Alternative platforms grow as regulation tightens

Identifying the right strategies is critical to success

Performance encouraging for investors
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Alternative investments can involve significant risks and the value of an investment may go down as well as up.
Equity-related strategies experienced a fairly quiet first half of 2012. Stephane Berthet, Head of FundLogic Alternatives, confirms that, as a platform, "we were able to raise assets predominantly in our established funds, although more so towards the end of last year".

Lower volatility strategies such as event-driven or global macro were preferred by investors because equity risk was too important. This favoured managers such as P. Schoenfeld Asset Management LP (PSAM), whose MS PSAM Global Event UCITS was able to raise a lot of assets, according to Berthet.

"Since Q4 2012, the improvement in market sentiment has meant that investors have become focused again on equity-related strategies. We started to see inflows towards the end of 2012 and this has continued on..."
into 2013,” confirms Berthet. Equity long/short funds with exposure to Asia, such as Indus Capital, have, in particular, enjoyed net inflows.

“For equity-focused managers on the platform, they have raised more than USD250million in assets so far this year,” adds Berthet.

Another fund that has attracted investor capital has been the MS Alkeon UCITS fund, a tech-focused growth fund which, according to Citywire, returned 12.33 per cent in 2012.

On aggregate, the FundLogic Alternatives platform has approximately USD1.4billion in AuA. A further three funds are in the process of being added but as Berthet confirms, “Our goal is not to be a ‘fund supermarket’. We onboard funds selectively as we try to identify gaps in the market. At this stage, we do not intend to have more than 25 to 30 managers on the platform.”

Alceda Fund Management operates the Alceda UCITS Platform (AUP). Since it launched in 2007, total assets on the platform have grown to over USD7billion, making it Europe’s largest independent UCITS platform.

To tap in to growing investor demand for regulated funds, the firm has opened up offices in Hong Kong and London; a market in which Helmut Hohmann, managing director of Alceda Fund Management, sees high potential for asset managers wishing to establish funds with a European passport.

This wider footprint is helping raise the profile of AUP. At the end of May 2013, the firm announced that it had successfully redomiciled the Stafford SICAV – Global Equity Fund for Rasini Fairway Capital, a long-established FoHF, to Luxembourg in a regulated UCITS format. The offshore fund had, until this point, been domiciled in the British Virgin Islands for 20 years.

“We sold all assets that were not UCITS-compliant in order to help them utilise the European passport to leverage broader distribution capabilities across Europe,” explains Hohmann, who continues:

“In addition we have added one global macro fund for managers based in London, as well as funds for two Australian managers. Our global remit is growing and we see a lot of potential for the future.”

Over the last 12 months, Alceda has added a total of 12 managers to its AUP, totalling around EUR700million in net new assets.

Alceda has also recently signed up two major US fund managers – Miller/Howard Investments and Clark Capital Management Group – as it bids to consolidate its position.

Of course, part of the trick for platform success is spotting the right talent. You can have the greatest distribution network in the world, but if the funds aren’t delivering on performance investors aren’t going to register interest.

Both Alceda and Morgan Stanley’s FundLogic Alternatives platform have recently entered strategic partnerships.

Alceda has teamed up with ECPI Group to deliver a series of funds based on the ECPI Global Megatrend Equity Index, moving AUP into the realm of sustainable investments. The idea being that both ECPI and Alceda will collaborate with international investment firms in providing a series of ECPI-related funds based on the “mega-trend” philosophy and each investment firm’s approach.

“There are different strategies we are currently working with spanning equity long/short and long-only, to bonds. One of the first asset managers is Northern Trust. They have a good seed capital pipeline, which we are happy about because we want managers on AUP to build good volume,” says Hohmann.

Morgan Stanley, meanwhile, has teamed up with Equinox Fund Management, a US-based multi-manager that specialises in CTAs, to help onboard a series of differentiated CTA funds. Four funds have
Our Hedge Fund Experience Now in UCITS

Access 2 High Profile Managers in UCITS – Canyon* and Winton**

†Figures as of 30th June 2013
*Canyon Capital Advisors LLC
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There remains a common misperception among some investors that UCITS fund structures are more costly than offshore funds due to additional reporting requirements, frequent NAV calculations and use of derivatives. But as Jason Funk, a member of the alternative investments business development team at Lyxor Asset Management is quick to point out, alternative UCITS funds are actually quite cost efficient.

“Hedge fund managers are responding to fee compression in the market. We see them launching UCITS funds to reach a completely different investor base. Although they are not always pari passu versions of their offshore strategies, they are being offered to investors at similar and often lower fee levels as managers seek to diversify their investor base. We are always surprised by the misconception of cost that continues with investors. Not only are the management fees often lower, compared to offshore hedge funds, but in some cases feature lower performance fees as well.”

Take Canyon Capital, whose Canyon Credit Strategy Fund, an event-driven credit fund, joined the Lyxor UCITS offering in February 2013. The fund is based on Canyon’s offshore credit and event funds. Whereas the offshore fund continues to use the tried and tested 2/20 fee structure, the UCITS version uses a 1/10 fee structure.

“They are doing this for two reasons: firstly, to offer the strategy to investors unable to invest in offshore funds. Secondly, because under UCITS rules, the fund is a slightly more constrained than the offshore fund; it’s not drawing from the full investment universe afforded in the offshore version,” says Funk.

The investment fund industry is undergoing a trend of convergence currently. Whilst on the one hand, hedge fund managers are doing cost benefit analyses and, where viable, launching UCITS versions of their offshore strategies, on the other hand traditional asset managers are moving away from the long-only universe. They are becoming more hedge fund-like by launching absolute return funds.

And when you consider the size of the UCITS universe, the scale of opportunity available to both traditional and alternative fund managers is huge. Today, alternative UCITS make up a small percentage of the UCITS universe with around EUR155 billion in AuM. In contrast, total UCITS AuM is around EUR6.6 trillion.

“UCITS funds may not necessarily be the cheapest to set up, but it’s the scale of opportunity that makes them worthwhile,” says Funk.

“With the AIFM Directive coming up, and managers unsure as to how they will be impacted, the UCITS wrapper is a good alternative for them to diversify their client base, both in Europe and beyond.”

The key to whether an alternative UCITS fund is successful, and profitable to the manager, is distribution. With a staff of more than 600 across Europe, managers that partner with Lyxor can be sure that their funds are getting out into the right markets, thus maximising their chances of building assets.

Lyxor’s UCITS single manager offering includes a small, highly reputable cast of external managers: Winton Capital, Canyon Capital, Tiedemann, Caxton Associates and Old Mutual Asset Management.

“All of these managers benefit from our distribution expertise across Europe. It can be difficult for managers to market UCITS effectively. Most do not have the sales teams on the ground needed to successfully market UCITS. We take care of a lot of the footwork in terms of marketing the funds,” says Funk.
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been added since October last year: Winton Capital, QIM, Mesirow Financial and Quest.

“We try to add managers that we believe investors want to invest in. It’s important to cross-check investor appetite with people who are used to buying these strategies, which is why we thought it would be useful to leverage Equinox’s expertise; not simply to onboard CTAs, but CTAs that can offer diversification,” explains Berthet.

Winton is a mid- to long-term trend follower, for example, while QIM is the world’s largest non-trend following CTA.

Once the right talent is discovered, platforms will want to see performance come through because with performance comes investor inflows.

“The key thing for us, with all our funds, is performance and something we always work hard on to get right,” states Ian Swallow, Head of UCITS Management at Man.

Man’s GLG European Equity Alternative fund has soft closed, for example, having attracted more than USD1billion in assets.

“Funds like this have not only delivered short-term performance but are based on a solid strategy and a proven track record; we’ve soft-closed the European Equity Alternative fund in order to protect investor interests and ensure the fund can continue to meet its objectives. Another fund in which we’ve seen strong inflows is our GLG Japan CoreAlpha fund (a long-only strategy led by Stephen Harker). That’s been on the back of strong performance: up +24.49 per cent YTD.”

The GLG Financials fund, up +6.4 per cent YTD, has also received strong inflows.

The net result is that total (including long-only) assets on the Man Group UCITS platform have swelled from USD8.4billion a year ago to USD9.8billion through May 2013.

“We’ve got some additional products lined up for later this summer. The pipeline is looking promising and we’re genuinely excited by the new funds that are scheduled to come on board,” adds Swallow.

Hohmann says that the highest inflows this year have been going to global macro managers and equity long/short managers. The best performer, YTD, has been in the Tideway Global Navigator Fund, managed by London-based Tideway Investment Partners and launched in September 2011. The fund, which invests primarily in fixed income and FX, is up +21.35 per cent over the past 12 months and up around +4.54 per cent YTD.

“We also have a CTA fund – the Amandea Hybrid fund – that has proven successful. It is the best in its peer group and is up +8.78 per cent over the past six months.”

All of this suggests that alternative UCITS platforms are doing a solid job of diversifying the talent available to investors, and enjoying some encouraging performance.

And whilst it is unlikely that growth is likely to abate any time soon, there are more regulations coming in to the UCITS market that will, undoubtedly, make managers’ lives more difficult.

ESMA, for example, has introduced new guidelines that first arose when looking at the use of indices and total return swaps (TRS) in ETF products. These tighter guidelines are now being applied to all UCITS funds and will effectively prevent managers from using customised indices; this is a big concern for those who trade commodities, and who need to rely on TRS to get around the issue of trading physical commodities.

Diversification is one key requirement. For example, a UCITS will not be able to invest in commodity indices that do not consist of different commodities. That means WTI Crude, Brent Crude, Gasoline and Heating Oil would be regarded as all sub-categories of the same commodity. This is not ideal for any manager that trades just energy contracts as part of their investment strategy.

On the issue of using custom indices, paragraph 51 of ESMA’s guidelines reads: “An index should not be considered as being an adequate benchmark of a market if it has been created and calculated on the...
request of one, or a very limited number of, market participants and according to the specifications of those market participants.”

So no opportunity for customisation.

Index providers will also be prevented from rebalancing the index on an intraday or daily basis and providing a clear transparency on the index methodology and creation to investors.

Andrew Knowles is Senior Vice President at RIMES Technologies, a specialist provider of managed data services including indices and benchmarks. He notes that the buy-side industry has been quite mature in dealing with the index transparency issue, having found solutions with their index providers to show the requisite level of detail, but adds that the index providers still have concerns.

“The big issue is having to put a website link in the fund prospectus to the constituents and security weights of the index being used. Understandably, index providers are concerned at having to provide that level of transparency because it’s their bread and butter. This is all about ESMA and the EU pushing for transparency. That’s what regulators want and that’s what these guidelines are addressing.”

On the customisation point, Knowles adds: “I think this is ESMA basically saying ‘you can’t do that anymore’. A benchmark needs to be exactly that: a well-known, well-defined vanilla index. But this doesn’t just affect hedge fund managers. Take a pension fund needing to prohibit self-investment. They require the index provider to remove their own stock and re-weight the rest of the index accordingly. Does that now mean they can no longer use a UCITS structure because of this customisation of the index?

“There are a lot of practical implications to this point on indexing that ESMA hasn’t fully elaborated on.”

These tighter guidelines suggest that European regulators are getting jittery over the increased adoption of the UCITS wrapper by hedge fund managers.

Addts Knowles: “I think the regulators got concerned when hedge funds moved in to UCITS and started to push the boundaries. They started getting cold feet, fearing what could happen if something went horribly wrong for investors.”

Even though the guidelines are quite tough, they will help bring back investor trust, according to Hohmann: “We always say that form follows function. If the manager needs commodities to make their strategy work we wouldn’t tell them to use a UCITS structure. Rather, we advise clients on alternative options i.e. Luxembourg Part II funds.”

Another stumbling block, which could benefit service providers like RIMES, relates to paragraph 61 of ESMA’s 2012/832 guidelines. This states that a UCITS must ensure that the financial index is subject to “independent valuation”. By whom, exactly, is unclear.

“We would be extremely well placed to provide such a service to asset managers and UCITS fund providers should that be the direction the legislation is to be interpreted. But there was nothing in the first Q&A on this issue, and even when I pushed ESMA they said it would be in the next Q&A,” clarifies Knowles, who adds:

“With the recent index scandals and poor public image of indices, it may be advantageous for fund providers to have their benchmarks and indices valued independently by a third party. We already roll up benchmarks from the constituents upwards and do checks on them so we could easily use a client’s own pricing hierarchy, or one provided by ourselves, to calculate those valuations.

“Anything we can do to remove the burden of the index and benchmark data side of things is clearly of benefit to clients and one less thing for them to worry about in the current regulatory environment.”

Andrew Knowles, RIMES Technologies
Over the past 12 months, total AuM in alternative UCITS funds has risen from EUR139 billion to EUR155 billion. In 2008, that figure stood at EUR28 billion.

Given that the majority of money coming into these products is mostly retail money, invested through private banks and FoHFs, the size of allocation is not substantial. As Amy Bensted, Head of Hedge Fund Products at Preqin, comments: “There’s still less than EUR200 billion invested so the industry is not growing as much as people expected a few years ago. However, we think alternative UCITS funds will remain a good option for investors who are looking for volatility dampening, liquidity and greater transparency.

“The appetite is growing, but the money is not there yet. I think we’re still a couple of years away from the big institutional money coming in to these funds.”

This month Preqin launches its latest special report on UCITS hedge funds (see www.preqin.com). Critical to the success of these funds, and what investors will always look at when selecting which funds to choose, is performance. And as the report shows, things are starting to look up for alternative UCITS compared to their offshore hedge fund brethren.

For Q1, 2013, alternative UCITS returned 2.46 per cent compared to 3.22 per cent for hedge funds. Over the last 12 months, the figures are 3.75 per cent and 6.88 per cent respectively.

This year is particularly encouraging because it demonstrates that given that they operate under tighter rules, alternative UCITS are doing exactly what they are supposed to do: keep pace with hedge funds, but sacrifice a little bit of performance for less volatility.

As the report shows, relative value, long/short equity and global macro are the most popular strategies as they seem to best fit the liquidity constraints of the UCITS framework. Relative value strategies are much less prone to liquidity swings. Results show that three-year volatility is just 2.1 per cent, compared to 6.9 per cent volatility for long/short equities and 4.3 per cent for macro strategies.

Taken as a whole, the three-year rolling volatility for UCITS hedge funds is in the 5 to 8 per cent range, whereas the S&P 500’s volatility range was 15 to 22 per cent.
In terms of overall performance, long/short equities lead the way. Between end-2009 and end-2012, they returned more than 8 per cent, and thanks to the strong equity market rally this year, that figure through March 2013 was in excess of 12 per cent. Relative value and macro strategies, during that three-year period, returned 5.08 per cent and 5.24 per cent respectively. Indeed, 54 per cent of all UCITS hedge fund launches in 2013 have been long/short equities, with macro strategies accounting for 31 per cent of launches.

Another encouraging point to note is that more than 70 per cent of UCITS hedge funds made positive gains over a three-year period, with more than half exceeding 10 per cent returns. In 2012, 40 per cent of funds were able to generate more than 5 per cent. Again, considering the attributes of these funds – better liquidity, regulated, transparent – these are respectable returns.

“There are some good performers in the alternative UCITS space now and some of the funds are starting to get large. That will have a positive impact. Size is important in attracting seed capital, gathering assets, and once more funds build momentum the space will become more interesting to institutional investors who want a lower volatility component to their alternative investments portfolio,” says Bensted.

“We are still in the early stages of evolution. I think in a few years it will look much more different and be a lot larger than it is now.”

Without doubt, the alternative UCITS space has crossed the Rubicon. This is not a transient trend. In many respects, given the profile of investors right now, it closely resembles the hedge fund industry of 15 years ago. Most of the money was HNW, FoHF money until suddenly, post-2008, institutions started to seriously ramp up their interest to the point where they now dominate the hedge fund industry. Alternative UCITS could well follow a similar trajectory over the coming years.

Year-to-date, the UCITS Alternative Index Global is up +0.94 per cent compared to +1.63 per cent for the calendar year 2012. Whilst long/short equity is the best performing strategy YTD, with gains of +3.39 per cent, one of the more surprising developments has been the performance of FoFs. The UAI Fund of Funds Index is up +1.24 per cent, having lost -1.34 per cent through 2012. June 2013 was a tough month, as equity markets pulled back, causing the index to give back 1.85 per cent.

Last July was certainly a tipping point, however. Between July 2012 and May 2013, the FoF Index – which is calculated by Geneva-based Alix Capital – generated positive returns every month, except for October (-0.54 per cent).

“Fund of funds are doing better than the wider market,” comments Louis Zanolin, CEO of Alix Capital. “For the first time since we began running the index, FoFs have been able to add value over and above the wider market, so that’s encouraging. The ones that have done well over the past 12 months are those that tend to have a large allocation to long/short equity – 50 per cent or more. Some of the single manager funds that have done well include Egerton Capital’s Schroder GAIA Egerton Equity Fund and the Odey UK Absolute Return Fund.”

Even though overall performance in the alternative UCITS space is good, Zanolin says that, “Since June 2012 inflows have largely been because of investors’ need for regulated products as opposed to performance per se. So it is very helpful to the industry to have a good period of performance.”

Lyxor Asset Management added three managers to its UCITS offering in early 2013, even though they only have short-term track records, performance for each has been strong thus far. The three funds in question are: Canyon Credit Strategy Fund, Tiedemann Arbitrage Strategy Fund, and the Lyxor/Winton UCITS Fund.

“Our new UCITS single manager hedge funds include a systematic trend-following CTA, a liquid event-driven global credit
Identifying the right strategies is critical

Interview with Ian Swallow

The key to offering a robust UCITS platform to support hedge fund strategies is making sure that what is being offered is suitable for the specific clients being targeted, according to Ian Swallow, Head of UCITS Management at Man. Over the last 10 years there has been a huge shift in market regulation. As hedge fund managers have moved into the UCITS space, so European regulators have been quick to increase the level of scrutiny on new launches. Put simply, the barriers to entry for launching an alternative UCITS fund are high. If you lack the ability to demonstrate a clear understanding of which strategies should best be targeted to UCITS investors, and to then work effectively with regulators to bring them to market, it is unlikely you will succeed.

With approximately 40 live funds spanning Ireland, Luxembourg and the UK, and over USD9 billion in AuM (through end of May 2013), Man has built a formidable platform to support its clients looking for UCITS regulated products. But as Swallow emphasises, the approach has not been to simply shoehorn existing Cayman hedge fund strategies into a UCITS wrapper and hope for the best. A careful, measured approach is paramount.

“We’re not here to try and leverage off successful offshore hedge fund strategies, give it the same name in a UCITS format and try and sell it. We won’t compromise our investment strategy just to fit it into a UCITS wrapper,” says Swallow.

“We only create UCITS funds in strategies that are best suited to work under UCITS guidelines. For example, we wouldn’t look to package some of our credit strategies in a UCITS format as we wouldn’t be able to provide the required liquidity terms; it’s not right for that kind of investment. So we need to make sure that the funds we are selling are the right ones.”

At Man, UCITS funds have largely enjoyed great success, precisely because they have delivered on performance, and attracted investor inflows: a virtuous circle. Take the UCITS version of the GLG European Long-Short strategy. This has now soft closed with more than USD1 billion in AuM as at the end of May 2013.

“Performance creates investor demand. Another in which we’ve seen really strong investor inflows is our GLG Japan CoreAlpha strategy,” confirms Swallow. A long-only strategy managed by Stephen Harker, it is currently up +24.49 per cent YTD.

Also key to Man’s success is its ability to leverage off years of structuring experience.

“We’ve onboarded funds spanning a range of assets, we’ve got good relationships with both legal counsel and the regulators themselves in Luxembourg, Ireland and the UK.

“This enables us to have more open conversations with them. We can explain the various risks involved in a proposed strategy and how we intend to manage those risks. It’s not about presenting something to the regulator and them saying yes or no, it’s more of a dialogue. We know the process of onboarding new funds, and we know how to explain things in a way that regulators understand.”

This expertise has helped Man successfully launch two UCITS-compliant managed futures funds for its AHL team, cognisant of the fact that both funds will readily comply with ESMA’s new guidelines on index creation and methodology.

“Fundamentally, to be able to offer useful, creative and successful alternative investment strategies within a UCITS framework, you need significant product structuring experience and resources,” confirms Swallow.
New Swiss regulations on marketing of alternatives

By Daniel Häfele

“I’d like to distribute my hedge fund in Switzerland – is that still possible?” “We are a specialist in offshore funds. Will you take us on as a legal representation client?”

At ACOLIN, we get questions like these almost every day. The answer to both is: yes, it is still possible to distribute hedge funds in Switzerland, but under certain conditions. And yes, we are open for business.

The laws now cover the distribution of all collective investments (CIS) in Switzerland, including AIFs such as hedge funds, as well as UCITS and other retail products.

The revised CISA demands that all CIS offered to qualified investors in Switzerland have to meet the following preconditions:

- Appoint a representative and a paying agent.
- Adding the representative and the paying agent to all Swiss fund documents (including KIIDs).
- Sign a distribution agreement with the representative to which Swiss law is applicable.
- Proof that you are in possession of an authorisation to distribute CIS in your country of origin.

The transition period of 1st March, 2015 only applies if you have been distributing CIS to Switzerland before 1st March, 2013 and for CIS launched before that date. If you plan to distribute newly or take new funds to Swiss investors or distribute grandfathered funds to new distributors, you will have to comply with the above-mentioned prerequisites from the start. In addition, distributors may ask you to comply earlier than the final date, as they may be subject to new regulations, effective this August.

Choosing a legal representative

Once you have decided to distribute in Switzerland, you will need to choose a representative. The following selection criteria should be considered:

- The representative has a licence that extends beyond March 2014. Banks, securities dealers, and insurance companies could offer representation services on the back of a banking or securities dealer licence. Now, they have to file a new application with FINMA to maintain this license.
- The representative is able to take on your fund. Not all representatives are equipped to accept offshore funds.
- The representative provides a distribution network, which gives you access to the distribution channels, as financial intermediaries can only do business with you on a contractual basis.

Working with ACOLIN

At ACOLIN, representation and distribution network management are our core businesses. Our set-up process, tried and tested by more than 50 clients, helps you to get into the markets without delay:

- We advise you on your fund registration and distribution strategy.
- We act as legal representative for your funds for the distribution to qualified and/ or non-qualified investors vis-à-vis the authorities, our distribution partners, and investors.
- We help you to set up and carry out your fund business in Switzerland.

The regulatory responsibilities of Swiss representatives are onerous. The start of our process is a detailed operational due diligence review of the funds and the manager, to determine if a minimum set of requirements, similar to the AIFM operational requirements, are in place. At present not all the regulations and constraints are fully defined and as the regulations become clearer, there will be changes in the services offered by the industry. We are working hard to remain at the front of these changes.
industry

“We’re pleased but we think there’s a lot more to come. We’ll be doing our utmost to replicate the level of outperformance last year; both this year and in future years.”

Vernon West, Skyline

Companies, and as such fits quite neatly into a daily priced UCITS fund. It is not, however, run pari passu to the offshore hedge fund.

“We use the same diligent, bottom up, fundamental approach and look for the same attributes in companies we invest with, but we are subject to UCITS risk limits, and that means the fund has a slightly more defensive, lower volatility profile,” says West.

Emerging markets have not had a good run this year. The MSCI Emerging Markets Index has slumped -13.55 per cent, falling -2.1 per cent alone on 3 July 2013 amid concerns of a slowdown in Chinese services industries. However, the Skyline UCITS fund has remained resilient – testament to the stock-picking talent of the team – and through 1H13 is up +1.4 per cent.

West confirms that in 2012 the hit rate for ideas in the fund was “rather high”, helping to lock in broad-based performance and strong alpha generation in both the long and short book.

“Notable themes that helped us on the long side were education in Brazil, travel in Latin America, and Turkish autos. On the short side, going short solar companies was a key trade in terms of profit generation, as was being short a Brazilian pulp and paper company,” says West, adding that in 2013 two key investment themes on the long side have been Russian hypermarkets and Chinese casinos.

“Russian hypermarkets are currently underpenetrated – representing around 10 per cent of total food retail footfall – so there’s plenty of scope to roll out the hypermarket format across Russia. Also, since the start of 2013 there’s been a ban on sales of alcohol in small shops, which has led to greater footfall in the hypermarkets.

“In Hong Kong, we’ve had positions in Chinese casinos and there again you’ve got

One of the best performing equity long/short funds is the Skyline UCITS fund, managed by London-based Skyline Capital. Last September, the fund completed its first year of trading and recorded an impressive 20.5 per cent return, placing it firmly in the top one per cent of all alternative UCITS funds.

The UCITS fund is based on the firm’s emerging market-focused long/short equity strategy. Assets have grown an impressive 65 per cent YTD to USD123million.

“We’re pleased but we think there’s a lot more to come. We’ll be doing our utmost to replicate the level of outperformance last year; both this year and in future years,” asserts Skyline’s CEO, Vernon West.

The strategy predominantly targets large- and mid-cap emerging markets-focussed

To stress, it is not always possible to offer pari passu versions of corresponding offshore hedge funds due to UCITS investment restrictions such as physical commodities or shorts. Accordingly, our UCITS hedge funds have been designed thanks to Lyxor’s proven experience in replicating alternative strategies coupled with the managers’ overall expertise in the given strategy.”

The fact that the nature of the alternative UCITS market is gradually changing might explain why performance is improving. Currently, only 12 per cent of funds are long/short equity, by AuM. That figure is much higher in the offshore market. Also, onshore equity-focused funds tend to be less directional and more market neutral in nature, but as Zanolin explains: “This is changing slowly, particularly with the rise of platforms bringing on US managers who tend to take more risk and be more directional. I expect that to further evolve in the future as more US managers enter this space. For the time being, the number of single managers who have performed really well in equity long/ short remains quite small.”

One of the best performing equity long/short funds is the Skyline UCITS fund, managed by London-based Skyline Capital. Last September, the fund completed its first year of trading and recorded an impressive 20.5 per cent return, placing it firmly in the top one per cent of all alternative UCITS funds.

The UCITS fund is based on the firm’s emerging market-focused long/short equity strategy. Assets have grown an impressive 65 per cent YTD to USD123 million.

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a penetration story; 2 per cent of Chinese have visited the casinos in Macao, versus 40 per cent of Americans who have visited Las Vegas. Coming into 2013, you had completion of some key railway infrastructure cutting the journey time to Guangzhou, which is helping drive incremental footfall.

"On the short side, we’ve had a couple of key winners in, broadly speaking, project businesses in the engineering space; super low margin businesses where we’ve seen evidence of pretty aggressive accounting treatment.”

Chris Nichols is Investment Director, Multi Asset Investments at Standard Life Investments. The firm’s Global Absolute Returns Strategy (GARS) fund is one of the largest funds in the alternative UCITS space – global AuM in GARS was GBP26.7billion through end-Q1, 2013, while the UK pooled fund was GBP16.7billion.

What makes the multi-strategy fund so scalable is that it uses the largest, most liquid, and most plain vanilla instruments to express investment views.

On Europe, one of the fund’s strategies that worked well overall until more recently this year was a financial capital structure strategy. As Nichols explains: “It was designed to hold senior credit of the European financial system long versus main credit index short, in addition to holding a small short position in European bank equities. That was a strategy that paid out 3.5 per cent per annum. However, as senior credit spreads began tightening in Q1 this year and equities performed well we exited the strategy.

“Another interesting theme for us is the story of France being unreformed versus Germany having reformed its labour market,” says Nichols. The fact that France has yet to start implementing austerity measures is not reflected in market pricing in either its bonds or equities says Nichols. “We have had a German 10-year bond versus a French 10-year bond position, which we recently re-struck as a German versus France equity position. On a three-year view, we think French equities are overpriced versus Germany’s.”

Performance-wise, between end-May 2010 and end-May 2013, GARS generated cumulative gross returns of 23.8 per cent (based on the UK unit trust). Over the past 12 months, gross returns were 10.37 per cent, while this year, through May, it is up +5.72 per cent.

"Year-to-date we’re seeing positive performance in the portfolio from things like US equities and global equities. The US dollar has been appreciating against the yen, Canadian dollar, and was very positive against the euro in Q1 although it pulled back a lot in Q2.

“Another good trade has been the Mexican peso against the Australian dollar. The slowdown in China is bad for Australia. The AUD had previously been suspended in the stratosphere by Chinese resource demand.”

Nichols says that some of the key ideas in GARS for delivering strong payout in an uncertain growth scenario are US equities, large cap versus small cap, and US tech sector versus Taiwan. Being long the US dollar is designed to deliver modest payout in a growth scenario but a stronger payout in a market downturn scenario.

“Those are some of the main elements right now. We also have a relative volatility strategy that would position us to make money from higher volatility in Asian markets relative to Western developed markets. We also added global REITs to the portfolio last December.”

West thinks there are a number of reasons to remain bullish on emerging markets but stresses the import of remaining selective and identifying themes that are in a “fundamental sweet spot”.

One of those themes ties in to next year’s FIFA world cup in Brazil.

“We expect a double-digit increase in incoming passengers. We have a position in a beverages company with 70 per cent market share – the dominant duty-free concession operator – and FIFA’s global sports-ware partner. We are well positioned for this event next year.”

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