Growth of CTAs Presents Opportunities

Article from – www.FINalternatives.com
Emanuel Balarie - April 22, 2009

After stealing the show in 2008 with a combined return of 13.4%, the managed futures sector posted a down quarter to start 2009. Through March, the Barclay CTA index was down 1.46%. While the decline in this sector was broad based, trend followers had an especially difficult time trading the choppy markets. But even with a declining sector, there were some CTAs that were able to post positive numbers for the first quarter.

Growing Interest in Managed Futures

In last quarter's edition, I boldly stated that "2008 will be known as a break out year for managed futures". After a down quarter, do I still believe this to be the case? I do. In fact, my assertions was not necessarily based on the positive returns of 2008, but rather on the non-correlated returns and other unique attributes that the asset class brings to investors. This was reaffirmed by the continued interests we are seeing from "new to managed futures" investors.

One way that we gauge this is by looking at the keyword searches that have recently come to our site. Over the past few months, we have seen an increase of searches that imply that investors are looking for additional knowledge on this asset class. We have also received requests from several investment advisors and brokers who are conducting research on behalf of their client base. The consensus opinion is that they are looking for investment products that can generate returns in all types of market conditions and that are non-correlated with their equity investments.

Implications of Increased Interest

But what are the implications of this increased interest?

For those in the industry, it is quite simple. It means that the assets under management will likely continue to grow at an exponential pace. For those in sales, it means that they will now have a much easier time selling the asset class. For CTAs, it means that there are now more people that will be willing to allocate to this sector, and hopefully their specific programs.

There will also likely be an increase in the number of Commodity Trading Advisors. One of the services that Balarie Capital Management offers is that we work with start-up or emerging CTAs. Over the past few months, we have seen an increased interest in our start-up CTA services. The traders that we have spoken with have a wide variety of backgrounds. Some are non-professional traders who have a dream of becoming a CTA and others are professional traders, with a great pedigree, that are looking to finally start their own shop.

The addition for these new CTAs can be both positive and negative for the industry. It is positive because it brings onboard a new round of talented managers. It is also positive for the investors because they have a greater choice for investments. However, one negative aspect will be that there will be a slew of traders who are professional by designation, but lack experience in terms of trading and risk management. Indeed, emerging CTA after emerging CTA has shown that posting numbers out of the gate is one thing…and maintain those numbers is totally different. Investors should be cautious about allocating funds with an inexperienced trader who has a few months of stellar performance.

© 2009-2010 Interconti, Ltd./ TW Merryman

Opportunities for Emerging Traders

Institutional investors and seed capital funds are eagerly looking for talented traders to seed. Specifically, we have noticed that there is a need for discretionary traders who specialize in a specific market or sector. If you are a start-up or emerging CTA and are interested in the services that we offer, please contact us for a free consultation.

Where Have All The Investors Gone?

While my above assertions paint a bullish case for this industry, the net outflows out of this industry might confuse some individuals in thinking that quite the opposite is happening. However, I believe that the recent outflows are temporary and simply a reaction to the global liquidity mess, stock market decline, and real-estate collapse. In other words, investors were not necessarily taking out their money because they were not satisfied with this sector; rather, they were taking out their money because they had to compensate for their other losses.

Investors have also suffered from an investment shell-shock of sorts. It seems that all aspects of their wealth have diminished. From massive declines in the real-estate market, to their stock portfolios getting hammered, to hedge fund blow-ups and ponzi schemes…it is no wonder that investors are taking a moment to catch a breather when it comes to reallocating capital. But this action, in my opinion, is temporary. We believe that investors will be looking for places to invest. In fact, we are already noticing that institutional investors are actively looking to allocate.

Risk

In this quarter's newsletter, we have included Fund of Funds Risk Management, a report published by Risk-AI, LLC. The report looks at the necessary steps to establish effective risk management, especially one it comes to quantitative due diligence and constructing a fund of funds or multi-manager portfolio. As we stated in last quarter's commentary, we feel that the proper way to participate in this managed futures sector is to have a diversified portfolio with allocation to a variety of managers. The key, however, is finding the right managers and constructing the right portfolio.

There has also been a focus on risk due to the amount of hedge fund blow-ups and ponzi schemes that have been uncovered over the past several months. There will be a few trends that will likely result. First, we believe that there will that there will be a trend towards hiring independent risk consultants to manage portfolios. In addition to the independent qualitative and quantitative due diligence that these consultants might offer, investors seem to be inclined to pay "extra" for another set of eyes that continually monitor their portfolios.

Another trend that we are seeing is that there seems to be a renewed interest into opening up managed accounts. While institutional investors have previously shied away from this format- preferring fund structures- we are now seeing requests for managed accounts. At the core of this transition, is that investors want to be able to see their accounts and verify the trading activity that is occurring in those accounts. In short, they want transparency. While not all CTAs will comply with this request, we do feel that some will have to re-evaluate their business models and lower their managed account minimums if they are looking to attract additional capital.

© 2009-2010 **Interconti, Ltd./ TW Merryman**

Managed Futures Drawdown a Buying Opportunity

Article from – www.SoveriegnSociety.com
Eric Roseman - April 21, 2009

The best performing alternative investments in 2008 didn't belong to rare fine wines, art, stamps or some commemorative coins. That prize belonged to managed futures or Commodity Trading Advisors (CTAs), several of which surged more than 30% in a year dominated by incessant volatility, a full-blown banking crisis and the evaporation of more than $25 trillion dollars of global wealth.

CTAs are now correcting sharply since March as a drawdown phase occurs - an anomaly driven by sharp trend reversals across several major asset classes combined with non-trending markets in other sectors. CTAs as a rule feed on market volatility.

CTAs are a subset of the alternative funds sector. The asset class is dominated by trend following trading systems introduced by mavericks like Richard Dennis in the late 1960s, who pioneered the term "Turtle Trading." Today, the majority of the industry's assets are dominated by trend following traders, including John W. Henry, Bill Dunn, Jerry Parker, Jr. and Paul Tudor Jones.

One of the leading programs in the United States is John W. Henry's Financial & Metals Portfolio, up a stunning 22.45% per annum since 1984 – more than doubling the returns generated by the S&P 500, the MSCI EAFE Index, long-term government bonds and commodities. An original $1,000 investment in the JWH Financial & Metals Portfolio in October 1984 would be worth $142,990 through March 31, 2009. That compares to just $8,656 for the S&P 500 Index, $7,095 for EAFE and $11.567 for the Barclays Capital U.S. Long-term Government Bond Index. In 2008, JWH F & M skyrocketed 47.3%.

CTAs trade more than 100 global futures markets 24-hours per day with leverage; though extremely volatile, they maintain a truly negative correlation to common stocks amid market crashes, corrections and systemic dislocations. As global markets crashed in the fourth quarter, for example, CTAs surged more than 15%, critically offsetting losses from stocks in traditional portfolios.

Another important point worth noting is that, unlike hedge funds, which are only now coming under regulatory scrutiny, managed futures have been heavily regulated for decades. Managed futures are also generally far more liquid than hedge funds since futures contracts trade daily.

The top traders in this unique asset class are available for less offshore.

In the United States, CTAs are sold through limited partnerships and typically require the investor to be accredited or harboring net assets of more than $1 million dollars. The minimum investment is usually about $500,000. Some brokers also distribute these products with a lower entry requirement but the fees are so enormous that breakeven rates make these investments daunting.

In Europe, some of the best traders are available, including Man-AHL Diversified, Winton Futures and Rivoli International. These funds are available in U.S. dollars and euros. European private banks can buy these products for your account and the minimum is much less – ranging from $30,000 to $100,000. For most investors, a maximum 10% allocation to managed futures or CTAs is sufficient.

Since stocks bottomed in March, CTAs have undergone a drawdown, defined as a peak-to-trough decline of 15% or more. A drawdown is part and parcel of investing in this volatile asset class and historically is the best time to buy a CTA.

© 2009-2010 Interconti, Ltd./ TW Merryman

In 2008, the top CTAs earned a bundle from shorting global stock index futures, commodities futures and foreign currencies vis-à-vis the dollar. They also rode the bull market in bonds as Treasury's went through the roof.

In the June issue of The Sovereign Individual (TSI) I'll delve into several alternative investments, including CTAs, while examining their bear market performance since 2000.

After lagging stocks in the 1990s bull market, alternative investments like CTAs, fine red wine, rare stamps and precious metals coins have exhibited a negative correlation to common stocks this decade. This decade has been marked by the highest degree of volatility in history following a crash across global markets last year and the tech bust in 2000.

Judging by the ongoing volatility and depth of this recession/depression, these and other alternative investments should continue to enjoy solid returns over the next several years, serving traditional portfolios with a reliable hedge. Learn more in June's TSI.

© 2009-2010 **Interconti, Ltd./ TW Merryman**