Introducing The ActiveAlts Contrarian ETF

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Summary

- Introduces a unique short squeeze ETF.
- Interviews the portfolio manager of the fund.
- Explains why this ETF is so unique.

On March 22, 2017, a unique ETF was launched called the **ActiveAlts Contrarian ETF (NASDAQ:SQZZ)** that is a first-of-its-kind actively managed ETF, which seeks capital appreciation by investing in companies with solid fundamentals that have very large short positions and are subject to a short squeeze. The SQZZ portfolio manager screens securities that are highly shorted to isolate indications of unexpected values.

The ETF invests in securities with market capitalization of $250 million or greater with at least $1 million a day in trading volume. The strategy does not have to be fully invested at all times, and it can raise 100% cash if warranted by market conditions, which may allow the fund to outperform in bear markets. As a special treat to my readers here on Seeking Alpha, I was able to actually interview the portfolio manager of the ETF and here is that interview:

With me I have Brad Lamensdorf, the founder of the **ActiveAlts Contrarian ETF**, a fund that focuses on short squeezes. Who doesn't like a good short squeeze? It's an innovative fund and Brad's background and experience tie in well with managing the strategy. With that let's learn more about the fund from Brad.

Mycroft: Brad, thanks for taking the time to speak with me today. There's a lot of ETFs that cover a wide array of sectors or strategies, but one that focuses on short squeezes is truly unique. Explain for my Seeking Alpha readers what a short squeeze is and a bit about your background as a manager.

Brad: A short squeeze occurs when the short position in outstanding shares of a company becomes too large. Such a situation creates overselling of an issue. It also produces an open-ended liability for all investors who are short that particular stock. Once a stock starts moving upward, there can be unlimited losses for the short investors. There is only one way for investors to "close" their positions. In other words, they must "buy to cover."

I started out working for the Bass brothers in their alternative division, where I worked with over twodozen differentiated alternative strategies. After six years with the Bass brothers, I started my own long/short hedge fund called Tarpon Capital. In 2009, I joined Ranger Alternative Management. I am the co-manager of HDGE, a short-only active ETF.

Mycroft: It's interesting that you've been shorting stocks for a while both in hedge funds and as co-manager of the **AdvisorShares Ranger Equity Bear ETF (NYSE: HDGE).** With SQZZ you're taking the opposite side of the trade. How has the experience as a short seller played a role into managing SQZZ?

Brad: As the manager of a short fund, I am constantly bombarded with outside research ideas. Many of these ideas are "crowded" shorts that involve companies whose stocks are already quite depressed. Such situations cost the short seller large fees when borrowing the stock. In my opinion, taking the other side of the trade in a stock that I like, and being able to earn extra interest, gives the strategy a competitive advantage in the marketplace.

Mycroft: What's your process for identifying short squeezes and what's an example of a squeeze that has taken place in the market recently?

Brad: We have created a proprietary screen of highly shorted stocks. This list is highly vetted, both fundamentally and technically, before a position is recommended for the portfolio.

Weight Watchers (NYSE: WTW), for example, is over 60% short and is being borrowed at over 20% a year annualized. I think the company's restructuring efforts are working, and I believe that Oprah is in the process of turning the company around. I can collect large amounts of interest while I wait for that process to work.

Mycroft: What about big cap stocks like **Apple (NASDAQ: (NASDAQ:AAPL)** or **Facebook (NASDAQ:)**? Are massive companies like that vulnerable short squeezes?

Brad: They certainly are. While the short interest ratio may not be high, the notional dollar amount of the positions can be enormous and are susceptible to a short squeeze.

Mycroft: So, you use both technical and fundamental analysis. It seems like most managers are in one camp or the other. Another interesting aspect of SQZZ is that unlike many funds, you do not need to be fully invested. What's your process for determining your overall exposure?

Brad: I use market timing as a tool to determine gross exposure. Breadth, sentiment and market-oriented liquidity are used in order to judge optimal exposure levels.

Mycroft: How low can your exposure go?

Brad: SQZZ can be 100% invested and has the ability to go to 100% cash. Cash can be a powerful hedging tool during overenthusiastic periods or during bear markets. This gives our fund quite an advantage.

Mycroft: It's nice to not be fully exposed if you feel confident the market is ripe for a pullback. How many positions do you expect to typically have if you're fully invested and what other risk management techniques do you have in place?

Brad: When fully invested, we expect to have 60-80 positions. Each position will be monitored technically, as price action is one of our important risk management tools.

Mycroft: I know that some shorts are expensive to borrow. How does SQZZ benefit from hard to borrow shorts?

Brad: Because we are long many hard-to-borrow names, our assets become valuable to many Wall Street lending departments. We have secured several lending agreements that will give us about 80% of the interest they receive by borrowing our securities, thereby creating extra yield.

Mycroft: Wow, so shareholders are going to benefit from the interest earned on hard-to-borrow stocks. That's very innovative in the ETF space because managers have kept that interest earned for themselves.

Brad: Yes, exactly!

Mycroft: In your opinion, how should investors and traders use SQZZ in their portfolios?

Brad: SQZZ is designed for capital appreciation and extra income obtained through its securities lending business. The ETF should be incorporated into the equity portion of an investor's portfolio.

Mycroft: What's the fund cost to own?

Brad: We have priced SQZZ as a liquid alternative product. Because of the securities lending component, the strategy is more expensive to run when compared to a general index fund. Our management fee is 1.55%.

Mycroft: Obviously, that's higher than an index fund. SQZZ seems like an alternative in a true sense of the word. Are you essentially managing this like a hedge fund strategy but in a publicly traded fund?

Brad: Precisely!

Mycroft: Where can investors get more information on the fund and strategy?

Brad: Investors can easily access information for SQZZ at activealts.com.

Mycroft: Brad, thanks for your time today. In my opinion, this is really one of the more unique and interesting ETF launches. Trying to profit from shorts gone awry and helping investors reach a higher yield through interest on hard to borrow stocks makes perfect sense. I wish you success with the fund.

Brad: Thank you. It was great being here with you today.

I am writing about this ETF today as I found it very unique and feel that it is a pioneer ETF, as no one has ever attempted this before. Here is an example of how unique this ETF really is, and in doing so let's talk about dividends, which is a very popular subject here on Seeking Alpha. SQZZ investors earn current income by receiving the majority of the interest from banks, which are paid by borrowers of the security.

Typically, when securities are loaned from an investor's margin account, the investor earns nothing - the payment is kept by the bank or broker. SQZZ is not typical for when it loans securities, the bank will pay the ETF the majority of the interest it may earn, that income goes to SQZZ investors in the form of a dividend.

Going forward, for those interested in taking advantage of potential short squeezes, but at the same time would also like to diversify among a large group of such investments, this ETF does it all for you in one shot and pays out a dividend as well.

To try to mirror what this ETF can do for you is extremely complicated and I am very impressed in how the ETF is structured in that it buys shares in the short squeezed companies and then loans those shares out in an environment where such securities are in short supply to be loaned out. Thus, we have a very complicated process managed by a true professional and expert and that is why I think this ETF will do very well going forward as the strategy sounds brilliant to me.

Disclosure: I am/we are long AAPL.

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