

Managed Futures Research Series – Part 1

Debunking Return and Performance Volatility
Misperceptions – Over a Quarter Century



Alternative Investment
Strategies

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Hypothesis

The intent of this research is to dispel the myths around managed futures as an inferior asset class compared to stocks and bonds.

Data

This research studies and contrasts 25 years of data from five widely known benchmarks:

- S&P 500 Total Return Index
- MSCI World Index
- GSCI Total Return Index
- JP Morgan World Government Bond Index
- Barclay CTA Index (managed futures)

Methodology

1. Examination of average returns over multiple time horizons.
2. Examination of average negative returns and number of negative performing periods over multiple time horizons.
3. Value Added Monthly Index, standard deviation, Sharpe and Sortino ratio, average losing and winning ROR, and drawdown studies are presented to depict alternate methods of examining long-term return and performance volatility.
4. Asset class performance during specific market cycles is assessed.

Executive summary

This study reveals that managed futures as an asset class have sustained attractive and consistent historical returns, draw downs, and volatilities compared with its peers, dispelling any time-worn misperceptions of the asset class.

Managed futures should be considered by long term investors as a source for long-term, consistent, risk-adjusted returns in a myriad of market cycles.

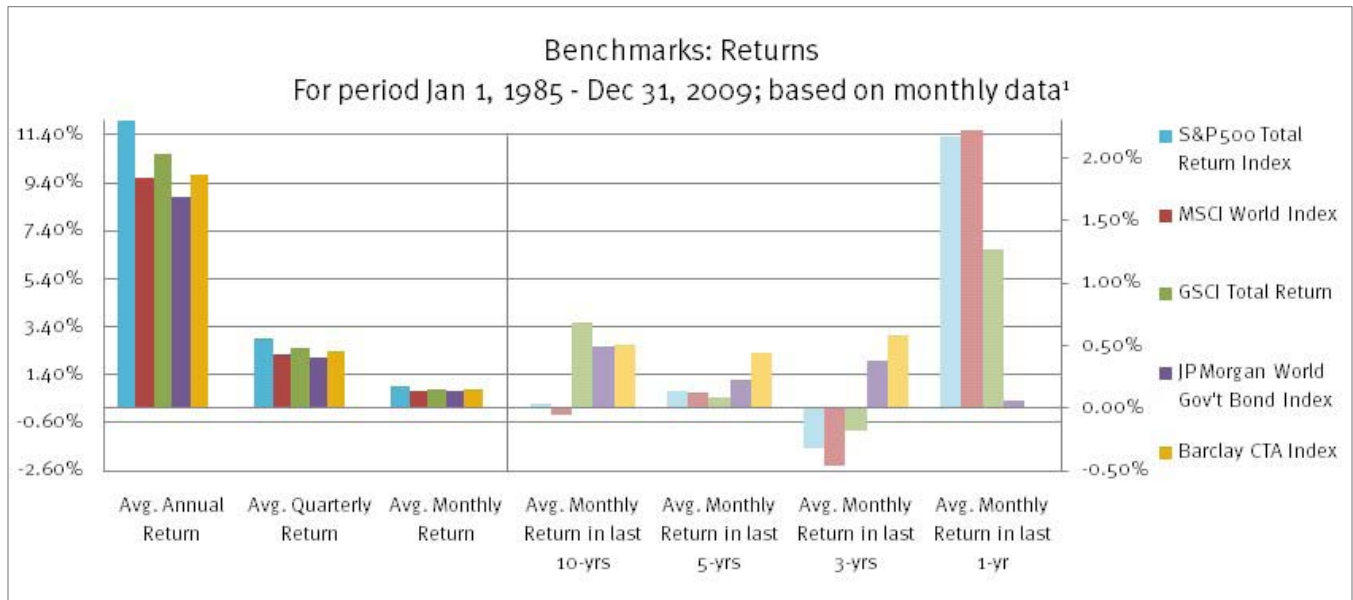
About managed futures

Managed futures are a form of alternative investment that take long or short positions in futures contracts in areas such as equity indices, currencies, and government securities, as well as traditional commodities such as metals and grains. Managed futures have historically displayed very low correlations to traditional investments such as stocks and bonds. This lack of correlation stems from the fact that managed futures draw their returns from different fundamental factors than traditional investments.

Misperception 1: managed futures haven't performed well over the long term.

This misperception is a common one, as most believe they are exclusively a short term strategy. To disprove this point, below, we illustrate the returns of managed futures compared against the returns of four benchmarks on an average annual, quarterly, and monthly basis between January 1st, 1985 and December 31st, 2009. Average monthly returns are then compared looking at the last ten years, five years, three years, and 12 months, ending December 31st, 2009.

The chart reveals that the average returns of managed futures over a 25-year time period are highly comparable to all other benchmarks on an annual, quarterly, and monthly basis. It also clearly displays that the average monthly returns of managed futures, with the exception of 2009, have outperformed most other benchmarks over multiple durations of time.



¹Source: Data gathered from BarclayHedge, Ltd.

Conclusion

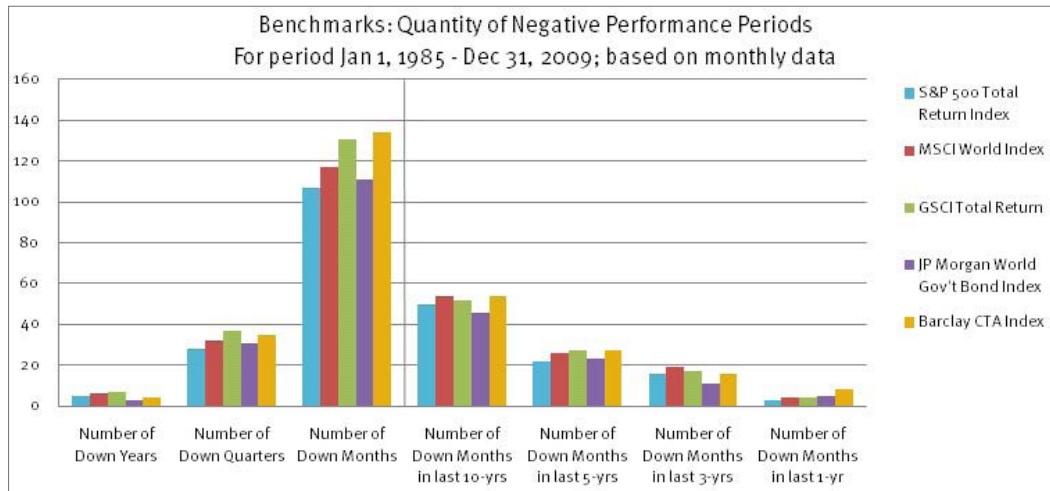
Managed futures not only exhibit average returns similar to their peers in the short term, but also over a longer time horizon and throughout various market cycles.

Misperception 2: managed futures have significantly more negative returns than securities.

This is probably the single largest misperception regarding managed futures as most believe they are very volatile compared with their peers.

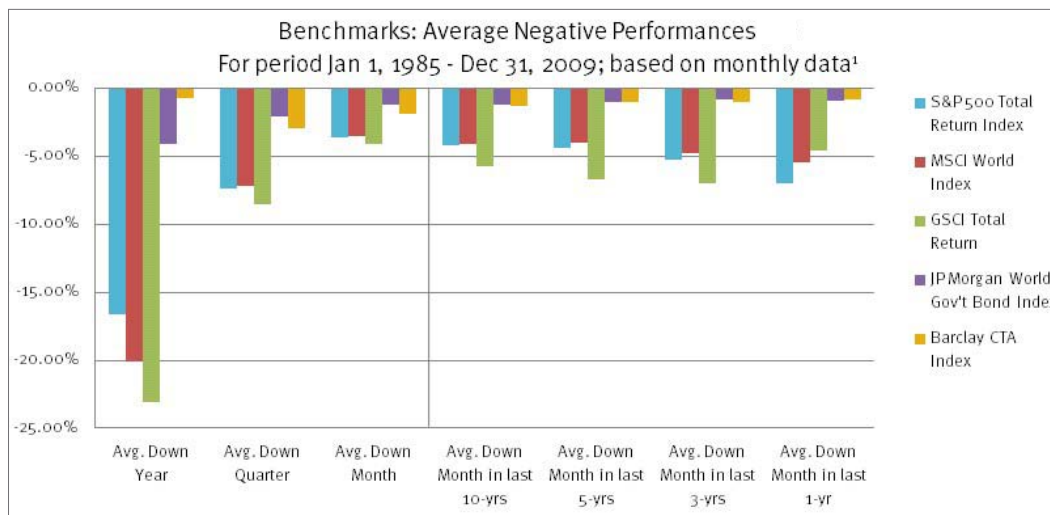
To counter this perception, the chart below illustrates the number of average down years, quarters, and months as well as the number of down months each benchmark has incurred over a ten-year, five-year, three-year, and 12-month period ending December 31st, 2009.

While the chart below demonstrates that the number of down periods for managed futures is slightly higher in some time frames....



Source: Data gathered from BarclayHedge, Ltd.

....the subsequent chart proves that the performance magnitude of managed futures' down periods is materially lower than with other asset classes.



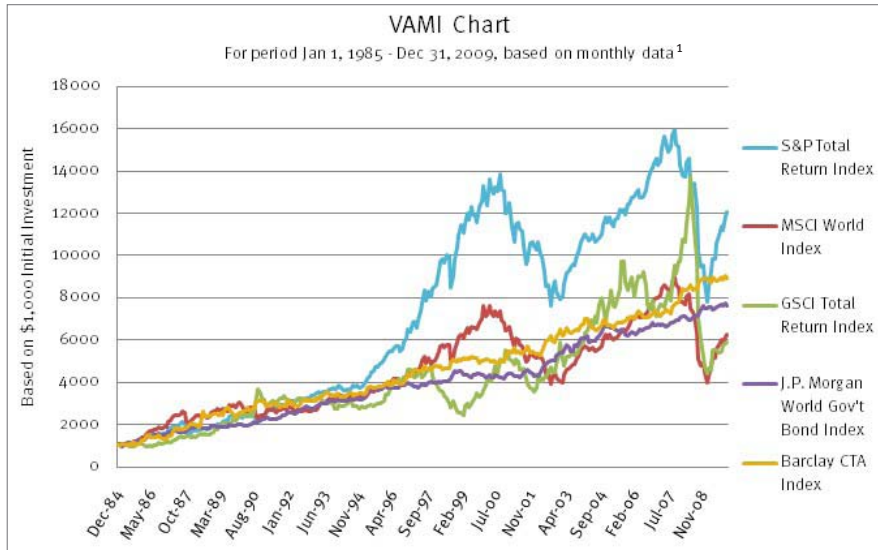
Source: Data gathered from BarclayHedge, Ltd.

Conclusion

While managed futures tend to have slightly more losing periods in some time frames, they tend to lose less money than other asset classes during down periods. Managed futures also exhibit less downside deviation than their peers over multiple time horizons and throughout various market cycles.

Misperception 3: managed futures are much more volatile than securities markets.

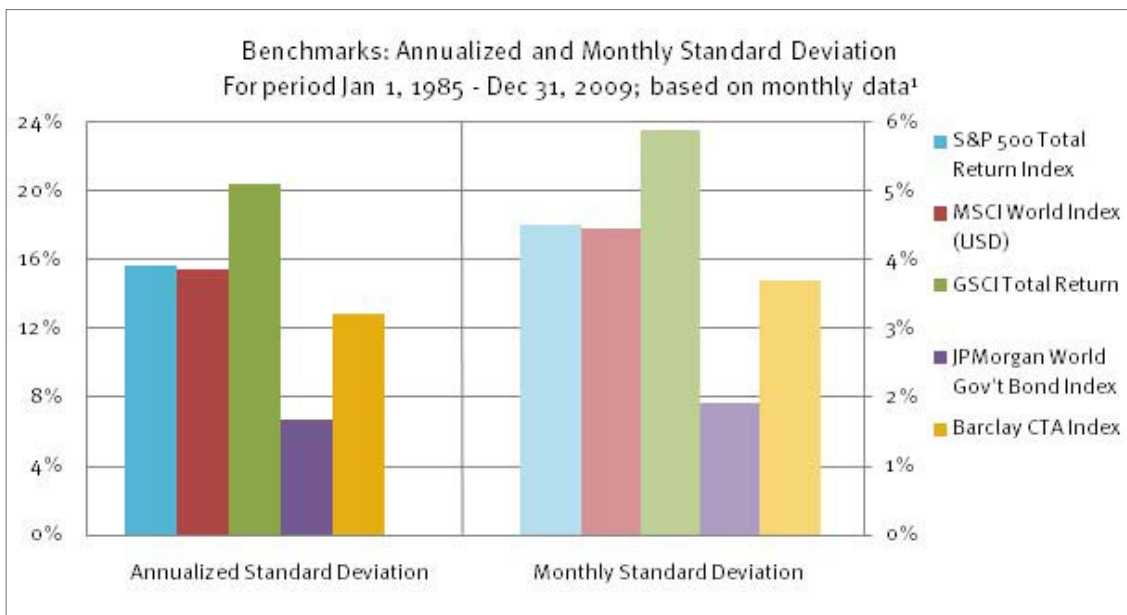
To disprove this point, we will look at performance volatility represented in a few ways. In the following diagrams, the Value Added Monthly Index (VAMI), the annualized and monthly standard deviations, the Sharpe and Sortino ratios, the average monthly losing and winning rates of return, and the draw downs of these five asset classes are observed.



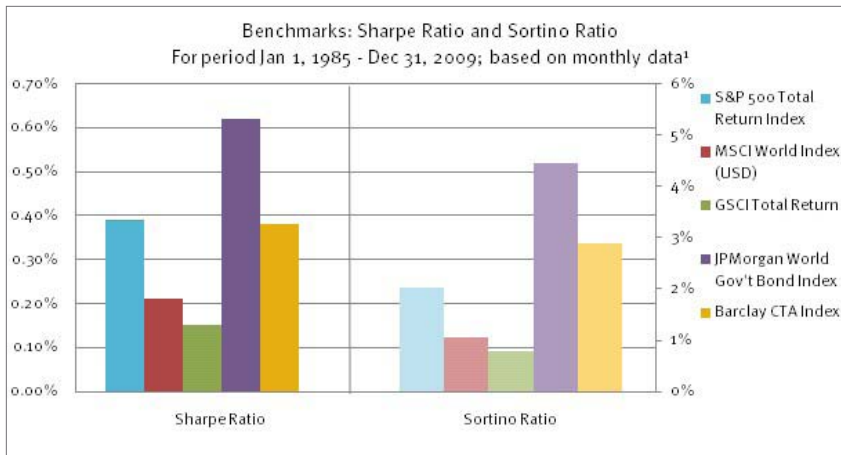
¹Source: Data gathered from BarclayHedge, Ltd.

The above graph shows the return of a \$1,000 investment in each of the five asset classes. Observing the returns displayed by each asset class over a 25-year span, it is evident that the performance volatility of managed futures is on the lowest end of the spectrum compared with its peers.

The below tables provide a few alternate examples supporting managed futures' consistent performance relative to its peers. Observing the annualized and monthly standard deviations, managed futures demonstrate lower percentages of standard deviation, illustrating more consistent returns.

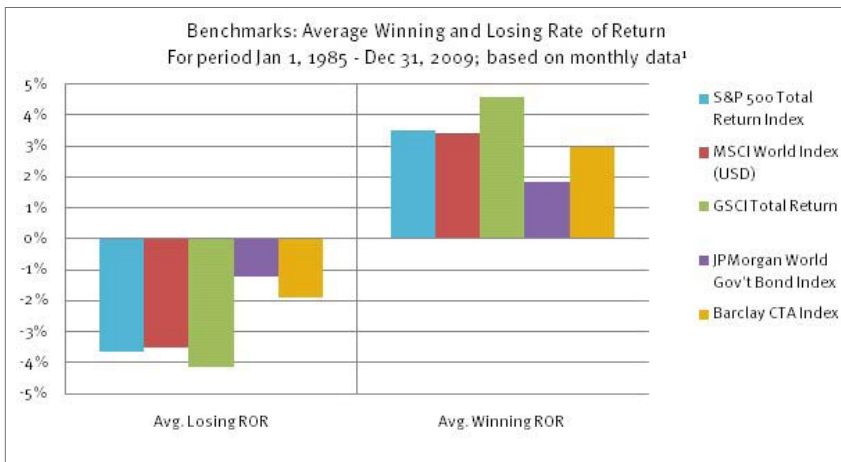


¹Source: Data gathered from BarclayHedge, Ltd.



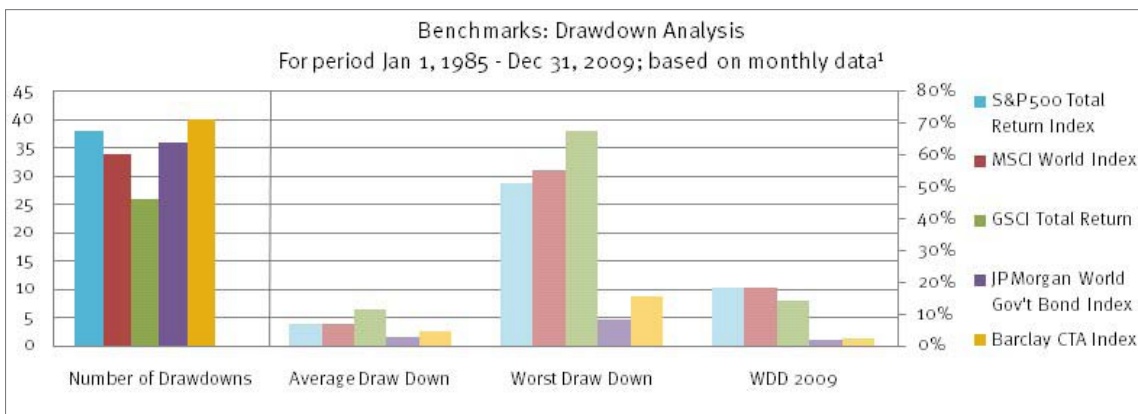
¹Source: Data gathered from BarclayHedge, Ltd.

Managed futures also maintain comparable or higher Sharpe and Sortino ratios when contrasted with the other benchmarks. In both cases, a higher ratio could indicate better risk-adjusted performance and/or lower volatility by the asset class.



¹Source: Data gathered from BarclayHedge, Ltd.

Additionally, the consistency of managed futures' performance is exemplified by the average losing and winning rates of return – in both cases displaying less erratic average monthly return percentages.



¹Source: Data gathered from BarclayHedge, Ltd.

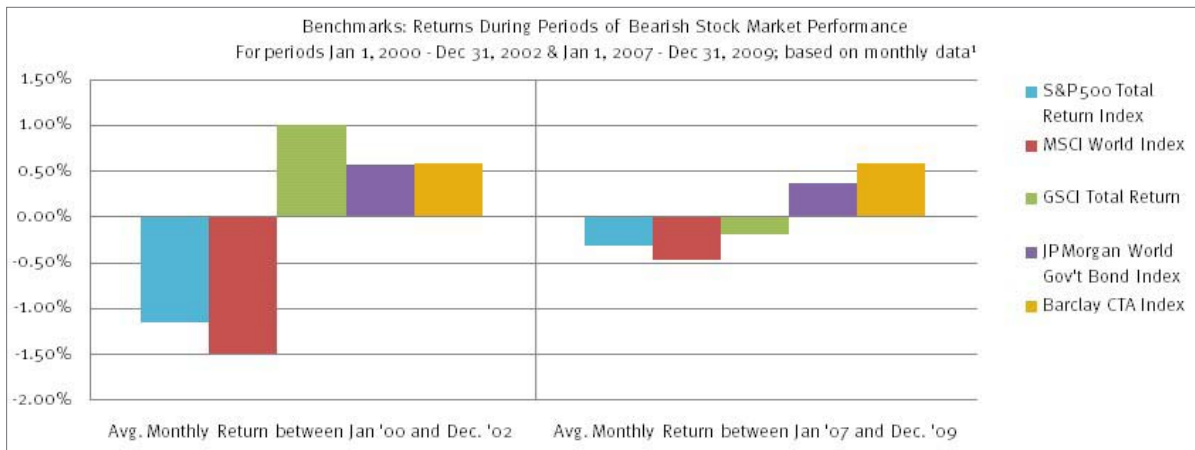
The last chart presents a drawdown analysis of the five benchmarks. This analysis further supports the consistency of managed futures' returns, with the average draw down and worst draw down of managed futures at some of the lowest levels among its peers.

Conclusion

The data clearly shows that managed futures exhibit fewer extreme up and down movements in performance, thus indicating less performance volatility compared with its peers.

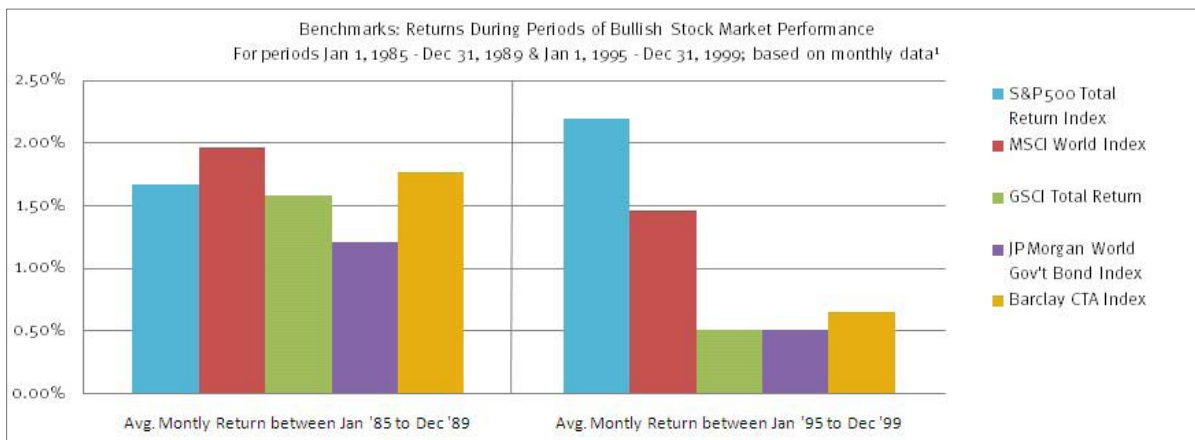
Misperception 4: managed futures only perform well when securities are down.

Finally, let's examine the performance of indices during notorious bull and bear markets. The following chart provides the average monthly returns of the five asset classes between two economically bearish periods.



¹Source: Data gathered from BarclayHedge, Ltd.

Most investors presume that managed futures outperform other asset types during bearish market cycles, but what is even more interesting is that managed futures also display positive average monthly returns during periods of bullish economic activity as the chart below indicates. Subsequently, the misperception that managed futures only perform well when traditional asset classes underperform is dispelled by this data.



¹Source: Data gathered from BarclayHedge, Ltd.

Conclusion

Managed futures have historically demonstrated positive monthly returns in both landmark bear and bull markets, disproving that the asset class only performs positively in times of economic duress.

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Key summary

The statistics presented in this study all point to the same conclusions: Long held misperceptions about managed futures are unfounded when the data is examined. The idea that managed futures are an unreliable performance driver and only suitable for short term, highly speculative traders is misplaced.

Additionally, since managed futures are capable of taking long and/or short positions in various markets (commodities, financials, foreign exchange, etc) and can exhibit negative correlations during bearish economies and positive correlations during bullish economies, it disproves that managed futures are only suitable as a portfolio hedge, acting as a source of return during poor market environments.

What's to come

In the second part to our research series, we will conduct further analysis of the correlation between the performance of managed futures and traditional asset types in various market cycles, debunking the misperception that managed futures are only negatively correlated to the market at large.

About MF Global

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We have designed our managed futures business to leverage several of MF Global's core competencies

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- Institutional risk management: A rigorous process of manager review and analysis.
- Futures leadership: Unparalleled knowledge of futures markets, trends, and trading strategies.

MF Global leverages these core strengths to provide professional money managers and serious investors access to unparalleled investment resources in the managed futures arena.

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