Peltz International, Inc.

Meet the Niche Manager: Global Macro Seminar

New York

May 23, 2018

Ted Parkhill

Nate Polachek

One of the main themes at Peltz International's "Meet the Niche Manager: Global Macro Seminar" last week was the advantage held by smaller managers.

"This is a huge advantage for smaller managers who can trade more arcane markets like tin, rubber, and lumber," said Ted Parkhill of Incline Investment Management, a trend following commodity trading advisor. "Recently we've made a lot of money in lumber. Many of the larger managers can't trade lumber because of their asset size. Smaller managers can."

Nate Polachek of Commodity Asset Management agreed. His firm focuses specifically on the industrial commodities complex, including aluminum, zinc, palladium, and tin. In his view, niche constrained strategies are where the edge is. He doesn't see the edge the mega-managers used to have.

Parkhill takes the view that some of the large funds are constrained more than they would like to have you know. "They pretend they are as diversified as the rest of us but they aren't. Some are so large, they can't trade markets like corn because they would bump into positions limits. So, they would have to trade bonds where there is capacity."

Polachek points out that mega funds can't shift on a dime. If there is a crisis situation, they can't easily get out of positions quickly. "We are capacity constrained - the maximum size we can go in our fund is $750 million. We invest in commodities like tin which has a ~$700 million open interest; for mega-funds that are trading hundreds of billions of dollars, tin is by and large not traded, as it doesn't move the needle."

Having worked at AQR and Bridgewater, where each fund owns significant percentages of the open interest in the markets Commodity Asset Management trades, Polachek says they have an edge in knowing how, and when they are going to trade.

Doing due diligence

In doing diligence on managers, Parkhill emphasizes that portfolio construction is what matters. Figure out how the portfolios are constructed when you look at managers.

Parkhill recommends asking what markets are traded. Many managers say they are diversified but they aren't. Ask them how often they trade these markets and what the core portfolio looks like.

Some systematic firms that boast several PhDs are pure window dressing. Ask who is managing the money? How the systems are run? Where does the buck stop?

Role of technology helps compete with larger managers

With technology, small managers can produce alpha and results that are comparable to the results of the largest managers. Parkhill observes that is why small managers are attractive.

At Commodity Asset Management, two people manage the portfolio. They also do the trading and have broker desks as back-ups. They monitor the markets 24/7. They've set up a system of alerts. Anytime a market hits a level, it alerts the two principals wherever they are. "As a niche manager, we can manage to the degree that the largest managers do. We've found off-the-shelf risk products that get us 95% of the way to where some of the largest managers are. A lot of good technology exists," adds Polachek.