Proprietary traders – then and now

- The Volcker Rule's ban on proprietary trading ignores the fact that no bank required a bailout due to proprietary losses; on the contrary, our analysis shows that prop desks of Top 13 banks made a strong positive contribution to banks' revenue during FY07-FY10.
- In this note, we look at ex-prop traders that have struck out on their own: the majority of them have done very well indeed, even without the support from their megabank employers. To us, this suggests that the Volcker Rule weakened banks without strengthening the system.

Prop traders made a strong positive contribution to banks' revenues and profit ...

After years of discussions, the key US financial regulators[1] approved 'Volcker rule' on 10-Dec-13; and EU regulators are currently finalising the equivalent – albeit reportedly softer – rules. One of the more high-profile aspects of the Rule is that it bans banks from using their own funds to speculate in the securities markets; in so doing, it purports to protect 'the taxpayer' from banks' losses.

Here, we first restate our well-documented view that prop trading never came close to destabilising any of the major banks and thus never required a 'taxpayer-backed' bailout. As shown in the Appendix, data from the Bank for International Settlements (BIS) demonstrates that prop trading losses of 15 US and UK-based banks totalled less than 4% of total losses and writedowns sustained by these banks during the original 'Crunch'. Our own research shows that prop trading gains of Top 13 investment banks during FY07-FY10 comfortably exceeded prop trading losses.

We do not argue that prop trading ever was particularly 'risk efficient': indeed, our product-level VaR analysis shows that, over the FY07-FY10 period, revenue/VaR returns for prop desks in all product areas were far below that achieved by banks' non-prop units – suggesting that prop desks were taking much more risk to earn their revenue. The profitability of those desks, however, vastly outstripped profitability of client-oriented desks over the same 4-year period: cost/income ratios of prop desks were a fraction of their non-prop sales & trading counterparts. Far from endangering the banks (which was never the case), the prop trading contributed positively to their profitability.

... and most have done very well since leaving

Everyone is a friend to a trader running a $10bn prop trading fund in a megabank, but life may be very different in a start-up, even for the highest-profile traders. With the Volcker Rule now a reality, we wondered how well ex-prop traders have fared outside their former megabank employers: if they did well, would they not have done even better if supported by a bank that can weather crisis far better than a stand-alone fund?

In this note, we prioritised prop traders that worked in segregated, active prop desks (as distinct from principal investments, characterised by the long[er]-term investment horizon) in capital markets divisions, as well as some traders that traded the bank's own money as part of their wider role and managers of banks' internal funds which commingled banks' own and client's money. We left out traders who run only 'friends and family' money, and those that joined existing firms, unless their new teams were clearly segregated from the rest of the firm. Finally, we focused on the recent 'crop' of prop traders, which left their banks in the wake of the original 'Crunch' and largely (though not exclusively) as a result of the then impending 'Volcker Rule'[2]. The resultant sample comprises 25 senior prop traders and their teams from 10 of 'our' Top 13 investment banks.

Defining 'success' is tricky. Most new funds mentioned here have only been trading for 2-3 years, a period arguably too short to build a credible track record, especially in an area of business as volatile as prop/hedge fund trading. Moreover, reliable data on fund performance in comparable time periods is not always available. Consequently, wherever possible, we looked at the combination of two factors: fund returns and AuM growth. We favour the latter, trusting that hedge fund investors will desert the underperforming funds; but also acknowledge that funds – especially the larger ones - often insist on a lock-in (typically 2-3 years, though rumoured to be 7 years at ex-MS PDT Partners).

We conclude that the majority of prop traders in this study are doing rather well: only now they are making money for their investors, rather than banks. From that point of view, it is difficult to escape the conclusion that Volcker Rule's anti-prop bias weakened banks, without strengthening the system.

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[1] The Federal Reserve, Securities & Exchange Commission (SEC), Commodity Futures Trading Commission (CFTC), The Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency (OCC).

[2] Unfortunately, this leaves out some hugely successful prop traders-cum-money managers, including GSPS alumni Frank Brosens of Tatonic Capital Advisors LLC, Thomas Steyer of Farallon Capital Management; MountKeller's founders Mark McGoldrick and Jason Maynard; and many others.

Prop traders: then and now

Bank of America Merrill Lynch	Srini Dhulipala Previous: Head of Fundamental Credit prop trading Latest: Kildonan Castle Asset Management LLP	↑	In Sept-10, BAML became one of the first banks to lay off prop traders from David Sobotka's team. In June-11, BAML closed down its 15-strong prop credit trading team, led Scott Brown. One of the more senior members of Brown's team, Srini Dhulipala, co-founded Kildonan Castle fund, in Oct-11, with an estimated $250m AuM; the latest information we have suggests the firm (numbering 10 employees as of Dec-13) nearly doubled its AuM to $450m as of mid-3Q13.
Barclays	Todd Edgar Previous: Ex-Head of Macro Trading Latest: Atreaus Capital LLC	↑	Edgar opened Atreaus Capital LLC, the liquid global macro and commodities fund, in June-12. The other founding partners were Dmitry Shklovsky (a colleague from Tudor Investment Corp), Peter Buschmann, Sinan Gumusdis and Michael Ridewood; this team worked together since 2005, at JPM and then BARC. Andrew Downes is the 6th partner, having joined from UBS. Atreaus started trading with $307m (including seed money from GS, rumoured to be c.$200m). The firm had a great start, doubling AuM by Feb-13 and achieving $672m by July-13.
BNP Paribas	Christopher Brandt Previous: Head of Strategic Trading Latest: Head of Markham Rae's rates and FX prop fund	?	At BNPP, Brandt ran London prop trading desk until Dec-10, when he co-founded (with Jonathan Martin, ex-Head of Risk Management at Blue Crest) Markham Rae, a prop trading firm which manages $340m for an unnamed French institutional investor. Markham Rae targets EUR1bn in total AuM; it reached $590m in late 2012). In Oct-11, Markham Rae launched the segregated prop trading fund run by Brandt (with Martin overseeing risk control). The fund started with AuM of $55m and focuses on currencies and rates. Our sources agree the fund did well, but we do not have firm data.
Citigroup	Andrew Hall Previous: Head Trader, Phibro Latest: Astenbeck Capital and CEO of Phibro	↑	Hall was the head trader of Citi's proprietary energy trading unit until Citi sold Phibro to Occidental Petroleum in late 2009. Hall is now CEO of Phibro… … and also runs Astenbeck Capital (20% owned by Occidental) with two ex-Phibro commodities funds. Returns outclassed most peers: since the launch in Jan-08, Astenbeck Master Commodities Fund II generated a total return of 54% through Aug-13.
	Sutesh Sharma Previous: Ex-Head of Principal Strategies Latest: Portman Square Capital	↓	Sharma co-founded Old Lane Partners with Citi ex-CEO Vikram Pandit. Citi bought Old Lane in July-07; Sharma became the bank's head of the prop trading team. Following the closure of the 15-strong prop desk in Jan-12, Sharma founded London-based Portman Square Capital, a multi-strategy relative value fund. The firm had a troubled start. Initially targeting $500m, it scaled its aim to $200m by Mar-13, and lost CEO Andrew Mack (ex-MS) and a key portfolio manager; in July-13, rumours emerged than the fund raised only $100m.
Credit Suisse	George 'Beau' Taylor Previous: Head, Commodities prop desk Latest: Taylor Woods Master Fund LLP	↑	Taylor ran CS commodities prop desk. In 4Q10, he left with several team members and opened – with Trevor Woods, CS' top energy arb trader – Taylor Woods Master Fund LLP. TW started trading with $150m of seed money from Blackstone; it posted negative returns in 2011 and 2012 (-5% and -2%), but excelled in raising new money: AuM grew to $500m at end-June-11 and to $1bn+ by Mar-12, when the fund closed to new investors. In 2013, while many peer funds struggled, TW was up 18% in the first 10 months.
	Charlie Chan Wai Kheong Previous: Trader, FX Prop Latest: Splendid Asia	↑	Chan publicly claimed that he made money in all but two of his 25 years at CS averaging double-digit returns; to our knowledge, CS did not object to these claims. Chan launched Splendid Asia, a macro hedge fund, in Aug-11. The fund is small – it launched with $37m, half of which was Chan's own money – but posted spectacular returns: up 63% y/y in 2012, with AuM of $105m.s

Source: Bloomberg, FINalternatives, HFI, HFR, Hedgeable, Institutional Investor, Reuters, WSJ. Tricumen analysis.

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Prop traders: then and now (cont.)

Deutsche Bank	Key Heigh Previous: Head, Global Macro trading Latest: Avantium Investment Management	↑	Kay, ex-Head of Emerging Markets debt trading and Head of Global Macro trading, left DBK in Apr-11 with seven colleagues and, in Oct-11 opened Avantium Investment Management, a macro fund focused on emerging markets. DBK did not seed the new fund but the founders could be forgiven for not noticing this: in its first 6 months, Avantium tripled AuM to $600m, posting gains of 7% since inception. The fund, which targets AuM of $1bn, won HFR's 2013 'Emerging Manager of the Year' award, and even found time to launch a rather neat Android app in 2013.
Deutsche Bank	Boaz Weinstein Previous: Credit trader Latest: Saba Capital Management LP	↑	Weinstein worked at DBK until 2009; as hugely profitable pre-Crunch years turned into a $1.8bn loss in 2008 (some positions rebounded later in the year), Weinstein moved his 15-strong team out of DBK. Saba Capital launched in Aug-09 with AuM of c.$150m; in the following 2 years, the fund achieved net annualised returns of 13%, comfortably within its stated target range. By late 2013, the firm's flagship fund reached a spectacular $4.2bn, in addition to c.$0.8bn AuM in Saba Capital Tail Risk Fund, launched in late 2010.
Goldman Sachs	Pierre-Henri Flamand Previous: Co-Head, GSPS Latest: Edoma Capital (closed)	↓	Flamand, ex-Co-Head of GS Principal Strategies (GSPS) left the bank in Mar-10. In Nov-10, Flamand launched Edoma Capital, the event-driven hedge fund with $1bn+ in commitments. Edoma reportedly peaked at $2bn AuM but suffered reversals in 2011 and 2012 (while its peers averaged gains of 5% in the same period, says HFR) and closed in Nov-12.
Goldman Sachs	Morgan Sze Previous: Head, GSPS Latest: CIO,	↑	Sze led GSPS APAC arm, which was rumoured to have managed AuM of $3bn in mid-2011. After Flamand's departure, Sze took over the global leadership of the team but left when GS closed GSPS in Sept-10 and founded HK-based Azentus Capital Management Ltd in Apr-11, with $1bn. The fund grew quickly – some say to nearly $2bn within a few months of inception – but performed poorly in its first year. Since then, however, it enjoyed a healthy growth: it returned 8% before fees by 1Q13 alone, and was rumoured to have reached $1.6bn AuM, making it one of the largest APAC funds.
Goldman Sachs	Elif Aktug Previous: Portfolio Manager, GSPS Latest: Agora Fund Ltd	↑	Ms Aktug, formerly Portfolio Manager at GSPS, in Apr-11 opened Agora, an internal long/short equity fund investing in large European companies within Pictet Asset Management in Geneva. Agora is said to have had a 'mixed' 2011. In May-12, however, PAM made the fund available to external investors; the first few months were difficult, but the performance quickly improved and the fund has not looked back: in 2013, it was up c.10% y/y, in line with its target annual returns of 8-12%. Agora's AuM reached $96m at end-Nov-13.
Goldman Sachs	Daniele Benatoff & Ariel Roskis Previous: GSPS traders Latest: Benros Capital Partners LLP	↓	Benatoff and Roskis were traders in the GSPS until Sept-10. Less than a year later, supported by $300m seed money from Brummer & Partners AB, the pair opened Benros Capital LLP, and event-driven, London-based hedge fund. Benros barely grew AuM in 2011 and 2012; reportedly underperforming event-driven peers; in Feb-13, the fund was closed down when Brummer (45% shareholder) decided to redeem its investment.

Source: Bloomberg, FINalternatives, HFI, HFR, Hedgeable, Institutional Investor, Reuters, WSJ. Tricumen analysis.

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Prop traders: then and now (cont.)

Goldman Sachs (cont.)	**Mark Carhart** Previous: Co-Head, Quantitative Investment Strategies (QIS) Latest: Kepos Capital		Carhart (who, alongside Raymond Iwanowski, who opened a small hedge fund at SECOR in Oct-13) co-led GS Quantitative Investment Strategies unit and Global Equity Opportunities and Global Alpha, GS' internal quant funds which suffered significant losses during the original 'Crunch' and were closed. In Oct-10, Carhart launched Kepos Capital wth 27 staff, many of them GS alumni. The fund's original goal was to raise $1bn; the firm fell far short of this goal, but performed strongly, achieving 13% return between inception and June-12, to reach AuM of $500m; it also won Institutional Investor's macro-focused systematic/quant award for 2013.
Goldman Sachs (cont.)	**Robert C Jones** Previous: Head, GSAM QES Latest: System Two Advisors LLP		Jones is one of GS' original 'quants': not a prop trader but well worthy of mention: he established and led GSAM Quantitative Equity Group and also managed GS' quant hedge fund Global Equity Opportunities Fund, from Mar-09, after the fund suffered disastrous losses in 2007-09 under Carhart and Iwanowski (see above). Jones left GSAM in 2010; in mid-2012, with $50m of seed money and quants from Blackrock and GS, he opened System Two Advisors LLP. The firm's investment method combines the 'traditional' quant approach with a decidedly high-touch, stock-specific analysis gleaned from research reports. It is early days yet, but the fund is believed to have doubled AuM by the end of 3Q13, to $100m.
J.P.Morgan	**Mike Stewart** Previous: Co-Head of prop trading / Head of Emerging Markets Latest: Whard Stewart Asset Management Ltd	?	In Feb-11, anticipating the pressure from Volcker Rule, JPM decided to move its main three prop trading teams out of Investment Bank and into asset management division. Stewart was asked to run the new fund; he was going to be joined by Deepak Gulati (equity derivatives specialist from the Proprietary Positioning Business - PPB), Fahad Roumani (credit) and approximately 50 traders. There were rumours that JPM was planning to seed the fund with c.$2bn. In Mar-12, however, Stewart left JPM with 4 colleagues and in Aug-12 opened Whard Stewart Asset Management Ltd, a global emerging markets macro and FX fund, in London. The fund started trading with $150m from a core group of investors. We hear the fund has done well since its inception, but do not have firm data.
J.P.Morgan	**Deepak Gulati** Previous: Head of Equities prop trading Latest: Argentière Capital	?	In Feb-12, in a move some thought partially prompted by Stewart's departure, Gulati anounced his intention to leave the bank, together with his JPM team – and with the full support of JPM. The new fund, Argentière Capital, raised $300m, making it one of the more significant launches of in 2013. The fund, which launched in June-13, has 15 staff and combines event-driven and quant investments, is said to target AuM of no more than $750m.
J.P.Morgan	**Fahad Roumani** Latest: Head of JPS Credit Opportunities Fund		The last member of the trio, Roumani, remained at JPM after Stewart and Gulati departed. He runs JPS Credit Opportunities fund, which JPM launched with $350m of its own money. The 20-strong fund did very well from betting on dislocations in European fixed income markets; by Oct-12, the fund, which returned 14% in that year, ammased $500m AuM – and that's after JPM cut its stake by c.25% (JPM plans to exit its stake entirely by mid-2014). Roumani targets $1bn AuM.
J.P.Morgan	**Andrew Pickup** Previous: Head, Proprietary Positioning Business (PPB) Equities Latest: Visium Asset Management LP	?	Pickup, ex-Head of the PPB Equities team, developed long/short prop unit in London and NYC and managed a multistrategy portfolio that combined long/short, convertibles and volatility. In Nov-09, Pickup joined Omni Partners to run a new long-short equity fund which quickly attracted $100m in seed funds. In Jan-13, Pickup went to Visium as a portfolio manager in the hedge fund's newly opened London office.

Source: Bloomberg, FINalternatives, HFI, HFR, Hedgeable, Institutional Investor, Reuters, WSJ. Tricumen analysis.

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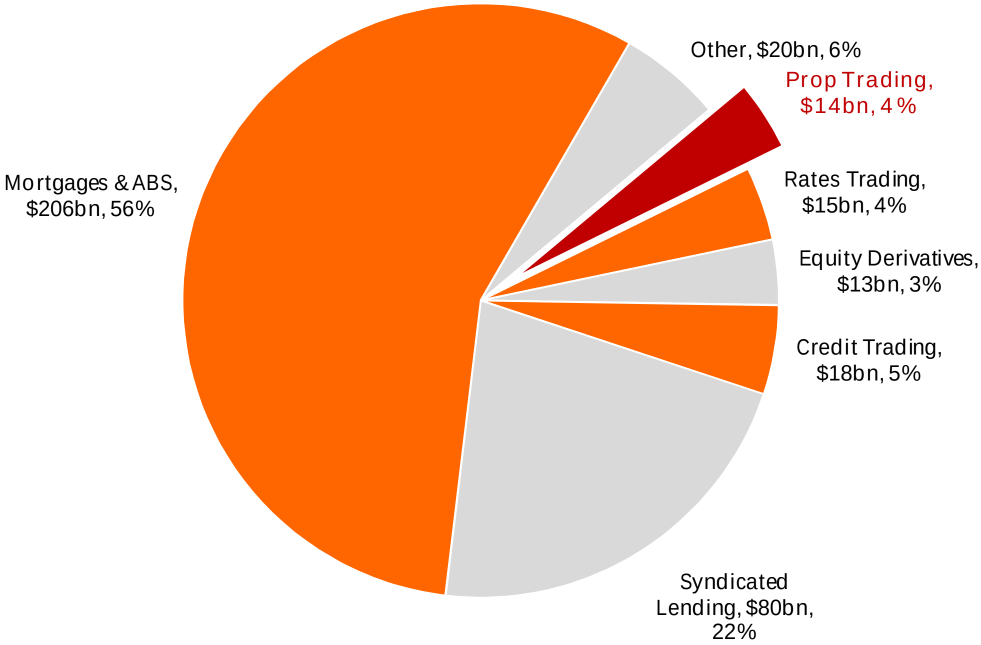
Prop traders: then and now (cont.)

Morgan Stanley	Peter Muller Previous: Head, Process Driven Trading Latest: PDT Partners LLC	Muller, a quant specialist, is a former Head of MS' Process Driven Trading desk that he founded in 1993. In Jan-11, Muller and MS reached an agreement that 60-strong Process Driven Trading desk will launch an independent advisory firm – called, surprisingly, PDT Partners - by the end of 2012. At MS, Process Driven Trading reportedly returned 20%+ annually over the previos decade. PDT Partners launched its first fund in July-12, with $500m of seed capital from Blackstone. To say the launch was well received would be a rude undestatement – by Oct-12, the fund closed to new investors with AuM of $1.5bn, despite eye-watering management and performance fees, of 3% and 35%, and up to 7-year lock-up period for investments. Also, very uncharacteristically, Blackstone did not insist on owning a stake in the firm to go with its large investment. By Feb-13, PDT Partners – now with two funds, staff of 90+ and office in NYC, London and HK – ran AuM of $2.3bn.
Morgan Stanley	Stephen Jamison Previous: Commodities trader Latest: Jamison Capital Partners	Jamison, a former commodities trader, launched Koppenberg Macro Commodity fund with AuM of $125m in 2009. Since then the fund reportedly returned 18%+ in 2010, a respectable 8% in 2011 and a modest <3% in 2012, outperforming competition. New money poured in: by Mar-13, the fund 'soft closed' to new money when AuM reached $1.5bn, nearly 2x the level of a year previously.
Morgan Stanley	Fabrizio Gallo Previous: Global Head of Equities (prop) Latest: Bank of America Merrill Lynch	At MS, Gallo was Global Head of Equities and Prop Trading (the second half of the title was dropped sometime in 2008). He left in Apr-09 and resurfaced in Brevan Howard, which hired him to run Equity Strategies Master Fund, comprising $600m of mostly Brevan Howards; own money. It is said that Gallo's fund achieved only meagre returns and Brevan Howard closed it in early 2011. In May-11, Gallo agreed to join BAML as Co-Head of Equities and EMEA Global Markets.
UBS	Shane Finemore Previous: Head, UBS Fundamental Latest: Manikay Partners	Finemore left UBS and launched his start-up fund Manikay Partners in Aug-08, with $300m, including seed investment from GS and his own $25m. The firm did well: in Nov-13, AuM stood at an estimated $1.7bn.
UBS	Gerard Satur Previous: Head of Macro Strategic Trading Latest: MST Capital Pty	? Satur ran UBS' team with a mandate to trade on macroeconomic trends. In Mar-12, as UBS scaled down prop trading, Satur left the bank and opened MST Capital in Sydney, with 6 staff. As of mid-2013, MST Capital had AuM of c.$165m in two funds (the 2nd, Baruch Global Macro, was launched in July-13, with $9m AuM), mostly from institutional investors. The fund targets 10-15% returns.

Source: Bloomberg, FINalternatives, HFI, HFR, Hedgeable, Institutional Investor, Reuters, WSJ. Tricumen analysis.

Appendix: Prop trading losses and gains

Losses sustained during the ‘Credit Crunch’, by business line
(5 US banks and 10 banks operating in the UK, Jan-07 – Mar-09)



Source: Bank for International Settlements (BIS), Tricumen analysis. Tricumen definitions apply.

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