# Berunda Capital: Key Differentiators

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**Prepared For:**
Information Purpose only

# How is Berunda different from other advisors?

Berunda Capital Management ("Berunda") is a FINRA registered financial advisor located in the US. There are over 32,000 investment advisors in the US. We are then often asked a question from our prospects: So how are we different?

First, we are an ***independent, fiduciary and 100% fee only advisor***. And of course, some advisors do fit that category as well, but not most. We typically advise our prospects to do their homework in terms of independence and fee-only advisors and some are often surprised that most large well-known brands are neither. We are also not a broker-dealer generating trading commissions or money selling third-party products to you.

**Independence, Fiduciary, Customized Portfolio Risk management and our unique investment processes are our key differentiators**

Second and more importantly, we believe that ***every investor requires a customized portfolio to reflect their unique investment objectives***. One of the major steps in the investment process is for the advisor to determine the investor's investment objectives and risk appetite. However, Berunda differs from other advisors in our approach to invest our client's funds to meet their investment or wealth targets in that there are no pre-determined simple model portfolio choices but an overall risk-budget or tolerance to manage your wealth.

Finally, and this is perhaps the most important: We have a ***unique investment process that manages your downside risk better***. That is, we make our own successful investment recipe using stocks, bonds and ETFs and completely avoid mutual funds. This is a key differentiator and most advisors are NOT equipped to deliver this feature to clients. We are unlike most advisory firms that collect advisory fees from clients by simply allocating to funds. And then collect distribution fees from mutual fund firms by serving as a simple static asset allocator of these funds.

**We also avoid mutual funds and typical diversification strategies by market cap and help manage client risk better**

The above last point of ***not using mutual funds*** and focusing on dynamic asset allocations are significant differentiators for us and deserves further discussion. We believe mutual funds simply add another layer of fees. Let us now look closer at the mutual fund industry and why we stay away from mutual funds and a typical diversification strategy for our clients:

(1) Historical actively managed ***mutual fund performance data are not encouraging***, showing significant under-performance across time.
(2) ***Typical diversification across market capitalization is useless***: Diversification of investor portfolio through various market cap and value/growth classification of mutual funds may actually mimic the broader market rather than provide some risk mitigation. We show here that diversification across asset classes may be more beneficial.

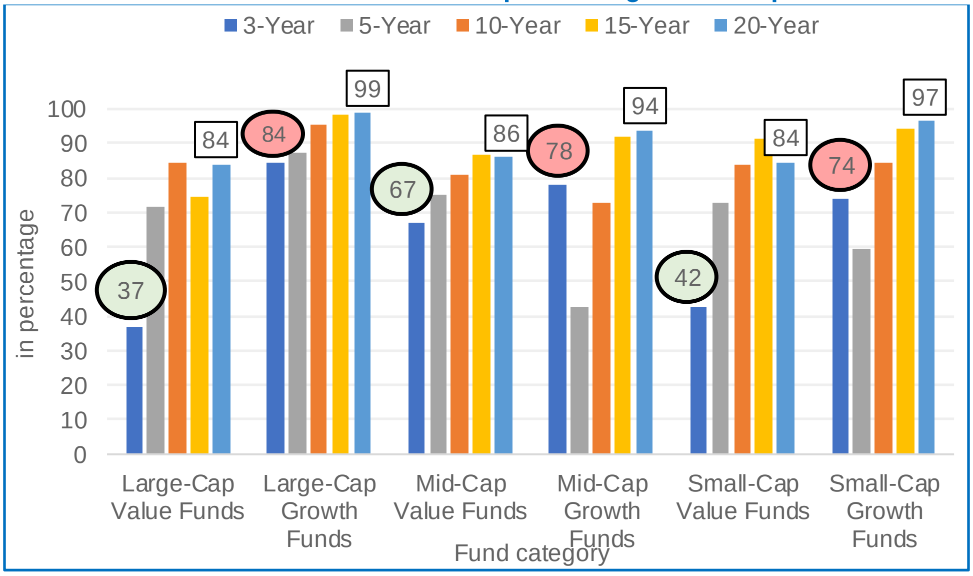
## Mutual funds show significant underperformance every year

**Most actively managed mutual funds underperform their benchmarks**

The S&P Global' SPIVA U.S. Scorecard ("SPIVA") measures the performance of actively managed US equity funds with respect to their comparable S&P indexes. The study (last published 2022 year-end) estimated that around 51% of large-cap funds underperformed its comparable S&P index in FY2022 and 81% of funds underperformed in FY2021. The study also estimated that around 63% of mid-cap funds and 57% of small-cap funds underperformed their comparable index in the FY2022.

Exhibit 1 below shows the historical performance of large, mid and small cap fund categories during different time periods. First, the underperformance of growth funds is significantly higher than value funds (as shown academically, there is some value to value). However, both value and growth funds' underperformance have remained high in the long-run.

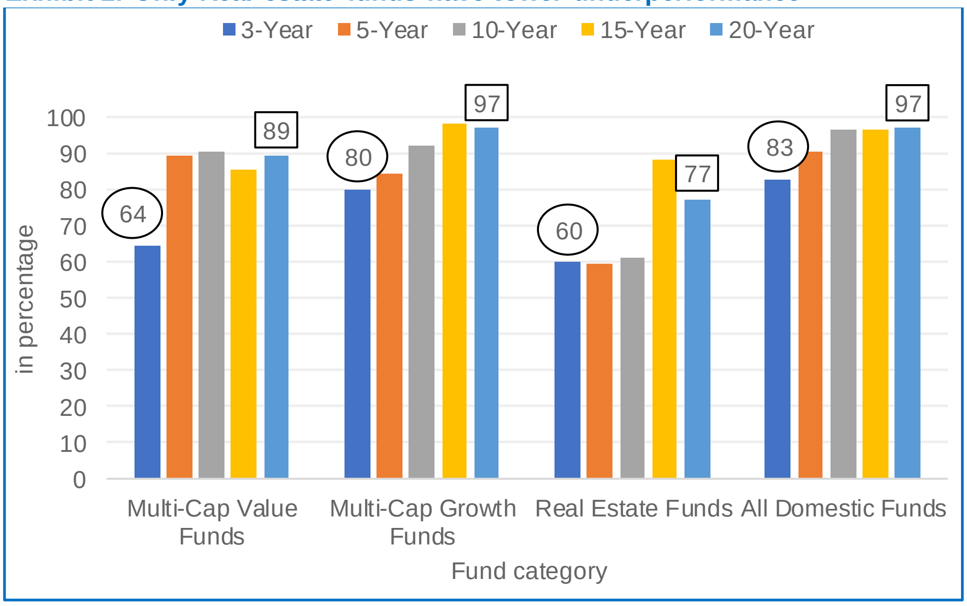
**Exhibit 1: % of U.S. mutual funds underperforming their comparable indices**




*Source: S&P Global, Berunda Capital Research*

Exhibit 2 below shows the historical performance of multi-cap, all US equity and real estate funds. We notice that the real estate fund category has perhaps lower underperformance in the long-run compared to all the other fund categories. Still, real estate funds appear as the least class of underperforming funds in the long-run at 77% of the funds underperforming over a 20-year period, not a great sign.

**Exhibit 2: Only Real estate funds have lower underperformance**




*Source: S&P Global, Berunda Capital Research*

## Typical diversification strategies may not help investors

Advisors typically choose (on behalf of their clients) to invest in mutual funds, and a pre-tailored asset class, as it saves a lot of advisor resources in managing their investments. The primary benefit of investing in mutual funds is believed to be its diversification and active management. However, one major drawback is that the advisor does not have any opportunity to choose the composition of its constituents and serves simply as an allocator. In this white paper, we delve into why we think the mutual funds are more like fast-food joints, offering similar products that are virtually indistinguishable and why the returns of most investors are highly correlated with the equity markets.

**Even Value and Growth mutual funds show positively strong correlation in the long-run, diluting offered benefits.**

Here we use the largest mutual fund company's offerings, Fidelity, as an example. Most firms' products are very similar to Fidelity's and this can be extended to most advisors and firms. A typical advisor simply allocates the fund in major categories of market capitalization, value & growth. We show here why this diversification may often be a useless exercise.

Exhibit 3 & 4 examines correlation for Fidelity's mutual funds namely FLVEX, FLGEX, FSMVX, FSSMX, FCPVX and FCPGX for 3-year and 10-year periods. Exhibit 3 shows that all the mutual funds possess positive correlation in the 3-year period. However, small-cap growth fund's correlation is comparatively lesser than other funds. Large cap entities such as AAPL, GOOG, TSLA, META and MSFT take the largest share in the equity market index. While, small-cap entities hold smaller share in the market index, hence small-cap fund has lower correlation with other funds.

**Exhibit 3: Only small-cap growth fund shows weak correlation**

| 3YR | Large-Cap Value | Large-Cap Growth | Mid-Cap Value | Mid-Cap Growth | Small-Cap Value | Small-Cap Growth |
|---|---|---|---|---|---|---|
| Large-Cap Value | 1 | | | | | |
| Large-Cap Growth | 0.76 | 1 | | | | |
| Mid-Cap Value | 0.99 | 0.78 | 1 | | | |
| Mid-Cap Growth | 0.93 | 0.86 | 0.95 | 1 | | |
| Small-Cap Value | 0.98 | 0.81 | 0.99 | 0.98 | 1 | |
| Small-Cap Growth | 0.44 | 0.79 | 0.49 | 0.71 | 0.58 | 1 |

*Source: Berunda Capital Research*

The table above shows that investing in small-cap growth fund perhaps may help an advisor in diversifying their client portfolios as they do not mirror the market. However, small-cap growth funds have underperformed in both the short run and long run.

Exhibit 4 shows that in the recent 10-year period, all the fund categories hold even stronger positive correlations with each other. From this correlation matrix it is evident that even value and growth mutual funds have strong correlations in the long-run.

**Exhibit 4: Positive strong correlations across all mutual fund categories**

| 10YR | Large-Cap Value | Large-Cap Growth | Mid-Cap Value | Mid-Cap Growth | Small-Cap Value | Small-Cap Growth |
|---|---|---|---|---|---|---|
| Large-Cap Value | 1 | | | | | |
| Large-Cap Growth | 0.97 | 1 | | | | |
| Mid-Cap Value | 0.98 | 0.91 | 1 | | | |
| Mid-Cap Growth | 0.99 | 0.98 | 0.97 | 1 | | |
| Small-Cap Value | 0.98 | 0.94 | 0.99 | 0.98 | 1 | |
| Small-Cap Growth | 0.94 | 0.98 | 0.89 | 0.97 | 0.92 | 1 |

*Source: Berunda Capital Research*

## In contrast, only few asset classes show strong correlation

Now, instead of funds by market cap and asset class, we now examine the correlations between 15 asset classes that we use at Berunda: ten SPDR select sector ETFs excluding XLC, Emerging market ETF (EEM), Vanguard's All world excluding US ETF(VEU), Invesco's US dollar index ETF (UUP), gold commodity (GLD) and iShares's U.S. aggregate bond ETF (AGG). We have excluded recently launched Communication Services (XLC) sector ETF from the asset class in order to minimize inconsistency in the long-run values.

### Exhibit 5: Asset class have no strong correlation in the short-run

| 3YR | XLY | XLP | XLE | XLF | XLV | XLI | XLB | XLRE | XLK | XLU | EEM | VEU | UUP | GLD | AGG |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| XLY | 1 | | | | | | | | | | | | | | |
| XLP | 0.20 | 1 | | | | | | | | | | | | | |
| XLE | -0.19 | 0.85 | 1 | | | | | | | | | | | | |
| XLF | 0.66 | 0.73 | 0.51 | 1 | | | | | | | | | | | |
| XLV | 0.34 | 0.94 | 0.79 | 0.84 | 1 | | | | | | | | | | |
| XLI | 0.57 | 0.78 | 0.55 | 0.93 | 0.85 | 1 | | | | | | | | | |
| XLB | 0.60 | 0.80 | 0.57 | 0.95 | 0.86 | 0.95 | 1 | | | | | | | | |
| XLRE | 0.78 | 0.61 | 0.28 | 0.86 | 0.71 | 0.73 | 0.82 | 1 | | | | | | | |
| XLK | 0.77 | 0.66 | 0.33 | 0.82 | 0.74 | 0.84 | 0.82 | 0.80 | 1 | | | | | | |
| XLU | 0.13 | 0.91 | 0.82 | 0.62 | 0.86 | 0.63 | 0.69 | 0.59 | 0.51 | 1 | | | | | |
| EEM | 0.68 | -0.34 | -0.62 | 0.25 | -0.20 | 0.20 | 0.20 | 0.28 | 0.27 | -0.41 | 1 | | | | |
| VEU | 0.81 | 0.20 | -0.14 | 0.68 | 0.34 | 0.69 | 0.67 | 0.62 | 0.71 | 0.04 | 0.82 | 1 | | | |
| UUP | -0.46 | 0.59 | 0.84 | 0.10 | 0.50 | 0.14 | 0.12 | -0.04 | 0.01 | 0.64 | -0.89 | -0.58 | 1 | | |
| GLD | -0.12 | 0.02 | -0.08 | -0.25 | -0.13 | -0.09 | -0.06 | -0.15 | 0.04 | -0.10 | -0.02 | 0.04 | -0.20 | 1 | |
| AGG | 0.44 | -0.67 | -0.92 | -0.22 | -0.58 | -0.29 | -0.28 | 0.01 | -0.05 | -0.69 | 0.79 | 0.44 | -0.95 | 0.16 | 1 |

*Source: Berunda Capital Research*

Exhibit 5 clearly shows that only a few of the 15 asset classes have positive strong correlation over 90% (indicated in blue) in the 3-year period. While asset classes are still somewhat correlated, the ***key takeaway is that they are significantly less correlated when compared to the prior typical mutual fund allocation classifications, based on market cap and value/growth*** and may therefore offer better diversification benefits.

### Exhibit 6: Some asset classes do not show strong correlation even in the long-run

| 10YR | XLY | XLP | XLE | XLF | XLV | XLI | XLB | XLRE | XLK | XLU | EEM | VEU | UUP | GLD | AGG |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| XLY | 1 | | | | | | | | | | | | | | |
| XLP | 0.94 | 1 | | | | | | | | | | | | | |
| XLE | 0.07 | 0.24 | 1 | | | | | | | | | | | | |
| XLF | 0.95 | 0.94 | 0.28 | 1 | | | | | | | | | | | |
| XLV | 0.95 | 0.99 | 0.25 | 0.95 | 1 | | | | | | | | | | |
| XLI | 0.96 | 0.96 | 0.26 | 0.99 | 0.97 | 1 | | | | | | | | | |
| XLB | 0.95 | 0.95 | 0.32 | 0.97 | 0.97 | 0.98 | 1 | | | | | | | | |
| XLRE | 0.94 | 0.92 | 0.34 | 0.92 | 0.93 | 0.92 | 0.92 | 1 | | | | | | | |
| XLK | 0.98 | 0.97 | 0.19 | 0.94 | 0.98 | 0.96 | 0.97 | 0.93 | 1 | | | | | | |
| XLU | 0.93 | 0.98 | 0.21 | 0.93 | 0.97 | 0.95 | 0.92 | 0.93 | 0.94 | 1 | | | | | |
| EEM | 0.81 | 0.66 | -0.04 | 0.79 | 0.70 | 0.79 | 0.78 | 0.68 | 0.75 | 0.66 | 1 | | | | |
| VEU | 0.93 | 0.85 | 0.16 | 0.93 | 0.88 | 0.94 | 0.94 | 0.85 | 0.91 | 0.83 | 0.93 | 1 | | | |
| UUP | 0.64 | 0.79 | 0.22 | 0.66 | 0.76 | 0.68 | 0.63 | 0.52 | 0.68 | 0.80 | 0.19 | 0.43 | 1 | | |
| GLD | 0.85 | 0.86 | 0.12 | 0.76 | 0.86 | 0.82 | 0.85 | 0.82 | 0.91 | 0.84 | 0.67 | 0.79 | 0.55 | 1 | |
| AGG | 0.85 | 0.76 | -0.39 | 0.71 | 0.75 | 0.74 | 0.70 | 0.67 | 0.79 | 0.78 | 0.73 | 0.75 | 0.52 | 0.76 | 1 |

*Source: Berunda Capital Research*

Exhibit 6 estimates that during the recent 10-year period, there is positively strong correlation in many of the asset class compared to 3-year period. However, some asset classes do not reflect strong correlations even during the longer 10-year period. For instance, Energy (XLE) relies only on the price of oil and natural gas. Therefore, other asset classes may not impact the Energy ETFs in the long-run. The message here is that investing by sectors and/or asset classes that have less correlations (vs. mutual funds). This could also help an advisor in diversifying their portfolio and thus have an opportunity to outperform the market.

For instance, in June 2022, inflation peaked in the US economy which helped energy entities to generate higher returns. In FY2022, S&P500 provided a return of -19.44. This was mainly because the market index was weighed heavily towards large-cap growth equities like GOOG, AAPL, MSFT and only smaller portion in energy equities. However, Berunda have managed to outperform the market in FY2022. As our portfolio comprises of many assets class that does not correlate with the market. This strategy has helped us in diversifying our portfolio in FY2022.

## Why pay more fees for these mutual funds that underperform?

Previously, we found that mutual funds are very likely to underperform the market in both the short/long run. Now, we address the other important thing about mutual funds - "*the price that an investor pays for it*". We noted that investments in mutual funds could attract an additional layer of costs over management fees the investors pay advisors. Some of the additional costs include front-end and back-end load charges, distribution fees, exchange fees and account maintenance fees. As mentioned earlier, these expenses are over the management fee investors they pay their advisors.

**Mutual funds incur significant additional costs and add another layer over advisory management fees**

The front-end and back-end load charges are sales commission paid to the brokerage during the purchasing and selling of shares in a mutual fund. Even though these load charges have declined significantly in recent times due to competition, even a small % of load charges do have significant impact on the long-term returns.

Similarly, distribution fee refers to the marketing and distribution costs associated with front-end and back-end load of mutual fund and is paid to the broker. This might also be indicated in 12-b fee that ranges between 0.25% - 1%.

Advisory firms that operate as both broker-dealer and investment advisor, issue such mutual funds, receive these additional fees that the investor pays. In addition, advisors may also receive commissions from the load-charges. Nevertheless, an advisor who suggest mutual funds to their clients may receive additional incentives as well as management fee. At the very least, most large advisors may also collect distribution fees from the mutual funds.

## Berunda is a dynamic allocator of asset classes

The primary benefit of investing with Berunda is that we do not engage in mutual funds that impose additional costs to the investor. Berunda is a 100% fee only advisor. We earn our income solely through management fees, which do not exceed 1.5% of AUM. Compared to some of our peers in the financial advisory segment, we consider ourselves as dynamic allocators of asset classes rather than a static age-based allocation advisor for investors, offering model portfolios and third-party products.

Berunda is also an independent advisor and a fiduciary. Being an independent advisor, we do our own research and devise investment strategies that best suit our clients. Further, we do not engage with other brokers or investment advisors to promote their mutual funds or products. Thereby, we do not collect any kind of trading commissions or other additional fees.

By completely avoiding mutual funds, our strategies greatly reduce correlated performance with the market. Currently, our portfolio comprises of assets that have lower correlation with the broader market, including value funds. While we may underperform the market indices from time to time, our portfolio has greater risk diversification and is expected to outperform our benchmarks on a risk adjusted basis in the long-run (See Disclosure).

### Sources

- SPIVA US scorecard
- Yahoo! Finance
- SEC

## Sri Nagarajan – Managing Partner

Sri Nagarajan
Managing Partner

Sri Nagarajan is the Managing Partner of Berunda Capital Partners. He is also the Principal of ValAn Global Solutions, a research support services firm. Prior to founding Berunda Capital and ValAn Global Solutions, Sri Nagarajan served as a Senior Research Analyst and Managing Director at Cantor Fitzgerald. Sri Nagarajan has also served as a senior analyst at various sell-side firms such as FBR Capital Markets & Co., RBC Capital Markets and UBS from 2002-12. Mr. Nagarajan has also worked as a senior investment analyst at Cohen & Steers Capital Management, a global asset management firm from 2007-9. From 1993-2000, Sri Nagarajan was a senior manager at Sabre, Inc., managing a team researching efficient scheduling optimization algorithms and macroeconomic forecasting models for the transportation industry. Mr. Nagarajan received his B.E. from Anna University, India, an M.S. in industrial engineering from Louisiana State University, M.S. in systems engineering from The University of Arizona, and an MBA in Finance and Strategic Management from The Wharton School of Business.



**Back tested performance is developed with the benefit of hindsight and has inherent limitations. Specifically, back tested results do not reflect actual trading or the effect of material economic and market factors on the decision-making process. Since trades have not actually been executed, results may have under- or over-compensated for the impact, if any, of certain market factors, such as lack of liquidity, and may not reflect the impact that certain economic or market factors may have had on the decision-making process. Further, back testing allows the security selection methodology to be adjusted until past returns are maximized. Actual performance may differ significantly from back tested performance. Back tested results are adjusted to reflect the reinvestment of dividends and other income and, except where otherwise indicated, are presented gross-of fees and do not include the effect of management fees, performance fees or expenses, if applicable. A transaction cost of 45-50 basis per one-way security trade, margin and borrowing rates at a 100-150 basis point spread to the risk-free rate, slippage of up to two full trading days (i.e., prices at market close on second day of the month) were assumed during the back testing. Please note all regulatory considerations regarding the presentation of fees must be taken into account. No cash balance or cash flow is included in the calculation.