A Brodie Consulting publication in conjunction with RQC Group

August 2021

The Hedge

Looking back at the past month's news and views

Funds down in July

No winning streak continues forever. After nine consecutive months of positive performance, the hedge fund sector closed down in July. For the month, the **HFRI Fund Weighted Composite Index** was down 0.60%, but remains up 9.45% for the year.

The **HFRI Equity Hedge (Total) Index** was down 0.76%, with positive performances from quant directional and equity market neutral outweighed by losses in energy and healthcare strategies, which were down 2.38% and 1.51% respectively. Equity indices continue to be the best performing HFRI strategy, up 11.12% for the year.

Event Driven was down 0.82% (**HFRI Event Driven (Total) Index**) in July, largely due to a more difficult month in the Multi-Strategy sector, which was down 3.11%.

Macro was marginally down 0.10% (**HFRI Macro (Total) Index**), but was the best performing strategy. The positive performances from systematic (+0.59%) were however set against losses from discretionary (-0.96%) and currency focused managers (-1.56%).

Looking at the Regional Indices, there were a wide dispersion of performances. The most notable was the **HFRI Emerging Markets India Index**, which was up 6.25%, while on the other end of the scale the Latin America Index declined 4.10%.

$1 trillion

Size of China's recent sell-off after regulatory crackdown

$135 billion

Man Group AUM as reported in H1 results.

China sell-off a mixed blessing

China's recent market crash has left multiple long-biased hedge funds nursing big losses but has proved a boon for those managers with short positions.

According to Bloomberg, the crash amounted to a $1 trillion sell-off as concerns about regulatory pressures took hold. Between them **Alibaba Group, Kuaishou Technology, Meituan** and **Tencent Holdings** all lost around $350 billion of market cap in July according to **Factset** data.

The rumours started in the internet chatrooms that China's largely unregulated private education sector would be forced to turn non-profit and the result was even worse than anticipated. China's largest education provider, **New Oriental Education & Technology Group**, lost half its value in an hour.

The sell-off dip has however been seen as a good entry point for investors, with data from research firm **EPFR Global** showing China focused funds recorded net inflows of $3.6 billion in the week to 28 July.

UBS launches women led investment portfolio

In a move to broaden and strengthen diversity, **UBS** has launched the Carmen portfolio to invest in hedge funds run by women, reports the Financial Times. The portfolio will be actively managed and employ quantitative analysis.

This move comes as large investors are increasingly using ESG criteria and tools to make their investments. In 2020, **Aberdeen Standard Investments** launched a similar fund.

The same article refers to **Preqin** data that shows women still only represent 10.9% of senior employees in hedge funds, which is a small increase on the previous year's numbers.

Upcoming Events

15 September 2021
AIMA Australia Annual Forum 2021
21 September
MFA Digital Assets 2021
21-22 September
Global Distribution Conference ALFI
22 September
MFA Data & Technology 2021 (virtual)

Click here to see further events in 2021

This newsletter is a selection of the previous month's sector news, trends, regulatory developments and best practices. Any opinions expressed are those of the author only and the newsletter does not constitute personal advise or a personal recommendation. We always seek to maintain tight editorial standards. If you have any comments on this content, please do not hesitate to get in touch with the team.

News

Man Group reports strong half year results

In its half-year results released on 28 July, **Man Group** reported record funds under management of $135 billion, with net inflows of $1.2 billion.

The **Financial Times** described the results as a 'blowout [signalling] a change in fortune for [the] wider sector.' There were particularly strong net flows into **AHL TargetRisk** and **Man Institutional Solutions**, which were offset by outflows from **FRM Segregated** and **Alternative Risk Premia**.

Absolute performance across the firm was up 8.6%, with alternatives up 5.8% and all **AHL** products closed the half in positive territory.

According to ***Luke Ellis'*** CEO Review, "strong absolute performance from [the] quant alternative strategies drove a significant increase in performance fees."

Eisler Capital raises $1bn

Eisler Capital, set up by *Edward Eisler* in 2015, has raised the second largest European fund this year, reports **Bloomberg.** The $1 billion multi-strategy fund, which started to trade on 1 July, is mandated to make leveraged bets and seeking returns of 12-15%.

Coffey looks to long-only market

Bloomberg reports on *Greg Coffey's* **Kirkoswald** expanding beyond hedge funds to include a long-only side, with a particular focus on emerging markets.

The $3.5 billion business, which was launched in 2018, recently hired New York based *Diana Amoa* from **JPMorgan Asset Management,** where she was a member of the Global Fixed Income, Currency and Commodities group, to run this unit.

This move comes shortly after the firm hired ***Joseph Mauro*** from **Light Sky Macro** to lead the firm's expansion plans and ***Neha Coulon*,** again from **JPMorgan**, to lead the firm's ESG push.

Einhorn focuses on Inflation

In *David Einhorn's* Q2 investor letter, published by **ValueWalk**, he writes that inflation is here to stay.

Einhorn makes the distinction between temporary inflationary bottlenecks and more structural problems, associated with long-term under-investment in traditional businesses, such as mills and miners, during a time when investors have been pouring money into technology companies. The result, he writes, will be higher prices as the traditional firms retool to increase production. In addition, the higher wages to *'lure'* employees back to the office and Fed *'tinkering'* with expansionary policies, will also lead to higher prices.

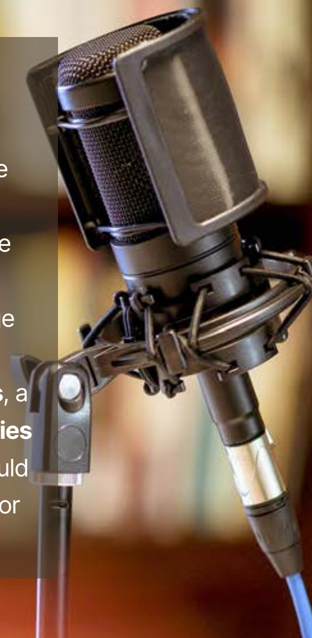
This newsletter is a selection of the previous month's sector news, trends, regulatory developments and best practices. Any opinions expressed are those of the author only and the newsletter does not constitute personal advise or a personal recommendation. We always seek to maintain tight editorial standards. If you have any comments on this content, please do not hesitate to get in touch with the team.

News (cont.)

Ackman changes tack

Bill Ackman has been forced to *'rejig'* his deal to buy 10% of **Vivendi's Universal Music Group**.

Having initially agreed to complete the deal through his SPAC, **Pershing Square Tontine Holdings (PSTH)**, US regulators raised concerns about the move, which Ackman described on **CNBC** as being a *"deal killer."* Investors also had concerns, with PSTH share price falling almost 20%. The deal would have used up the bulk of the SPAC. Instead, Ackman will make the investment through his hedge fund, **Pershing Square Holdings**, a move that **Jefferies** analysts said would be a *'big outlay'* for the fund.



GSK defies Elliott

Taking little notice of **Elliott Management's** recent *'recommendations,'* **GlaxoSmithKline** (GSK) has appointed *Brian McNamara*, an *'insider,'* as head of its consumer healthcare division. Elliott had been calling for a six-month review of its consumer division, which GSK is planning to spin off and list, along with a process to *"select the best executive leadership."*

Elliott ups the ante at Duke

Showing that there is no rest for the activist, **Elliott Management's** 'standoff' with **Duke Energy Corporation** is *'heating-up,'* writes **Barron's.**

Having announced its stake in the energy firm two months ago, the manager has been engaging with Duke investors and received what it called *'an outpouring of feedback.'*

In their usual letter to the target Board, which they released via **PR Newswire** on 19 July, Elliott called for Duke to: 1) enhance the Board's independence; 2) improve operational performance in Florida; 3) increase focused and enhance value in Indiana; and 4) attain a premium valuation. Duke response is that the activist is *"cherry picking."*

This newsletter is a selection of the previous month's sector news, trends, regulatory developments and best practices. Any opinions expressed are those of the author only and the newsletter does not constitute personal advise or a personal recommendation. We always seek to maintain tight editorial standards. If you have any comments on this content, please do not hesitate to get in touch with the team.

News (cont.)

Archegos aftershocks

Credit Suisse's 165-page report by law firm **Paul, Weiss, Rifkind, Wharton and Garrison** into its **Archegos** failings makes for tough reading, showing the *'bank failed to properly monitor tens of billions of dollars of exposure,'* reports **Bloomberg**.

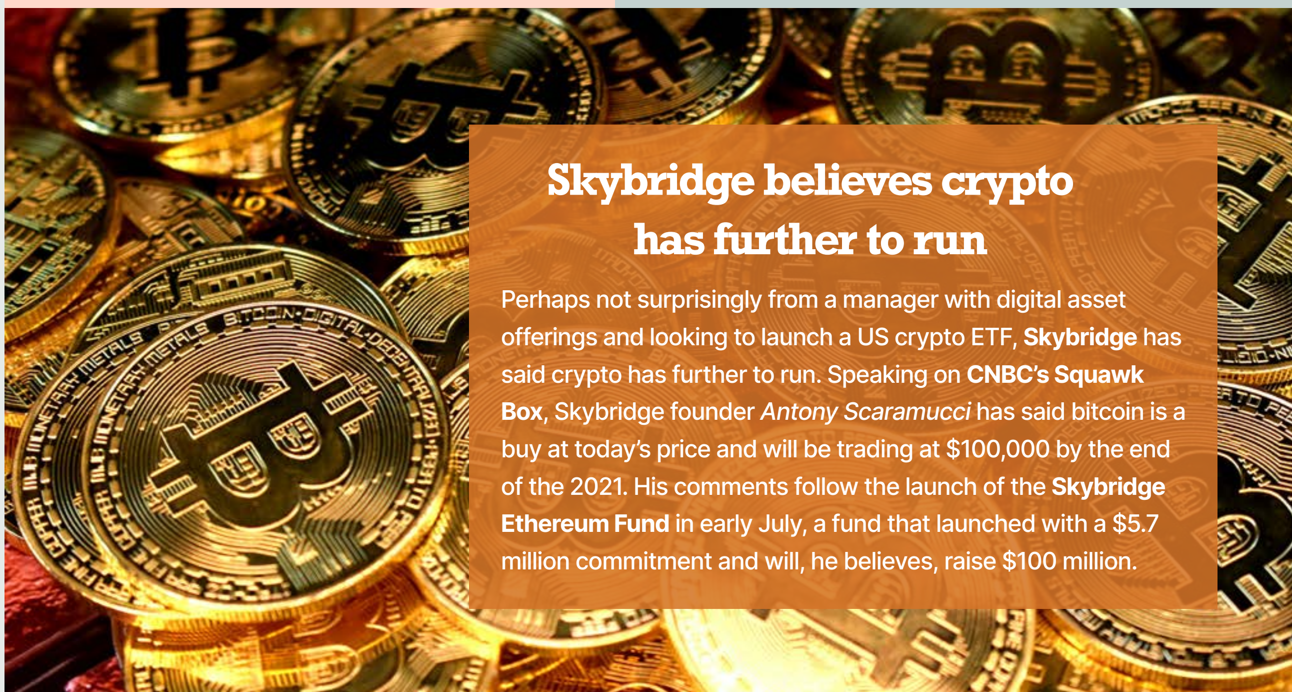
The damning report points to due diligence failings, but no criminality inside the bank.

The bank booked an additional loss from Archegos in its second quarter earnings of $653 million. It has also announced a new Chief Risk Officer, with the appointment of ***David Wildermuth***, formerly at **Goldman Sachs**.

Funds avoid Binance

Hedge funds are increasingly giving **Binance** a wide berth, given the flood of negative headlines and increased regulatory scrutiny. The **Financial Times** reports that several funds have curbed their trading, with crypto specialist **Tyr Capital** saying it had *"significantly decreased its exposure."*

In response to the concerns, Binance is taking a series of what appear to be game-changing – or perhaps last ditched – steps to allay concerns, including becoming a regulated financial institution, winding down its futures and derivatives products business in Europe, appointing a new CEO and cutting the amount of risk that clients can take to 20 times leverage.



Skybridge believes crypto has further to run

Perhaps not surprisingly from a manager with digital asset offerings and looking to launch a US crypto ETF, **Skybridge** has said crypto has further to run. Speaking on **CNBC's Squawk Box**, Skybridge founder *Antony Scaramucci* has said bitcoin is a buy at today's price and will be trading at $100,000 by the end of the 2021. His comments follow the launch of the **Skybridge Ethereum Fund** in early July, a fund that launched with a $5.7 million commitment and will, he believes, raise $100 million.

Gensler doubles down on crypto criticism

SEC chairman ***Gary Gensler*** became the latest regulator to take aim at the crypto market.

He called on Congress to give the SEC more power to police what he describes as *'the Wild West of crypto-trading.'* Gensler said that he was *'specifically targeting cryptocurrency exchanges for regulation,'* which currently do not fall under the agency's remit.

This follows Japan's financial regulator saying that it will look at digital currencies as part of its crackdown on money laundering.

But Gensler is more a progressive than Luddite when it comes to crypto, having taught courses on crypto finance at MIT. On the one hand he urges caution and on the other he said that he believes it *"could continue to be a catalyst for change in the fields of finance and money."*

This newsletter is a selection of the previous month's sector news, trends, regulatory developments and best practices. Any opinions expressed are those of the author only and the newsletter does not constitute personal advise or a personal recommendation. We always seek to maintain tight editorial standards. If you have any comments on this content, please do not hesitate to get in touch with the team.

News (cont.)

Growth in sustainable investing

Sustainable investments today amount to $35.3 trillion in AUM, according to the biennial Global Sustainable Investment Review (GSIR). This is just over a third of all professionally managed assets in the US, Canada, Japan, Australasia and Europe, and is an increase of 15% over two years.

According to the Review, we have seen the 'global acceleration of an international sustainability agenda driven by international agreements such as the **Paris Agreement** and the **United Nations Sustainable Development Goals**, both of which are calling out the important role of finance.'

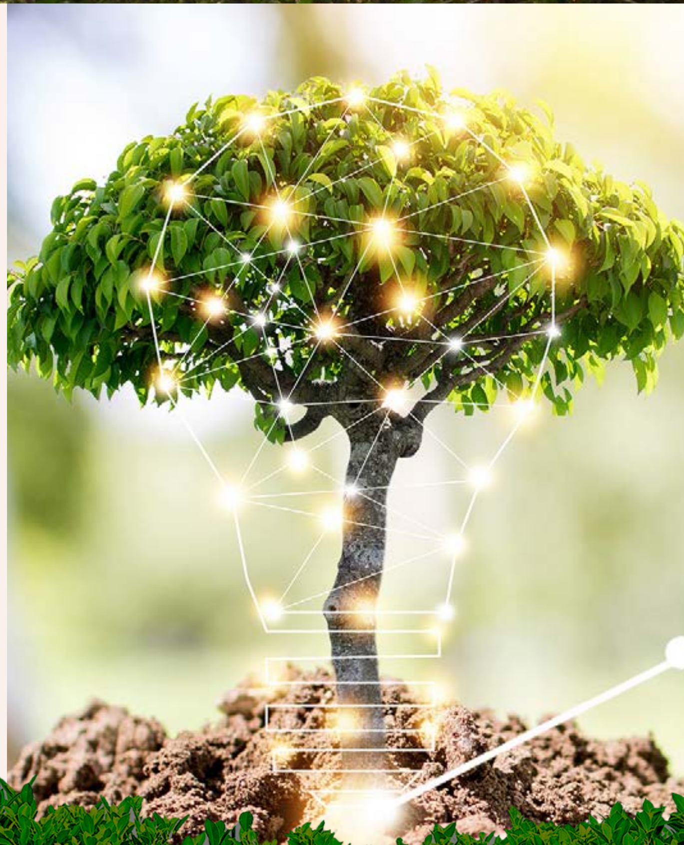
The largest increase in sustainable investments over the two years has been in Canada (48%), followed by the United States (42%). But it is the United States and Europe that represent more than 80% of global sustainable investing assets.

The most common sustainable investment strategy is ESG integration, accounting for $25.2 trillion in AUM, followed by *'negative screening, corporate engagement and shareholder actions, norms-base screening and sustainability-themed investment.'*

Higher quality ESG requirements

The **FCA** has written to the chairs of authorised fund managers on the need to improve the quality of ESG funds put forward.

The head of the FCA's asset management supervision unit, ***Nick Miller***, has said that they had seen a high volume of applications for the authorisation of funds with an ESG focus. Miller added that while the FCA welcomed *"innovation,"* he is *"concerned by the number of poor-quality fund applications"* and the *"impact this may have on consumers."* As a result, the FCA has created guiding principles for fund managers, for pre and post authorisation to help AFMs ensure that they are complying with ESG requirements.



This newsletter is a selection of the previous month's sector news, trends, regulatory developments and best practices. Any opinions expressed are those of the author only and the newsletter does not constitute personal advise or a personal recommendation. We always seek to maintain tight editorial standards. If you have any comments on this content, please do not hesitate to get in touch with the team.

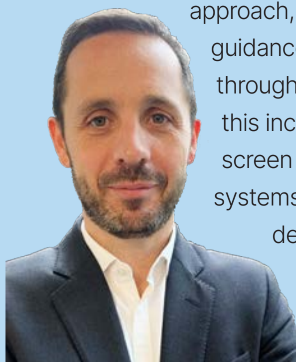
Guest Article

Time for an Operational Due Diligence Therapy Session?

In the following Guest Article, Quentin Thom, Co-Head, perfORM Due Diligence Services, takes a 'therapy' approach to ODD.

There are so many different pressures on managers, both new and existing, that all too often they can fail even the simplest ODD tests. Managers rightly focus on the day-to-day running and growing of their business, but at the same time they need to be able to face up to the challenges and pitfalls associated with an investor ODD review.

To achieve this, we take what we call an 'ODD therapy' approach, providing an additional level of guidance to 'patients' to guide them through the potential mire. Today, this includes the virtual world of screen sharing (including process and systems walk throughs), data rooms, dealing with the pandemic and a 'new hybrid normal', blending WFH and the office, cyber and information security threats, to name a few.

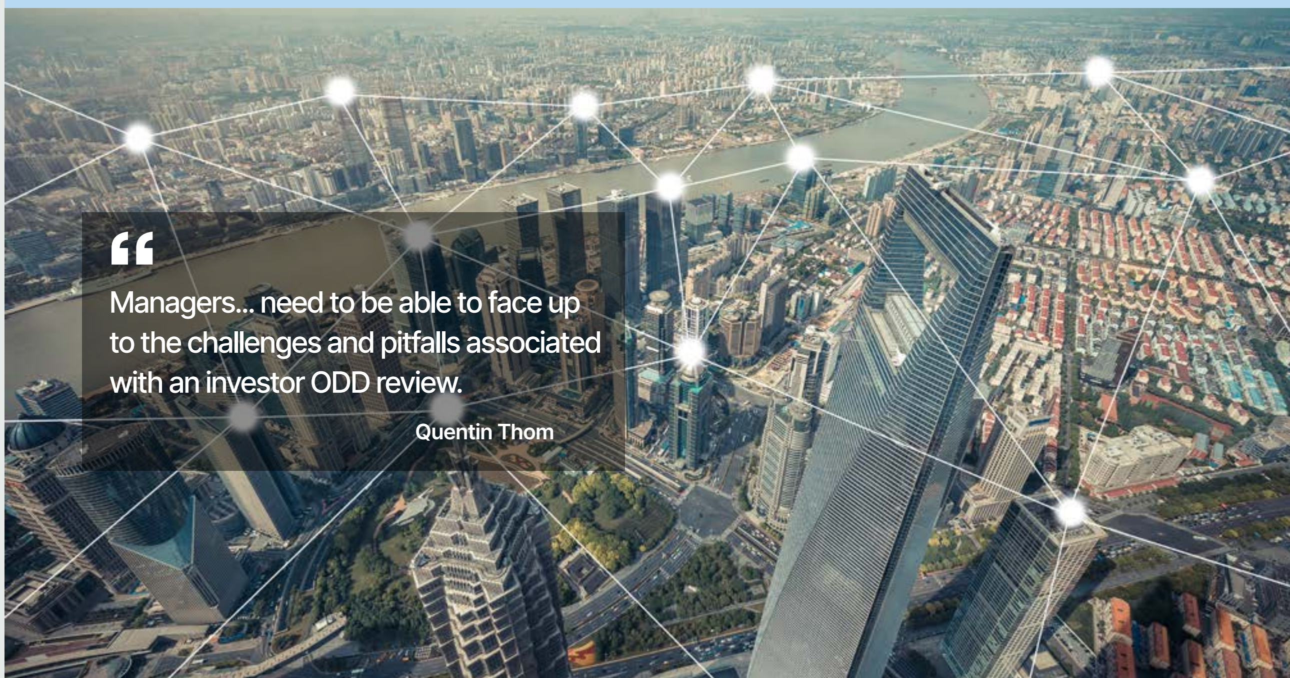


Quentin Thom

Managers need to demonstrate to investors a willingness to adopt and maintain best practices, as well as always looking to improve operationally. Our approach to working with managers is akin to therapy sessions, for it is about breaking down their current approach and setting it against the reality of an ever-more-demanding institutional expectation.

Such an approach has the traditional characteristics of an institutional ODD process (including detailed manager and fund level documentation review) with the added benefit of 'counselling' that includes higher-level guidance and recommendations, rarely provided in live-fire investor ODD reviews. The goal is to avoid the simple ODD mistakes.

As in therapy, it is designed to be painless, but it is designed to go deep into the manager's processes, aligning the core objective of ODD - to get invested and stay invested - with 'operational conviction'. Now more than ever, investors have a choice on how they do this and will consider the time, cost and resources available in order to continue to meet this objective.



> "Managers... need to be able to face up to the challenges and pitfalls associated with an investor ODD review.
>
> Quentin Thom

This newsletter is a selection of the previous month's sector news, trends, regulatory developments and best practices. Any opinions expressed are those of the author only and the newsletter does not constitute personal advise or a personal recommendation. We always seek to maintain tight editorial standards. If you have any comments on this content, please do not hesitate to get in touch with the team.

Marketing

Presented by

Don't undervalue the importance of your website

It is almost always an error to underestimate the value of a website. Time and again websites are the first port of call for any basic investor due diligence. This is emblematic of a brand and should be a clear representation of the manager. If the website strays from what the manager is saying in their presentation, or vice versa, or is just not obvious, then it is a potential DD red flag.

A website is an inexpensive marketing tool, but time should be spent to ensure that the messaging is clear. It is often surprising how little copy there is on a website, which should make this straightforward exercise, but it rarely is. All too often hours are spent coming to a compromise over a particular line. The result should be simple and well written, and never ever over complicate the story.

There are always going to be funds, such as ***Greg Coffey's* Kirkoswald** and ***Jim Simons'* Renaissance Technologies** that can afford to have basic placeholder sites. The strength of their brands go far beyond the website; in fact, the very brevity of this information is part of their mystique. But most managers are not in this position and instead need to use their website as an important part of their marketing armoury to tell their story.

WWW.BRODIECG.COM

REGULATORY

Presented by

FCA Business Plan

The **FCA** has published its Business Plan for 2021/2022, which sets out its key areas of focus for the coming year.

This is the first Business Plan under the stewardship of ***Nikhil Rathi,*** the FCA's current CEO who took office in October 2020. Against a backdrop of Covid and Brexit, the FCA acknowledges that it needs to be transformative, in terms of innovation, assertiveness and adaptiveness.

Items of interest for asset managers include:

- Ensuring that the wholesale sector better suits UK markets and the needs of investors and companies, whilst retaining regulatory standards that are at least as robust as that of the European Union
- Increasing the supervision of ESG attributed of asset managers' investment products, with a focus on ensuring that such products are promoted in a manner that is clear, fair and not misleading. As detailed in an earlier article in this Newsletter ('FCA creates guiding ESG principles'), the FCA subsequently sent a 'Dear Chair' letter to Authorised Fund Managers ('AFMs') (i.e. lead managers of authorised funds) on this topic; the key messages are also of interest to other types of asset manager
- A supervisory focus on AFMs, following the findings of their June 2021 review
- Continuing to work with other parties on establishing the right framework for long-term asset funds (LTAFs)
- A focus on six of the most important cross-market issues: fraud; financial resilience; operational resilience;

Cont'd over page

RQC GROUP (cont.)

Cont'd from page 7

international cooperation; diversity and inclusion; and ESG

- A tougher approach to authorisations with greater focus on scrutinising applicant firm's financials and business models. The FCA is also increasing its supervision of newly authorised firms.
- 'Use it or lose it' – an initiative looking at removing a firm's permissions if they are not carrying out regulated activities
- A continued focus on market abuse and financial crime

Revisions to SPAC Listing Rules

The **FCA** is changing the Listing Rules that apply to special purpose acquisition companies (SPACs). These are companies formed for the sole purpose of identifying and acquiring suitable business opportunities. At the IPO stage they are effectively *'shell companies'* pending the acquisition(s).

There has been a presumption that a SPAC's listing is when it announces a potential acquisition target, or if details of the proposed acquisition have leaked. This is to protect investors from disorderly markets.

The changes, which take effect on 10 August 2021, remove the presumption of suspension for SPACs that meet certain criteria intended to strengthen the protections for investors. These include:

- A 'redemption' option allowing investors to exit a SPAC prior to any acquisition being completed
- Ensuring money raised from public shareholders is ring-fenced
- Requiring shareholder approval for any proposed acquisition
- A time limit on a SPAC's operating period if no acquisition is completed
- The US leads the way in SPACs, with $87 billion raised in the first 3 months of 2021 alone (compared to $83 billion for the whole of 2020). The UK lags behind, but it is hoped that these more relaxed rules will make London a more competitive venue for SPAC listings.

FCA Publishes Policy Statement on Investment Firms Prudential Regime

The **FCA** has set out its latest feedback on the **Investment Firms Prudential Regime** ('IFPR'), which affects most investment firms and asset managers, and takes effect on 1 January 2022.

Policy Statement PS21/9 discusses comments received from industry stakeholders following an earlier Consultation Paper.

Topics of interest include regulatory capital and liquid assets requirements, risk management including the introduction of the 'ICARA' process (which replaces the 'ICAAP'), remuneration and regulatory reporting.

IFPR is a comprehensive overhaul of the prudential regime. It aims to consolidate the framework for firms whilst making it more aligned with the risk profile of the sector. The final rules are expected to be published in Q4, 2021.

This newsletter is a selection of the previous month's sector news, trends, regulatory developments and best practices. Any opinions expressed are those of the author only and the newsletter does not constitute personal advise or a personal recommendation. We always seek to maintain tight editorial standards. If you have any comments on this content, please do not hesitate to get in touch with the team.

RQC GROUP (cont.)

SEC Division of Examinations Publishes Risk Alerts

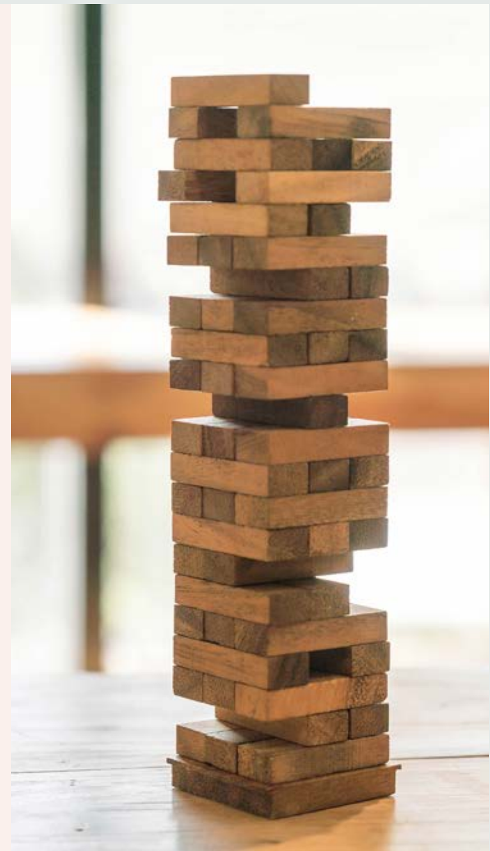
The **SEC's** Division of Examinations has published two Risk Alerts of interest to the buy-side.

The first of these highlights in detail the most common compliance issues observed by its staff related to principal and agency cross trades. Firms are encouraged to review their written policies and procedures to ensure that they are consistent with the **Advisers Act** and the rules thereunder.

A principal trade is where a firm transacts a security between its own account and a client's account. A cross trade includes where a firm transacts a security between two client accounts.

The second of these discusses the most frequently cited deficiencies identified by its staff as relates to wrap fee programs. These are portfolios where a comprehensive charge is levied by an investment manager or investment advisor to a client for providing a bundle of services. Firms that recommend wrap fee programs are encouraged to consider and adopt policies and procedures to address such risks, conflicts, and challenges.

These Risk Alerts provide an indication as to the SEC's examination priorities and are therefore of interest to all SEC registered investment firms.



If you have any questions about **The Hedge**, or would like to have a colleague added to our distribution, do please contact the team at **thehedge@brodiecg.com**

This document has been produced by Brodie Consulting Group in conjunction with RQC Group.

Brodie Consulting Group is an international marketing and communications consultancy, focused largely on the financial services sector. Established in 2019 by Alastair Crabbe, the former head of marketing and communications at Permal, the Brodie team has extensive experience advising funds on all aspects of their brand, marketing and communications.

Founded in London in 2007 and with a dedicated office in New York, **RQC Group** is an industry-leading cross-border compliance consultancy specializing in FCA, SEC and CFTC/NFA Compliance and Regulatory Hosting services, servicing clients with AUM in excess of $580 billion.

Alastair Crabbe
Director
Brodie Consulting Group
+44 (0) 778 526 8282
acrabbe@brodiecg.com
www.brodiecg.com

United Kingdom:
+44 (0) 207 958 9127
contact-uk@rqcgroup.com
United States:
+1 (646) 751 8726
contact-us@rqcgroup.com
www.rqcgroup.com

To listen to The Hedge podcast click here.

This newsletter is a round-up of the previous month's sector news, trends, regulatory developments and best practices. Any opinions expressed are those of the author only and the newsletter does not constitute personal advise or a personal recommendation. We always seek to maintain tight editorial standards. If you have any comments on this content, please do not hesitate to get in touch with the team.