



Opalesque Roundtable Series '14

NETHERLANDS

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Editor's Note

Dutch pensions, family offices struggle to find ESG in hedge funds

Over the last five years, the number of hedge funds in the Netherlands has more than doubled, from 17 to about 40. Some of them, like Saemor and WinCap, have seen a growing interest from local and international investors, also due to their returns in 2014 (14% and 8.5% respectively by August) and their low volatility or correlation.

The Netherlands is also the home of some large and sophisticated pension funds. One of them is Uninvest, the pension fund set up by Unilever. Over the past year, Uninvest has transitioned from the hedge fund of funds structure to currently 70% direct investments. This has served the institution well, as it views the global hedge fund community as “enormous talent pool” that their internal staff can now also access and interact with more closely.

However, if there is one thing Uninvest is not interested in seeing in a hedge fund, it's beta. The pension applies a **beta constraint of 0.2** to its hedge funds portfolios, which means that “most of the long/short equity funds available in London, for example, are not interesting for large diversified institutional clients given their high beta and costs.”

The other aspect Uninvest is looking for in a hedge fund is adherence to certain **ESG** (Environmental, social and corporate governance) standards. This is important to Unilever, because the principle of sustainability should be reflected not only as a corporation but also in its pension plans' investments, and therefore also in the hedge fund pools. How does Uninvest implement ESG with hedge funds? What is an appropriate approach? What are they looking at? Why is tax (i.e. are the managers paying a fair level of personal taxes) an issue?

The fight to get hidden hedge fund costs “above table”

And how about cost? While in general hedge fund managers have become fairly transparent about fees, they are not always willing to be forthcoming with all the expenses. This is also a reason pensions tend to work with large external operational due diligence firms who, amongst other tasks, will split out all costs, including hidden fees.

The Dutch pensions are not the only investors looking for sustainability in alternative investments. The new **Privium sustainable alternatives fund**, sponsored by a multi family office, has been set up in the fund of funds format with a broad mandate. The fund can invest in microcredit funds, sustainable real estate and sustainable hedge funds. However, the manager admits that until now, his team has *“not yet found the hedge fund that meets our sustainability criteria”*. This sounds like an opportunity for hedge funds willing to step ahead and cooperate with those investors on the ESG side.

The Opalesque 2014 Netherlands Roundtable was sponsored by ABN AMRO Clearing and Eurex, and took place September 9th in Amsterdam with:

1. Thomas Heidstra, **Portfolio Manager Hedge Funds, Uninvest (Unilever Pension Fund)**
2. Gildas LeTreut, **Global Head of Prime, ABN AMRO Clearing**
3. Sven Bouman, **Founding Partner and CEO, Saemor Capital**
4. Iwan Vink, **Founder and Managing Director, WinCap**
5. Ruud Smets, **Partner and Portfolio Manager, Theta Capital**
6. Mark Baak, **Director, Privium Fund Management**
7. Lothar Kloster, **Head of Buy Side Relations, Eurex**

The group also discussed:

- Are there strong empirical links between ESG factors and stock price returns?
- Which costs are sometimes charged to a fund that shouldn't?
- Are we at the end of a valuation cycle for deep value strategies?
- Why should a hedge fund should return at least 10%+ per annum?

- ABN AMRO Clearing: A different type of prime broker
- Eurex' new Euro Swap Future and how Eurex' cross-margining can potentially offset up to 70%
- The great rotation: Why hedge funds of funds are coming back into fashion
- "Not a separate asset class": Why more investors are using hedge funds as a better way to invest in traditional assets

Enjoy!

Matthias Knab
Knab@Opalesque.com

Participant Profiles



(LEFT TO RIGHT)

Mark Baak, Lothar Kloster, Sven Bouman, Thomas Heidstra, Ruud Smets, Iwan Vink, Gildas Le Treut, Matthias Knab.

Cover photo: Vincent van Gogh: Bulb fields and windmills near Rijnsburg, 1886. Photo by Dennis Jarvis.

Introduction

Iwan Vink

WinCap Investment Management

My name is Iwan Vink, I am Co-Founder and Director of WinCap Investment Management running the WinCap Fund.

In 1998 I started as a risk manager at a market maker in equity derivatives and later at ABN AMRO Clearing. Then I moved into a trading position for two institutions before I started my own proprietary company at the end of 2008 making 40%+ return for almost 4 consecutive years. In 2012 WinCap began to offer our value investing strategies to a broader public and accepting investors' money.

We have one fund manager running his long book hedged with index ETFs or futures. He buys stocks with a 50% discount to the market and/or sector and hedges his market exposure by shorting index. Another manager is independently running his short book by selling stocks that are "frauds" and/or heavily overvalued hedged by long index. They both have to perform and deliver alpha. Besides these two strategies we deploy a couple of short-term trading strategies to enhance the performance of the fund.

Ruud Smets

Theta Capital Management

My name is Ruud Smets. I am a Partner and Portfolio Manager at Theta Capital Management here in Amsterdam. Our firm has been specializing in managing portfolios of hedge funds for 13 years now.

We run one fund of funds, the Theta Legends XL Fund, which invests with a selection of the most reputable and longest standing hedge funds in the world. The fund invests across the main hedge fund strategies. One of the attractions of the Legends Fund is that it offers access to managers that have been closed to new investors for many years and that charge high minimums for those who are allowed in. On average the 10 underlying funds have been around more than 17 years and have annualized over 14% over that period with around half the volatility of the MSCI World. We believe the selected managers will continue to offer great risk-adjusted returns across different environments going forward. A unique aspect of the Legends Fund is that it has a listing at the Amsterdam stock exchange and therefore allows investors to buy and sell the fund daily without having to satisfy a high minimum.

The other side of our business is that we run individual, bespoke portfolios of hedge funds for large professional clients including some of the largest family offices here in the Netherlands. For large investors with a long investment horizon we believe this is the best way to invest in hedge funds. It's very cost efficient and avoids commingling investors with varying objections and expectations in one product. Over time this translates in better performance, albeit at the cost of limited liquidity.

Gildas Le Treut

ABN AMRO Clearing

My name is Gildas Le Treut. I am Global Head of Prime at ABN AMRO Clearing. This entails responsibility over a client segment which covers alternative investment fund managers, asset management firms, institutional investors and banks. This also implies responsibility over our Prime project that aims at developing and enhancing our services to meet the needs and constraints of this industry group.

ABN AMRO Clearing is a fully-owned subsidiary of ABN AMRO, providing global execution, clearing, custody and financing services initially for proprietary trading and market making firms, but recently largely expanded into the alternative investment space.

We are one of the leading clearers in the world, covering more than 85 markets across asset classes ranging from derivatives and securities to energy-commodities, FX and OTC products. We constantly seek to expand not only our market and product coverage but also our client segment.

We have a mission statement, which I like very much: "Making our client globally competitive". This is a very easy sentence to say, but actually a constant challenge to implement. Indeed, helping clients to grow entails staying on top of technology, innovation and regulation. This represents challenges and opportunities at the same time.

Thomas Heidstra
Univest Company

My name is Thomas Heidstra. I am a Portfolio Manager Hedge Funds at the Univest Company. Univest Company is the in-house investment service for the Unilever Pension Funds.

Unilever Pension Funds are at about \$35 billion worldwide, from which about \$1.3 billion are in hedge funds assets. My primary responsibility is looking after those hedge fund assets.

I joined about two years ago. Before I used to be a colleague of Ruud at Theta Capital until two years ago.

Right now we are busy with restructuring the portfolio. It used to be a fund of hedge funds.

Although I am based in Holland, my main investments are all outside of Holland, so all over the world. However, the things I am currently working, particularly the cost and the transparency of the funds, are important globally as well as for our domestic industry.

Mark Baak
Privium Fund Management

I am Mark Baak. I head up the Dutch office for Privium Fund Management. Privium is a fund management platform with offices in Amsterdam, London and Hong Kong. We have fund structures in Luxembourg, Cayman and the Netherlands. Total AUM is now close to USD 500 million and increasing rapidly.

We provide bridges between investor requirements and investment talent. Our focus as a solution provider is to make sure that portfolio managers can spend as much time on their portfolios and as little time on all the rest. We believe that this is the best service we can provide to the end investors.

We are currently busy setting up a fund of hedge funds for a large multi family office and we have just launched the Privium Sustainable Alternatives Fund.

Lothar Kloster
Eurex

My name is Lothar Kloster. I am working for Eurex where I am Senior Vice President in the Marketing and Sales Department, focusing on institutional sales and relationship management.

I am sure you are familiar with Eurex, which is one of the leading derivatives exchanges, with more than 2,000 derivative products, mainly fixed income, equity, equity index asset classes, as well as FX and other asset classes.

Eurex also owns and runs Eurex Clearing, which is clearing all Eurex products, and recently also offers a clearing for OTC derivate instruments, mainly OTC interest rate swaps.

Sven Bouman
Saemor Capital

I am Sven Bouman, Founder and CEO of Saemor Capital. We are the manager of the Saemor European Alpha Fund. The fund was launched in 2008, with the backing of AEGON as a seed investor.

The fund is a market-neutral European equities fund with a widely diversified portfolio, investing in stocks both on the long and short side.

We employ quantitative strategies for stock selection and portfolio construction. Our main engine is a multifactor model, which is composed of fundamental and technical factors that have proven track record as predictors for future stock returns. This enables us to rank all stocks in our universe on multiple factors like the earnings yield ratio, analyst revisions and balance sheet strength. We buy stocks that rank attractively in our model. Long positions are ideally stocks that are cheaply valued, enjoy improving business and earnings trends, show strong price technical and have strong business fundamentals. For our short book we look for stocks that score poorly on most of these factors.



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Sven Bouman: We had quite a good year so far. The fund is up 14% as of the end of August. Our stock selection model has more or less fired from all cylinders throughout the year. Earnings momentum has been our best factor family.

Stocks where analyst revised earnings estimates upwards have been highly in favor. Most other factors also showed a positive pay-off, although their performance varied over the course of the year.

At the beginning of the year equity markets were in a risk-on mode, which meant that deep valuation factors like price-to-book delivered strong returns. Subsequently investors were looking for higher yielding stocks. From the second quarter onwards, the European economy experienced some weakness and investors started to shed risk and buy into quality assets. Since May quality factors started to perform. Companies with decent balance sheets, with stable earnings over time and low price volatility did well as a result.

The Saemor fund was able benefit from these trends as our model has a few unique features, one them being its adaptiveness. During the course of the year we have put more emphasis on risk-off, defensive factors. This is important as the underlying economic environment keeps changing and the predictive strength of some factors varies depending on the macro environment.



Iwan Vink: The WinCap Fund is up 8.5% per the end of August which is also a good result because we achieved this with a 60% long / 60% short book. Unfortunately our trading models didn't contribute that much. While we had some volatility in July, for most of the year there was not a lot of volatility.

Deep value worked out quite well, but possibly we are at the end of a valuation cycle where a lot of deep value stocks are not as cheap as they were say half a year, one year or a couple of years ago. We monitor the markets carefully, as we are very focused on the risk side to prevent losses for our investors.

So in general, we are very cautious, but still, here and there we find some interesting stocks that are relatively cheap compared to the index. It is typically good for our strategies when the markets make a correction. At the other end it is easy to find stocks with an extreme valuation or with growth projections that are not very likely to be achieved in the coming years, to sell short. So, from the long side we are waiting for more volatility to come back to the market that will give us the opportunity to benefit from it, but we need to have patience and wait for that.

We still have a couple of months to go before the year is over, and we are confident that our returns will be 10%+ this year, what will be ok. As long as the fund is returning less than 10%, it's a bit of a hard sell to new investors despite the fact we are a low volatility fund. A lot of potential investors have many asset classes they are very happy with, especially after the five years of bull run in the stock market. Some of those investors don't even care if they are going to lose 10% or 15% on those assets.

I think a hedge fund should return at least 10%+, but even then, some investors doesn't see the inflection points of bond and stock markets and that it may be a good moment now to shift to an alternative market neutral investment.



Ruud Smets: I must say the returns of both Sven and Iwan this year have been very good relative to most of their hedge fund peers.

We are currently up around 4% across our portfolios, which is a bit slow compared to the last few years but which still compares favorable to the hedge fund universe.

What's been working well this year is the event driven strategy. There has been a lot of corporate activity such as mergers on the back of reasonable valuations, cheap financing being available and improving visibility on growth especially in the US.



Another strategy that has done really well is trend following. While most money managers would not have expected a further rise in government bond prices to the extent we have seen, this was one of the trends correctly picked up by their models.

On the other hand global macro funds have not yet delivered. Their big themes such as US versus EUR rates, Japan, and long USD have not worked this year although they have been picking up more recently. However, with the discrepancy in economic growth between the US and Europe becoming clearer and central bank policy reflecting this and becoming more data driven, I do believe these trades could well be strong contributors going forward. And when they do, this could well be accompanied by lower equity and bonds markets.

Iwan Vink

Some fund of funds do actually try to pick styles depending on the macro environment, going from one strategy to another depending on the foreseen risk-reward. Are you doing that actively as well?

Ruud Smets: To some extent yes, but with a big caveat: trying to predict all the time which strategy will do well in the next six months can easily result in chasing the best performers of the last 6 month. Over the long run this will strongly impair your investment results. There are definitely certain periods in which the environment throws up opportunities or risks which allow us to add value by active strategy allocations. In 2006 we got rid of our long credit exposure and added some short-biased credit funds. After things settled down in 2009 we added to our distressed debt managers. More recently, in 2013 we increased our event driven equity exposure as the environment was becoming very favorable for corporate activity. These are only 3 meaningful moves over a period of 8 years, but they have certainly made a big impact on results.

As a more overriding theme, being somewhat contrarian will help performance over the long run. Many investors left the trend following space in 2013 after being invested since 2009, chasing the strong returns in 2008. Trend following is our best strategy year-to-date with returns around the 20% mark. The same could well be true for global macro funds for the period ahead of us. While many of the funds that have done well over the last period, take long credit funds as a prime example, are likely heading for much lower returns and are showing a less interesting risk-return profile.

Thomas Heidstra: We have been doing quite a few things this year, let me start going over the performance. We apply a beta constraint for our hedge funds portfolios, meaning that shouldn't have a beta of more than 0.2.

We have return targets of cash plus 4, and so far we are up about 3% for the year which is probably a reasonable reflection of the industry returns for this year. We will probably meet our return targets, but that's not to say that we are ecstatic about that, particularly if you look at what other asset class have done, but maybe I will come back to that later.

What has worked fairly well this year was our transition away from the fund of funds structure, which was quite diversified in terms of fund of funds and enormously in terms of hedge funds – however with no control, no transparency and quite high costs compared to a direct structure; so that has been a significant change over the last twelve months.

From an investor perspective, the funds are more or less doing what they are supposed to do. In terms of return targets, while there may be a bit of a disappointment perhaps, the main aspect here is that the client also has a good understanding of the global investment climate. For example, if you look at the returns of a bond portfolio, nobody internally at our place and probably no external bond manager would have forecasted how good those returns will be this year. In that context investors are still satisfied with that returns, if it was not for the high level of costs.

Like many other pension funds, we are trying to do a lot, maybe too much at the same time. So for example, we are talking about costs with the managers directly now, or we try to implement an ESG policy, which is very important for Unilever because the principle of sustainability should be reflected not only as a corporation but also in our pension plans' investments, and therefore also in the hedge fund pools.

When implementing an ESG policy, we are trying to set something up that makes sense, meaning it will have to go beyond just a box ticking exercise. For example, we are also trying to get in idea what sort of taxes the managers pay. Are the managers paying a fair level of personal taxes, or can they get away with internally deferring profits into a fund, which is a topic that I find personally quite interesting apart from the ESG aspect of it.

Another aspect of running a hedge funds portfolio within a pension to try to access these knowledge strategies for the broader institution. The global hedge fund community represents an enormous talent pool, and we feel we can gain a lot more from interacting more closely with the funds we are invested in than just say giving them their allocation and have them run with it. I am not suggesting that a pension should now outsource all management to those mega hedge funds or multi strat funds out there, but rather have a constructive dialogue with a couple of managers about how to use their strategies and how you should build your portfolios. As we are direct investors now, we started that communication, and it is working well for us.



Matthias Knab

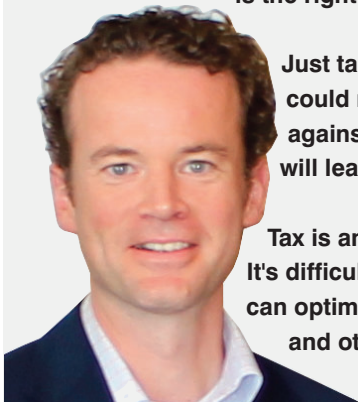
Univest has transitioned their hedge fund investments from a fund of funds to direct. Can you tell us more about that process and also about your team?

Thomas Heidstra: About the team, you are looking at it. I mean, that's the eternal conflict of pensions. Of course, Univest would like to do more, but they are constrained for example by direct budgets for personnel

So that is a structural, industry-wide issue, and while you'd think to see all costs in the proper context should be a no-brainer, it's not. It is an industry-wide issue to get budgets for your team. In the end, we have to maneuver smartly with the money that we have.

But having said that, we have the budget for an advisor which is currently Aksia, so we transitioned away from the previous set up where we had two advisory structure, which was quite a bit more expensive. All the work that we require - operational due diligence and to some extent the investment due diligence – is done by Aksia for a fixed dollar amount per year. So they helped us internally to build out the portfolio which is now 70% direct.

Thomas Heidstra: We are doing it basically in trying out small steps. When it comes to ESG and hedge funds, it is a challenge to get to a solution or an approach that makes sense. We don't want to work with an exclusion list for our hedge funds for example, which is a route that a lot of people have taken. I think this is difficult, and I am not sure this is the right way to go.



Just take a deeper look at all these different types of the ESG. For example, at governance, you could make a case that activists are there to improve governance, but they here we came up against the fact that as a corporate entity, should we be really investing in activists? Maybe we will leave that for the time being.

Tax is an issue that's important for a lot of people, particularly from the pensioners' perspective. It's difficult to explain that a highly remunerated manager pays much lower tax levels because he can optimize his tax structure compared to someone who has always paid his pension contribution and other taxes. I think it's actually impossible to explain.

Sven Bouman

How do you implement ESG? Do you only invest in funds which have incorporated the concept into their investment strategies?

Thomas Heidstra: Well, to be honest, no, not necessarily, because the offer is not that interesting – if I put it very bluntly, people just put a stamp on that and say it's ESG. So that's exactly what we don't want to do, because then you get to the box ticking type exercise.

So it's more from what we at Unilever and other participants think as relevant, and then try to combine that as well as possible within the framework of running a certain hedge fund strategy.

And I have just mentioned taxes, because I think that's very interesting. There are a number of governance and social issues involved, but taxes for private equity and hedge funds are really topical.

Mark Baak: I agree with Thomas. We just launched the Privium sustainable alternatives fund, which has a broad mandate. We can invest in alternatives like microcredit funds, sustainable real estate and sustainable hedge funds. The latter would be ideal given the monthly liquidity with 15 days' notice on our fund.

But we don't have any sustainable hedge funds in the portfolio at the moment. The reason is that both we and Triodos MeesPierson, our investment advisor, have not yet found the hedge fund that meets our sustainability criteria. I hope that this will improve in the near future, by high quality groups like Saemor Capital considering sustainable hedge fund launches.

Generally, we see more demand for fund of hedge funds (FOHFs). One reason for this flow could be reducing allocations to fixed income. Most recent data showed a 12% annualized growth for FOHFs over the first half of this year. We will support that growth, as we are launching a FOHF before the end of the year, which will be seeded by a multi family office.





ABN·AMRO Clearing

save the date -11 February 2015

The Amsterdam Investor Forum

Wednesday
11 February 2015
09:00 – 17:00 hrs

ABN AMRO Clearing is pleased to announce it will organise its fourth Amsterdam Investor Forum. Like previous editions this event will focus on the current opportunities and challenges of the alternative investment industry. The Forum will be a strategic meeting place for Institutional Investors and (Alternative) Investment Managers.

In previous years the Amsterdam Investor Forum welcomed speakers like Stuart Fiertz (Cheyne Capital Management), Graham Neilson (Cairn Capital) and Nassim Taleb (Universa). For the 2015 edition we have the challenge to match that level of speakers and that the agenda topics will adequately reflect what is on your mind in the current market environment.

We look forward to welcoming you at The Amsterdam Investor Forum 2015.

We have a limited number of places available and reserve the right to exclude registrations.

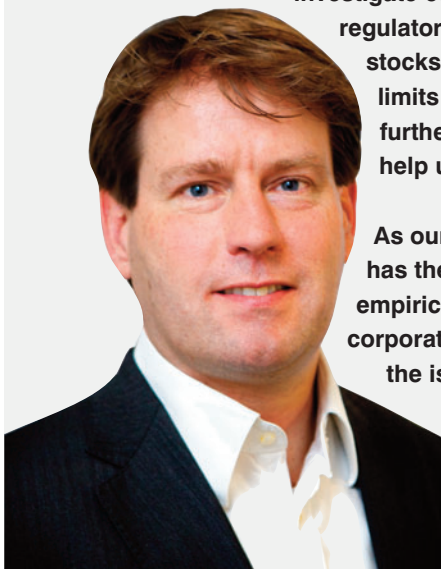
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Sven Bouman: We also look at ESG and have incorporated it into our risk management framework.

What sets Saemor apart from pure quantitative managers is that we also use fundamental insights in our portfolio construction process. Our portfolio managers each cover a number of sectors, speak with sector analysts and investigate corporate events. M&A, poor governance, accidents, product recalls, litigation and regulatory decisions can have a strong impact on the stock prices. We tend to exclude these stocks from our investable universe or limit the potential position size. These position limits are fed into our portfolio optimization process. We are looking to quantify this further. We now have access to a big database of ESG factors, this data could potentially help us further in this process – not as an alpha driver but more as a risk factor.



As our focus is first and foremost on generating alpha, we only include a new factor if it has the potential to improve our returns further. As of yet we haven't found a strong empirical link between ESG factors and stock price returns. The most promising are corporate governance metrics, as poorly-governed companies tend to underperform. But the issue with these datasets is that the history is relatively short. For these reasons we have not included ESG into our alpha model. That said, if you look at our model, we definitely already have included a number of factors which have a strong overlap with ESG. Factors like balance sheet strength and stability of earnings point our portfolio to the more sustainable companies.

Gildas Le Treut: With respect to your question, we have been very busy implementing solutions to help our clients dealing with regulatory challenges. We also spent a lot of our time reinventing ourselves. For the last 30 years, we gained recognition and a strong brand in servicing proprietary trading and market making firms across different markets and products. But for us, over the last 2 years, a large part of the growth came from servicing alternative investment funds.

These new clients were either major industry players looking for operational efficiency and a financially sound counterparty, but also from emerging managers, teams of traders starting their own funds, looking for a Prime Broker specialised in their strategies. These clients expect more high touch and bespoke services, so along with other factors, there was a need for us to reinvent ourselves and enhance our services as a specialised prime broker.

We are thus investing in building and enhancing cap intro services, execution services, product coverage, reporting, etc., to adjust ourselves to the demands of hedge funds.

With respect to market trends, we are quite big in the CTA and managed futures space, and as we touched upon already, we have seen a kind of recovery there. Last year was pretty bad for CTAs and quants, and although we have seen upward trends, there is an important dispersion of the performance between managers. Some CTAs deliver a very strong performance while others are still struggling, but the overall sector has been doing better.

In Europe, we have seen a lot of interest from investors for equity strategies, particularly equity long/short, equity market neutral and merger arbitrage, probably because of the interest for new IPOs in Europe. We have experienced a steady growth of assets in these strategies over the last 12 months.



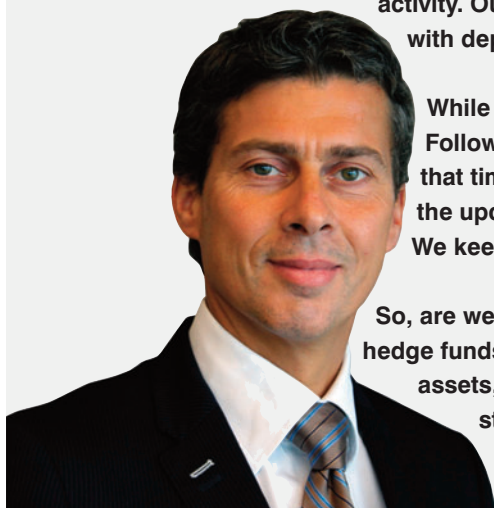
Iwan Vink

I am a client of ABN Amro Clearing. Where do you see the big advantage of say ABN Amro Clearing compared to other clearers or prime brokers?

Gildas Le Treut: That is a very good question, especially because we are positioning ourselves as a different kind of prime broker. This comes from our history and our strengths. Contrary to most other prime brokers, we are coming from the processing and post-trading side of the business. That is a big difference from the other major prime brokers which are usually investment banks. ABN Amro Clearing grew by the combination of a leading global clearing firm and top rated global custody platform, to service very demanding top tier institutions.

We are now known to be efficient, nimble, innovative, financially sound and extremely focused on hedge funds' strategies where our cross assets-cross markets correlation is unmatched. There are not many prime brokers that cover all asset classes in one legal entity, in one back-office and risk system and that truly provide cross products offsets.

Coming with a strong post-trading angle also has its advantages when addressing some of the regulations today. If we look at AIFMD for example, this was of high importance to work with other partners, such as depository banks. We speak the same language. AIFMD regulation is all about asset protection and segregation mechanisms all along the processing flow. This is definitely part of our DNA as a custodian and a clearing firm, dedicated to servicing clients' activity. Our legal framework and our flexible account structure made it easier to speak with depository banks, who take responsibility and liability for restitution of assets.



While we always acted as a cash PB, we are also expanding on synthetic products. Following Lehman's bankruptcy, cash PBs evolved into synthetic prime brokers. At that time, we had to go with that route as well for some specific clients. However, with the upcoming regulations like Basel III, it may make sense to come back to cash PB. We keep both options open.

So, are we different? Yes, we are different but, above all, we are specialized in certain hedge funds' strategies where we believe we provide un-matched and efficient cross-assets, cross-markets integrated execution, clearing and financing services. These strategies are mostly high frequency, quants and CTAs, arbitrage, relative value and equity alternative strategies.

Iwan Vink

With AIFMD, the role of the depository will be more important. Is there a dynamic within ABN to take that role as well as you are already the custodian of most of the assets?

Gildas Le Treut: We spent a lot of time analyzing whether we should expand our services to depository and fund administration, and become a one-stop-shop for managers. Fund administration, prime brokerage and depository services are very different types of businesses that require very different sets of expertise.

Although it is commercially attractive to be able to provide more services to clients, I think the current industry landscape requires the use of true experts in their fields. I strongly believe that you cannot be a leading prime broker, a sound depository bank and a great administrator. We are a global custodian and a local sub-custodian in Europe, but this is very different from being a depository bank.

We have decided not to expand our services in that direction but build strong relationships with partners, experts in fund administration and depository services. We like the idea of leaving our clients with the choice to determine who is the best fund administrator and depository for their strategy, instead of trying to rebuild or reinvent the wheel.

So for the last 18 months, especially for AIFMD, we have been working closely with depository services and fund administrators, who are probably the best in their sector. We believe in this best of breed solution where funds managers choose the best specialized provider for their business. Funds managers do not want to be forced to use providers that are not fully geared to their business. This is what may happen when using global banks.

Gildas Le Treut: What I can tell is that regulations, especially Basel III, are changing the hedge funds industry landscape and that we are very much focused on finding ways to reduce the impact of Basel III, and notably costs, for our clients. Every regulation represents on one side a challenge that requires a lot of investments in people, in IT, etc. At the same time, regulations are also an opportunity. If I just take EMIR and mandatory clearing of OTC derivatives, as an example, it provided us as a clearer, a great opportunity to access a new product segment, the interest rate swaps, complement our service offering and leverage our expertise in clearing. We captured this opportunity and now rank amongst the largest pure IRS clearers in Europe.

If we look at AIFMD, we have almost the same picture: challenges linked to AIFMD reporting and segregation, and opportunities to demonstrate our flexibility and build strong partnership with depository services firms.

Now, the real challenge is to adapt our services to help clients coping with regulatory changes while at the same time regulations might well contradict each other. For instance, Basel III costs might well force prime brokers to reduce their swap books, while at the same time AIFMD forces alternative managers to trade their equities in the form of CFDs or swaps. It is clear that certain alternative funds managers will have to adapt their trading strategies depending on the limitations of their prime brokers.



Ruud Smets: The barriers of entry of launching a successful fund have definitely gone up a lot and raising money for a startup fund has been extremely difficult the last few years. It's great to see some funds succeeding here at home despite these barriers. The quality of those who make it as a result I believe is generally higher than before the crisis.

When we look at new funds, we typically see significant additional business risk compared to more established funds. This is something we need to get well compensated for in order to get involved and it's not an area we are very active in. We do see many start ups as we have a research partner that does allocate actively to new funds. Every now and then we find some extraordinary talent for which an early involvement can make a big difference.

In terms of investor interest in hedge funds, this is still at a low point here which can be partially explained by poor experiences in and after 2008, but also by the strong rally in equities and bonds of the last couple of years. I have no doubts that investors will start looking more at hedge funds when their relative returns are sticking out better. A turn in the bond market could well be the kick-off to this. And what they will then find is a more mature industry with lots of lessons learned and a more realistic promise. At Theta, we have already seen strong interest from large, sophisticated investors for a number of years, and this will be typically followed by the broader investor community.



Gildas Le Treut: We see a lot of dynamism in terms of creation of new funds in the Netherlands, it's quite impressive. There are a lot of good ideas, a lot of willingness to start, but raising capital, especially for emerging managers, remains the challenge.

The last couple of years, investors had a tendency to allocate to the same type of large, billion or multi billion funds managers. Funds below the €50-€70 million mark were definitely struggling in raising their profile and get investments from large allocators.

However, the dynamic recently changed, mainly driven by family offices looking for the new ideas, new talents, and different ways of investing. Family offices love partnerships and are generally good at selecting the right managers. They often manage the set-up of the funds and all the administrative tasks, and let the managers do what they are good at: trading. This often means that the family office is very much "hands on" which might be the price to pay for emerging managers to reach a certain size.



Thomas Heidstra: I don't have a very strong opinion on the Dutch universe because our current portfolio is biased towards the U.S. and a little bit in London. But we do get quite a bit of information and reports, and we can see that there are some good funds and good people here.

But as Gildas and others mentioned before, a fund needs to get past a certain threshold, and that's a challenge. For example, we work with Askia and have access to their screening list of 350 funds where they have done operational due diligence, so all is checked there and perfectly good. The challenge is really for the new fund here in Holland to get on their approved list, or for Aksia, what is the additional value to get a new Dutch fund on, from their perspective, for example?



If you look at how the London or U.S. markets have developed, they were driven mostly by domestic investors primarily. I agree with everyone that there is a lot of talent here, but the challenge is getting off the ground given the competition from the established funds in U.S. and in London.

But it would be good in the end also for investors if that changes. For example, if you look at the long/short equity funds that are available in London, most of them are not interesting for large diversified institutional clients given their high beta and costs.

So while that points to opportunities out there for start ups to do things differently, the challenge is how to get it off the ground? You need some domestic investors, as I said. That has been tried in the past obviously, and maybe still we can still give it another try to get to a critical mass. I'm not sure that's going to happen but maybe we'll see one or two more in the near future reaching a decent size and that could get the broader industry going.

Mark Baak: I have been involved in manager selection for more than 10 years. I don't think the environment in Netherlands is significantly different to the environment in Singapore or New York. It's always difficult for managers to launch, this is true here and elsewhere, now and 10 years ago.

Despite the challenges, the number of hedge funds in the Netherlands has more than doubled over the past five years, from 17 to about 40.

The hurdles to launch a hedge fund have increased globally over past few years. The costs of running the business and coping with regulations have made it more difficult for smaller funds. That's good for platform providers like us. On balance, we benefit from this trend as more portfolio managers launch their funds with us.

The demand for hedge funds in the Netherlands is mainly coming from wealth managers, private banks and family offices.

Like any other insurance company, the Dutch insurance companies are also impacted by Solvency II. So I don't expect any decent inflow for hedge funds from insurance companies.

With pension funds, we see a big difference. Some pension funds have their own professional teams, are experienced, and are able to have a good dialogue with the regulator. The DNB, the Dutch Central Bank, openly stated that they have got nothing against pension funds investing in hedge funds, if the pension fund manager can explain what they are doing and what the pension exactly did to come to their hedge fund allocation.



Sven Bouman

Mark raised interesting points about the Dutch Central Bank, who said pension funds have to be in control of their investments. I hope that it also helps our case. If you want to be in control, you have to know where you invest in and what the manager does. This should benefit managers who offer full transparency and have repeatable investment processes.

Lothar Kloster

To what extent do you see the demand from end investors like pensions for hedge funds, and away from fixed income investments, driven by the current low yield environment?

Mark Baak: Yes that certainly plays a role, but pension funds are rather limited to invest in hedge funds because of their asset-liability restrictions. Family offices have more flexibility to allocate according to the best risk-return profiles and they on average have much higher hedge fund allocations. Pensions cannot invest like that, but Thomas has a better insight about that.



Thomas Heidstra: There are differences here also between Europe and US. In the US, you can see a state plan making very large allocations to hedge fund strategies in order to meet certain return targets, although those flows then tend to go to the very large hedge funds. We do not see these in the Netherlands, we see rather the reverse. With all the regulatory pressure and focus on costs, Boards at the moment are leaning towards reducing or eliminating their hedge fund exposure which makes the overall asset raising environment tough, I would have thought.

Iwan Vink: Having started just two years ago, we are an emerging manager. In our marketing, we are focusing on the retail investors plus the high net worth individuals up to the smaller family offices. Although most Dutch potentials are not familiar with investing in hedge funds, they are not happy with the low yields on cash and bonds and are looking for alternatives. So they start looking to hedge funds from both a diversification and return perspective.

What's positive is that we are starting to get enquiries coming in from the smaller family offices and advisors who are looking for investments and finding us. We are quite happy with that. While the low volatility environment is a challenge in terms of achieving good returns for a fund like us, it does also bring us new clients, so it's a kind of balance there.



Matthias Knab Are offering your investors access via UCITS?

Iwan Vink Right now we don't offer UCITS, our minimum investment is EUR 100,000. The fund is not regulated under AIFMD, but we will probably have to do that next year. But even then, we would maintain the same minimum investment.

Sven Bouman We are seriously looking into the idea of launching a UCITS fund. It can be a carbon copy of our current strategy, so with low volatility and market neutrality. The UCITS format suits our strategy very well. We have heard from private banks like ABN Amro that the demand for UCITS is definitely on the rise. So this is on the top of the agenda of our investor relations managers right now.

Gildas Le Treut Where do you see the most interest from investors for your type of strategy and returns?



Sven Bouman: At the moment, mostly in Northern America, so the US and Canada. Here in the Netherlands the appetite for hedge funds is low but slowly improving, especially amongst high net worth individuals. Currently our investor base is still mostly Dutch. Capital raising takes time and we are confident we will continue to grow and broaden out. During the last couple of years we have met a lot of investors who keep on tracking us. We travel regularly to the US, the UK, and lately also to the Middle East to see investors.

Our performance, size and profile makes us interesting for a lot of investors across the globe. As mentioned earlier, we have insurance company AEGON as a cornerstone investor. That represents a very stable base of assets, which has enabled us to invest in the business and to set up an institutional infrastructure. The assets under management are over \$700 million, which is comfortably above the minimum size threshold of most fund of hedge fund managers. Also from a regulatory and governance perspective, we comply with high standards of the AIFMD, among others.

Matthias Knab Please tell us more about your process and your capabilities to deliver pure alpha. Thomas had mentioned he is not interested in the beta part at all, so please share with us more details about your procedure and results in that respect?

Sven Bouman: The Saemor fund is market-neutral with a relatively low volatility of 8% to 10%, and it has enjoyed strong returns over the last five years with over 9% per annum. This is pure alpha. If you look at our return profile, the correlation with existing markets whether you compare us to the MSCI Europe or S&P, is zero to slightly negative. If you correlate our hedge returns with the peer group of market neutral hedge funds, long/short hedge funds, or hedge funds in general, it's also close to null.

That means we have performed well when equity markets and other funds had a difficult time, and vice versa. This return profile definitely helps investors to diversify both their equity and hedge fund investments.

Matthias Knab Who of you is working on new products or new ideas?

Sven Bouman

On the longer term, we have an interest to port our strategy to a global product. This will broaden the opportunity set and thereby the alpha potential. If you look at our current model, all the factors that we have included also work in other parts of the world. At our previous employers we also ran global models and strategies.

Mark Baak: After we have launched our Privium Sustainable Alternative Funds, we are now working on a new bespoke fund of funds for a multi-family office as an appropriate vehicle for them to invest in hedge funds. They decided that fund of funds for various reasons was the best way to do that. The majority of the allocations will be to the bigger multi-strategy managers.



Lothar Kloster

We continue to expand our suite of derivative products, e.g. in the fixed income segment. The currently challenging market environment, is reflected in the volume development: while volume in our government bond benchmark products is slightly decreasing, we see rising volumes in our futures on the French and Italian government bonds as well as in our 30year Buxl futures during the first half of this year..

Lothar Kloster: Against the background of the EMIR regulation with mandatory clearing of OTC interest rate swaps we have just launched a Euro Swap Future. This contract essentially provides the economics of an OTC interest swap, but with the benefits of a standardized futures contract, e.g. exchange traded, with a transparent open order book, but also offering off-book transactions, and of course centrally cleared and risk managed like all other future contracts

Gildas Le Treut

Isn't it a bit contradicting with Eurex's other initiatives to become a CCP for IRS?

Lothar Kloster

Well, one instrument doesn't necessarily exclude the other.



Lothar Kloster: Currently, Eurex Clearing offers EMIR compliant clearing of OTC interest rate swaps with more than 35 clearing members admitted and more than 140 registered customers in onboarding, and we continue to expand that clearing service, in terms of participants, products and currencies. Our newly launched Swap Futures contract is designed in such a way, that upon expiry open positions are fulfilled by way of physical delivery of an underlying OTC interest rate swap. So you could use that futures contract in order to manage your exposure and offers physical delivery and establish a corresponding OTC swap position essentially offering investors the choice between a listed future and CCP-cleared OTC swaps for managing interest rate exposure.

So while the swap futures might in some instances substitute an OTC swap, I'd suggest that it's an instrument of a more complementing nature.

Iwan Vink

I have a question regarding the collateral for swaps. How is that defined? When I buy a equity swap through Eurex, I also need to deposit collateral. How does that look compared to the margin on a future? Can you elaborate more on this?

Lothar Kloster: Yes, collateral has to be put as initial margin for both swap futures and OTC interest rate swap positions. And in addition, daily variation margin in cash applies to both instruments. However, exchange traded futures and OTC swaps represent a different types of instruments for the purpose of clearing.

Consequently, EMIR regulation stipulates that futures contracts are margined with a two-day margin horizon whereas an OTC swap is margined with a five-day horizon. Furthermore, contract maturity – 3 months for futures compared to much longer maturity or up to 30 years for swaps - as well as outstanding notional amount have to be taken into consideration for margining. So from that perspective margin requirement for OTC swaps tends to be somewhat higher compared to swap futures.

On the other hand, since both swap futures and OTC swaps are cleared by Eurex investors have the advantage cross margining. Positions in swap futures contracts and positions in OTC swap contracts are margined within one margin group and you could realize margin offsets. So depending on how your portfolio is structured you could have margining offsets potentially of up to 60%-70%.



Gildas Le Treut

In this industry, you must continuously invest and innovate, not only to stay on top of competition but also to support our clients in a challenging environment.



Gildas Le Treut: Product innovation is mainly driven by our capacity to correlate in our risk model the new product with other asset classes traded by the clients. It is our business to manage risk on behalf of clients and to ensure that we help them in their strategy, wherever they trade and on whatever product. So if they trade a derivatives on Eurex and the underlying on Euronext, we will correlate those and create some risk offsets.

As an example: for volatility funds we are now implementing Varswaps. These pure OTC products offset other listed volatility products in clients' portfolio. Interest rates swaps are already part of our cleared product range since 2010, and Varswaps will be added as an OTC product this year.

Lothar Kloster: Sharing Iwan's previous observation overall market environment was recently characterized by relatively low volatility – the low was in June with something like 13 points in the VSTOXX index but volatility has come up a little bit since then. Nevertheless, we see rising volume in our volatility products with a daily average of 28,000 contracts. In addition to VSTOXX products, we also look into broadening the product range and plan to launch a variance futures contract in September. This instrument essentially provides the economic exposure of an OTC variance swap, but with the advantages on an exchange traded and centrally cleared derivative.

Matthias Knab

Anyone of you wants to share an outlook or also market view for our industry? Where are we going next?

Mark Baak: I believe there will be a big opportunity for hedge funds when investors will stop using hedge funds as a separate asset class. Many hedge funds can be seen as part of existing asset classes. For example, when investors start using long/short equity as a replacement for long only equities, or long/short fixed income as fixed income.

A strategy like long/short equity has proven to be much better for investors in terms of risk return than long-only equities. If I have to choose between a broad basket of long-only equities and a selection of long/short equity hedge funds, then I would definitely go for the long/short equity hedge funds. I see some sophisticated and unconstrained investors doing this for many years now.

The family office that asked us to launch the FOHFs for them is no different. When they talk to us, they are not discussing equity long/short hedge funds with us because those are already part of their equity book. In their perception, a long/short manager is just an equity manager but with more flexibility than a long only manager. The flexibility they look for is to go short and to remain in cash when there are not sufficient opportunities available. Hedge fund manager can also decide on which stocks they want to spend their time and effort, regardless of the index weighting of such a stock. A constrained long only global equity manager must have an opinion on Apple, Novartis and Tencent.



Sven Bouman: From now on, we will have a bit more desynchronization in the world. QE in the US will be brought down, while Europe and Japan are stepping on the gas.

In Europe there is a tug of war going on at the moment amongst market strategists. The 'let the data talk' camp is on one side of the rope. The European economy is slowing down, still growing but less strongly. On top of that we have some extra risks coming from the Ukraine and Middle East. And in such an environment, you typically need to have a quality tilted portfolio.

On the other side of the rope, we have the guys who say 'don't fight the ECB'; every deterioration in the data will be met with a policy response from the ECB. And in such an environment, you should buy high-risk stuff, deep-value stocks.

We still don't know, of course, how this battle will end. That will create a bit more volatility and dispersion in Europe in the short term. The longer term outlook for European equities still looks good. Equities are supported by ample liquidity supplied by the central banks, M&A and the recovery of the economy. This environment should provide ample opportunities for market-neutral, long-short equity, event-driven and CTA funds.



Ruud Smets: I agree with Mark that investors should not view hedge funds as a separate asset class where they purely aim to achieve uncorrelated returns. Hedge funds are a pool of some of the smartest investors out there with the freedom to invest across asset classes and with a wide range of instruments. They should be allowed to capitalize on large market movements, meaning betas can be high over certain periods. Our investors typically do view hedge funds that way and as a result use them as a better way of playing the traditional asset classes.

There is a high cost involved and only the very best in our view warrant these fees. You don't want to pay these fees just for a levered play on risky assets for example. If you are able to find and access the best managers and you employ a long investment horizon while minimizing turnover in your portfolio, you can achieve substantially better results than investing directly in the underlying asset classes. If you can then also manage the risks involved well,

often related to the structure of the funds, hedge funds can actually substitute a fairly large part of your portfolio. This is how our most sophisticated investors approach hedge funds and they have done very well over the years.

The structure for our bespoke portfolios has been created to optimally execute on this philosophy and we apply the same principles with our Legends Fund. Invest only with the very best and limit turnover in the portfolio to the minimum. I believe investors will come to appreciate again the results you can achieve with this over time. Especially when equity and bond returns become more muted than we have seen over the last few years.

What will help hedge funds to stand out is a more data dependent central bank policy, compared to the full-on liquidity flooding. We are starting to see this. This will result in more valuation driven markets which is definitely a good thing for hedge funds.



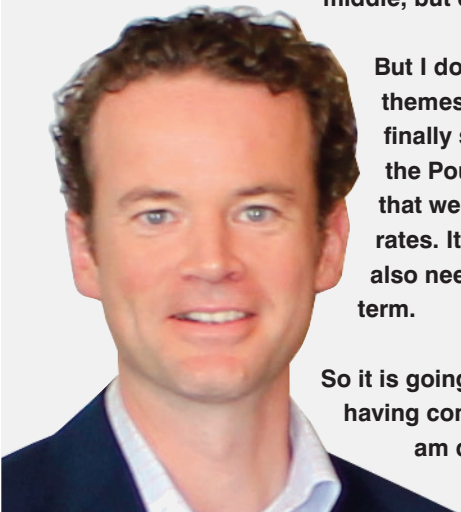
Thomas Heidstra: Mark mentioned long/short equity, we don't have a lot although it could be interesting given the protection you get from the short book. If you get paid for having some protection against a significant equity market downturn, that is obviously interesting. The problem is that not many managers have done that.

What we run against is that the pricing is wrong. Why is the pricing of the hedge fund completely separate from say a active long-only manager? In an ideal world, what we should be doing is using a certain fee structure of a particular active long only manager and build on top of that according to what the hedge fund manager offers. The result will be a much lower fee level than what is currently being asked.

In my view, if you really want this industry to grow, the pricing will have to come down, which simply starts with where the active managers are. So fees are something we are working on, but in general I am not very hopeful they will change very much in the short term. But if you look at management fees and you get up towards a 1% level for long/short equity, we have come quite a bit from where we were two years ago when we had a fund of funds product.

Let's say you have a couple of long/short equity managers who provide an attractive return together with a downside protection, and low correlation to markets. And then you can actually say, "well compare this to an active long-only equity manager active with a correlation of .9", and the hedge fund will become actually a lot more interesting.

Also, going forward, I think it is an extremely interesting time for global macro, which so far has been our biggest disappointment. If you look at our performance, relative value has been good, the fund of funds have been in the middle, but discretionary macro has been awful...



But I do think the environment going forward this year will be interesting. A lot of the themes managers have been playing like the US-Europe divergence that you mentioned finally started making money. The uncertainty around the Scottish referendum is moving the Pound, and we still have an ongoing discussion about the Euro. I'm not sure I agree that we have all that much tailwind, but we certainly are in an environment of much lower rates. It is going to be very interesting to see how effective the measures are since we also need some fiscal restructuring. Europe is going to be very difficult and very long-term.

So it is going to be a very interesting environment. We are hopeful that managers who are having complete freedom will find some original ideas to make some money. In that sense, I am quite optimistic for next year.

Mark Baak: I would like to add a combined comment regarding fees, business stability and smaller managers seeding. AIMA put out interesting research relating to the alignment of interest between the investors and the hedge fund managers.

Along with that I think it is possible to get hedge fund fees down in return for a longer or larger commitment. If an investor has a higher amount invested with a hedge fund for a longer period of time, that could work for both sides.

I agree that many pension funds won't be seeding managers, however seeding is also a proven way to get fee discounts or a stake in the company, or both.



Sven Bouman

I have one question for Thomas. I understand pension funds have to calculate their total expense ratio which also includes the underlying costs from external managers. In your experience, are hedge fund managers transparent in the costs they incur? Management fees and performance fees are relatively simple to deduce, so I am referring to other operational costs.

Thomas Heidstra: Hedge fund managers are fairly transparent about fees in my experience. They are not always willing to be forthcoming with all the expenses, but that is also a reason why we work with Aksia, who have an operational due diligence team of close to 40 people, and that is one of their tasks: to split out all the costs, get all the hidden costs as well, getting those above table, and come up with a total expense ratio for the fund.



When we used the fund of funds structure and we tried to get information from the fund of funds managers about our cost base, we never got the the costs above-table with some, while with others, it took a long time, let's put it that way. But if you go directly to the manager, I think in the current environment a proper fund will be transparent and know that they have to provide the data.

Sven Bouman

Which aspects of costs are the most critical in your experience?

Thomas Heidstra: Sometimes you find that the smaller costs may get charged to the fund. For example, legal fees typically can get charged to the fund, but not always. There is also a whole debate about things like research fees, trading costs, or soft dollars. So we are typically talking about the lower dollar costs, but they add up.

I think a couple years ago managers thought that it was enough to disclose the audit fees, administration costs, management and performance fees, and that should be it. But today's standard is to be transparent and provide all costs, and add them all up. And if you want to go further, you can also look at slippage costs and impact costs, but that may be a step too far for us.

Sven Bouman

It's also difficult to make an apples to apples comparison on those aspects.

Thomas Heidstra

I agree, you have to stop somewhere and draw alignments. You have to do what is sensible.

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