HEDGE FUNDS REVIEW

Managed futures on the rise as investors chase diversification

By Kris Devasabai, 4/4/11

Managed futures has grown to become the single largest strategy in the hedge fund universe. Strong inflows and performance have helped make it a popular diversifier for many portfolios.

In 1983 Harvard professor John Lintner published a seminal paper illustrating how an allocation to managed futures could dramatically improve the risk adjusted returns of an investment portfolio. Twenty-seven years later managed futures have become an investment vogue and allocations to the strategy are growing at a startling pace.

Commodity trading advisers (CTAs) running managed futures programs experienced record inflows in 2010, according to data from BarclayHedge. Combined assets managed by CTAs reached $267.6 billion at the end of 2010, an increase of over 25% from $213.6 billion in 2009. That makes managed futures the single-largest strategy in the hedge fund universe, representing almost 15% of industry assets, according to BarclayHedge numbers.

This is not simply a case of investors chasing performance. CTAs generated only modest returns of around 7% last year and were broadly flat in 2009 when most other strategies posted large gains on the back of the powerful rally in equities.

Instead, the focus is on managed futures as a source of uncorrelated returns that can help diversify a broader portfolio. These properties came to the fore in 2008 when managed futures programs returned over 14% on average despite large declines in global markets.

The contrarian performance of managed futures is the key to its value as a diversifier. A study by the CME Group and AlphaMetrix in 2009 revisiting Lintner's original paper found the BarclayHedge CTA Index had positive returns in 12 of the 15 worst months for equities since 1987.

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http://www.risk.net/hedge-funds-review/feature/2245131/managed-futures-rise-investors-chase-diversification