

September 2008



“It’s time to revisit the basket rule and give the fund more flexibility.” - New York State Comptroller

The New York State Common Retirement Fund, the third largest pension fund in the world, posted a return of 2.56% for the 2007-2008 fiscal year. The fund, which outperformed the S&P 500 (-5.1%) for this fiscal year, did well to achieve a positive return given the current market conditions. New commitments in excess of \$300 million were made to hedge funds. According to New York State Comptroller, Thomas DiNapoli, the fund could have achieved better returns if not for the basket rule. The basket rule, under New York law, limits investments in private equity, real estate, and absolute return products to 25% of the total portfolio.

Morningstar to implement rating system for funds of hedge funds

Chicago based Morningstar Inc. is leveraging its database of hedge funds to develop a rating system for over 3,500 funds of hedge funds. Currently, the firm has a rating system for over 5,000 hedge funds. Ryan Tagal, director of hedge funds at Morningstar, believes that the rating system will help investors differentiate one fund of hedge funds from another.

“Small funds have historically been more profitable than bigger hedge funds.” – Pertrac Managing Director, Meredith Jones

A Pertrac study has shown that smaller funds, that are not well known, continue to perform better than their much larger hedge fund brethren with assets

in excess of \$500 million. According to hedge fund consultant Richard Wilson, funds managing assets between \$10 million and \$100 million tend to perform better than larger funds due to their ability to respond more quickly to market movements. In spite of their superior performance, smaller funds have lagged larger funds in attracting asset inflows due to several reasons including lack of infrastructure and lack of diversification.

Short sale ban expires with little fanfare

On 12th August the SEC ban on naked short sales of 19 financial institutions, which was announced in mid-July, expired with little fan-fare. Many hedge funds were short financials in July leading to lackluster performance from the asset class. The S&P banking index rallied 48.68% from its July low as a result of the SEC order. According to Jim Chanos, a well-known short seller who is renowned for uncovering improprieties at Enron prior to its collapse, restrictions on short sales undermine prices because they remove liquidity.

Pension funds embrace hedge funds

After resolving a legal wrangling with unions, the \$78 billion New Jersey pension plan has set the stage to increase its 11.5% allocation to hedge funds. The unions had sought to curb investments in hedge funds. Bill Clark runs the pension plan and intends to attain a target allocation of 19% to hedge funds. Other State pension plans, including Texas and California are following suit with their intentions to increase the amount that they allocate to hedge funds.