CFTC Risk Disclosure Statement

THE RISK OF LOSS IN TRADING COMMODITIES CAN BE SUBSTANTIAL. YOU SHOULD THEREFORE CAREFULLY CONSIDER WHETHER SUCH TRADING IS SUITABLE FOR YOU IN LIGHT OF YOUR FINANCIAL CONDITION. THE HIGH DEGREE OF LEVERAGE THAT IS OFTEN OBTAINABLE IN COMMODITY TRADING CAN WORK AGAINST YOU AS WELL AS FOR YOU. THE USE OF LEVERAGE CAN LEAD TO LARGE LOSSES AS WELL AS GAINS.

IN SOME CASES, MANAGED COMMODITY ACCOUNTS ARE SUBJECT TO SUBSTANTIAL CHARGES FOR MANAGEMENT AND ADVISORY FEES. IT MAY BE NECESSARY FOR THOSE ACCOUNTS THAT ARE SUBJECT TO THESE CHARGES TO MAKE SUBSTANTIAL TRADING PROFITS TO AVOID DEPLETION OR EXHAUSTION OF THEIR ASSETS. THE DISCLOSURE DOCUMENT CONTAINS A COMPLETE DESCRIPTION OF THE PRINCIPAL RISK FACTORS AND EACH FEE TO BE CHARGED TO YOUR ACCOUNT BY THE COMMODITY TRADING ADVISOR ("CTA").

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To access the database:

1. Request a pin number at altavra.com.
2. After you receive your pin number, you can access the database at portfolio.altavra.com.
3. In the database, click on “List of Programs” at the top of the page to view all of the programs in the database.

*PLEASE NOTE: There is no fee to access the database. This is not a trial access. The pin number does not expire.

Managed Futures: Glossary of Terms

A

Active Management

Refers to the use of a human element – such as a single manager, co–managers, or a team of managers – to actively manage an investment portfolio. Active managers rely on analytical research, forecasts and their own judgment and experience in making investment decisions on what securities to buy, hold and sell. The opposite of active management is called passive management, better known as indexing. Investors who believe in active management do not follow the efficient market hypothesis. They believe it is possible to profit from the stock market through any number of strategies that aim to identify mispriced securities. Investment companies who believe it possible to outperform the market employ professional investment managers to manage one or more of the company's product offerings. The objective with active management is to produce better returns than those of passively managed investments.

Absolute Return

An outright return achieved irrespective of overall market direction. Whereas traditional investments typically measure their success in terms of whether they track or outperform a key market benchmark or index (relative returns), hedge funds, Commodity Trading Advisors (CTAs) and alternative investment strategies aim to achieve outright positive returns irrespective of whether asset prices or key market indices rise or fall (i.e. absolute returns rather than relative returns).

Accredited Investor

An accredited investor is a sophisticated investor who meets or exceeds minimum SEC requirements for net worth and annual income especially as they relate to some restricted offerings. The SEC Criteria are as follows.

Any director, executive officer, or general partner of the issuer of the securities being offered or sold, or any director, executive officer or general partner of a general partner of that issuer.

Any natural person whose individual net worth or joint net worth with that person's spouse, at the time of his purchase exceeds $1,000,000.

Any natural person who had individual income in excess of $200,000 in each of the two most recent years or joint income with that person's spouse in excess of $300,000 in each of those years and has a reasonable expectation of reaching the same income level in the current year.

Any trust with total assets in excess of $5,000,000, not formed for the specific purpose of acquiring the securities offered, whose purchase of the securities is directed by a person who has such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment.

Any organization that was not formed for the purpose of acquiring the securities being sold, with total assets in excess of $5,000,000.And, any entity in which all of the equity owners are Accredited Investors.

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Active Risk
A type of risk that a managed portfolio creates as it attempts to beat the returns of the benchmark against which it is compared. In theory, to generate a higher return than the benchmark, the manager is required to take on more risk. This risk is referred to as active risk. The more an active portfolio manager diverges from a stated benchmark, the higher the chances become that the returns of the fund could diverge from that benchmark as well. Passive managers who look to replicate an index as closely as possible usually provide the lowest levels of active risk, but this also limits the potential for market–beating returns.

Aggregation
The policy under which all futures positions owned or controlled by one trader or a group of traders are combined to determine reportable positions and speculative limits

Alpha
Widely considered to be a measure of the "value added" by an investment manager. It is therefore regarded as a proxy for manager or strategy skill. Alpha is sometimes described as out performance of a benchmark or the return generated by an investment independent of the market – what an investment would hypothetically achieve if the market return was zero. More specifically, alpha is sometimes described as the return of an investment less the risk–free interest rate, or the return of the portfolio less the return on the S&P 500 index or some other relevant benchmark index.

Alpha Generator
Any security that, when added to an existing portfolio of assets, generates excess returns or returns higher than a pre–selected benchmark without additional risk. An alpha generator can be any security; this includes government bonds, foreign stocks, or derivative products such as stock options and futures. Keep in mind that alpha itself measures the returns a portfolio produces in excess of the return originally estimated by the capital asset pricing model, on a risk–adjusted basis. Therefore, an alpha generator adds to portfolio returns without adding any additional risk, as measured by volatility or downside volatility. This follows modern portfolio theory in allowing investors to maximize returns while keeping a certain level of risk.

Alternative Investment
The terms "alternative investment" and "hedge fund" often get used interchangeably as hedge funds are an important and growing part of the alternative investment arena, which also includes private equity and debt, venture capital and real estate. Do not confuse hedge funds with Managed Futures. Managed futures clients have their funds held in segregated accounts at a Futures Commission Merchant (FCM).

In the field of asset management, the essential defining features of alternative investments are: the pursuit of absolute returns. That is: The quest to achieve a positive return regardless of whether asset prices are rising or falling.

Freedom to trade in a wide range of assets and instruments employing a variety of styles and investment techniques in diverse markets.

Reliance on the investment manager's skill and application of a clear investment process to exploit market inefficiencies and opportunities with identifiable and understandable causes and origins.

Alternative investment managers may take advantage of pricing anomalies between related financial instruments, engage in "momentum" investing to capture market trends, or utilize their expert knowledge of markets and industries to capture profit opportunities that arise from special situations. The ability to use derivatives, arbitrage techniques and, importantly, short selling – selling assets that one does not own in the expectation of buying them back at a lower price – affords alternative investment managers rich possibilities to generate growth in falling, rising and unstable markets.

Analysis of Variance (ANOVA)
A statistical analysis tool that separates the total variability found within a dataset into two components, random and systematic factors. The random factors do not have any statistical influence on the given dataset, while the systematic factors do. The ANOVA test is used to determine the impact independent variables have on the dependent variable in a regression analysis. The ANOVA test is the initial step in identifying factors that are influencing a given data set. After the ANOVA test is performed, the analyst is able to perform further analysis on the systematic factors that are statistically contributing to the data set's variability. ANOVA test results can then be used in an F–test on the significance of the regression formula overall.

Annualized Compound Rate of Return
The rate of compound return (ROR) shown on an annualized basis. Obviously the higher the Rate of Return (ROR), the greater the historical annualized rate of performance.

Arbitrage
The technique of exploiting pricing anomalies between related financial instruments within and between markets with the aim of producing positive returns independent of the direction of broad market prices. By establishing long positions in under–valued assets and short positions in over–valued assets, arbitrageurs aim to capture profit opportunities that arise from the changing price relationship between the assets concerned. Specific investment styles that apply arbitrage techniques include convertible bond arbitrage, fixed income arbitrage, statistical arbitrage, and merger or risk arbitrage.

Arbitration
The process of settling disputes between parties by a person or persons chosen or agreed to by them. NFA's arbitration program provides a forum for resolving futures–related disputes between NFA Members or between Members and customers.

Associated Person (AP)
An individual who solicits orders, customers or customer funds on behalf of a Futures Commission Merchant, an Introducing Broker, a Commodity Trading Advisor or a Commodity Pool Operator and who is registered with the Commodity Futures Trading Commission.

At–the–Money Option
An option whose strike price is equal, or approximately equal, to the current market price of the underlying futures contract.

Average Annual Return (AAR)
A percentage figure used when reporting the historical return, such as the three–, five– and 10–year average returns of a Commodity Trading Advisors' managed program. The average annual return is stated net of the programs operating expense ratio, which does not include sales charges, if applicable, or portfolio transaction brokerage commissions When you are selecting an investment program, the average annual return is a helpful guide for measuring the programs long–term performance. However, investors should also look at a program's yearly performance to fully appreciate the consistency of its annual total returns. For example, a five–year average annual return of 10% looks attractive; however, if the yearly returns (those that produced the average annual return) were +40%, +30%, –10%, +5% and –15% (50 / 5 = 10%), the program's recent performance (past three years) is quite poor.

Average Recovery Time (ART)
This is the average time in a recovery from a drawdown measured from the low point of the drawdown to a new peak.

B

Backwardation
A futures market in which the relationship between two delivery months of the same commodity is abnormal. The opposite of Contango.

Barclay Index
The Barclay CTA Index measures the composite performance of established programs. For purposes of this index, an established trading program is a trading program that has four years or more documented performance history. Once a trading program passes this four–year hurdle, its subsequent performance is included in this un-weighted index. The Barclay Index does not represent an actual portfolio, which could be invested in, and therefore the index performance results should be deemed to be hypothetical in nature and of comparative value only.

Barclay Ratio
This ratio was developed by Barclay Trading Group, Ltd. In simplest terms the Barclay Ratio is equal to the trend of the VAMI divided by the standard deviation of the monthly returns. Although similar in certain respects to the Sharpe Ratio, it has a much higher correlation with percentage of profitable 12–month time windows than any other reward/risk ratio.

Basis
The difference between the current cash price of a commodity and the futures price of the same commodity

Benchmark
A standard against which the performance of an investment manager can be measured. Generally, broad market and market–segment stock and bond indexes are used for this purpose. When evaluating the performance of any investment, it's important to compare it against an appropriate benchmark. In the financial field, there are dozens of indexes that

analysts use to gauge the performance of any given investment including the S&P 500, the Dow Jones Industrial Average, the Russell 2000 Index .

Beta
A measure of how sensitive an investment portfolio is to market movements. The sign of the beta (+/–) indicates whether, on average, the portfolio's returns move in line with the market (+), or in the opposite direction (–) to the market. If the beta of a portfolio relative to a benchmark index is equal to +1, then the returns on the portfolio follow those of the index. By definition, the beta of that benchmark index is +1. A portfolio with a beta greater than +1 tends to amplify the overall movements of the market, while a portfolio with a beta between 0 and +1 tends to move in the same direction as the market but not to the same extent. A portfolio with a beta of –1 tends to move in the opposite direction to the market.

C

Call Option
An option which gives the buyer the right, but not the obligation, to purchase ("go long") the underlying futures contract at the strike price on or before the expiration date.

Calmar Ratio
A ratio used to determine returns relative to drawdown's (downside) risk in a futures portfolio or other similar investment vehicles. The Calmar ratio is determined by dividing the compounded annual return by the maximum drawdown, using the absolute value.

Generally speaking, the higher the Calmar ratio the better. Some programs have high annual returns, but they also have extremely high drawdown risk. This ratio helps determine return on a downside risk–adjusted basis. Most Calmar ratios utilize 3 years of data.

Capacity
The amount of investment capital that can be comfortably absorbed by a manager or strategy without a diminishing of returns. One useful indication of whether or not a manager or strategy faces capacity constraints is to analyze the degree to which they experience slippage in the execution of their strategy or trades.

Capital Guarantee Fund
An investment vehicle offered by certain institutions that guarantees the investor's initial capital investment from any losses. Even though these products prevent investors from losing their invested capital, they also limit the amount of return that investors can obtain if the investments appreciate. This is how the offering institutions can afford to guarantee the principal investment.

Carrying Broker
A member of a futures exchange, usually a clearinghouse member, through which another firm, broker or customer chooses to clear all or some trades.

Cash on Cash Return
A rate of return commonly used in real–estate transactions. The calculation determines the cash income on the cash invested: Cash on Cash returns equal the annual dollar income divided by the total dollar investment.

Clear
The process by which a clearinghouse maintains records of all trades and settles margin flow on a daily mark–to–market basis for its clearing members.

Clearinghouse
An agency or separate corporation of a futures exchange that is responsible for settling trading accounts, collecting and maintaining margin monies, regulating delivery and reporting trade data. The clearinghouse becomes the buyer to each seller (and the seller to each buyer) and assumes responsibility for protecting buyers and sellers from financial loss by assuring performance on each contract.

Clearing Member
A member of an exchange clearinghouse responsible for the financial commitments of its customers. All trades of a non–clearing member must be registered and eventually settled through a clearing member.

Cluster Analysis
An investment approach that places investment instruments into groups based on the correlation found among their returns. Instruments with high positive correlations are grouped together and segregated from those with negative correlation. Between each cluster, very little correlation should exist. Holding investments in each cluster provides the investor with a diversified portfolio. Cluster analysis enables the investor to eliminate any overlap in his or her portfolio by identifying securities with related returns. This approach increases diversification, which provides the investor will a less risky portfolio.

Compound Annual Rate of Return (CARR)
The compounded ´growth´ of an investment that has been achieved each year to enable the initial price to grow to the latest selected price over a particular time period.

Commodity Futures Trading Commission (CFTC)
The federal regulatory agency established in 1974 that administers the Commodity Exchange Act. The CFTC monitors the futures and options on futures markets in the United States.

Commodity Pool
An enterprise in which funds contributed by a number of persons are combined for the purpose of trading futures or options contracts. Also referred to as a Pool.

Commodity Pool Operator (CPO)
An individual or organization which operates or solicits funds for a commodity pool. A CPO is generally required to be registered with the CFTC.

Commodity Trading Adviser (CTA)
The manager or adviser of a managed futures program. The term reflects the fact that early futures markets were commodities–based and were set up to enable producers and buyers to hedge against possible price movements in the underlying asset.

Commoditize
The act of making a process, good or service easy to obtain by making it as uniform, plentiful and affordable as possible. Something becomes commoditized when one offering is nearly indistinguishable from another. As a result of technological innovation, broad–based education and frequent iteration, goods and services become commoditized and, therefore, widely accessible. In the past few decades, previously "modern" things such as microchips, personal computers — even the internet itself — have become essentially commoditized.

Compound Annual Return
This is the rate of return which, if compounded over the years covered by the performance history, would yield the cumulative gain or loss actually achieved by the trading program during that period.

Compounding
The ability of an asset to generate earnings, which are then reinvested in order to generate their own earnings. In other words, compounding refers to generating earnings from previous earnings

Conditional Value at Risk (CVaR)
A risk assessment technique often used to reduce the probability a portfolio will incur large losses. This is performed by assessing the likelihood (at a specific confidence level) that a specific loss will exceed the value at risk. Mathematically speaking, CVaR is derived by taking a weighted average between the value at risk and losses exceeding the value at risk. This term is also known as "Mean Excess Loss", "Mean Shortfall" and "Tail VaR. Conditional Value at Risk was created to be an extension of Value at Risk (VaR). The VaR model does allow managers to limit the likelihood of incurring losses caused by certain types of risk – but not all risks. The problem with relying solely on the VaR model is that the scope of risk assessed is limited, since the tail end of the distribution of loss is not typically assessed. Therefore, if losses are incurred, the amount of the losses will be substantial in value.

Constant Proportion Portfolio Insurance (CPPI)
A strategy that synthetically reproduces the pay–out of a put or call option through dynamically adjusting the delta hedge of the underlying asset. Unlike a conventional option, the investment exposure (or participation) of the underlying asset will change over the life of the structure.

Contango
A futures market in which prices in succeeding delivery months are progressively higher. The opposite of Backwardation.

Convertible Arbitrage
Convertible Arbitrage involves purchasing a portfolio of convertible securities, generally convertible bonds, and hedging a portion of the equity risk by selling short the underlying common stock. Certain managers may also seek to hedge interest rate exposure under some circumstances. Most managers employ some degree of leverage ranging from zero to 6:1. The

equity hedge ratio may range from 30 to 100 percent. The average grade of bond in a typical portfolio is BB–, with individual ratings ranging from AA to CCC. However, as the default risk of the company is hedged by shorting the underlying common stock, the risk is considerably better than the un-hedged bond's rating indicates.

Convertible Bond

A bond issued by a company that has a set maturity date and pays interest in the form of a coupon. It has features of both a bond and stock and its valuation reflects both types of instrument. It gives the holder the option to convert the bond into a specific number of shares of the issuing company – in other words, it has an ´embedded option´.

Correlation

Correlation is a measure of the interdependence or strength of the relationship between two investments. It tells us something about the degree to which the variations of returns from their respective means move together. So if two investments are positively correlated, when one performs above its mean return it is likely that the other will also perform above its own mean return. If two investments are negatively correlated, when one performs above its mean return it is likely that the other will perform below its mean return. Note that correlation says nothing about the mean returns themselves – they could both be up, or both down, or one could be up and one down. To measure the strength of the relationship, we use the correlation coefficient. Values range from –1 (perfect negative correlation), through 0 (no correlation or uncorrelated) to +1 (perfect positive correlation). From a risk management perspective, it is generally favorable if two investments are uncorrelated because it means that there is no identifiable directional pattern or proportional relationship between the deviations of their monthly returns from each of their respective trends – sometimes investment B is positively correlated to investment A when the returns of A are positive and negatively correlated when they are negative, meaning that over a period of time our strategy returns get closer to non–correlation. This produces a smoother overall return profile.

Correlation Coefficient

A measure that determines the degree to which two variable's movements are associated. The correlation coefficient will vary from –1 to +1. A –1 indicates perfect negative correlation, and +1 indicates perfect positive correlation.

Covariance

A measure of the degree to which returns on two risky assets move in tandem. A positive covariance means that asset returns move together. A negative covariance means returns move inversely. One method of calculating covariance is by looking at return surprises (deviations from expected return) in each scenario. Another method is to multiply the correlation between the two variables by the standard deviation of each variable.

Covered Option

A short call or put option position which is covered by the sale or purchase of the underlying futures contract or physical commodity.

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Cross–Hedging

Hedging a cash commodity using a different but related futures contract when there is no futures contract for the cash commodity being hedged and the cash and futures market follow similar price trends (e.g., using soybean meal futures to hedge fish meal).

Cross Correlation

A statistical measure timing the movements and proximity of alignment between two different information sets of a series of information. Cross correlation is generally used when measuring information between two different time series. The range of the data is –1 to 1 such that the closer the cross–correlation value is to 1, the more closely the information sets are.

Cumulative Return

The aggregate amount that an investment has gained or lost over time, independent of the period of time involved. Presented as a percentage, the cumulative return is the raw mathematical return of the following calculation, Current price of Asset minus Original price of Asset divided by the Original price of Asset.

D

Deflation

A general decline in prices, often caused by a reduction in the supply of money or credit. Deflation can be caused also by a decrease in government, personal or investment spending. The opposite of inflation, deflation has the side effect of increased unemployment since there is a lower level of demand in the economy, which can lead to an economic depression. Declining prices, if they persist, generally create a vicious spiral of negatives such as falling profits, closing factories, shrinking employment and incomes, and increasing defaults on loans by companies and individuals. To counter deflation, the Federal Reserve (the Fed) can use monetary policy to increase the money supply and deliberately induce rising prices, causing inflation. Rising prices provide an essential lubricant for any sustained recovery because businesses increase profits and take some of the depressive pressures off wages and debtors of every kind.

Delta

The sensitivity of an option price to moves in the price of the underlying asset.

Derivatives

A financial instrument, traded on or off an exchange, the price of which is directly dependent upon the value of one or more underlying securities, equity indices, debt instruments, commodities, other derivative instruments, or any agreed upon pricing index or arrangement. Derivatives involve the trading of rights or obligations based on the underlying product but do not directly transfer property. They are used to hedge risk or to exchange a floating rate of return for a fixed rate of return.

Designated Self–Regulatory Organization (DSRO)

When a Futures Commission Merchant (FCM) is a member of more than one Self–Regulatory Organization (SRO), the SROs may decide among themselves which of them will be primarily responsible for enforcing minimum financial and

sales practice requirements. The SRO will be appointed DSRO for that particular FCM. NFA is the DSRO for all non–exchange member FCMs.

Disclosure Document
The statement that must be provided to prospective customers that describes trading strategy, fees, performance, etc.

Disequilibrium
A situation where internal and/or external forces prevent market equilibrium from being reached or cause the market to fall out of balance. This can be a short–term byproduct of a change in variable factors or a result of long–term structural imbalances. This theory was originally put forth by economist John Maynard Keynes.

Many modern economists have likened using the term "general disequilibrium" to describe the state of the markets as we most often find them. Keynes noted that markets will most often be in some form of disequilibrium – there are so many variable factors that affect financial markets today that true equilibrium is more of an idea; it is helpful for creating working models, but lacks real–world validation.

Distressed Securities
Distressed Securities strategies invest in, and may sell short, the securities of companies where the security's price has been, or is expected to be, affected by a distressed situation. This may involve reorganizations, bankruptcies, distressed sales and other corporate restructurings. Depending on the manager's style, investments may be made in bank debt, corporate debt, trade claims, common stock, preferred stock and warrants. Strategies may be sub–categorized as "high–yield" or "orphan equities." Some managers may use leverage. Fund managers may run a market hedge using S&P put options or put option spreads.

Distribution of Monthly Returns
This report displays the number of months in which a trading program's monthly performance historically has fallen within varying performance increments.

Drawdown
An investment is said to be in a drawdown when its price falls below its last peak .The drawdown percentage drop in the price of an investment from its last peak price. The period between the peak level and the trough is called the length of the drawdown period between the trough and the recapturing of the peak is called the recovery. The worst or maximum drawdown represents the greatest peak to trough decline over the life of an investment.

Drawdown Report Specifics
A drawdown is defined as a loss of equity from a peak to valley in a single month or period of consecutive months.

The Drawdown Report presents data on the percentage drawdown's during the trading program's performance history ranked in order of magnitude of loss.

Depth: Percentage loss from peak to valley
Length: Duration of drawdown in months from peak to valley

Recovery: Number of months from valley to new high

Start Date: Month in which peak occurs.

End Date: Month in which valley occurs.

E

Economic Value of Equity

A cash flow calculation that takes the present value of all asset cash flows and subtracts the present value of all liability cash flows. This calculation is used by banks for asset/liability management. The value of a bank's assets and liabilities are directly linked to interest rates. By calculating its EVE, a bank is able to construct models that show the effect of different interest rate changes on its total capital. This risk analysis is a key tool that allows banks to prepare against constantly changing interest rates.

Efficiency Index

This is a ratio calculated by dividing the annual return by the annualized monthly standard deviation.

Emerging Markets

Emerging Markets funds invest in securities of companies, or the sovereign debt of developing or "emerging" countries. Investments are primarily long. "Emerging Markets" include countries in Latin America, Eastern Europe, the former Soviet Union, Africa and parts of Asia. Emerging Markets – Global funds will shift their weightings among these regions according to market conditions and manager perspectives. In addition, some managers invest solely in individual regions.

Emerging Markets – Asia involves investing in the emerging markets of Asia.

Emerging Markets – Eastern Europe/CIS funds concentrate their investment activities in the nations of Eastern Europe and the CIS (the former Soviet Union).

Emerging Markets – Latin America is a strategy that entails investing throughout Central and South America.

Equity Hedge

Equity Hedge investing consists of a core holding of long equities hedged at all times with short sales of stocks and/or stock index options. Some managers maintain a substantial portion of assets within a hedged structure and commonly employ leverage. Where short sales are used, hedged assets may be comprised of an equal dollar value of long and short stock positions. Other variations use short sales unrelated to long holdings and/or puts on the S&P index and put spreads. Conservative programs mitigate market risk by maintaining market exposure from zero to 100 percent. Aggressive programs may magnify market risk by exceeding 100 percent exposure and, in some instances, maintain a short exposure. In addition to equities, some programs may have limited assets invested in other types of securities.

Equity Market Neutral

Equity Market Neutral investing seeks to profit by exploiting pricing inefficiencies between related equity securities, neutralizing exposure to market risk by combining long and short positions. Typically, the strategy is based on quantitative models for selecting specific stocks with equal dollar amounts comprising the long and short sides of the portfolio. One example of this strategy is to build portfolios made up of long positions in the strongest companies in several industries

and taking corresponding short positions in those showing signs of weakness. Another variation is investing long stocks and selling short index futures.

Event–Driven

Event–Driven is also known as "corporate life cycle" investing. This involves investing in opportunities created by significant transactional events, such as spin–offs, mergers and acquisitions, bankruptcy reorganizations, recapitalizations and share buybacks. The portfolio of some Event–Driven managers may shift in majority weighting between Risk Arbitrage and Distressed Investment instruments, while others may take a broader scope. Instruments include long and short common and preferred stocks, as well as debt securities and options. Leverage may be used by some managers. Program managers may hedge against market risk by purchasing S&P put options or put option spreads

F

Fisher Effect

A theory describing the long–run relationship between inflation and interest rates. This equation tells us that, all things being equal, a rise in a country's expected inflation rate will eventually cause an equal rise in the interest rate (and vice versa).

Fixed Income Arbitrage

Fixed Income Arbitrage is a market neutral hedging strategy that seeks to profit by exploiting pricing inefficiencies between related fixed income securities while neutralizing exposure to interest rate risk. Fixed Income Arbitrage is a generic description of a variety of strategies involving investment in fixed income instruments, and weighted in an attempt to eliminate or reduce exposure to changes in the yield curve. Managers attempt to exploit relative mispricing between related sets of fixed income securities. The generic types of fixed income hedging trades include: yield–curve arbitrage, corporate versus Treasury yield spreads, municipal bond versus Treasury yield spreads and cash versus futures.

Fixed Income: Convertible Bonds

Fixed Income Convertible Bond funds are primarily long only convertible bonds. Convertible bonds have both fixed income and equity characteristics. If the underlying common stock appreciates, the convertible bond's value should rise to reflect this increased value. Downside protection is offered because if the underlying common stock declines, the convertible bond's value can decline only to the point where it behaves like a straight bond.

Fixed Income: High–Yield

Fixed income High–Yield managers invest in non–investment grade debt. Objectives may range from current income to acquisition of undervalued instruments. Emphasis is placed on assessing credit risk of the issuer. Some of the available high–yield instruments include extendible/reset securities, increasing–rate notes, pay–in–kind securities, split–coupon securities and usable bonds.

Fixed Income: Diversified

Fixed income Diversified fund may invest in a variety of fixed income strategies. While many invest in multiple strategies, others may focus on a single strategy less followed by most fixed income hedge funds. Areas of focus include municipal bonds, corporate bonds, and global fixed income securities.

Fixed Income: Mortgage–Backed

Fixed Income Mortgage Backed funds invest in mortgage–backed securities. Many funds focus solely on AAA–rated bonds. Instruments include: government agency, government–sponsored enterprise, private label fixed– or adjustable–rate mortgage pass–through securities, fixed– or adjustable–rate collateralized mortgage obligations (CMOs), real estate mortgage investment conduits (REMICs) and stripped mortgage–backed securities (SMBSs). Funds may look to capitalize on security–specific mis-pricings. Hedging of prepayment risk and interest rate risk is common. Leverage may be used, as well as futures, short sales and options.

Fundamental Analysis

The underlying proposition of fundamental analysis is that there is a basic intrinsic value for the aggregate stock market, various industries or individual securities and that these depend on underlying economic factors. The identification and analysis of relevant variables combined with the ability to quantify the future value of these variables are key to achieving superior investment results. A wide range of financial information is evaluated in fundamental analysis, including such income statement data as sales, operating costs, pre–tax profit margin, net profit margin, return on equity, cash flow, and earnings per share.

Fundamental analysis contrasts with technical analysis which contends that the prices for individual securities and the overall value of the market tend to move in trends that persist.

Futures

A future is a derivative instrument that involves a contract to buy or sell an asset (stock index, commodity, currency, fixed income or other security) for delivery at a future date at a specific price.

Futures Commission Merchant (FCM)

An individual or organization which solicits or accepts orders to buy or sell futures contracts or commodity options and accepts money or other assets from customers in connection with such orders. An FCM must be registered with the CFTC.

Futures Contract

A legally binding agreement to buy or sell a commodity or financial instrument at a later date. Futures contracts are standardized according to the quality, quantity and delivery time and location for each commodity. The only variable is price.

Futures Industry Association (FIA)

The national trade association in the United States of America for Futures Commission Merchants.

G

Gearing

In finance, gearing (or leverage) is using given resources in such a way that the potential positive or negative outcome is magnified. It generally refers to using borrowed funds, or debt, so as to attempt to increase the returns to equity.

H

High Watermark

A requirement that an investment program must recoup any prior losses before the investment manager may take a performance (incentive) fee. In addition to performance losses, prior losses may include any combination of fees that the investment manager charges, such as management and administrative fees.

Hurdle Rate

The level of return (often the risk–free interest rate) which investment managers sometimes stipulate net new highs must exceed in order for performance fees to be charged.

I

Incentive Fee

Fee paid as an incentive to the general partner of a hedge fund or a Commodity Trading Advisor, the amount of which depends on his/her performance, usually relative to some benchmark index. Such a form of compensation could in fact extend to any financial professional, but tends to be most common among people directly responsible for managing funds.

Inefficient Portfolio

A portfolio that delivers an expected return that is too low for the amount of risk it requires, or equivalently, a portfolio that requires too much risk for a given expected return.

Internal Rate of Return (IRR)

Internal Rate of Return. The rate of return that would make the present value of future cash flows plus the final market value of an investment or business opportunity equal the current market price of the investment or opportunity.

Intrinsic Value

The amount by which a call or put option is in the money, calculated by taking the difference between the strike price and the market price of the underlying asset.

Investment Strategy

An investor's plan of distributing assets among various investments, taking into consideration such factors as individual goals, risk tolerance and horizon.

J

No Entry

K

Kurtosis

Kurtosis characterizes the relative "peakedness" or flatness of a distribution compared with the normal distribution. Positive kurtosis indicates relatively peaked distribution. Negative kurtosis indicates relatively flat distribution.

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L

Leverage

Leverage and gearing effectively mean the same thing: the process or effect of ´gearing up´ or magnifying exposure to an investment strategy, manager or asset. Leverage can be achieved by borrowing capital or using derivatives . A leveraged investment is subject to a multiplied effect in the profit or loss resulting from a comparatively small change in price. Thus leverage offers the opportunity to achieve enhanced returns, but at the same time can result in a loss that is proportionally greater than the amount invested.

Lock–up

A time period during which a new investor in a hedge fund may not withdraw any capital committed to the fund.

M

Macro

Macro involves investing by making leveraged bets on anticipated price movements of stock markets, interest rates, foreign exchange and physical commodities. Macro managers employ a "top down" global approach, and may invest in any markets using any instruments to participate in expected market movements. These movements may result from forecasted shifts in world economies, political fortunes or global supply and demand for resources, both physical and financial. Exchange traded and over–the–counter derivatives are often used to magnify these price movements.

Managed Futures

The segment of the alternative investment industry which actively trades and manages futures instruments. The advisers that focus their asset management efforts on futures are known as CTAs (Commodity Trading Advisors) They invest on both the long and short side of the market and usually employ quantitative or technical analysis and systematic investment processes.

Margin

The amount of capital that has to be deposited as collateral in order to gain full exposure to an asset.

Mark–to–Market

To debit or credit on a daily basis a margin account based on the close of that day's trading session. In this way, buyers and sellers are protected against the possibility of contract default.

Market Neutral

Denotes an approach to investment where the emphasis is on the value of securities relative to each other and the use of arbitrage techniques, rather than market direction forecasting. By emphasizing the relative value of securities and the exploitation of pricing anomalies between related securities, practitioners of market neutral approaches aim to generate profits regardless of the overall direction of broad market prices. Market neutrality is generally achieved by offsetting or hedging long and short positions or maintaining balanced exposure in the market. The term market neutral can be applied with some justification to the majority of alternative investment styles because of their ability to capitalize both on upward or downward price moves or to profit in a wide range of market environments.

Market Timing
Market Timing involves allocating assets among investments by switching into investments that appear to be beginning an uptrend, and switching out of investments that appear to be starting a downtrend.

Merger Arbitrage
Merger Arbitrage, sometimes called Risk Arbitrage, involves investment in event–driven situations such as leveraged buyouts, mergers and hostile takeovers. Normally, the stock of an acquisition target appreciates while the acquiring company's stock decreases in value. These strategies generate returns by purchasing the stock of the company being acquired, and in some instances, selling short the stock of the acquiring company.

Managers may employ the use of equity options as a low–risk alternative to the outright purchase or sale of common stock. Most Merger Arbitrage funds hedge against market risk by purchasing S&P put options or put option spreads.

Simulation
A mathematical technique used to model the price characteristics of an investment structure based on random simulations of the underlying assets or variables that affect the price of that investment. This form of analysis involves constructing multiple Net Asset Value (NAV) paths for a product, net of all appropriate fees and interest, using random samples of gross monthly returns. The price characteristics that can be modeled using this powerful technique are known as ´path–dependent´ characteristics, such as risk, return, and drawdown's, which depend on NAV movements over the life of an investment structure.

Momentum
The speed of price change over a period of time. Momentum based investment styles, notably trend following approaches, aim to capitalize on the acceleration in directional price movements, be they upward or downward.

N

National Futures Association (NFA)
Authorized by Congress in 1974 and designated by the CFTC in 1982 as a "registered futures association," NFA is the industry wide self–regulatory organization of the futures industry.

National Introducing Brokers Association (NIBA)
NIBA is a non–profit organization for guaranteed and independent introducing brokers.

Negative Gearing
Negative gearing is a form of financial leverage where an investor borrows money to buy an asset, but the income generated by that asset does not cover the interest on the loan. (When the income does cover the interest it is called positive gearing.) A negative gearing strategy can only make a profit if the asset rises in value by enough to cover the shortfall between the income and interest which the investor suffers. The investor must also be able to fund that shortfall until the asset is sold.

Net New Highs
A net new high is reached when the net asset value of an investment exceeds the previous peak level in the net asset value (also known as the ´high watermark´). Performance fees are levied on net new highs.

Net Asset Value
The value of each unit of participation in a commodity pool. Basically a calculation of assets minus liabilities plus or minus the value of open positions when marked to the market, divided by the total number of outstanding units.

Notional Funding
Notional funding is the term used for funding an account below its nominal value. For example, assume a CTA requires a minimum investment of $1,000,000 (the "Nominal Value") and the margin requirement is $50,000.

The investor can either deposit $1,000,000 to "fully fund" that minimum investment requirement or she can invest only a portion of the $1,000,000, as long as she meets the $50,000 margin requirement. Now assume that the investor decides to fund the $1,000,000 account with $100,000 (the "Funding Level"). This means that the investor is using leverage of 10X—ten times $100,000 equals the $1,000,000 minimum investment. The difference between the Nominal Value ($1,000,000) and the Funding Level ($100,000) is $900,000. The $900,000 is referred to as "Notional Funding".

O

Omega
These are total probability weighted gains / losses. The steeper the curve is, the less the possibility of extreme returns (risky distribution is flatter). The function is equivalent to the return distribution itself, as it combines effect of all of its moments. Returns are distributed into loss and gain above and below a return threshold and then the probability weighted ratio of returns above and below a threshold is considered.

Option
A derivative instrument that gives the holder the right, but without any obligation, to buy (call) or sell (put) a security or asset at a fixed price within a specified period or at a particular future date.

P

Performance Fee
Often referred to as an incentive fee, this is the fee earned by a manager on profits that surpass the previous high watermark – the peak level in the net asset value of an investment since inception. The calculation of performance fees is sometimes based on that portion of the new highs which exceeds a hurdle rate such as the risk–free interest rate.

Portfolio Efficient Frontier
By plotting the intersection of risk and reward for different investments or weightings of assets, one can generate a risk/reward curve or ´frontier´ for those investments. The efficient frontier is the point on such curve where an investment combination delivers the most favorable balance of risk and reward.

Principal Protection
An arrangement or mechanism built into an investment product whereby investors are assured that their initial or investment is secure and that this amount will at the very least be returned to them when such a product reaches its maturity date. Principal protection features can take a variety of forms, including capital guarantees provided by banks.

Proforma
A representation of a track record that is developed to show the effect on actual performance of intended or potential adjustments for different fee structures, portfolio allocations or other variations in the investment structure upon which the original track record is based. It is important to note that a proforma is based on actual trading results and differs from a simulation, which models the hypothetical performance of a portfolio or investment approach that has yet to be applied or implemented in actual trading.

Q

Qualitative Analysis
Analysis that uses subjective judgment to evaluate investments based on non–financial information such as management expertise, cyclicality of industry, strength of research and development, labor relations and depth of operational infrastructure. Qualitative analysis evaluates important factors that cannot be precisely measured rather than the actual financial data about a company.

Quantitative Analysis
Quantitative analysis uses statistical techniques to develop investment models using key financial ratios and economic indicators. The use of objective data facilitates the comparison of a large universe of investment products to identify a select range of potential investment possibilities. Quantitative analysis deals with measurable factors in contrast from qualitative considerations such as the character of management.

R

Redemptions
The time period in which an investor in a hedge fund or a mutual fund may withdraw his or her capital from the fund. For example, quarterly redemption allows an investor to withdraw capital every quarter.

Relative Value Arbitrage
Relative Value Arbitrage attempts to take advantage of relative pricing discrepancies between instruments, including equities, debt, options and futures. Managers may use mathematical, fundamental or technical analysis to determine mis-valuations. Securities may be mispriced relative to the underlying security, related securities, groups of securities or the overall market. Many funds use leverage and seek opportunities globally. Arbitrage strategies include dividend arbitrage, pairs trading, options arbitrage and yield curve trading.

Risk–Adjusted Performance
Risk relative to return – the return achieved per unit of risk or the risk associated with a particular level of reward, typically represented by the Sharpe ratio. Improving the risk–adjusted return depends either on increasing returns and maintaining the level of risk, or maintaining the level of returns and lowering the associated risk.

S

Segregated Account
A special account used to hold and separate customers´ assets from those of the broker or firm.

Self–Regulatory Organization (SRO)
Self–regulatory organizations (i.e., the futures exchanges and National Futures Association) enforce minimum financial and sales practice requirements for their members.

Sharpe Ratio
A measure of risk–adjusted performance that indicates the level of excess return per unit of risk. In the calculation of Sharpe ratio, excess return is the return over and above the short–term risk free rate of return and this figure is divided by the risk, which is represented by the annualized volatility or standard deviation. In summary the Sharpe Ratio is equal to compound annual rate of return minus rate of return on a risk–free investment divided by the annualized monthly standard deviation. The greater the Sharpe ratio the greater the risk–adjusted return.

Skewness
Skewness characterizes the degree of asymmetry of a distribution of returns around its mean. Positive skewness indicates a distribution with an asymmetric tail extending toward more positive values. Negative skewness indicates a distribution with an asymmetric tail extending toward more negative values.

Slippage
The difference between the sample or target price for buying or selling an asset and the actual price at which the transaction takes place.

Sortino Ratio
A measure of risk–adjusted performance that indicates the level of excess return per unit of downside risk. It differs from the Sharpe ratio in that it recognizes investors´ preference for upside (´good´) over downside (´bad´) volatility and uses a measure of ´bad´ volatility as provided by semi–deviation – the annualized standard deviation of the returns that fall below a target return, say the risk free rate.

Standard Deviation
A widely used measurement of risk usually used to represent volatility derived by calculating the square root of the variance of the returns of an investment from their mean.

Sterling Ratio
This ratio is also a comparison of historical reward and risk and was developed by Deane Sterling Jones. The Sterling Ratio is equal to the average annual rate of return for the past three calendar years divided by the average of the maximum annual drawdown in each of those three years plus 10%.

Strategy
The particular investment process employed by a manager in the application of an investment style.

Stress Testing

Stress testing is a method of determining how the program will behave during a period of financial crisis. We use the worst monthly S&P500 returns as a stress time. You can also use hypothetical scenarios (for example Monte Carlo simulation) or known historical events (for example Russian debt default in 1998 or 9/11 terrorist attacks).

Structured Product

Typically provides principal protection, invests across a range of styles and managers, provides increased investment exposure and requires a high level of structuring expertise with respect to blending investment approaches, financing, liquidity and risk management.

Style Analysis

The general idea of Style Analysis is to attempt to explain, or understand, the return stream of a given investment program in terms of a set of asset classes (or style factors). Specifically, for a set of n asset classes, to try and find a corresponding set of n fixed weights (or percentages). These weights are then applied to the returns of their respective asset classes, with the hope that their sum closely approximates the returns of the given fund, for each data–period in succession and over the range of data periods as a whole. At the same time, it is desired that the composition determined by the analysis reflect the actual style of the target fund.

This is a part of the multifactor analysis. We use the returns-based method developed by F. S. Lhabitant in 2001 (please refer to the white paper section of the managed futures/forex database) which is an adjusted application of the analysis initially suggested by Sharpe in 1998. CS/Tremont hedge fund indices are used as factors and Beta coefficients are used as exposure to these style indices.

T

Technical Analysis

The basic premise of technical analysis is that prices move in trends that persist and this characteristic can be used to achieve superior returns. Technical analysis often uses computer programs to examine market data such as prices and volume of trading to make an estimate of future price trends and an investment decision.

Unlike fundamental analysis, technical analysis is not concerned with the financial position of a company.

Total Return

The total percentage return of an investment over a specified period, calculated by expressing the difference between the investment's initial price and final price as a percentage of the initial price.

Trading Adviser Report (TAR)

A performance report produced by an investment manager that is made available, usually on a monthly basis, to clients with holdings in a particular product. The report details the change in net asset value of a product and explains performance in light of market conditions as well as any relevant portfolio changes and developments.

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Track Record
The actual performance of an investment since inception, usually represented by audited monthly returns, net of fees.

Trend
The general direction of the market, a relatively persistent upward or downward price movement over a period, sometimes represented by the mean of price changes in that period.

U

Unit
A generic term used to describe the ´instrument´ (share, bond, unit) which is issued by a product. Investors subscribe to or invest in a product by buying units and redeem their holding by selling units at the prevailing net asset value per unit, as detailed in the relevant product prospectus.

V

Value–Added Monthly Index (VAMI)
VAMI is defined as the growth in value of an average $1000 investment. VAMI is calculated by multiplying (1 + current monthly ROR) X (previous monthly VAMI). VAMI assumes the reinvestment of all profits and interest income. Incentive and Management Fees have been deducted.

Value–At–Risk (VAR)
A widely used risk measurement technique that calculates (at a pre–specified level of probability) the loss that would be experienced in a day or some other pre–specified time horizon in the event of an increase in volatility or an adverse correlated move in market prices, assets or the investments making up a portfolio.

Volatility
Volatility is the measurement of risk used most often in the investment industry. Put simply, it measures how variable price changes are in relation to the price trend for an investment. It is important to note that volatility says nothing about the direction of the trend itself. Expressed in slightly more technical terms, volatility is a measure of how much a set of returns for an investment deviates from the price trend or mean of that investment. It is usually calculated as ´standard deviation´ and expressed as "annualized volatility" – the standard deviation on a yearly basis.

W

Webs
World Equity Benchmark Securities are exchange traded funds that track various foreign country indices such as the U.K., German, and French equivalents of the S & P 500 Index.

Weighting
The relative proportion of each of a group of securities or asset classes within a single investment portfolio.

X

No Entry

Y

Yield

The amount of interest or dividend paid on a loan or an investment, expressed as a percentage. The yield on a stock is calculated by dividing the dividend by the current market price.

Z

Zero–Coupon Bond

This type of bond matures at its face value, is sold at a deep discount to its face value and pays no coupons. The key advantage of this type of bond is that there is no reinvestment risk, although there is the draw back of not being able to benefit from a rise in market interest rates.

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