

Democratizing Finance

An Interview with Nancy Davis, Founder and Portfolio Manager, Quadratic Capital Management LLC

EDITORS' NOTE Nancy Davis is the portfolio manager for the Quadratic Interest Rate Volatility and Inflation Hedge ETF and the Quadratic Deflation ETF. Davis began her career at Goldman Sachs where she spent nearly ten years, the last seven with the proprietary trading group where she became Head of Credit, Derivatives and OTC Trading. She has been the recipient of numerous industry recognitions. Barron's named her to their inaugural list of the "100 Most Influential Women in U.S. Finance." Institutional Investor called her a "Rising Star of Hedge Funds." The Hedge Fund Journal tapped her as one of "Tomorrow's Titans." Davis writes and speaks frequently about markets and investing, and has been profiled by Forbes, and interviewed by Barron's, The Economist, The Wall Street Journal, and The Financial Times, among others. She is a frequent guest on television including CNBC, Bloomberg, CNN, CBS, and ABC.



Nancy Davis

FIRM BRIEF Quadratic Capital Management LLC (quadraticllc.com) is an innovative asset management firm founded in 2013 by Nancy Davis. The firm has utilized its significant expertise in the interest rate volatility and options markets to construct IVOL in a way that helps mitigate the downside risk of the strategy while maintaining upside potential.

What was your vision for creating Quadratic Capital Management and how do you define the firm's mission?

My vision was to be the first to bring options and hedging strategies usually found in private funds to the public markets, essentially democratizing them. Before Quadratic launched

IVOL, most fixed income investors had no choice but to be short convexity and short volatility. Our mission is to give regular fixed income investors long convexity and long volatility in an exchanged traded fund in a potentially tax-friendly wrapper with no lockups at a fraction of the cost compared with private fund vehicles.

Will you provide an overview of Quadratic Capital's business?

Quadratic is an innovative asset management firm that manages the portfolios for two exchange traded funds – IVOL and BNDD. Our investment approach is based on our expertise in investing through options. We like to buy options because we like to stay on the asymmetric side of the trade, where the potential upside is larger than the maximum downside. A lot of firms that trade options are actually in the business of selling them. The problem with selling options is when you sell an option, you've given someone else control over what and when you have to buy.

Most fixed income investors are only short options because the bond benchmarks have a large weight towards mortgages. If you invest in a mortgage, most of the time you own an agency obligation combined with a short option. U.S. homeowners are long the option to pre-pay but if you own the financial mortgage, you're short options to homeowners, and whenever you're short options, you're short volatility.

I think of our funds as solutions to problems most investors must either confront or ignore. For example, our IVOL fund helps investors with their embedded short volatility position. Our BNDD fund helps investors who are concerned that the U.S. economy is in a prolonged slump.

What have been the keys to the strength of Quadratic Capital and how do you describe the Quadratic Capital difference?

Our funds solve several problems for investors. For example, our IVOL fund helps investors deal with the embedded short volatility from their mortgage-backed securities. It has offered very low correlations with – and therefore helps diversify – the major stock and bond indices. It has provided very consistent, tax-efficient income without taking on corporate credit risk.

Our success is largely a function of the innovations we've brought to market. But we don't innovate for its own sake. We're trying to solve specific problems facing investors. Using options as a core element of our funds is a major difference.

What do you see as Quadratic Capital's responsibility to be engaged in the communities it serves and to be a force for good in society?

Our funds can be very helpful for working people all over the country. Higher inflation hurts everybody, but it hits people on fixed incomes and limited budgets harder, and people who are not qualified investors don't have a lot of ways to deal with it. Our IVOL fund is designed to help hedge against inflation, to protect purchasing power. And it works just the same in a teacher's 403(b) as it does in an account at any exclusive private bank.

I am a big advocate of having this hedge against inflation to fight the loss of purchasing power and I believe we have democratized the market for any and all investors with our funds.

Did you always know that you had an entrepreneurial spirit?

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Nancy Davis at the New York Stock Exchange in front of the IVOL listed banner

I've worked for some really talented people over the years, and I tried to learn as much from them as I could. Quadratic is my attempt to put together all the best lessons that I learned during my time on Wall Street. It's been exciting and rewarding and a tremendous amount of work.

Quadratic Capital has accomplished much in its ten years of existence. Are you able to enjoy the process and take moments to reflect on what you have built?

I've always enjoyed the process. It's been quite a journey and I try to savor it, but I'd say I'm never satisfied; I always want to be on that soapbox on a daily basis educating investors. It doesn't even feel like work because I love what I do. That passion drives my desire to advocate and educate.

Do you feel that there are strong opportunities for women to grow and lead in the industry?

Yes and no. When I was at Goldman, I was given a lot of responsibility very quickly and allowed to keep growing. As well, from my experience there has been a recent push for greater diversity in the financial world, and I personally have always tried to be very supportive of talented people in the industry, women and men. That said, there aren't a lot of women-owned asset management firms in the world. With the big push to make sure there are women on corporate boards, I don't understand why there isn't a push for more women-owners. If you buy the argument that having people of different backgrounds and different ways of thinking makes for a better process and

outcome, then surely more investment should be made to support women owning and operating their own businesses.

What advice do you offer to young people interested in a career in finance?

Don't major in finance or business administration. I am a big believer in liberal arts education. If you go to work at a bulge bracket bank, they will teach you everything you need to know. Learn about the world, and how and why it came to be what it is. Study what smarter people than you thought and wrote about what it means to be a human and what is important and worth studying and what isn't. Not only will you be much more interesting to talk to, but you'll be a better investor, too.

I also say that if people get into finance to make money, that is definitely the wrong reason. Do something because you love it – whatever that is – and you will usually outperform people doing that same thing for money.

What do you see as the keys to effective leadership and how has operating Quadratic Capital affected your views on leadership?

Well, there are lots of ways to be a good leader, but there are some common traits. First, you have to have a clear vision of what you want. If you're a leader, that implies that you're leading towards something. Leaders are always focusing on tomorrow and let their teams take care of today. If you're just holding down a seat, it's hard to be a leader.

Then I think you must be a communicator. You may know what you want to do, but if you can't get your team to believe it or see it with you, it will be very challenging to motivate that group to its peak. And that includes listening. Leaders need to understand what is really going on around them. It's easy to sit in a corner office and have a Mr. Smithers from the Simpsons tell you, "Gutsy decision, sir" after everything you do. But you'll make bad decisions that way.

Lastly, I think you've got to be a worker. You've got to put in the hours. I am a big fan of the band Whiskey Myers. They have a song called "The Wolf" and the chorus includes the lines, "I'll be prowling while you sleep. You're playing for fun but I'm playing to eat." I love that line. I think that's the correct mentality. You need to be the first car in the parking lot, the last computer monitor turned off. You can't ask people to work harder than you do. Well, you can, but they won't. ●

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