

# BEST ALTERNATIVE INVESTMENT HOUSE

## DE Shaw

### The brightest people have helped DE Shaw generate the best returns

It is easy to be in awe of highly secretive alternatives house DE Shaw & Co. The firm might not be the first to use complex mathematics and computer programmes to exploit inefficiencies – so called systematic statistical arbitrage – but it has certainly been one of the most successful. And its success is a result of its people. “It’s a firm of rocket scientists,” says one industry consultant.

Its results have been equally impressive, with consistent double-digit returns and funds under management that have more than doubled in the past 18 months.

Its founder, David Shaw, insists on employing only the most “extraordinary” individuals.

Shaw himself has an exceptional employment history. He served as chairman of the panel on educational technology for president Bill Clinton, and is also the treasurer of the American Association for the Advancement of Science. At present he spends much of his time involved in the firm’s technology ventures business.

A staff of 20 is responsible for recruitment alone, whittling down the average of 500 applications for each post. A background in finance is not essential; the firm’s motto is: “It’s easier to teach smart people to do finance than to teach financial people to be smart.”

Among DE Shaw’s 500 staff are 50 PhDs, as well as recipients of the Putnam Award

and Maths Olympiad gold medals. Perhaps the best-known employee to make it through the rigorous selection process was Jeff Bezos, who left to start Amazon.com.

But if thoughts of number-crunching tech-geeks spring to mind, think again. DE Shaw focuses on nurturing creativity. Its offices are headquartered in Manhattan, and were designed by US architect Steven Holl.

Black vinyl, frosted glass, ambient lighting and geometric art more in keeping with a media company adorn the walls and floors, while dress code is strictly “wear what makes you comfortable”.

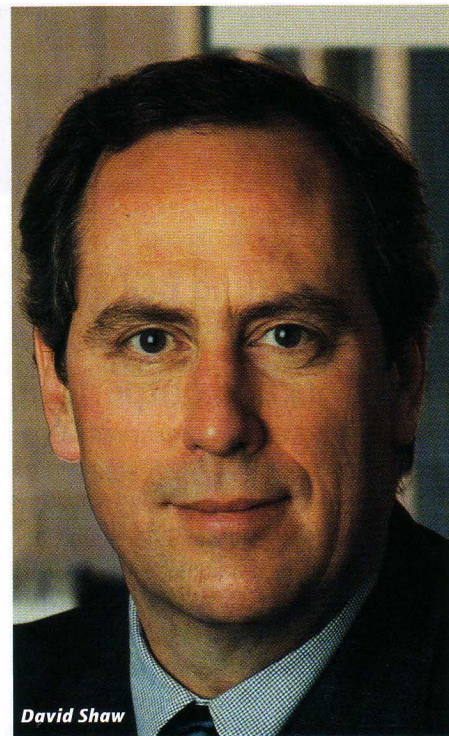
It’s a concept that seems to work. Since the beginning of 2004, DE Shaw’s assets have rocketed from \$6.7 billion to \$15.9 billion. And returns are impressive.

DE Shaw started life in 1988 in high-tech equity and equity derivative trading, using its quantitative methods to pursue absolute-return strategies. Over the 16 years that the firm has been trading in that area, it has never had a losing 12-month period.

But diversification was soon on the agenda. After just a few months, DE Shaw started trading in Japanese warrants, becoming a major market-maker in the security during the go-go period of the late 1980s and early 1990s – a business it sold to KBC in 2000/01.

The firm now has 15 strategies spanning foreign currencies, fixed income, convertible arbitrage, long/short and macro. Last year a blend of its strategies net of fees returned 17.5%, and so far this year, the return is 8.4%.

Its ability to produce positive returns when the rest of the world is struggling has made DE Shaw the envy of its peers. The firm started limiting its exposure to convertible bond arbitrage as early as two years ago – fortuitously, the strategy has performed poorly for many months. In addition, its macrostrategies are up 16% this year – a considerable outperformance of Hennessey Group’s macro index, which has returned 2.3% year to date. And in futures



David Shaw

and currencies, DE Shaw is up around 9% this year.

Says one analyst: “Some of the brightest minds on Wall Street work there. There’s nothing negative to say about them. The performance speaks for itself.”

DE Shaw ploughs its staff and money into developing and improving its automated trading systems, and the firm is now looking to leverage its quantitative techniques in absolute return strategies to relative return long-only products in the institutional asset management space. It has recently begun marketing its enhanced index product with a five-year track record using the same techniques as it does for its market-neutral equity strategies, with the aim of outperforming a given benchmark of between 1% and 3% a year.

In terms of business lines, DE Shaw is also expanding. It has a group in Houston, for example, that originates loan in competition with commercial banks.

The firm has also been branching out into strategies that require qualitative analysis, such as distressed securities and energies. ■