Smart Allocations to Systematic Asset Managers

As an institutional allocator, family office or wealth manager, you need uncorrelated alpha to complement traditional liquid investments. The systematic hedge fund landscape is a good place to find it. But the terrain is difficult, hard to understand, and hides potential risk.

The temptation is to stay on familiar ground, or to follow the crowd. Allocating only to the biggest names is a likely path to underperformance as their sheer size works against them. Jumping on the current hot strategy or manager will likely lead to disappointment as hot inevitably turns cold.

Meeting your target requires allocations to a range of strategies which have the potential to deliver uncorrelated returns, crisis alpha, and tail risk protection. As with the rest of your portfolio, the best hedge fund allocations are designed purposefully with your objectives and constraints in mind.

Why Systematic Asset Managers?

Systematic managers are the scientists of asset management. They see market relationships through the lens of statistics and probability. Their trading systems may seem like a black box, making it hard to invest. But their controlled and consistent approach lends itself to analysis and prediction.

Discretionary managers are the philosophers of asset management. They look beyond markets into the real world of cause and effect to build their investment theses. Their approach is easier to understand and invest in, but their performance can be less predictable.

Coming from an engineering background, we chose to focus our efforts on systematic managers. They make an ideal complement to discretionary managers and your existing liquid portfolio. Let us open the black box so you can invest with confidence.

Our Process

Like the managers we specialize in, we take a systematic approach to asset allocation. It all starts with you and your requirements, and takes off from there:

- **Search & Screen:** We narrow the universe of 10,000+ managers to a list of candidates in the 100’s.
- **Quantitative Analysis:** We identify the top contenders based on your requirements. Using our proprietary toolkit, they are grouped, ranked, and ready for due diligence.
- **Trading System Due Diligence:** We verify that managers follow sound practices for research, development, deployment, operation, and monitoring of their trading systems.
- **Capital Allocation:** Using our Empirical Space Portfolio model we build portfolios optimized to your requirements, taking advantage of the managers’ most valuable performance characteristics.

We provide everything you need to make smart allocations to the right systematic asset managers.
There are around 10,000 hedge fund programs accessible via separately managed accounts, SMA platforms, and commingled funds. In addition, there are 600+ liquid alts products. And then there are the programs that are not even in the databases!

It’s a big universe – we make it manageable.

For each investor, we start with three questions:

- What are your objectives?
- How much capital will you deploy?
- What are your “hard” constraints?

The answers to these questions will define our search and screen mandate. We build a set of screening rules and apply them across industry databases. We tap our network for undiscovered gems you won’t find in the databases. Our goal is to narrow the universe from thousands to hundreds, while retaining all the high-potential candidates.

Quantitative Analysis

Many of the standard manager performance statistics are ill-constructed for their purpose. If you rely exclusively on them you will experience lower returns, larger down-side surprises, greater correlation, and worse drawdowns than you expect. To differentiate effectively between managers you need to uncover the deeper story hidden in the numbers.

Like the managers themselves, we take a systematic approach to manager quantitative analysis.

We use mathematical clustering to divide the candidates into distinct groups driven by your investment mandate. We then compare managers to their peers within their own cluster.

Our proprietary suite of statistics is specifically designed to differentiate between managers using the most highly prized features of their performance. We pay particular attention to skew, conditional value at risk, correlation, and autocorrelation.

Many of the statistical measures we use are enhanced to make them more fit for purpose, less susceptible to outliers, and more robust. Detection of change algorithms help identify discontinuities in the performance record to avoid crediting or penalizing a manager for past performance that is unlikely to be repeated.

We narrow the field of candidates down to our contenders, organized into groups, ranked, and ready to move on to the trading system due diligence phase.
Trading System Due Diligence

Systematic programs compound the challenge of protecting your investment from the risk of fraud and operational error. To achieve the confidence you need to write a ticket:

- You must understand and be comfortable with the mathematical principles of the trading system.
- The manager must demonstrate rigorous development and testing processes.
- The trading system must be deployed, managed, and monitored in a robust manner.

From years of developing trading systems, and as director of research at The Bornhoft Group, an award-winning pioneer in multi-manager CTA funds, I have a firm grasp on the processes required to design, test, tune, and deploy a systematic trading strategy.

While we cannot relieve you of responsibility for completing your own thorough due diligence, any contender who fails to pass our rigorous trading system due diligence will not be considered as a finalist for inclusion in a portfolio.

Capital Allocation

You have searched the universe of managers, analyzed them in-depth, completed extensive due diligence, and are now ready to make your allocations. It took a lot of work to select your finalists.

Standard portfolio construction methods such as MPT ignore the very performance characteristics that you are paying a systematic manager to deliver. In addition, they make assumptions about your preferred measures of risk and return.

We employ our Empirical Space Portfolio model to:

- Optimize for multiple risk-return objectives, finding Pareto optimal sets of portfolios.
- Capitalize on key performance characteristics of your selected managers.
- Respect as many or as few constraints as your investment policies require.

We use Monte Carlo techniques, which preserve key features of the managers’ historical returns (the empirical data), to evaluate the expected performance of each potential portfolio. Depending on the number of managers and the allocation increment, the portfolio search space can be immense. We employ a variety of optimization algorithms from exhaustive, through gradient descent to genetic search, to find the set of optimal portfolios.

We build portfolios that are optimized to your specific objectives: we put you firmly in the driver’s seat.
Additional Services

Manager Risk Profile: quantitative due diligence
- See the full risk picture for individual Managers and find subtle differences between them.
- Confidently allocate to higher return opportunities armed with clearer expectations.
- Monitor manager performance for style drift and loss of edge.
- Exploit available time-series relationships.

Portfolio Risk Profiles: make better allocation decisions
- Get all the benefits described above applied at the portfolio level – show your portfolio in the best light.
- Exploit relationships amongst portfolio components and potential new allocations.
- Identify data outliers to improve analysis and to flag early warning signals.
- Test sensitivity of risk and performance metrics to portfolio changes.

Portfolio Optimization: your allocation edge
- Identify the performance metrics that you want optimized.
- Tailor risk constraints to meet your requirements.
- Optimize capital allocation to maximize your key performance metrics without violating risk constraints.

NEW Model Portfolios: get the full range of our model portfolios delivered quarterly

Ian Rayner

I was Chief Operating Officer and Director of Research for The Bornhoft Group, an award-winning pioneer in multi-manager CTA funds. As COO I built institutional quality operations throughout our firm. As Director of Research I developed statistical tools for delving deep into manager performance, and building robust portfolios.

Our team placed hundreds of millions of dollars with quant managers. We allocated capital to the biggest names and to the smallest niche players. We screened 1,000’s, analyzed 100’s, and completed operational due diligence on the best to construct our portfolios. During my tenure, our flagship program returned over 40% per year.

I hold a Masters in Chemical Engineering from Queens’ College, Cambridge University. I graduated one of only 10 Palmer Scholars in my class in the MBA program at The Wharton School, University of Pennsylvania.

Contact

Call us today discuss ways to build systematic asset managers and quantitative trading funds into your portfolio.

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Credits: “The Dead Zone”, Julian Coquentain; Cluster Chart Logo, Arafat Uddin, Noun Project; Gears Magnifier, Carlos Sarmento, Noun Project; Round Puzzle, Magicon, Noun Project.