

Asset Management Forum

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Abstracts

Hedge funds: sell-side investments versus buy-side demand

Prof. Dr. François-Serge Lhabitant

Hedge funds proliferate, but many private and institutional investors seem increasingly dissatisfied with their returns. In our presentation, we will argue that the majority of sell-side hedge fund portfolios currently suffer from obesity, over-diversification, alpha-beta confusion, hot-money flows, and seriously lack portfolio construction and risk management principles. We will illustrate some of solutions to these problems, which have been successfully implemented by sophisticated large-size buy-side pension funds and endowments, as well as recently evidenced by academic research.

How Can Institutional Investors Benefit from Recent Advances in Hedge Fund Performance Forecasting?

Prof. Dr. Robert Kosowski

Given the recent decline in average risk-adjusted hedge fund performance, the ability to pick hedge funds that will outperform other funds on a risk adjusted basis has become more important than ever. Recent advances in hedge fund selection have improved the ability of investors to forecast risk-adjusted hedge fund returns. These advances include methods to address various data and performance measurement biases, optimal benchmark selection and Bayesian methods based on related assets with longer time series histories. These findings are of particular importance for sophisticated institutional investors (such as pension funds, for example) who face the option of either investing directly in individual hedge funds or in funds of hedge funds. A successful implementation of individual hedge fund selection by institutional investors can make the outsourcing of hedge fund selection to funds of hedge funds, which charge an additional fee, potentially less attractive.

Investing in Synthetic Hedge Funds

Prof. Dr. Harry Kat

Over the last five years pension funds have developed quite an appetite for alternative investments, and especially hedge funds. Realizing that the alphas that once may have existed in hedge funds have evaporated by now, today the main reason for pension funds to invest in this asset class is diversification. When looking for new diversifiers, pension funds do not necessarily have to venture out into new, unexplored territories, however. With a little help from modern option pricing theory, it is possible to construct dynamic futures trading strategies, which generate returns with the same risk-return profile as that of hedge funds, or any other alternative asset class for that matter. Accurately replicating the risk-return profile, but sharing none of the drawbacks of real hedge funds, including the need for extensive due diligence, liquidity, transparency and capacity problems, such strategies provide pension funds with a very attractive alternative for direct hedge fund investment. In my presentation, I will show the audience how these "synthetic hedge fund strategies" are derived as well as present a number of detailed examples, based on several well-known hedge funds (of funds).

The Alpha is dead, long live the Alpha!

Dr. Nils Tuchschnid

With its growing importance over time, the Hedge Funds industry is now facing a number of issues: capacity limitation, increasing scrutiny of regulators, potential limited quantity of truly management skills, as well as overcrowded consensus trades. Of course, one could claim that these struggles are typical of any industry entering into its maturity phase. But does it mean that the so-called “Alternative Investments” are now becoming “Traditional”? Does one have to believe that passive index products will actually start to compete with actively managed portfolios? In other words, does one have to conclude that Alpha is in fact just a hidden Beta exposure?

Well, we doubt it.

Funding Long-Term Liabilities: A Global Perspective

Alan Brown

The provision of adequate pensions to the retired population is an important aspect of social policy in all developed countries.

With bond yields declining to near generational lows, and with liabilities increasingly being discounted at market rates, funding ratios of pension plans have come under extreme pressure. In the space of three years, funding ratios in the United States fell from an average of about 115% to around 80%. In the face of such intense pressure, industry best practice has come under scrutiny. Starting by questioning some basic assumptions about funded pension systems in general, and then challenges today’s standards of best practice, there will be an attempt to address more focussed topics such as

- Fixed Income – Movement away from benchmark oriented strategies
- Equities – In the search for higher and more consistent Alpha
- Alternatives – Evolvement from Single or Fund of Funds strategies towards Multi-strategy solutions.

The common theme amongst these focussed topics is improving risk/return dynamics and finding ways to improve efficiency and cost effectiveness. In a world of low nominal returns, managing risk and improving net returns is vital if we are to deliver on the pension promise that society demands.