

Hedge funds set to be back in game



John J Papesh, Pharos Financial Group (SUPPLIED)

By
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The worst may be over for hedge funds with redemptions recording a decline for the third consecutive month in March and industry players expecting stability to return soon.

Net investor redemptions and liquidations in March were an estimated \$23.97 billion (Dh87.7bn) compared to investor outflows of \$41.14bn in February and \$165.25bn in January this year, Hedgefunds.net said in its latest report.

Estimates show hedge fund assets fell an additional 1.01 per cent in March 2009 to \$1.724 trillion compared to reductions of 2.51 per cent in February and 7.56 per cent in January 2009.

"The slowdown signals near-term net redemptions may be coming to an end," the data agency said.

"It makes sense that the worst is over in terms of the pace of redemptions. Similar to past crises that we have seen, investments bounce back and there will always be demand for good risk-adjusted returns.

"A lower VIX and easier money market conditions will eventually bring back inflows into the hedge fund sector as investors gain confidence in the financial system," Jeffrey Meyers, Head of Macro Sales with Newedge, told **Emirates Business**.

VIX is the ticker symbol for the Chicago Board Options Exchange Volatility Index, a popular measure of the implied volatility of the S&P500 benchmark.

According to Hedgefunds.net, which has a database of 7,600 fund products, the estimates for March indicate that investor outflows continued, but the rate of redemptions decreased for the third straight month.

This comes as a positive signal for the industry, which saw redemptions touching a peak in December.

According to industry estimates, almost 1,500 hedge funds shut down last year with more than half of the closures happening in the fourth quarter. Investors pulled money from performing as well as non-performing funds and the beginning of the year brought fresh challenges to the segment.

Assets under management recorded a steep decline from the \$2trn level in November. London-based International Financial Services estimates show global hedge fund assets dropped almost 30 per cent to \$1.5trn by the end of last year.

At the end of this year's first quarter, hedge fund assets fell an estimated 10.78 per cent, or \$208.36bn.

Redemptions accounted for a net \$217.75bn reduction and liquidations accounted for an estimated \$12.61bn, while performance accounted for a rise of \$22.01bn.

The hedge fund industry is estimated to have contracted 41 per cent from the asset level peak in June to the current trough, it said.

The crisis has also changed investor attitudes with a leaning towards higher transparency and easier liquidity, industry analysts said.

"Investors have become more prudent when completing their due diligence," said John J Papesh from Pharos Financial Group, adding: "While investors have historically chased performance, now they are becoming more focused on other variables when considering funds like getting to know the manager better, track record, resumes of the team and service providers. Hence, experience fund managers are evolving for the better which means better investment choices not only for investors but for an industry that is here to stay."

The crisis has also changed the way hedge funds are managed. "Given the increased scrutiny on funds and the possibly that there were too many funds pre-crisis, the surviving funds today are more likely to deliver better performance, offer better transparency, become regulated and behave more ethically and friendly towards their clients," said Papesh.

Opportunities would exist for funds that have a stronger risk management and ability to adapt to changes, he said.

"Investors are asking for more due diligence, more transparency and shorter notice periods for liquidity.

Lyxor index down

The Lyxor Global Hedge Fund index, an investable index based on Lyxor's hedge fund platform, which tracks the overall hedge fund universe, was down -0.38 per cent in March. Since the beginning of the year, the index is up 42 basis points.

March witnessed significant and brutal trend reversals on most asset classes, Lyxor said in a statement.

Bottom-up company news on the financial sector's profitability triggered a massive equity rally in this sector (close to 60 per cent) that filtered through to other sectors as economic indicators exceeded downbeat expectations.

In such a market environment, strategies with a positive equity bias were this month's best performers, it said.

Long bias equity funds gained 4.3 per cent, nevertheless slightly underperforming equity markets.

Compared to historical standards, managers remain defensively positioned.
