



The Argent Mid Cap Portfolio:

A balanced blend of quantitative and fundamental processes

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Executive Summary

Roughly half the alpha generated in the Argent Mid Cap Strategy is due to our proprietary quantitative model, and the other half is due to our disciplined fundamental approach to investing in good businesses. The following pages detail a study in which we created a Simulated Argent Mid Cap Strategy and a Pure Quant Monte Carlo Portfolio. Through this analysis we demonstrate that we are able to generate meaningful and consistent outperformance versus both the benchmark and the Pure Quant Model Portfolio.

Introduction

Since its inception, the Argent Mid Cap Strategy has been successfully managed using a blend of quantitative and fundamental investment processes. A fair question, and one that we are often asked, is how much of the strategy's alpha is attributable to our quantitative efforts compared to our fundamental process? Based on Monte Carlo simulations, the short answer is that roughly half the alpha is due to our proprietary quantitative model, and the other half is due to our disciplined fundamental approach to investing in good businesses.

Argent's proprietary quantitative model is the basis of the Argent Mid Cap Strategy's investment process. Called the "Argent Alpha Model," it generates a list of buy and sell candidates. The portfolio manager then applies fundamental analysis to select a handful of securities from these dynamic lists.

In our analysis we used the Monte Carlo simulation technique to produce an estimate of Mid Cap Strategy performance resulting from implementing a purely quantitative investment process. We then compared this simulated performance to the actual performance of the Argent Mid Cap Strategy, and found that its combination of quantitative and fundamental analysis outperformed a purely quantitative process relying solely on the Argent Alpha Model.

What is the Argent Alpha Model?

The Argent Alpha Model is a dynamic, 25 factor tool that ranks stocks from 1(best)-10(worst) via factors that are grouped into four main categories. The factors are categorized in groups for research reasons as those within each group tend to correlate with each other more than they correlate with the other groups. The individual factor weights are then summed to determine the weight of each of the four categories. The baseline weight of each group is 25%. The group weights can range from 10% to 40%. The universe of mid cap stocks is then ranked by decile from best to worst (see Figure 1). Historically, the approximately 400 stocks in deciles one through three outperform the universe by 270 basis points on an

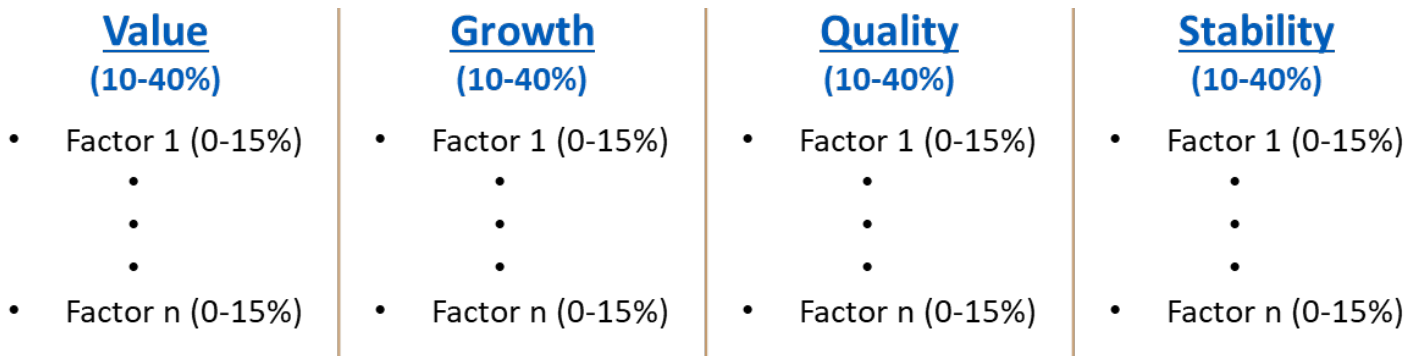
annualized basis. Stocks that rank in the top 30% of the Argent Alpha Model are candidates for further review. A more in-depth discussion of the Argent Mid Cap Strategy can be found in the Appendix.

Our Study

We created two testing portfolios for our study. The first portfolio we call the Pure Quant Monte Carlo Portfolio. To create this portfolio we collected the historical model rank values for the Argent Mid Cap investable universe, which were used to generate pools of candidate stocks for purchase and sale over the history of the strategy. The Monte Carlo simulation performs repeated trials of a portfolio construction process. The simulated portfolio executes stock transactions according to fixed

Figure 1:

Individual factor weights are summed to determine the weight of each of the four categories. The baseline weight of each group is 25%. The group weights can range from 10% to 40%.



Factor weights are customized by sector and have a baseline weight of 4% that can range from 0-15%.

Factor weights are dynamic and fluctuate as market conditions change.

Our Study (cont.)

quantitative rules based on historic model score values, with turnover and portfolio size consistent with the Argent Mid Cap Strategy over its history. We randomly select individual securities from the “buy lists” generated by the model, and perform a similar random selling of portfolio securities with low model scores (the “sell list”). The simulated portfolios begin by buying stocks at random from the initial buy list. We average the performance of a single simulated portfolio with many other distinct simulated portfolios to form an average performance for the Pure Quant Monte Carlo Portfolio.

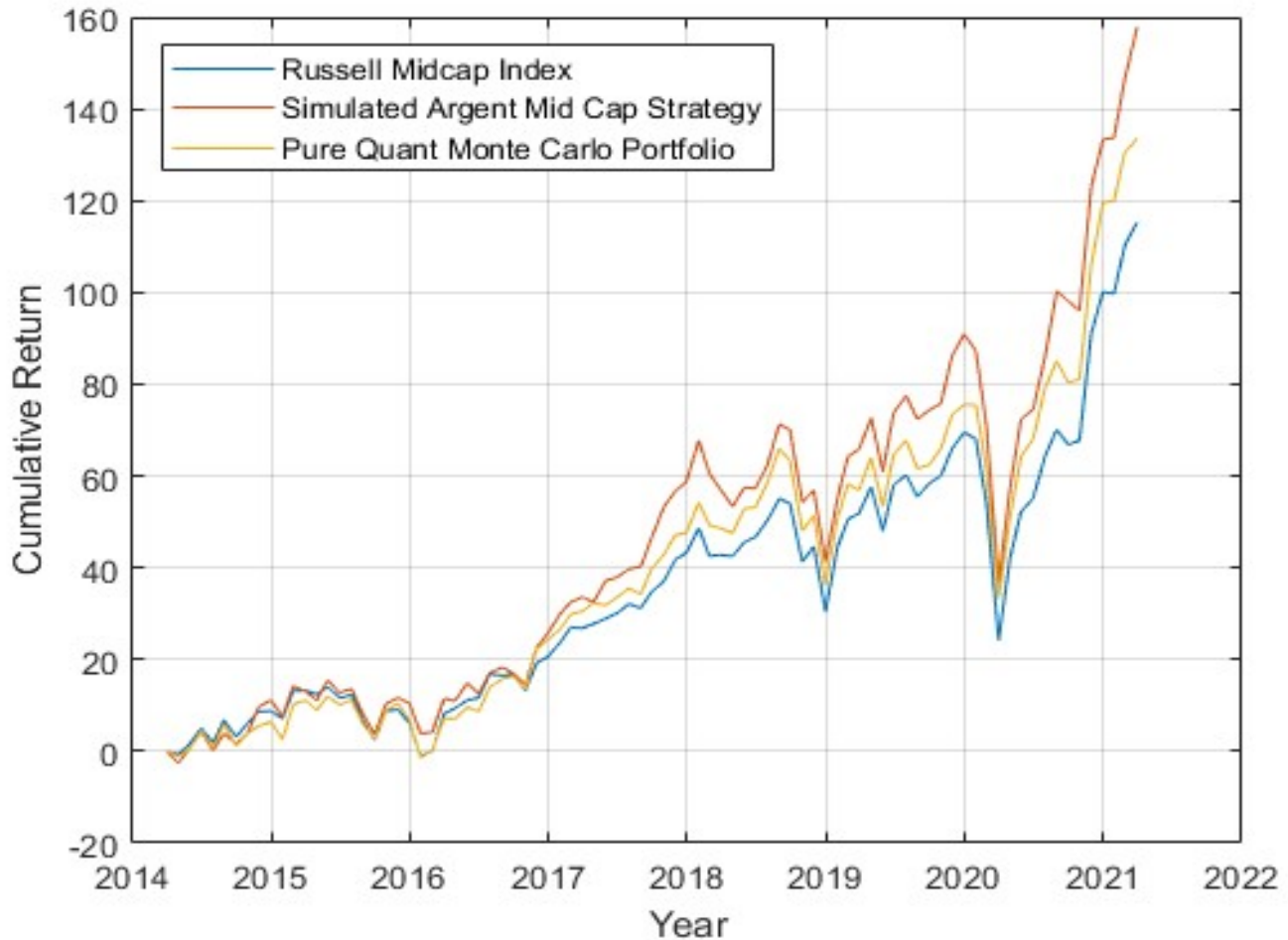
The second portfolio we call the Simulated Argent Mid Cap Strategy. To generate the performance of this portfolio we use the month-end holdings of the Argent Mid Cap model portfolio to calculate the performance on a monthly buy-and-hold basis.

The Results

The cumulative return results are shown in Figure 2, in which the blue line represents the performance of the Russell Midcap Index, the yellow line represents the performance of the Pure Quant Monte Carlo Portfolio, and the red line represents the performance of the Simulated Argent Mid Cap Strategy. In looking at the chart it is clear that the Simulated Argent Mid Cap Strategy, with its combination of quantitative and fundamental processes, has outperformed both the Pure Quant Monte Carlo Portfolio and the Russell Midcap Index. Moreover, the Pure Quant Monte Carlo Portfolio lies roughly midway between the benchmark and strategy for most of the time frame under consideration.

The Results (cont.)

Figure 2: Comparison of the Simulated Argent Mid Cap Strategy performance versus a Pure Quant Monte



The Results (cont.)

Table 1 shows the parameters and comparative results of our Monte Carlo simulation. The Pure Quant Monte Carlo Portfolio generates a return of 12.8%, outperforming the Russell Midcap Index by 1.2%, or 120 bps of annualized outperformance over the 7-year period from 3/31/2014 to 3/31/2021. Importantly, this result represents the average of 1,000 individual portfolio simulations. The individual portfolio

simulations are directly comparable in portfolio size, turnover, and sampling frequency to the Simulated Argent Mid Cap Strategy and represent an idealized performance with zero transaction costs and monthly sampling. The Argent Mid Cap Composite results, provided only for reference, are GIPS-compliant and account for implicit transaction costs and daily cash flows.

The Results (cont.)

Table 1: Performance and Monte Carlo parameters

Parameter	Value
Start Date	3/31/2014
End Date	3/31/2021
Buy Rule	Top 3 Deciles
Sell Rule	Bottom 5 Deciles
Number of Repeated Trials	1000
Sampling Frequency	Monthly
Portfolio	Annualized Return
Russell Midcap Index	11.6%
Pure Quant Monte Carlo Portfolio	12.8%
Simulated Argent Mid Cap Strategy	14.5%
Argent Mid Cap Composite (Gross of fees)	13.7%

Conclusion

The Simulated Argent Mid Cap Strategy consistently outperforms both the benchmark and the Pure Quant Monte Carlo Portfolio returns. The reason is Argent's fundamental security selection process adds value above that of the "Pure Quant" model approach. While most quantitative managers struggle to meet performance levels generated by their back tests, we ascribe the Simulated Argent Mid Cap Strategy performance over the Pure Quant Monte Carlo Portfolio simulation to Argent's fundamental security selection processes.

By seeking to own good businesses with above-average profitability, generating above-average cash flow and with management teams that are good stewards of capital, we are able to generate meaningful and consistent outperformance.

For more information about Argent's Mid Cap portfolio or other strategies, contact **Kirk McDonald, CFA—Portfolio Manager, Argent Mid Cap Strategy** at: (314) 725-6000 or kmcdonald@argentscapital.com.



Appendix: Argent's Mid Cap Strategy Stock Selection Methodology

Argent's Mid Cap strategy utilizes an integrated blend of quantitative and fundamental research to identify opportunities to purchase ownership stakes in good businesses undergoing positive internal or external change. We seek to own these companies for the long term. Argent believes that companies undergoing positive change, driven either by internal or external factors, frequently experience underappreciated growth. We believe that good businesses are those that exhibit above-average profitability, generate above-average cash flow and have management teams that are good stewards of capital.

Argent's Mid Cap process begins by screening the approximately 1,500 companies with market capitalizations in the range of the Russell Midcap Index and market liquidity of \$20 million. The resulting universe is 1,200 mid cap companies with acceptable trading volume. This universe is then screened by our proprietary quantitative tool. The Argent Alpha Model is utilized to point the team toward the right companies, in the right sectors, at the right time with positive change.

The Argent Alpha Model is a dynamic, 25 factor tool that ranks stocks from 1-10 via factors that are grouped into four main categories. The factors are categorized in groups for research reasons as those within each group tend to correlate with each other more than they correlate with the other groups. The four factor categories in the Argent Alpha Model are the following:

Value

Value factors measure whether a stock is rich or cheap compared to other stocks in its sector. An example of a value factor in the Argent Alpha Model is price to free cash flow. Value factors tend to work best during those periods characterized as "value" markets.

Growth

Growth factors measure how fast a stock's sales, earnings and cash flows are growing relative to other stocks in its sector. An example of a growth factor in the Argent Alpha Model is our proprietary measure of unexpected cash flow from operations which identifies companies generating a higher cash flow from operations than in the past. Growth factors tend to work best during those periods characterized as "growth" markets.

Quality

Quality factors measure the quality of a company's earnings, balance sheet and stewardship of capital. An example of a quality factor in the Argent Alpha Model is cash flow return on assets. Quality factors tend to work best during those periods characterized as "quality" markets.

Stability

Stability factors are a differentiator for the Argent Alpha Model and are one of the things that makes it unique. The Stability factors march to their own beat and exhibit low correlation to each other and low correlation to the factors in the other three groups. These factors provide the model with stability and help ensure it performs well in any market cycle. Examples of Stability factors in the Argent Alpha Model include proprietary measures of a company's stewardship of capital and factors utilizing Natural Language Processing of corporate communications.

Factor weights are customized by sector and have a baseline weight of 4% that can range from 0-15%. Factor weights are dynamic and fluctuate as market conditions change. Dynamically weighting the factors ensures the model remains aligned with current market conditions and adjusts as market conditions change. The individual factor weights are then summed to determine the weight of each of the four categories. The baseline weight of each

group is 25%. The group weights can range from 10% to 40%. To calculate the final Alpha score of a potential investment, the factor scores are summed for each of the 25 factors. The universe of mid cap stocks is then ranked by decile from best to worst. Historically, the approximately 400 stocks in deciles one through three outperform the universe by 270 basis points on an annualized basis. Stocks that rank in the top 30% of the Argent Alpha Model are candidates for further review.

When a potential investment demonstrates an attractive Alpha Model score, we selectively identify stocks for further research using a process designed to point us toward the right sector. For stocks that rank in the top 30%, we confirm that the factors that are working for each company score are also working well in its designated sector. We also utilize HOLT financial software to further shape the buy list to include only those stocks that have a history of consistently earning returns above their cost of capital, and where management has a proven track record of being good stewards of capital. Approximately 150 companies make it through this portion of our selection process.

Once we have identified the right stocks in the right sector, we work to identify the right time to invest in the stock. To determine the right time, we check the Argent Alpha Model's historical accuracy tracking a stock. Stocks that track well in the Model move to the top of the buy list. Once that list of approximately 25 companies is established, we utilize our proprietary Market Cycle Model to confirm that the potential buy candidate reflects the style characteristics that are working well in the current phase of the market cycle or will perform well in the next market cycle. The Argent Market Cycle Model divides the market into four phases based on the change in economic growth rates:

1) Recovery: the year-on-year rate of change is negative but accelerating

2) Expansion: the year-on-year rate of change is positive and accelerating

3) Slowdown: the year-on-year rate of change is positive but decelerating

4) Contraction: the year-on-year rate of change is negative and decelerating

Where we are in the market cycle dictates the style orientation of the portfolio. Based on the Market Cycle Model, the portfolio moves within a risk-controlled band of value, growth, economic sensitivity, and quality relative to the Russell Midcap benchmark. Two-thirds of the holdings in the Argent Mid Cap portfolio are positioned for the current market cycle and one-third of the portfolio is tilted to take advantage of the next phase of the market cycle. While the Argent Mid Cap has style tilts based on the Market Cycle Model, the strategy maintains a decidedly core orientation.