

November 2008



October was a slow motion crash with hedge funds “hanging” in there

The global financial crisis continued to wreak havoc across financial markets during October. The S&P 500 Equity Index finished the month with its worst monthly drop since 1987 – down 17% and the MSCI World Equity Index dropped 19%, the most in its 38-year history.

The average US stock fund declined by 23% in value during the month of October with the largest US stock mutual fund i.e. Growth Fund of America down by 19% for the month. On the contrary, hedge funds incurred smaller losses – once again demonstrating the benefit of diversification across asset classes and strategies. The HFRX Equal Weighed Strategies Index was down 9.8% in October - less than half of that of global equities.

Ban on short selling “hurt” hedge fund strategies

The restrictions on short selling imposed by regulators impacted negatively on some of the strategies employed by hedge fund managers. The most widely used hedge fund strategy is long/short equity. The short ban prevented the funds from adding to their short positions as the market continued to decline. Another strategy that “suffered” is convertible arbitrage. Sadly, with managers not allowed to short additional shares as prices fell, they were forced to sell bonds to try and maintain a balance in their portfolios.

Lastly, another strategy badly impacted is statistical arbitrage. Such funds use computerized models to look for anomalies to exploit in the market. Without the ability to short, many statistical arbitrage models have been disrupted.

Your “safe” money isn’t so “safe”

The Reserve Primary Money Fund, one of the oldest money market funds in the US, became the first money market fund in more than a decade to lose money when it was forced to write down \$785 million worth of Lehman debt to zero last month. The fund’s assets dropped by 60% to \$23 billion in two days and the fund was forced to temporarily suspend redemptions – so much for the “safety” of cash.

The FSA does not see a need for more hedge fund regulation – Reuters

The Financial Services Authority (FSA) has played down the notion that hedge funds need more regulation. FSA chief, Hector Sants said, “I don’t particularly think more regulation is needed, but I do think more effective regulation is needed”. He also stated that hedge funds have been able to endure market turmoil better than other firms in the financials service industry.

NYC Pension Fund Comptroller believes that it is “a good time” to invest in Hedge Funds – NYC Comptroller, William Thompson

William Thompson, one of the overseers of the New York City Pension Fund, announced in a CNBC interview that “perhaps this is a good time to get in”. Thompson alluded to the fact that they are looking at more conservative strategies. The fund, which has assets under management in excess of \$100 million, expects to ride-out the equities slump by allocating more resources to alternative assets.