Aaro Capital

Aaro Crypto Fund Indices ("ACFI")

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Aaro Capital

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1 Summary

Aaro Capital was established in 2018 with the aim of being the first institutional quality investment specialist focused on Distributed Ledger Technology (DLT) and cryptoassets. Aaro opens up the exciting and rapidly evolving DLT and cryptoasset growth story for sophisticated investors.

Given the rapid growth of DLT and cryptoassets, investors are now looking for tools to benchmark their allocations against indices that measure the performance of actively managed funds in this asset class. There is evidence that, on average, active crypto funds outperform the market. There is, however, large dispersion in their quality.

Aaro Capital has launched a comprehensive suite of **Crypto Fund Indices** to meet this growing need. The broadest of these indices covers the full range of DLT and cryptoasset investment strategies available through funds. The four sub-indices cover each of the main investment approaches that are taken. These are based on Aaro Capital's extensive research and knowledge of the widening fund universe.

Aaro Capital has developed, owns, and administers five (5) fund indices:

Index Name	Short Name	Abbreviation
Aaro Crypto Fund Index - Composite (PG)	Aaro Composite Index (PG)	ACFI.C
Aaro Crypto Fund Index - Long Term (PG)	Aaro Long Term Index (PG)	ACFI.L
Aaro Crypto Fund Index - Trading (PG)	Aaro Trading Index (PG)	ACFI.T
Aaro Crypto Fund Index - Non Directional (PG)	Aaro Non Directional Index (PG)	ACFI.N
Aaro Crypto Fund Index - Multistrategy (PG)	Aaro Multistrategy Index (PG)	ACFI.MS

2 Background

The **Aaro Crypto Fund Indices** (**"ACFI"**) are intended for investors seeking a broad representation of fund performance across different DLT and cryptoasset investment strategies.

It is important to note that Aaro has developed its own set of strategy definitions. These are grouped by investment aim, rather than by style or sector. This is to provide investors with a more useful set of groupings, since to do so simply by strategy can bring together funds with widely divergent investment aims. Traditional strategy categories, even those developed for hedge funds, can be difficult to apply to this asset class. It is hoped that this will help to establish fresh standards in this novel space, within which Aaro has found that traditional categorisations are of limited use from an investor perspective.

The Aaro Crypto Fund Indices have also been constructed initially as dynamic peer groups, hence the use of the acronym, **"PG"** (**"Peer Group"**). Like traditional peer groups, they can be used as a guide for expected return characteristics from different investment approaches. Given the fast-changing nature of the DLT and cryptoasset space, the historical values of the indices will change over time as new funds are identified and incorporated in the indices. This ensures the indices remain relevant and reflective of the evolution of the fund universe.

3 Intended Use

3.1 Audience

The primary target audience is institutional and other professional investors who wish to track the development of actively managed DLT and cryptoasset funds, as well as fund managers looking to show their performance against widely recognised benchmarks that are representative of their peers.

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3.2 Availability, Distribution and Use

The Aaro Crypto Fund Indices are updated and distributed monthly. They can be viewed, analysed and downloaded at https://aaro.capital/indices. All are currently non-investable.

Email updates can be sent directly to relevant publications, databases, and professional investors upon request.

The Aaro Crypto Fund Indices can be used freely for internal purposes. They can also be reproduced and distributed if reference is made to Aaro Capital.

4 Index Definitions

4.1 Aaro Crypto Fund Index – Composite (PG)

The Aaro Crypto Fund Index – Composite (PG) provides a broad measure of the performance of over 100 active fund managers that allocate to Distributed Ledger Technology (DLT) and cryptoassets. It is equally weighted and designed to act as a peer group. The index is base weighted at 100 at May 2017 and does not contain duplicate funds. It is denominated in US dollars.

The Aaro Crypto Fund Index – Composite (PG) acts as a composite index and includes all types of strategies. The four sub-indices (i.e. Long Term, Trading, Non Directional, Multistrategy) group the constituents based on their underlying strategies based on investment aim. These sub-indices are designed to provide more granular benchmarks based on different strategies employed by DLT and cryptoasset fund managers.

4.2 Aaro Crypto Fund Index – Long Term (PG)

The Aaro Crypto Fund Index – Long Term (PG) provides a broad measure of the performance of active fund managers that allocate at least 70% of their capital to Long Term strategies focused on Distributed Ledger Technology (DLT) and cryptoassets. This includes buy-and-hold, early-stage, liquid venture, special situations, and yield enhancing approaches. It is equally weighted and designed to act as a peer group. The index is base weighted at 100 at May 2017 and does not contain duplicate funds. It is denominated in US dollars.

4.3 Aaro Crypto Fund Index – Trading (PG)

The Aaro Crypto Fund Index – Trading (PG) provides a broad measure of the performance of active fund managers that allocate at least 70% of their capital to Trading strategies focused on Distributed Ledger Technology (DLT) and cryptoassets. This includes both systematic and discretionary approaches. It is equally weighted and designed to act as a peer group. The index is base weighted at 100 at May 2017 and does not contain duplicate funds. It is denominated in US dollars.

4.4 Aaro Crypto Fund Index – Non Directional (PG)

The Aaro Crypto Fund Index – Non Directional (PG) provides a broad measure of the performance of active fund managers that allocate at least 70% of their capital to Non Directional strategies focused on Distributed Ledger Technology (DLT) and cryptoassets. This includes various forms of arbitrage, as well as yield generation through lending, staking, farming, airdrops and forks. It is equally weighted and designed to act as a peer group. The index is base weighted at 100 at May 2017 and does not contain duplicate funds. It is denominated in US dollars.

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4.5 Aaro Crypto Fund Index – Multistrategy (PG)

The Aaro Crypto Fund Index – Multistrategy (PG) provides a broad measure of the performance of active fund managers that allocate at least 70% of their capital to multiple strategies focused on Distributed Ledger Technology (DLT) and cryptoassets, but not falling within the sole remit of the Long Term, Trading or Non Directional strategy areas. It is equally weighted and designed to act as a peer group. The index is base weighted at 100 at May 2017 and does not contain duplicate funds. It is denominated in US dollars.

5 Strategy Definitions

Aaro Capital conducts research on all funds included in the Aaro Crypto Fund Indices. This is in order to determine the appropriate strategy classification for each fund. Aaro uses proprietary classifications which are based on investment aim, rather than style or sector. As such, they may differ from the strategy classifications used by some fund managers and allocators.

5.1 Long Term

These strategies aim to offer exposure to long term developments in DLT and cryptoasset markets. They are often positioned as most attractive during bull markets, with high returns and high volatility.

Long term strategies include investments in the following:

- **Listed tokens:** These are usually in the form of early-to-mid stage tokens with an investment horizon of 6 to 24 months and reasonable liquidity. Most investments of this type are long-biased. Opportunistic shorts may, however, be in play along with special situations and yield enhancing trades.
- **Unlisted tokens:** These are usually in the form of pre-auction SAFTs (“Simple Agreement for Future Tokens”) that allow for discounts relative to public offerings. These can offer attractive vesting schedules for early investors. They can also offer higher liquidity relative to traditional private equity investments. Unlisted tokens usually experience a realisable event within 3 to 12 months.
- **Listed equities:** These are usually in the form of public market equities that are regarded as likely to benefit from DLT and cryptoasset developments. The holding period for such investments is around 3 – 24 months, although liquidity is usually very high.
- **Unlisted equities:** These are usually in the form of private, more illiquid deals designed to benefit from DLT and cryptoasset developments. The due diligence and allocation considerations involved for such opportunities is similar to those used by venture capital and private equity firms.
- **Other:** This can include network activities. Some managers regard the ability to participate directly in networks as being of great benefit, both in terms of opportunistic special situations trades, as well as being able to extract additional yield from existing investments. Protocol splits, new product launches, staking, masternodes and DeFi activities, amongst others, can offer ample opportunity for Long Term strategies to generate alpha.

5.2 Trading

In combination, Trading strategies aim to offer the long term upside of cryptoasset markets, whilst hedging against short term volatility. They include both systematic and discretionary approaches, with high returns and reduced volatility.

Trading strategies include the following:

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- **High Frequency**: This includes approaches designed to be uncorrelated to cryptoasset market movements, with high turnover and using little to no leverage. Strategies here may employ sophisticated machine learning or neural network models.
- **Mean Reversion:** This involves using quantitative models to identify when a market enters oversold (below mean) or overbought (above mean) territory and trading on a reversion. Holding periods are typically short.
- **Relative Value:** This includes exploiting temporary discrepancies in the prices of correlated assets, with the expectation that they will eventually converge. The more effective approaches in this area still tend to be discretionary, with trading horizons of months rather than days.
- **Trend Following:** This strategy profits from trend and momentum effects in the market through predominantly systematic approaches. The goal is to enter when a new trend is identified and exit before reversion, hence holding periods can be long and market exposure high.
- **Discretionary Trading:** This includes the use of technical, on-chain, sentiment and macro indicators to make discretionary trading decisions on a select number of cryptoassets. Holding periods are typically long. There is some overlap with Long Term approaches, although funds of this type are at the more liquid end of the spectrum.

5.3 Non Directional

These strategies aim to produce a positive return regardless of market direction. They are often positioned as most attractive during bear markets, with low returns and low volatility.

Non Directional strategies include the following:

- **Arbitrage:** Funds of this type aim to exploit temporary price discrepancies by simultaneously purchasing and selling equivalent assets, or the same asset, across multiple markets. Examples include cross exchange arbitrage, futures basis arbitrage, swaps arbitrage, calendar spread arbitrage, volatility arbitrage and structural arbitrage.
- **Yield:** Funds of this type aim to exploit temporary price discrepancies that arise from one-off events, or from activities taking place directly on a distributed ledger. There is some overlap with Long Term yield enhancing approaches, but Non Directional strategies are usually fully hedged. Examples include trading around airdrops, protocol splits, lending, yield farming, staking and mining.

5.4 Multistrategy

These strategies have mixed objectives, with overlap across Long Term, Trading or Non Directional approaches. They are often positioned to perform across multiple market cycles, with high returns and reduced volatility.

Examples of multistrategy approaches include:

- A fund with the mandate to engage in automated arbitrage, lending, relative value trades, puts on highly correlated blockchain equities, momentum trades and unlisted token investments.
- A fund with the mandate to engage in arbitrage, DeFi lending, fundamentally driven special situations trades and short term opportunistic trading.
- A fund with the mandate to engage in lending, trend-following and smart beta trades.

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6 Methodology

6.1 Inclusion Criteria

To be eligible for inclusion in the indices, funds must fulfil the following criteria:

- Allocate at least 70% of their capital to active DLT and cryptoasset investment strategies
- Fall under one of the strategy categories defined by Aaro Capital: Long Term, Trading, Non Directional, Multistrategy
- Have at least $1m in assets under management
- Have a track record of at least 3 months
- Contribute consistent and timely performance
- Report returns as a commingled, single manager fund (i.e. no fund of funds, managed accounts, proprietary trading or back tests)
- Report monthly returns
- Report returns net of all fees, excluding AuM inflows and outflows
- Report returns in US dollars

6.2 Index Construction

The Aaro Crypto Fund Indices aim to provide an accurate representation of fund returns. Therefore:

- When a fund satisfies the criteria for inclusion, its whole track record is added to the index.
- Where a fund has more than one share class, only the highest fee-paying share class is included.
- Funds that shut down or close to new investment are still included to avoid skewing results through survivorship bias.
- Funds that change strategy or exhibit style drift are reclassified, with historical returns grouped under the old strategy category, and future returns grouped under the new strategy category.
- Constituent funds are periodically checked against the criteria for inclusion and for outliers.

6.3 Outliers

Outlier constituents are checked and removed using a combination of statistical analysis and discretion:

- Fund returns are compared against each strategy index's average +/- 3 standard deviations.
- For funds with returns outside of this threshold, discretion is applied to determine whether the under or outperformance is genuine.
- For funds with returns within this threshold, returns are cross checked against findings from internal due diligence to confirm their validity.

6.4 Weighting

The Aaro Crypto Fund Indices are equally weighted and updated monthly. To calculate the monthly return of each index, the mathematical mean (average) return of the constituent funds is calculated. This is calculated as follows:

$$\sum_{i=1}^{n}\left(\frac{Return_i}{n}\right)$$

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Where *n* is the number of funds in the index.

Unlike other indices, monthly values are not asset-weighted nor median returns. Asset weights can disproportionately overweight managers who successfully market their product in investor hot spots. They can also underweight capacity constrained funds. Instead, equal weights provide a more holistic view of the average performance of funds.

6.5 NAV Calculation

The NAV of each index is set to 100 at inception, with changes thereafter driven by the monthly returns. This is calculated as followed:

$$\boldsymbol{NAV_t = NAV_{t-1} \times (1 + ROR_t)}$$

Where ROR_t refers to the return in current month *t* and is calculated as above.

6.6 Updates

The Aaro Crypto Fund Indices are updated once a month.

Given the fast-changing nature of the DLT and cryptoasset space, the historical values of the indices will change over time as new funds are identified and incorporated in the indices. This ensures the indices remain relevant and reflective of the evolution of the fund universe.

6.7 Constituent Events

An “Constituent Event” refers to one or a combination of the following:

- When it is not possible or reasonably practicable to determine the price or value of a constituent;
- When the value of a constituent is not announced or is otherwise unavailable when such announcement or availability would be normally scheduled;
- The occurrence of an event that can affect a constituent, including, but not limited to, major market disruption, systems failure, natural or man-made disaster, personnel loss, cyber security breaches, regulation, events affecting reputations, or any other similar circumstances.

If a Constituent Event occurs in any form, Aaro Capital may make adjustments to the provisions of the indices to account for such Constituent Event as it determines appropriate, including, without limitation, delaying the application of any procedures or requirements of the construct of the indices.

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7 Aaro Index Committee ("AIC")

7.1 Members

The AIC is currently comprised of the following individuals:

- Peter Habermacher – CEO & Co-founder of Aaro Capital
- Ankush Jain, CFA – CIO & Co-founder of Aaro Capital
- Peter Rigg, CFA – Head of Investment Research at Aaro Capital (previously Global Head and CEO of HSBC Alternative Investment Group)
- Stuart MacDonald – Chairman of Aaro Capital (previously Director of Hedge Funds at Henderson Global Investors)
- Tushar Patel – Managing Partner at HFIM (member of Aaro Capital's Advisory Board)
- Eric Bissonnier, CFA - Head of Multi Asset Solutions at LumRisk and CEO & Founder at BISFICO (member of Aaro Capital's Advisory Board)

7.2 Role

The AIC provides oversight on the methodology of the Aaro Crypto Fund Indices, with a focus on ensuring sufficient continuity and diversification.

The committee does not decide on the actual composition of the indices. It may, however, intervene in certain cases such where strict application of the methodology may affect the representativeness of the indices, for example in the case of a Constituent Event.

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8 Appendix

8.1 Changes to Methodology

There have been no changes to methodology since inception of the indices.

Date	Revision	Process
09/05/2022	Launch of Aaro Crypto Fund Indices (PG)	N/A

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