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Fund using freelance programmers beats US stock market

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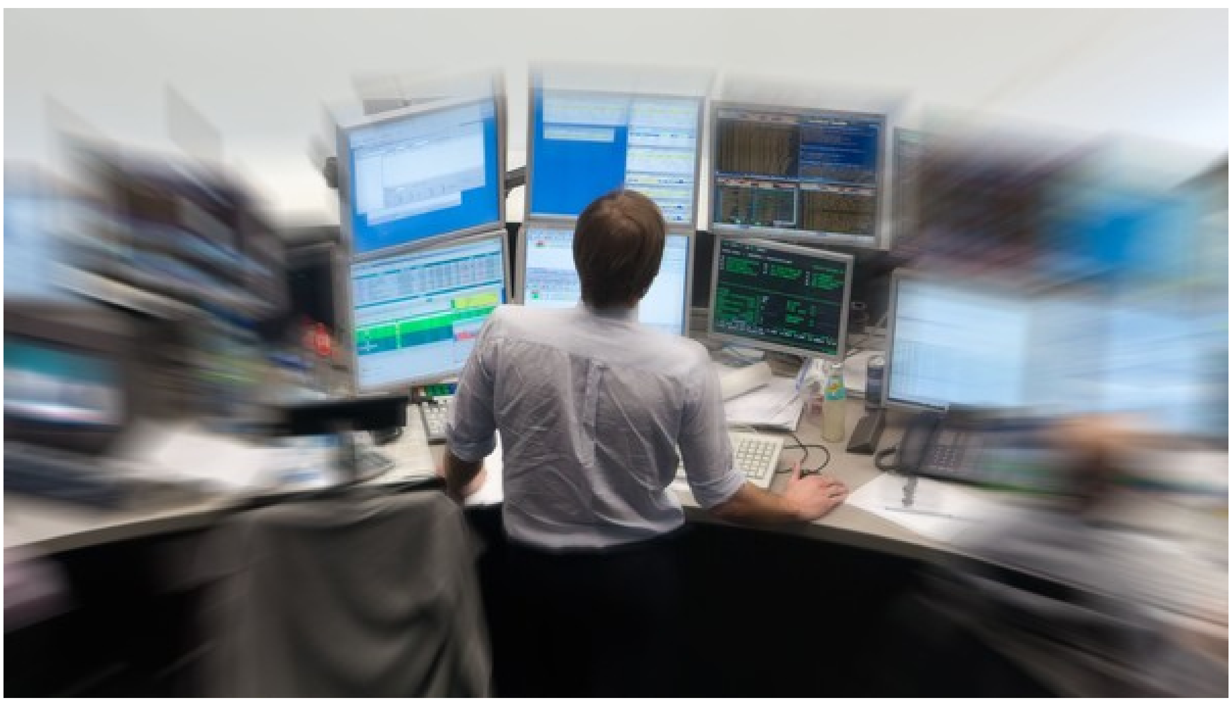

A "crowdsourced" hedge fund that uses the trading algorithms of a handful of freelance programmers notched up a 1.93 per cent gain net of its theoretical fees in its first full quarter of trading — beating the US stock market.

Boston-based Quantopian runs a platform for programmers, mathematicians and data scientists that allows them to design and test stock trading algorithms, offering a $100,000 trading kitty to the best-performing strategy every month, with the winner keeping any profit they make over the next six months.

Its community of registered "quants", or quantitative traders, swelled to nearly 60,000 last year, when it also started an internal hedge fund seeded with its own capital. This harnesses the best set of algorithms on its platform, sharing 10 per cent of the proceeds with the authors.

Quantitative investing — using complex mathematical models, supercomputers and even artificial intelligence techniques to identify profitable patterns in the swelling sea of "Big Data" — has been around for several decades. But it has become increasingly popular in recent years, thanks to the enviably strong and steady returns by the industry's heavyweights, such as Renaissance Technologies, DE Shaw and Two Sigma.

But there is a shortage of talent, with many computer scientists preferring to work in Silicon Valley, so hedge funds have had to offer various competitions or establish alliances with universities to ensure a pipeline of talent. Quantopian offers members access to data and coding tools so they can trade as a sideline to their main jobs, or even from home.

Quantopian's unaudited 1.93 per cent first full quarter returns are net after the fees paid to the authors, an assumed 2 per cent management fee and the firm's own 10 per cent performance fee — a structure that mimics the common "two and 20" hedge fund fee structure. The S&P 500 rose 0.8 per cent during the first quarter.

John Fawcett, Quantopian's founder and chief executive, stressed it was important to "stay sober" on the early, unaudited results on trading the initial slug of $500,000 of capital, but said the initial results were encouraging.

"The number of algos and the size needs to be ramped up in the coming months to achieve our objectives."

The plan is to open up the hedge fund to outside investors once its record has been established. Quantopian's initial foray used computer-powered strategies for the US stock market designed by eight members — who range from a mechanical engineer in Australia to a US software developer at an internet search company — but the company plans to eventually use 20-30 algorithms at any given time.

It plans to increase the firepower of the nascent hedge fund to $1m of capital this year, and increase the leverage of the hedge fund from close to one time its capital to three times. In time it intends to ramp up the leverage to six times capital to enhance the returns.

While there is growing enthusiasm over the potential for "DIY quants" to go head-to-head against industry heavyweights, thanks to widely-available quick internet connections and increasingly powerful personal computers, some sceptics warn that these freelance algo traders will over time not do much better than their more primitive day trader predecessors.

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