OPALESQUE

Opalesque Round Table Series '12

CANADA

Opalesque Roundtable Series Sponsor:

eurex

opalesque.com

Editor's Note

Small, but beautiful: Canadian hedge funds

Over the last five years, the assets of Canadian hedge funds grew from $12 billion to $30 billion. Given the times we are in, that's a nice growth rate. Currently, 48 hedge funds and fund of funds are members of AIMA Canada, the Alternative Investment Management Association. While $30 billion is still small compared to other hedge fund centers, the industry has become quite diversified in terms of strategies, and many top service providers are active in the country.

The hedge fund managers at this Opalesque Canada Roundtable make their point that they also deliver. For example, Donville Kent has outperformed the TSX Composite every year since launch in 2008; cumulative return since inception is a gain of 132% versus a loss of 1% for the TSX Composite.

What do Canadian individual and institutional investors want?

Since the 1990s, the majority of private Canadian investors has not made any money with the typical Canadian long-only asset managers, and there is a clear desire for change. The Roundtable highlights a number of ways hedge funds can now capitalize on the mass disillusionment amongst this investor class.

Institutional investors in Canada are finally beginning to appreciate the need for alternatives as complements to their traditional assets. The smaller institutions are most likely to outsource their needs, while larger institutions would only consider outsourcing to gain access to a very specialized strategy, while always giving preference to developing new strategies in-house.

The Opalesque 2012 Canada Roundtable was sponsored by Kaufman Rossin Fund Services and Eurex and took place in the offices of Deloitte in Toronto, Canada on September 12th with:

1. **Veronika Hirsch,** Chief Investment Officer BluMont Capital
2. **Frank Maeba,** Co-Founder, Breton Hill Capital
3. **Jordan Zinberg,** Managing Director and Portfolio Manager, Donville Kent
4. **Chris Dopp,** Senior Vice President, Eurex
5. **Darcy Morris,** Co-Founder. Ewing Morris Investment Partners
6. **Ari Shiff,** President and Founder, Inflection Management
7. **Prof. Luis A. Seco,** Sigma Analysis and Management; Director, Mathematical Finance Program, University of Toronto

discussing:

- **Where do Canadian hedge funds find opportunities? Which strategies are still working?**
- **Insights into the Canadian equity market: how to evaluate energy companies, and how to invest beyond energy**
- **Small is beautiful: In contrast to other regions, the scalability of Canadian hedge funds is not in question**
- **How to get seeded by CalPERS**
- **Why hedge funds will cope better with the regulatory push for increased capital requirements and collateral than traditional firms**
- **Strong outlook for activist investing: Driven by hedge funds and international investors, shareholder activism in Canada is on the rise**

Enjoy the read!

Matthias Knab
knab@opalesque.com

Cover Photo: Toronto

Participant Profiles

(LEFT TO RIGHT)

Matthias Knab, Ari Shiff, Luis Seco, Frank Maeba, Jordan Zinberg

Darcy Morris, Veronika Hirsch, Chris Dopp


KAUFMAN ROSSIN
FUND SERVICES
GO BEYOND
EXPECT A HIGHER STANDARD
INDEPENDENT
We're objective, with no conflicts of interest, like an independent administrator should be.
QUALIFIED
Born out of one of the nation's top CPA firms, we apply strict process control to every element of our work.
STABLE
Our unusually high staff retention means no starting over - we get more valuable each day.
ETHICAL
We remain accountable to our clients, to their investors and to our standards.
Christine Egan | cegan@krfs.com | 646.522.1621
www.krfs.com | funds@krfs.com
FUND ADMINISTRATION GUIDED BY STRICT ACCOUNTING PRINCIPLES
SERVING NORTH AMERICA SINCE 1994
NEW YORK | BOSTON | SAN FRANCISCO | DALLAS | CAYMAN ISLANDS | MIAMI

Introduction

Chris Dopp
Eurex Exchange

My name is Chris Dopp and I am a Senior Vice President on the Buy-Side Relations team at the Eurex Exchange. The Buy-Side Relations team is responsible for all the exchange's relationships with hedge funds and CTAs throughout the U.S., Canada, Latin America and the offshore financial centers.

Eurex Group is one of the world's leading derivatives exchange operators offering a broad range of international benchmark products, including the most liquid fixed income and equity index markets in the world. With market participants connected from 700 locations worldwide, trading volume on the Eurex Exchange exceeds 1.5 billion contracts a year.

Additionally, Eurex Clearing is one of the world's largest clearing houses and is at the forefront of international development in risk management and central counterparty clearing.

Frank Maeba
Breton Hill Capital

I am Frank Maeba, a Managing Partner and Co-founder at Breton Hill Capital. Breton Hill is a global macro fund, where we focus on trading equities, FX, and commodities. We use a trend following discipline, which allows us to be very opportunistic and tactical across a wide variety of asset classes. I believe we have an edge in security selection and position structuring where we use a combination of cash, futures and options to create better risk/return across our portfolio.

We launched last year so we are coming up on our one year anniversary. We have institutional backing from CalPERS which is the largest pension investor in North America.

Ari Shiff
Inflection Management

I am Ari Shiff, President and Founder of Inflection Management. I've been working in the fund of funds space since 1997. We launched the Inflection Strategic Opportunities Fund in 2010 and began taking in outside capital January 1st 2011. ISOF is a fund of hedge funds created to provide portfolio diversification for our clients via a tax efficient structure. We do that by strategically accessing global opportunities that are typically not accessible to investors via traditional instruments like stocks. A good example is the abundance of deep value assets that are being created by ongoing market dislocations around the world, like the current sovereign debt crisis in Europe.

Our flexible investment style allows us to select what we consider to be the most appropriate mix of strategies to suit diverse market conditions and to seek to capitalize on near-term trading opportunities at the same time.

We search for opportunities in two primary ways, one by developing macroeconomic themes and then searching for the best hedge fund managers to execute the strategy. And secondly, we search globally for hedge fund talent that has demonstrated an expertise in exploiting current opportunities through their own idea generation and structure.

Jordan Zinberg
Donville Kent Asset Management

My name is Jordan Zinberg, and I am a Managing Director and Portfolio Manager at Donville Kent Asset Management in Toronto. Our firm was founded by Jason Donville in 2008. We manage the DKAM Capital Ideas Fund, which is an equity long/short fund that invests in Canadian public companies of any size across all sectors. Our fund focuses on companies that have a track record of earning high returns on shareholders equity, reasonable valuations and positive share price momentum. We are well known in Canada for being superior stock pickers and using a high degree of concentration within our fund.

Since our launch in 2008 our fund has outperformed the TSX Composite every year and our cumulative return since inception is a gain of 132% versus a loss of 1% for the TSX Composite over the same time period. The Capital Ideas Fund has produced an annualized return of 25% since inception for our investors.

Veronika Hirsch
BluMont Capital

I am Veronika Hirsch, a founder and the CIO of BluMont Capital, a subsidiary of Integrated Asset Management. Integrated specializes in developing and managing innovative alternative strategies which complement traditional portfolios by enhancing returns while improving overall risk management.

At BluMont, I have been managing several alternative products since 1997. Currently I have two funds under my management whose main focus is protection of capital while delivering consistent absolute returns. These long/short funds use limited leverage and invest predominantly, but not exclusively, in Canadian equities and convertible instruments. The funds invest in companies of all sizes, but I have had most success picking winners from the mid-caps. Because of the flexible mandate, I can adapt fund strategy to changing economic circumstances and market moods, but I never compromise my stock picking principles, which revolve around management track record. I am looking for management teams with proven ability to deliver better than industry growth rates while maintaining conservative balance sheet. Since inception, each fund has achieved more than double the returns of the main Canadian equity index.

Luis Seco
Sigma Analysis and Management

My name is Luis Seco, I am a professor at the University of Toronto where I am the Director of the Mathematical Finance Program. I am also the President and CEO of Sigma Analysis and Management. Sigma operates managed account platforms of alternative investments, advises on hedge funds and provides portfolio analysis services to institutional investors.

Darcy Morris
Ewing Morris & Co

My name is Darcy Morris. Along with my partner John Ewing, I co-founded a firm called Ewing Morris & Co. in September, 2011. The guiding principle behind our firm is to build the investment company that we would want to be a client of. That means that our firm:

- focuses on investment results, rather than gathering assets;
- communicates with clients in a candid way whether it is good news or bad news;
- employs an understandable investment philosophy based on sound principles;
- has managers that are invested meaningfully on the same terms as their clients;
- and we measure ourselves using absolute returns rather than relative returns.

Our investment approach can be described as applying a private equity mindset to public companies. That means we analyze businesses from the perspective of buying the entire company and have a limited number of carefully chosen, well- researched holdings in our portfolio that we plan to keep for several years.

We also believe we have three structural advantages that help us to provide superior investment results over time.

The first one is our size. Size is the enemy of returns and managing a relatively small pool of capital allows us to take advantage of opportunities that larger firms cannot. Secondly, we have a flexible mandate and invest across market cap, geographies, as well as up and down the capital structure. And the last advantage is focus. We believe great investment ideas are rare and have no interest in watering the wine with our one hundredth best idea.

In our knowledge no one ever sits across the table and describes their investment approach as overpaying for low-quality, shrinking businesses run by a crooked management. In this sense we tend to find terms like “value”, “growth” and “momentum” as too generic and not very enlightening when it comes to investment strategies. Instead, we describe our strategy using the analogy of a sports play book. A championship team will have perfected in practice a number of different plays. Whatever the game situation, no matter what the weather conditions are, no matter what the defense does, no matter whether they are playing home or away, they have different strategies to score.

We have four main “plays” in our investment playbook. The first “play” is what we call the “Great Business”. These are companies with great economics, durable moats and compelling growth opportunities. Our second play is what we call “Cheap Assets” - businesses where the market price of their stock is trading at less than the underlying asset value of the business. The third play is investing in “Great Capital Allocators”. These are businesses where there is a great investor at the helm, for example Berkshire Hathaway. Finally, our last play is shorting broken business models. Here, we are not looking for the next Sino-Forest or Enron, although that would be nice if we found it, but rather investing in businesses with a structural crack in the foundation - things like Blockbuster when a player like Netflix comes along or HMV as iTunes comes along, these sorts of things.

Matthias Knab **From your perspective as Canadian hedge fund managers and investors, where do you find opportunities these days?**

Frank Maeba: One of our larger trades is being long U.S. equities right now. The central banks have brought forth all their QE policies, they have banded together to put a floor on tail risk and we definitely see upward momentum across a lot of different sectors. We do have a good exposure to U.S. equities, including a number of higher beta sectors like financials and materials, and you could say we have a bit of a value bias regarding the stocks we buy.

There are a couple of macro fundamentals underpinning our long view of equities, but also on a technical and sentiment basis you have the upcoming U.S. election, in addition based on institutional data, it looks like managers are pretty under allocated for risk, so there is a realistic chance that we could see a rally chased into year end.

Frank Maeba We have also done well being long grains. You have heard about the drought conditions in the Midwest and how it has been negatively affecting corn, soybean and wheat crop yields; we have been long grains for the better part of three months. Prices have consolidated at the top end of the range, but we think there are potential catalysts for another leg up into year end.

Ari Shiff Our firm attempts to deliver portfolio diversification in a structure that is tax efficient for Canadian investors. We direct our services to Canadian high net-worth and institutional investors, and we assume that our clients already have exposure to Canadian and US equities, a certain amount of real estate, and possibly some direct or indirect commodities - all holdings typically found in Canadian investor portfolios.

Ari Shiff: We strive to provide exposure to alternative assets, strategies, and opportunities that are not easy for individual investors to access. So far in 2012 we have had an extremely good year, and are net over 11.5% to the end of August.

We typically have a few core themes within our portfolio at any given time, and often hedge those themes. A good example would be our mortgage backed asset managers. Canada has a very strong and healthy mortgage infrastructure. By contrast, the US has gone through some rather well publicized problems. Several of our managers have done very well accessing deep value and yield while trading distressed US mortgaged securities. We are also finding excellent value in distressed corporate bonds, particularly emerging market distressed, and in activist long/short investing.

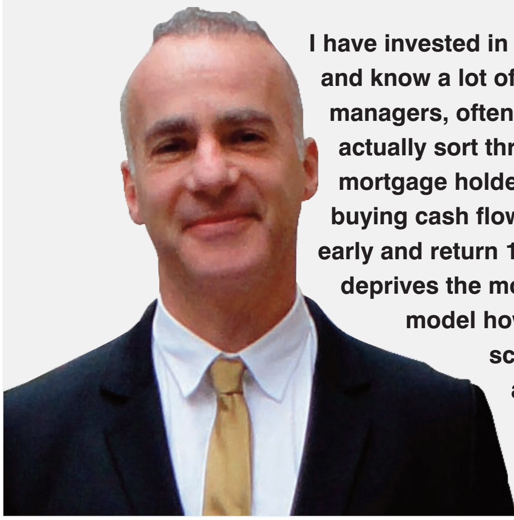
Matthias Knab **Can you tell us more about the Canadian mortgage market and how it differs from the U.S.?**

Ari Shiff Well, the weaknesses of the US mortgage market are in stark contrast to the strengths of the Canadian mortgage market. The biggest difference with Canada is the size and scale of the dislocation in the US. We're talking about a dislocated asset class in the trillions of dollars. The genesis of the issue of course is that so many banks and insurers were taken over by the US government since 2008.

Ari Shiff: In taking over the banks and insurers, the US government ended up taking on the mortgages that the banks were holding, on the order of millions of mortgages worth trillions of dollars. Prices were further beaten down when many mortgage backed securities lost their ratings and therefore their pension investors.

The government proceeded to sell their holdings as best as it could, depending on what the market could absorb. The flood of product collided with a dearth of investors due to the collapse of liquidity and changes in government regulations on who could trade these instruments. The result was, and continues to be, that many of these types of assets are selling at ridiculously low prices,

Inflection Management's approach to this opportunity has been to find veteran managers who know how to accurately value the assets and trade them. Typically, they are ex-Countrywide, ex-Goldman, or ex-Lehman Brothers employees, and therefore have a long history of familiarity with the assets, how they originated, and how they are traded.



I have invested in managers in the MBS space since 1998, so, we know the space quite well, and know a lot of the managers who trade in this space particularly well. We turn to managers, often veterans in the strategy, who have constructed databases and models to actually sort through the tranches and analyze them right down to the level of each mortgage holder and analyze the risks and opportunities. Because you are essentially buying cash flows, one of the potential upsides is that individuals will prepay their mortgage early and return 100 cents on the dollar. A potential downside is a mortgage default that deprives the mortgage holder of a cash flow stream. Using technology, our managers can model how many people are going to pay early, late, or not at all, over many possible scenarios such as interest rate changes, and then trade with a knowledge advantage. Back in 2008, the prediction was that this would be a two- or three-year opportunity. It's now 2012, and the opportunity isn't going away any time soon.

Jordan Zinberg: The predominant theme in our portfolio right now is defensive growth stocks, which we define as companies that can grow in excess of 20% per year regardless of the economic environment. Of course, everybody wants to own companies like this, so the second piece of the analysis is finding those stocks with high sustainable growth rates that currently trade on a reasonable valuation.

We often find high growth companies in Canada that are ignored by the overall investor community due to lack of analyst coverage, complex accounting, or simply because they are in an "unsexy" industry. We are agnostic to market cap, however we have found the sweet spot in Canada to be in the mid-cap space. Mid-caps typically have enough of a track record to give us comfort in management's ability to generate returns, offer adequate liquidity, and can be priced inefficiently at various points in the cycle which we look to capitalize on.

Jordan Zinberg

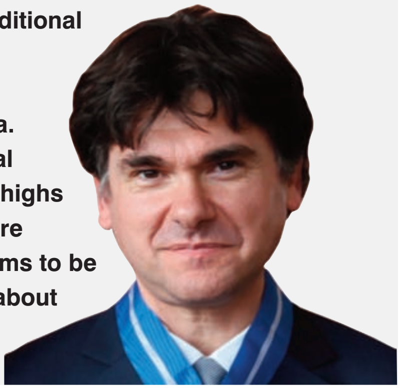
We aim to find what we think are the best eight or 10 companies in Canada and then make relatively large bets on those companies. The primary tenets of our strategy involve stock-picking and concentration as opposed to leverage or complex portfolio engineering.

Veronika Hirsch: The two strategies I manage are thematically very similar. My portfolios are seldom concentrated, however I usually construct a diversified portfolio around one or two themes. For example, one of the themes we like right now is growth by M&A. Current global condition of persistently weak and unpredictable economic growth has led to low interest rates and depressed valuations. Companies endowed with a clean balance sheet, clever strategy and the ability to pick accretive acquisitions and then execute flawless integrations will be able to achieve faster growth than would be possible during normal economic times while improving their leadership position in the industry during the process. This is where our search for superior management teams comes in handy. Good management teams will have all of the above attributes, ready to conquer the world. In fact the more difficult the environment, the more differentiated the management teams will become, and the more opportunities for growth will become available.

We play the M&A theme from both sides, so we like the consolidators as well as the prey. Obviously the acquiring companies are easier to identify than the targets, but both can be immensely rewarding.

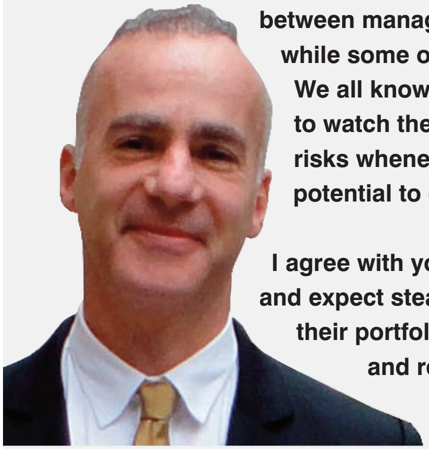
M&A is our favorite theme, but dividend growth also works well during uncertain times. When investors shorten their time horizon, few things are more appealing than regular dividend payments. Again, good management teams will figure out that companies which reward their shareholders with growing dividends will be eventually rewarded with superior valuations, which in turn will reduce their cost of capital and allow them to successfully compete in the M&A world. So to some extent, both of our themes work well together.

Luis Seco: We see a big paradigm shift since 2008. Managers that have exposure to traditional risk premia have difficulty providing value in the current environment.



What we see at the same time is the emergence of non-traditional sectors of risk premia. Managers who are, for example, volatility driven, but which do not fall into the traditional compartmentalization of hedge fund styles. Most strategies continue to be below their highs of five years ago, which to me means that the search for return has become a much more difficult exercise than it has been in the past. And there is not a single strategy that seems to be fulfilling that objective across the board. I think it is more about the manager, and less about the strategy.

Ari Shiff: I am not sure I totally agree with you. Yes, a number of strategies that have worked in the past do not necessarily work now, but I do think there are strategies that have a seasonality to them, and that there are certainly some strategies whose season is actually now. Moreover, depending on the macro environment, which of course we have to continue to monitor, some strategies have the potential to produce healthy returns over the next several years.



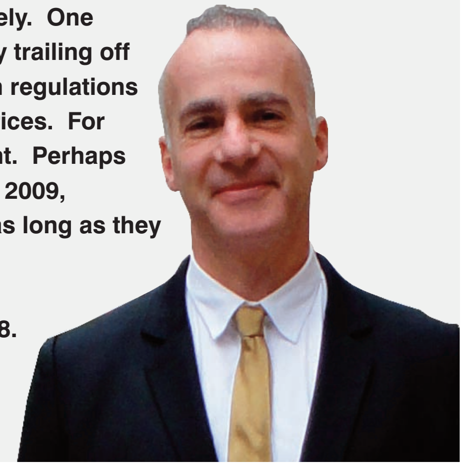
At Inflection Management, we run a fund of funds, so one of the things we do is allocate money between managers. Some strategies have certainly produced very good returns since 2008, and while some opportunities may be tailing off, there are other opportunities with no end in sight. We all know when such a time comes, things can end relatively abruptly, and therefore you have to watch the macro-economic backdrop carefully, prepare for your exits and hedge away tail risks whenever possible. But at the moment, for a number of strategies, we think there is the potential to continue running for at least another year until we may see the first warning signs.

I agree with you very strongly that as an investor you cannot sit comfortably in any single strategy and expect steady returns year after year. You are quite right about that! Investors need to manage their portfolio of hedge funds just as they manage their portfolio of stocks, dynamically adding and removing exposures as market conditions dictate. There are some very enticing strategies available right now.

Luis Seco Can you give us some examples of those?

Ari Shiff: We generally favor volatility and the world has not been short on that lately. One strategy that produced strong returns post 2008 but that now appears to be slowly trailing off is corporate distressed bonds. The collapse in liquidity in 2008 and the change in regulations unleashed a torrent of very good quality corporate distressed bonds at bargain prices. For managers who knew what they were looking at, the opportunities were self-evident. Perhaps it was a bond they were willing to pay a $100 for before 2008 and that was now, in 2009, selling for $60. They could certainly spot that there was an opportunity to trade, as long as they knew what their exit strategy was going to be.

Of course we are seeing far less of that particular opportunity in the US since 2008. However, it appears they are about to manufacture a whole lot of new distressed corporate debt in Europe, and there will likely be a similar opportunity there.



Ari Shiff For some of the themes we develop, spotting a two year opportunity is a good starting point, having a three year opportunity gets us excited, and if the opportunity extends beyond four years we think we are doing very well.

Darcy Morris We launched our fund on September 9th, 2011 - we just had our one year anniversary, and in our first year of business we returned 14.5% net. Of course, we know that if you run a good split time in the first mile of a marathon you don't stop to celebrate. We're pleased however that we had a fine start.

Darcy Morris: We think there are lots of opportunities in the Canadian equity markets and there is a structural reason for that. One of the peculiarities of the Canadian market is that most of the domestic investment talent in this country gravitates towards the natural resources and mining sectors. Even the international talent that comes to Canada to hunt for investment opportunities tends to concentrate on these sectors. This makes sense since Canada has a relative abundance of land and is known internationally as a natural resource provider. As a consequence, however, we find the market we are focusing on – small and mid-cap "real businesses" - very inefficiently priced. It is this area of the Canadian market – business like software technology, distribution, etc. – that offers us compelling investment opportunities with less competition.

Chris Dopp Working at an exchange, I can comment with a more holistic view. We see an aggregation of flows across asset classes and much of what is being said today confirms our observations. The overall theme appears to be looking for strategies and approaches that differentiate a fund from others and capitalize on more granular exposures.

We have experienced growth in new products that provide access to more specific exposures. For example, with the breakdown in correlations between European sovereign debt yields, hedge funds and CTAs see opportunity in trading the various levels of credit throughout Europe. In addition to Eurex Exchange's traditional German government bond complex, we have introduced futures on Italian and French government bonds. The products have been well-received by the marketplace and liquidity has grown exponentially from both the traditional and alternative investment communities.

Matthias Knab **Let's look at some of the differences and strengths of the Canadian financial markets and hedge fund industry compared with other regions. Opalesque recently wrote about some of the developments AIMA Canada informed us about. For example, the assets of Canadian hedge funds grew from $12 billion to $30 billion during the last five years. That is quite a good growth given the times we are in. Currently, 48 hedge funds and fund of funds are members of AIMA, the Alternative Investment Management Association. This is also a good number - you have a well diversified industry here. What else can you add about the Canadian market?**

Chris Dopp I cannot speak specifically about any individual hedge fund, but as a person who is covering the hedge fund industry in total for all of the Americas, I can speak about trends that I see here as opposed to the U.S.

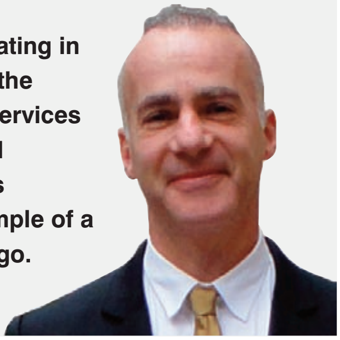
One is the previously mentioned advantage of Canadian hedge fund managers having relatively smaller assets under management and the nimbleness that provides. There has been extensive research produced that shows that the performance of smaller funds actually outpaces bigger funds on a consistent basis. As an aside, it is interesting that the bulge bracket funds continue to raise the majority of assets.

Chris Dopp: The institutionalization of the investor base in the U.S has created a situation where large managers have grown rapidly. In doing so, they are losing the scalability of their strategies and are expanding outside of their core competency. This can be challenging. Meanwhile, funds here in Canada are not even close to the point where their scalability is in question. There is tremendous room for asset growth and this will continue to be a strength for Canadian funds going forward. As an example, the Canadian managed futures industry is only in its infancy and there are some extremely talented managers here.

Frank Maeba When we started our fund, we never really thought of Toronto as a geographical constraint in respect to launching a hedge fund. In this industry, there are thousands of hedge funds across the globe, and if you are an investor and you are demanding talent, you have a way of finding it, no matter where it is in the world.

Frank Maeba: The talent pool here in Canada has been growing and improving, there is definitely more talent that is getting recognized on a broader scale. People who have worked internationally are coming back to Toronto to launch their own hedge funds. In the past the landscape may have been dominated mostly by long/short resource focused equity funds and fixed income, but now you are also seeing other strategies like macro, market neutral or credit that are also gaining traction. So as you said, the industry is in growth mode here.

Ari Shiff: As a seeker of talent we have been very pleased to see more and more funds operating in Canada that have caught our interest. The standards here have been improving not only on the manager side but also in the service providers and related industries that offer world-class services and platforms to support this industry growth. For example, we chose Kaufman Rossin Fund Services as our fund administrator, a company that offers top notch services for hedge funds particularly those managing less than $500 million. Also Deloitte, our auditor, is a great example of a firm providing a level of talent to the industry that simply did not exist in Canada five years ago.

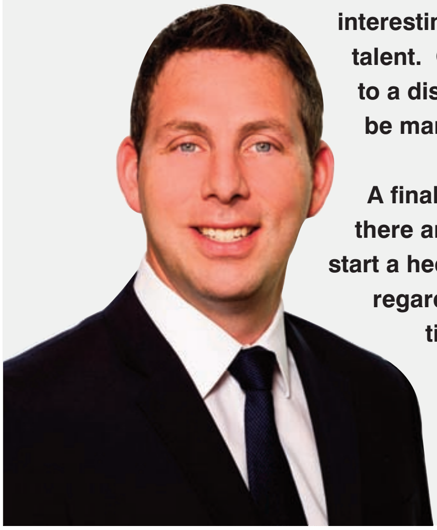


Ari Shiff If Canada continues to follow the example of the US and Europe, we will see greater adoption of the fund of funds model as the investor base matures. History has shown that the first wave of early adopters tends to dabble in single strategy funds and then, as they come to appreciate the dynamics and returns of hedged investing, they become aware that they need managerial expertise to maintain repeatable performance and dynamically manage exposures. That evolution mirrors earlier generations' experience in the stock market, when the dabbling and speculating that characterized the early part of the 20th century evolved and professionalized as investors turned to the broker and investment community to provide sustainable performance.

Jordan Zinberg: Matthias mentioned before the size of the hedge fund industry in Canada is now estimated at $30 billion. While the trend has been positive and that asset base has been growing consistently, I believe Canada is still a very small player in a global context. You can easily find a number of hedge fund firms in the U.S. that are larger than our entire domestic hedge fund industry, and I think it is interesting to reflect for a moment about why that is.

One reason is that Canada was a little bit late to the party---the hedge fund industry did not really emerge here until the mid 1990s. As with any industry, it takes time for participants as well as service providers to mature and catch up with global peers. You must also keep in mind that at 35 million people, Canada's population is relatively small, and the investor base can only support an appropriate number of funds.

In addition, Canadian investors and financial institutions tend to be relatively conservative by nature. We get an interesting perspective on this when we present to investors in the US, as we also manage a US domiciled fund for American investors. US investors seem much more open to hedge fund strategies, and usually have a higher allocation to hedge funds within their portfolio then their Canadian counterparts. That said, an interesting dichotomy exists when we bring the discussion around to the subject of manager talent. Given that there are only around 200 hedge funds in Canada, our country is home to a disproportionate number of extremely talented managers that I believe would easily be managing ten times the assets if they were based in New York or London.



A final reason that comes to mind regarding the growth of the industry in Canada is that there are relatively high barriers to entry. Unlike several other countries, it is not easy to start a hedge fund in Canada. Canadian funds must register with provincial regulators regardless of size, there are strict capital requirements that must be maintained at all times, and portfolio managers must be licensed. In order to obtain a license, individuals must apprentice under another portfolio manager for several years and must also complete a number of educational requirements. There are some great managers in this country that deserve global attention, and while things are progressing nicely, there is still quite a bit of work to do.

Veronika Hirsch: On the one hand, it is an advantage for hedge funds in Canada to be generally small, as the experience has been that small funds usually outperform large funds. On the other hand, small funds have limited appeal for institutional investors who need proof of scalability and for investors in general who associate size with safety. Canadian investors are very conservative and they seem to prefer funds distributed by large, well recognized, brand name institutions such as banks or established mutual fund companies. This is certainly an impediment to the growth of independent hedge fund companies, even though they often attract more talented managers. All else being equal, my belief is that a talented manager would prefer to work for a smaller, independent, less rigid hedge fund company than for a bank. But he/she often gets frustrated with the difficulty and slow progress of growing assets and might eventually abandon the effort for a less suitable but more financially rewarding position.

This problem is not unique to Canada. A participant on a recent Opalesque Roundtable mentioned that investment track record is often a secondary consideration for potential investors when choosing a hedge fund, because they value safety more. So even though there are good growth opportunities in Canada because the hedge fund world here is still relatively small and undeveloped, it might never prosper to the same level as the hedge fund industry in the US or UK.

Darcy Morris: A progressive aspect of our industry is that hedge funds can be structured to run much leaner than a traditional asset management firm. This means that managing a smaller pool of capital is less of a barrier to entry.

Canada is a tiny country. With around 35 million people in Canada the population of California is bigger than our country as a whole. Our stock market accounts for only about 3% of the global markets. So often times we are lagging countries like the US in the latest investment trends and developments. For instance, most people in Canada continue to invest in equities using the traditional long-only model. Long-only asset managers are where the bulk of the private wealth is invested currently in Canada. As we know the long-only model worked well through the bull run of the 1990s.

Since the 1990s however, a lot of private investors have not made any money with the typical Canadian long-only asset manager, and there is a clear desire for change. For firms like Ewing Morris & Co. there is an opportunity to capitalize on the mass disillusionment amongst the Canadian investor class. Furthermore, traditional long-only investment managers are compensated as a fixed percentage of assets and incentivized to go about gathering as many assets as possible. In our model, our compensation is skewed towards our investment results.

Darcy Morris It is not in our best interest to grow to a size that will impact our ability to provide superior investment results. People are starting to recognize that it makes more sense to have an investment manager compensated for performance rather than through a fixed percentage of assets.

Chris Dopp About a week ago, I read a survey stating that two-thirds of hedge fund assets under management are from institutions and that 80% of the institutions in 2011 either grew or maintained their hedge fund allocations. So, it is obvious that institutions, such as pension funds, endowments and family offices, are the driving force in hedge fund asset growth.

Chris Dopp: Do you find the fact that the largest institutions and pension funds in Canada are actually managing their alternative investments internally as opposed to allocating to outside fund managers to be a hindrance in raising assets in Canada? Do you see that changing? For example, have you heard of anyone starting an emerging manager program, like many US institutions have done?

Jordan Zinberg: There are some areas within the alternative management space, such as real estate, private equity and infrastructure, where institutional investors have historically preferred to build internal teams. With respect to hedge funds specifically though, this is not the case. We have had recent meetings with decision makers at several large Canadian institutions and virtually all of them are looking to increase their allocation to hedge funds by utilizing talented external managers as opposed to trying to replicate strategies internally.

I think that if you are a Canadian manager running a highly directional strategy that involves Canadian large cap stocks, then institutional players would likely not be interested because they can easily do that in house or use ETFs to capture similar return streams. However, if you can demonstrate the ability to generate risk-adjusted alpha on a consistent basis, then I believe Canadian institutional investors are going to be very interested.

Veronika Hirsch: Larger institutions in Canada all manage alternative strategies in-house. They have developed the capability because they have been managing various alternative strategies for years. Canadian hedge funds can receive institutional mandates, but they are most likely to be awarded by small institutions, because they usually lack in-house expertise. These mandates would most probably be relatively small, thus it is very unlikely that Canadian hedge funds will ever achieve the multi billion dollar size of many US based funds.

Institutions in Canada are finally beginning to appreciate the need for alternatives as complements to their traditional assets. The smaller institutions are most likely to outsource their needs, while larger institutions would only consider outsourcing to gain access to a very specialized strategy, while always giving preference to developing new strategies in-house. A large pension fund, dissatisfied with the results of its in-house managed strategy, would replace its investment team, rather than consider outsourcing the mandate to an outside manager with excellent proven track record. The institution might try to poach the investment team responsible for the good track record, rather than outsource the mandate to them.

Frank Maeba: I can only speak from our direct experience and what we had to do to receive an initial investment from CalPERS. You definitely have to clear a high benchmark for what you have to provide on the investment strategy, operational side, infrastructure and governance. CalPERs is a sophisticated institution that already does everything – either through an in-house team, or external manager allocation. You obviously need to deliver a unique investment strategy that can generate returns and that is accretive to their overall portfolio.

On the operational side you need to provide the highest quality risk management and transparency. Governance was very important, especially after 2008. In our case, we selected a highly experienced and independent Board of Directors, which included an investor from a Middle East sovereign wealth fund, a regulator from the Cayman Monetary Authority and another was a well established Cayman investment lawyer.

Frank Maeba From the beginning, we had an open dialogue with our client and tried to align our interests as much as possible when it came to negotiations. There were a lot of boxes to check to get the allocation and the truth is, you need to check every last single one.

Ari Shiff When it comes to the alignment of interests, being small can in some ways benefit managers. I suspect most of us are in the same situation, in that we have some of our own money invested in our own strategies, and clients like to see that. Clients really like this type of alignment of interest in a meaningfully substantial way, and with a smaller fund that is easier to accomplish than if your AUMs are very large. But having said that, even when we speak to very large funds, a $10 or $20 billion fund, they still make a point of highlighting that their own investment makes them one of the biggest investors in their fund. The importance of aligning interests never really goes away.

Matthias Knab **Veronika, you direct and market your funds to retail. Can you explain to us more about this model and distribution channel?**

Veronika Hirsch: We distribute our funds primarily through the brokerage channel targeting sophisticated investment advisors. A successful advisor will have influence over a large pool of assets, and once he/she gets to appreciate the attributes of a particular fund, he/she can make sizeable allocations to the fund across the client base. Communication with the advisor is paramount to make sure the fund's attributes fit the advisor's needs. The advisor

must of course have confidence in the product's ability to deliver on its strategy, and equally important, must feel comfortable with the fund company, its operations, infrastructure, risk management and governance.

Even though our firm has access to most distribution channels, we also need approval for each and every fund, before we are allowed to talk to the advisors about the product. Most of the firms we distribute our funds through are not that different from the large institutions, in that they would prefer advisors to sell internally managed funds rather than third party products. I am not even sure that better profitability is the main driver for this preference. Equally important are control over the product and safety of the assets.

Matthias Knab **What is the appetite for retail alternative investment products here in Canada? Is there a good understanding of the product?**

Veronika Hirsch: I think Canadian retail investors have decent understanding of alternative investment products, however their appetite isn't always predictable. During difficult markets, when it would be appropriate to include non-correlated hedge strategies into their portfolios, retail investors are too timid and they mostly stick with very conservative income products. What is odd is that allocations to hedge strategies increase during rising markets, when retail investors feel brave. So even though they understand the products, retail investors don't seem to trust them enough to use them for their intended purpose in tough environments.

Veronika Hirsch I do not know who drives these decisions, the advisor or the retail investor. It is hard to tell for us, because we mostly talk to the advisors. Perhaps it is the advisors who are afraid to make allocations to hedge products during difficult markets, as they fear losing clients if the funds don't perform as expected.

Matthias Knab **Sometimes assets from retail investors have the reputation of being "hot money", i.e. retail investors are not considered to be sticky investors. However I often hear from fund managers who do have retail investors that retail is actually the stickier money compared to some other investor groups. What is your experience?**

Veronika Hirsch I think retail money is reasonably sticky, especially because of the sheer number of individuals involved in the fund. Thousands of investors are unlikely to come to the same conclusion at the same time about their experience with the fund, especially since their purchase dates and price vary widely. They are unlikely to wake up the same morning and decide they have lost faith in the manager.

Matthias Knab **But sometimes a crisis can frighten many people at the same time, no?**

Veronika Hirsch: Yes, absolutely. This is when the advisor should step in to make sure that the retail investors are making rational decisions and buying, selling or keeping the right mix of products. But you are right, people tend to be affected by events and respond in a similar fashion at the same time. If there is negative press about a rogue hedge fund manager, some investors panic out of all hedge funds, even though they had good experience with the funds in their portfolio. Hedge funds are also exposed to an advisor's judgment. If an advisor has made poor investment choices and as a result is losing clients, a hedge fund will suffer redemptions even though it was the only product that performed well in clients' portfolios.

Jordan Zinberg: It has always been fascinating to me that the majority of retail investors tend to perceive hedge funds as risky, when in fact if you choose the right manager, you should end up achieving superior returns with less risk. Equally fascinating is that despite Canada's highly regulated financial markets, my mother can open an account with any brokerage firm in the country and buy a highly speculative penny mining stock in her account the next day, but if she wants to buy a top quality hedge fund in her brokerage account, there can be a large number of restrictions imposed.

Luis Seco: I just wanted to add one more thing to the discussion on Canadian hedge funds and I will speak as an academic now because there is one issue that was not brought up: the issue of Canada as a brand. Canada as a brand has been improving over the last years and it has had very positive effect on many sectors of the Canadian economy, the banks for example, or universities. I know that the Canadian brand is actually helping some Canadian hedge funds.

Luis Seco Of course hedge funds are not as well organized in their brand management as a bank is, or even a university. So for many hedge funds this is not an issue. But the reality is that many of the investment decisions that investors make are complex and not based on black and white facts, they are sometimes driven by considerations such as brand and Canada has emerged as a leader in this regard.

Matthias Knab **Following up on this, do you market mostly to Canadian investors or do you already get a significant amount of assets from international investors?**

Darcy Morris Our investor base consists mainly of wealthy Canadian individuals. These people are mostly entrepreneurs, business operators and very successful investors in their own right. Our investment approach of analyzing businesses resonates with them and they can relate when we talk about businesses from an operational perspective. Our view is that we will manage as much money as we deserve to manage for the type of client we deserve to have. I think that if you can communicate a clear investment strategy, have decent pedigree, proven trust and competence, then it's rational for people to outsource part of their assets to you.

Ari Shiff We set up Inflection Management specifically to address institutions, endowments, and Canadian taxable high net worth investors by creating a structure that is potentially tax advantageous. At the moment we have no investors outside of Canada, though our returns put us in the top decile of fund of funds globally.

Jordan Zinberg Both our Canadian and US domiciled funds consist of a mixture of high net worth individuals, family offices and fund of funds. Interesting to note is that some of our American investors view their investment in our fund not only as a way to get exposure to Canadian equities, but also a currency diversifier, as they are concerned about the short to medium term outlook for the US dollar. Our investor base has not gone beyond North America as of yet, however we would consider launching an offshore fund at some point in the future.

Matthias Knab **Luis, you also act as an allocator on behalf of your clients. Can you add some comments about what trends, preferences or issues you are seeing from your perspective regarding the Canadian end investors?**

Luis Seco Investors are becoming more sophisticated, more demanding and they are going after a return within a certain risk profile, they are much more knowledgeable about their risk appetite. For example, there is decreased appetite for operational risk, which typically comes without a premium and therefore is a loosing proposition. We are a managed account platform as a reaction to this shift.

Luis Seco: There is decreased appetite for credit risk, counter party risk and business risk, which again comes with a very small premium, and is not worth it; this is underpinning the recent trend we have seen among many hedge funds to seek multi-prime broker structures and the use of managed accounts.

And finally, all this is related to something else that I see as a trend, which is investors' appetite for timely information, which is growing. I very often say that the financial sector continues to be one of the few sectors where ignorance is still an excuse. In many circles, this is much less so, and in general, investors are much more demanding on information, they want to be in control. Not knowing what is happening is no longer an excuse.

Jordan Zinberg Luis, many investors with managed accounts are able to watch the price movements within in their portfolio on a real time basis. Do you believe this helps or hinders them in their decision making?

Luis Seco Information is a tool, which if used wrongly can be also used to do damage to yourself, like any tool. Investors are becoming more demanding and they will know how information can be used to their advantage and not against their interests.

Matthias Knab **Tell us more about your outlook? Are you excited or concerned? Are you working on new products?**

Chris Dopp One element of a derivatives exchange's normal business practice is to constantly develop new and innovative products, which we will certainly continue to do. However, as was mentioned earlier, the current environment is such that returns can be almost secondary, since investors are also looking for safety. Therefore, either due to regulation in the U.S. and Europe or investor demand, there is a growing need in the market for increased transparency and a desire for increased risk management. For some time, the Eurex Group has been developing technology to achieve these goals in a comprehensive manner.

Chris Dopp: We have been a market leader in providing participants with tools to accurately manage risk in real-time. Additionally, we have developed a model for full physical segregation of positions and margin collateral that provides the highest level of client asset protection. We are also in the process of instituting a revolutionary portfolio-based risk methodology for calculating margin and collateral requirements that will provide maximum capital efficiency. Besides, we will launch EurexOTC Clear which will provide central counterparty clearing service for OTC derivatives with the initial focus on interest rate swaps. These regulatory initiatives and investor demands have already started here in

Canada as well.

One thing that is certain from these developments is the growing need for collateral in a time when the pool of eligible collateral is shrinking. Therefore, we are working toward being able to measure risk as accurately as possible, so that funds can use collateral in the most efficient manner.

Matthias Knab **Do you think this regulatory push for more collateral will affect the viability of investment or trading strategies?**

Chris Dopp: **I believe that it is less of an issue in the hedge fund world, because the hedge fund world has a long history of pledging sufficient collateral and the capital requirements are already built into their strategies. It will be more of an issue for traditional money managers, where the largest investors have often not needed to post collateral. That said, the increased capital requirements will have an impact on return expectations, but they will not eliminate the viability of the strategy.**

Darcy Morris I think our industry does a rather poor job of setting investment return expectations up front. A vital part of the investment business is to align not only interests but also return expectations. For instance, there is going to be a large disconnect if you as a manager are making investments focused on a three year time horizon but your investors are measuring you based on daily short-term market fluctuations. Most likely when you see great opportunity, you will have clients running for the exits.

Our goal in managing money is to double money over a reasonable time frame, which we define as five to seven years. That translates back into 10-15% per year. As we see it, in any five year period we will probably have three average years, one down year and one outstanding year - so we won't do 15% every year in a straight line. Of course, the so-called bad years will likely offer opportunities to put more money to work than we have before and it is critical to have an investor base that will agree and stand by you.

When investors evaluate managers, they should also make sure to put the market period into context. The last 10 years were much harder to make money than the decade before that. So the current environment of volatility, say starting in 2007, lets you much better evaluate the skill of a manager rather than periods where we experienced prolonged bull or bear markets.

Frank Maeba: **I like the prospects for our fund going forward. I was just reading a Barclays piece saying that macro was one of the most heavily invested strategies since 2009, and they estimated that out of the $80 billion of new money coming into hedge funds this year about 75% will be allocated to global macro.**

I believe that our fund can do well for our investors for a couple of reasons, including some Luis alluded to. What first comes to mind is the way we invest. We do not have a structural long bias across anything we trade; for example right now we are tactically long equities, but in the Fall we were actually short. Being nimble and having the ability to shift capital to opportunistic trades over a medium term time period will continue to be very important going forward, especially in this macro driven and challenging environment.

With a trend following discipline, we tend to have a long volatility profile. Generally, our strategy can do very well in the tails, and in the past it has done well even in prolonged down markets.

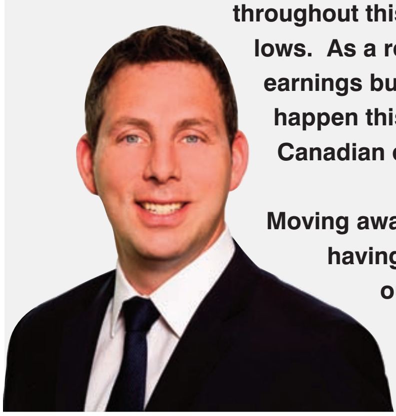
Currently, markets are exposed to large macro risks such as the European debt crisis, the looming fiscal cliff, as well as the uncertainty around the end result of QE. Couple that with a low growth outlook, and we may be stuck in a deflationary environment like Japan experienced in the 90s. What is interesting during this period is that the Nikkei actually had massive bull runs, rallying 50-60% over a two year span before collapsing over the next multi-year cycle - how do you make money in that kind of challenging environment? We believe you have to be tactical and opportunistic and use a broad and diverse tool kit in order to capture returns in this kind of environment.

Ari Shiff: Similar to Frank we make money off volatility. We see ourselves in year four of a long-term credit deleveraging cycle. We do not see any shortage of dislocations popping up. Europe is obviously going to be a big source for distressed assets, and it will be interesting to see how things play out there given that European banks and governments tend to hide their problems and bury them internally in the hope that they will disappear rather than monetize them and let the marketplace determine a fair value. That kind of politicking will lead to continuing bouts of volatility and we are positioning ISOF to potentially profit from the opportunity.

Jordan Zinberg

We continue to be bullish on our strategy as well as the overall Canadian equity market. Consistent with the rest of the world, there is a great deal of uncertainty present in virtually all types of asset classes in Canada. The current situations in Europe, China and the US weigh on our domestic equity market in a variety of ways, however valuations suggest that equities remain extremely attractive.

Jordan Zinberg: Equity valuations peaked in Canada at the height of the tech bubble in 2000 and markets have been flat over the past 5 years. However, what many investors fail to realize is that earnings have been growing steadily throughout this entire period. Despite strong earnings growth, valuations remain at generational lows. As a result, the next rally in Canadian stocks will likely not come from dramatically rising earnings but from expansion of the market multiple. We don't know if that multiple expansion will happen this year, next year, or the year after, but we believe we are in for a pretty sharp rally in Canadian equities.



Moving away from Canadian equities in general and to our strategy more specifically, we are having no trouble finding attractive investments within the Canadian equity market that meet our strict investment criteria. Our portfolio companies continue to generate returns on shareholders equity in excess of 25% and the majority of these stocks trade on single digit P/E ratios.

Veronika Hirsch: I agree with what was said, and while for all of us around this table the environment will remain difficult over the next say five years, we should benefit from this environment, as we have the ability to outperform traditional funds because of the larger variety of investment tools we have at our disposal. Clearly our ability to short stocks becomes immensely valuable during market corrections.

So five years from now, hedge funds should be able to gain more mandates, and be allocated more money than traditional funds, because hedge funds would have delivered better results. In fact the longer the malaise lasts, the more differentiated the performance track records should become. Theoretically speaking. In five to 10 years we can maybe have another round table and see how well our predictions turned out.

Luis Seco: Equity indices are at their 2006 levels, bond yields are historically low. There is a chance market beta will not continue to be a likely source of return. But I think opportunities exist everyday, I am more with Frank on this one. Being tactical, knowing what you are doing, having the right timeframes in mind is more critical than in the recent history. We will have to go to the seventies to find markets that have moved sideways for an extended period of time.

Matthias Knab — **Any final comments about Canada, Canadian hedge fund industry and Canadian opportunities?**

Darcy Morris — If you come to Canada to hunt for investment opportunity the odds are pretty high that you will be looking into the energy space. I think our firm looks at investing in energy a little differently than most others and thought I'd share our view.

Darcy Morris: When evaluating an energy company, most investors tend to focus on the economics of existing assets, sometimes assigning extra value for undeveloped land. However, many oil and gas wells deplete at 20-30% annually which means existing assets will disappear within five years. Management is therefore tasked with reallocating the capital earned from drilled wells every year. And they invest a lot of capital! For example, EnCana, which is currently worth $15 billion, reinvests about $5 billion annually. Considering the magnitude of spending that can occur, the future value of an energy company will be heavily influenced by its future investment decisions. Consequently, when considering an energy investment, we focus our attention on management's capital allocation record.

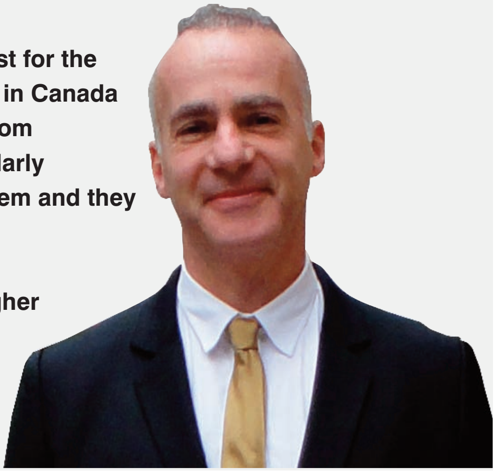
We recognize that the valuation of energy companies cannot ignore oil and gas prices. We also recognize that commodity cycles are inevitable. However, the cyclical nature of commodity prices provides good capital allocators additional opportunities to create value. When commodity prices are low they can acquire competitors at favorable prices and when commodity prices are high, they can raise money at higher valuations. These opportunities exist for all businesses but occur much more frequently in commodity businesses. In our opinion this means having a great capital allocator at the helm of an energy company is particularly valuable.

Luis Seco — I think there is new element of risk management that is going to appear in the investment sector. It is going to be a mutated, expanded version of the risk management that banks for example have done, starting in 1996, because banks are regulated in different ways to investment funds.

Matthias Knab — **Any idea of the characteristics of that?**

Luis Seco: Well, I have my own views. Take regulatory capital, with measures such as VaR. It is very appropriate for banking regulation, but investment funds will move towards new measures closer to the concept of economic capital, which also take into account return, and which is not present in the risk regulatory framework. We may also see increased focus on liquidity risk. But they may not always be quantifiable; take due diligence processes: they used to be a phone call, now they can take months. And the focus on operational risk is likely to continue to grow.

Ari Shiff: Thinking in the same terms as Luis, we are all so astutely aware of technological evolution in so many areas. We see it all around us and yet, in my opinion, the hedge fund industry has done a very poor job of explaining that hedge funds in fact represent the technological evolution of the investing industry, and that the tools we use in our business are geared towards both improving returns and rigorous risk mitigation. Those tools developed alongside the rise in computing power, but they are not as extensively employed by the long-only equity managers that most investors are so familiar with and are so deeply invested in.



I just find it incredible how many of us will run out and buy the latest iPhone just for the iterative improvements in its performance, and yet many, if not most, investors in Canada haven't upgraded to the higher level of investing technology that is available from long/short hedge funds combined with modern portfolio theory. That's particularly startling when you consider that for most people money is very important to them and they spend a great deal of time thinking about how to protect it and grow it.

The technology now exists to attempt to mitigate risk. Investors can pursue higher returns and strive to reduce portfolio risk at the same time. That's a beautiful thing, an advantage our parents and grandparents could not access. I hope that going forward more people will start paying more attention to this issue.

Veronika Hirsch I can't resist one final reflection about the future of Canadian public companies.

Veronika Hirsch: Historically, Canadian investors have been very complacent about the quality of corporate management. Companies have been poorly managed for decades without any criticism or repercussions, eventually falling prey to a global acquirer when valuations became depressed enough. Things have started to change, to a large extent because of US based activist hedge funds getting involved in efforts to surface value from underperforming assets of poorly managed companies. We have recently seen several management teams replaced because of investor dissatisfaction with their past performance. This is an incredibly encouraging development for the survival of the very few world sized companies left in Canada. In future, demanding strategic changes and/or replacement of management teams will become an alternative to takeovers for poorly performing companies. As a result, Canada might be able to keep and grow more world sized companies and one day may cease to be the land of the small cap!!!

Darcy Morris: That is correct, shareholder activism in Canada is on the rise. The activist initiatives we've seen lately are coming from international investors who gladly stir up the old boy's boardroom network that so often exists in Canada. Our country's size is again a structural reason for this. With such a small population you end up with very tight knit communities, especially amongst the investment and business community where wealth is concentrated.

For example, in one of my former firms we had a number of opportunities to actively propose initiatives to management teams when we thought they had gone off course. However, once we would examine the company's board it would inevitably be, "wait a minute, this Director is a client, and this Director is connected to so-and-so, so let's back off and just sell the stock - we do not need to cause a fuss here."

Another reason why Canada is attractive for international investors with an activist mentality is the fact that you need 10% ownership of a company to call a meeting in the U.S., while it takes 5% in Canada.

Darcy Morris So correct, Veronika's comment on opportunities in activist investing in Canada is spot on and more opportunities will be created for everyone out there.

Jordan Zinberg Canada has a growing pool of very talented hedge fund managers operating in a domestic market that has large pockets of inefficiency. This combination leads me to only one conclusion: the future is very bright for the Canadian hedge fund industry.