Hedge fund managed accounts 2013

Private MAPs are a significant growth area

Examining the potential impact of AIFMD

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and that 18 per cent planned to introduce them over the next five years.

With respect to hedge fund managers, those figures were even higher.

“We covered about 186 hedge fund managers in our research. What we found was that 35 per cent had introduced managed accounts since 2008 and 22 per cent planned to introduce them over the next five years,” explains Patrick Hayes, Head of Hedge Fund Operations (Ireland), State Street.

Given that State Street administrates over USD650 billion in assets it is well placed to pick up on industry trends. Aside from noting increased activity around funds-of-one, which

As a solution for investing into hedge funds the managed account model is nothing new. As a way to access liquid hedge fund strategies with greater transparency and risk controls in place to help investors make more informed investment decisions, managed accounts play a vital role. And according to a recent AIFM industry survey, managers are becoming all too aware of this.

In the State Street 2013 Alternative Fund Manager Survey, released a couple of months ago in collaboration with Preqin and which involved speaking to 400 global alternative fund managers, 26 per cent of all alternatives managers said that they had introduced managed accounts since 2008

Private MAPs represent a significant growth area

By James Williams
typically involves a FoHF allocating to a managed account mandate where they and their investors are the sole investors, Hayes says that managed accounts are becoming more of a go-to option for smaller managers still heavily involved in the fund raising cycle.

“Over 80 per cent of newer managers said that one of the biggest challenges they face is fundraising. Managers need to differentiate themselves and it does seem to be that managed account activity is more prevalent in the small and mid-sized manager space,” says Hayes.

This is borne out by the fact that managed account platform providers – both bank-owned public platforms and independent platforms – are enjoying continued growth.

Dr Stavros Siokos is the CEO of Mayfair-based Sciens Alternative Investments. The platform is largely comprised of commingled assets and currently boasts around 40 fund managers representing a range of trading strategies. Recent additions to the platform include the likes of Japan-based Stats Investment Management (Ginga Service Sector fund, a long/short equity strategy focused on the technology and service sectors) and US-based Revolution Capital Management (a CTA).

“We’ve seen gross assets under management on the platform increase fourfold from USD300million to USD1.2billion since we bought the platform and our assets are up 35 per cent year-on-year. When we bought the platform we had 13 CTAs. Now, half the managers on the platform are CTAs and the other half are equity long/short, credit long/short and global macro,” confirms Siokos.

One of the key drivers for growth in the Sciens MAP, as well as other platforms like InfraHedge, Man FRM, and Deutsche Bank’s dbalternatives MAP, is customisation. With recent high-profile events such as the implosion of MF Global, investors with the deepest pockets – public pension funds, endowments etc – want total control and segregation of their assets. This push for segregation is good news for platform providers who are keen to provide the infrastructure support and run the operational side of things, whilst at the same time giving investors free reign over which service providers and managers they wish to allocate to.

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Patrick Hayes, State Street

“We’ve been pioneering that approach with Dutch pensions manager PGGM, whereby we designed a fully dedicated platform for them, and a bit more recently with CalSTRS (California State Teachers’ Retirement System) to build a customised strategic solution in the global macro space,” says Lionel Paquin, Head of Lyxor Managed Account Platform, which currently runs the largest independent commingled MAP with some 100-plus managers for investors to choose from.

“Managed accounts are not just a secure framework, they are a flexible investment solution in which fees can be adapted, guidelines can be enforced, cash utilisation can be optimised, leverage can be modified etc. Having a private MAP is a secure but also an investment-driven solution for institutional investors.”

FRM, the fund of funds division of Man Group, runs approximately USD8.2billion in assets on its managed accounts platform. Stephen McGoohan heads up FRM’s managed accounts business and is unambiguous in stating the “huge importance” of setting up customised solutions for clients going forward. He notes that whilst large institutions have the assets necessary to set up their own MAP, “You also need the experience and expertise that comes from a long history in establishing managed accounts and a significant technology infrastructure to process and aggregate the volume of data. As a result we are experiencing an increase in the number
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Examining the potential impact of AIFMD

Interview with Lionel Paquin

“It is most welcome to have a dedicated regulatory framework for alternative funds than no framework at all,” comments Lionel Paquin, head of Lyxor Managed Account Platform (MAP), when discussing the potential impact of the AIFM Directive on the alternatives industry.

“Offshore hedge funds have traditionally been viewed as “black box” investments. The directive changes this. It gives institutions the opportunity to invest in offshore complex strategies in an onshore regulated format.”

It is eminently possible that market regulation could prove to be an unexpected fillip for the hedge fund industry and, by extension, leading platform providers like Lyxor. Why? In Paquin’s opinion, European institutions who are not currently invested in offshore alternative funds may view the directive as opening the door to their investing in onshore hedge funds because of the greater transparency and control on offer. This in turn could help managers raise more assets. The bigger managers become, the more likely they are to offer managed account mandates.

“The directive could be a major catalyst for European institutions who were previously conservative about hedge fund investments,” states Paquin. Moreover, unlike the UCITS regulatory framework, which is not compatible with all alternative strategies, the AIFMD framework is focused on the fund manager.

Rather than viewing the directive as a potential threat to managed accounts, Paquin is upbeat and constructive on the opportunities for Lyxor.

“We have effectively set our own quasi-regulatory standards with our MAP for more than 15 years now. We have third party controls in place, independent valuations, independent risk management, so we welcome and understand the reasons for regulation but we don’t view it as a panacea,” says Paquin, who further explains how the directive will benefit managed account providers: “Becoming AIFMD-compliant won’t guarantee that all hedge funds have excellent performance, impeccable reputation and have the right investment process and the right operational organisation. As a MAP provider our value proposition to investors is to create a consistent investable universe based on managers we ourselves have selected.

“Choosing the right managers is key and that requirement won’t vanish with AIFMD,” asserts Paquin. “We offer homogeneous reporting, a homogeneous trade cycle and many services associated with that that are necessary to investors.”

Mandatory state-of-the-art independent risk management and valuation are core features of the managed account business and key requirements in protecting investors against asset misappropriation, asset mispricing and strategy misrepresentation - risks that will remain in offshore funds post-AIFMD, according to Paquin.

An added opportunity for Lyxor under the directive will be to support non-European hedge fund managers who do not wish to become fully compliant as AIFMs.

“They have three options; either ignore Europe altogether, comply with the directive by establishing their own AIFM which could be expensive and resource-consuming or partner with Lyxor through a win-win deal where we assume the role of the AIFM.

“We can take the responsibility of setting up an AIFMD-compliant vehicle in Europe on behalf of the manager. There will be some rules they will need to comply with as a trading advisor of Lyxor but nothing compared to becoming fully compliant with the AIFMD.”

This, says Paquin, will help strengthen Lyxor’s value proposition to both investors and managers: “We will be able to actively promote ourselves to professional investors and help non-European managers distribute their strategies in Europe.”
of large institutions coming to us to discuss partnership arrangements.

“Clearly there are a number of positives to having segregated managed accounts but the question remains: Do investors always have the necessary capital to commit to a particular manager to secure a managed account? Often this is only possible when pooled with other investors in commingled accounts.

“The minimum asset size for a managed account largely depends on the investment strategy; maybe they want liquid CTAs, equity long/short. The barriers to entry for such strategies are lower and institutions may find it easier to secure an SMA with such a manager. However, for more credit-orientated strategies they’ll need to commit more assets,” says McGoohan.

Investors who go down the customisation route also need to be mindful of the greater burden of running managed accounts from a regulatory reporting perspective. Building out their own technology infrastructure is a massive commitment. That’s why many of the customisation solutions are partnerships. A pension fund can go to the likes of InfraHedge or FRM with a shopping list of managers and hand over the operational responsibility of monitoring the mandates on a day-to-day basis.

“We already have the infrastructure in place. It’s something that I’m sure is another key concern when institutions are thinking of doing this themselves,” adds McGoohan.

Akshaya Bhargava is the CEO of InfraHedge, whose investor-centric model to running managed accounts has enjoyed huge success. Although pleased that client assets have grown and the firm’s model is “growing in acceptance” Bhargava believes that the adoption of managed accounts is still at an early stage.

“We strongly believe in the benefits like transparency and control that managed accounts provide and much of our activity during the year has been focused on preaching the gospel and dispelling the misconception that managed accounts are complex and expensive to set up and run.”

Akshaya Bhargava, InfraHedge

matures I believe there will be many variants of the core notion of customisation that will be quick to implement and will be available at a reasonable cost. I believe that this trend will only accelerate.”

Be that as it may, one potential limitation to going down the customisation route is lack of choice. For managers who offer mandates on commingled platforms it doesn’t matter how many investors are allocating. They only need to keep on top of one mandate. That’s not the case when large institutions start to get ambitious and decide on segregation. There are only so many separate mandates a manager can expect to support operationally; their resources are finite.

“Managers have to overcome compliance and operational hurdles and are choosing which accounts to keep; they’ll likely keep the biggest mandates (in dollar terms) and offload smaller mandates to reduce the operational burden,” says McGoohan.

Hayes says that ultimately it depends on the manager and their infrastructure capability to handle individual mandates: “If the strategy is trading pari passu with the offshore fund and the investor is writing a significant ticket I think it’s easier for managers to absorb these mandates. If you’re a start-up you could probably only handle one or two mandates.

It’s a scale game. The bigger the ticket size the easier it is for a manager to justify building out their resources.”

Like FRM’s McGoohan, Siokos says that these customisation or ‘infrastructure’
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Passion to Perform
Strengthening expertise in managed accounts

Interview with Kristin Castellanos

At Deutsche Bank Fund Services, one of the industry’s leading alternative fund and managed account administrators (the bank also boasts two leading MAPs in the form of dbSelect and dbAlternatives), putting the tools in the hands of its clients to meet the unique reporting challenges of managed account mandates is a priority.

This is critical in today’s marketplace where regulation is shaping the way fund managers approach investment management. Whilst the likes of Form PF and AIFMD are aimed at hedge funds, they naturally impact the way data is processed and delivered in managed accounts.

“You have to be a global player to understand these regulatory implications. Regulations authored in local jurisdictions have the potential to impact the investment industry across the globe,” says Kristin Castellanos, Director GTB Product Management, Deutsche Bank Fund Services.

“As a global bank with a commitment to this business, we have access to governmental and regulatory affairs and market advocacy teams that not only keep us advised on regulatory changes but give us a global perspective on how these changes impact our clients and their investors.”

For administrators, staying on top of regulation is only half the challenge. The other challenge is understanding what clients want. “Take FATCA as an example. We know what its implications are but what do clients want from us to help them comply? That’s when things move into analysis and product/system development and that’s where we are today,” explains Castellanos.

Deutsche Bank has focused on building out its flexible technology platform; a vital exercise considering the added regulatory burden of collecting counterparty details for OTC transactions under Dodd-Frank and EMIR.

“We’ve got the technology in place to collect all of that data and report it either to the responsible officer of a fund or to the investment manager to help them with their regulatory and investor reporting,” adds Castellanos.

“In addition to enhancements to our technology architecture, regulation has also prompted us to take a look at what works from a target operating standpoint in terms of a “follow the sun” model.

“That means having systems that can collect a wide variety of data from different sources and process it efficiently. Our team in Bangalore takes those feeds from different counterparties, reconciles them and sends them to our Dublin centre of excellence where daily indicative NAVs are compiled. Each morning when a manager switches on their computer in London or New York, exception reports for any unresolved breaks and all of the daily reporting – attribution reports, P&L reports and exposure reports – are already there.”

Regulation has, therefore, helped enhance the service levels for both funds and managed accounts and as Castellanos notes, it has forced the whole industry “to adopt a more efficient operating model and systems that can process high volumes of data”.

This is no more apparent than in the area of middle office support. Beyond the standard back-office support function, Deutsche Bank’s clients are able to avail themselves of reports that precisely mirror the way they view the world from a trading perspective.

As Castellanos concludes: “If you’ve got the inputs right and you’ve got the systems that can handle them you should be able to give clients the outputs they require. Our systems, our analytics and client reporting have to be a natural extension of the way the manager views the world. It’s key to delivering exactly what they want.”
solutions represent a huge growth area for Sciens’ managed accounts business. He confirms that Sciens is currently working on an infrastructure project. "It is becoming more popular to provide the knowhow and to build tailor-made solutions; this is a real growth area for us. We have already completed two such projects, one for an Asian institution, the other a Middle Eastern institution and have three more in the pipeline."

Siokos says that each institution has different requirements. Some prefer to select their own managers if they have sufficient internal resources, while others will simply say ‘Here’s X million dollars, these are our targets and objectives, please advise us on how to achieve them’. 

“The three projects we are working on right now are a mixture of the two," adds Siokos.

Aside from regulation and fears over another Madoff-type incident, one of the key drivers behind increased adoption of private MAPs among institutions is the fact that it gives them the opportunity to invest in smaller and mid-sized managers they wouldn’t normally consider. “Having a private MAP gives you the flexibility to invest in these managers which invariably have the potential to deliver enhanced returns compared to large managers.

“I don’t think private MAPs will completely take over, however. For large institutions they are another product type but they could help loosen up investor capital and bring it in to the alternatives market. Overall, I see the emergence of private MAPs as a positive trend for the industry,” says Hayes.

What is undeniable is that institutions appreciate the open architecture model provided by the likes of FRM and InfraHedge. FRM, for example, has no affiliations with service providers, a point that is becoming increasingly important in McGoohan’s view: “On the investment side, the fact that we have research and risk professionals who understand the strategies that investors are looking for is also a clear positive for us. We’re finding that that is something very important to potential investors. We understand the challenges and risks that they face as we’ve been using managed accounts as an investor for 15 years.”

For both CalSTRS and PGGM, Paquin says the approach centres on partnership and building something that “exactly and fully responds to the investor’s requirements. Any future investor can come to us and say ‘I would like to use this administrator, I’d like to establish a mandate with this manager’. It’s fully open. We can implement whatever the investor wants.

“Having said that, investors can benefit from leveraging our size and negotiating power within the industry towards administrators, custodians, prime brokers and managers, which might not be the case if they choose their own.”

Bhargava advises that any institution thinking about the private MAP option should spend time at the outset thinking through their MAP requirements and how to ensure that the customisation requirements meet their investment objectives.

“We spend a lot of time with clients on this. Once there is a long-term roadmap, it becomes very easy to implement in small steps. It ensures that every step is consistent with the stated end vision.”

This is not to suggest in any way that the commingled managed account solution is about to become redundant overnight. They are in no way incompatible with the customised solutions being talked about here, and as Bhargava states, there’s no reason why customised commingled solutions can’t evolve going forward: “Groups of investors could conceivably come together and use their collective scale to create commingled structures which are entirely customised to their requirements.”
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Managed accounts are not a new phenomenon, despite some of the media hype which would lead readers to assume that they are a recent addition to investors and investor’s armoury. In fact historically most CTAs would never have opened a fund if they had not started life offering managed accounts, which they did as a way to corral Assets Under Administration (“AUM”).

But, as soon as they had sufficient AUM they then formed a fund and encouraged their smaller investors to switch. This was because it was much more efficient for the manager to manage one fund account rather than a collection of often quite small managed accounts. It has to be said that many of the smaller investors were happy to go the fund route for their own convenience.

That convenience largely reflects the fact that the fund is administered for the investor, whereas the managed account administration is usually left up to the investor. Having said that, many of the larger institutional investors (educational endowments, as well as pension and sovereign wealth funds) prefer the managed account for very specific reasons, including, inter alia, the fact that managed accounts provide the investor with certain clear advantages over investing through a fund.

For example managed accounts provide full and open transparency, with the ability for the investor to control the trading (i.e. close the account if necessary on demand). Full transparency means that a managed account offers daily dealing which is not usually available through a fund.

It is important to remember that transparency within a managed account is not always what it is cracked up to be. An investor in a managed account who has full transparency is in the position to see what is going on and, as such, takes on some of the responsibility and risk should the account blow up – why didn’t they see it coming?

This criticism would apply particularly to managers of funds of funds or managers of other third party investment vehicles such as endowments or pension plans and the problem is of course that many of the managers of the managed accounts offer complex trading programmes which require complex minds to analyse. This is not always (in fact rarely) possible with a small investor. Even the very large institutional investors may not have the expertise in house. It has to be recognised that investors in a fund of funds will expect the manager of that fund of funds to understand the investments that they have made and to be able to interpret the trading activity. They will not be forgiven easily if there is a blow up which was neither anticipated nor understood by the manager of the fund of funds.

Other advantages are that the investor can negotiate customised terms with the manager, not only with regard to reporting, fees and other administrative matters, but also the investor may want to customise the actual trading activity – say exclude Forex Trading, or increase the weighting in metals - neither of which can be done by an investor in a fund. Managed accounts usually have lower admin costs and furthermore the
investor has a greater control over the bank accounts and cash movements – this has become very important post-Madoff.

The introduction of the managed account platform, which if I recall correctly, must have been at least 10 or even 15 years ago, has added a new dimension, particularly for institutional investors and indeed for many managers. A well run managed account platform will, or should, generate sales and thus has a marketing advantage, assuming the platform operator has any promotional expertise. However it can be seen that managed account platforms on the whole (with a couple of clear exceptions) are often more expensive than a stand-alone managed account and often match the cost of a fund, including internal expenses.

It goes without saying that anybody getting involved with a managed account platform should do their due diligence and days when one could say that they are safe because they are mostly run by big banks has been proven to be wishful thinking. Having said that, there is, at the time of writing, one particular quite large managed account platform having major, apparently cashflow, problems, although nobody is quite sure what they are because everything is “alleged” but, as of today, nothing is “proved”.

Another advantage of a managed account platform, particularly a private or customised managed account platform, is that the manager of that platform can carry out in-depth risk monitoring on a daily basis which you will not get if you invest in a fund and of course the investment is not pooled with any other entity or investor. Furthermore, it is possible to establish a managed account as a quasi multi-strategy fund by allocating different portions of the assets of the account to different managers.

Having said all of that, for a managed account platform to be efficient, the operators must have advanced technology and systems to match. This may be provided in-house or can be outsourced to the administrator that is selected to administer the platform. In this day and age the administration of funds and for that matter managed accounts is no longer a simple accounting process designed to produce an accurate NAV, which frankly was the primary function of the administrator ten years or so ago. Today administrators are data processors.

The NAV calculation is a given but the reports that are required both by managers and their investors, as well as regulators are now detailed and complex and in many cases customised. That is another advantage of the customised managed account platform in that the data that goes in, and is drawn down by the administrator, can then be processed and regurgitated in the form of a wide variety of reports i.e. data that can be manipulated to produce these reports.

Reports can vary from classic performance reports, with attribution, to detailed risk analysis. It is stating the obvious that as investors become more sophisticated, their investments become more sophisticated and their requirements become more sophisticated, so the reports produced by the administrator need to become more sophisticated.

It is very easy to say all that but with the plethora of regulation that has been pouring out of Europe and the United States, in particular, over the past two years, the pressure on IT departments to produce the reports that are required by the regulators as well as the managers is enormous. Most administrators have stepped up to the plate and some have announced new reporting platforms – indeed Custom House will be announcing in the very near future their own “Gateway” reporting module which will make life a lot easier for many managers and investors.

Dermot S. L. Butler is Chairman of Custom House Global Fund Services Limited, a member of the TMF Group, which offers 24/7, a total administration service out of fully integrated offices in Chicago, Dublin, Malta and Singapore.

For further information, please visit the Custom House website: www.customhousegroup.com or contact: Dermot S. L. Butler, dermot.butler@customhousegroup.com.

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Managed Accounts 2.0
– The rise of the buy-side MAP

By James Williams

As more hedge fund managers, particularly start-ups and emerging managers, accede to offering managed account mandates it would appear that buy-side institutions, be they fund-of-hedge-fund firms or investment advisory firms, are trying to steal a march on the big publicly-owned banking platforms. The general premise is that these institutions are more closely aligned to investors, they understand their needs and are more solution-driven than distribution-driven.

To that extent, we are seeing something of an evolution in the managed account space as more and more institutional money gets allocated to hedge funds. In the past, investors in hedge fund managed accounts were more focused on the defensive attributes they offered: good governance, good control, segregation, liquidity, transparency etc. But as Omar Kodmani, President, Permal Group, one of the world’s leading alternative fund-of-fund firms with USD22billion in assets, comments: “That’s Managed Accounts 1.0. We feel that things have advanced quite a bit from there. The new requirements of Managed Accounts 2.0 are much more than that. It’s no longer about investing for defensive reasons but how to achieve desired investment objectives.

“Where we feel there’s a lot of scope for differentiation is in the return-seeking part of the equation (more offensive attributes). It’s not just about controlling risks but returns as well. We can generate differentiated returns by having higher quality managers on our platform, as well as boutique managers where we feel we have the operational security to take them on board and exploit the alpha generation that they can offer. In addition, we
look to change the mandates with managers to try and generate higher returns, which we can do, for example, by asking them to run more concentrated portfolios."

Factor in the ability to negotiate fees with managers, further improving overall performance, and one begins to understand how firms like Permal are bringing an investment solution approach to running buy-side MAPs.

Every manager that gets onboarded is done so with an investor mindset. This is why FoHF firms, who have the experience and expertise in manager selection, are potentially a compelling option for investors. Right now the Permal platform has 87 managers representing some USD8billion of assets; for comparison, that figure was sub-USD7billion only 18 months ago.

According to Kodmani, that figure of 87 managers is not static; each year anywhere up to 10 or 15 names will be replaced if they no longer meet the investment criteria.

“A two-year run rate is probably the average. We always seek the best return potential for our clients and if we decide after six months the investment proposition no longer holds value that’s okay, we’ll remove the manager and move on.”

Omar Kodmani, Permal Group

Controlling the investment mandate as the investment advisor is certainly a key differentiator. A lot more focus is given to analysing investment risk in the portfolio and providing more fiduciary intelligence than investors would potentially get elsewhere. This means that many institutions are a lot more comfortable with the idea of investing in a commingled mandate, rather than incurring the additional costs (higher tickets) of having separate managed accounts.

“We’ll have certain institutions that come to us and say ’We are going to make a large allocation to a specific manager’ and if that allocation is large enough we can offer them dedicated investment vehicles. If those allocations are going to be smaller then they may have no choice but to allow for a commingled vehicle which Guggenheim can then show to other potential investors, providing economies of scale for everybody. “Many institutional investors are comfortable with the commingled account option because they realise that we offer separation of governance from trading. They’re not worried about a manager imposing gates or having style drift, or potential valuation issues because we provide an independent oversight of everything that goes on in the account vehicle on a day-to-day basis,” says Chitkara.

Even though institutions are moving towards direct investing, be it through commingled funds or managed accounts, many will still avail themselves of consultants and advisors who have the expertise and resources necessary for a pension fund, for example, to identify which managers to invest in. Once they’ve identified those...
Managed accounts: more than operational vehicles

By Stephen McGooohan

FRM, now part of Man Group Plc, is one of Europe’s established alternative investment specialists and runs an extensive buy-side managed account platform with USD7.9 billion in assets (as of 1 October 2013).

FRM treat their managed accounts as more than just operational tools; they provide benefits in the investment process. Improvements to the research, risk management and portfolio management processes are expected to result in improvements in the overall investment performance for clients; a point FRM are keen to stress is their foremost concern.

Examples of utilising the investment potential of managed accounts include the ability to tailor the use of leverage in the account to adjust the expected volatility of the underlying trading programme; carve-out specific strategies that don’t add sufficient value; or restrict financial products that do not meet investor’s liquidity requirements, such as private holdings. The ability for an investor to control these factors could expand the investible universe to include managers who would otherwise have been excluded.

This level of control over the underlying strategy combined with the transparency that managed accounts provide has the potential, in FRM’s view, to enhance the portfolio management process.

One example is by improving the ability to manage volatility at the portfolio level through stress loss monitoring and providing investors with the tools required to run more concentrated portfolios. Managing a portfolio of hedge funds is also as much about controlling exposures to asset classes and risk factors as it is about buying and selling hedge fund managers. Portfolio managers at FRM and investors in FRM’s managed accounts can view key risk and performance information by asset class both aggregated at the portfolio level and specific to individual investments. This enables FRM’s portfolio managers to manage their gross and net exposures in line with their mandates, designed for and with end investors. This, in turn, allows investors the opportunity to discuss increasingly bespoke constraints on FRM.

These bespoke constraints could be ensuring that certain exposures within the portfolio have been kept to zero for regulatory purposes, or that exposure to certain asset classes is within a set limit; often to enhance an investor’s non hedge fund portfolio. This can be done on segregated portfolios of managed accounts where FRM has full investment discretion, but increasingly clients are asking for advisory arrangements where the level of involvement by FRM is tailored for the client.

Another important method of improving performance for clients is via negotiation of lower fees. The critical aspect for platform providers to achieve this is scale; something that FRM believes it has.

As a result of active negotiation with the investment manager, if the assets in a managed account rise above a certain level it is often the case that the incremental management fees will drop. FRM’s investors are direct beneficiaries as any negotiated discounts are passed directly to them, not FRM. The same is true with service provider fees.

In summary, FRM believe that managed accounts are more than the simple operational vehicles they are often portrayed as. Because of the direct investment focus of the company, they are in no doubt that managed accounts can be a benefit to all investors; be it in commingled fund of funds, advisory mandates or fully segregated accounts.
When we say ‘managed accounts,’ we mean that we set up fund vehicles where we are the registered investment advisor and can step into certain fiduciary roles at the direction of our clients.”

Ajay Chitkara, Guggenheim Fund Solutions

Permal team developing top-down investment themes, after which the appropriate manager(s) is approached to exploit the chosen theme. This is an important trend because it’s putting FoHF firms on more of a front foot.

“I do think it is putting players like us in the driving seat in terms of being an activist with regards to portfolio allocation, thematic investing, choosing which managers to use and how to use them. If in the past end-investors thought that their investment partner was merely someone that provided them with access to managers that is no longer the case today. We’re shifting the influence to us,” says Kodmani.

A good example of this thematic approach to managed account investing is the US energy revolution. Kodmani says that they’ve scanned the universe of US long/short equity managers, identified the best talent, and approached those managers to run a mandate that is focused purely on identifying winners and losers in the US energy revolution.

And it seems that managers are quite receptive to this approach.

“When we are developing thematic ideas we tend to get a strong response from managers. They are willing to cooperate because for them it’s also breaking new ground. If the strategy works then they can offer it as a new product to their investors so there’s an R&D benefit to them,” adds Kodmani.

For the managers themselves, they must ensure that they have a strong operational framework in place to support managed account mandates. Key to this is automation. The world of spreadsheets and utilising myriad systems to keep track of trade

“When we say ‘managed accounts,’ we mean that we set up fund vehicles where we are the registered investment advisor and can step into certain fiduciary roles at the direction of our clients.”

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Institutional credibility is vital for managers

Interview with Paul Compton

“There is what I call a Holy Trinity for hedge funds. They’ve got to be able to raise capital, they’ve got to be able to deliver performance, and they’ve got to be able to control costs,” says Paul Compton, head of strategy in SunGard’s asset management business. Within the context of managed accounts, the last point on cost control is especially important.

One of the clear drivers of interest in managed accounts among institutional investors is the need to demonstrate to their own stakeholders that they have all the checks and processes in place to mitigate the risk of fraud. Managed accounts give them the segregation of funds and the transparency they need, but as demand grows, so does the operational complexity for managers.

“Operating managed accounts places a premium on a manager’s ability to automate things like allocations, fee calculations and service potentially a large number of investors, each within effectively their own separate fund,” says Compton.

Automation, says Compton, is now an imperative. Managers cannot rely on spreadsheets when they have multiple managed account mandates as things like tax reporting become too complex. Each mandate will be slightly different, and it is this customisation feature that makes managed accounts more demanding than a commingled fund where all investors are treated equal.

“The kind of investor that wants to be segregated will expect a high standard. The world of spreadsheets might not be something they want to see when they do their operational due diligence,” adds Compton.

In a recent survey of global hedge funds conducted by SunGard, 82% of senior hedge fund executives agreed that institutional credibility is ‘extremely’ or ‘very important’ to their business, especially when it comes to raising capital from institutional investors. To be successful requires having a robust automation process.

SunGard understands this and last year rolled out Hedge360 to deliver institutional credibility in a cost-efficient way. Hedge360 provides a hosted, integrated platform for hedge funds to pick and choose proven solutions in areas such as portfolio management, fund accounting and investor allocations that deliver precisely the kind of automation now required by the industry.

“Hedge 360’s investor accounting capabilities support the proper automated handling of all investors, including managed account investors,” says Compton, noting that overcoming the complexities of multiple fee structures is a key component.

“Managed accounts aside, most hedge funds have a pretty complex entity structure whether it’s masters and feeders, partnership-based accounting for US investors, equalisation-based accounting elsewhere. Some investors are carved out in side pockets and remain in only the liquid investments. Potentially you have almost as many fee calculation formulas as investors.

“This creates a high level of complexity in the investor accounting process. With SunGard, hedge funds can manage all those different fee structures in an automated way.”

Hedge360 is a cloud-based platform. Therefore, by choosing a proper investor accounting platform as they evolve and potentially take on managed accounts, hedge funds have the ability to control costs yet still present a robust institutional-quality operational framework to investors.

“That’s the benefit of having a hosted, integrated platform. We can take care of the technology management and infrastructure, which deploys proven solutions with a lower total cost of ownership. With institutional credibility now a priority for any fund looking to raise capital, we can provide that institutional-quality framework, allowing hedge funds to automate their processes as they take on more managed account mandates.”
lifecycles from front to back is pretty much over. This is especially so for managers who take on managed account mandates because the level of detail and additional reporting required is substantial.

SunGard has been quick to respond to this. Last year it rolled out Hedge360, a hosted integrated platform composed of various modules, all of which are designed to work in synch to give managers the operational robustness investors now demand.

“InvesTier is our investor accounting solution and is the most relevant to managed accounts. It’s a very powerful platform for managing investor allocations, fee calculations, tax reporting etc. We now have 20 global clients using the Hedge360 platform and feel good about the pipeline going forward,” explains Paul Compton, head of strategy in SunGard’s asset management business.

Institutional credibility is imperative for today’s hedge fund manager says Compton. Using automated systems on a platform that gives them transparency and control of their business is a key consideration, especially for newer managers who have the opportunity to raise assets through offering managed accounts.

“With Hedge360, managers don’t need to take on a large internal IT group, they don’t have to spend money on hardware and separate systems, and they have the ability to add different modules – and different functionality – as they evolve,” says Compton.

Deutsche Bank Fund Services is one of the industry’s leading managed account administrators. Over the last few years it has developed a highly flexible and sophisticated technology infrastructure to support the exacting demands of managed account reporting both to investors and regulators. Given that it operates two leading MAPs of its own – dbSelect and dbAlternatives – the firm is ideally placed to respond to changing market conditions.

Kristin Castellanos is the head of Product Management, Deutsche Bank Fund Services Alternatives. She notes that clients have responded particularly favourably to the fact that all reporting is now done through the bank’s Autobahn portal.

“It’s a single sign-on to all of the applications used at Deutsche Bank. When our clients log on to Autobahn they can now access a customised dashboard that consolidates all of their Deutsche Bank applications in a home page toolbar. This allows them to click on any client-based application and see all of their customised reports, many of which have been designed to be presentation-quality. These reports are often sent upstream to their investors and include attribution and exposure pie charts, bar graphs and other types of customised graphics. Today’s administrator has to be able to put these kind of value-added tools into their clients’ hands.”

A key focus of its administration capability has been the gradual build out of its middle office services over the last 18 months. The key driver for this is transparency. Castellanos confirms that Deutsche Bank systems now have the capability “to allow managers to track exactly where we are in the NAV calculation cycle. This is all about giving clients more transparency into our workflows. We have begun internal testing and should be able to offer this to clients by Q2 next year.”

As Castellanos rightly points out, with managers having to deal with so much data by virtue of regulation, or because they are running multiple versions of the same investment strategy, what they absolutely need, regardless of whether it’s a Cayman fund or a managed account, is a single view of their world.

“A fund manager wants that holistic view of the world no matter how many funds, managed account mandates they might have. We allow clients to see all their portfolios in aggregate, see their overall exposure and basically see everything they want regardless of whether they are the AIFM or not – which is important if they are acting as a sub-advisor to a managed account on a platform.”

A good point given that this is exactly the case when managers join Guggenheim Fund Solutions’ platform.

Chitkara believes that the model Guggenheim has developed will be important to the hedge fund industry, going forward: “The model that we’ve created will be the only way that many institutional investors are going to get comfortable making large allocations to hedge funds because they know we are completely aligned with their interests.”

Kristin Castellanos, Director GTB Product Management, Deutsche Bank Fund Services

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