

Meet the Manager: Tony Caine, LJM Partners

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**Meet
The Manager**

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LJM Partners has deep expertise in options pricing and volatility, but besides trading, founder Tony Caine's other love is supporting academically talented inner city youth in realizing their dreams of a college education. To that end, **LJM Partners** has established the LJM Foundation and Summit 54 (named because Caine kicked off the launch of the nonprofit organization by climbing 54 Colorado peaks of more than 14,000 feet.)

Caine last spoke to HedgeFund.net in 2006 for this column.

HedgeFund.net: Since the last time you spoke to HFN in 2006, what has changed in your fund?

Tony Caine: Other than a few gray hairs from 2008, we've matured a lot as an organization. We've grown in our risk management and in some of our analytical tools. We've hired individuals with great depth in the hedge fund industry and in risk management that have Ph.D.s in risk management, physics and in quantitative finance. So we've added a quant level with individuals who are far smarter than I am to do two things: optimize the returns we're generating and develop models where we can contain risk within acceptable parameters for our clients.

HFN: Could you please elaborate on LJM Partners' strategy?

TC: We have varied strategies. We've developed great expertise in options premium management, in that we manage portfolios that take advantage of inefficient pricing of options and to maximize our decay in managing a portfolio with both long and short positions. So unlike when you last interviewed me in 2006, all of our funds now contain various degrees of hedging.

So if you were to look at our prime strategies: one is termed aggressive, which we have small amounts of hedging; one is called moderate aggressive, in which we target maybe 24% per annum, that has a reasonable degree of hedging; and we have a conservative strategy that we call preservation growth, which has great degrees of hedging.

HFN: Are there any specific sectors on which LJM focuses?

TC: We trade exclusively options on the S&P 500 Index in our three primary strategies. We have a fourth strategy which is an intraday volatility trading strategy that incorporates the S&P, NASDAQ, as well as oil.

HFN: How did you come to this particular focus for your investing strategy?

TC: It goes all the way back to 1981 when I traded my first equity option. How we evolved to this stage is that I traded equity options steadily through the 1980s when I was involved in high-tech -- I spent the first 16 years of my career in the technology industry -- but all the time while I was working the tech sector I traded options for my own account. Over the years, I evolved to trading options on the S&P futures exclusively for two reasons. First, it provided the best risk/reward model in that a broad index was not susceptible to the micro-economic events that can impact an individual equity. Second, because of liquidity; there is very good liquidity on the S&P futures options.

HFN: Did the 2008 economic crisis change any of your approach to trading?

TC: There have been dramatic changes since 2008. 2008 was a shot across the bow for anyone trading volatility. There was a period in 2008, with our aggressive and moderate-aggressive funds where we went straight to the sidelines. Once we got back into the markets, we reordered our risk tolerance and our risk models to include the tail events of 2008. So we've really changed our risk appetite and our risk profile and have ratcheted it down our target returns to adhere to a modern day reality that volatility can come into the markets at a blink.

HFN: Have you experienced growth in the last couple of years during the economic recovery?

TC: We have had some growth. At the time preceding the crash of 2008, the bulk of our assets were in managed accounts. In 2008, of our three strategies, our most aggressive strategy lost 46%; our moderate-aggressive strategy lost 15%, very palatable. Our most conservative strategy actually profited net approximately 9%. The good news was that it profited; the bad news was that the highest allocation in our funds was to our most aggressive strategy.

There was a drawdown of capital from exceeding \$400 million all the way down to about \$150 million. Today we are at approximately \$300 million.

So we rebounded quite well and the strategy we are directing more clients toward is our preservation and growth. The performance characteristics are such that in April, when we will finish four full years, over the period we will have growth close to 10% net for our clients.

In Q4 of 2008, when volatility was hitting its peak, we made money in the fourth quarter and in March of 2009, when the S&P reached 666, its lowest point, the preservation and growth fund was at its high water mark.

HFN: What do you see are the opportunities for a firm like yours going forward?

TC: Our historic markets have been high-net-worth individuals, family offices and smaller institutions -- Tier 3 and 4 institutions. Our opportunities are with Tier 1 and Tier 2 institutions. We're doing a lot of modeling where we can deliver products for those clients where we can cap risk exposure and maximize returns. So the big opportunity for us is to work with Tier 1 institutions to convince them that portfolios of options can be managed to tame risk while simultaneously taking advantage of mispricing and inefficiencies.

Historically, any firm that is viewed as "option premium writing," is viewed as the devil's work. I don't even like to use that term anymore because we have evolved where we first look at risk containment so that we can take advantage of more volatile markets.

We can wake up and get out of bed and markets can be gap-limit down. We can see a 10% gap in the market in a blink. We can not only profit in a sideways market, we can also take advantage if a market erodes comparable to what it did in 2008.