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The Shifting Role of Alternative Market CTAs

Executive Summary

Alternative market CTA performance has weakened in recent years, and for the first time, the strategy has underperformed more traditional CTAs.

In this paper, we delve into the past drivers of alternative market CTA performance, drawing comparisons with trend following in traditional CTA markets.

We then show how, even with modest performance expectations, alternative markets can make a valuable contribution as part of a diversified CTA strategy or portfolio of CTAs.

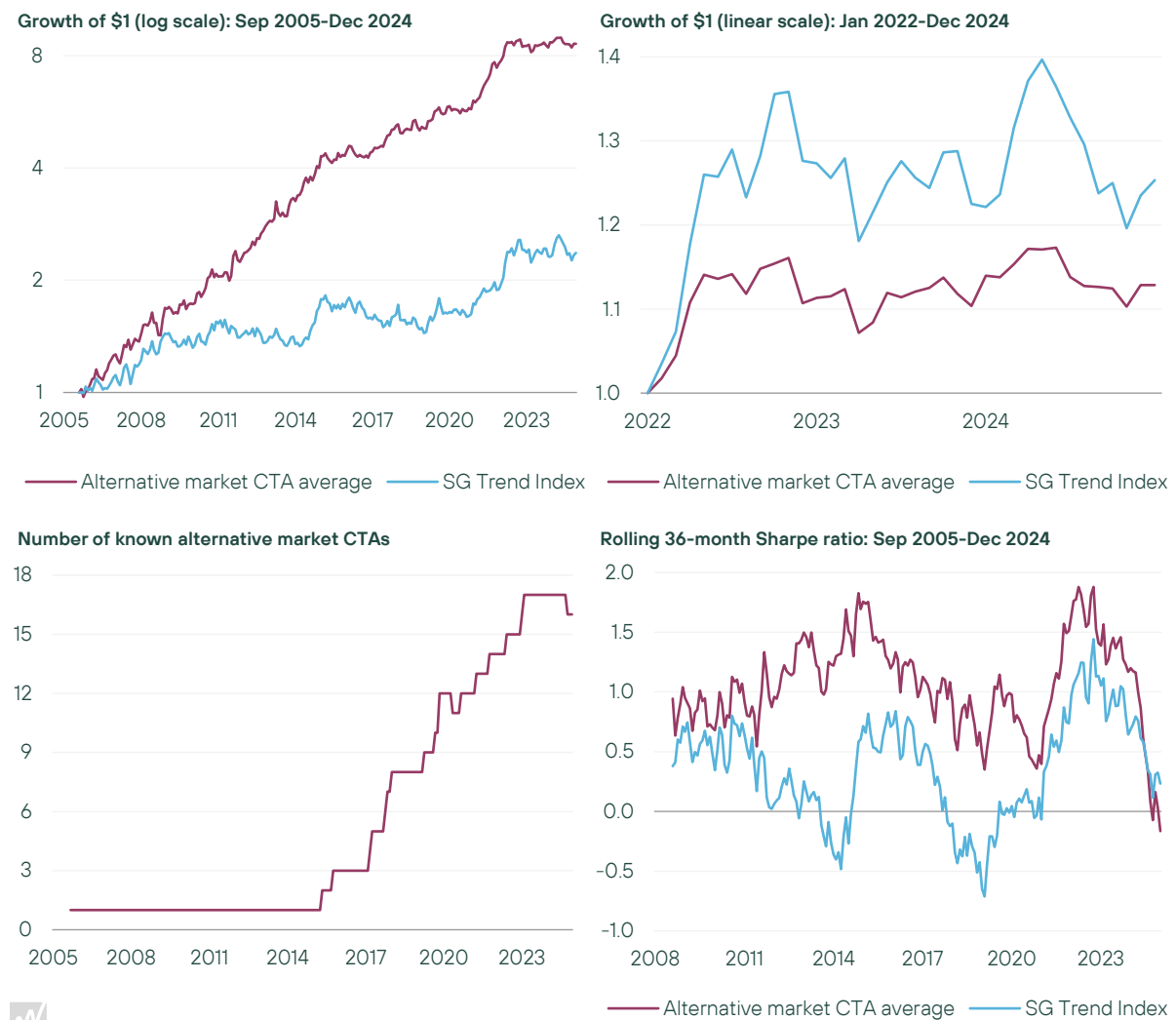
Finally, in an appendix, we examine alternative market liquidity and discuss how assets under management can affect strategy design.

Is the party over for alternative market CTAs?

After outperforming the wider trend-following CTA industry for many years, CTAs focused on alternative markets had a difficult 2024, with the two largest strategies by assets under management posting the worst calendar-year returns in their 20-year and 10-year histories.

It is not only the largest alternative market CTAs that have struggled recently; returns across the space have been muted, with average performance trailing the SG Trend Index for the first time over a rolling three-year window. At the same time, alternative market CTAs have proliferated and their assets under management have grown considerably: we identify at least 16 alternative market CTAs trading today, with a combined \$29 billion of assets, around double the figure reported five years ago.¹

Figure 1: Average alternative market CTA performance compared to the SG Trend Index



Source: Winton, HFR, NilssonHedge, marketing presentations, as at 31 December 2024. **Past performance is not indicative of future performance.** The alternative markets group includes 18 known alternative market CTAs, of which two have stopped reporting and are assumed to be closed. While most are diversified across all the major alternative market sectors, three focus solely on Chinese markets, one on alternative commodities and one on alternative financials. Two are positioned as non-trend alternative markets CTAs. The **SG Trend Index** reflects the performance of the 10 largest trend-following CTAs open to new investment. Further information on the index's methodology is available on Societe Generale's [website](#).

¹ AUM estimated based on strategy data collected from HFR, With Intelligence, NilssonHedge and marketing presentations, as at 31 December 2024.

The distinction between *alternative* markets and the *major* futures and forwards markets traded historically by CTAs is somewhat arbitrary and open to interpretation. The matter is confused further by the fact that the industry's leading diversified CTAs trade both the traditional CTA markets and alternative markets. Generally though, alternative market CTAs focus specifically on OTC markets, emerging market futures, and newer or non-standard futures. Some alternative market CTAs also include equity sectors, ETFs, synthetic assets, and volatility instruments.

The decline in returns for alternative market CTAs is not a surprise: we have long believed that the performance of trend following in alternative markets would converge to the levels seen in traditional CTA markets as more managers begin to trade them. The real and enduring benefit of alternative markets, and alternative commodities in particular, is their highly diversifying properties, much like many of the traditional commodity futures. As a result, the diversification generated – rather than the historical performance delivered – should be the main input when sizing exposure to alternative markets in a diversified CTA strategy.

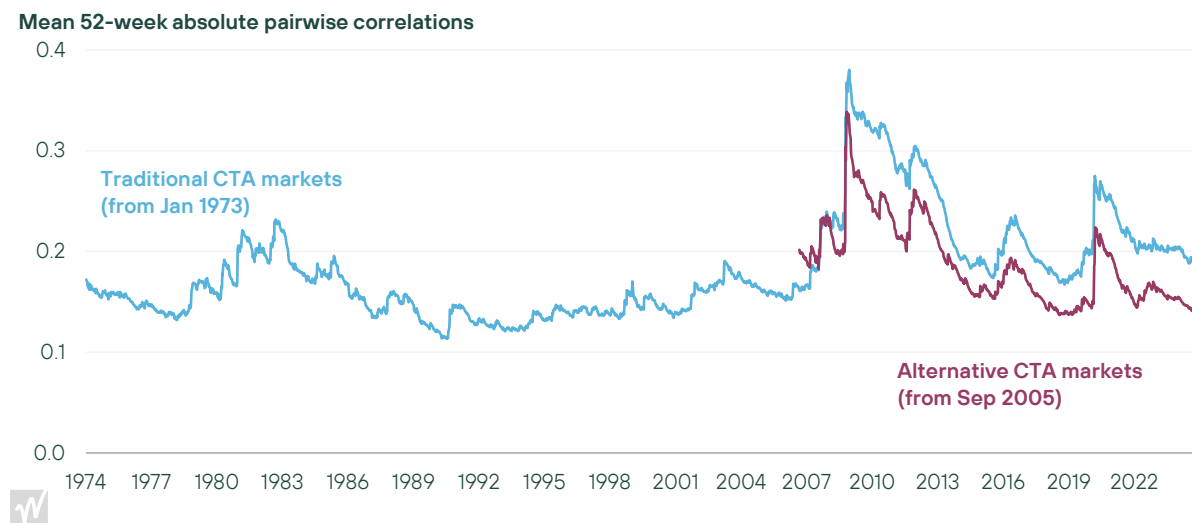
Over the rest of this paper, we examine the recent drop off in alternative market CTA returns by reviewing the evolution of the strategy's performance drivers since the first alternative market CTA began trading in 2005. We contextualise this performance by comparing it to trend following on traditional CTA markets since 1973. And we then show why – even with modest performance expectations – alternative markets can make a valuable contribution as part of a high-quality diversified CTA or portfolio of CTAs, improving the range of expected performance outcomes.

In short: alternative markets are still a valuable addition to a diversified CTA or portfolio of CTAs, but perhaps not quite as much as their performance in the 2010s would suggest.

Past drivers of alternative market CTA outperformance

Trend following tends to have a low Sharpe ratio in any individual asset, so the strategy benefits from being applied to many uncorrelated markets. By this measure, alternative markets look appealing, especially after an increase in correlation between markets following the 2008 global financial crisis. As Figure 2 highlights, alternative market correlations spiked less than traditional market correlations in 2008 and have been consistently lower ever since.

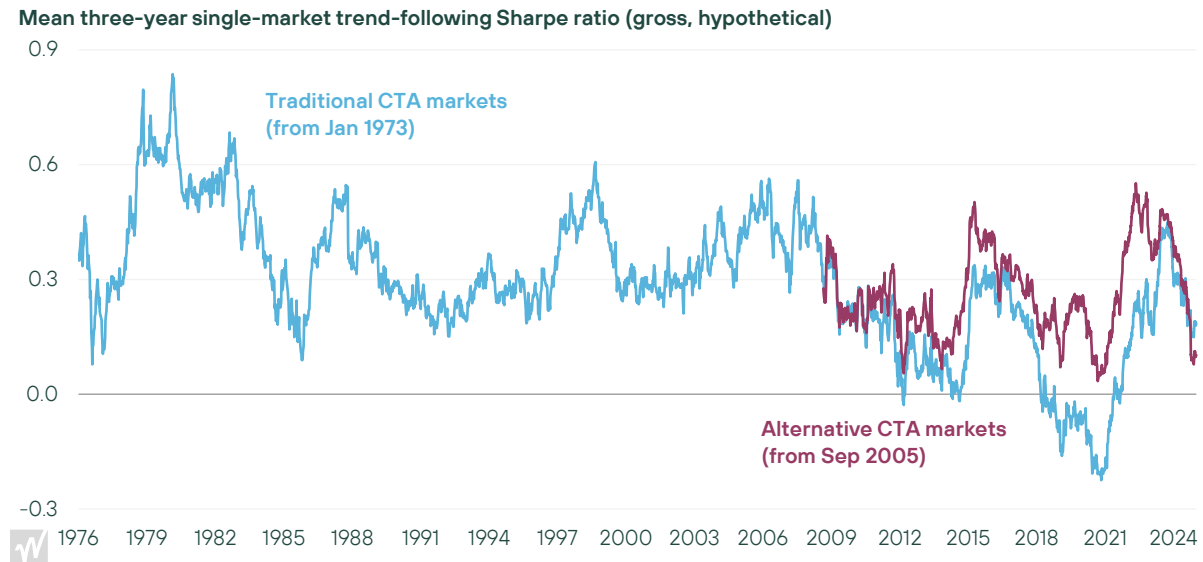
Figure 2: Lower inter-market correlation in alternative markets



Source: Winton, Bloomberg, as at 31 December 2024. The 52-week exponentially weighted correlations are calculated using front-month contract returns and weekly return data to mitigate timing effects. Traditional CTA markets are included from when data is available, starting with a universe of 37 markets in 1973 and ending with the current ~150-market universe. Alternative market correlations are included from September 2005, the reported start date for the oldest alternative market CTA. The universe includes 74 markets in September 2005, with a bias to emerging market currencies and interest rate swaps until 2009, and this figure increases to over time to the ~150 markets today.

The underlying markets also showed more profitable trending behaviour in the 2010s that was more consistent with the behaviour seen in traditional CTA markets prior to 2009, avoiding the bouts of negative performance. This is visible in Figure 3, which compares the mean single-market Sharpe ratio of a long-term trend-following strategy on alternative and traditional CTA investment universes.

Figure 3: Higher average individual market Sharpe ratios



Source: Winton, Bloomberg, as at 31 December 2024. Hypothetical slow trend-following strategy simulated on a universe of alternative and major markets shown for research purposes only. The universe used is the same as in Figure 2. Returns are shown gross of transaction costs and fees to show the efficacy of a trend-following signal in these markets. Alternative CTA market Sharpe ratios are shown from 2009. **They do not reflect actual trading results and are not representative of a strategy or investment product.** Hypothetical performance results have many inherent limitations, some of which are described below. No representation is being made that any account will or is likely to achieve profits or losses similar to those shown. In fact, there are frequently sharp differences between hypothetical performance results and the actual results subsequently achieved by any particular trading program. One of the limitations of hypothetical performance results is that they are generally prepared with the benefit of hindsight. In addition, hypothetical trading does not involve financial risk, and no hypothetical trading record can completely account for the impact of financial risk in actual trading. For example, the ability to withstand losses or to adhere to a particular trading program in spite of trading losses are material points which can also adversely affect actual trading results. There are numerous other factors related to the markets in general or to the implementation of any specific trading program which cannot be fully accounted for in the preparation of hypothetical performance results and all of which can adversely affect actual trading results.

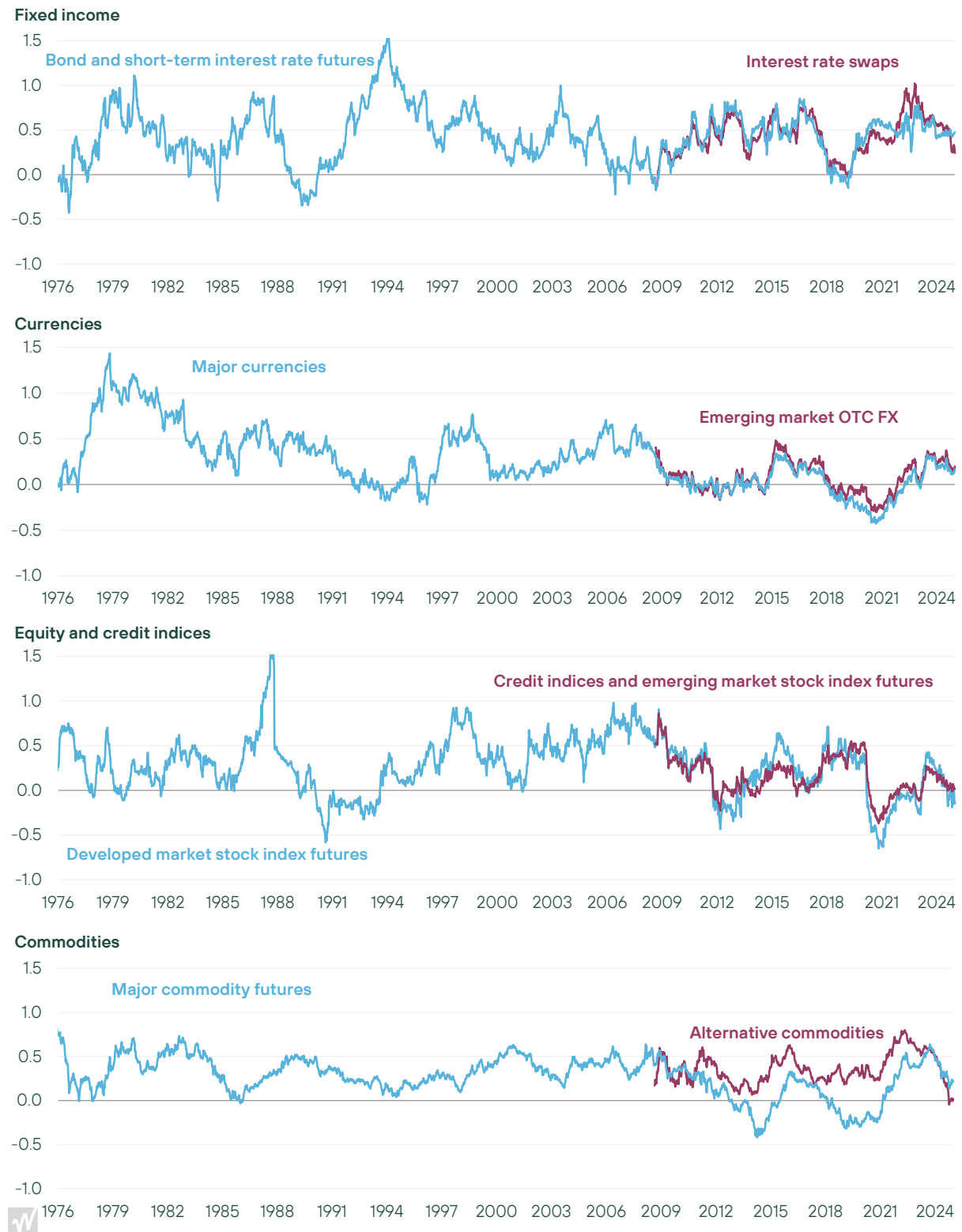
The combination of both greater diversification between markets and more profitable trending behaviour in the underlying markets explains the higher overall Sharpe ratios versus more traditional CTAs in the 2010s. The two previous figures also suggest that a decline in single-market Sharpe ratios has driven the recent weaker returns, rather than a decline in diversification between markets.

Past outperformance has been driven mostly by commodities

Drilling into the historical returns of trend following on alternative markets reveals the variation in historical outperformance across asset classes. In Figure 4, we examine the mean gross Sharpe ratios by sector of a hypothetical trend-following strategy and compare this figure for alternative and traditional CTA markets.

These plots suggest that much of the alternative market CTA outperformance in the 2010s was driven by commodities. In contrast, performance has been broadly similar between alternative and traditional CTA markets in fixed income, currencies and equity/credit indices, albeit with some short-term variation. And while the recent weakening in performance was spread across the asset classes, commodities are showing the largest average Sharpe ratio decline.

Figure 4: Rolling hypothetical three-year gross mean Sharpe ratio by asset class/instrument type



Source: Winton, Bloomberg, as at 31 December 2024. Slow trend-following strategy simulated on a universe of alternative and major markets. Returns are shown gross of transaction costs and fees to show the efficacy of a trend-following signal in these markets. The above results are based on a hypothetical trend-following strategy shown for research purposes only. **They do not reflect actual trading results and are not representative of a strategy or investment product.** Hypothetical performance results have many inherent limitations, some of which are described below. No representation is being made that any account will or is likely to achieve profits or losses similar to those shown. In fact, there are frequently sharp differences between hypothetical performance results and the actual results subsequently achieved by any particular trading program. One of the limitations of hypothetical performance results is that they are generally prepared with the benefit of hindsight. In addition, hypothetical trading does not involve financial risk, and no hypothetical trading record can completely account for the impact of financial risk in actual trading. For example, the ability to withstand losses or to adhere to a particular trading program in spite of trading losses are material points which can also adversely affect actual trading results. There are numerous other factors related to the markets in general or to the implementation of any specific trading program which cannot be fully accounted for in the preparation of hypothetical performance results and all of which can adversely affect actual trading results.

Perhaps the biggest takeaway from Figure 4 is how *unexceptional* the average performance of trend following on alternative markets looks when compared to traditional CTA markets over the long term. Even the strong performance of trend following in alternative commodities over the past decade is consistent with the levels of performance seen in the major commodity futures prior to the 2008 global financial crisis, as well as major fixed income markets for most of the recent period.

Towards diversification

The concentration of the strong past performance in commodities, combined with the increased participation of CTAs in these markets, makes us sceptical that alternative market CTAs will continue to outperform the wider CTA industry to the extent that they have in the past. Although it is too early to see the full effects of larger assets under management in alternative markets CTAs, the recent weakening of performance is supportive of our view.

This is not to say that investors or CTA managers should abandon alternative markets altogether. We believe that these markets have a lot to offer industry-leading diversified CTAs and well-constructed portfolios of CTAs because of the valuable diversification they provide to traditional CTA markets. The focus should instead shift to how this exposure is achieved and how it can be combined more efficiently with traditional CTA exposures and diversifying signals.

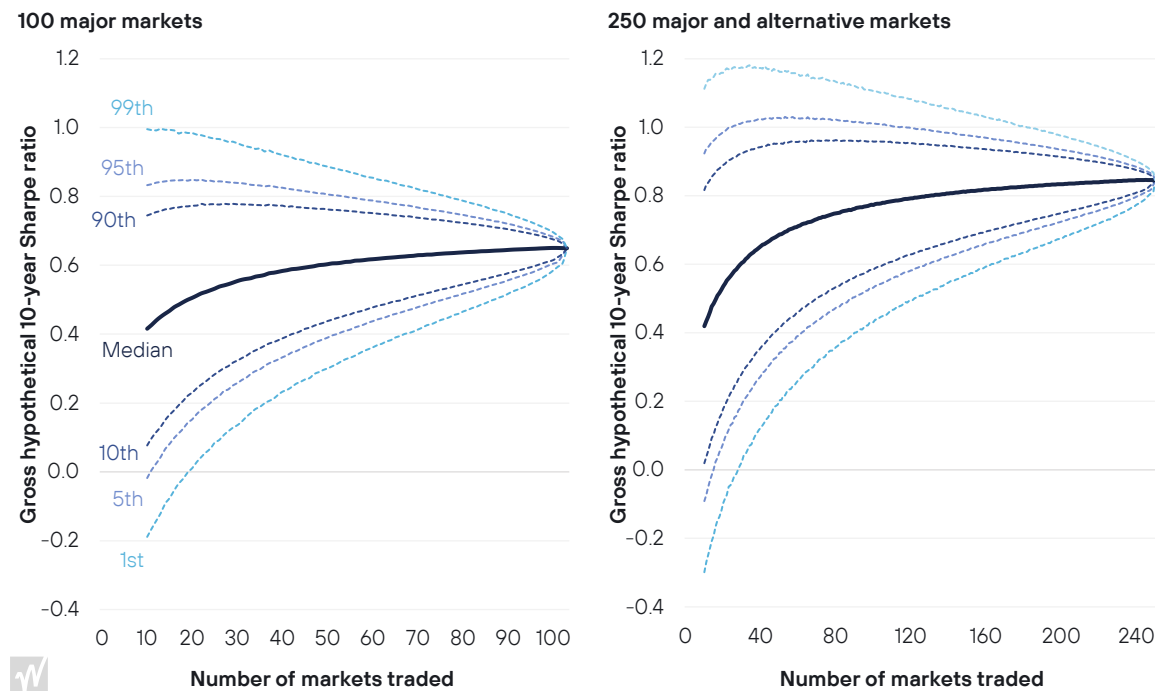
Over time, trend-following strategies have performed well and added resilience to investor portfolios, especially in years like 2008 and 2022. But there is no way of knowing in advance when and in which markets trends will appear in the future. Trend-following strategies therefore benefit greatly from diversification across sectors – look for example at the extraordinary trend in cocoa prices during 2023 and 2024. This argues in favour of adding alternative markets to maximise the benefits of diversification. The more independent markets present in the portfolio, the wider opportunity set of future trends there are to profit from.

The analysis in Figure 5 illustrates this point. We show the range of 10-year Sharpe ratios through to the 31 December 2024 (y-axis) from trend following on different sizes of trading universe (x-axis) starting at a 10-market portfolio. To visualise the range of outcomes observed over this 10-year period, we select at random up to 100,000 combinations of markets for each size of trading universe.

In the left plot, we constrain ourselves to selecting universes from the 100 major futures and currencies that have been traded widely by CTAs for decades. In the right plot, we look beyond the traditional 100 CTA markets and include another 150 alternative markets. These alternative markets have been selected carefully to ensure that they are diversifying for traditional CTA markets.

Importantly, we have penalised the simulated trend-following performance on the alternative markets so that the average Sharpe ratio is close to that achieved by the traditional CTA markets over the past decade. Even after this adjustment, the right chart shows how the improved diversification from the additional markets shifts the range of 10-year Sharpe ratios higher.

Figure 5: Range of Sharpe ratios for a number of markets traded over the past 10 years



Source: Winton, as at 31 December 2024. Returns are shown gross of transaction costs and fees to show the efficacy of a trend-following signal in these markets. The above results are based on a hypothetical slow trend-following strategy shown for research purposes only. **They do not reflect actual trading results and are not representative of a strategy or investment product.** Hypothetical performance results have many inherent limitations, some of which are described below. No representation is being made that any account will or is likely to achieve profits or losses similar to those shown. In fact, there are frequently sharp differences between hypothetical performance results and the actual results subsequently achieved by any particular trading program. One of the limitations of hypothetical performance results is that they are generally prepared with the benefit of hindsight. In addition, hypothetical trading does not involve financial risk, and no hypothetical trading record can completely account for the impact of financial risk in actual trading. For example, the ability to withstand losses or to adhere to a particular trading program in spite of trading losses are material points which can also adversely affect actual trading results. There are numerous other factors related to the markets in general or to the implementation of any specific trading program which cannot be fully accounted for in the preparation of hypothetical performance results and all of which can adversely affect actual trading results.

Of course, Figure 5 also shows how outperformance is possible by picking the right subset of markets, but this is not, in our view, a source of persistent alpha given the unpredictability of trend following performance in any individual instrument type, asset class or market. Instead, we believe that maximising diversification is a more sustainable way for CTA strategies to deliver to investors the idiosyncratic returns for which they are renowned.

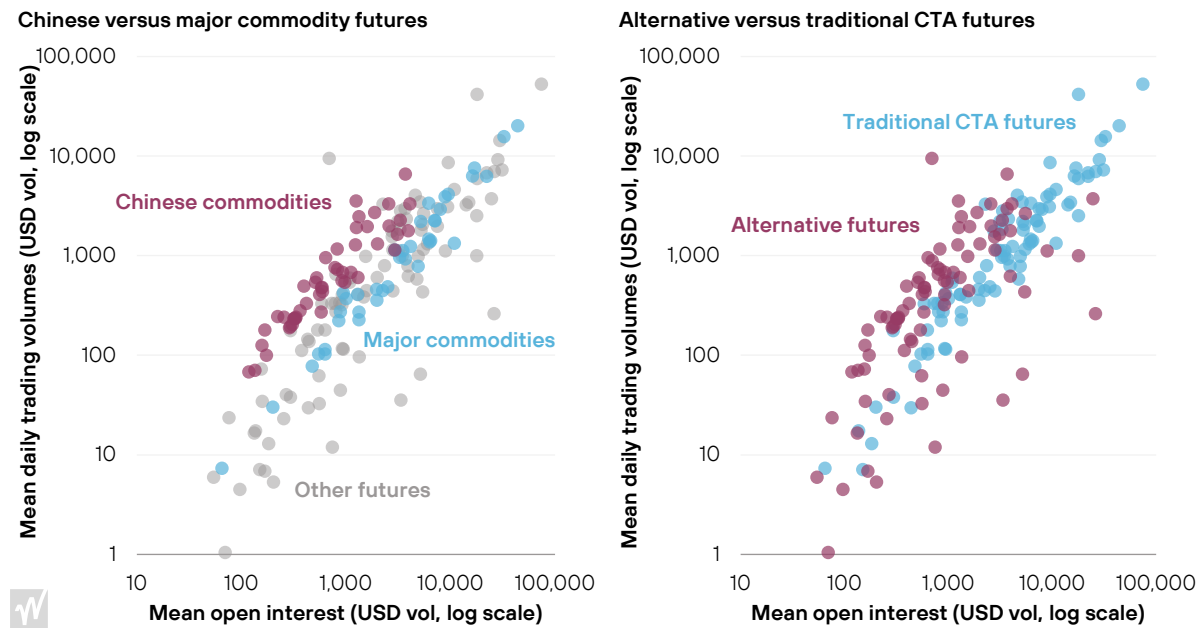
A more complete discussion of the various considerations underpinning the design of a diversified CTA strategy – including the markets traded – can be found in our [Selecting a trend-following CTA](#) white paper.

Appendix: A note on alternative market liquidity

A common misconception is that alternative markets are necessarily “illiquid”. This is normally given as a reason by CTA managers for not investing in the infrastructure needed to trade these markets.

As in major futures markets, there is a spectrum of liquidity in alternative markets. Chinese commodity futures, for example, have comparable liquidity to the world’s major commodity futures, while smaller traditional CTA futures, such as rough rice, orange juice and New Zealand bills, are similar in size to the smaller, usually newer futures in alternative market trading universes.

Figure 6: Futures market liquidity comparisons



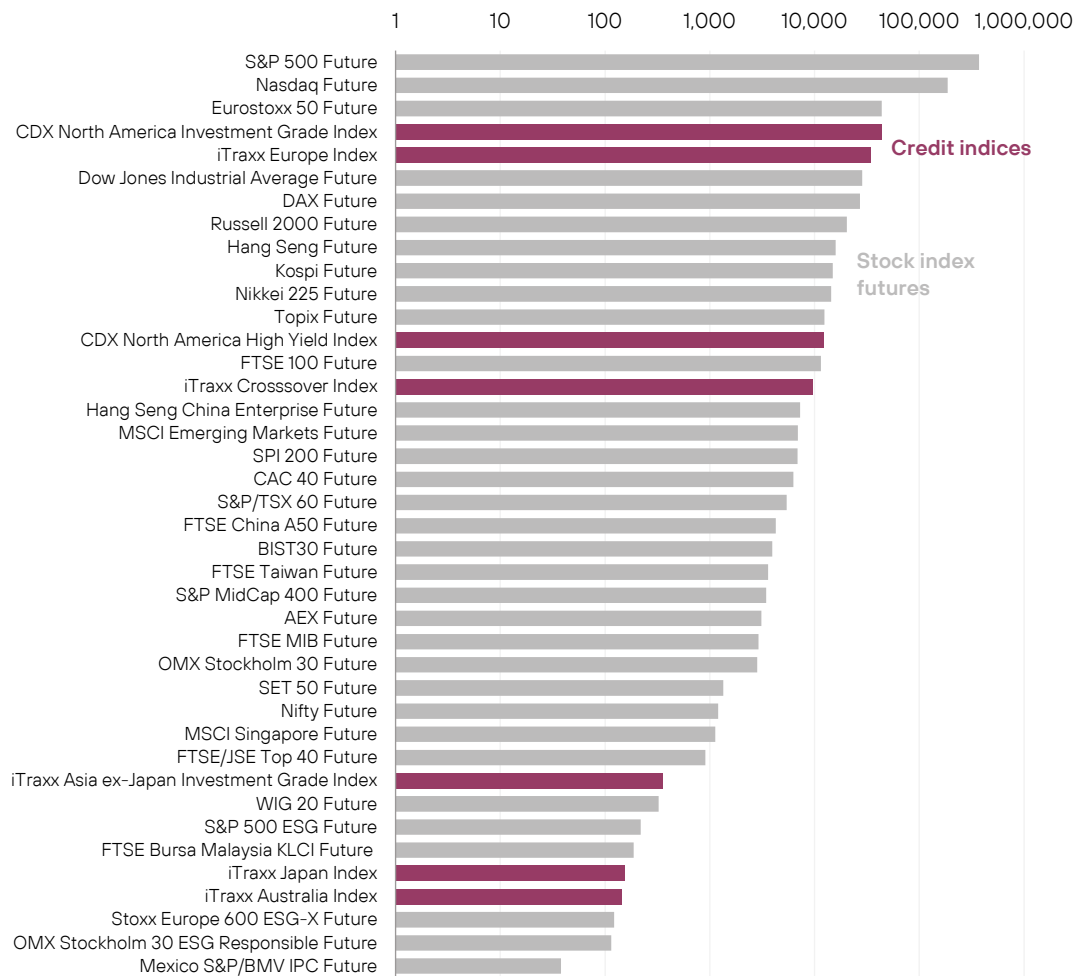
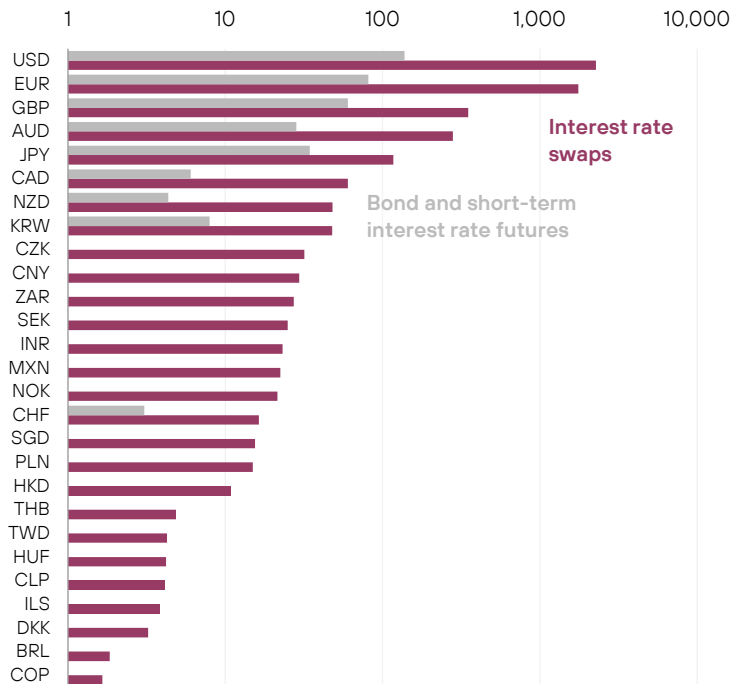
In addition, liquidity is often present in markets, but not visible on an exchange. OTC trading volumes for interest rate swaps and credit indices, for example, are comparable to the on-exchange volumes for interest rate and stock index futures (see Figure 7). For these markets – and for the futures where a large proportion of trading is OTC, such as European power – access to liquidity requires a panel of executing brokers, often including specialists in particular sectors.

While alternative markets sit on a spectrum of liquidity, it is the case that in *aggregate* liquidity is worse than in major markets. This is particularly true when accounting for the correlation properties of the markets: diversification favours a large allocation to the alternative commodities, but this is where the liquidity constraints are felt first. As a result, liquidity begins to have an impact when assets under management starts to drive decisions around the composition of the strategy.

For example, one way to increase the capacity of an alternative market CTA is to tilt the portfolio towards the larger, more-liquid markets, such as interest rate swaps and credit indices. Another is to include markets that are correlated with traditional CTA markets, such as developed market interest rate swaps with bond future equivalents or equity sectors.

Instead, managers of alternative market CTAs should constrain assets under management to ensure sizeable exposure to the more capacity-constrained commodity markets. These are the markets that are most complementary to both traditional CTA markets and the financial assets that dominate investors' portfolios.

Figure 7: OTC and exchange-traded market liquidity comparisons

Index futures and credit indices: 2023 mean daily trading volumes (USD millions, log scale)**Interest rate futures and swaps: 2022 mean daily trading volumes (USD billions, log scale)**

Source: Winton, Bloomberg, S&P Global 2023 Fixed Income Index Products Annual Report Credit Overview, BIS Triennial Central Bank Survey. Data as at year specified.

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