock or an earnings momentum stock?” he says. “Secondly, what is the particular volume that we’re trying to buy relative to the day’s volume? Third, how volatile is that stock? What is the volatility or range it’s traded in over the last few days? Taking those components, we hope to direct the trader to which algorithm is best suited to work their order for that stock.”

QSG’s products can recommend position sizes to users, according to Sargent. “We arrive at a very specific impact charge that we follow for our clients through our different trading solutions,” he says. “We really look directly at that charge and aggregate it on a name-by-name basis.”

Quotient Investors, which uses QSG’s Factor Analyst and Virtual Research Analyst, found that they became like a research partner, according to Bertolotti. “They help my efforts by leveraging what I can do, by looking at some things that I’m not looking at,” he says. “They became more than just a data provider.” □