HOLDING COURT

Toby Crabel may have steered his systematic trading firm through more than two decades of fluctuating markets, but a first quarter performance among the sector's best shows he's not lost his edge. *HFMWeek* explores the factors behind Crabel Capital Management's longevity

BY WILL WAINEWRIGHT

Time-spans are short in the business world constructed and inhabited by Toby Crabel. The average trade at Crabel Capital Management lasts less than a day, and just 1% are active for more than 48 hours. Outlays are low too, with a high volume of small trades deployed via whichever channels are liquid enough to deliver them. But while trades are short-lived, Crabel's firm has been anything but. Now in its 21st year, the nearly $1.7bn AuM firm, headquartered in California, may be a veteran by CTA standards, but shows no sign of stagnation – the firm's flagship posted a peer-leading 12.38% for Q1, according to BarclayHedge data. *HFMWeek's* sister publication, *CTA Intelligence*, spoke to the softly spoken Crabel, who played tennis professionally before cutting his teeth on the trading floors of Chicago during the 1980s, to analyse the factors responsible for his firm's endurance in the cut-and-thrust world of CTAs.

DIVERSIFICATION

HAVE MANY EGGS IN MANY BASKETS

Crabel's trading strategy is premised on diversification. Small trades are placed for short time periods through as many available channels as possible, be they futures, cash interest rates or more complex instruments.

The golden rule is liquidity. "I found it convenient and sound statistically to find strategies that could be applied universally to all markets in the same way," says Crabel of the approach he developed during the 1980s.

Just as the same bets are made via different instruments, they are spread across different geographic markets too. "What we try to do is diversify in as many ways as possible," says Crabel, who targets "even allocations to regions, sectors and markets".

"If you do believe there is a small edge you want to exploit it using it as many different ways as possible, in parallel," adds Chekhlov. "The edge is tiny, so you extract maximum value by making the same bet multiple times within different markets and using different instruments."

THEORY

DON'T BE AFRAID TO BUCK THE TREND

Crabel's reputation as a counter-trend expert is an apt description not only of a major part of his trading style, but neatly sums up how he has overturned established views, according to industry peer Alexei Chekhlov, of New York-based quant firm Systematic Alpha Management. "Styles deployed by many of the short-term trading firms today can be traced back to Toby Crabel's book and the start of the 1990s," he says. His volume, *Day Trading with Short-term Price Patterns*, was published in 1990 and proved ground-breaking in an era when the theory of efficient markets was dominant. "It was not a popular theory at the time," continues Cheklov, "but many traders that followed him had that book on their coffee tables."

The industry was transformed during the mid-2000s by technology, which exploded the existing limits of short term trading. "The impossible became possible," says Chekhlov of the move to automation, "but again to begin with it was a minority game." Crabel was at the vanguard of using the new technologies to their full extent and adjusted to fit the times – most of his firm's trades now last less than a day.

TECHNOLOGY
MOVE WITH THE TIMES

Like many rivals, Crabel's returns declined in 2008 and 2009 – but he admits that a renewed focus on technology since then has been just as crucial to the firm's subsequent impressive performance as less volatile markets. "If you go back five or six years, when we were putting our automated platforms together it wasn't clear to me that we needed such intense work on the execution side in order to capture the edge from our strategies," says Crabel. "So I'd say in 2009 there was a very strong push towards development and ways to execute more effectively, to bring costs down."

Rapid execution is crucial in the systematic sector, particularly in Crabel's short-term business where trades come and go in seconds. "Strong technology is a hugely important component of success in the systematic world," explains Kevin Craney, a broker at Chicago-based RJO Futures. "Execution has become far more important in recent years with the advent of high-frequency trading. When you go after liquidity you need the speed to be there."

It has paid off for Crabel in style. "Whatever profit we had in 2012 is probably attributable to execution," he adds. "If we had the same cost structure that we did in 2009 (a flattish year) we would have had similar returns in 2012 as we did in 2009."

RECRUITMENT
LOCATION, LOCATION, LOCATION

Although the West Coast is home to Silicon Valley, the beating heart of America's tech sector, most quantitative asset managers are based in the traditional East Coast hedge fund hubs of New York and Connecticut. Here, too, Crabel has gone against the grain, having relocated to Los Angeles in 2009, which he thinks has helped him access the best talent.

"One of the benefits we have now that we are in California is that we are really one of very few quantitative firms," he says. "It's very competitive in New York but in Los Angeles there is not as many quant shops therefore we're a pretty good option when smart people are looking for jobs."

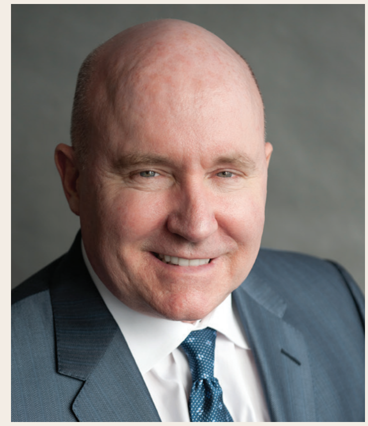
Recruiters add that workers are also attracted to California as the Golden State does not enforce non-compete clauses, meaning they can switch between firms more easily. "The proximity of Silicon Valley to a lot of great tech talent graduating from top universities provides a huge pool of potential employees," says Carlos Mejia, a managing partner at recruitment firm Options Group. "This combination provides the ideal place for firms to hire people, especially hedge funds that rely heavily on technology." The weather helps too, of course.

INVESTORS
DON'T FORGET YOUR ROOTS

Crabel got his start in the late 1980s and early 1990s managing accounts for wealthy clients and he says things have come full circle since then, with most inflows since 2008 coming via managed accounts, rather than the commingled product. "Because of the issues that came up in 2008 with banks and some of the hedge funds investors have been very interested in managed accounts," he says. "It had been difficult at first to replicate our performance in a fund in a managed account because we have so many trades but we did find a way to do so." He adds that demand for the products is still backlogged.

However, Crabel has, in common with the rest of the industry, been facing more pressure from clients on fees, particularly as the firm has traditionally charged on the high side (it takes 30% of all performance gains in its multi-product offering). "It's totally understandable that the clients are concerned about fees," says Crabel. "I prefer to be proactive about fees and pass along any cost savings that we can to the clients. There are certain things that the client can do to possibly getting lower fees including multi-year lock-ups where the client guarantees to some extent that the capital will stay in the firm."

TENNIS COURT TO TRADING DESK



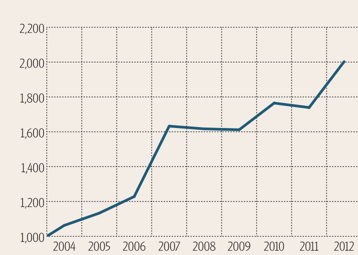
It is fair to say Crabel did not take a conventional route to systematic stardom. Not many expert traders emerge from the tennis court, but Crabel's scholarship and teaching career – he played the sport competitively in Europe during the 1970s – helped finance his early trades in Chicago's newly formed options market. He initially studied finance at Florida Technological University, before learning his trade in the Mid-West during the 1980s.

He wrote *Day Trading* in 1990 and had an enlightening spell working for industry luminary Victor Niederhoffer. He was ready to go it alone with his firm by 1992 and Crabel Capital Management has become a respected and established force in the space, notching up annualised returns of 12.31% over the last decade, its second in business.

The firm now manages nearly $1.7bn and is run from headquarters in Los Angeles, with smaller offices in Wisconsin and Connecticut. It employs 63 people, with about a quarter on the research side, and 57-year-old Crabel still serves as CEO and CIO. He told *HFMWeek* that plans are under way to ensure a long-term succession, with key figures at the company slowly building up stakes.

CRABEL MULTI-PRODUCT (A) PERFORMANCE

Graph charting the compound growth of $1,000 since 2004. 2013 YTD performance as of end Q1 is 12.38%.



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