



# Vantage Point FX Enhanced Return Opportunities Trading Update



May 2020

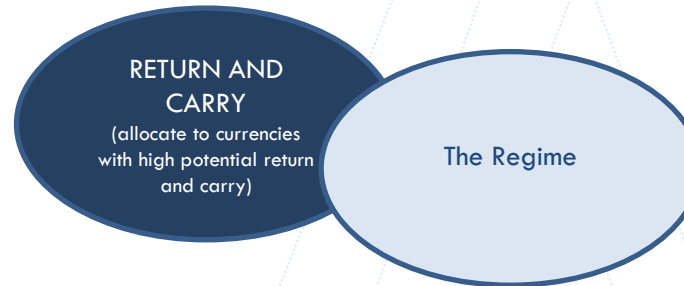
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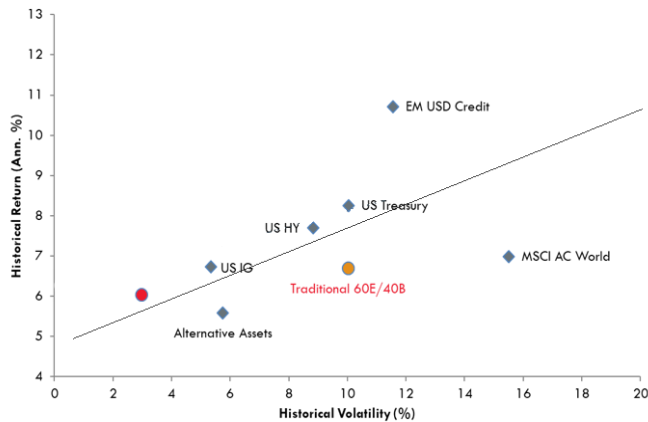
# Proposed Fund Summary

The FX Enhanced Return Fund will be an unleveraged fund designed to take advantage of short term and long term pricing opportunities in global currencies via FX forwards and options.

## Components and return drivers



## Target gross risk and return profile



## Asset classes and instruments

FX forwards and FX NDFs

FX derivatives

Sovereign Bonds & Rates products

Total Net Returns: 5-7%

Volatility: 5-7%

Correlation to Global Equity: 0.5

# Introduction – FX Enhanced Return

## **Aim:**

To seek enhanced returns via FX (developed and EM) currency trading

## **Capacity:**

USD 2 billion+

1m	YtD	Inception	Ann. Vol	Sharpe
-0.12%	-0.51%	0.33%	4.80%	0.11

## **Investment Process (Quantamental Model):**

- Start with systematic models to highlight opportunities in 30+ currencies;
- Modern techniques including machine learning employed;
- Using human discretion to make allocations in the context of macro/geopolitical factors and with consideration for liquidity and risk exposure (see Appendix).

# Introduction – FAQ

## Why employ active currency management?

- Currencies are often used as a policy tool so there can be intervention from non-economic participants: Governments or Central Banks
- Valuation anchors (e.g. REER or PPP) in currencies only work over very long time frames, but can be important at extremes.
- Trends in currencies tend to persist more than other asset classes.
- Interest rate carry has tended to be a valid signal of risk compensation over time – it incorporates fundamental risk like external positions, capital flows, inflation and monetary policy.

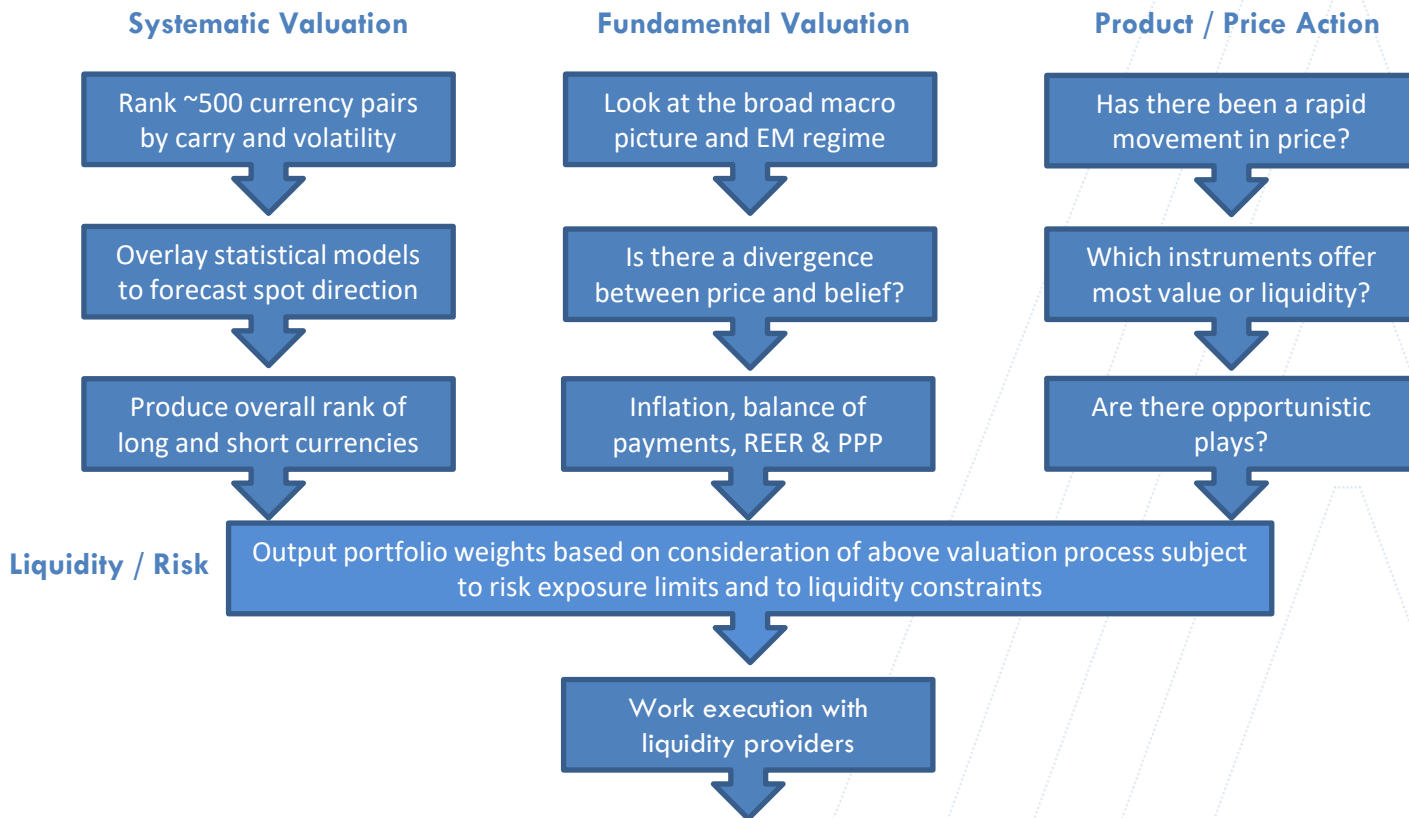
## How?

- The expansion or contraction in front end interest rate carry (the risk premium) in EM can be traded or scaled.
- This can be implemented in a “risk-neutral” way by using a funding currency with similar or correlated risk characteristics (e.g. CNH/TWD).
- We will avoid pegged exchange rates (e.g. HKD) to avoid one-off gap risk.
- G10 historically provides carry (USD, AUD, NZD), funding (EUR, DKK, SEK) and episodic opportunities (GBP).

## Our Approach

- Focus on carry through front end FX Forwards when risk compensation is high and volatility is elevated (and vice versa).
- Ability to Implement the EM carry strategy partly through options, volatility or variance.
- Discretionary over-ride where excessive risk premium is deemed as justified (TRY, ARS etc).
- Hands on approach to execution as elevated risk premium tends to be inversely correlated to liquidity and volatility.
- Focus on regime-change FX drivers...inflation, monetary & fiscal policy, politics (trade, Central Bank independence etc).

# Portfolio Composition – Quantamental Investment Choice

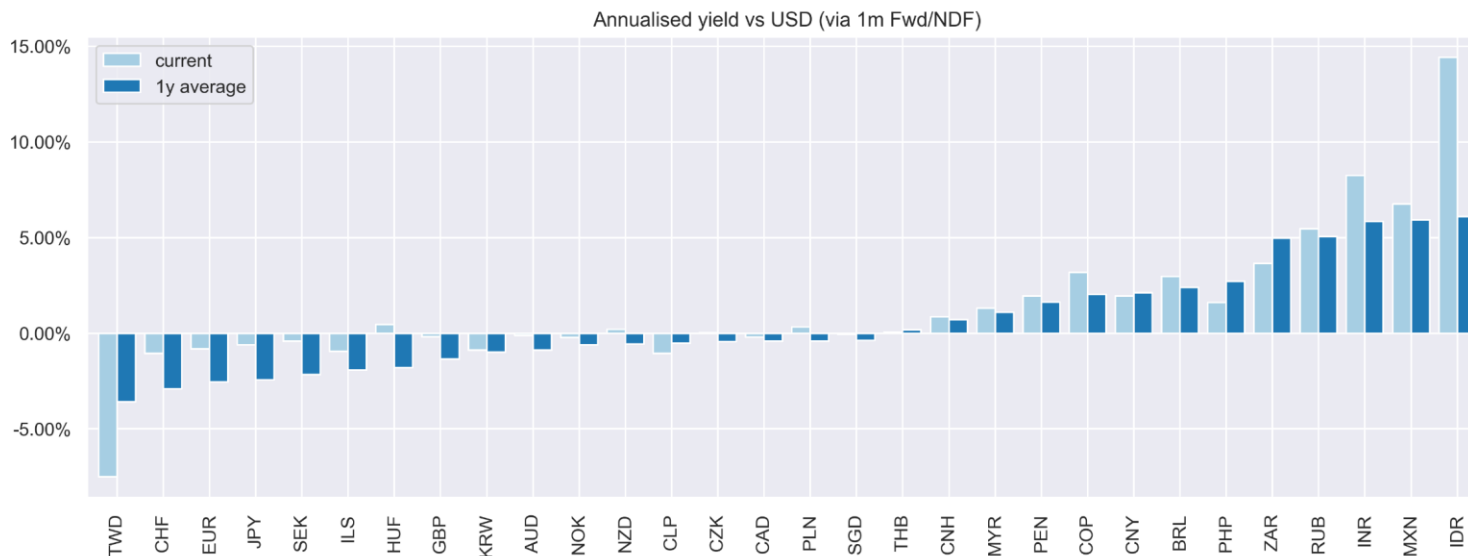


# Sources of Alpha – Carry

The chart below shows a snapshot of current implied yields versus the USD through 1m forwards

- Typical FX carry strategies seek to make revenue by being long high yielding currencies vs the USD.
- USD-neutral strategies reduce exposure to the USD by shorting low yielding currencies vs the USD.
- Position sizing can sometimes be related to recent FX volatility – deploying more risk weighted capital to lower volatility pairs or ranking pairs according to historical Sharpe ratios.

**This can lead to increased risk taking in low volatility periods and cause losses into major events**





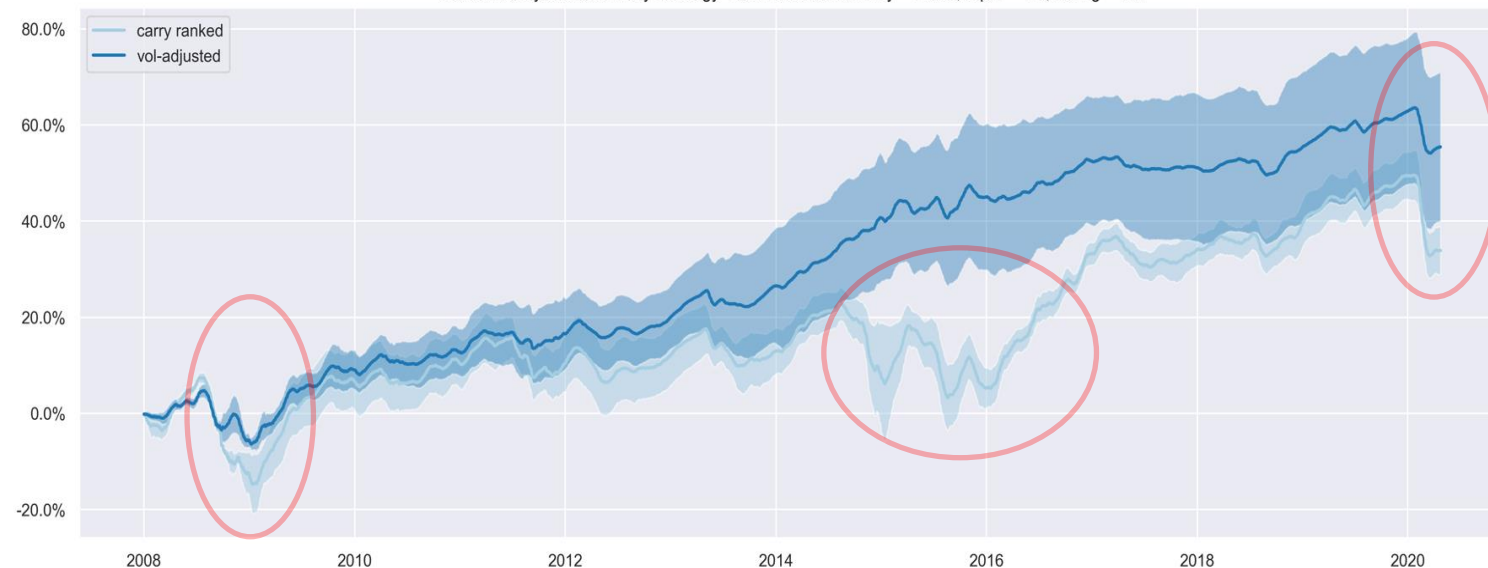
# Sources of Alpha – Carry

## Graph shows a traditional Carry Model strategy

- 30+ FX pairs are ranked by pure yield ('carry ranked') or by historical Sharpe ('vol-adjusted')
- Top ranked (N) long and short positions taken in 1 month tenor (bands in graph for N=1 to 6)
- Vol-adjusted ranking generates typically smoother returns than pure yield ranked
- Nevertheless, typical carry strategies experience periods of drawdown (GFC, Russia, COVID19)

Quantamental model seeks to reduce major periods of drawdown

Illustrative Systematic Carry Strategy Total Returns: emOnly = False, topN = 1-6, rolling = 1M



Source: Bloomberg



# Sources of Alpha – Multiple Indicators

## Looking at multiple systematic models

- Combining multiple systematic models such as momentum/trend and vol premium with carry.
- RHS shows example of individual EM ccy rankings from statistical models with indicative overall ranking.
- Below table shows correlations of strategy returns (if they were run on a purely systematic basis)

## Example Correlations

	carry	vol_prem	momentum
carry	1.00	-0.12	-0.17
vol_prem	-0.12	1.00	0.10
momentum	-0.17	0.10	1.00

## Example Rankings of EM CCYs

BRL	12	11	16	18	17
CLP	7	8	21	20	16
CNH	11	12	18	10	14
CNY	15	15	7	7	9
COP	13	13	5	21	15
CZK	10	10	9	8	7
HUF	4	4	8	6	2
IDR	17	19	2	11	13
ILS	3	3	20	3	5
INR	18	21	6	1	11
KRW	6	7	19	15	12
MXN	21	20	15	16	21
MYR	2	2	1	13	1
PEN	14	14	17	14	19
PHP	16	16	10	2	9
PLN	9	9	11	12	8
RUB	19	18	3	17	17
SGD	8	6	12	5	6
THB	5	5	14	4	4
TWD	1	1	13	9	3
ZAR	20	17	4	19	20

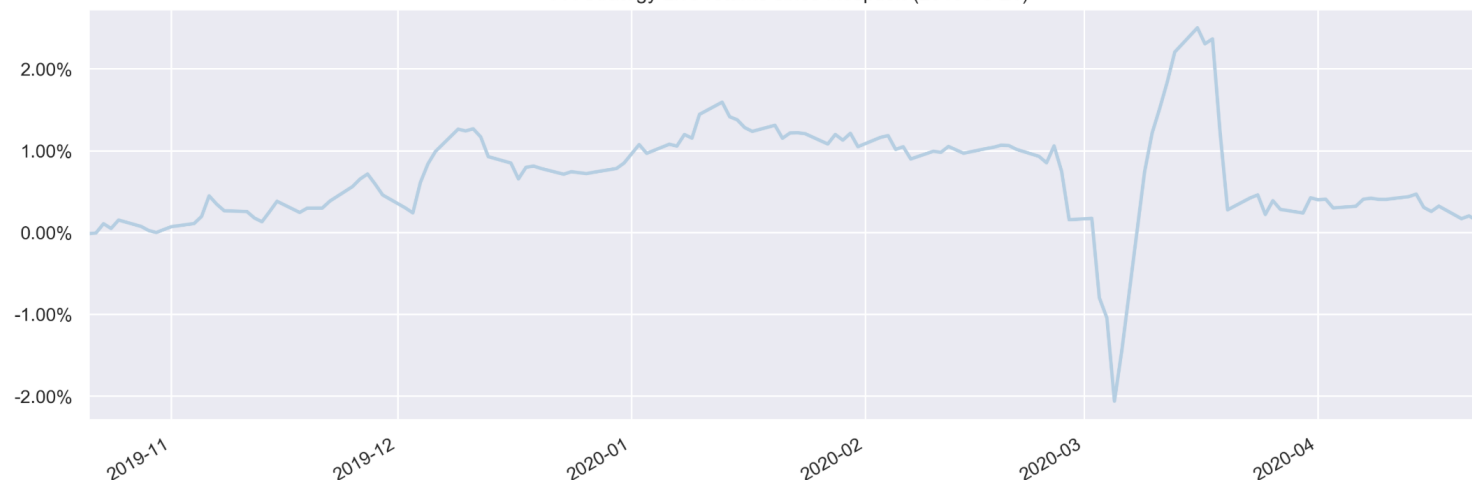
carry\_eq carry\_vol vol\_prem moment Avg\_rank

# Live FX Strategy Performance since Inception

As of: 24-Apr-20				new trades								
				57%	Total Return %NAV	Apr-20	Mar-20	Feb-20	Jan-20	Dec-19	Nov-19	Oct-19
					0.33%	-0.12%	0.22%	-0.83%	0.21%	0.38%	0.42%	0.04%
OPEN	Trade	Direction	Position as %NAV	Trade Return %NAV	Apr-20	Mar-20	Feb-20	Jan-20	Dec-19	Nov-19	Oct-19	
	CNHTWD	Long	57%	-0.02%	-0.12%	0.09%						
CLOSED	MSCI EM Hedge	Short	0% (*)	7.82%	0.00%	7.51%	0.31%					
	TWDINR	Short	29%	-1.66%		-1.40%	-0.26%					
	TWDIDR	Short	14%	-1.64%		-1.55%	-0.09%					
	EURIDR	Short	14%	-1.33%		-1.18%	-0.14%					
	CHFIDR	Short	14%	-1.19%		-0.80%	-0.39%					
	EURMXN	Short	16%	-2.02%		-1.90%	-0.12%					
	CHFIDR	Short	14%	-0.81%		-0.54%	-0.27%					
	TWIDKRW	Short	29%	-0.62%			0.03%	-0.65%				
	TWDINR	Short	29%	0.41%			0.09%	0.32%				
	CNHTWD	Long	57%	0.33%				0.59%	-0.25%			
	USDILS	Long	29%	-0.04%				-0.04%				
	INRTWD	Long	14%	0.17%					0.12%	0.05%		
	INRMYR	Long	14%	0.18%					0.07%	0.11%		
	IDRMYR	Long	29%	0.20%					-0.01%	0.21%		
	EURMXN	Short	29%	0.32%					0.45%	-0.13%		
	CNHTWD	Long	29%	0.22%						0.19%	0.04%	

(\*) Average daily CoB position for the week

FX Strategy Live returns since inception (2019-10-21)



# Live Strategy Performance vs Systematic

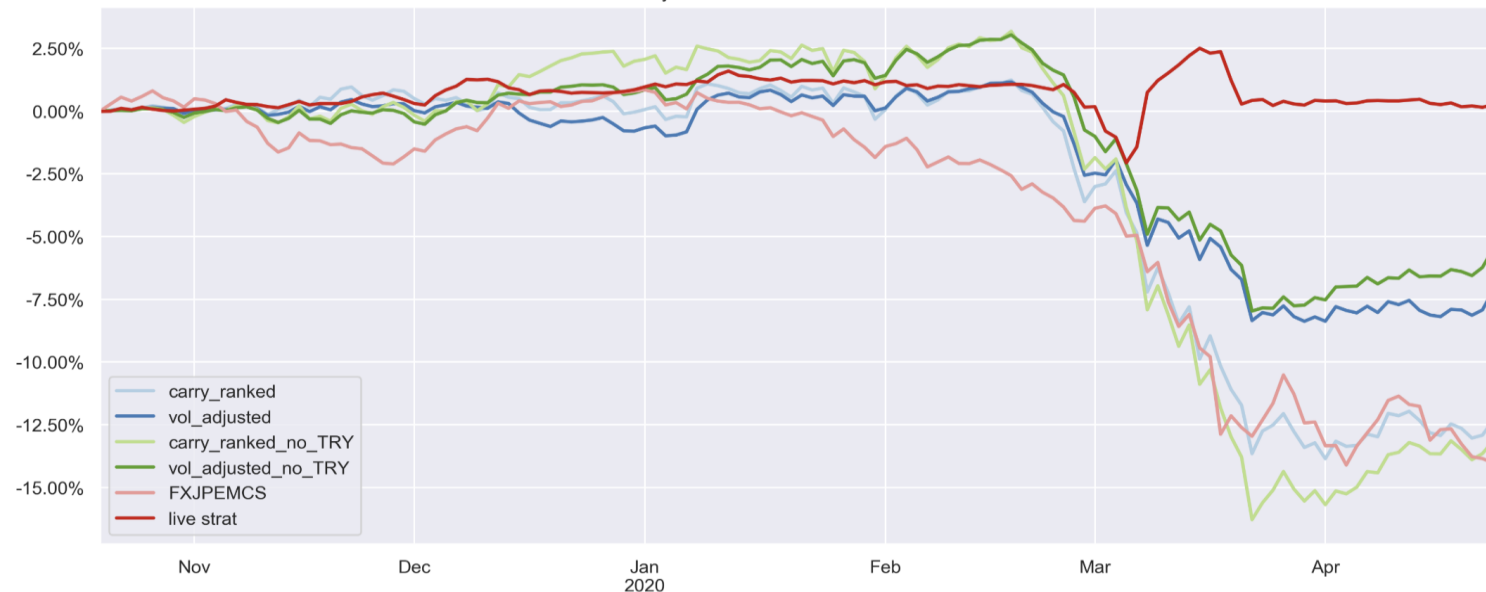
## Live Strategy has easily outperformed pure systematic and JP Morgan EMFX Carry Index

- Reduced risk exposure into and during COVID19 period
- Avoidance of USD exposure (exception a USDILS hedge trade during Iran/US episode)
- Use of MSCI EM Index Futures to hedge our exposures during the midst of COVID19 while still earning FX carry.
- Conscious decision to steer clear of TRY and ZAR (as outlined in prior presentation)

## Quantamental / discretionary strategy has avoided losses in a real-world stress scenario.

Correlation	SPX	MSCI EM	JP EMFX	systematic	live strategy
SPX	1.00	0.88	0.60	0.70	-0.06
MSCI EM	0.88	1.00	0.68	0.70	-0.15
JP EMFX	0.60	0.68	1.00	0.56	-0.10
systematic	0.70	0.70	0.56	1.00	-0.02
live strategy	-0.06	-0.15	-0.10	-0.02	1.00

Illustrative systematic vs live returns since : 2019-10-21

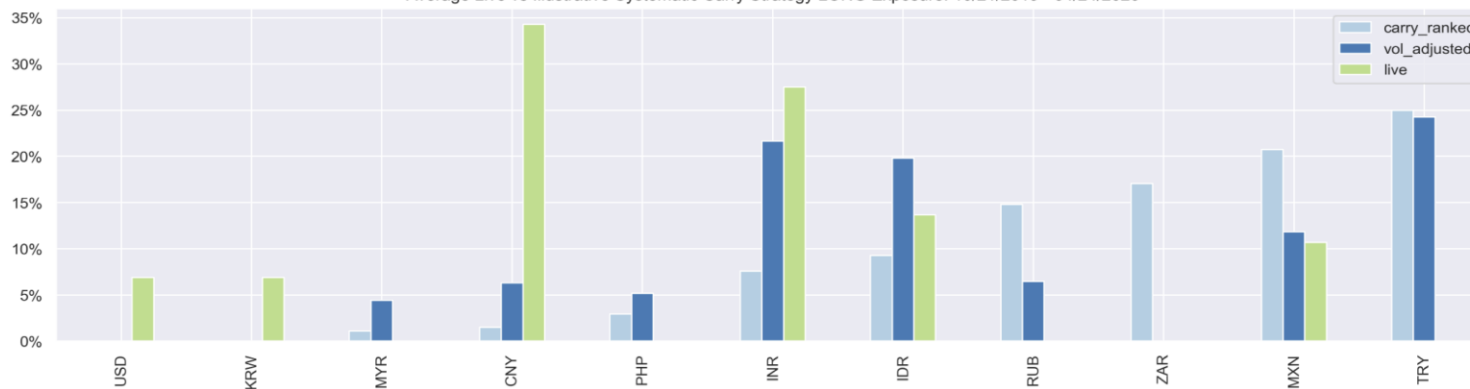


# Live Strategy Performance vs Systematic

## Live Strategy has easily outperformed pure systematic and JP Morgan EMFX Carry Index

- Reduced risk exposure into and during COVID19 period
- Avoidance of USDXXX exposure (exception a USDILS hedge trade during Iran/US episode)
- Conscious decision to steer clear of TRY and ZAR (as outlined in prior presentation)
- Focus more on Asian region pairs with economic rationales behind low historic volatility.

Average Live vs Illustrative Systematic Carry Strategy LONG Exposure: 10/21/2019 - 04/24/2020



Average Live vs Illustrative Systematic Carry Strategy SHORT Exposure: 10/21/2019 - 04/24/2020

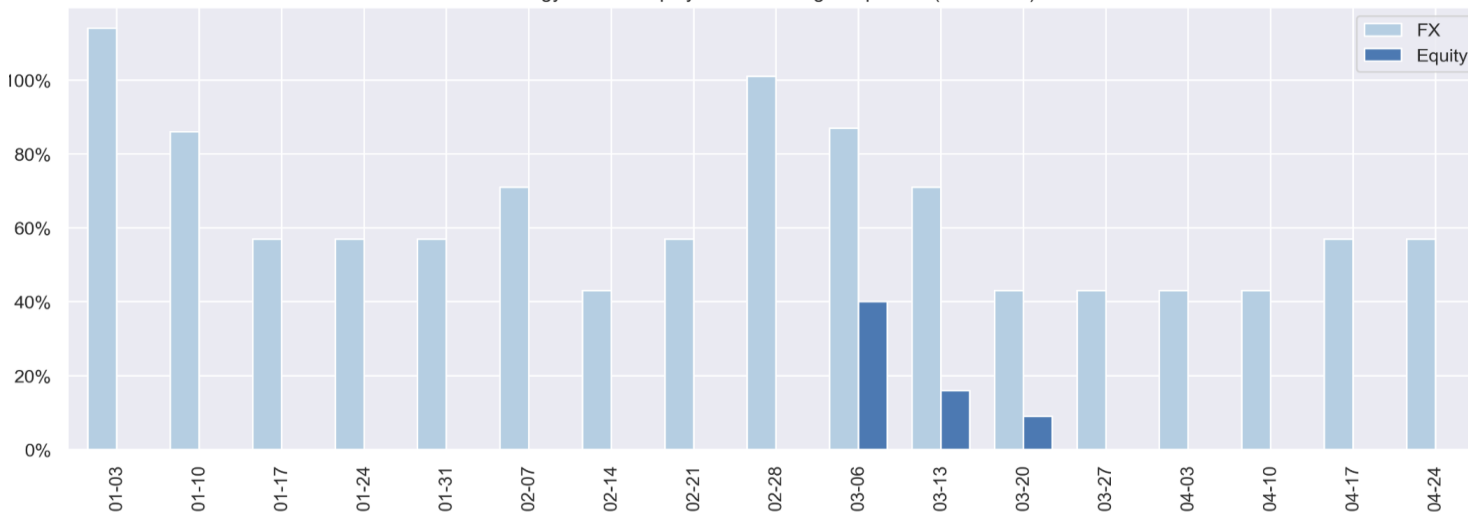


# Live Strategy Performance vs Systematic

## Live Strategy has easily outperformed pure systematic and JP Morgan EMFX Carry Index

- Average unhedged notional exposure in 2020 has been 64% for several reasons:
  - Lack of compelling spot entry levels for EURMXN trades in January.
  - De-leveraging ahead of CNY holiday period for liquidity reasons
  - Reticence to build positioning in early Feb with the developing coronavirus episode
  - Avoidance of long IDR, in particular, early in the episode despite >15% yield.
- In late Feb we entered several positions: short EUR & TWD vs long MXN & IDR after what we then felt was a capitulation in the spot markets (6-8% moves). This took us to 100% exposure. Additionally, we added short equity hedge positions (via MSCI EM Futures) as we felt:
  - There were risks of further squeezes in both EM and developed FX currencies.
  - Regional equities were still trading rich and were an effective delta hedge versus our portfolio
  - Holding the hedge would allow us to continue to earn carry in our FX positions (>8% at the time).

Live Strategy FX and Equity Futures Hedge Exposure (%notional) in 2020



Exposure in early Jan includes USDILS spot hedge during US/Iran episode which means absolute exposure exceeds 100%

# Looking forward – hedging strategies

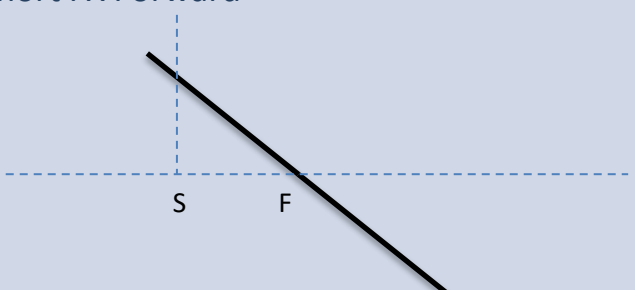
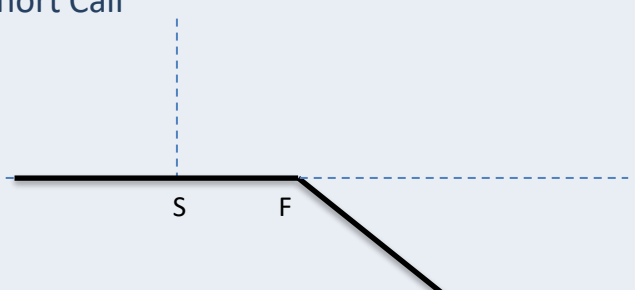
There are several ways we can reduce our risk exposure. The most obvious is unwinding open positions (with associated bid-offer costs for broken date NDFs). We can also naturally de-leverage the position by not rolling out trades that are due to fix (5% daily de-leverage assuming 1 month traded products).

Given our recent experience of hedging the portfolio with MSCI EM Futures, there are other possible hedges we can consider in the future (here we are using FXJPEMCS as a proxy for our portfolio risk).

Instrument	Daily liquidity (USD bio)	Beta to FXJPEMCS	Comments
MSCI EM Futures	5	~ 2.0	Strong correlation in risk-off moves. Proved effective in Q1 2020. Adds cross-instrument basis risk to portfolio.
USDKRW 1m NDF	40	~ -0.7	Classic point of liquidity for EMFX. Liquid but liable to squeezes. Liquid options market.
XXXJPY FX spot	> 100	0.4 – 0.9 depends on pair	Very liquid and correlated in risk-off moves.
FX Options			See following pages for strategy ideas.
FXJPEMC Index product and similar		1.0	Relatively costly during a move but can be a quick way to remove delta risk.

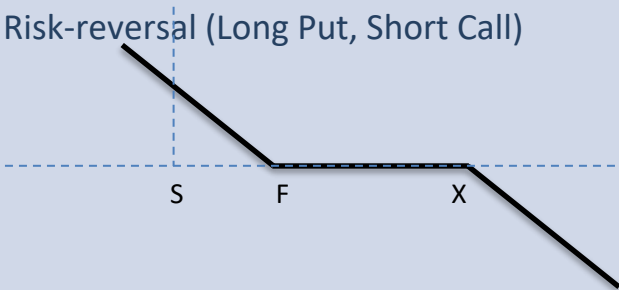
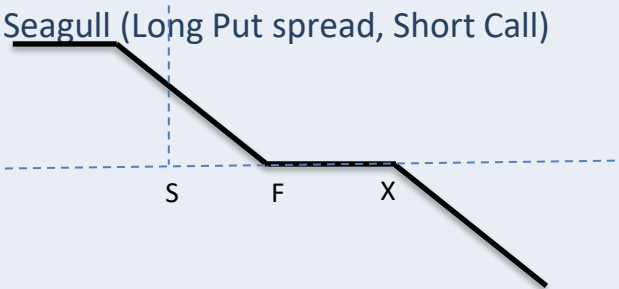
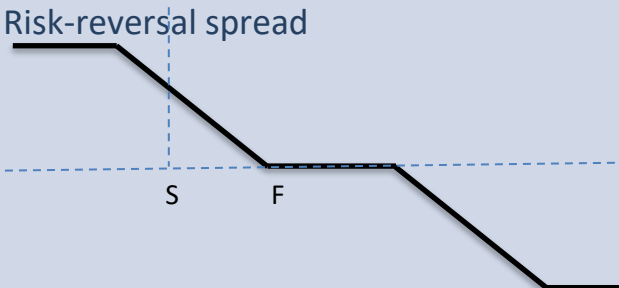
# Looking forward – enhanced options strategies

We can use options strategies to enhance yield (eg just selling an option struck at the forward) or to reduce risk (and cap upside or reduce yield). Below we tabulate a few standard strategies and when they may be suitable depending on market views. Note that option liquidity is sparse in some of the more esoteric crosses.

Name and Payoff Profile	Market view
<p>Short FX Forward</p> 	<p>Bearish spot No vol views Unlimited upside/downside Liquidity in all pairs</p>
<p>Short Call</p> 	<p>Bearish spot Short vol Short skew Earn premium Unlimited downside Upside capped at premium Liquidity in some crosses</p>



# Looking forward – enhanced options strategies (2)

Name and Payoff Profile	Market view
<p>Risk-reversal (Long Put, Short Call)</p>  <p>The graph shows a payoff line that starts at a high level on the left, slopes downward through point S, becomes horizontal between points F and X, and then slopes downward again to the right. A vertical dashed line is at S, and a horizontal dashed line is at the level of F and X.</p>	<p>Bearish spot Mildly long vol Short skew Pay small premium Unlimited upside/downside Losses start beyond strike</p>
<p>Seagull (Long Put spread, Short Call)</p>  <p>The graph shows a payoff line that is horizontal at a high level on the left, slopes downward through point S, becomes horizontal between points F and X, and then slopes downward again to the right. A vertical dashed line is at S, and a horizontal dashed line is at the level of F and X.</p>	<p>Mildly bearish spot Short vega Neutral skew Earn premium Unlimited downside Capped upside Losses start beyond strike</p>
<p>Risk-reversal spread</p>  <p>The graph shows a payoff line that is horizontal at a high level on the left, slopes downward through point S, becomes horizontal between points F and X, and then slopes downward again to the right, eventually leveling off at a lower horizontal line. A vertical dashed line is at S, and a horizontal dashed line is at the level of F and X.</p>	<p>Mildly bearish spot Flat to mildly long vega Long skew Pay small premium Capped upside/downside</p>

# Looking forward – portfolio tail hedges

Major risk events tend to generate directional volatility in all pairs. Choosing the cheapest tail hedge from a basket of risk-sensitive pairs can be an effective way to reduce premium outlay while maintaining upside. Below is an example of a back tested systematic options tail hedge strategy we have shown to clients.

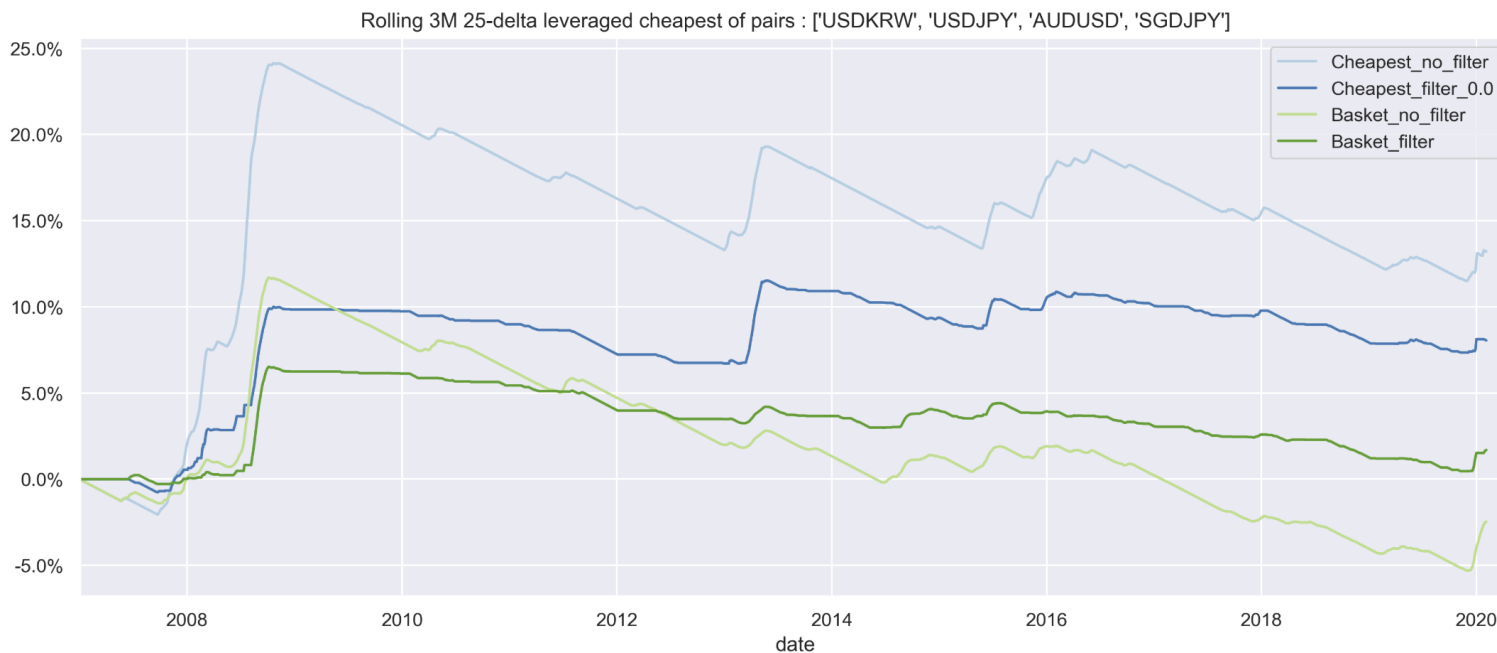


Chart shows rolling 3m 25-delta tail hedge strategies. Green lines correspond to equally weighted baskets with and without risk filters (a VPAM proprietary risk sentiment indicator). Blue lines correspond to a strategy which selects 1 currency pair on each day, solely based on the cheapest premium. Variations with and without the risk filter prior to entry are shown. Chart shows that both risk filter and cheapest tail hedge choice reduce PnL bleed while remaining responsive to risk events. Table highlights number of trades for each currency pair during the observed period in 2007-2019.

Trade count	
<b>USDKRW</b>	513
<b>USDJPY</b>	913
<b>AUDUSD</b>	543
<b>SGDJPY</b>	1447

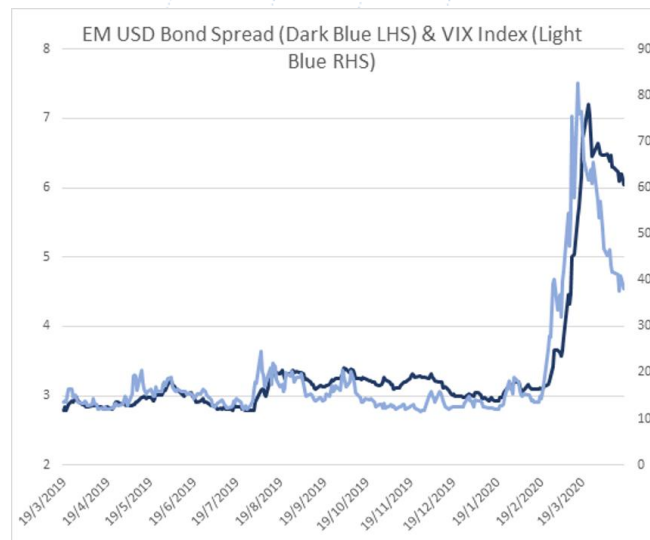
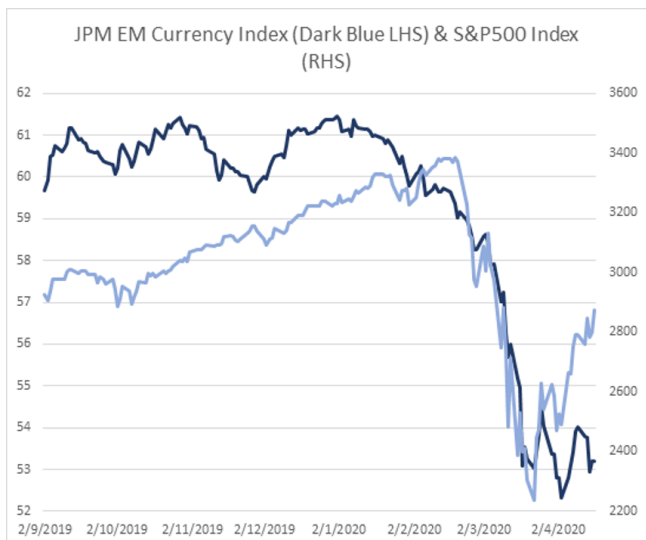
# Looking forward – EMFX market opportunities

In contrast to the (relative) optimism in equities, the rebound in EMFX has been very subdued ; on a spot basis the JP EMFX Index has only bounced by 2.4% above the recent trough compared to more than 25% for US equities. Similarly, the rebound in EMFX has been modest compared to the decline in equity volatility and emerging market risk premia.

Recent measures taken by the Federal Reserve, IMF and others clearly have had a positive impact on dollar liquidity and funding spreads and carry or risk compensation is starting to look attractive.

However, differentiation also remains important ; not all carry remains equal.

The relative weakness in emerging currencies might also be a better reflection of the fragile nature of global final demand. On the positive side, most emerging market currencies are trading at comparable real effective valuations to the Asian crisis in 1997, with a considerably stronger share of world exports and better balance of payments. We have remained cautious and selective with a focus on the cross rates that have high yields and strong economic linkages such as CNH/TWD.



# Appendix



# Proposed Portfolio Composition - Risk Exposure

**We consider the sizing of our FX exposures to several factors:**

- Overall portfolio exposure / leverage
- Volatility / Sharpe control (pair or basket level)
- Geographic considerations (currency blocks)
- Developed vs Emerging currencies
- Deliverable / Non-deliverable currencies
- Liquidity of the underlying currency and product
- Other factors pre-agreed with the investor

*Sample block exposure limits (1 bio notional)*

	Block 0	Block 1	Block 2	Block 3
Full	1000	700	600	400
No Latam	1000	800	600	0
Only Asia	1000	0	1000	0

*Example of currency blocks (NDF currencies highlighted)*

Block 0	Block 1	Block 2	Block 3
USD	CZK	SGD	MXN
EUR	HUF	CNY/CNH	BRL
JPY	PLN	THB	CLP
GBP	ILS	KRW	COP
CHF	RUB	INR	
AUD	ZAR	MYR	
NZD	TRY	TWD	
CAD		IDR	
NOK		PHP	
SEK			

*Sample individual currency limits for given block limit*

Block 0	1000	Block 2	600
USD	1000	SGD	400
EUR	1000	CNY/CNH	300
JPY	1000	THB	300
GBP	1000	KRW	250
CHF	800	INR	250
AUD	1000	MYR	250
NZD	700	TWD	250
CAD	700	IDR	200
NOK	500	PHP	150
SEK	500		

# Our Team

## LIQUID STRATEGIES



**Nick Ferres**  
Chief Investment  
Officer



**Chris Colman**  
Head of Quant &  
Senior Portfolio  
Manager



**Graham Bibby**  
Head of Trading,  
Liquid Market  
Strategies



**Shaun Khoo**  
Analyst

To be hired: Equity Senior PM, Credit Senior PM, Senior Analyst

## PRIVATE ASSETS



**Prad Mazumder**  
Managing  
Director,  
Private Assets



**Nick Croom**  
Managing  
Director,  
Private Assets

## MANAGEMENT TEAM & OPERATIONS



**Colin Mullins**  
CEO



**Paul Thomas**  
Managing Partner



**Koh Ting Wei**  
COO



**Glenn Goh**  
Head of Operations

## ADVISORY BOARD



**Andrew Coloretti**  
Adviser



**Michael Fowler**  
Adviser



**David Tice**  
Adviser



**Kinsey Cotton**  
Adviser

# Portfolio Team

## **Nick Ferres** – Chief Investment Officer / Co-founder

- Former Head of Multi Asset Solutions and Portfolio Manager for Multi Asset Funds at Eastspring Investments (Prudential PLC)
- Lead Portfolio Manager for the Prudential Hong Kong Life Funds while managing tactical asset allocation and providing strategic asset allocation oversight for Prudential subsidiaries in Hong Kong, Thailand and Singapore. The assets grew from \$20 to \$60 billion over the period.
- Investment Strategist and Portfolio Manager for Multi Assets at Goldman Sachs Asset Management in Australia. At GSAM, Nick managed the Multi Asset Funds. The flagship product of this range, Income Plus, was top performing over the five years during which Nick was lead manager.
- BA (Hons) in Economic History and Politics from Monash University, Australia, a Graduate Diploma in Economics, and a Graduate Diploma in Applied Finance.

## **Chris Colman** – 20+ years Investment Bank trading experience

- Former Managing Director at Barclays Investment Bank
- Roles included: Global Head of Electronic FX Trading, Global Head of FX Derivatives Trading and Head of FX Trading Asia.
- Experience trading:
  - FX Spot, forwards, options, exotic derivatives, bond futures, swaps, xCCY basis swaps, swaptions.
- Cambridge University educated (Theoretical Physics and Computer Science)

## **Graham Bibby** – 30 years Investment Bank experience

- Former Managing Director at Barclays Investment Bank
- Roles included: Head of Macro Sales in Singapore
- Advising Macro HFs on investing & trading strategies
- Experience trading:
  - FX Spot, forwards, options, local and developed market rates, credit derivatives.
- Current Head of Trading at Vantage Point AM



# Contact

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