

MANAGED MONEY

TOP TRADERS
OF 2011

BY DANIEL P. COLLINS

Every year is different in managed futures, and 2011 was more different than most. Performance-wise, it was the worst year in the 32-year history of the Barclay CTA Index, and the MF Global debacle froze many CTAs in their tracks. Despite this, we found several managers who not only survived, but thrived in the choppy and volatile conditions.

All the best traders will tell you that the most important aspect of being a successful trader is strong risk management. But they are referring to market risk: Not having too much leverage, having defined exits, not being overly concentrated in one market and avoiding illiquid markets. One risk most managers have not worried about much is counterparty risk; in fact, they trade on regulated, centrally cleared markets specifically to avoid it. Many even promote the advantage of not having the risk of a fraudulent manager through offering managed accounts kept with the customer's broker. Until recently, the idea that funds held in segregated accounts would be in peril was down on the risk scale.

Cranwood Capital Management, LLC
Splendor Capital Management Ltd.
Stratford Capital Management, Inc.

Sadly, we spoke to a couple of managers who told customers their money would be safe if MF Global happened to go into bankruptcy, even after it was clear the firm was under stress.

How widespread was the MF Global carnage? We ventured as far as Shenzhen, China to find one of our 2011 Top Traders, but even that wasn't far enough to avoid the fallout from MF Global.

Splendor Capital Management's exposure to MF Global was minimal but real, and the Chinese firm already has written off a small portion of their assets because of it.

All of our top traders had some exposure. Cranwood Capital Management operated a fund and traded through MF Global. Fortunately they have a low margin requirement and hold most of their funds in a separate account at UBS just for that reason. "Once we caught wind that MF Global was having problems, I wired out a good chunk of the money, leaving the bare minimum," says Cranwood's Pete Powers. Still the firm missed 25% of the trading days in the fourth quarter because of the MF Global situation.

Stratford's Kevin Benoit was in the midst of his second superb year and was close to welcoming several new customers through MF Global accounts. Those accounts were not opened and may never open. While people talk about the funds still outstanding because of the crisis, measuring the total cost in terms of lost trading days, lost brokerage, lost incentive fees and spooked customers leaving the space will be impossible.

As for 2011, the Barclay CTA Index registered only its fifth negative year out of 32 and its worst overall at -3.00%. It was a bad year for trend-followers and, while every difficult year produces a few

outlier trend-followers who do well, they were harder to find in 2011.

"It was a difficult trading market," says BarclayHedge President Sol Waksman. "Take a look at how many times during the year, from one month to the next, you would have the stock market rallying, stock market crashing, rally, stock market crashing. Gold [saw] the same thing. The dollar [had] the same thing. One month risk-on, one month risk-off, those are difficult environments for trend-followers."

Troy Buckner, founder of NuWave Investment Management, says it has been a tough environment for three years because of a general weaker directional persistence. "It has been a weak five years and the strategies that survive become the ones that tread water effectively until the directional persistence is back. Whether the markets are going up or down, at least they are going up or down with persistence," Buckner says.

NuWave earned just over 7% in its medium-term pattern recognition program. Buckner does not define himself as a trend-follower, but they usually are exploiting the same moves, so he would be happy to be in the plus column.

Even many of the short-term traders with strategies built to perform well in periods without sustained trends tend

CRANWOOD: The butterfly effect

When you ask why his firm had such a good year in 2011, Cranwood Capital Management CEO Pete Powers says it simply was lack of a bad year. See, Powers has been trading butterfly spreads in the Treasury futures complex for more than a decade and the only truly bad stretch came in 2009 when the credit crisis dried up the liquidity. Even then his fund only dropped 1.78%.

"Liquidity dampens volatility to a tradable level for a strategy like mine. In 2009, the Citadels, the Bear Stearns, the Lehmans, all the interest rate desks shut down," Powers says. "I don't need volatility, I just need volume, enough to get in and out of the butterfly spread because we get flat every day at 3 p.m."

The Ohio-based fund owns six seats on the Chicago Board of Trade (CBOT) to qualify for member rates for his highly active fixed income arbitrage strategy.



PETE POWERS AND HIS TEAM

PHOTO BY ROGER MASTROIANNI

of the butterfly together and we are always on the bids and offers trying to get an edge."

The trade is not only market-neutral but also yield-curve-neutral. "If we are short 10s, we are long fives and 30s," Powers says. "Basically, we are looking at discrepancies intraday in the relationship in those three maturities as they relate to each other. We don't take any directional risk, and in theory we don't take any steepening

or flattening risk because each trade has both elements."

The increased volume in the complex has led to greater opportunities as Cranwood earned 17.74% in 2011. That number comes with an annualized standard deviation below 10%, meaning they outperformed most managers on a risk-adjusted basis. "The risk profile that we present is by far our most attractive asset," Powers says.

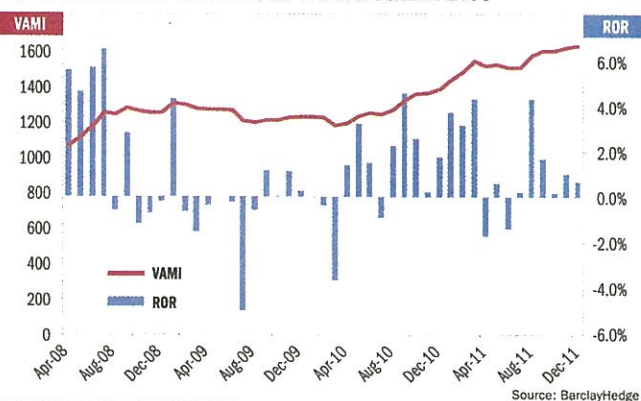
Good execution is key. "Obviously buying bids and selling offers is ideal, but more importantly we don't do worse than bid, bid, bid; we are not going to give up an edge if we don't have to." The strategy is time and personnel intensive, so if they didn't add value, it wouldn't make much sense to have eight people executing. "We would probably look to automate, but automating the strategy has not proven to be fruitful because an automated system is going to sell the bids and buy the offers, giving up a chunk of the move," Powers says. "Right now the team aspect, the assembly line approach, far outperform any type of automation."

Surprisingly, the long-term zero-interest-rate-policy by the Fed has benefitted the program. "It is a lot easier to predict. [Price] stays in a band over a group of years," Powers says regarding the effect of the zero-rate policy. "Volume takes off at any hint of an uptick in rates so the fact that volume is still strong and we are at these low rates gives me the confidence that things are only going to get better for this strategy."

Rising volume and the need for more products is a good sign for Cranwood. "We are doing three auctions a week, two weeks out of every month. The volume is going to be astronomical over the next 10 years," Powers says.

Not only is volume growing, but also the emergence of the Ultra Bond (30-year bond future with a longer minimum maturity) will add another facet as Cranwood plans to begin trading a 10-year, 30-year, Ultra butterfly in 2012. This should allow Cranwood, currently with \$39 million under management, to spread its wings.

CRANWOOD CAPITAL MANAGEMENT



Powers learned the trade on the CBOT floor and perfected it in after-hours electronic markets, which allowed him to move back to Ohio and build an execution team made up of family and friends. The team of eight trades in shifts over the 23-hour market day.

Cranwood trades the two-year, five-year, 10-year Treasury note butterfly and the five-year, 10-year, 30-year Treasury bond butterfly with one trader executing one leg of the spread and another the other leg.

"We do them simultaneously," Powers says. "One trader will be legging the NOB (buying 10-year and selling 30-year), at the same time I am selling the FYT (buying the 10-year, selling the five-year), so we are building the body