

Nominees for Alternatives Fund Manager of the Year

A brand-new award for some experienced alternative mutual fund managers.

Fund Spy | 12-18-12 | By Nadia Papagiannis, CFA

This year, for the very first time, we are nominating three managers for our new Morningstar Alternatives Fund Manager of the Year award. Morningstar began distributing Fund Manager of the Year awards in 1987, first to a single stock or bond manager, and then, starting in 1995, across the domestic-stock, international-stock, and fixed-income categories. Selecting Fund Manager of the Year nominees is a year-long process, and we seldom nominate managers operating in narrow segments of the market (sector funds, for example).

So, it's notable that, 25 years later, our Fund Manager of the Year awards are considering a broader range of managers who don't fit any standard investment bucket. Morningstar defines alternative investments as those that do not fit neatly in our traditional equity or fixed-income style boxes—either because they invest in different asset classes, take long and short positions, or because they are illiquid. Just a few years ago, one could gain access to alternative investments only via private vehicles with high minimum investments and strict redemption terms. Now these same strategies, such as long-short equity, market-neutral/arbitrage, or managed futures, are widely available in exchange-traded funds and mutual funds, with low minimum investments and daily liquidity.

There are currently 361 alternative mutual funds (as of Dec. 17) across several different categories. Almost 60% of these funds launched post-2008, and the total assets in all 361 alternative funds constitute less than 2% of the entire fund universe. Nevertheless, these investments are increasing in importance as advisors look to them to reduce and diversify the risk in their traditional stock and bond portfolios. (See our annual Morningstar Barron's survey.)

What our new Fund Manager of the Year award means, then, is that alternative investments, particularly those in liquid vehicles such as mutual funds and ETFs, are here to stay. Here are three alternative mutual fund management teams we'd like to recognize as the cream of the crop for 2012.

Michael Aronstein From MainStay Marketfield (MFLDX) Year-To-Date Return through Dec. 16: 11.6%

Manager Michael Aronstein—who served as manager of global investment strategy for Merrill Lynch in the 1980s, president of Comstock Partners (an RIA) in the late 1990s, and chief investment strategist for Oscar Gruss & Son in the 2000s—launched this macroeconomic-themed long-short equity mutual fund in 2007. The fund has earned a 5-star Morningstar Rating over the past three and five years, as well as a Bronze Morningstar Analyst Rating. (Morningstar launched qualitative analyst ratings on 40 alternative mutual funds in June 2012, and 40 more will debut in early 2013, covering 85% of alternative mutual fund assets).

Unlike most funds in the long-short category, this fund weathered the entire 2007-09 financial crisis (only 29 of the category's 83 funds were around prior to 2008). From early 2007 through early March 2009, the fund lost 22.8%, relative to the S&P 500's 50% dive, by shorting financial and emerging-markets stocks early on. Then Aronstein invested in cyclical stocks and shorted long-dated Treasury ETFs in 2009 and 2010, benefiting from the stock market's recovery. More recently, in 2012, Aronstein made money for investors in the second quarter by shorting emerging-markets stocks (iShares JPMorgan USD Emerging Markets Bond (EMB) and Baidu Inc. (BIDU), for example). Through Dec. 16, the fund has outperformed the S&P 500 on a risk-adjusted basis (using annualized daily Sharpe ratio) and ranks 11 and 14 out of 83 funds in the category in terms of absolute (11.6%) and risk-adjusted returns, respectively. The fund's success has attracted significant assets, and it is now the second-largest fund in the long-short category (\$3.8 billion as of Nov. 30).

Effective October 2012, the fund was adopted by MainStay Investments, which is now the advisor to the fund. Since then, the fees have gone up for this once no-load, no 12b-1 fee fund. Aronstein and Marketfield remain the subadvisor, however, so its prospects still look good.

**Team From Calamos Market Neutral Income (CVSIX)
Year-To-Date Return through Dec. 16: 5.6%**

This year we are nominating two funds from the market-neutral category. Both are team-managed, and both are closed to investors, but that's where the similarities end. Calamos Market Neutral Income allocates about 50% of its capital to a convertible arbitrage strategy and 50% to a covered call-writing stock strategy that is hedged with index put options. This fund has been around for more than 20 years (although prior to 2006, the strategy included only the convertible arbitrage component), and it boasts a 4-star three-, five-, and 10-year Morningstar Rating. Morningstar's analysts have awarded it a Bronze Morningstar Analyst Rating.

This year marked another fine showing for the fund. Its 5.6% (year to date through Dec. 16) absolute return and its risk-adjusted (Sharpe ratio) return rank near the top of 31 funds in the category, respectively. Convertible bonds and stocks both fared well this year, giving this fund a boost as it takes on a little more market risk than many of its peers (its three-year monthly beta to the S&P 500 through November was 0.42). Assessing its risk-adjusted performance relative to a market benchmark is a little more difficult. Using a 50/50 benchmark of the Bank of America/Merrill Lynch All Convertibles All Qualities Index and the CBOE S&P 500 Buy Write BXM Index (rebalanced quarterly), this fund has generated a positive alpha of 2.6% this year.

What drives performance in Calamos Market Neutral Income is the same as what drives performance across Calamos' suite of convertible-bond funds--a deep research bench and decades of experience. Managers John Calamos Sr., John Calamos Jr., John Hillenbrand, Steve Klouda, Jeff Scudieri, Jon Vacko, Christopher Hartman, Joe Wysocki, and Gary Black run this fund in particular (with Hartman handling many of the day-to-day duties), and most of the managers have been at the helm for at least nine years. The intermediate research analysts average 11 years of experience, and many started as junior analysts at the firm. Black, the co-CIO, is the newest addition, having replaced Nick Calamos in August 2012.

**Team From TFS Market Neutral (TFSMX)
Year-To-Date Return through Dec. 16: 6.5%**

This fund is currently the only alternative mutual fund receiving a Morningstar Analyst Rating of Gold. It's also one of the oldest in the market-neutral category, sporting an eight-year track record. The fund follows a quantitative small-capitalization equity arbitrage strategy, in a \$1 long/\$0.66 short ratio, looking for mispricings in three broad

areas: fundamental data (earnings surprises, for example), "follow the smart money" (insider buying, for example), and order imbalances (overbought or oversold stocks, for example).

Although TFS Market Neutral takes on slightly more market risk than some of its strict market-neutral peers (Morningstar defines market-neutral, equity market-neutral, and arbitrage strategies as those whose stock market beta ranges between negative 0.3 and 0.3, and this fund's three-year monthly beta to the Russell 2000 through November was 0.23), it has consistently beaten its category on a risk-adjusted basis, and it has consistently produced alpha above its exposure to small-capitalization stocks). The year 2012 was no exception. Through Dec. 16, the fund has exhibited the category's highest absolute return (6.5%) and one of its highest Sharpe ratios, as well as a significant positive alpha to the Russell 2000. The fund's long-term risk-adjusted performance is also admirable, earning a 5-star Morningstar Rating over the past three- and five-year periods.

Beyond the fund's performance, there's a lot to like about this fund's management team of Eric Newman, Richard and Kevin Gates, Larry Eiben, Chao Chen, and Yan Liu. Five of six portfolio managers are equity partners at their 100% employee-owned firm, TFS Capital, whose code of ethics requires management to invest 50% of their liquid net worth in TFS mutual funds. Consequently, the management ownership levels are some of the highest among mutual fund managers. The team has experienced no turnover since the fund's debut and has added resources as assets have grown. The team is also sensitive to capacity, and the fund (now at \$1.86 billion) has been closed to new and most existing investors since June 2011. Although we'd like to nominate alternative funds that are open to new investors for the Fund Manager of the Year award, this fund is too good to not mention.

Nadia Papagiannis is the Director of Alternative Fund Research at Morningstar.

The following information is provided by Calamos Investments:

Information contained herein is for informational purposes only. Nothing presented herein is or is intended to constitute investment advice, and no investment decision should be made based on any information provided herein. The information contained herein, while not guaranteed as to the accuracy or completeness, has been obtained from sources we believe to be reliable. The opinions referenced are as of the date of publication and are subject to change due to changes in the market or economic conditions and may not necessarily come to pass.

Calamos Market Neutral Income Fund CVSIX (Class A Shares) as of 11/30/2012

Number of Holdings: 384 **Total Net Assets:** \$2.5 billion **Beta** (since inception 9/4/90 vs. S&P 500 Index): 0.25 **Portfolio Turnover (12 Months):** 76.21% **Sharpe Ratio** (since inception 9/4/90): 0.72 **Alpha (10 Year):** 2.63% **Strategy Allocation** (% of Portfolio): Covered Call, 44.8%; Convertible Arbitrage, 55.2%

Morningstar Ratings: The fund's Class A shares received 4 stars for 3 years, 4 stars for 5 years and 4 stars for 10 years out of 60, 48 and 22 Market Neutral funds, respectively, for the period ended 11/30/12 **Morningstar Category Rankings:** The fund's Class A shares ranked 5 for 1 year, 4 for 3 years, 11 for 5 years and 15 for 10 years out of 112, 60, 48 and 22 Market Neutral funds, respectively for the periods ended 11/30/12

Average Annual Total Returns	1-Year	3-Year	5-Year	10-Year	15-Year	20-Year	Since Inception	Gross Expense Ratio	Net Expense Ratio
Market Neutral Income Fund (Inception 9/4/90) A share Returns at NAV	6.18%	4.76%	2.38%	3.81%	5.84%	6.34%	6.95%	1.22%	1.22%
Market Neutral Income Fund (Inception 9/4/90) A share Load-Adjusted Returns	1.16%	3.09%	1.38%	3.31%	5.49%	6.08%	6.72%	1.22%	1.22%

Performance data quoted represents past performance, which is no guarantee of future results. Investment return and principal value will fluctuate so that shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance quoted. Load-adjusted returns take into account the Fund's maximum 4.75% front-end sales load. For performance current to the most recent month end, visit www.calamos.com.

Important Risk Information: An investment in the Fund(s) is subject to risks, and you could lose money on your investment in the Fund(s). There can be no assurance that the Fund will achieve its investment objective. Your investment in the Fund is not a deposit in a bank and is not insured or guaranteed by the Federal Deposit Insurance Corporation (FDIC) or any other government agency. The risks associated with an investment in the Fund can increase during times of significant market volatility. The Fund also has specific principal risks, which are described below. More detailed information regarding these risks can be found in the Fund's prospectus.

The principal risks of investing in the Market Neutral Income Fund include: convertible securities risk, synthetic convertible instruments risk, convertible hedging risk, covered call writing risk, options risk, short sale risk, interest rate risk, credit risk, high yield risk, liquidity risk and portfolio selection risk.

As a result of political or economic instability in foreign countries, there can be special risks associated with investing in foreign securities, including fluctuations in currency exchange rates, increased price volatility and difficulty obtaining information. In addition, emerging markets may present additional risk due to potential for greater economic and political instability in less developed countries.

Before investing, carefully consider the Fund's investment objective, risks, charges and expenses. Contact 800.582.6959 for a prospectus containing this and other information. Read it carefully.

CALAMOS®

Calamos Financial Services LLC, Distributor | 2020 Calamos Court | Naperville, IL 60563-2787 | 800.582.6959 | calamos.com | © 2012 Calamos Investments LLC. All Rights Reserved. Calamos® and Calamos Investments® are registered trademarks of Calamos Investments LLC. 1651 12120 R