

# Seeking Alpha $\alpha$

## Trading Like the Hedge Funds Do

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With the market starting the year quite well -- S&P 500 is up over 4% as of Friday's close -- we might be tempted to assume that the rest of 2012 will go as smoothly, and start allocating higher percentage of our portfolios to U.S. equities. After the past year, which resulted in zero returns for the S&P 500, who can blame us? It's also an election year, so things we may certainly feel things are looking rosy.

That might well be the case, but of course we will not know for sure till the end of the year. As for myself, I feel there are still too many macro unknowns left to be resolved, so I remain quite cautious.

With that in mind, I would like to suggest a different tact than simply "increasing allocation to equities." I am talking about alternative strategies in general, which can be pursued through alternative ETFs. I'm focusing on these, and not on mutual funds, for a few reasons: ETFs are transparent, they trade intraday, they provide better liquidity, they have lower cost and they may provide tax advantages.

As for alternative ETFs, specifically, my major reason for starting to look at these is that they provide prudent portfolio diversification. As I have written before, major endowment funds -- at such universities as Harvard and Yale -- make room for alternative strategies among several other asset classes (equities, fixed income and real assets, such as commodities and real estate). As of September, in fact, Harvard's endowment fund shows a 16% allocation to alternative assets, or absolute return.

What characterizes alternative assets is that they typically have low correlation to broad stock indices, and they aim to provide low volatility. They also make for an excellent portfolio-diversification tool, meaning that high-quality alternative-strategy funds provide for better risk-adjusted returns. In other words, to a large extent alternative funds will reduce your volatility, while only paring back on returns to a comparatively slight degree.

These alternative strategies provide for low correlation and lower volatility because they use hedging techniques -- just like hedge funds do. A typical hedged approach, aptly named the long-short strategy, will involve simultaneous long and short exposure on certain securities. Some of these aim to deliver alpha from both the long and short positions, while others aim to do so from long positions, while hedging with short positions.

So, now -- presuming you like the idea of diversifying your portfolio and reducing your risk -- where do you find more information about these ETFs? There are several good sources, but I especially like ETFdb.com and IndexUniverse.com. In fact, I've used both to put together a combination of alternative and long/short ETFs, and ultimately I came up with a list of 21 funds:

### Long/Short ETFs

Ticker	Name
<b>AGLS</b>	Accuvest Global Long Short ETF
<b>ALT</b>	iShares Diversified Alternatives
<b>BTAH</b>	QuantShares U.S. Market Neutral Beta
<b>BTAL</b>	QuantShares U.S. Market Neutral Anti-Beta
<b>BWV</b>	iPath CBOE S&P 500 BuyWrite Index ETN
<b>CHEP</b>	QuantShares U.S. Market Neutral Value
<b>CSLS</b>	Credit Suisse Long/Short Liquid ETN
<b>CSM</b>	ProShares Credit Suisse 130/30
<b>CSMN</b>	Market Neutral Global Equity ETN
<b>HDG</b>	ProShares Hedge Replication
<b>JFT</b>	First Trust Enhanced 130/30 Large Cap Index
<b>MCRO</b>	IQ Hedge Macro Tracker
<b>MOM</b>	QuantShares U.S. Market Neutral Momentum
<b>NOMO</b>	QuantShares U.S. Market Neutral Anti-Momentum
<b>PBP</b>	PowerShares S&P 500 BuyWrite Portfolio
<b>PTO</b>	PowerShares Ibbotson Alternative Completion Portfolio
<b>QAI</b>	IQ Hedge Multi-Strategy Tracker
<b>QLT</b>	QuantShares U.S. Market Neutral Quality
<b>RALS</b>	ProShares RAFI Long/Short
<b>SIZ</b>	QuantShares U.S. Market Neutral Size
<b>SSAM</b>	AdvisorShares Rockledge SectorSAM

Source: ETFdp.com and IndexUniverse.com

This is my first cut, based on the criteria I have established above. Although a 21-name list might seem daunting, it is actually not a very long list, relative to other type of asset classes from the endowment category list.

In any case, with those choices established, the next step is deciding which particular alternative ETF to add. The criteria you use could be limiting yourself to an equity or options ETF, or to one that employs active management or follows an index. You could also pick a fund that's market-neutral or dollar-neutral, one that's factor-driven or goes on fundamental valuations, to name just a few options here.

So there are several themes in this table. If you are looking for highly quantitative ETFs that are highly focused on specific hedge fund strategies I would look to the six QuantShares ETFs.

If you are looking for Long/Short strategies you have Accuvest Global Long Short ETF ([AGLS](#)), Credit Suisse Long/Short Liquid ETN ([CSLS](#)), ProShares Credit Suisse 130/30 ([CSM](#)), First Trust Enhanced 130/30 Large Cap Index ([JFT](#)).

Market Neutral ETFs there are the above mentioned QuantShares and their inverse, as well as Credit Suisse Market Neutral Global Equity ETN ([CSMN](#)) and QuantShares U.S. Market Neutral Quality ([QLT](#)).

For a dollar neutral strategies (i.e. the long exposure equals the short exposure) there are ProShares RAFI Long/Short ([RALS](#)) and Rockledge SectorSAM ([SSAM](#)).

SSAM is considered (as far as I know) the only Absolute Return ETF out there.

Regardless of what you choose, though, I continue to strongly believe in prudent portfolio diversification by allocating to different asset classes. Adding alternative long/short ETFs will go a long way toward achieving that goal.

**Disclosure:** I am the Portfolio Manager of the AdvisorShares Rockledge SectorSAM ETF Fund. I am long [SSAM](#).