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Why managed futures funds beat the market

While hedge funds worldwide had a bad 2008, many managed futures funds performed well. Superfund founder Christian Baha explains why.

Market views
Deutsche Bank's chief strategist maps out where investment opportunities now lie

Bonds outlook
Inflation-linked debt looks irresistible to Pimco's Bill Gross

Collectibles
Selling wine at auction can be as easy as drinking it

Alternatives update
Hedge funds suffer worst losses but beat markets

COVER STORY

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BLOOMBERG

| BY KELVIN TAN |

Christian Baha, founder of managed-futures outfit Superfund, couldn't be happier. Last year, while most asset classes including alternative ones such as hedge funds and commodities turned in record losses, his range of funds, which topped the performance league of all Singapore-registered hedge funds, had one of their best years in terms of returns after generating gains ranging from 20% to 66%.

Even more pleasing to Baha was the fact that in 2008, when all managed futures funds flourished after achieving average gains of 15.6% as measured by the Credit Suisse/Tremont Hedge Fund index, the alternative asset class showed it was capable of delivering high uncorrelated returns regardless of what was happening to the broader financial markets.

"[Managed futures funds] are going to be the asset class for the next decade because they have been proven to perform well in both bull and bear markets," declares the 40-year-old, Vienna-based Superfund founder in a recent interview with *Personal Wealth*.

A managed-futures strategy generally involves betting on the direction of currencies, commodities, equities and bond securities using financial futures contracts. Most managed-futures money managers, also known as commodity trading advisers, use a systematic method of trading.

"Generally, managed futures fall into a fairly simple matrix with three axes — long term or short term, trend following or countertrend, and discretionary or model-driven. Each combination has a different set of investment characteristics, but generally they are not correlated with other financial assets," explains Peter Douglas, principal of local hedge-fund research firm GFIA.

An asset class for everybody

Baha, a former member of the Austrian police force, started Superfund 13 years ago because he wanted "everybody in the world" to have access to managed-futures funds, which he claims are "one of the few asset classes" in the world that consistently deliver "high performance with relative low risk".

"Why should this asset class be available only to institutions and not for everybody?" says Baha, who has spent a considerable amount of money and effort over the years promoting his funds through advertisements and marketing campaigns in the various countries where Superfund's products are sold.

Superfund's sponsorship activities are extensive and include Formula 1, skiing, the performing arts and even an Austrian football club known as FC Superfund. "We don't own [the club]. We just sponsor it. That is just for branding. Wherever we can do branding and it makes sense, we will do it," says Baha, who also owns a listed Austrian financial-software company called **TeleTrader**.

Presently, Superfund, which has offices in over 20 countries worldwide including Singapore, manages some US$1.6 billion ($2.4 billion) for over 50,000 investors, 80% of whom are individual investors. In Europe and the US, Superfund's managed futures funds, which require a minimum investment of as low as €5,000 ($9,800) and US$5,000 respectively, are delibrately made affordable to the investing public. "In many of the countries where we are selling our products, everybody can invest in [our funds], even those with €50 for some of our [regular] savings plans," Baha enthuses.

However, in Singapore, although the minimum amount for the most affordable range of Superfund funds — the Strategy A products — is only US$5,000 or €5,000, these can only be sold to accredited investors who have a net worth of at least $2 million or an annual net income of $300,000. This is because Superfund's range of funds, as with hedge funds, are classified by the Monetary Authority of Singapore as products under the restricted Collective Investment Schemes. "Singapore clients need to be accredited investors," says Aaron Smith, managing director of Superfund Singapore. "But our goal here is to educate the public about managed futures," he adds.

Given that retail investors in Singapore can easily open individual futures and options trading accounts with financial brokerages and trade in high-risk financial derivatives, Baha questions the logic of restricting managed futures funds run by professional money managers to only wealthy investors.

"People [in Singapore] can open an options trading account today, put

Q&A with Mr Superfund

***Personal Wealth*: In 1992, you teamed up with your business partner Christian Halper — a software developer — to devise systematic trading programs. In 1995, you came up with TradeCentre, a program to spot trends in the commodity futures markets. And in 1996, you launched your first fund in Vienna. Can you tell us what types of technical indicators your systems use to generate a buy and sell signal?**
Baha: We use a lot of [common] technical indicators that you would know of. They are nothing special. It is just how you combine them in the right way. Besides those, there are some indicators that we developed in-house. On which specific indicators we are using, we are not commenting. But to be successful in trading, you have to have signals to enter the market as well as when to get out. More importantly, it is how much your risk in one trade, be it 1%, 5% or 10% of your portfolio.

Tell us about your risk-management techniques and stop-loss orders?
We define how much we want to lose in a losing trade. The maximum loss in any trade is 1% of our assets under management. That is the maximum risk we take in any one position. If the market is very volatile in the energy or stock indices for example, we will take a very small position in the funds. You don't want to get stopped out with the [high] daily volatility. But if you have a market that is smooth with [acceptable] volatility, then you may want to take a bigger position.

Obviously, you have come a long way since your early days. What was the biggest setback that you have encountered with Superfund?
The biggest setback was in the very early days when it was very difficult to raise assets. When we started, we had only US$460,000 in assets. It took us two years to reach US$1 million in March 1998. That was the hardest time. But after that, everything just went smoothly.

From 1987 to 1994, you were a policeman patrolling the streets of Vienna. Did you encounter any life threatening incidents?
Thankfully no. I didn't experience any shooting incidents and I didn't shoot at anybody. Vienna is quite a peaceful place. It is not like New York or Harlem.

Tell us about your personal investment portfolio. What do you invest in as a private investor?
My money is where my mouth is and that is in physical gold, silver and real estate. And the majority of my private investments is in my own funds.

What about stocks?
No, the only stock I have is my listed company TeleTrader. I won't say stocks are a bad investment. There is just too much money in stocks today.

Lastly, how would you respond to critics who say you spent too much time and money on marketing, sponsorships and advertisments for your funds?
It is our decision on where we spend our money. It is our money we earned from fees after we delivered good returns. We are unlike banks who spent money and needed a rescue package from the government. We do marketing because we want to establish the brand. It will be a big advantage for us over the long term. But I can assure you that we are spending our money very carefully because it is our money. We are making the private investors in our funds very rich and we are expanding and building our brand. We think it is good that more people understand managed futures.

all their money on one bet and lose all of it. But they are not allowed to invest in managed futures," he states with evident frustration. "I know this kind of regulation is to protect individual investors. But you are preventing people from getting into a high performing, well-diversified asset class. It should be open to everybody and people should be educated about it," adds Baha, who is hoping that the local financial authorities will ease the restriction on his range of funds.

Bets that did well in 2008

According to Baha, the main reason most managed futures funds did well last year was the prevalence of strong up-and-down trends in financial markets over the past 12 months. "Higher volatility doesn't necessarily mean better timing for us. We normally like constant trends and constant markets. The most important thing is to have trends, whether they are in the up or down directions."

Superfund, whose funds currently trade in over a hundred different markets, deploys complex computer systems developed by Baha and his business partner, and Superfund's chief technology officer, Christian Halper, to spot price trends in commodities, currencies, stocks, bonds and other securities. Once a sustainable trend is identified, the firm's quantitative model, which uses many different technical-analysis indicators, will issue a buy or sell order. "Trading is executed automatically," explains Baha, who employs 50 people in the trading department to make sure that trade orders are implemented and executed properly. Big trades are usually broken up into smaller orders so as "not to move the markets", he says. "We don't want to move the markets with our orders. We never want to be seen in the market. We are a trend follower and not a trend maker."

For 2008, most of the markets and securities that its funds traded in performed incredibly well, claims Baha. "When we had such high performance numbers like in 2008, you normally would make money in many different areas. If only one area is performing, you won't make returns that high."

The most profitable bets, he says, were the long trades on gold, which surged to over US$1,000 an ounce in early 2008, and shorts on oil and metals, whose prices more than halved over the past 12 months. "Bonds and short-term interest rate markets were also good on the short side. In addition, we made plenty of money in equities and stock indices on short trades," beams Baha (See table for the performance of the Superfund range of funds last year).

Gold to surge to US$1,500

Among the commodities that Baha and his team are most bullish on in terms of price upside in the medium term is gold, whose price he predicts will hit US$1,500 in "'a few years' time". He points out that its price will surge because of hyperinflation and the weakening of the US dollar.

"The money printing presses in the US are running like crazy. They are just printing too much money. In the future, people will recognise that [the US dollar] will lose its value and they will look for safe-haven physical assets such as gold [as a store of value]," says Baha.

Once the market starts to lose confidence in the greenback, high inflation or hyperinflation will be on the cards, he warns. "Now, we have a deflationary environment, but as soon as inflation starts to creep up, oil and other commodity prices will go through the roof."

So bullish is Baha on gold that his firm has funds that are priced in ounces of the yellow precious metal to allow investors to benefit from the appreciation in gold's price. Called the Superfund Gold funds, it converts investors' subscriptions into gold. During redemptions, the value of the funds will be converted from gold back into an investor's currency of choice.

The high fees

Without a doubt, the performance of Superfund's range of funds has been respectable over the years. For instance, the flagship Superfund Q-AG returned 776.41% (or an average annual gain in access of 18%) from its inception in March 1996 to end-2008. The fund managed to generate positive, double-digit gains in 10 of its 13-year history.

Still, potential investors in Superfund's products need to be aware of their lofty fees, say fund observers. The firm's SICAV funds sold in Singapore currently charge a one-off upfront sales fee of 4.5%, annual management fee of 6% and a performance fee ranging from 25% to 35% when a fund hits a new high (The performance fees are 25% for the low-risk Strategy A funds, 30% for medium-risk Strategy B funds and 35% for the high-risk Strategy C products). Adding up all the fees, a Superfund product generally needs to achieve returns of at least 6% to 8% before investors see any gains.

These fees are just too high, according to GFIA's Douglas. "As managed futures are scalable and liquid, they should also be cheap." He points out that the total expenses of managed futures funds "should be cheaper" than the average of Singapore-registered unit trusts, which generally have an annual expenses of about 2% of assets under management (AUM). "When evaluating Superfund, you should look at how they performed against other managed futures funds and what their total expenses are," adds Douglas.

Hedge funds typically charge a 2% annual management fee plus a performance fee of 20%. One of the world's biggest managed futures funds, the Man AHL Diversified, with assets of more than US$3.5 billion, currently charges an annual management fee of 3% and a performance fee of 20%, all of which are lower than Superfund's.

When asked to comment on the high fees, Baha points out that "cheap things are no good and good things are not cheap". He reasons that the better the funds are, the higher their fee structure. "That is generally true for the best managed futures funds out there. There are other funds that charge more than we do. For example, [hedge fund manager] Jim Simons [of Renaissance Technologies Corp] charges 46% incentive fees for his Medallion Fund," argues Baha, who adds that his funds have still managed to give attractive net-of-fees gains to investors over the years.

"Our Strategy A funds have achieved an average gain of 18.5% net of fees over the past 13 years. For Strategy B funds, the average gain was 23% over nine years and 31% for Strategy C funds over eight years. So, the argument not to buy something because the fees are high is very wrong because you would lose all the high performance and the opportunity to diversify your portfolio in a non-correlated asset class," he points out. Baha even challenges investors to find a better-performing managed futures fund out there that charges a lower fee. "If you find a cheaper one, I would recommend that you invest there. It is not easy to find a good managed futures fund."

20 best performing Singapore-registered alternative/hedge funds

NAME	CLASS	1-YR % VALUE
Superfund Cayman	Hedge/Managed Futures	65.93
Quadriga Superfund Futures C USD Class R	Hedge/Managed Futures	56.72
Superfund GCT USD	Hedge/Managed Futures	52.43
Quadriga Superfund Futures C EUR Class R	Hedge/Managed Futures	52.01
Superfund Gold B	Hedge/Managed Futures	43.93
Quadriga Superfund Futures B USD Class R	Hedge/Managed Futures	41.39
Quadriga Superfund Futures B EUR Class R	Hedge/Managed Futures	40.57
Superfund Gold C	Hedge/Managed Futures	37.31
ACL Alternative Limited	Hedge/Multi Strategies	37.30
Man AHL Diversified Plc	Hedge/Managed Futures	33.23
Superfund Gold A	Hedge/Managed Futures	31.87
James River Navigator Futures LLC A	Hedge/Managed Futures	30.20
Superfund Q-AG	Hedge/Managed Futures	29.53
Man AHL Currency	Hedge/Global Macro	28.91
Quadriga Superfund Futures A EUR Class R	Hedge/Managed Futures	28.53
Man AHL Diversified Markets EU	Hedge/Global Macro	26.38
Aspect Diversified USD	Hedge/Managed Futures	25.39
Permal Systematic Macro Ltd A	Hedge/Global Macro	25.13
Man AHL Diversified Futures Ltd	Hedge/Managed Futures	24.93
Winton Futures B USD	Hedge/Managed Futures	21.09

Information as at Dec 31, 2008

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Trend followers continue to do well

Looking ahead, managed futures, one of only two hedge-fund strategies that made money last year (the other one being dedicated short bias), are likely to continue to shine this year, according to hedge-fund research firms.

"We expect trend following and arbitrage strategies in the commodity and currency markets to be profitable in the near term, says a December report by Asia hedge-fund research firm Eurekahedge. A recent report by Credit Suisse/Tremont offers similar views. "The managed-futures sector has continued to deliver despite adverse market conditions, generating positive performance and bolstering investor confidence in the strategy. While the hedge-fund industry as a whole has experienced net outflows for 2008, the sector [saw] positive inflows every month [last] year, even during months of negative performance."

For his part, Baha says as long as the financial markets in 2009 continue to exhibit strong directional trends both up and down, he is confident his funds will maintain their winning streak. To generate alpha or excess returns, he reveals that his research team of 20 employees is currently trying to develop trading strategies that would take advantage of very short-term market trends, which are uncorrelated to the longer-term market direction. If team succeeds in developing such a strategy, that could be another avenue for gain making for his range of funds, he tells *Personal Wealth*.

According to a recent Bloomberg report, Superfund plans to hire 110 people, increasing its staff by 25% in 2009. Superfund, which employs 440 staff worldwide, will be adding jobs in marketing, public relations, sales, trading, programming and legal operations in a bid to boost AUM by as much as 30% this year, Baha told Bloomberg.

As to when Superfund's products will be available to the man-on-the-street in Singapore, Baha says he hasn't got a clue. "It is in the hands of the regulators in Singapore to make an asset class like managed futures publicly available and not to discriminate against it in favour of money-losing asset classes and risky investments like stocks, real estate and derivatives." E