

THE THREE 'E'S

Education is the key to eliminating the bad boy image of hedge funds, says Robbie Alexander

Hedge funds make convenient whipping boys. To begin with, the industry is populated with colourful characters, especially given it attracts the best and the brightest who have excess eccentricities.

We have seen Soros knock the pound out of the European Exchange Rate Mechanism while bringing the Bank of England to its knees (arbitraging a whole country out of Europe was pretty nifty. Rarely do people knock at the doors of the BoE looking for clever investment ideas).

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We have seen hedge funds accused of acting as rapacious animals attacking the wealth of Asia; we have seen LTCM charged of shaking the foundations of the altar of finance; and now the runaway price of oil cannot be addressed without mentioning those devious speculative hedge funds (nothing to do with bombs, warring armies, hurricanes or the Chinese using as much oil as water).

KEEPING QUIET

Not one word was uttered (okay, maybe a few) suggesting perhaps in all these instances the market participants, including governments, should shoulder the bulk of the blame that gave rise to unsustainable mispricing anomalies.

Hedge funds, it would appear, are the culprits in all these calamities, naturally! Haven't you seen this film before? Global macro fundamentals as well as geopolitical factors give rise to a myriad of financial anomalies such as supply and demand issues for commodities, currencies and financial instruments being under or overvalued. It is not a hedge fund that has precipitated this

unsustainable or unwarranted pricing incongruity but, as with anything else, it is the hedge fund that will be remembered as the capitalistic charlatan that profited from these situations.

MAINTAINING BALANCE

Ironically, it is the hedge fund that brings equilibrium to the fundamental laws of open market democracy. In fact, according to Alan Greenspan, hedge funds now play an important role in providing liquidity for the capital markets that not long ago was filled by investment banks and their proprietary trading desks.

According to the 26 August issue of *The Economist*, there is little difference between global investment banks and giant hedge funds, so why is the contempt not shared between two similar market participants that at their core generate returns from trading in the market?

The reason for the difference of opinion is regulation and branding. Banks are perceived to be better regulated; hence hedge funds carry the stigma and burden of being shrouded in secrecy. But the age of regulation is fast approaching.

SIGNING OVER TO REGULATION

Over last summer, the Securities and Exchange Commission (SEC) voted to require hedge fund managers to register with the SEC in line with the 1940 Investment Advisors Act, forcing rather mild financial regulation and disclosure information.

The issue of branding is interesting, as one can argue this is as a result of the industry misunderstanding hedge funds as well as the hedge fund industry, which has done a poor job in helping investors to better understand what they are about.

The three Es are an imperative for all in order to bridge this 'understanding gap': education, education, education! Implement it successfully, and this unwarranted bad boy image should dissipate.

So watch this space for additional requests, as regulatory institutions provide legitimacy to these bad boys who, after all, bring liquidity and price efficiency to the market.



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