



# Opalesque Round Table Series '11 LONDON

Opalesque 2011 Roundtable Series Sponsor:



# Editor's Note

London still dominant location for hedge funds in Europe

Recently, there has been some disquiet about the hedge fund industry in the U.K.: the tax regime is regarded as unhelpful or even a threat, and while some fund managers “voted with their feet”, others not willing to move physically have set up an asset management business in Malta and continue to just provide research from the U.K.

However, London is still the dominant location for hedge funds in Europe, with the highest concentration of Europe's talent, assets, risk taking, service providers and new launches. As an industry, hedge funds continue to play an increasingly important role for institutions, and via UCITS also for retail investors.

The Opalesque 2011 U.K. Roundtable took place July 5th in London with:

- **Melissa Hill, Managing Principal, Sabre Fund**
- **Mark Leader, Director of Marketing, Sloane Robinson**
- **Charles Tritton, De Putron Fund Management**
- **Julian Treger, Co-Founder, Audley Capital Advisors**
- **Loic Fery, CEO and Founder, Chenavari Investment Managers**
- **Morten Spenner, CEO, International Asset Management Ltd.**
- **Eoin Murray, CEO, Callanish Partners**
- **and sponsors Dermot Butler, Custom House Group and Joe Taussig, Taussig Capital.**

The average investor has really not seen real growth in the Western markets over the last ten years. Therefore, read about which strategies and innovative investments these hedge fund veterans recommend at the moment. The current and future volatility is considered to offer attractive risk-on trades - provided they are not just bluntly long - in the following areas:

- **Three investment opportunities in European Credit**
- **High conviction opportunities and catalyst trades**
- **Event/stressed situations – how hedge funds started to “create” their own events**
- **Equities, particularly Asian / emerging market equity and commodities**

In addition, read...

- **How emerging managers can launch with \$35 and grow to \$2bn in four years**
- **How start up hedge funds can get fund administration for only 8,000 Euros**
- **How FATCA and new FBAR Regulations will burden the industry and pile up costs**
- **What the Hedge Fund Standards Board found about actual hedge fund governance**
- **Risks and Benefits of UCITS funds: How the first publishing of the Draft AIFM Directive led to a flood of UCITS launches, and why investors should know the differences between pure UCITS funds and synthetic UCITS strategies**

Enjoy “listening in” to this new Opalesque Roundtable!

Matthias Knab

Director Opalesque Ltd.  
Knab@opalesque.com

# Participant Profiles



(TOP TO BOTTOM)

Mark Leader, Charles Tritton, Julian Treger, Morten Spenner, Eoin Murray, Dermot Butler, Melissa Hill, Loic Fery, Joe Taussig

# Introduction

**Dermot Butler**  
Custom House Group

My name is Dermot Butler. I am the Chairman of the Custom House Group of companies. We are fund administrators based in Malta with subsidiaries in Dublin, Chicago, Singapore, Luxembourg, Netherlands, and Guernsey. We specialize in alternative investments and hedge funds, including CTA funds, Funds of Funds, Managed Accounts and, of course, both Real Estate and Private Equity Funds. We have a system that enables us to follow the sun, and provide around-the-clock service from our global network of offices. As a result, we are doing daily valuations for about 25% of the 550 or so funds and sub-funds that we act for. In aggregate we have about \$50 billion under administration.

**Melissa Hill**  
Sabre Fund Management

My name is Melissa Hill, I am the Managing Principal of Sabre Fund Management. We are a \$650 million quantitative equity boutique. We have been running money in the award-winning market neutral Sabre Style Arbitrage strategy since 2002. The strategy is accessible via three co-mingled funds and managed accounts. One of the three funds is a UCITS fund with daily liquidity. The business comprises a team of 15 and is primarily a partnership between myself and Dan Jelacic, the architect of our Sabre Style methodology.

**Eoin Murray**  
Callanish Capital Partners

My name is Eoin Murray. I am the CEO and one of the Founding Partners of Callanish Capital Partners. We established the partnership in the middle of 2008 with a unique sense of timing! In May 2010 we launched our first fund, the Callanish Global Macro Fund, with seed capital awarded by IMQubator Investment Management, the Dutch seeding platform established by APG, the world's second largest pension asset manager. The Fund is a systematic global macro strategy with a focus on diversification, liquidity, and risk management, and in the last 12 months has returned over 10.7%. We are running, at the moment, around \$40 million.

**Morten Spenner**  
International Asset Management

I am Morten Spenner, CEO of International Asset Management, which is an investment boutique that customizes solutions using hedge funds sourced from across the globe. We run about \$3 billion today, and we do that predominantly for institutional investors including sovereign wealth. Since the firm was founded back in April 1989, we have been focusing on bespoke, liquid solutions for clients where we customize the portfolio - including the actual structure through which the clients invest - and providing innovative in-depth. This ensures that clients have genuine appreciation for their exposure and how it fits their overall portfolio. We have an office here in London as well as in New York, Stockholm, and Madrid. We are majority owned by the employees, which is rare these days in fund of hedge funds, and supported by our minority shareholders Jefferies Inc. and Sir Ronald Cohen.

**Joe Taussig**  
Taussig Capital AG

My company is Taussig Capital AG in Switzerland. We partner with hedge fund managers to create insurance companies and banks. The hedge fund managers' motivation is to increase assets in the form of permanent capital, and the motivation for the investors is that we have almost consistently outperformed the managers' core funds, and offer better liquidity and better tax treatment in certain countries; particularly in the UK, Canada, and the U.S. Our most visible company is Greenlight Capital Re, which is a publicly traded reinsurance company with more than \$2 billion in assets managed by David Einhorn. It has outperformed the Greenlight funds by 7% per year since inception, and for UK or U.S. taxable investors outperformance has been 10% per year since inception.

**Julian Treger**  
Audley Capital

I am Julian Treger, co-founder and partner at Audley Capital, which advises on about \$700m of assets under management. We started Audley back in 2005 to create niche products and hedge fund strategies with high barriers to entry that can actually produce alpha, in the form of 20% plus annual returns. The flagship strategy is the Audley European Opportunities Fund, which is founded upon friendly activism in Europe, and has achieved those returns. We believe in engagement and that the

tendered farm does better than the absentee landlord. We try to create high returns with higher, but not extraordinary, volatility. At the moment, the fund is largely focused on BRIC infrastructure, European recovery, natural resources and distressed restructurings.

Audley also launched a global mining equities hedge fund late last year in conjunction with a senior ex-Glencore exec. Similar to the flagship fund, it engages with managements especially in the small cap arena to help extract shareholder value. Audley is also launching a negative Japan fund in the next couple of months.

**Mark Leader**  
Sloane Robinson

I am Mark Leader, partner and Deputy-CEO of Sloane Robinson. We are a London based, long-biased, long/short equity manager founded in 1993. Today, we run about \$7.0 billion of assets across a variety of different strategies. Two-thirds of our assets are currently invested in Asian and emerging markets.

**Charles Tritton**  
De Putron Fund Management  
Limited(DPFM)

My name is Charles Tritton. I am the CIO of the discretionary trading business of De Putron Fund Management Limited commonly known as DPFM. We were founded in 1997 and are among the older European hedge fund groups. We are known for our beta neutrality and our trading style, which is very much European focused. Since we developed this strategy in January 2008, we have achieved a top-decile risk adjusted performance versus our peer group. We have an experienced team of 15 investment professionals with an average investment experience of 16 years and a hedge fund experience of 8 years.

**Loic Fery**  
Chenavari Investment Managers

My name is Loic Fery. I am the Founder and Managing Partner of Chenavari Investment Managers. We are a hedge fund based in London, focused on fixed income credit markets, with approx \$1.8 billion assets under management. We run two funds at the moment, The Chenavari Multi-Strategy Credit Fund, and Toro Capital I, a dedicated structured finance and asset backed securities fund.

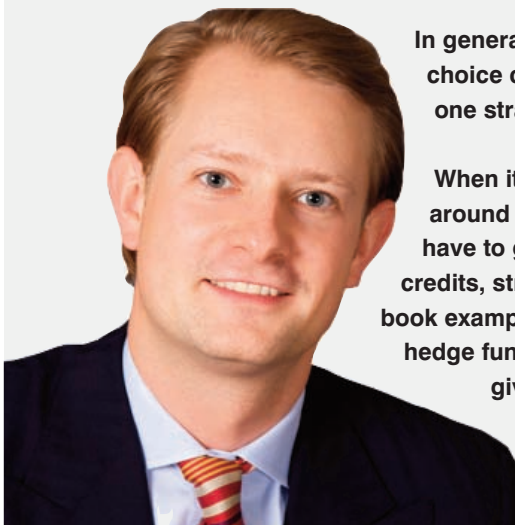
**Morten Spenner**

Until April, I would say that we saw a certain normalization coming back into the system. After that, we went back into this risk-on, risk-off mode where investors are just a little bit overly cautious and therefore not committing to positions as they were before. The market gyrations will continue until there is more consensus on what comprises the new “norm”.

I would argue that the difference between 2011 and 2010 is that hedge fund managers, in general, seem to be more committed with respect to the risk positions they have on, and so they tend to hold positions longer. That said, during May and June some managers have been changing their positioning in response to risk management - particularly commodity managers, which isn't necessarily a surprise to anyone.

**I would argue that the difference between 2011 and 2010 is that hedge fund managers, in general, seem to be more committed with respect to the risk positions they have on, and so they tend to hold positions longer. That said, during May and June some managers have been changing their positioning in response to risk management - particularly commodity managers, which isn't necessarily a surprise to anyone.**

**The areas that we, as a firm, look most favorably upon are equities, particularly Asian and emerging market equity, commodities, and then what I would call event/stressed situations.**



**In general, though, we have assets allocated to just about all strategies, and our choice comes much more down to manager selection as opposed to overweighting one strategy over others.**

**When it comes to certain niches we are looking at, one of them is the development around European banks. As their regulation is being tightened, many of them will have to get some of the riskier assets off their books. That could involve structured credits, stressed assets where hedge fund managers can almost play the classical text book example of providing liquidity to a seller that might be a bit distressed and the hedge fund manager steps in and offers the seller a fair value, but also a value that gives them a substantial upside.**

**Morten Spenner**

Many investors hoped investment returns would be stronger in 2011, but there is not much to show for it yet with returns averaging flat 'til end June. Of course, one has to be careful with consensus views, but it seems as if the consensus view is that normalization is slowly continuing and that the second half of 2011 will be a much more interesting from a return perspective. It speaks to the old phrase that “alpha is lumpy”.

The areas that we, as a firm, look most favorably upon are equities, particularly Asian and emerging market equity, commodities, and then what I would call event/stressed situations.

In general, though, we have assets allocated to just about all strategies, and our choice comes much more down to manager selection as opposed to overweighting one strategy over others.

When it comes to certain niches we are looking at, one of them is the development around European banks. As their regulation is being tightened, many of them will have to get some of the riskier assets

off their books. That could involve structured credits, stressed assets where hedge fund managers can almost play the classical text book example of providing liquidity to a seller that might be a bit distressed and the hedge fund manager steps in and offers the seller a fair value, but also a value that gives them a substantial upside.

## Mark Leader

I would agree with a lot of what Morten has said. We have also seen a more challenging market in terms of return opportunity in the first half of the year. I believe a lot of that has come from the violent rotations that have occurred within both regions and sectors as market participants have grown increasingly sensitive to the ongoing macro/economic concerns, predominantly in developed markets, effectively creating mini risk-on and risk-off moments in markets.

Another point I notice is that we seem to have been operating in an environment where investors are still feeling burned from the illiquidity that they suffered in 2008. In particular, in our area of emerging markets and Asia, we have seen a lot of money entering those markets through ETFs and passive funds rather than through more directional managers. The downside is that this has exacerbated the high levels of correlation in markets, as this indiscriminate money does not necessarily flow into the best stock ideas, nor where the best returns might be achieved. However, such behaviour is completely understandable given the liquidity issues faced through the global financial crisis.

**I notice is that we seem to have been operating in an environment where investors are still feeling burned from the illiquidity that they suffered in 2008. In particular, in our area of emerging markets and Asia, we have seen a lot of money entering those markets through ETFs and passive funds rather than through more directional managers. The downside is that this has exacerbated the high levels of correlation in markets, as this indiscriminate money does not necessarily flow into the best stock ideas, nor where the best returns might be achieved. However, such behaviour is completely understandable given the liquidity issues faced through the global financial crisis.**

**Year to date we have seen a greater dispersion of returns within the market, not just in the underlying company fundamentals, because that has been there for some years, but in the performance of the underlying share prices. That is really encouraging, because it allows alpha generators such as ourselves, to be able to take advantage of the winners and the losers.**

**When it comes to high conviction opportunities, I see two worthy of note. The first is Japan, where we see a nearer-term return to production levels that are probably about 90% of where they were prior to the earthquake and tsunami. A lot of sell side analysts still believe that production will not fully return until the end of this year, so we see a nice opportunity to make money there. However, unless we see some fiscal reflation in the domestic economy, then it is unlikely that we will see a domestic recovery providing longevity to the investment opportunity.**

**The other encouraging opportunity that we see is more of a multi-year secular investment opportunity in Greater China. As our clients have witnessed, for some time now we have had quite a non-consensual view that China is going to engineer a soft landing, as inflationary pressures abate and the bulk of monetary tightening passes. We believe that the June inflation number was the peak and that we should start to see inflation come down into the second half of the year.**

Mark Leader



Year to date we have seen a greater dispersion of returns within the market, not just in the underlying company fundamentals, because that has been there for some years, but in the performance of the underlying share prices. That is really encouraging, because it allows alpha generators such as ourselves, to be able to take advantage of the winners and the losers.

We see a lot of opportunity coming along in the second half of this year and possibly next, should (as we anticipate), many of the perceived risks get either resolved or postponed. This does not mean that they have vanished completely, though.

There are still many genuine unresolved risks from a lack of growth through to fiscal imbalances. In particular this is true for the US, however, provided that dollar is going to remain relatively stable (or only slightly weaker or slightly stronger) we do not see there being a significant near-term problem, it is usually when there are rapid moves in the currency that greater problems emerge.

When it comes to high conviction opportunities, I see two worthy of note. The first is Japan, where we see a nearer-term return to production levels that are probably about 90% of where they were prior to the earthquake and tsunami. A lot of sell side analysts still believe that production will not fully return until the end of this year, so we see a nice opportunity to make money there. However, unless we see some fiscal reflation in the domestic economy, then it is unlikely that we will see a domestic recovery providing longevity to the investment opportunity.

The other encouraging opportunity that we see is more of a multi-year secular investment opportunity in Greater China. As our clients have witnessed, for some time now we have had quite a non-consensual view that China is going to engineer a soft landing, as inflationary pressures abate and the bulk of monetary tightening passes. We believe that the June inflation number was the peak and that we should start to see inflation come down into the second half of the year.

We are not anticipating a reversal of monetary policy, but simply a pause in tightening. With an economy growing at over 9% per annum, even post tightening, we can buy some very encouraging investment opportunities. These are unlikely to be in the more export focused manufacturing areas, but those exposed to the domestic economy. The opportunity is not just China, but Greater China as a whole – things like natural resources or Western companies selling luxury goods into China. There is a whole range of opportunities to take advantage of the growth in GDP per capita, and disposable income.

I would also add that we expect sometime early next year that India will once again present itself as an attractive investment opportunity. We are not lacking ideas in this market, but just awaiting the appropriate time for some of the macro risks to come out of the equation, at that point we will feel much more comfortable putting the risk on at the individual stock level.

## Charles Tritton

Usually, when you ask a bunch of hedge fund managers, who can go long and short, they will always say there are great opportunities. However in reality the first half of 2011 has proved to be a difficult one for most European hedge fund managers. The question is, of course, going forward will the opportunities be greater or worse than they were before?

**Usually, when you ask a bunch of hedge fund managers, who can go long and short, they will always say there are great opportunities. However in reality the first half of 2011 has proved to be a difficult one for most European hedge fund managers. The question is, of course, going forward will the opportunities be greater or worse than they were before?**

**I personally believe the opportunity set is improving because the macro world in Europe has dominated equity prices.**

**It is our role to exploit the inefficiencies of the market. This means that the more volatile, the better the risk reward is, although it can sometimes take time for the profits to crystallize. In addition I feel that the amount of competing capital has fallen sharply as a result of the withdrawal of proprietary trading from the banks. This should result in a better stream of trading profits for us.**

**Currently over 50% of our book is in what we term catalyst trades. Morten already mentioned the opportunity around European banks - we have been involved in most of the restructurings of European banks so far in 2011 and we do not expect this process to halt anytime soon.**



Charles Tritton

I personally believe the opportunity set is improving because the macro world in Europe has dominated equity prices. It is our role to exploit the inefficiencies of the market. This means that the more volatile, the better the risk reward is, although it can sometimes take time for the profits to crystallize. In addition I feel that the amount of competing capital has fallen sharply as a result of the withdrawal of proprietary trading from the banks. This should result in a better stream of trading profits for us.

Currently over 50% of our book is in what we term catalyst trades. Morten already mentioned the opportunity around European banks - we have been involved in most of the restructurings of European banks so far in 2011 and we do not expect this process to halt anytime soon. For example, we are looking forward to the Spanish banking IPOs of Banca Civica and Bankia, which are being priced at less than half times book. That does not mean they are cheap but it provides extra data points for us to trade.

Going forward, I agree with Mark's comments on China. Do we have a problem if they are growing at 5%? Even at this level there will be opportunities for European companies to sell more products to China.

Greece has significant problems about solvency and liquidity, which we do not expect to disappear in the short term. Indeed we expect them to recover whenever the elastoplasts, applied by the EU, need replacing.

I think, if we remain flexible and disciplined as we have always done, we should continue to generate good returns in the second half of 2011.

## **Julian Treger**

The average investor has really not seen real growth in the Western markets over the last ten years. So, how do you make good money going forward?

One is to be active and to create your own event. For me, event-driven isn't really the appropriate word, because it implies some passivity. We as investors aim to be active and try to really affect the future path of a company. Ideally we want to be transformational in some way. I believe this approach to legally and intelligently create your own performance will be increasingly valued by investors.

I want to talk briefly about an extraordinary disparity that I find very striking. We live in a world where growth is propelled by two main drivers: one is technological innovation, the other industrialization. Now, on the one hand there are stocks like Zynga, which hit the market with hockey stick projections like 40 times revenues and 300 times profit multiples, yet with the other driver we find commodity big caps at just under five times EBITDA, mid-caps at three to four times and small caps at two to three times. The contrast between the ratings of these groups, with the risk that tech companies are very open to competition whereas commodity equities own fundamentally irreplaceable resources, suggests there is compelling value in mining stocks.

Regarding China, I continue to believe the Chinese are managing very well, I don't think they will tighten much further. With that, I believe we have reached an important junction. It is easier for Audley and others with a similar expertise to make money out of China and India by finding the things they want in the West or emerging markets, and this is a theme on which we are focused.

I agree that going forward the market will present opportunities to investors. I think Greece has gone away for a while, and no American politician is going to vote for a debt cap, because being the guy who brings down the financial system is not going to win you votes. For a certain period we are risk on, and as people cannot put their money into T-Bonds due to the low rates, money will find its way into equities and commodities.

Another theme we are pursuing is centered around best emerging market companies that until recently were very eager to get listed on places like AIM or Frankfurt to gain access to Western capital, when at the same time the ratings in the West were higher than in their home markets. That is now reversed, which I think is interesting and reflects the direction of the change in power between the developed and emerging markets that happened over the last ten years. These companies have become orphaned because they are neither well known in their home markets nor followed in London or Frankfurt. I

believe there is definitely an arbitrage opportunity to encourage those firms to get listings in Mumbai, Singapore, Hong Kong, or Shanghai and then ultimately transport their primary ratings to those markets.

**The average investor has really not seen real growth in the Western markets over the last ten years. So, how do you make good money going forward?**

**One is to be active and to create your own event. For me, event-driven isn't really the appropriate word, because it implies some passivity. We as investors aim to be active and try to really affect the future path of a company. Ideally we want to be transformational in some way. I believe this approach to legally and intelligently create your own performance will be increasingly valued by investors.**

**I want to talk briefly about an extraordinary disparity that I find very striking. We live in a world where growth is propelled by two main drivers: one is technological innovation, the other industrialization. Now, on the one hand there are stocks like Zynga, which hit the market with hockey stick projections like 40 times revenues and 300 times profit multiples, yet with the other driver we find commodity big caps at just under five times EBITDA, mid-caps at three to four times and small caps at two to three times. The contrast between the ratings of these groups, with the risk that tech companies are very open to competition whereas commodity equities own fundamentally irreplaceable resources, suggests there is compelling value in mining stocks.**

**Another theme we are pursuing is centered around best emerging market companies that until recently were very eager to get listed on places like AIM or Frankfurt to gain access to Western capital, when at the same time the ratings in the West were higher than in their home markets. That is now reversed, which I think is interesting and reflects the direction of the change in power between the developed and emerging markets that happened over the last ten years. These companies have become orphaned because they are neither well known in their home markets nor followed in London or Frankfurt. I believe there is definitely an arbitrage opportunity to encourage those firms to get listings in Mumbai, Singapore, Hong Kong, or Shanghai and then ultimately transport their primary ratings to those markets.**



**Julian Treger**

The key is, as always, to be flexible. The overall decline of volumes in the market and the lack of interest in stories have meant that tremendous inefficiencies have developed over the last couple of months.

### **Charles Tritton**

I agree regarding the decline of the volumes. If you just take the overall trade volumes and strip out the high frequency trading part, you will find that volumes have really collapsed and you can see how uninterested people are in the European equity markets today.

In addition I agree with Julian that there are always interesting situations and extreme valuations in individual shares. Dispersion of stock returns is already present but I expect to see this grow as volumes grow after the summer. This could result in significant gains for hedge fund returns in the final 1/3rd of the year.

At the same time, I think the corporate financiers have been much quieter than they anticipated in the first half of 2011. Many IPOs and other corporate transactions failed to materialize.

Private equity failed to divest companies from their portfolios and pricing is becoming cheaper. If the transaction volume created by the investment bankers increases, then there should be good opportunities for most hedge fund groups to extract value.

**Eoin Murray**

With the end of QE II, we would also expect a return to normalized market conditions, which for a systematic manager such as ourselves can only be a good thing.

We are never keen on government or central bank intervention in the markets – such behaviour makes our life a lot more difficult as we witnessed in the first half of 2011, although we managed to preserve capital while remaining fully invested and even made money in June at a time when other managers struggled. This highlights the need for diversification and solid risk management. We are very much looking forward to moving from a capital protection mindset to a return generation focus in the second half of this year.

**Loic Fery**

Let me add here a more moderate viewpoint, we think volatility will remain very high in the markets and, therefore, we are not completely risk-on at the moment.

In European credit, we see three types of investment opportunities: first, the relative fundamental value between corporate credit spread premiums that are widening and the actual corporate deleveraging that is taking place, second the European asset backed securities, and third the investment opportunities arising from the European banks' regulatory capital situation.

**We think volatility will remain very high in the markets and, therefore, we are not completely risk-on at the moment.**

**In European credit, we see three types of investment opportunities: first, the relative fundamental value between corporate credit spread premiums that are widening and the actual corporate deleveraging that is taking place, second the European asset backed securities, and third the investment opportunities arising from the European banks' regulatory capital situation.**

**First, most corporate credit spread levels are too wide compared to the fundamental leverage observed.**

**The second type of opportunity is related to the aftermath of the crisis in the most complex credit products, in particular, securitization products. Obviously, everything that is cheap is not good, but they are still very cheap securitization papers that will end up money good even in a double dip scenario. It is still possible to source assets that will return 15% yield on stress scenario. Our fund that focuses on European ABS (namely Toro fund) is up 27% during H1 2011. The first half of the year was extremely difficult from a market standpoint, but still our investment style in that space has allowed us to generate significant returns to our investors.**

**The third opportunity leads us to the regulatory environment and the transformation that is currently required within the European bank industry. Here, we are looking at a longer investment horizon of three or five years. We have a European bank, regulatory, capital credit opportunities strategy that engages in customized deals where we cherry pick assets from a bank's balance sheet. Depending on the type of deal and depending on the period, IRRs between 15 and 20% can be generated.**

**Again, I would remain overall fairly cautious on the macro environment. The current volatility and the volatility we will see in the next few months will be actually very good points for the risk-on trades, provided they are not just bluntly long.**

**Loic Fery**



First, most corporate credit spread levels are too wide compared to the fundamental leverage observed. A credit spread is a reflection of risk premium compared to some certain fundamental situation in a company, especially the net debt/EBITDA leverage and the ability of the company to repay its debt. If you take in consideration the situation of high-yield European corporates at the beginning of 2009, high-yield European companies had in average 3.9 times net debt EBITDA ratio in average. At the end of 2010 they had 3.2 times, and at the end of this year it will probably be 2.5 to 2.7 times in average. In the meantime spreads have tightened a little bit, but very little. Actually, they have

tightened primarily in 2009, they were pretty flat in 2010 and are widening in 2011.

This actually means that the spread paid for the risk is actually much better today than what it was in 2009. Surprisingly, this is opposite to the perception that everyone seems to have. The spread per turn of leverage in corporate credit, in specific corporate credits in Europe is actually at some of the highest points, excluding the exceptional six months we had at the end of 2008 and at the beginning of 2009. Let us not forget that Germany is having a year-on-year growth above 5% per annum, that we see exceptional deleveraging stories and that some companies post extremely solid earnings.

Yes indeed, we are bearish about the financial system and the sovereign environment in Europe as we think there are real issues that can show up, probably earlier than everyone thinks. However, the reality of the corporate deleveraging is there, and the first type of opportunity I am describing here is to benefit smartly from the corporate environment, while not being overexposed to the surrounding volatility. This being said, we think the best strategy on corporate credit at the moment is to be credit spread neutral and to have a long volatility element, because the reason for corporate credit spreads being wider compared to their actual fundamental value lies in the contagion effect of sovereign and bank issues

The second type of opportunity is related to the aftermath of the crisis in the most complex credit products, in particular, securitization products. Obviously, everything that is cheap is not good, but they are still very cheap securitization papers that will end up money good even in a double dip scenario. It is still possible to source assets that will return 15% yield on stress scenario. Our fund that focuses on European ABS (namely Toro fund) is up 27% during H1 2011. The first half of the year was extremely difficult from a market standpoint, but still our investment style in that space has allowed us to generate significant returns to our investors. We think there are still limited and selective opportunities to buy.

The third opportunity leads us to the regulatory environment and the transformation that is currently required within the European bank industry. Here, we are looking at a longer investment horizon of three or five years. We have a European bank, regulatory, capital credit opportunities strategy that engages in customized deals where we cherry pick assets from a bank's balance sheet. Depending on the type of deal and depending on the period, IRRs between 15 and 20% can be generated.

Again, I would remain overall fairly cautious on the macro environment. The current volatility and the volatility we will see in the next few months will be actually very good points for the risk-on trades, provided they are not just bluntly long. To summarize it: have good long idiosyncratic picks on a fundamental perspective, be positive convexity or long vol, immunize your portfolio against market beta.

### **Melissa Hill**

After a really strong 2009 and 2010, 2011 has proved to be somewhat more challenging for aspects of our diversified quantitative process. We generate returns from three main drivers – having the right allocation to the style themes being rewarded by the market, capturing the trends in these style portfolios and from price reversal anomalies. The first few months of the year have seen a good return to stat arb but very little reward to fundamentals. It's been like an extended inflexion point with risk on/risk off sentiment changing frequently.

**I agree with Loic that we will probably see higher levels of volatility in the near term. I think we should expect more pain from the austerity measures that have been taken to deal with the global debt crisis. But in the process of deleveraging and rebuilding household balance sheets, whilst affecting GDP growth, shouldn't mean a low return environment for active investors.**

**Our process is quantitative, dynamic, market and sector neutral and style agnostic. And we trade globally. If you can look through the noise and detect general signals – in our case style based themes – I believe that there is a significant opportunity to translate this environment into a good opportunity set.**

**Melissa Hill**



I agree with Loic that we will probably see higher levels of volatility in the near term. I think we should expect more pain from the austerity measures that have been taken to deal with the global debt crisis. But in the process of deleveraging and rebuilding household balance sheets, whilst affecting GDP growth, shouldn't mean a low return environment for active investors.

Our process is quantitative, dynamic, market and sector neutral and style agnostic. And we trade globally. If you can look through the noise and detect general signals – in our case style based themes – I believe that there is a significant opportunity to translate this environment into a good opportunity set.

## **Dermot Butler**

From the point of view of a hedge fund administrator, the first six months of 2011 have been quite positive. We at Custom House have seen our assets grow back up to approximately US\$50 billion, which was the peak in the third quarter of 2008. Ironically, we had not suffered any major problems at that time and I was, rather smugly, beginning to think that we were immune. This was because we had always refused to take on any credit funds, where the manager required us to accept the manager's spreads and run our own pricing models. We believed that this was not only an unnecessary risk, but did not comply with our stated function, to provide independent verification of prices and valuations, etc. We could not be independent if we were actually creating the price in the first place. So having reached that smug conclusion, inevitably Lehmans and Madoff came up behind and bit each cheek. Even so, we only had one major collapse, which was a fund of funds that had leveraged its Madoff positions, and all the others were relatively small. The main decline was because we had several good performing liquid funds that became ATM machines. I am glad to say that, perhaps as a result of honouring their commitments and allowing investors to get out without imposing any gates, those funds have now recouped virtually all, if not more than was taken out in the panic.



**From the point of view of a hedge fund administrator, the first six months of 2011 have been quite positive. We at Custom House have seen our assets grow back up to approximately US\$50 billion, which was the peak in the third quarter of 2008. Ironically, we had not suffered any major problems at that time and I was, rather smugly, beginning to think that we were immune. This was because we had always refused to take on any credit funds, where the manager required us to accept the manager's spreads and run our own pricing models. We believed that this was not only an unnecessary risk, but did not comply with our stated function, to provide independent verification of prices and valuations, etc. We could not be independent if we were actually creating the price in the first place. So having reached that smug conclusion, inevitably Lehmans and Madoff came up behind and bit each cheek.**

**Dermot Butler**

What we have seen, and this has been gradual over 2010 and 2011, has been an increase in interest in managed accounts for those funds that can provide the liquidity required by investors. We have seen funds of funds returning to the market with a more responsible attitude to liquidity matching. We are beginning to see the return of the family office and high net worth investor – we had already seen the institutional investor come back last year and they are continuing to prove to be strong supporters of the industry.

We are seeing a much greater due diligence from all investors, and that can only be a good thing. We have also seen a lot of start-ups, but it has been noticeable that these are divided into the big start-ups who are able to get off the ground and raise substantial monies – hundreds of millions of dollars – and the more common smaller start-ups who are having great difficulty in raising any money whatsoever.

Nevertheless, I am confident that our industry is going to flourish whilst managers still remember the debacle and therefore, operate as hedge funds. Opportunities going forward will depend upon the ability of the managers to protect capital and select the appropriate strategies.

**Charles Tritton**

Let us put the U.K. in context of both Europe and the U.S. The U.S. is still the dominant player as far as hedge funds and investors are concerned and indeed I think they have probably moved even further ahead than they were pre-crisis. I was talking to a large allocator in the U.S. the other day and they are generally disappointed by the performance of the European hedge fund industry and have increased their U.S. exposure at the expense of their European hedge fund holdings. Their exposure to Asian managers remains static, although they admit that the common factor in Asia is beta.

**London is still very much the dominant location for hedge funds. There has been a lot of talk about Switzerland, Monaco, and various other places within Europe gaining market share, but in terms of AuM they are still small, especially when it comes to where the risk is being taken.**

**I think it is interesting to note that we have Norwegians, Swedes, French, German and English working in our fund, and also that the service providers are still based here in the U.K. I do think if some of the overseas locations, for example Switzerland, would actually scale up their capacity to service our industry better, their market share may grow in the long run. However today the probability that your performance suffers from a move out of London is reasonable high and performance remains the most important asset of a hedge fund.**



Charles Tritton

So, on a global basis, Europe has disappointed. As far as Europe is concerned, London is still very much the dominant location for hedge funds. There has been a lot of talk about Switzerland, Monaco, and various other places within Europe gaining market share, but in terms of AuM they are still small, especially when it comes to where the risk is being taken.

I think it is interesting to note that we have Norwegians, Swedes, French, German and English working in our fund, and also that the service providers are still based here in the U.K. I do think if some of the overseas locations, for example Switzerland, would actually scale up their capacity to service our industry better, their market share may grow in the long run. However today the probability that your performance suffers from a move out of London is reasonable high and performance remains the most important asset of a hedge fund.

**Julian Treger**

I agree London is dominant in European hedge funds, but the tax regime is unhelpful and is eroding its dominance. There is definitely cause for the government to look at these issues again, as tax is a very important consideration for nearly all concerned.

**I agree London is dominant in European hedge funds, but the tax regime is unhelpful and is eroding its dominance. There is definitely cause for the government to look at these issues again, as tax is a very important consideration for nearly all concerned.**

**Particularly in Europe, the fixation on microsecond liquidity is, however, not beneficial, and I believe people in the U.S. are quite puzzled by this. A lot of money is flowing into UCITS, but in some instances performance is disappointing and up to 50% lower than what the true hedge fund should be doing. Investors in Europe need to accept different risk profiles for different duration investments. Moving over a bit into medium-term investments will present them interesting opportunities, because it is a much less crowded space. If you are going to be in a microsecond fund, those are not going to be able to perform as easily, because you need some time for these investments to mature.**



Julian Treger

From an activist perspective, we see the UK market becoming increasingly diversified, less concentrated, which is an interesting development. This fixation on higher liquidity we have had for the past couple of years means we have much more open share registers now. It is not anymore required to own 25% of a company to try and make a difference, you can do that now owning 5% or 10%, and that makes our strategy easier to execute.

Particularly in Europe, the fixation on microsecond liquidity is, however, not beneficial, and I believe people in the U.S. are quite puzzled by this. A lot of money is flowing into UCITS, but in some instances performance is disappointing and up to 50% lower than what the true hedge fund should be doing. Investors in Europe need to accept different risk profiles for different duration investments. Moving over a bit into medium-term investments will present them interesting opportunities, because it is a much less crowded space. If you are going to be in a microsecond fund, those are not going to be able to perform as easily, because you need some time for these investments to mature.

### Loic Fery

Regarding the U.K. perspective, one of the two strong advantages of London that will probably not change in the short-term is people - investment management is all about people, it is about talent. We have here an abundance of talent, which is important. However, by definition, a hedge fund is very scalable, so when a firm becomes more established and has built up all the necessary core talent, that is when the idea of moving away can become tempting. If the fiscal policy and other macro factors continue to deteriorate, things may come close to the point where most of the established firms think about or execute a backup plan.

**One of the two strong advantages of London that will probably not change in the short-term is people - investment management is all about people, it is about talent. We have here an abundance of talent, which is important. However, by definition, a hedge fund is very scalable, so when a firm becomes more established and has built up all the necessary core talent, that is when the idea of moving away can become tempting. If the fiscal policy and other macro factors continue to deteriorate, things may come close to the point where most of the established firms think about or execute a backup plan.**

**Apart from the great talent pool, the U.K. has a strong regulator. Having dealt with the French, the Irish and Luxembourg regulators, we found the U.K. FSA by far the most professional.**

Loic Fery



Apart from the great talent pool, the U.K. has a strong regulator. Having dealt with the French, the Irish and Luxembourg regulators, we found the U.K. FSA by far the most professional. I think it is very important that investors can take a lot of comfort in what the FSA does, but even for ourselves as asset managers it is good to have a good regulator, someone that can turn around things quickly, who has clear deadlines and is able to answer questions.

Regarding UCITS, I believe the Luxembourg regulators can do better in their approach. A lot of politicians have entered the debate trying to further regulate the industry - I mean the concept is good, they should all focus on finding the right framework for the benefit for the investor. The strong inflows into UCITS is just creating the next bubble and, hopefully, this bubble will not explode too soon. So far we have resisted launching a UCITS III despite the demand from investors. This might be a development for our firm in the second half of the year, but it will not be a tracking error product only trying to replicate the performance of an offshore fund.

### Morten Spenner

London is still a very prominent hedge fund center, and you can see that in the number of new launches as well. Going forward, though, the U.K. has to consider how the country continues to invest in the industry and encourage the industry. There has been, more recently, a lot of disquiet about the industry and it has been more seen as a negative rather than as a positive. If this dynamic continues for the medium to long-term, then the industry will have to react to it.

London is still a very prominent hedge fund center, and you can see that in the number of new launches as well. Going forward, though, the U.K. has to consider how the country continues to invest in the industry and encourage the industry. There has been, more recently, a lot of disquiet about the industry and it has been more seen as a negative rather than as a positive. If this dynamic continues for the medium to long-term, then the industry will have to react to it.

Of course, it cannot do that quickly because the mobility of humans is a slow thing. That said, we have seen clear examples of hedge funds 'voting with their feet'.

I also want to bring up a topic that I believe has become a real concern in our industry. I think that today, many investors can be very confused as to what hedge fund means. In the 'old days', things were pretty straightforward. A hedge fund was typically a BVI or a Cayman company most often managed out of London or New York.



**Morten Spenner**

Today, investors are faced with an array of "hedge funds" and structures including managed accounts, managed account platforms, UCITS, onshore funds etc. that I believe complicate matters greatly for investors as they find differentiation difficult. I believe that investors are essentially looking for the same three things as before: talented managers, great interest alignment, and a robust business structure. That said, the variety of structures and 'wrappings' are making it confusing for them to appreciate the genuine hedge fund universe.

Of course, it cannot do that quickly because the mobility of humans is a slow thing. That said, we have seen clear examples of hedge funds 'voting with their feet'. We have to contrast that potential trend with another development we have noticed, which is that there are more and more managers that are what I would call "local". For example, a lot of Asian managers set up shop in Asia now. When it comes to Europe, you can also see managers setting up in different regions here, just like we have seen it in the U.S. where some managers have moved or set up outside of New York. This is quite possible, and you can generate good returns despite not being next to Wall Street or Fifth Avenue.

I also want to bring up a topic that I believe has become a real concern in our industry. I think that today, many investors can be very confused as to what hedge fund means. In the 'old days', things were pretty straightforward. A hedge fund was typically a BVI or a Cayman company most often managed out of London or New York.

Today, investors are faced with an array of "hedge funds" and structures including managed accounts, managed account platforms, UCITS, onshore funds etc. that I believe complicate matters greatly for investors as they find differentiation difficult. I believe that investors are essentially looking for the same three things as before: talented managers, great interest alignment, and a robust business structure. That said, the variety of structures and 'wrappings' are making it confusing for them to appreciate the genuine hedge fund universe. Perhaps the UK and London regulators and the industry could do more to help support the industry by educating investors and by supporting hedge funds and structures delivering the three mentioned features

**Loic Fery**

For me, the definition of a hedge fund would be a company that manages a single offshore fund. This is what I would call a true hedge fund. The reality of the current market is that most alternative firms are sophisticated asset-managers running managed accounts, UCITS, Cayman hedge funds, QIF, SIF and advisory mandates.

**Eoin Murray**

As an emerging manager, it is important for us to be in one of the main hedge fund centres in order for us to continue the process of building critical mass in our business while at the same time generating performance and protecting capital. For us, being headquartered in London is absolutely vital to maintain exposure to global allocators.

**As an emerging manager, it is important for us to be in one of the main hedge fund centres in order for us to continue the process of building critical mass in our business while at the same time generating performance and protecting capital. For us, being headquartered in London is absolutely vital to maintain exposure to global allocators.**

**Eoin Murray**



The UCITS question is an interesting one. Whilst there are many advantages with respect to UCITS, we certainly have a fear that many investors see them as the answer to some of their liquidity mismatch issues. I do have a big concern that UCITS are used for the wrong kind of investment strategy, for example an emerging markets, small-cap equity manager offering weekly or better liquidity, which is simply not appropriate for the underlying investment. Equally there are strategies that are well-suited to the structure but investors should not assume that a UCITS structure will necessarily offer greater downside protection.

**Dermot Butler**

I probably should not start this, but I personally think that UCITS have been miss-sold. I think they are going to become one of the big miss-selling themes in the hedge fund industry over the past 18 months or so. I believe they have been sold because they are regulated and therefore they are “safe” which is simply not the case. There were, I think, three or four UCITS funds that lost money through Madoff. Alright, the custody arrangements are supposed to make such issues safe in Europe, but I believe - and correct me if I am wrong here - HSBC settled at US\$62.5 million out of US\$312 million. That does not seem to make it to terribly safe.

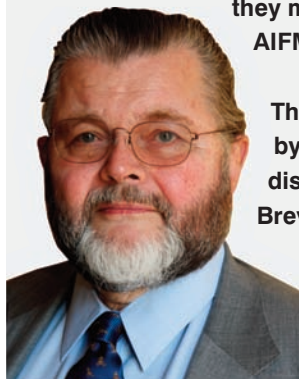
I do not think anybody actually believes that UCITS ensure you have a competent manager. The danger is that people using UCITS now may say “oh, it is regulated - tick the box - that is safe.”

From the managers' side, I believe a lot of them started UCITS funds because of the Draft AIFM Directive, published in April 2009. If you had a UCITS fund, you were exempted from the AIFM Directive, which made people feel they must have a UCITS fund, at least during that confusing period where nobody knew how the final AIFM directive would eventually look.

**I personally think that UCITS have been miss-sold. I think they are going to become one of the big miss-selling themes in the hedge fund industry over the past 18 months or so. I believe they have been sold because they are regulated and therefore they are “safe” which is simply not the case. There were, I think, three or four UCITS funds that lost money through Madoff. Alright, the custody arrangements are supposed to make such issues safe in Europe, but I believe - and correct me if I am wrong here - HSBC settled at US\$62.5 million out of US\$312 million. That does not seem to make it to terribly safe.**

**I do not think anybody actually believes that UCITS ensure you have a competent manager. The danger is that people using UCITS now may say “oh, it is regulated - tick the box - that is safe.”**

**From the managers' side, I believe a lot of them started UCITS funds because of the Draft AIFM Directive, published in April 2009. If you had a UCITS fund, you were exempted from the AIFM Directive, which made people feel they must have a UCITS fund, at least during that confusing period where nobody knew how the final AIFM directive would eventually look.**



**Dermot Butler**

**There were also some misconceptions on the managers' side. Some of them have thought that just by having a UCITS they will be able to sell it to the retail market. The truth is that you must have distribution lined up and in place before you even launch a UCITS fund. Of course, if you are a Brevan Howard or a Sloane Robinson, that means if you are large enough that you can divert investment into a UCITS and you start your UCITS fund with \$200 million or \$300 million, then your fund will have a smooth start.**

If the 2009 Draft version of the AIFM Directive had been adopted, then, of course, nobody would be investing in Europe anyway. If I recall correctly, there was a situation where not only was it illegal to sell your non-EU fund to members of the European community - whether individual or corporate - but they were not going to be allowed to buy your fund if they wanted to. Therefore, some of the things they put in there were quite ridiculous.

But there were also some misconceptions on the managers' side. Some of them have thought that just by having a UCITS they will be able to sell it to the retail market. The truth is that you must have distribution lined up and in place before you even launch a UCITS fund. Of course, if you are a Brevan Howard or a Sloane Robinson, that means if you are large enough that you can divert investment into a UCITS and you start your UCITS fund with \$200 million or \$300 million, then your fund will have a smooth start. But for most funds that come in with \$30 million, \$40 million or \$50 million, things look a bit different as they have to bear both the set up costs for the UCITS funds and the costs for running it and, on top of that, deal with the restrictions that disallow most hedge fund strategies. If a manager gets a good deal with a bank that will promote the fund, that is a different story too, however generally the challenge of finding money for small managers has not changed much in the last two years.

### **Melissa Hill**

We run a UCITS fund that we started this year. I think Dermot made some very good points. In addition, it is very important for investors to be educated as to the difference between what I would call pure UCITS funds and synthetic UCITS strategies.

As market neutral manager, our UCITS fund mirrors the offshore fund and the tracking error is basis points. For us, and I think for any other manager like us, it is a good business decision to launch a UCITS because it does open other avenues of capital to alternative managers and enables us to pitch for money allocated to an equity bucket rather than an alternative one.

**It is very important for investors to be educated as to the difference between what I would call pure UCITS funds and synthetic UCITS strategies.**

**As market neutral manager, our UCITS fund mirrors the offshore fund and the tracking error is basis points. For us, and I think for any other manager like us, it is a good business decision to launch a UCITS because it does open other avenues of capital to alternative managers and enables us to pitch for money allocated to an equity bucket rather than an alternative one.**

**With UCITS we can target the IFA market, private wealth management and high net-worth market, which is very difficult to do with offshore funds, particularly for tax reasons.**

**One of the things we learned post 2008 is that diversification of the investor base is absolutely paramount. Alternative asset managers need investors with different time horizons and holding periods on their investments. What we have seen so far of retail type investors is that they are actually quite sticky; they hold their investments for quite a long time and seem to react more slowly than the professional hedge fund market to short term news.**

**From our perspective, UCITS is a success. We are currently offering daily liquidity which, admittedly, added work operationally therefore we hired more people. If you compare it dollar-for-dollar with the offshore funds, the offshore fund is higher margin to the business but we wanted to be able to offer flexible investment solutions to our clients and it is another choice alongside the managed accounts that we run.**

**Melissa Hill**



It is correct that the retail market is hard to penetrate, unless you have got some kind of partnership arrangement in place. But you also have the opportunity to access our own domestic market here, and

help London to be an even better place for hedge fund managers, as with UCITS we can target the IFA market, private wealth management and high net-worth market, which is very difficult to do with offshore funds, particularly for tax reasons.

One of the things we learned post 2008 is that diversification of the investor base is absolutely paramount. Alternative asset managers need investors with different time horizons and holding periods on their investments. What we have seen so far of retail type investors is that they are actually quite sticky; they hold their investments for quite a long time and seem to react more slowly than the professional hedge fund market to short term news.

From our perspective, UCITS is a success. We are currently offering daily liquidity which, admittedly, added work operationally therefore we hired more people. If you compare it dollar-for-dollar with the offshore funds, the offshore fund is higher margin to the business but we wanted to be able to offer flexible investment solutions to our clients and it is another choice alongside the managed accounts that we run.

**Dermot Butler**

I cannot argue with any of that - it is horses for courses. A strategy like yours can work well in UCITS funds. UCITS have been a remarkable retail long only product since they were introduced in 1986, but I think in the last couple of years a number of people have been tempted into UCITS who shouldn't, and on top of this, UCITS funds can be expensive.

I also believe that the stampede into UCITS has been reduced this year, since the revised AIFM document was published in November, which proved to be something of a damp squib. Any American manager who has a Cayman fund can now apparently carry on using the private placement regime to market to investors in Europe. It means that nothing has really changed except a whole lot of worry.

**Joe Taussig**

Regarding London, not only is capital mobile, but talent is also mobile. I live in Switzerland, so I have watched some of this migration, and by setting up two banks in Malta, I have also seen an even different form of migration. Some of those with London roots who are willing to move physically - like Philippe Jabre or Alan Howard - have physically moved. Some of those with London roots who are not willing to physically move have set up an asset management business in Malta and provide research from London. With the new Malta - U.S. tax treaty, we are now seeing U.S. based managers setting up in Malta, just like their British brethren.

It will be interesting to see what happens in the U.S., because for years the U.S. manager could defer his fees, and the vast majority of wealth from hedge fund managers in the Forbes 400 sits in their offshore deferred comp. But the managers lost this benefit in the TARP Bill. There is a tremendous amount of pressure, they all have to repatriate by 2017, and they cannot continue to defer the fees.

As such, the economics of the business have changed drastically in the U.S. On top of that, the managers could lose the partnership attribution. I do not know if you are aware of it, but in America, the hedge fund manager's fees on his funds are considered to be a partnership attribution, offering him the same characteristics for capital gains purposes that the investors enjoy. For example if you are a long/short equity or deep value and hold your positions for years, you are getting capital gains treatment on fees, so to speak. There is a big movement now to change that.

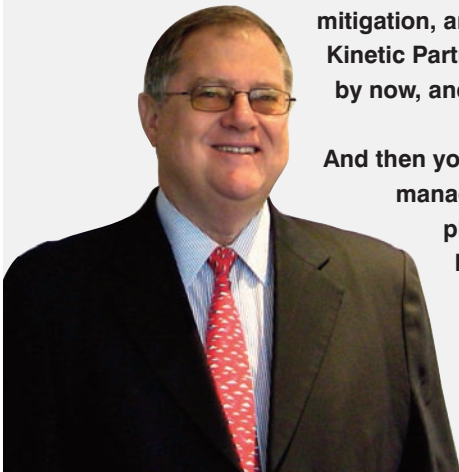
I do not think the Americans are going to take some of the steps that Londoners have, because in general it is psychologically difficult for Americans to move overseas and they do not enjoy the work permitting rights of Schengen. Before 9/11 only 10% of Americans had passports. But since taxes are a huge drag on the compounding effect of wealth, some will take some sort of action. To illustrate this point, assuming there would have been no deterioration in performance, if Berkshire Hathaway had been based in Bermuda, it would be worth \$6 trillion today as opposed to just about \$150 billion (ex-Burlington Northern). That is how much tax takes out of compounding. I would say a significant amount of our clients spend a significant amount of their brain cells on tax mitigation, and I see the same thing here in Europe. I think David Butler from advisory firm Kinetic Partners told me they have moved something close to 100 managers to Switzerland by now, and most of them are coming from London.

Not only is capital mobile, but talent is also mobile. I live in Switzerland, so I have watched some of this migration, and by setting up two banks in Malta, I have also seen an even different form of migration. Some of those with London roots who are willing to move physically - like Philippe Jabre or Alan Howard – have physically moved. Some of those with London roots who are not willing to physically move have set up an asset management business in Malta and provide research from London. With the new Malta – U.S. tax treaty, we are now seeing U.S. based managers setting up in Malta, just like their British brethren.

It will be interesting to see what happens in the U.S., because for years the U.S. manager could defer his fees, and the vast majority of wealth from hedge fund managers in the Forbes 400 sits in their offshore deferred comp. But the managers lost this benefit in the TARP Bill. There is a tremendous amount of pressure, they all have to repatriate by 2017, and they cannot continue to defer the fees.

As such, the economics of the business have changed drastically in the U.S. On top of that, the managers could lose the partnership attribution. I do not know if you are aware of it, but in America, the hedge fund manager's fees on his funds are considered to be a partnership attribution, offering him the same characteristics for capital gains purposes that the investors enjoy. For example if you are a long/short equity or deep value and hold your positions for years, you are getting capital gains treatment on fees, so to speak. There is a big movement now to change that.

I do not think the Americans are going to take some of the steps that Londoners have, because in general it is psychologically difficult for Americans to move overseas and they do not enjoy the work permitting rights of Schengen. Before 9/11 only 10% of Americans had passports. But since taxes are a huge drag on the compounding effect of wealth, some will take some sort of action. To illustrate this point, assuming there would have been no deterioration in performance, if Berkshire Hathaway had been based in Bermuda, it would be worth \$6 trillion today as opposed to just about \$150 billion (ex-Burlington Northern). That is how much tax takes out of compounding. I would say a significant amount of our clients spend a significant amount of their brain cells on tax mitigation, and I see the same thing here in Europe. I think David Butler from advisory firm Kinetic Partners told me they have moved something close to 100 managers to Switzerland by now, and most of them are coming from London.



And then you have people who do not want to physically move from London setting up their management company in Malta. There are at least 10 funds in the \$3 billion to \$5 billion plus range that have moved their management companies to Malta. Not the human beings, but they place the orders through the trading desk in Malta and have some kind of transfer pricing on research to allow them to live in their home country and keep the kids at school etc. Those things can really affect London over time.

Joe Taussig

And then you have people who do not want to physically move from London setting up their management company in Malta. There are at least 10 funds in the \$3 billion to \$5 billion plus range that have moved their management companies to Malta. Not the human beings, but they place the orders through the trading desk in Malta and have some kind of transfer pricing on research to allow them to live in their home country and keep the kids at school etc. Those things can really affect London over time. Right now London has a great advantage, because it is here that traders can jump from the larger institutions and be entrepreneurial and start their own shop, but if London is not careful, it will wither.

Matthias Knab

The rate of new fund launches is always a good indication about the health and momentum in any hedge fund region. Can you tell us more about those emerging managers – where are they coming from, what strategies do they run? How do they succeed?



OPALESQUE'S GOT

# TALENT

Find countless new ideas, opportunities and investment talent in the new:

Emerging Manager  
Fund Database

A SQUARE (Alternative Alternatives)  
Fund Database

- Performance
- Diversification
- Uncorrelated
- Alternative
- Alpha

Logon now at [www.opalesquesolutions.com](http://www.opalesquesolutions.com)

Opalesque subscribers get free access!

## Dermot Butler

If you go back to the years before 2008, a launch with US\$100 million was considered petty cash, however now, getting US\$100 million can be a life long ambition. If a manager is any good and can start with the support of a capable distribution network, he may still start a fund with \$200 or \$300 million, but for the ones smaller than US\$100 million, growing assets is still very difficult.

The biggest investor group in the world, the famous “family and friends” only make very small ticket investments and therefore a lot of managers really start with very small sized funds. Under such conditions, is it both very difficult to even start a fund, because it is uneconomic, and because of the chicken-egg situation when it comes to money raising. We all know about it. You need a track record before you can get any money, and you got to have some assets before anyone else will put some money with you, and it goes on like that. As fund administrators we are seeing a lot of that.

The silver lining we are beginning to see is the reemergence of the high net worth and family office investors who are coming back into this market. These investors were originally the founders of the American hedge fund industry, and they have certainly come back in the States, and now also in Asia and here in Europe we see a greater emergence of the private family money coming into hedge funds. Hopefully they keep on doing this with that same old attitude of taking greater risk for a greater reward.

**At Custom House we launched a platform in Malta called the Nascent Fund, designed to help emerging managers to get off the ground. The cost of setting up a stand-alone fund is probably about \$30,000 or \$35,000 if you are very careful, but if you decide that you need a certain big name lawyer or advisor on your letterhead, then you are spending anything up to \$150,000 to set up your fund. For a large manager it is fine to do so, but for a small manager who aims to hopefully raise \$30 million but who will probably start with less than \$10 million, such costs can be crippling. And on top of this, your operation has to bear the costs of running your fund, which can be anything from \$80,000 to \$120,000 a year, even at really tight prices. Again, this is no issue for a larger fund, but \$120,000 of a \$10 million fund is very expensive – i.e. 1.2% p.a.**

**The Custom House Nascent Fund is a Professional Investor (umbrella) Fund (“PIF”) in Malta that has subsidiary funds, which are fully segregated umbrella “legs” that enable start up managers to buy or lease a leg (sub-fund) for just 8,000 Euros. The whole solution is packaged and structured; they just plug in their strategy. We have the bankers and the fund continues to use their prime broker. We have a local auditor in Malta and we charge a very low fee for administration in the first year, which is frankly a loss leader.**



Dermot Butler

At Custom House we launched a platform in Malta called the Nascent Fund, designed to help emerging managers to get off the ground. The cost of setting up a stand-alone fund is probably about \$30,000 or \$35,000 if you are very careful, but if you decide that you need a certain big name lawyer or advisor on your letterhead, then you are spending anything up to \$150,000 to set up your fund. For a large manager it is fine to do so, but for a small manager who aims to hopefully raise \$30 million but who will probably start with less than \$10 million, such costs can be crippling. And on top of this, your operation has to bear the costs of running your fund, which can be anything from \$80,000 to \$120,000 a year, even at really tight prices. Again, this is no issue for a larger fund, but \$120,000 of a \$10 million fund is very expensive – i.e. 1.2% p.a.

The Custom House Nascent Fund is a Professional Investor (umbrella) Fund (“PIF”) in Malta that has subsidiary funds, which are fully segregated umbrella “legs” that enable start up managers to buy or lease a leg (sub-fund) for just 8,000 Euros. The whole solution is packaged and structured; they just plug in their strategy. We have the bankers and the fund continues to use their prime broker. We have a local auditor in Malta and we charge a very low fee for administration in the first year, which is frankly a loss leader.

There is an operational fee, which is just a flat 20 basis points for all ongoing organizational costs,

except administration, audit and trading related costs. In the second year, we would will increase the fee a bit and again in the third year. At the end of the third year, or even before that, the fund would aim to have grown to a standalone fund size. At that point, if they have done well, they should leave the umbrella fund and continue raising money. They already have their track record through their share class in the Nascent Fund and can easily setup their own fund. And if they have not been doing well, at the end of the two years, they probably should go back to the farm anyway. We are really committed to get managers off the ground, and hopefully, one out of every ten will be a winner.

**Matthias Knab**

## **How many managers do you have now in the Nascent Fund?**

**Dermot Butler**

We have got about eight of them, either in the fund or the pipeline, and we are planning to add a U.S. version soon and also a Shariah version. We are beginning to find a lot of interest in Shariah funds from start up managers in Malaysia and in Singapore.

**Melissa Hill**

One of the reasons why it has become so much harder to set up a new fund is the consolidation in the fund of hedge funds industry, particularly in Switzerland and France. Many firms have not survived the crisis as independents and it was these businesses who used to be among the entrepreneurial early day investors for hedge fund start-ups. Overall, the industry has become so much more institutionalized. In illustration I believe the figure that came out at the end of last year was that some 70% of hedge fund assets are run by 100 managers.

This means the business has shifted hugely in favor of the buying power of the institutions and with that has come the highly increased levels of operational due diligence that are required, which puts small managers at a competitive disadvantage. I see this as a rather negative development, because really one of the great things about the hedge fund industry when it started was that it was highly entrepreneurial, and small, but talented; groups of people could build very robust businesses and do well with relatively low assets. Going forward, this will be much tougher without some form of strategic backing.

**Loic Fery**

Maybe I can relate some of my experience, because we still consider ourselves emerging managers as Chenavari is four years old. At the launch, I believe we made the good choice to over-invest heavily in our infrastructure: we started with only \$35 million assets under management but we structured the firm as if we were a \$500 million fund. This meant to a certain extent we over-invested, and we accepted to run at a higher cost base than revenues for an initial period of time. But, it allowed us

**Maybe I can relate some of my experience, because we still consider ourselves emerging managers as Chenavari is four years old. At the launch, I believe we made the good choice to over-invest heavily in our infrastructure: we started with only \$35 million assets under management but we structured the firm as if we were a \$500 million fund. This meant to a certain extent we over-invested, and we accepted to run at a higher cost base than revenues for an initial period of time. But, it allowed us to scale our business faster and helped us attract investors because of the way we were set up and that we had decided that “being a few smart guys with Bloomberg terminals in a garage was simply not us”. Beyond our performance, which helped too, this strategic decision really allowed us to grow.**



**Our firm has grown a lot since then, and having the right infrastructure from day 1 was key, because certain boxes have to be ticked before the money flows into any asset manager. Of course, performance is important, but the truth is that today sophisticated investors spend more time with the operational DDQ than with the investment team of the manager.**

**Finally, I don't think we should un-tag ourselves as an emerging manager, as this is a spirit and we have kept it. As an example, despite strong investor demand, we decided to close one of our funds to new inflows recently.**

**Loic Fery**

to scale our business faster and helped us attract investors because of the way we were set up and that we had decided that “being a few smart guys with Bloomberg terminals in a garage was simply not us”. Beyond our performance, which helped too, this strategic decision really allowed us to grow.

Our firm has grown a lot since then, and having the right infrastructure from day 1 was key, because certain boxes have to be ticked before the money flows into any asset manager. Of course, performance is important, but the truth is that today sophisticated investors spend more time with the operational DDQ than with the investment team of the manager.

Finally, I don't think we should un-tag ourselves as an emerging manager, as this is a spirit and we have kept it. As an example, despite strong investor demand, we decided to close one of our funds to new inflows recently. We have decided not to be running a commercial operation where size matters; we care about delivering steady performance and make our investors happy. So I hope we can remain an emerging strong manager for a long time: it is the same thing when we talk about emerging markets like China and India who by now are also pretty much emerged!

### **Eoin Murray**

It is still a difficult environment for capital raising for emerging managers, despite some of the encouraging headlines that we see in the papers. I think when they actually refer to capital allocations being made to small managers, what they really mean is managers with over \$500 million, which is not small from where I am standing! Eventually, investors will need to differentiate and diversify away from the ‘brand’ name hedge funds and re-enter the emerging manager space, challenging the larger funds and ensuring the continued growth and development of the industry as a whole.

Coming from an institutional background as well, we made decisions like Loic when we setup to put in place the right infrastructure, the right setup with the recognized top-tier service providers, so that we would meet the demands of the institutional market segment. Over the last 3 years we have been able to refine policies and procedures to ensure we continue to meet the highest institutional demands with our infrastructure and, importantly, this includes oversight by each of the founding partners of the critical business functions of investment, risk, operations and compliance and client service.

### **Dermot Butler**

Just a small word of caution regarding what we have called here “the brand name service providers”: a lot of them are not really interested to take on small managers. I heard a story the other day from a manager who had been running several billion before the crash, but is now at around \$400 million, and his administrator threw them out. Well, \$400 million is a lot of fees for an administrator and I think it is very arrogant behaviour to dump them out of hand.

### **Morten Spenner**

In the current environment, there is a lot of fear of making mistakes on the investors' side, as there are people on the other end wanting the capital... However, we do see with some regularity people setting up shop. They have to be much more careful these days as it takes much longer to establish a firm today. Managers also have to be more creative with how they structure fees or liquidity, for example. I think some people have come up with interesting solutions on the fee side.

I think that it will continue to be difficult for emerging managers and some start-ups will not even come off the ground as a result. Investors' behavior in terms of acceptance and risk taking will continue to shift slowly, bit by bit as we have seen. We are all aware of the fact that recently the majority of capital have moved to brand names as well as to regulated solutions, and that has also been the case within fund of hedge funds. This is expected to change – we are seeing evidence of this already – but it will not change to the degree that the industry will be “flooded” with new hedge funds. The standards demanded today are simply too high for that. Those who actually start out now tend to be more committed; they have capital for longer and have better thought about how to approach their audience. The newer managers we have invested in over the last two years all have very strong stories. There are not so many of them, but their quality has increased which in the end will reflect well on the industry.

Money has moved out of fund of hedge funds for many different reasons. Our Chairman Albert Fuss notes with some humor that after having been in business with IAM for 22 years creating tailor-made solutions focused on mid-sized hedge funds sourced across the globe, it is ironic that now people want to talk to him about it. But better late than never!

## Julian Treger

It is clear that smaller funds are the lifeblood of the industry and there is always a cycle of creation and destruction. As the rules and regulations for investment banks are changing now, a lot of the macro traders spin out and set up funds. Another dynamic could be that if some of the larger funds do not perform in due course, people with great pedigrees will leave from there and set up their own fund. For any new fund starting out now, I believe it will be very helpful to follow distinct themes. As the world always changes, a plethora of new themes always comes up, it could be anything from agricultural funds or backing Facebook.

**It is clear that smaller funds are the lifeblood of the industry and there is always a cycle of creation and destruction. As the rules and regulations for investment banks are changing now, a lot of the macro traders spin out and set up funds. Another dynamic could be that if some of the larger funds do not perform in due course, people with great pedigrees will leave from there and set up their own fund. For any new fund starting out now, I believe it will be very helpful to follow distinct themes.**

**There will always be new ideas on the theme side, but also the way in which the industry develops new products will change. I believe we will see a higher emphasis on incubation and seeding platforms, and people will be more attracted by firms that have multi-strategy products which allow them to rely on the central service backbone, which is just another form of incubation.**

Julian Treger



Therefore, there will always be new ideas on the theme side, but also the way in which the industry develops new products will change. I believe we will see a higher emphasis on incubation and seeding platforms, and people will be more attracted by firms that have multi-strategy products which allow them to rely on the central service backbone, which is just another form of incubation. For example, someone came to me a few months ago with an idea about Japan, saying that things will be okay this year, but next year Japan may face more issues because of demographics, etc. We are going to back him and give him a chance, and I believe this cycle of creation and innovation will always be there.

## Morten Spenner

I agree with Julian's point about change. As humans, it appears, we have a trait that says, "the world is like what we can see today and it will continue being like what we can see today" and simply just extrapolate from there. I see this as a danger the industry may suffer from, as more inexperienced consultants get involved or "basic ratings" becomes the way to assess the quality of managers. Partly, this development goes to explain the recent shift towards safety in numbers and brand names, etc. But I would very much agree with Julian that if you look at the history of the hedge funds, there have been some spectacularly large funds out there that have gone out of favor and the industry has then been developed by emerging managers.

The industry itself, investors and the media need to contend with what constitutes a hedge fund. Some appear to borrow more from the 'standards' of the long-only world and emphasize size, brand, and operational capacity. Others – like IAM – are in the more old-fashioned camp focused on exceptional investment talent and risk management expertise, genuine alignment of interest combined with a robust business set-up.

## Charles Tritton

Everyone is obsessed by new launches, but I personally am much more fixated by closures; funds that shut down, that make compulsory redemptions or fund managers who close their funds to join multi-strategy funds and I suspect you'll see much more going on here than the amount of new fund launches. For example, a manager who ran \$150 million in his own fund very successfully recently gave it up to join us. The reason why he did it is, because he can spend more time managing his portfolio and has more stable capital and should earn more with us than running his \$150 million fund.

The background here was that the strategy was capacity constrained. Of course, if you are a macro-trader or CTA who can run billions of dollars and manage to grow your assets, your options are much

greater, but the reality is that the vast majority of people who can generate consistent alpha do have a capacity constraint and in these cases the risk reward is against you launching your own fund.



**Everyone is obsessed by new launches, but I personally am much more fixated by closures; funds that shut down, that make compulsory redemptions or fund managers who close their funds to join multi-strategy funds and I suspect you'll see much more going on here than the amount of new fund launches. For example, a manager who ran \$150 million in his own fund very successfully recently gave it up to join us. The reason why he did it is, because he can spend more time managing his portfolio and has more stable capital and should earn more with us than running his \$150 million fund.**

**The background here was that the strategy was capacity constrained.**

**Charles Tritton**

I would argue that the universe of management companies based in Europe is actually shrinking, particularly on an asset-weighted basis. Therefore I think that we will sadly follow a similar distribution profile of assets as experienced by the traditional asset management companies. This is why you will see fewer new hedge fund management companies launched in the future. It is too expensive and time consuming relative to the risks. In addition the ongoing costs of regulation, risk management and capital requirements seem to be permanently increasing.

**Mark Leader**

I am encouraged by the Nascent Fund structure Dermot refers to as it allows the start-up managers to develop their businesses in an appropriate manner and timescale without the impact of nearer-term cost pressures undermining their decision making (especially in the early days). However, we do see conditions in the industry becoming tougher for smaller sized managers with mediocre performance. The issue faced for these firms is the need to raise assets to cover the ever-increasing costs of being in business. Costs which have taken a step higher as a result of recent scandals, intensifying regulations, increasing demands for transparency and compliance with various standards.

**Dermot Butler**

Regulatory costs, the cost of complying with new regulation is building up rapidly so fast that almost nobody has really realized the aggregate cost. I read an article on The UK Bribery Act, I think it came from KPMG, and they cited one manager who said it was going to cost him a million a year just to make sure that they were doing the right things and that all their staff understood and monitored everything about bribery. These are horrifying costs, aren't they? And the other one was the cost of trying to comply with the U.S. FATCA.

**The cost of complying with new regulation is building up rapidly so fast that almost nobody has really realized the aggregate cost. I read an article on The UK Bribery Act, I think it came from KPMG, and they cited one manager who said it was going to cost him a million a year just to make sure that they were doing the right things and that all their staff understood and monitored everything about bribery.**



**Dermot Butler**

**Joe Taussig**

Some years ago, the U.S. passed a law that any interest had to have withholding, and the first thing everybody did was to dump treasury bonds. The lawmakers then had to give the portfolio interest exemption, because they could not afford to have everyone dump their treasuries.

The problem with FATCA is that the legislation is passed, and if anyone holds over \$50,000 in U.S. securities and dies, the qualified intermediaries have to basically tag them for U.S. estate tax purposes.

I think the investors' reaction to that will be that they threaten to or actually dump U.S. securities. I think this will get serious, as it is a completely bone-headed type of legislation as it stands right now.



**Some years ago, the U.S. passed a law that any interest had to have withholding, and the first thing everybody did was to dump treasury bonds. The lawmakers then had to give the portfolio interest exemption, because they could not afford to have everyone dump their treasuries.**

**The problem with FATCA is that the legislation is passed, and if anyone holds over \$50,000 in U.S. securities and dies, the qualified intermediaries have to basically tag them for U.S. estate tax purposes. I think the investors' reaction to that will be that they threaten to or actually dump U.S. securities. I think this will get serious, as it is a completely bone-headed type of legislation as it stands right now.**

**Joe Taussig**

**Dermot Butler**

And it is not just FATCA – there is also the new FBAR Regulations - the problem is now that if you are a U.S. based signatory on a foreign account - for our purposes let's assume a manager sitting in Fairfield County says that he wants to move money from one foreign fund account to another - so a guy at the administrator in our Chicago office gives the instruction and signs it. He then has to report – note: the individual, not the administrator, not the manager, not the fund - the individual has to report to the U.S. government that he, the investor, has this account.

**There is also the new FBAR Regulations - the problem is now that if you are a U.S. based signatory on a foreign account - for our purposes let's assume a manager sitting in Fairfield County says that he wants to move money from one foreign fund account to another - so a guy at the administrator in our Chicago office gives the instruction and signs it. He then has to report – note: the individual, not the administrator, not the manager, not the fund - the individual has to report to the U.S. government that he, the investor, has this account.**

**In the end, what is happening is that a lot of our clients will say, “well, give the instruction in Malta.” And then, we do not have to report. But then again, that is going to make the transfer a bit less efficient.**



**Dermot Butler**

In the end, what is happening is that a lot of our clients will say, “well, give the instruction in Malta.” And then, we do not have to report. But then again, that is going to make the transfer a bit less efficient, because it cannot necessarily get done in the same day unless they are prepared to pay to have somebody sit up all night in Malta. We do run 24/5 through our global office network around the world, but we do not run individual 24-hour offices.

But nevertheless, the costs will be higher, you need more people to get such a transfer done in Malta instead of in Chicago. Also, I think Joe's comment re FATCA bears serious consideration and maybe someone should worry what happens when people start dumping their U.S. investments because of the hassle factor. And that really is a terrible reflection on this ill-considered regulation.

**Matthias Knab**

**This is certainly an unhealthy trend globally. Are there more views about the current developments around regulation, or the future of hedge funds in the U.K.?**

**Mark Leader**

There is one aspect I probably should have raised earlier about one of the strengths of London, which is that a tremendous amount of fundamental stock picking talent is based here. Now, for the reasons that we discussed earlier, the last couple of years has not been a good environment for active stock

selection, but I do think that if we see the dispersion of returns continuing, we are likely to see a return back to a favoring of active fundamentally driven stock picking, together with a recognition that a more passive strategy like ETF investments will be giving you very pedestrian returns.

**A tremendous amount of fundamental stock picking talent is based here. Now, for the reasons that we discussed earlier, the last couple of years has not been a good environment for active stock selection, but I do think that if we see the dispersion of returns continuing, we are likely to see a return back to a favoring of active fundamentally driven stock picking, together with a recognition that a more passive strategy like ETF investments will be giving you very pedestrian returns.**



**The rationale is that an overall index may stagnate, but individual stocks within that index may be generating strong ROE's and cash flow, which if recognized by the market could lead to outperformance. In such a situation the search for talent will be on, and on that basis, I believe London could see further inflows as global investors recognize the wealth of talent there.**

**The other thing to note about London is the importance of its time zone and corporate service you receive when based here.**

**Mark Leader**

The rationale is that an overall index may stagnate, but individual stocks within that index may be generating strong ROE's and cash flow, which if recognized by the market could lead to outperformance. In such a situation the search for talent will be on, and on that basis, I believe London could see further inflows as global investors recognize the wealth of talent there.

The other thing to note about London is the importance of its time zone and corporate service you receive when based here. Being able to deal in Asian markets in the morning and American markets in the afternoon (in what would be a normal working day) is an important advantage that will lead to the continued establishment of global investment firms in London. This is a really important advantage that you simply just cannot compete away.

Just as important is the corporate service Sloane Robinson benefits from in London. In recognition of our longer term investment time horizon companies often like to see us on their shareholder register, which often means that they want to meet with us when they are in London. This is hugely beneficial as it provides us the opportunity to meet senior executives and extract information, which tends to be outside of sell side research.

### **Julian Treger**

I think language as well plays into hands, with English being the language of business. As we pointed out, London and the U.K. as a financial center definitely have some tremendous advantages, but I believe the government needs to recognize and nurture those things rather than take them for granted.

I continue to believe - rather idealistically - that people will be attracted by returns. I think the funds of funds sector needs to really demonstrate that it can create alpha, otherwise they may come under tremendous threat. My take is that institutions will find the markets increasingly trading sideways, because there is just no growth in Europe and in the West, and therefore they will be attracted by hedge funds, which can produce better risk adjusted returns.

Last week, I was in the U.S. meeting with institutional investors, including several endowments. They need to cope with a 5% inflation rate on their general costs. In order to only fund themselves with a 5% return, it still cannot be achieved through a simple fixed income strategy or investing in government bonds. These people are really scratching their heads looking for better solutions. That trend will continue and hedge funds will be the beneficiaries.

The general perception of hedge funds has also become more realistic and positive. If we just go back to pre-2008, we all remember how some people or media fingered out hedge funds as the major sort

of disruptive agents in the financial sector, but in reality many more banks and insurance companies needed to be bailed out than hedge funds.

**Last week, I was in the U.S. meeting with institutional investors, including several endowments. They need to cope with a 5% inflation rate on their general costs. In order to only fund themselves with a 5% return, it still cannot be achieved through a simple fixed income strategy or investing in government bonds. These people are really scratching their heads looking for better solutions. That trend will continue and hedge funds will be the beneficiaries.**

**The general perception of hedge funds has also become more realistic and positive. If we just go back to pre-2008, we all remember how some people or media fingered out hedge funds as the major sort of disruptive agents in the financial sector, but in reality many more banks and insurance companies needed to be bailed out than hedge funds.**

**If you look back the past five or 10 years, hedge funds have created a lot of value, whereas banks and insurance companies, which were seen as safe, conservative havens, have actually destroyed a lot of value for all of us, for their investors and for the tax payers.**

**Julian Treger**



If you look back the past five or 10 years, hedge funds have created a lot of value, whereas banks and insurance companies, which were seen as safe, conservative havens, have actually destroyed a lot of value for all of us, for their investors and for the tax payers.

**Joe Taussig**

I recently read an article saying that the 10 biggest hedge funds returned more earnings to their investors than the six most profitable global banks. I think that is phenomenal. It was my estimate that these 10 hedge funds employ something like 5,000 to 6,000 employees total, and the six banks may be close to one million. Just Citibank alone has 260,000.



**Joe Taussig**

**I recently read an article saying that the 10 biggest hedge funds returned more earnings to their investors than the six most profitable global banks. I think that is phenomenal. It was my estimate that these 10 hedge funds employ something like 5,000 to 6,000 employees total, and the six banks may be close to one million. Just Citibank alone has 260,000.**

**Julian Treger**

Well, this shows that our industry needs to do much better PR as well.

**Eoin Murray**

That is a good point, and I believe it is incumbent on all of us around the table to continue to manage the overall perception of our industry beyond matters of performance. Whether it is real or not, there is a perception out there that we as a collective group dislike transparency, that we do not want to provide liquidity, that we want to remain mysterious but these attributes do not necessarily appeal

**I believe it is incumbent on all of us around the table to continue to manage the overall perception of our industry beyond matters of performance. Whether it is real or not, there is a perception out there that we as a collective group dislike transparency, that we do not want to provide liquidity, that we want to remain mysterious but these attributes do not necessarily appeal to the new investors that are increasingly interested in what we are doing, which include large institutions but also the more medium-sized pension funds. London is well placed to lead the correction of that misperception.**

**Eoin Murray**



to the new investors that are increasingly interested in what we are doing, which include large institutions but also the more medium-sized pension funds. London is well placed to lead the correction of that misperception, which can only be good for the industry.

### **Melissa Hill**

If we can drive the communication agenda up as an industry, then probably also the politicians will be more favorable towards the asset management industry in London; I think that will be very important.

From the investing side, as market cycles are shortening with roving global capital, this will be pointing investors very firmly towards hedge fund investing rather than the traditional long-only managers, as we are better able to cope with risk and the opportunities that come with those shorter market cycles.

### **Mark Leader**

I agree, investors should not lose sight of the quality that exists within the hedge fund industry. It is correct that our sector started off as a very entrepreneurial niche industry, but over time it has become more populated and the concern we had was whether all of these new entrants truly had the talent to deliver. In most cases I think we can say they have, but in the coming few years we should not be surprised to see a gradual attrition of those who don't. However, we note that most people within hedge funds continue to earn their spurs in the traditional relative return investment companies and banks before making the step into the absolute return world.

**We note that most people within hedge funds continue to earn their spurs in the traditional relative return investment companies and banks before making the step into the absolute return world.**



**One of the benefits of this background is that the generally high standard of care that is drilled into these individuals by these institutions is often transferred across into our industry. As one of the founding members of the Hedge Fund Standards Board, this really became quite apparent to us when setting this up. Initially, quite a number of people were concerned that it would be a significant effort to hit the standards proposed. However, it turned out that almost everybody in the industry was already doing everything right in the first place.**

**Mark Leader**

One of the benefits of this background is that the generally high standard of care that is drilled into these individuals by these institutions is often transferred across into our industry. As one of the founding members of the Hedge Fund Standards Board, this really became quite apparent to us when setting this up. Initially, quite a number of people were concerned that it would be a significant effort to hit the standards proposed. However, it turned out that almost everybody in the industry was already doing everything right in the first place. That is a really strong element of the London hedge fund industry that should give people a lot of comfort. When it comes to looking for a safe home for their assets, I believe London is a pretty good place for them.

### **Dermot Butler**

I would endorse your statement about the Hedge Funds Standards Board, because I was Deputy Chairman of AIMA at that time and had a good insight on this important initiative.

I want to share two final thoughts – one on technology the other on the topic of financial frauds and what must be addressed to make this industry safer. As a fund administrator that is active globally, one of the things we consistently come across now is a greater demand for more detailed, more specialized and more customized reporting from managers. Certain managers want to report one type of attribution; other managers want other types of attribution. Doing such customized reports is not difficult, and we are happy to do them, even though at times it can be a bit time consuming to set them it up, but in the end, it is for the investors' benefit too.

Regarding frauds, the one thing that Madoff and more importantly the Petters scandal revealed was the fact that no one in the hedge fund food chain seems to have accepted responsibility for

independently verifying the existence of the assets. Everyone just took the numbers at face value: if the manager said they held these assets - well sure, they have got them!

**Regarding frauds, the one thing that Madoff and more importantly the Petters scandal revealed was the fact that no one in the hedge fund food chain seems to have accepted responsibility for independently verifying the existence of the assets. Everyone just took the numbers at face value: if the manager said they held these assets - well sure, they have got them!**

**Of course, if you have a CTA who uses independent large prime brokers, then you get two independent reports and trade blotters and you reconcile them, and there is not much more needed to prove they got the positions. But where you have an unhealthy relationship like Madoff where his brother, son, or whoever it was who ran the broking and quasi-custodial side, then that does need verification.**

**In the case of Petters, as I understand it, they were putting up monthly loans to fund the inventory of companies like Wal-Mart and Costco. Then they started to raise more money and started to buy other assets, which was not ever part of the investment strategy. With Petters, someone should have checked whether they could identify any assets that had actually been lent against and if they existed at all. I believe the same should apply to almost any illiquid asset. All those assets should get verified.**

**The auditors have not accepted this responsibility, and therefore I would say somebody needs to stand up and do this job, and it is going to cost money.**

**Dermot Butler**



Of course, if you have a CTA who uses independent large prime brokers, then you get two independent reports and trade blotters and you reconcile them, and there is not much more needed to prove they got the positions. But where you have an unhealthy relationship like Madoff where his brother, son, or whoever it was who ran the broking and quasi-custodial side, then that does need verification.

In the case of Petters, as I understand it, they were putting up monthly loans to fund the inventory of companies like Wal-Mart and Costco. Then they started to raise more money and started to buy other assets, which was not ever part of the investment strategy. With Petters, someone should have checked whether they could identify any assets that had actually been lent against and if they existed at all. I believe the same should apply to almost any illiquid asset. All those assets should get verified.

The auditors have not accepted this responsibility, and therefore I would say somebody needs to stand up and do this job, and it is going to cost money. For example, verifying the existence and title of an office block in Bromley is a lot easier and cheaper than it is in Guatemala City, but if you happen to be investing in real estate in Guatemala City, then verification of all assets is vital, and I do not think many people realize this yet. We at Custom House are looking into this as a new service for clients.

**Matthias Knab**

**What inflows are you seeing at the moment? What is it that investors are now looking for?**

**Loic Fery**

In the past two months we saw large inflows coming from the pension world. They started shifting assets from a very directional credit allocation to more market neutral, which corresponds to the core theme of our strategy. On a broader base, at the moment we see two investor groups that are deploying large amounts of money to work within the alternative investment industry: the pensions – European, U.S. and Canadian pensions – on the one hand, and the large family offices which as well have been allocating quite substantially in past few months.



**In the past two months we saw large inflows coming from the pension world. They started shifting assets from a very directional credit allocation to more market neutral, which corresponds to the core theme of our strategy. On a broader base, at the moment we see two investor groups that are deploying large amounts of money to work within the alternative investment industry: the pensions – European, U.S. and Canadian pensions – on the one hand, and the large family offices which as well have been allocating quite substantially in past few months.**

**Loic Fery**

As far as alternative managers are concerned, there is really no receipt for success or failure, but I think there are a couple of principles we should stick to, because they serve us in the long term and represent what investors are looking for.

The first thing is, do what you say and stick to it. That means, if you target a specific niche you are good at with your strategy, stick to that and stay around that. If it is niche by definition, this also means the capacity is small, so do not be afraid to close funds, which we did with one of our funds. We delivered a superb performance and inflows were piling up, but we still closed the fund to protect the longer-term performance for our investors

Second, do not be afraid to share what you do. When we started, our operational paradigm was “let us show what we do”, and we realized quickly that this was not really the standard for all. The standard thinking was rather “well, I have positions and when I disclose them to the market, the market may be attacking it”. But generally, if people want to take the same position as you, your fund will actually benefit. We have no problem if investors want full transparency about our book.

The third point is to manage expectations. There are strategies where you can expect to deliver 8% to 10% on a steady basis, and there are strategies where if you accept more volatility you can deliver 20, 20+, or 25 on the long-run. Fund managers have to be clear with the investor what net performance he can expect. Investors should not assume that because they pay a hedge fund manager 2 and 20 fees that they are going to get 20% net performance.

### **Morten Spenner**

I think in the investor community there has been a real shift away from this notion of buying a product from the alternatives managers out there to wanting to enter into relationships. Today, investors look for people they can trust and who work with and for them, and that includes more customized solutions and reporting, and more time with the manager when due diligence is conducted, etc.

**One of the features investors now tend to accept more is concentration risk. Of course, they need to appreciate the finer details but – once “due diligence” is completed – they view concentration as a positive. The more investors really understand hedge funds and alternatives, as they go through their studies and their investigations, they will come to recognize that hedge funds’ story overall does stack up and that the people on this Roundtable together with our colleagues and peers can add genuine value for them.**

**Morten Spenner**



One of the features investors now tend to accept more is concentration risk. Of course, they need to appreciate the finer details but – once “due diligence” is completed – they view concentration as a positive. The more investors really understand hedge funds and alternatives, as they go through their


studies and their investigations, they will come to recognize that hedge funds' story overall does stack up and that the people on this Roundtable together with our colleagues and peers can add genuine value for them.

**Charles Tritton**

London is clearly the capital of the hedge fund industry in Europe but within it we have two types of companies.

The industry has bifurcated. There are the very large brand names, which are very much being run conservatively and mainly for fees, and then you have the more traditionally run hedge fund boutiques, which are focused on performance. London has both of these models in abundance.

Investors have to remember that if they can identify firms, large or small, which have a process for compounding returns over the good and bad times you will outperform virtually all asset classes, and that is why the hedge fund industry, despite all its present challenges, has an extremely healthy future.



**The industry has bifurcated. There are the very large brand names, which are very much being run conservatively and mainly for fees, and then you have the more traditionally run hedge fund boutiques, which are focused on performance. London has both of these models in abundance.**

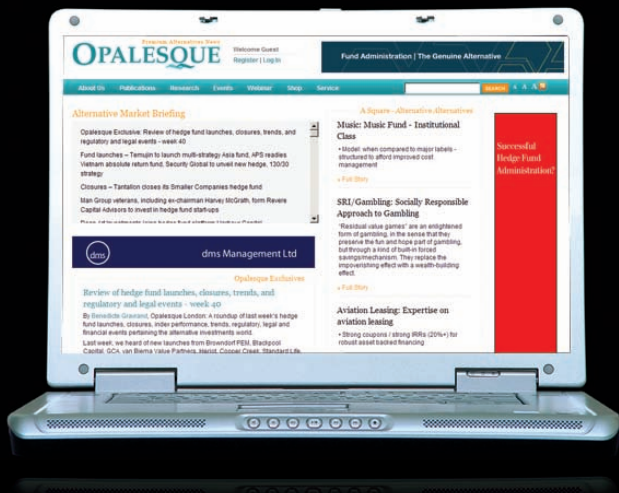
**Investors have to remember that if they can identify firms, large or small, which have a process for compounding returns over the good and bad times you will outperform virtually all asset classes, and that is why the hedge fund industry, despite all its present challenges, has an extremely healthy future.**

**Charles Tritton**

# accurate

## professional reporting service

No wonder that each week, Opalesque publications are **read by more than 600,000 industry professionals in over 160 countries**. Opalesque is the only daily hedge fund publisher which is actually read by the elite managers themselves



**Opalesque Islamic Finance Briefing** delivers a quick and complete overview on growth, opportunities, products and approaches to Islamic Finance.

**Opalesque Futures Intelligence**, a new bi-weekly research publication, covers the managed futures community, including commodity trading advisers, fund managers, brokerages and investors in managed futures pools, meeting needs which currently are not served by other publications.

**Opalesque Islamic Finance Intelligence** offers extensive research, analysis and commentary aimed at providing clarity and transparency on the various aspects of Shariah compliant investments. This new, free monthly publication offers priceless intelligence and arrives at a time when Islamic finance is facing uncharted territory.

**Alternative Market Briefing** is a daily newsletter on the global hedge fund industry, highly praised for its completeness and timely delivery of the most important daily news for professionals dealing with hedge funds.

**A SQUARE** is the first web publication, globally, that is dedicated exclusively to alternative investments with "research that reveals" approach, fast facts and investment oriented analysis.

**Technical Research Briefing** delivers a global perspective / overview on all major markets, including equity indices, fixed Income, currencies, and commodities.

**Sovereign Wealth Funds Briefing** offers a quick and complete overview on the actions and issues relating to Sovereign Wealth Funds, who rank now amongst the most important and observed participants in the international capital markets.

**Commodities Briefing** is a free, daily publication covering the global commodity-related news and research in 26 detailed categories.

The daily **Real Estate Briefings** offer a quick and complete oversight on real estate, important news related to that sector as well as commentaries and research in 28 detailed categories.

The **Opalesque Roundtable Series** unites some of the leading hedge fund managers and their investors from specific global hedge fund centers, sharing unique insights on the specific idiosyncrasies and developments as well as issues and advantages of their jurisdiction.

**OPALESQUE**

[www.opalesque.com](http://www.opalesque.com)