

## Project 2: Portfolio Analyses and Showcase your work

### Introduction

Effectiveness in Finance research and industry necessitates a facility with data aggregation, combination, selection, and manipulation. In the previous project, you are asked to write general code to assemble a data set from different sources, and developed foundational skills of data acquisition, cleaning, and merging. In project2, you will combine data from multiple CSV files into a single table, calculate stock returns, compute variables using returns and merge tables to achieve our desired output variables. The coding work needs to be done collaboratively using git. Beyond the coding, this project 2 codebase helps us investigating the relation between total volatility and expected stock returns using univariate portfolio analyses. It tries to address whether investors can earn significant returns by investing in a volatility long-short portfolio. Furthermore, we want to help you develop the skills to showcase your work. Your team will need to record a video primarily for describing the portfolio analyses methodology and how the codebase has been designed and implemented.

### The Source Files

All required files are included in a zip archive with the following structure:

<ZIPFILE>

```
|__ project2/
| |
| |__ __init__.py
| |__ config.py
| |__ project_desc.pdf
| |__ zid_project2_characteristics.py
| |__ zid_project2_main.py
| |__ zid_project2_portfolio.py
| |__ zid_project2_etl.py
| |
| |__ data/
| | | <many csv files here>
```

where

- project2/ represents the main folder containing all the project files.
- zid\_project2\_main.py, zid\_project2\_etl.py, and zid\_project2\_characteristics.py contains the functions you need to write for this project. These are the files you need to submit.
- project\_desc.pdf is the PDF version of this document.
- data/: This is the sub-directory where all the data files for this file are stored. Inside this folder you will find many files. Each <tic>\_prc.csv contains stock price data for the ticker <tic>. These CSV files include the column names in a header row of text.
- config.py is the configuration module for this package. **You should not modify this file.**

### Instructions

**Important:** This project is a group project. Do not exchange complete or partial codes with students from **other** groups. Please do not post any project related questions in public online forums.

**Again, please do not post any project related question in a public online forum, including the discussion board in ED. We will deduct marks from your project if you violate this important rule.**

### Preparing the files for this project

1. Copy the project2 folder into the toolkit project folder. Afterwards, your toolkit folder will look like:

```
toolkit/                                <- PyCharm project folder
| ...
|__ project2/                           <- New folder
| |
| |__ __init__.py
| |__ config.py
```

```

| |__ project_desc.pdf
| |__ zid_project2_characteristics.py <-This is one of the files you need to edit
| |__ zid_project2_main.py           <-This is one of the files you need to edit
| |__ zid_project2_portfolio.py
| |__ zid_project2_etl.py           <-This is one of the files you need to edit
| |
| |__ data/
| |   | <many csv files here>
| ...
|__ toolkit_config.py               <- Your toolkit_config.py (required)
| ...

```

2. Unless explicitly stated below, **do not change any variable, import statement, function, or parameter names in the project2 module.**

## How to complete this project

This project coding section has 11 parts, which should be completed in sequence. Except parts 1, 3, and 6, all other parts will be marked.

You can find the number of marks for each part at the end of this document. Each part is described in detail in the next section.

### Overview:

- Part 1: Read the documentation for the following methods:

- pandas.DataFrame.mean
- pandas.Series.concat
- pandas.Series.count
- pandas.Series.dropna
- pandas.Series.index.to\_period
- pandas.Series.prod
- pandas.Series.resample .....

In the project coding section, you can utilize modules covered in our lectures, listed above and any others. We suggest reading the documentation and examples of a new module before using it and incorporating it into your project.

- Parts 2 to 7: Complete the functions in scaffolds: zid\_project2\_main.py, zid\_project2\_etl.py, and zid\_project2\_characteristics.py. See the step-by-step instructions below.
- Part 8: Answer the described in Part 8 below by setting the value of the relevant variables in zid\_project2\_main.py (i.e., Q1\_ANSWER, Q2\_ANSWER, etc. . . )
- Part 9: Add t\_stat function in zid\_project2\_main.py. See the step-by-step instructions below.
- Part 10: share your team's project 2 git log. See the step-by-step instructions below.
- Part 11: share your zoom recording link of the project 2 mini-presentation. See the step-by-step instructions below.

## How to submit the project and the peer review form

Please make sure each *group* submits one project and each *student* submits a peer review form:

1. Each **group** should submit **3 completed version** of .py files: zid\_project2\_main.py, zid\_project2\_etl.py, and zid\_project2\_characteristics.py. Your team should choose one member who will be responsible for submitting the project. There is no need to tell us in advance who the team representative will be.
  - The group representative should copy and paste the entire contents of the three zid\_project2\_<.>.py modules to ED.
  - Please make sure only one team member submits the group project. If multiple members of the same group submit, we will only consider the last submission by any student belonging to the group.
  - Remember to press “Mark” to submit your project. Your project will not be submitted until you do so.

2. The purpose of test functions in `zid_project2_<...>.py` is assisting your coding. You can edit it when coding. For the finalised version you submit in ED, please only update the parts we point out, i.e., `<COMPLETE THIS PART>`, the variables we ask you to define a value, like `Q1_ANSWER` etc, and add functions if we ask you to do. Keep all the other parts the same, like functions' docstring, test functions, etc.
3. Each student must also complete an individual peer review form: The peer review form will be available in Moodle (not ED). We will make an announcement when the form is ready to be completed. This form is to be completed individually by each student.

To make sure this process is clear to everyone, here is an example. Suppose a group consists of three students A, B, and C. The group decides that student A will submit the `zid_project2_<...>.py` files.

- Student A will submit the files through ED. Student A will copy the content of the completed 3 `zid_project2_<...>.py` files, navigate to the "Submit your codes here" slide in ED, and then paste the code. After that, student A will press "Mark" to submit the code.
- Students B and C should ignore the "Submit your codes here" slide in ED.
- Students A, B, and C will then separately complete their individual peer review forms in Moodle (not ED).

## Completing the three `zid_project2_<...>.py` modules

After setting up your PyCharm development environment with the project files (see instructions above), modify the `zid_project2_<...>.py` modules by following the steps below, in sequence.

### Part 1: Read the relevant documentation

Read the documentation for the following methods:

- `pandas.DataFrame.mean` (note the parameter `axis` which will indicate if the mean will be computed column-wise or row-wise)
- `pandas.Series.concat`
- `pandas.Series.count`
- `pandas.Series.dropna`
- `pandas.Series.index.to_period`
- `pandas.Series.prod`
- `pandas.Series.resample`

### Part 2: Include a statement to import the config and util modules

Open the `config.py` and `util.py` files included in this project in PyCharm. **Please do not modify these modules.** Note that these files include constants (e.g., `DATADIR`, `TICMAP`, `TICKERS` etc.) and auxiliary functions (e.g. `test_print`, `color_print`, etc.). The config and util modules must be imported by the `zid_project2_main.py` module. This is because the module needs access to the constants and functions defined in `config.py` and `util.py`.

Complete the import portion of the `zid_project2_main.py` module by creating two new import statements. These statements should import the module `config.py` and `util.py` which is part of the zip file provided to you. Your import statement must:

- Take into account that the `config.py` and `util.py` modules are inside the `project2` package.
- Import the `config.py` module using `"cfg"` as an alias (so, `"as cfg"`)
- Import the `util.py` module without giving it an alias

### Part 3: Follow the workflow in `portfolio_main` function to understand how this project construct total volatility portfolios

In this project, we are going to use the simplest methodology to construct equal-weighted quantile and long-short portfolios. To understand this codebase, you need to read the functions and its docstrings following the workflow in `portfolio_main` function in `zid_project2_main.py`.

The project consists of three parts. The first part is called ETL, which stands for extract, transform, and load. It involves a three-phase process where data is extracted from an input source, transformed (including cleaning), and then loaded into an output data container. In this project, the `zid_project2_etl.py` file is used to calculate

daily and monthly stock returns using price data imported from the project's data folder. The output of the step is a dictionary containing the return series.

The second part focuses on constructing characteristics. In this project, our aim is to test whether a volatility long-short portfolio yields significant returns. To achieve this, we will compute the characteristic of volatility for the stocks in our investment universe. The `zid_project2_characteristics.py` script is designed to calculate monthly volatility for each stock using daily returns. The output of the script is a DataFrame containing the monthly returns and volatilities of the stocks.

The third part involves constructing portfolio returns. It will generate a DataFrame containing the equal-weighted average monthly returns of quantile and long-short portfolios.

#### **Part 4: Complete etl scaffold to generate returns dictionary and to make `ad_ret_dic` function works**

- **Part 4.1: import needed modules**

Create import statements to import all modules you need in this script. Please keep the aliases consistent throughout the project. For example, use `'cfg'`, `'etl'`, `'cha'`, and `'pf'` as an alias for `config.py`, `zid_project2_etl.py`, `zid_project2_characteristics.py` and `zid_project2_portfolio.py` in `project2` folder. For modules like `pandas`, you can decide the shortcut for them. But you need to keep the aliases consistent throughout the project.

- **Part 4.2: Complete the `read_prc_csv` function**

Complete the indicated part of the function `read_prc_csv` so it produces the output described in the docstring. You can test this function by calling the `_test_read_prc_csv` test function.

- **Part 4.3: Complete the `daily_return_cal` function**

Complete the indicated part of the function `daily_return_cal` so it produces the output described in the docstring. You can test this function by calling the `_test_daily_return_cal` test function.

- **Part 4.4: Complete the `monthly_return_cal` function**

Complete the indicated part of the function `monthly_return_cal` so it produces the output described in the docstring. You can test this function by calling the `_test_monthly_return_cal` test function.

- **Part 4.5: Complete the `aj_ret_dict` function**

Complete the indicated part of the function `aj_ret_dict` so it produces the output described in the docstring. You can test this function by calling the `_test_aj_ret_dict` test function.

#### **Part 5: Complete `cha` scaffold to generate data frame containing monthly total volatility for each stock and to make `char_main` function work**

- **Part 5.1: import needed modules**

Create import statements to import all modules you need in this script. Please keep the aliases consistent throughout the project. For example, use `'cfg'`, `'etl'`, `'cha'`, and `'pf'` as an alias for `config.py`, `zid_project2_etl.py`, `zid_project2_characteristics.py` and `zid_project2_portfolio.py` in `project2` folder. For modules like `pandas`, you can decide the shortcut for them. But you need to keep the aliases consistent throughout the project.

- **Part 5.2: Read the `cha_main` function and understand the workflow in this script**

Please read the docstring of `cha_main` and figure out the workflow of this script. You can test this function by calling the `_test_cha_main` function.

- **Part 5.3: read the `vol_input_sanity_check` function and use it to test if the inputs of `zid_project2_characteristics` are proper**

Read the `vol_input_sanity_check` function. You can test this function by calling the `_test_vol_input_sanity_check` test function. When use or test this function, you should specify its three parameters. For `'ret'`, you can use either the made-up return dictionary generated by `_test_ret_dict_gen` function or the output from etl script. For `cha_name` and `ret_freq_use`, please follow the `cha_main` docstring to specify.

- **Part 5.4: Complete the `vol_cal` function**

Complete the indicated part of the function `vol_cal` so it produces the output described in the docstring. You can test this function by calling the `_test_vol_cal` test function.

- **Part 5.5: Complete the `merge_tables` function**

Complete the indicated part of the function `merge_tables` so it produces the output described in the docstring. You can test this function by calling the `_test_merge_tables` test function.

## **Part 6: Read and utilize portfolio construction functions in `zid_project2_portfolio.py` to answer some of the questions in Part 7**

Read the functions in this script and fully understand how the project is constructing total volatility portfolios. You can utilize the test functions to get a better understanding.

## **Part 7: Complete the auxiliary functions**

Complete the following auxiliary functions following the instructions specified in their docstrings:

- `get_avg`: Calculates the average value of a column for a given year.
  - `get_cumulative_ret`: Calculates cumulative return of all columns in a DataFrame.
- You can test these functions by calling appropriate test functions.

## **Part 8: Answer questions**

For this part of this project, you should answer the questions below. Your answers should be included in the `zid_project2_main.py` module. For example, answer Q1 by setting the value of `Q1_ANSWER` in the `zid_project2_main.py` file.

All your answers should be strings. If they represent a number, include 4 decimal places unless otherwise specified in the question description. When marking this part of the project, we will ignore string capitalization (i.e., lowercase vs uppercase characters).

To answer the questions below, you need to finish the coding work and then run `portfolio_main` function in the `zid_project2_main.py` with the following parameter values:

- `tickers`: all tickers included in the dictionary `config.TICMAP`,
- `start`: '2000-12-29',
- `end`: '2021-08-31',
- `cha_name`: 'vol'.
- `ret_freq_use`: ['Daily'],
- `q`: 3

Specifically, these parameters instruct the codebase to construct equal-weighted average monthly returns of tertile and long-short portfolios. These portfolios are formed by sorting the stocks specified in the `TICKERS` variable in `config.py` based on their volatility within the previous month (vol). The sample period spans from 2000-12-29 to 2021-08-31.

Please name the three output files as `DM_Ret_dict`, `Vol_Ret_mrg_df`, `EW_LS_pf_df`. You can utilize the three output files and auxiliary functions to answer the questions.

## **Part 9: Add `t_stat` function**

We've outputted `EW_LS_pf_df` file and save the total volatility long-short portfolio in 'ls' column from Part 8. Please add an auxiliary function called '`t_stat`' in `zid_project2_main.py`. You can design the function's parameters and output table. But make sure it can be used to output a DataFrame including three columns:

1. `ls_bar`, the mean of 'ls' columns in `EW_LS_pf_df`
2. `ls_t`, the t stat of 'ls' columns in `EW_LS_pf_df`
3. `n_obs`, the number of observations of 'ls' columns in `EW_LS_pf_df`

When calculate t stat of 'ls', use formula below:

$$t = \text{mean of 'ls'} / \text{Standard error for mean of 'ls'}$$

Be careful, please add the function in `zid_project2_main.py`. The name of the function should be `t_stat` and including docstring.

After calculating, replace the '?' of `ls_bar`, `ls_t` and `n_obs` variable in `zid_project2_main.py` with the respective values.

## Part 10: share your team's project 2 git log

In week6 slides, we introduce Git and show how to work collaboratively on Git.

- You are not necessary to use your UNSW email to register the git account.
- When you set up your username in git, you will follow the format `zidFirstNameLastName`,
  - for example: `zid1234567SarahXiao`
- Please follow the instruction in week6 slides to work with your teammates. The team leader will need to create a Project 2 Repo on GitHub and grant teammates access to the Repo. For teammates, you will need to clone the repo and then coding as a team.
- The team will need to generate a git log from git terminal.
  1. You can use `'cd <...>'` direct your git terminal access to the project 2 directory,
  2. Export the git log using command:  
`git log --pretty=format:"%h%x09%an%x09%ad%x09%s" >file_name.txt`  
Here is an example output:

```
.....
dae0fa9 zid1234SarahXiao      Mon Feb 12 16:33:22 2024 +1100  commit and push test
fa26a62 zid1234SarahXiao      Mon Feb 12 16:32:02 2024 +1100  commit and push test
800bf27 zid5678DavidLee       Mon Feb 12 16:12:30 2024 +1100  for testing
.....
```

Please replace the `""?""` of `git_log` variable in `zid_project2_main.py` with your team's project 2 git log.

## Part 11: project 2 mini-presentation

In this part, you are going to record and present a strictly less than 15 minutes long presentation. You should seek to briefly describe:

1. What are the null and alternative hypotheses that the project 2 is testing
2. What's the methodology of the portfolio construction and how is it implemented in Project 2 codebase?
3. What inferences can we draw from the output of Part 9, including the average return and t-stats of the long-short portfolio?
4. Do you think the results are reliable? Why or why not?
5. Is there any further work you would like to pursue based on Project 2? Share your to-do list.

In this project, you are to work collaboratively in groups. But for this part 11, it is up to the group to decide whether all the members are in the presentation video or not. Please use Zoom to record it. The final submission should be a zoom recording link.

### Important:

- The file `zid_project2_main/etl/characteristics.py` contains placeholders for your answers.
- You should replace the relevant variables in `zid_project2_main/etl/characteristics.py` files with your answers. For instance, your answer to Q1 in Part 8 should be included in the variable `Q1_ANSWER`.

• You can create a separate module and then use the functions you defined to answer the questions.

**HOWEVER, THE ONLY THREE MODULES YOU SHOULD SUBMIT ARE `zid_project2_main/etl/characteristics.py`.**

• All your answers should be strings. If they represent a number, include 4 decimal places unless otherwise specified in the question description.

• Here is an example of how to answer the questions below. Consider the following question:

Q0: Which ticker included in `config.TICMAP` starts with the letter "C"?

`Q0_ANSWER= '?'`

You should replace the `'?'` with the correct answer:

`Q0_ANSWER = 'CSCO'`

## Administrative Guidelines and Hints

We will enforce the following:

1. This assessment must be completed in groups, but you should not cooperate with students from other groups. Failure to do so may result in a full loss of marks.
2. Late submissions are allowed, but will be penalised following the guidelines described in the course outline.

## Hints

Your code should be portable, working in a variety of settings. For example, we should be able to run your codes in different computers using different operating systems. We should also be able to import and run your code from other modules.

The following hints should help you correct any portability mistakes:

1. The contents of your `zid_project2_main/etl/characteristics.py` modules **must not contain any direct reference to folders in your computer**. In other words, you must use the variables in the `config.py` and the `os` module to create path variables.
2. When writing functions in the file `zid_project2_main/etl/characteristics.py`:
  - Do not modify the function names or the parameters.
  - Only modify the parts indicated by the "<COMPLETE THIS PART>" tag or add functions if you are asked to.
3. **Only** submit `zid_project2_main/etl/characteristics.py` modules.

## How we will mark your assessment

The following parts of this assessment will be marked. The project is worth a total of 100 marks.

- Part 2: Importing modules inside the project2 package (1 marks)
- Part 4: complete etl scaffold to generate returns dictionary and to make `ad_ret_dic` function works (20 marks)
- Part 5: complete cha scaffold to generate dataframe containing monthly total volatility for each stock and to make `char_main` function work (20 marks)
- Part 7: Auxiliary functions:
  - `get_avg` function (2 marks)
  - `get_cumulative_ret` (2 marks)
- Part 8: Answer the following questions:
  - Each question is worth 1.5 marks (for a total of 15 marks)
- Part 9: Add `t_stat` function(5 marks)
- Part 10: share your team's project 2 git log (5 marks)
- Part 11: project 2 mini-presentation (30 marks in total)
  - 1.What are the null and alternative hypotheses that the project 2 is testing (2 marks)
  - 2.What's the methodology of the portfolio construction and how is it implemented in Project 2 codebase? (20 marks)
  - 3.What inferences can we draw from the output of Part 9, including the average return and t-stats of the long-short portfolio? (3 marks)
  - 4.Do you think the results are reliable? Why or why not? (2marks)
  - 5.Is there any further work you would like to pursue based on Project 2? Share your to-do list. (3 marks)