

A quarter to forget

At a glance

	Q1	Q2
Trend-based	9.1%	(12.3%)
Discretionary	4.4%	(3.3%)
Systematic	2.8%	(4.4%)
Trading subsectors		
Currency	2.2%	(5.4%)
Diversified	5.7%	(8.7%)
Financial	5.3%	(5.2%)
Stock-index	3.3%	1.1%

The second quarter of 2004 will undoubtedly be one many trading advisors would prefer to forget. Trend-based traders suffered the most, losing a whopping 12.3%, compared with a gain of 9.1% in the first quarter.

In the trading subsectors, diversified traders took the biggest hit, losing 8.7%. Only stock index traders stayed in positive territory, returning 1.1%, compared with a gain of 3.3% in the first quarter.

UK-based **Oxeye Capital Management's** Futures and Options program topped the charts in the stock-index category, up 9.5% for the quarter and

22.3% for the year. The program's ideal scenario is to sell high volatility and buy low volatility. "The markets suited us down to the ground because the year started with relatively low volatility but it just kept getting lower," says **Oxeye's Martin Petherick**. The challenge for the next six months, he says, will be to manage the move from a low volatility to a high volatility environment.

Ansbacher Investment Management in New York also benefited from lower stock index volatility. Its program sells options short in the hope of profiting when they expire worthless, an outcome more likely to occur in low volatility markets.

"So the market played into our hands very nicely," says Max Ansbacher, whose program was up 6.9% for the quarter.

Currency and financials traders were not so fortunate. A lack of trends and a distinct transition from low to high volatility currency markets made it difficult for many to find solid ground.

Most losses occurred in April, when advisors were caught up the proverbial creek without a paddle—a trend, any trend, with which to row to shore.

"A lot of currency trading models rely on a trend type of behavior, but that tends to only succeed when there is sufficiently low volatility in the market to be effectively useful to trading," says Henry Green, the chief investment officer at Jacobson Fund Managers in London.

While stock-index traders were enjoying lower volatility markets, currency traders were navigating a transition to higher volatility markets. "We have left the low volatility market, which were the classic conditions from which to benefit from purely trend following returns," says Green.

Nevertheless, Jacobson navigated this transition relatively well compared with its peers, with its two leveraged programs down only 0.5% and 1.3% for the quarter. The firm's global macro program was up 1.2%.

Volatility was a major reason for recent losses, says John Taylor, founder and chairman of New York-based FX Concepts. "The first Friday of every month when the US announced employment numbers, there was outrageous volatility every time no matter what that number was," he says.

The firm's Global Currency and Developed Markets Currency programs were down 3.9% and 3.7%, respectively.

The erratic market behavior of recent months was not a surprise to Taylor, whose programs had predicted as much. But knowing what was around the corner was only half the battle.

He says the markets were extremely difficult to trade because many of the carry trades that had been successful for FX in the second half of 2003 needed to be unwound to adjust to 2004 conditions.

"It is hard to completely get out of something right away because the system only makes gradual steps," says Taylor. "How much money can one move out of the New Zealand dollar in a short amount of time? Not very much."

Advisors that were well placed to benefit from a strengthening US dollar were also caught out when this didn't happen. Nevertheless, Taylor believes the US dollar and interest rates will weaken sooner than later, an opinion that puts him in a distinct minority.

"I personally think that the US economy will be turning down by the election," he says.

Despite declining returns, assets continued to flow into managed futures at an impressive rate. FX Concept's Developed Markets Currency program finished June with \$3.2 billion under management after adding \$670 million during the second quarter and \$532 million in the first.

The firm also received an additional \$2 billion to be managed as part of a managed account. These commitments brought the firm's assets to approximately \$11 billion.

Netherlands-based Transtrend saw assets in its Enhanced Risk USD program rise above \$1 billion after adding \$105 million in the second quarter. This came despite a 5.3% loss for the period.

Connecticut-based Graham Capital's DTG program, which crossed the \$1 billion threshold in the first quarter, added a further \$240 million in the second quarter.

Some programs fell below asset milestones. RG Niederhoffer Capital Management's onshore program dipped below \$1 billion to end June at \$985 million.

Assets in Connecticut-based Quantitative Financial's IPS Currency Program also lost ground, falling below \$2 billion in May after having reached that point in January. The firm's Global Macro program maintained assets above the \$1 billion mark—a milestone it achieved in February this year.

By Elise Coroneos