



First quarter of 2009 - one step forward but two steps back for equity markets? Hedge funds off to a good start

As the Federal Reserve, Treasury and governments around the world stepped up efforts to address the financial crisis, investors showed glimmers of willingness to take on more risk. However, it wasn't enough to prevent global equity markets from posting the sixth consecutive losing quarter – even after a strong rally during March.

During the first quarter of 2009 equity markets fell 12% (as represented by the MSCI World Index). In contrast hedge funds “weathered the storm” and preserved capital in volatile global markets ending the quarter essentially flat with the *HFRX Equal Weighted Strategies Index* down marginally by 0.27%

Almost half of institutional investors plan to increase hedge fund allocations over the next twelve months

Results from a State Street 2009 hedge fund study show most institutions intend to increase (49%) or maintain (39%) their allocation to hedge funds in the upcoming year. The majority of funding for new hedge fund positions is expected to come from equity allocations (80%). This is in comparison to 2007 when two in five institutions (39%) planned to draw from bond allocations to fund new hedge fund positions.

“Although hedge fund allocations declined slightly over the past year, we anticipate growth will resume later in 2009, as institutional investors continue to focus on diversification and risk

management” - Gary Enos (Executive Vice President at State Street)

How should hedge funds prepare for regulatory change?

Auditing firm PricewaterhouseCoopers last month published a paper on hedge fund regulation. Some of the highlights from the paper are: -

- New regulatory action is likely to result in greater oversight of hedge funds;
- Risk management and transparency have become increasingly important;
- Fund managers should prepare for stronger governance structures, controls and compliance policies; and
- Investors are demanding increased independence and oversight of the valuation process.

MFA outlines key considerations for regulatory reforms

Hedge fund industry body, the Managed Funds Association (MFA), has outlined various considerations that it believes policy makers should undertake as they debate regulatory reforms to stabilise the financial system. This includes the vital role hedge funds can play in assisting the Association with its efforts to resolve the banking crisis.

“Hedge funds remain a significant source of private capital and can continue to play an important role in restoring liquidity and stability to our capital markets” - Richard Baker (CEO of the FMA).