Capital Trading Group
One Financial Place
440 S LaSalle Street, Suite 2301
Chicago, IL 60605
Ph: 800.238.2610
www.CTGtrading.com

They say "early birds get the worm." Yet, for most emerging CTA managers, early-bird investors are notoriously hard to come by.

It's a classic Catch-22. Allocators want to see AUM and a track record before investing with an emerging manager. But emerging managers need AUM to build a track record and prove themselves capable of running a solid business.

Faced with the perception that established managers are less risky than emerging managers, a majority of investors take the "easy" road and invest with the big boys. Although, as is often true in life and the markets, the "easy" road isn't always the "best" road.

Let's first explore the underappreciated value of investing with an emerging manager. Then we'll tackle common objections… and how to overcome them.

For one, emerging managers are hungry! If success breeds complacency, emerging managers have none of the fat-and-happy syndrome that can make established managers slip. What they do have is new ideas, cutting-edge research and novel strategies.

It's hard to teach an old dog new tricks. But "new tricks" are precisely in the wheelhouse of "new managers." Therefore, emerging managers can flex competitive advantage in their ability to bring new strategies to market. And from an investor's perspective, staying ahead of the curve often requires listening to an emerging manager's fresh perspective.

Emerging managers can also be more flexible and nimble than established managers, whose capacity to employ niche strategies and trade in liquidity-challenged markets can become significantly constrained as their AUM grows. Those constraints can lead to a number of challenges for large managers, including decreased returns and decreased diversification.

Various studies have shown the tendency for the returns of large, established managers to cluster around the group's median return. This could be because large managers are increasingly forced into financial sector markets (highly liquid), and out of smaller diversifying markets (less liquid), as their AUM grows. It could also be explained by the tendency for large managers to become increasingly risk averse as their management fees grow. Either way, compressed dispersion of returns is typical among large, established mangers.

Meanwhile, several studies have also shown that emerging managers are generally able to produce higher returns than established managers. Aggarwal and Jorian[1] completed one such study, analyzing the returns of nearly 1,000 hedge funds, including managed futures (CTA) programs, over a 10-year period. They found that emerging managers were able to produce 2.3% excess alpha during their first

two years of trading. Excess returns for individual funds were persistent for up to five year, then subsequent returns decreased by an average of 42 basis points each year thereafter.

Finally, early-bird investors can often negotiate attractive fees structures with emerging managers and pay far less than the standard 2/20. Cliff Asness of AQR has said the only way he's found to increase the returns of a trend-following strategy is to *charge lower fees* for it. And of course Jack Bogle of The Vanguard Group would whole-heartily agree with that sentiment – "a penny saved is a penny earned."

All told, there are clear advantages, from multiple perspectives, to investing with emerging managers. And so it begs the question: *what's stopping investors from doing so?*

We believe it comes down to the perception of risk.

Psychologically, it's easier for individual investors and institution allocators alike to "herd" invest with a small group of the biggest and most established managers. It *feels* safer, psychologically, even if it isn't the optimal thing to do.

Indeed, overcoming that psychological barrier is a formidable challenge. But it can be done. You just have to ask the right questions.

Due diligence is an important process for all allocation decisions, but particularly so for investors considering emerging managers. That's why we recommend individual investors seek the guidance of trusted managed futures veterans, like Capital Trading Group. Our experience with emerging managers allows us to separate the wheat from the chaff, so to speak, and match investors with the emerging managers who are best aligned with their investment objectives.

Principal - Nell Sloane

Nell Sloane is a principal and co-owner of Capital Trading Group (CTG). Nell began her career over 30 years ago at the Chicago Futures Exchanges. She initiated her introductory to the industry by working for a grain trader at the CBOT. As she continued to handle the trade execution, reconciliation and capital raising, she moved on to becoming a featured contributor to various online industry related publications. Nell eventually launched her own commodity newsletter providing fundamental and technical analysis entitled "The Opening Belle".

Her registrations include the Series 3 and 7. Ms. Sloane presently is a member of the Vistage International, which is the world's leading chief executive organization helping business owners make better decisions and becoming better leaders in their communities. She is an active participant in raising money for charities such as American Cancer Society, Mercy Home for Boys and Girls, Diabetes foundation and Make-a-Wish. Nell previously volunteered with the international au pair agency matching host families with childcare and was previously an Executive Member of Chicago Finance Committee. During her spare time she loves to golf, horseback ride and travel.

If you have any questions about this article, please feel free to call CTG at **800.238.2610** or email at nsloane@CTGtrading.com

DISCLAIMER: Capital Trading Group, LP ("CTG") is an Introducing Broker and a member of the NFA. CTG does not warrant the correctness of any information herein or the appropriateness of any transaction. The contents of this electronic communication and any attachments are for informational purposes only and under no circumstances should they be construed as an offer to

sell or a solicitation to buy any futures contract, option, security, or derivative including foreign exchange. The information is intended solely for the personal and confidential use of the recipient of this electronic communication. If you are not the intended recipient, you are hereby notified that any use, dissemination, distribution or copying of this communication is strictly prohibited and you are requested to return this message to the sender immediately and delete all copies from your system. All electronic communication may be reviewed by authorized personnel and may be provided to regulatory authorities or others with a legal right to access such information. At various times, CTG may have positions in and effect transactions in securities or other financial instruments referred to herein. Opinions expressed herein are statements only of the date indicated and are not given or endorsed by CTG unless otherwise indicated by an authorized representative. Due to the electronic nature of electronic communication, there is a risk that the information contained in this message has been modified. Consequently, CTG cannot guaranty that messages or attachments are virus free, do not contain malicious code or are compatible with your electronic systems and CTG does not accept liability in respect of viruses, malicious code or any related problems that you may experience. Trading in futures or options or other derivatives entails significant risks which must be understood prior to trading and may not be appropriate for all investors. Please contact your account representative for more information on these risks. Past performance of actual trades or strategies cited herein is not necessarily indicative of future performance. Privacy policy available upon request.