Crossbow Partners
Experience & Discipline

Newsletter April 2023

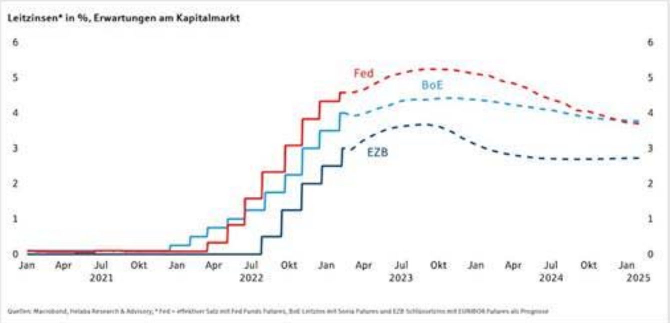
Interest rate outlook

The long-standing zero interest rate policy was abruptly ended in 2022 to combat stubborn inflation. The cycle of interest rate hikes is now coming to an end and after a further hike of 0.25% in May 2023, the Fed is expected to pause in order to monitor the impact of the measures. The regional banking crisis in the USA will lead to tighter credit conditions and will also help to cool down the overheating of the economy. Market participants are therefore already expecting significantly lower interest rates in the USA by the end of 2023.

At the short end, however, we believe interest rates will remain high for longer as inflation will come back significantly but is still a long way off the 2% inflation target in the US and Europe. Central banks are keen to avoid a second wave of inflation, which would require even more drastic measures. This offers very attractive, risk-free yields at the short end of 5% in the US and 4% in Europe for longer periods of time, which will generate further large capital reflows into money market funds.


Stefan Steiner

On the other hand, the stock markets are celebrating a bear market rally as if there were no problems. We would take the opportunity to lock in some profits and make the investment strategy more defensive. Professional investors are increasingly hedging themselves, which can be clearly seen from the rapidly rising put/call ratio in the OTC market. The same protection can be achieved by increasing the ratio of long/short strategies at the expense of passive long-only products. Volatile market segments are particularly suitable for a long/short investment strategy. In this regard, we see good opportunities in Asia, in commodities and in growth stocks, where active investment decisions create a great deal of added value.



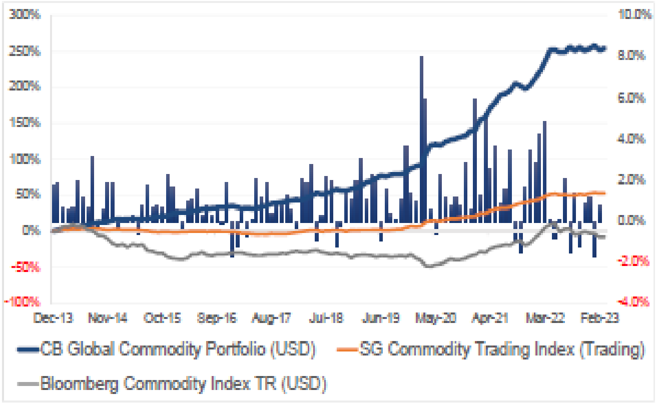
For more information please contact Stefan Steiner at ss@cb-partners.com.

In the limelight

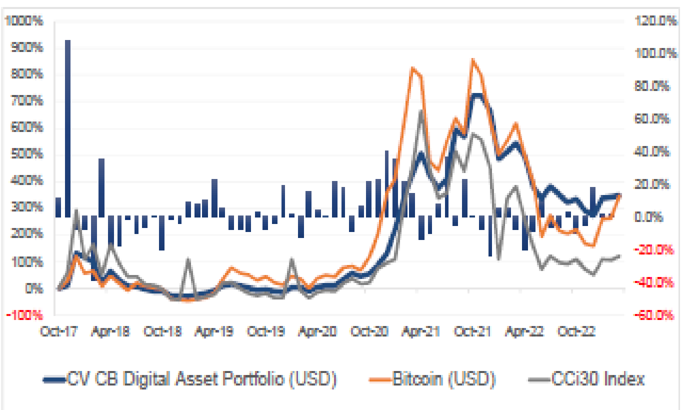
Fundamental drivers for the energy transition will support commodities for years to come, but prices will remain volatile. After strong gains in the first six months of 2022, commodities as measured by the Bloomberg Commodity Total Return Index subsequently gave back more than half of these gains between July 2022 and March 2023. The CB Global Commodity Portfolio (USD) participated in most of the upside, but generated substantial alpha and protected capital during the corrective phase. The liquidity of the strategy is monthly with 45 days' notice.

After experiencing a massive drop in value in 2022, digital assets - Bitcoins in particular - were the big outperformers in the first quarter of 2023. Despite regulatory hurdles, the space continues to expand and a growing number of large asset managers are active in crypto. There are attractive investment opportunities for the managers in the CV CB Digital Assets Portfolio or the CV CB Digital Alpha Portfolio. The liquidity of the strategies is monthly with 45 days' notice.

Cumulative returns since January 2014



Cumulative returns since November 2017

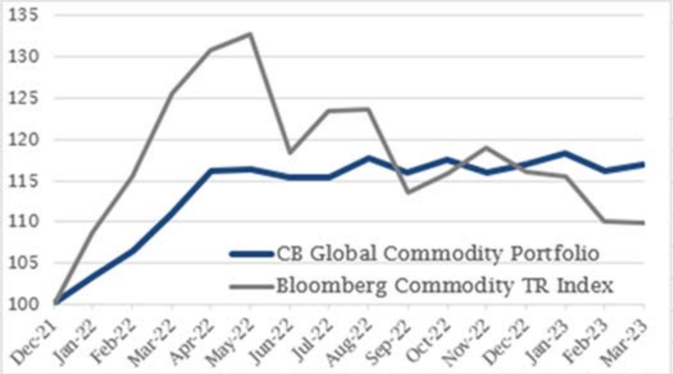


A smoother ride in commodities

The adverse price movements of commodity markets since June 2022, after strong returns in 2021 and the first part of 2022, represent a good case study to illustrate the improved risk/return profile that hedge funds can provide thanks to their active and flexible investment approach.

Entering 2022, the outlook for commodities continued to be constructive and commodities were up a strong +32.5% (Bloomberg Commodity Total Return Index, ‘BCOMTR’) from January to May 2022. However, fears of a global recession caused BCOMTR to plunge in June 2022 and commodities have been on a downward trend ever since. The good news is that commodity hedge funds can preserve capital or even generate positive returns during negative commodity markets, and thus generate a much more attractive return profile.

Taking as example the certificate CB Global Commodity Portfolio (USD), which invests solely in specialized commodity managers, shows that the recent negative results of commodities can be reduced, if not avoided. After the certificate participated in the bullish phase, it was then slightly positive (+0.6%) from June 2022 to March 2023, while commodities were down -17.2% during that period. The certificate’s positive result (alpha generation) from June 2022 to March 2023 came mainly from short positions in energy, trading in the agricultural sector, and the fact that no manager had a significant detraction. This illustrates the ability of active managers to limit losses (see Max drawdown in the table). Although structural fundamental drivers such as supply tightness and demand from the necessary energy transition will continue to support commodities for several years, their prices will remain volatile. We thus recommend to get exposure to the asset class through a diversified multi-manager portfolio that invests in commodity focused hedge funds managed by seasoned managers.



	Jan 2022 - May 2022	Jun 2022 - Mar 2023	Jan 2022 - Mar 2023	Max drawdown Jan 2022 - Mar 2023
CB Global Comm. Portfolio	16.3%	0.6%	17.0%	-1.8%
Bloomberg Comm. TR Index	32.7%	-17.2%	9.9%	-17.2%

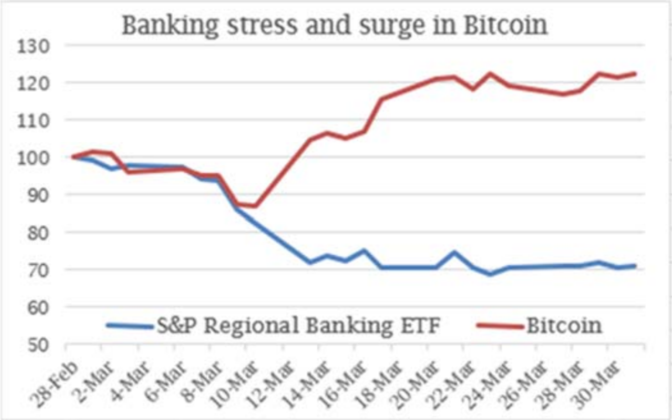
David Friche

Comeback of digital assets

Digital assets, and Bitcoin (BTC) in particular, were the clear outperformers in Q1 2023, which came as a surprise given the recessionary macro outlook prevalent in 2022 and the high correlation between digital assets and risk assets. But in January, as hopes of a possible soft-landing of the US economy and the Fed slowing down its pace of rate hikes emerged, capital flowed into risk assets, and digital assets (Cci30 Index +38.7%) including BTC (+38.8%) were up strongly.

After a range bound February (BTC +0.9%, Cci30 -1.6%), March proved to be a stand-out month for BTC (+22.7%) amid extreme market events, as three US banks were closed down within a few days. The bank turmoil forced the Fed to intervene, causing its balance sheet to balloon, and pushed safe haven assets (gold, BTC) higher. BTC was supported by its original role of decentralized peer-to-peer payment or store-of-value i.e. an alternative to the traditional financial system. Most other tokens had modest performance in March (Cci30 +7.5%).

As many long biased digital asset hedge funds are focused on altcoins rather than BTC, they underperformed BTC in January and March. Accordingly, CV CB Digital Asset Portfolio (USD) lagged BTC in Q1 2023, while CV CB Digital Alpha Portfolio (USD), being much less directional, continued to generate low volatility returns.



Despite US regulators being currently rather hostile towards digital assets, the space continues to expand, as ETH went successfully through its major Shanghai upgrade, some of the largest asset managers are active in crypto, blockchain games capture increasing attention, and big brands continue to embrace NFTs. The opportunity set is thus exciting especially for active managers in the space, and hence for the two CV CB products.

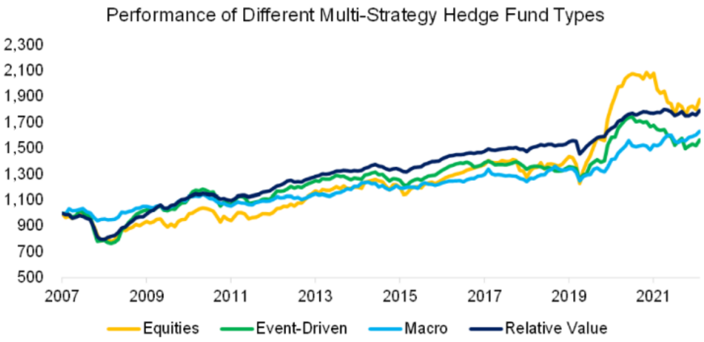
For more information please contact David Friche at df@cb-partners.com.

Multi-strategy hedge funds: Jack of all trades, or master of none?

Nicolas Rabener published his thoughts on Multi-Strategy Hedge Fund in the CAIA Association Blog: Citadel made USD 16bn in profits in 2022, Millennium 8bn, and Point 72 2.4 bn. These returns are spectacular as all three are multi-strategy funds that allocate capital to hundreds of trading teams. The goal is to harvest excess returns from many different sources and create a diversified portfolio. The expected return should be low, but consistently positive and not very volatile. Citadel's 38% return in 2022 had anything but these features. Given such stellar performance, the interest in multi-strategy hedge funds is rising again. Therefore he took a closer look at the main features of such Multi-Strategy Hedge Funds.

Asset under Management: The market share of multi-strategy funds as a proportion of the total assets of the hedge fund industry highlights that this has only increased marginally from 12% to 14% over the last 5 years.

Performance: Due to their tight risk management and reduction of drawdowns, the multi-strategy portfolios tend to be market neutral and often are leveraged aggressively. Although the returns for different multi-strategy hedge funds focusing either on equities, event-driven, macro or relative value strategies should be completely different, the performance since 2008 was remarkably similar.



Correlation: Similar as for performance, although the correlation between the different multi-strategy approaches should be low, all of them are above 0.6. This begs the question of what these multi-strategy fund managers are allocating to as the various trading teams seem to be offering just beta to equities, which most investors already have exposure to.

Nicolas Rabener confirmed his earlier view, that multi-strategy funds are not a desirable allocation, as capital allocators will get an average return. This due to the fact that beside the earlier mentioned out-performer there are as well under- performer, like TCI in 2022 which lost USD 8bn.

Hedge funds trading strategies and leverage


Armin Vogel

Wenli Huang, Wenqiong Liu, Lei Lu and CongMing Mu introduce learning into the hedge fund managers' risk choice problem with imperfect information. They find that with a constant but unobserved expected return on investment, learning induces managers to take more risks and increases manager compensation.

When the return is stochastic, learning increases manager compensation and induces an aggressive leverage choice when funds perform poorly or managers' belief about fund returns is low.

When funds are close to the high-water mark or the return belief is high, the learning effect reverses. This situation generates a flatter leverage ratio, which helps explain the cross-sectional dispersion of hedge fund strategies' market betas.

Finally, comparative statistics for transition intensity show that procyclicality in the hedge fund industry declines.

Anomaly discovery and arbitrage trading

Xi Dong, Qi Liu, Lei Lu, Bo Sun and Hongjun Yan analyze a model in which an anomaly is unknown to arbitrageurs until its discovery, and test the model implications on both asset prices and arbitrageurs' trading activities. Using data on 99 anomalies documented in the existing literature, they find that the discovery of an anomaly reduces the correlation between the returns of its decile-1 and decile-10 portfolios. This discovery effect is stronger if the aggregate wealth of hedge funds is more volatile.

Finally, hedge funds increase (reverse) their positions in exploiting anomalies when their aggregate wealth increases (decreases), further suggesting that these discovery effects operate through arbitrage trading.

Next Crossbow Event - Save the Date

On Wednesday, June 21, 2023 from 4:00 p.m. we are holding an event in the Zunfthaus zur Waag in Zurich, to which we cordially invite you.

A separate invitation will follow in due course.

If you wish the above mentioned paper, please contact Armin Vogel at av@cb-partners.com.