

## ROBUST PORTFOLIO MANAGEMENT

Karim N. Taleb, Principal, Robust Methods LLC

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***“Our portfolio construction is ‘black-swan’ proof. Our strategy is unique to the extent it can continue generating returns which are uncorrelated to benchmarks and peers.” Karim Taleb***

***What is your brief assessment of the market?***

*I am surprised at how equities - excluding Japan - have shrugged off the devastating earthquake and tsunami. This is more remarkable given the fragile state of the developed economies and the Mideast uprisings that have been taking place prior to the disaster.*

*The fuel that lifted markets the past year, namely the stimulus and the artificial liquidity, is about to run out soon. The downside pressure is increasing at this stage.*

***So how does an investor deal with that?***

*It is certainly a time to be prudent and reassess positions for vulnerabilities.*

*Traditionally safe governmental bonds for instance are particularly at risk in the current state of*

*affairs. Short-volatility strategies as a group, including funds of hedge funds, need to prepare for a deep correction or a potential replay of 2008.*

***What is the investment philosophy at Robust Methods?***

*We accept the market for what it is; a constant tug of war between the bulls and the bears. We do our best to position the portfolio with the leading camp.*

*Our philosophy hence is not to adopt strong and rigid views, be they quantitative or judgmental.*

*Having strong market opinions and becoming attached to them is a dangerous thing when it comes to trading.*

*One clearly cannot change the market or make it conform to desirable views.*

***How does the investment process work given the above?***

*It is a tactical methodology that relies on applied statistics and probability theory. Our trading models blend theoretical constructs with quantitative methods to measure trends and pricing biases in the markets.*

*We enter and exit positions in an opportunistic manner hence, and based on the pricing biases detected.*

*The price biases in the market can change quickly and one must stand ready to seize the opportunity - agility and adaptability are paramount.*

***Do you short stocks, or use leverage?***

*We short the market as an index but avoid shorting individual names. As to leverage, we steer away from it and do not borrow money.*

**What is your investment objective?**

Gross annual returns of labor + 10% is our target, while maintaining a downside volatility of less than 12%.

Equally important is to provide uncorrelated returns to equities, bonds, and major indexes.

**Do you have a lock-up or redemption fees.**

There are no lock-ups or redemption fees. Liquidity is monthly with no strings attached.

**Any insight into the inner workings of the strategy?**

The speed and volatility patterns of markets have changed over the recent years with the advent of high frequency trading and quasi real-time event processing.

In terms of mechanics, the strategy requires a tighter and faster coordination between playing offense and defense, or adding risk and taking it off. Granted, this is much easier said than done.

**What is unique about your portfolio management approach?**

The strategy is unique to the extent that it can continue generating a return pattern exhibiting little correlation to benchmarks and peers. It brings substantial value to most investors.

Our portfolio is robust with an inherent positive volatility bias. It made money in 2008, a year during which most blue chip hedge funds lost heavily.

**How is your approach different from peers?**

**“Having strong market opinions and becoming attached to them is a dangerous thing when it comes to trading. One clearly cannot change the market or make it conform to desirable views.”**

The general approach is rather established. The difference is in the execution of a certain concept; two managers may have the same mandate yet one makes money and the other one doesn't.

**How did your hedge fund career get started?**

It started with opening my mailbox while in college and finding some junk mail touting stocks.

My background in quantitative disciplines came in handy too.

**What drives you every morning to be in this business?**

My motivation is to manage a robust portfolio that creates value to clients and friends. Markets are a tough place to be and odds are totally stacked against most investors.

Classic buy-and-hold strategies or even plain money in the bank have been a losing proposition in real terms over the past 10 years. A change in this trend is unlikely anytime soon, and if anything, it is likely to worsen given the current monetary and fiscal policies.

Investors are being caught in a think or sink situation.

**Talking about robust portfolios, how do you define robust?**

Do you want it fast or do you want it to last?

Robust is strong and resilient - it cannot be easily toppled. Think of it as a sumo wrestler in a squatting pose.

**End**