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Transparency, Client Service on Hedge Fund Agenda

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By Paul O'Dowd

Institutional investors have not let last year's poor hedge fund returns change the way they feel about the investment, says a new survey conducted by SEI and Greenwich Associates. According to the survey, investors appear committed to the space for the long-term but are looking for more transparency and better client service.

The survey of three groups of pensions in the U.S., U.K. and continental Europe was conducted over two periods of time in August and November 2008. The first survey found that 90% of institutions polled either increased or maintained their allocations to hedge funds over the past two years. In November, 75% of a smaller group re-surveyed said they remain unchanged with their commitments to hedge funds.

Hedge funds, which have an average allocation of 7.4% among respondents, do currently have an image problem with performance being the biggest concern. "Between the first and second surveys, the number of investors naming performance as their biggest worry about hedge funds rose from 67% to 84%," states the survey. "In the 2007 SEI sponsored survey of U.S. institutional investors, "poor performance" was only the third-ranked concern and was named by fewer than one in six of those interviewed. Other top-ranked concerns identified in the current survey were a lack of liquidity, funds not accomplishing their stated goal, and headline risk."

In response to last year's turmoil, fund managers are increasingly placing more of a focus on transparency, a far cry from a few years back when many hedge managers did what they could to keep transparency low. "Successful hedge funds and funds of funds commit to transparency," says Phil Masterson, managing director for SEI's investment manager services division. He feels it will be demanded by institutions in the future as they will likely levy "parameters" on funds that won't be able to be broken.

Specifically, Masterson feels transparency in operations, trading, risk management and compliance are some of the most important areas. With operations, for example, investors want to know what the valuations are of the underlying assets. He says from the first survey to the second, there was a noticeable jump in transparency interest.

One firm that is increasing transparency is hedge fund shop Tuckerbrook Alternative Investments, which has moved to daily asset transparency statements. These statements, which are prepared and delivered by the funds' independent administrator, Citi Hedge Fund Services, gives investors the daily market value of assets in their accounts.

"We lived through 2008 like everyone else did," says John Hassett, a principal at the

\$600 million fund, "and when it came to an end, this was the outcome of our analysis." He says clients have been talking about increased transparency for some time, adding they have also wanted it more frequently combined with third-party verification. He says even if clients aren't reading statements every day, they are comforted just knowing they are there.

Another area of interest, according to Greenwich Associates managing director Rodger Smith, is for hedge funds to build client relations teams going forward. Unlike their long-only brethren, hedge funds have been slow to build up client relations teams. "Clients want to talk more to understand what you are doing and why you are doing it," he says. "Clients want to be walked through the portfolio, the strategy and to understand why hedge managers are making the moves they are."

When performance is good, clients don't really need to speak to client relations teams nearly as much, says Smith. However, when performance is falling below expectations these teams come up big. "Client relations gives them an advantage, especially when performance is weaker," he says, because the fund is capable of walking the client through what occurred while the portfolio managers stick to their tasks at hand. Hedge funds are going to have to beef this up if they want to be players in the industry, he says.