



Achieving uncorrelated Performance in Global Markets

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Good morning and thank you for the invitation to speak at this prestigious event.

I'm Elena Ambrosiadou, co-founder of IKOS and I welcome the opportunity to speak today about uncorrelated Alpha generation.

Most of us in the Hedge Fund industry have seen some great years. We grew in success, attracting more capital from investors, until we were managing MORE of the world's assets than ever before. Collectively we have been, and still are, a force to be reckoned with in the world of international finance.

As managers and investors, it's essential for us to know and understand what delivers success in Asset Management.

What structures, what people and skills, what qualities and ideas are essential for the future?

I advocate that a clear, long term vision and philosophy applied within a well-organized structure and with constant investment in resources are the key prerequisites. And before I start let me underline three words that characterize successful managers.

Alpha, sustainability, and evolution.

As the CEO of a hedge fund that has been in business for 16 years, I can state with confidence that the key to achieving longevity is consistent alpha generation.

Investors must feel confident that a manager will be around to deliver future performance for them in a sustainable way.

Let us now discuss how Uniqueness in other words Alpha uncorrelated to the markets, Sustainability meaning performance consistency, and Adaptability meaning innovation and evolution can be assured by a scientific approach to hedge fund management.

In all human endeavours it has been difficult to deliver growth with improvement. But two things - science and communication - broke through these barriers.



I am a chemical engineer by training and I'm a great believer in processes, technology, and the scientific method - the essence of which is coming up with a hypothesis, and testing it continuously for contradictory evidence.

Only in this way can a body of knowledge be assembled which has lasting value and which can be built upon by many minds over many generations.

The result is not just an investment philosophy but a total infrastructure that is maintained by an organization or society which is fit for purpose.

I am a firm believer in the scientific method as the foundation of robust and globally scalable portfolio management.

In a highly competitive environment, there are huge advantages to a scientific and systematic approach.

How can we evaluate these in the context of hedge fund performance characteristics on behalf of investors?

Trading Targets

Hedge funds are defined by their targets. These are measurable. Expected and actual return, given expected strategy-related risk at a given level of leverage.

But what other targets should we have? I mentioned earlier that I would explain why scientific systematic approaches have excellent survival characteristics, and now is the time to explain why.

Alpha generation

As hedge funds, alpha generation should always be our primary aim. But today, more than ever, capital preservation is also key. Alpha, which is a measure of a fund's uniqueness, ensures survival through independence.

In our quantitative and systematic strategies we constantly carry out performance attribution analysis measuring the alpha we are producing, whilst evaluating what is changing in the behaviour of markets to impact alpha generation, and we keep seeking more sources of alpha through research and the improvement of our technology.

Diversification



For a sustainable economy we need diversification of products and demand patterns so we can 'ride' fluctuations in the environment. Achieving a diversified low-risk approach is easier when you have a systematic strategy where the contribution of each alpha stream is well measured and understood. The scientific process aims to deliver returns uncorrelated to the markets and other managers by extracting alpha from multiple sources. That is a key part of our approach, enabling us to generate alpha in a consistent sustainable way.

Liquidity

Liquidity is the freedom of moving resources around. This provides tremendous advantages to investors and fund managers alike - both in terms of protecting the asset base and seeking opportunities. Investors often undervalue liquidity and illiquid markets flatter mediocre strategies. But we place an unusually high value on liquidity. Systematic strategies are more likely to be developed around liquid markets and instruments and more nimble at allocating resources in a dynamic environment.

Testability, Repeatability, scalability

We need testable, repeatable, scalable infrastructures.

Yes, a human trader gets better with experience, but so do our systems and technology. We have the advantage of being able to analyse the process minutely and objectively, making improvements all the time and building on our performance year on year. Our approach, as with any structured approach, provides essential objectivity and hence repeatability in alpha generation. A systematic infrastructure also overcomes the problem of expertise being invested in only a very few people – a huge issue for the hedge fund industry.

Knowledge is built into efficient processes hence it is scalable in its application. We must never underestimate the importance of a powerful and well controlled infrastructure at any time, but particularly at a time of crisis.

At such times scalability makes the difference between a shut down or intelligent throughput management. Systematic strategies are able to navigate both redemption pressures and counterparty risk more effectively. This massive difference in cost management, stress levels, and business continuity gives the structured systematic high technology approach a definitive survival edge.

Transparency



Investors need transparency. Are we able to deliver transparency in a systematic approach?

Absolutely.

The power of systematic strategies is increased by the means of execution - electronic trading. Automation, when properly implemented, can deliver virtually error-free environments with continuous mark to market profit and risk assessment. All of this translates to unparalleled portfolio, risk, position, and performance transparency.

Risk Management

Risk management encompasses all processes, from regulation to recruitment, competition to counterparties, from tax to disaster recovery. Risk management processes incorporate many aspects of control theory. In a global economy, trade relationships, idea sharing and capital flow generate connectivity of resource management and growth cycles.

Risk management is the process by which we control dynamic systems into acceptable limits of performance fluctuations. In the scientific method we evaluate the type and size of inputs that can cause fluctuations by analyzing historical data over long time frames.

Since the systems can handle huge amounts of data very rapidly and adjust to market conditions, they provide speed and flexibility at low cost all of which are pre-requisites for risk management.

Altogether what I have been describing is a total systematic understanding for success in trading. And because it can be built into the very structure of the way a Hedge Fund manages, it can create lasting value for investors. Without argument, the scientific method is a cornerstone of success.

Why Not

So why isn't everyone a successful completely-automated systematic trader?

To set up a systematic strategy takes time and investment in technology. Older managers have an advantage. Just as in biological evolution it took Energy PLUS Time to get from amoeba to human, so in technology based investing experienced managers have a definitive edge.

Having a system doesn't make one invincible or infallible some managers get to love their system too much to change it as the markets evolve. Only those able to adapt survive. As



new managers arrive they have to overcome increasingly intelligent competition and structural expertise.

This happens in biological systems, in refinery technology, and in communications technology.

So how can structure help rather than hamper experienced managers?

Adaptability

Intelligence (the use of information) within a structure fosters agility, adaptability and survival. That is the place of the human mind in the scientific approach. In today's world the intelligent manager uses technology to go beyond what the human eye can see.

The US historian Joseph Tainter has something pertinent to say about this in the Collapse of Complex Societies.

He argues that societies become more complex as they try to solve problems. The response to something like gaining access to sources of energy, for example, is to create new layers of bureaucracy and infrastructure, leading to the problem of diminishing returns.

Are there some parallels in the current markets? Are there some evolutionary lessons to be learnt by fund managers who want to run intelligent organizations and succeed into the next generation?

I believe there are.

Efficiency and cost control

Smarter organizations are those who manage the parameters of information management, cost, location and position, and systems evolution intensively.

I'll use the IKOS global distributed trading infrastructure as an example. We deploy a globally distributed execution system in Tokyo, Europe and the US, without traders or offices, but with well-structured intelligent systems seeking, exploiting and providing liquidity at the point of minimum latency. This process has taken 8 years to complete and has depended on hardware improvements, exchange systems development, broker systems, and communications technology. Fourteen years ago we were doing 5,000 trades a day – that figure is now over 100,000 in all listed liquid asset classes, equities, futures and spot FX.



What is the benefit to the investor? Alpha generated through liquidity provision, better risk management and cost control. One thing is clear. You must invest energy in both platform maintenance and transformation before the effects of a downturn or critical environmental changes become apparent.

Geography

In today's world, communications technology means we can be part of the information/data highway wherever we are.

What does this mean?

It means that managers who successfully deploy technology can position themselves in order to make the most of a global resource pool.

So how does positioning affect survival?

Historically, concentration in any trade, led to big booms followed by deterioration in performance and eventual liquidity problems during reversals.

This does NOT have to be the case in today's markets where electronic connectivity allows you to trade 24 hours a day from anywhere in the world. Now, being close to the market no longer means physical proximity. It means being close to your regulator, your investor and your service provider, all of which happens via electronic media continuously, and in regular patterns via reporting, face to face meetings and due diligence processes.

The evolved manager of today, who is the electronic manager can navigate away from crowded markets through trading, resource and location independence. Geographical flexibility is not about offshore, unregulated tax havens – IKOS, for example, is regulated by 5 bodies, including the United States SEC. I must mention that 25 out of the top 50 European managers, including IKOS, are SEC registered which demonstrates the truly global nature of our business. Geographical and positioning flexibility is about being able to attract the best from around the globe and at the same time be a global player with global infrastructure. Operate locally but manage globally.

Culture of innovation

In a very real way, ideas are our currency, and our integrity is the cornerstone of our reputation. A strong, independent and individual culture is an organizational survival mechanism and through innovation it contributes to the management of change.



Management

At times of crisis good business management becomes very important. Strategies, Systems, Procedures and People must all deliver results.

If you have modularity built into processes this will help you to control risk and change. Planning helps you to know what to change and when. If people are not in the mental or emotional space which permits change then the management must inject the energy to encourage the teams to break through the barrier.

Conclusion

So to summarise, our thesis today has been that consistent alpha generation is the key to long term survival.

We have shown that efficient alpha capture depends on aggregating liquidity, processing information at sub-second intervals, and applying intelligent execution methodologies to reach the markets for price discovery. As technology is constantly developed by all market participants, the reduction in the size of trade, and the increase in frequency means that minimization of trading cost is crucial. The resources required to be a leading player in any market are significant and the use of information technology in its broadest sense is the key success factor of the intelligent manager.

We have argued that alpha can be produced by well-organized trading systems and processes which are a lot more robust and scalable if they continue to be developed based on the scientific method.

We have also explained that an efficient well run organization, has a long term vision, makes plans, invests capital, and renews itself.



Future

Before we conclude I would like to ask each one of you to contemplate the following important questions: what in your past approach should you keep? What should you discard? And how should you evolve?

For many of us times have been hard - seriously challenging - but we have survived and now we can be more realistic about the future and its opportunities.

I'm not alone in believing this.

MIT professor Andrew Lo was quoted in a Hedgeweek Special report in February as saying that he..."expects to see spectacular growth in the hedge fund industry in the fourth quarter of this year."

Let's hope he is right!

I have argued for a systematic approach and for the need for the hedge fund industry to adapt in order to thrive! I hope you have heard plenty in my speech to inspire debate and I will be delighted to take your questions in the time that remains.

Thank you for your kind attention