

May 2009



“The Hedge Fund of Tomorrow” – building an enduring firm will depend on addressing key shortcomings

The 2009 hedge fund study conducted by *The Bank of New York Mellon and Casey, Quirk & Associates* states that the hedge fund industry is going through a “transformational period” and must address key shortcomings in its business and operating models. The events of 2008 have changed the old dynamic. Enduring firms will need to more closely align their business models with investor needs for transparency and liquidity.

The study found that institutions remain firmly committed to hedge fund investing and that hedge fund assets will bottom out at approximately \$1 trillion in 2009, after which capital appreciation and \$800 billion in net inflows over the next four years will push global levels to \$2.6 trillion by 2013.

The study also revealed that funds of hedge funds will solidify their role as the primary hedge fund distribution channel, capturing almost 60% of net inflows between 2010 and 2013 by continuing to offer services most investors will find difficult to replicate on their own, such as manager-sourcing and ongoing due diligence.

Hedge fund redemptions to bottom mid-year

According to *Eurekahedge*, as a result of hedge fund returns outperforming global equity benchmarks, hedge fund redemptions have slowed this year. Growing consensus indicates that redemptions will bottom in June and *Eurekahedge* expects inflows to overshadow redemptions towards year-end.

The expected decline in redemption pressures will assist hedge fund managers to put larger

portion of capital to work, which should translate into better returns in upcoming months. Tighter regulations and increased transparency of the hedge fund industry may also attract investors.

Hedge funds aided by bank cutbacks – this creates huge opportunities (FT.com)

The world financial crisis is benefiting hedge funds in the form of less competition from the previously powerful trading desks of investment banks.

Many investment banks had begun to take similar positions as their hedge fund clients, which in turn lead to an outcry from hedge funds as they faced imitation from the trading desks of the banks they used for financing. Less competition for investments makes it easier to capitalise on opportunities and in addition, bank cutbacks are expanding the talent pool for established hedge funds to cherry pick staff.

Non-traditional assets enjoying increasing allocations

Consulting firm Mercer’s latest European Asset Allocation Survey found 35% of UK schemes and 60% of European schemes expect to introduce “new” investment classes to manage future investment risk. Investment Consulting Head for Europe, Tom Geraghty stated “*funds are looking at ways to manage the risk inherent in their schemes mainly through diversification of their assets.*”

The survey also found UK schemes favouring hedge funds, tactical asset allocation and active currency, with European schemes favouring hedge funds, commodities and high yield bonds. In addition, the survey found a reduction in benchmark allocations to equities, accelerated by the 2008 market turmoil.