Managed Futures is an alternative investment strategy that seeks to take advantage of price trends in global asset classes – an approach referred to as trend following. What makes the strategy unique is its potential to perform in both rising and falling markets. As part of a long-term strategic asset allocation, we believe that Managed Futures can offer investors:

- **A Diversifying Source of Returns**
- **Opportunity to Perform in Bull and Bear Markets**
- **Potential to Manage Downside Risk**

Please read important disclosures at the end of this paper.
What is Managed Futures?

Managed Futures involves trading futures contracts — agreements to buy or sell a particular asset in the future at a price set in advance. The assets could be equity indices, fixed income, currencies or commodities, all of which are traded on liquid markets around the world. Investors who pursue Managed Futures generally buy (“go long”) assets that have been rising in price and sell (“go short”) assets that have been falling in price, betting that these trends will continue.

This approach, also referred to as trend following, is not new. Hedge funds and Commodity Trading Advisors (CTAs)¹ have been pursuing trends in futures markets since the 1970s.

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¹ A commodity trading advisor (CTA) is an individual or firm who provides individualized advice regarding the buying and selling of futures contracts, options on futures or certain foreign exchange contracts. The CTA registration is required by the National Futures Association, the self-regulatory organization for the industry.

Source: AQR. Past performance is not a guarantee of future performance.
Why Does Managed Futures Work?

Managed Futures seeks to capitalize on price trends, or the tendency of markets to move in the same direction (either up or down) for a sustained period of time. There are a number of theories as to why this happens but studies in behavioral finance suggest that certain biases may explain the start and continuation of trends. Here are some examples:

**Start of Trend**

*Anchoring:* Investors focus too heavily on historical data and underreact to new information, causing prices to move more slowly towards fair value.

*Disposition Effect:* Investors may sell winners too early in an attempt to realize gains, or may hold onto losers too long in an attempt to avoid losses.

**Continuation of Trend**

*Herding:* After prices have trended for a while, some investors jump on the bandwagon, prolonging trends and potentially pushing prices past the point of fair value.

*Confirmation Bias:* Investors tend to look for information that confirms what they already believe and view recent price moves as representative of the future.
The cycle of investor under- and overreaction, depicted below, is what sustains price trends in markets and creates an opportunity for investors who spot them early. Ultimately, trends come to an end as prices tend not to deviate from fair value indefinitely.

**Lifecycle of a Trend**

![Diagram of Lifecycle of a Trend]

Source: AQR. The chart above is an illustration and not representative of an actual investment.

Managed Futures relies on a systematic, rules-based process to identify trends as they develop. In doing so, the strategy eliminates human emotion from the decision-making process of when to buy and sell.

**Having the flexibility to hold long and short positions enables Managed Futures to potentially benefit from both positive and negative price trends.**
When Does Managed Futures Work?

Because the strategy relies on the presence of sustained price trends in markets, Managed Futures has historically performed best when markets go from good to great or bad to worse. Below are two examples of favorable environments for Managed Futures; periods marked by steadily rising or falling prices.

**Good-to-Great**

**Commodity Markets mid-2000s**

October 1, 2006 – May 31, 2008

**Bad-to-Worse**

**Global Financial Crisis**


![Graph of Bloomberg Commodity Index](image1)

![Graph of S&P 500](image2)

Source: Bloomberg. For illustrative purposes only. *Past performance is not indicative of future results.*

When Does Managed Futures Struggle?

Conversely, in choppy or range-bound markets, or during trend reversals, Managed Futures tends to struggle. Over the long term, however, Managed Futures has a proven track record of delivering positive returns. What makes it potentially valuable to investors is its tendency to perform well when other asset classes are struggling.
Benefits of Investing in Managed Futures

A Diversifying Source of Returns

Many investors’ portfolios have traditionally relied on two sources of returns: stocks and bonds. Alternative strategies, such as Managed Futures, provide investors an additional opportunity for positive returns that may come at a time when traditional assets, such as stocks and bonds, are struggling. Adding diversifying sources of returns may help to reduce a portfolio’s overall volatility as well as improve returns.

In the chart below, we show the returns of a 60% stock/40% bond portfolio versus the SG Trend Index, which tracks the performance (net of fees) of the ten largest managers of trend-following strategies. While the cumulative returns are similar, what is important to note are the highlighted periods which demonstrate the strategy’s historical ability to perform well when stocks and bonds have struggled.

Managed Futures Has Delivered Attractive Historical Returns
January 1, 2000 – June 30, 2017

Source: Morningstar, Societe Generale. 60/40 Portfolio is 60% S&P 500 Index and 40% Barclays Aggregate Bond Index, rebalanced monthly. Note: Individual managers in SG Trend Index may have significantly higher or lower levels of volatility and/or returns. Past performance is not indicative of future results.
Opportunity to Perform in Bull and Bear Markets

Another compelling attribute of Managed Futures is its tendency to do well in both strong (“bull”) and weak (“bear”) markets. This is largely explained by the fact that most extreme down or up markets have not happened overnight, but are the result of continued deterioration or improvement in economic conditions.

In prolonged down markets, Managed Futures tends to position itself “short” — that is, the strategy sells assets — as markets begin to decline and seeks to profit if markets continue to fall. Similarly, in sustained up markets, Managed Futures tends to position itself “long” — the strategy buys assets — and aims to profit if the rise continues.

When the returns of Managed Futures are compared to the returns of the global stock market below, the strategy has performed best during extremely strong or weak markets.

Managed Futures Has Historically Performed Well in Bull and Bear Markets
January 1, 2000 – June 30, 2017

Source: AQR, Bloomberg, Societe Generale. Note: Individual managers in SG Trend Index may have significantly higher or lower levels of returns. “Bear Markets” represents the worst 30% of the MSCI World Index’s quarterly returns, “Bull Markets” represents the best 30% of quarterly returns, and “Normal Markets” represents the middle 40% of quarterly returns. Past performance is not indicative of future results.
The global financial crisis represents a classic example of how Managed Futures may perform in troubled markets. Going into the fourth quarter of 2008, equity and energy prices had been declining; government bond prices had been rising. This led to Managed Futures being positioned short equities, short energy commodities, and long government bonds. These positions profited as the same trends continued throughout the quarter, while the stock market and other strategies suffered.

Managed Futures Provided Protection During the Global Financial Crisis
October 1, 2008 – December 31, 2008

On average, Managed Futures has helped when investors needed it the most, during those very difficult equity bear markets.
Managed Futures in a Portfolio

Investors seek alternative investments — that is, alternatives to buying and holding traditional assets like stocks and bonds — in order to increase the expected return of their portfolios while improving diversification and reducing the magnitude of losses if global markets suffer. We believe Managed Futures can meet all of these criteria.

Given the strategy’s propensity to be diversifying to traditional assets, Managed Futures should be viewed as a valuable component of a long-term strategic asset allocation. Over time, the strategy may help to improve returns, reduce risk and mitigate the likelihood of large losses for the overall portfolio.

Like any investment strategy, Managed Futures can go through challenging periods of performance. We believe that investors who develop a clear understanding of how the strategy works and the role it’s designed to play in a portfolio will be better positioned to stay invested over the long term and reap the potential diversification benefits when they need it the most.

Source: AQR. Past performance is not a guarantee of future performance.
About AQR

AQR is a global investment management firm built at the intersection of financial theory and practical application. Since 1998, AQR has implemented a systematic, research-driven approach to managing traditional and alternative strategies for some of the world’s largest institutional investors. In 2009, AQR began offering its innovative, risk-managed strategies to mutual fund investors in order to provide them with investment solutions that can improve portfolio diversification.

AQR’s senior management team has been working together and managing alternative investment strategies, including Managed Futures, since the mid-1990s. What distinguishes AQR’s approach to managed-futures investing is our emphasis on diversification across asset classes and trend signals, as well as our focus on risk management and efficient trading execution.

Disclosures: Foreign investing involves special risks such as currency fluctuations and political uncertainty. The use of derivatives, forward and futures contracts, and commodities exposes the Fund to additional risks including increased volatility, lack of liquidity, and possible losses greater than the Fund’s initial investment as well as increased transaction costs. This fund enters into a short sale by selling a security it has borrowed. If the market price of a security increases after the Fund borrows the security, the Fund will suffer a potentially unlimited loss when it replaces the borrowed security at the higher price. Short sales also involve transaction and other costs that will reduce potential Fund gains and increase potential Fund losses. When investing in bonds, yield and share price will vary with changes in interest rates and market conditions. Investors should note that if interest rates rise significantly from current levels, bond total returns will decline and may even turn negative in the short term. There is also a chance that some of the fund’s holdings may have their credit rating downgraded or may default.

This Fund is not suitable for all investors. An investor considering the Funds should be able to tolerate potentially wide price fluctuations. The Funds may attempt to increase its income or total return through the use of securities lending, and they may be subject to the possibility of additional loss as a result of this investment technique. Risk allocation and attribution are based on estimated data, and may be subject to change. Diversification does not eliminate the risk of losses.

Barclay Aggregate Bond Index: a broad-based benchmark that measures the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market.

Bloomberg Commodity Index: a broadly diversified commodity price index distributed by Bloomberg Indexes. It tracks 22 commodity futures contracts across seven sectors.

MSCI World Index: a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets.

S&P 500 Index: a free-float market capitalization-weighted index of 500 of the largest U.S. companies. The index is calculated on a total return basis with dividends reinvested.

SG Trend Index: an index designed to track the 10 largest (by AUM) trend-following CTAs and to be representative of trend-followers in the managed futures space.

One cannot invest directly in an index.

Investors should carefully consider the investment objectives, risks, charges and expenses of the Funds before investing. To obtain a prospectus containing this and other important information, please call 1-866-290-2688 or visit www.aqrfunds.com to view or download a prospectus online. Read the prospectus carefully before you invest. There are risks involved with investing including the possible loss of principal. Past performance does not guarantee future results. AQR Funds are distributed by ALPS Distributors, Inc. AQR005822 09/30/2018