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Dalton Street Capital shuns traditional investing for quantitative model

Left-right: Nick Selvaranam and Alan Sheen of Dalton Street Capital with Steve Tucker executive chairman of Prodigy Investment Partners. **Jessica Hromas**

by **Joyce Moullakis**

Dalton Street Capital wants to prove to local investors that quantitative factors and analysis can deliver better returns than relying on traditional investment research and stockpicking.

The new boutique firm set up by former Credit Suisse duo Alan Sheen and Nick Selvaratnam is the latest fund to partner with former MLC boss Steve Tucker's Prodigy Investment Partners.

Mr Selvaratnam was up until recently head of equities at Credit Suisse Australia and Mr Sheen, who helped form the algorithm and model implemented by Dalton, was formerly a proprietary trader at the investment bank.

They are both trained engineers with an interesting take on investing.

"I've spent almost my whole life avoiding investment analysts," Mr Sheen quipped. "With this algorithm we only bring in actual figures of volatility and liquidity and rearward-looking actual numbers."

He noted the firm looked to capitalise on a "behavioural bias" between the US and Asia Pacific markets.

Dalton has kicked off an absolute return fund that aims to provide positive returns in all market cycles. The underlying model draws on quantitative principles as well as behavioural finance.

The fund, which targets investors that want returns that are uncorrelated to any index benchmark or traditional asset class, aims to hold about 50 investments in underlying securities across markets including Australia, Singapore, Hong Kong, Japan, Korea and Taiwan.

It also employs derivatives and futures strategies to take advantage of market volatility.

Mr Selvaratnam said the strategy took greater interest in overriding market factors over stock-specific ones.

"We believe we have a deeper understanding of interrelated market behaviour and we are capturing that through the strategy," he said.

He points out that between 2007 and 2011 – encapsulating the global financial crisis and the fallout – the strategy had average annual returns, not taking into account fees, of more than 20 per cent.

During the period 2011 and 2016 annual average returns were of similar magnitude.

Dalton is hoping to tap into volatility being a significant theme in 2016, particularly given events such as the successful Brexit vote and the fact that many local investors want to diversify away from traditional strategies.

"Volatility is one of the biggest input factors in our model," Mr Selvaratnam said.

"As with Brexit, other events that come to mind where our strategy experienced success include the Fukushima nuclear disaster and the global financial crisis."

More traditional hedge funds have faced scrutiny again this year as investors questioned their fee structures versus returns.

Dalton does not, however, intend to engage in short selling. As part of its strategy, the fund uses leverage every trading day but derivative positions are closed out at the end of every day.

The product disclosure statement notes a 1.5 per cent annual management fee and a performance fee of 20 per cent. The performance levy kicks in above a hurdle rate of 1.5 per cent return per annum.

Risks in the PDS include potential changes to regulations across the markets and large movements against the Australian dollar. The fund's currency exposure is hedged though.

Mr Tucker said Dalton had a distribution agreement with a partner in Asia and was in discussions with research groups, high net-worth and institutional investors, family offices and financial advisers.

Street Talk revealed the formation of Dalton Street in May. It is the latest boutique to partner with Mr Tucker and broking and funds group Euroz.

Mr Tucker wants as many as eight boutiques within Prodigy over the next four to five years.

Mr Tucker's Prodigy is a joint venture with Euroz and added its first boutique, Flinders Investment Partners, a year ago. Flinders is an emerging companies fund.