



Opalesque Round Table Series '09 SINGAPORE

Introduction

Dear Reader,

After publishing our phenomenal Opalesque Zurich Roundtable with Alexander Ineichen and many other leading Swiss alternatives leaders in March 2009 (which can be accessed in our Roundtable Archive on the website), we are proud to present the 2009 Opalesque Singapore Roundtable. The 2009 Singapore Roundtable took place on April 2nd at the local office of Customhouse Group, who also sponsored the event. I also want to thank Peter Douglas for helping me to put the following group together:

1. Zack Kembar, COO, [Capstone Investment Advisors \(Singapore\)](#)
2. Christian Stauffer, Portfolio Manager, [LH Asian Trade Finance Fund](#)
3. Daren Riley, Co-Founder, [Riley Paterson Investment Management](#)
4. Daryl Ee, Director for Alternative Investments, [BNP Paribas Asset Management Singapore](#)
5. Peter Douglas, Principal, [GFIA](#)
6. Han Seng Low, Investment Management Division, [United Overseas Bank Limited](#)
7. Dermot Butler, Chairman of [Custom House Global Fund Services](#)
8. Han Ming Ho, Partner, [Clifford Chance](#)
9. Prof. Melvyn Teo, Centre Director for [BNP Paribas HF Centre at Singapore Management University](#)

After the recent meltdown, Asia based consultants and investors are now observing a new wave of startups - and they point out that this is exactly what happened post the last Asian crisis. A lot of the great names of the Asian hedge fund industry were actually set up around the end of the Asian crisis. They were very small for a number of years, before they finally attracted attention and started to gain critical mass. Funds like Artradis in Singapore, or LIM or ADM in Hong Kong - a lot of what are now the biggest established managers actually started as small boutiques post the Asian crisis, and ran very small amounts of money for quite long periods.

- What is the opportunity set the [new Asian start-up managers](#) are targeting? What is their typical profile?
- How has Singapore as an investment management center evolved over the last year? Did you know that the most recent regulatory initiatives aim to establish [Singapore as a fund domicile](#)?
- Why should you "hire your risk manager from Singapore, and your trader from Hong Kong", as the saying goes? What are the underlying reasons for such [cultural differences](#)?
- Read how hedge fund managers explain the dynamics of the [natural healing process](#) which occurs in Asia when the marginal investor, the foreigner, has gone - and how to profit from it.
- The consensus is that the Asian hedge fund industry is going to produce good performance numbers mid-term - [who are the investors](#) who participate in the upswing?
- What is the margin by which Asian focused hedge funds with head or research offices in their investment regions have [outperformed](#) their counterparts managed from the U.S. or U.K. - and why?
- and much more... 29 pages full of real intelligence!

Enjoy "listening in" to the 2009 Opalesque Singapore Roundtable!

Matthias Knab
Director Opalesque Ltd.
Knab@opalesque.com

Cover Photo: Central district of Singapore

Participant Profiles



Standing (left to right)

Matthias Knab, Han Seng Low, Prof. Melvyn Teo, Dermot Butler, Christian Stauffer, Zack Kembar

Seated (left to right)

Daryl Ee, Daren Riley, Peter Douglas, Han Ming Ho

Introduction

Dermot Butler

Custom House Global Fund Services
Ltd.

My name is Dermot Butler. I am the Chairman of Custom House Global Fund Services Ltd., which is a group of administration companies based in Malta, Dublin, Luxembourg, Chicago, Netherlands, and of course we have a very active office here in Singapore with 65 people. We currently administer about 500 funds and sub-funds, over 20% of those are daily dealing NAVs.

Zack Kembar

Capstone Investment Advisors
(Singapore)

Zack Kembar, I am the COO of Capstone Investment Advisors (Singapore). We are a small investment manager within a larger global infrastructure.

Capstone has about 110 employees globally in New York, London and Singapore. We opened our Singapore office in January and officially launched our Asian funds in March. As a general matter, Capstone's strategy is relative value volatility trading across asset classes. In Singapore, our main fund trades equity, fixed income, foreign exchange, and commodity volatility and we are initially focused on the equity and foreign exchange markets. We have approximately 10 employees here and enjoy the support of our larger US platform.

Christian Stauffer

LH Asian Trade Finance Fund

My name is Christian Stauffer. I am the principal manager of the LH Asian Trade Finance Fund. This is a trade finance fund managed out of Singapore focusing on the Asian region and on short term secured raw material, commodities, and manufacturing trade finance transactions. Our assets are essentially short term revolving trade finance facilities (debt) extended to regional producers and traders, or raw material and manufacturing. We are 12 people here in Singapore looking after the funds. We have been in operation for almost five years now. The Fund was created in September 2006 and performance was up 6% in 2008, after being up 8% in 2007.

Han Ming Ho

Clifford Chance Law Firm

I am Han Ming Ho from the law firm Clifford Chance. I head up the funds practice group in Singapore, which is part of a larger Asia-wide funds practice group. We advise alternative investment fund managers on fund formation as well as regulatory issues. Our clients include hedge funds, as well as private equity, close-ended fund managers. The team in Singapore consists of five, including myself. The Singapore office as a whole has about 50 fee earners including partners. I am also the Deputy Chairman of AIMA Singapore National Group.

Daren Riley

Riley Paterson Asian Opportunities
Fund

My name is Daren Riley. I run the portfolio management of the Riley Paterson Asian Opportunities Fund together with Stewart Paterson. We established the fund in June 2007 and are based in Singapore. The fund was up 20% in 2008, with a volatility substantially below the markets and our peer group. We deploy a macro investment process and express our views purely in non-Japan Asian equities. We are opportunistic; we set our bias given the position in the economic cycle.

We aim to exploit the re-ratings and de-ratings of Asian equities through a cycle. We are very nimble. In 2009, our assets are up almost 100% year to date, from a low base. The capacity is calculated based on liquidity, we are always able to liquidate the fund within three days.

We selected Singapore as our destination after a lot of looking throughout the globe. Stewart and I moved from Hong Kong specifically to be here, after having lived for a decade in Hong Kong. We find the infrastructure great and are very privileged to be here.

Prof. Melvyn Teo
Singapore Management University

My name is Melvyn Teo; I am an associate professor of finance at SMU, the Singapore Management University. I am also a Director at the BNP Paribas Hedge Fund Center at SMU. This center essentially does research on hedge funds. We also organize seminars, conferences, and education programs on hedge funds.

My research, naturally, centers around funds. Examples of my research include looking at informational asymmetries - whether there are any advantages to being located close to one's investments for hedge funds, investigating capacity constraints for hedge funds, and analyzing the reasons for those capacity constraints.

Han Seng Low
United Overseas Bank Group

I am Han Seng from the United Overseas Bank Group. We are a leading Asian financial institution with on-the-ground presence all over Asia, and domestic subsidiaries in China, Indonesia, Thailand, and Malaysia. I help to look after the banks proprietary investments in equity and equity-related instruments - private equity funds and hedge funds. We started investing in alternatives relatively early - our first private equity fund in 1988 and our first hedge fund in 2002.

However, those investments are still a relatively small part of our portfolio. The idea for private equity is to seek a higher return by taking a little bit more liquidity risk, and for hedge funds, to try and mitigate some of the volatility in the market. Generally we are long across our entire balance sheet, so the idea is to try to make some money when the markets don't go up... We are generally quite conservative in our investment approach.

As I mentioned we started to invest in hedge funds in 2002, and we are expanding these investments now. It is still a small portfolio, about \$150m in about ten funds. Being conservative, we started investing in strategies that we understand well - equity long-short, strategies with no leverage, and with managers that we know well.

Over the last couple of years, we have been looking to expand our exposure into Asia and also globally. Unfortunately, the prevailing environment made it difficult for us to invest aggressively with confidence. Particularly here in Asia, we have had some difficulties in finding managers that can give us enough confidence that they would be able to perform in adverse market conditions, given that Asian markets have been up generally since 2003 until quite recently.

However, we are excited with the current environment, because we can actually have a chance to find managers that have a track record through a full cycle. We anticipate that we will quite significantly increase our allocations to hedge funds.

Daryl Ee
BNP Paribas Asset Management
Singapore

My name is Daryl Ee, I am a Director for Alternative Investments at BNP Paribas Asset Management Singapore. In this role, I represent Fauchier Partners, which is the fund of hedge funds capability of the BNP Group.

Fauchier Partners was founded in 1995 and has a 14 year track record of strong, stable, and uncorrelated returns. Total AUM today stands at about \$5.5 billion. Our principal office is in London with subsidiary offices in New York (for research), and Guernsey. We focus mainly on institutional investors.

In the early days, our first clients were the UK universities and charities, and this has helped shape our conservative approach to managing money. In addition, we focus a lot on capital preservation and protecting the reputation of the gatekeepers and the people who entrust their assets with us.

Peter Douglas
GFIA

Peter Douglas, I am the Principal of GFIA. GFIA started just over ten years ago. We are a research firm and conduct research on managers and their funds. We cover exclusively skill-based managers: in effect, any boutique who is looking for alpha from public markets - mainly hedge funds and long-only, unconstrained managers.

Geographically, we started looking at broad Asia in 1998, including Japan, China, India, and Australia. In 2004 we added Latin American strategies, and in 2006 we added the frontier markets of Eastern Europe, Middle East, and Africa. We sell our services both as a consultant, where we are like a gatekeeper/advisor to professional investors that have an interest in our universe, or want outsourced due diligence, and we also offer discretionary management. We advise the Wittenham Group of fund of funds, which includes an Asian fund of funds which has just reached its third birthday.

According to Bloomberg, this fund is the second best performing Asian fund of funds over those three years, which is fine. However I am more proud of the fact that we have a correlation of 0.6 to Asian fund of funds and 0.4 with to Asian equity. That means the fund not only performed, which is good, but importantly, the vehicle has been a great diversifier as well.

I also represent the Asia-Pacific region on the Council of the Alternative Investment Management Association (AIMA), and I am a Director of the Chartered Alternative Investment Analyst (CAIA) Association.

Taking up Han Seng's lead, he is excited about investing in hedge funds now, or about selecting hedge fund now. What are the specific opportunities currently in the hedge fund space or in some select strategies?

Daren Riley

Let me start with an important observation that for an investor, hedge funds are a broad and deep menu, and investors and potential investors need to understand what they invest in, and also the managers need to make sure that the investors understand them, that is important.

If you look at the Asian investment industry, it is paramount that you understand the volatility within cycles. You are acting in a very volatile environment, which is a tremendous wealth provider and wealth taker in bull and bear markets. The markets are incredibly volatile, but volatility presents opportunities.

Along with that, one of the disappointments over the last 18 months was that the correlations between asset classes have moved towards the factor one, at least people are arguing or expressing such an assessment. So truly, the ability to diversify, or the effect of diversifying wasn't what one would have hoped. Going forward, we hope that these correlations would start to diverge and that the prospects for diversification will improve again.

The reality of Asian equities is that they become very liquid and very illiquid quickly, and they tend to re-rate and de-rate between 3 and 1 times book with fairly regular rapidity. Therefore, the structure that you can choose as an equity hedge fund manager allows you the benefit of delivering asymmetric correlations. Investors say they want uncorrelated returns, however many wish to have uncorrelated returns in a bear market but more correlated returns in a Bull market.

The trick is understanding what they really want to achieve. Are you part of a large portfolio, or are you running a lot of their money independently for a lot of time?

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The trick is understanding what they really want to achieve. Are you part of a large portfolio, or are you running a lot of their money independently for a lot of time?

Commenting on the outlook for the region, I think that we are witnessing a very large improvement in financial liquidity. One of the great negatives of Asian equities in downturns is the deterioration of liquidity. As volatility rises, the liquidity can deteriorate. Often the hedge fund exposures fall as volatility rises, and rise when the trend is in the opposite direction.

In my view, volatility may go down over the coming 12 months, and probably that means higher exposures, which can lead to more market liquidity. Add to that the improvement in financial liquidity and you have a powerful environment for equities, particularly mid cap. Therefore, I would expect the markets to offer greater opportunities. If you include a value perspective, the markets are reasonably well placed at this moment.

Summing up, I believe that Asia is in a good position to do well, and I still believe that a

macroeconomic guided strategy is vitally important because we are valued and perform within a high-risk asset class. A high-risk asset class is often judged by the weakest link or the lowest common denominator, here that may well be Eastern Europe or a any other event, who knows what it might be.

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This means we have to be alert to other risky assets. One of the challenges for Asian equities for the next 12 months is an investor in America or in Europe can also take a risky bet at home, if he wants to. But apart from that, it is very clear that for instance Asian corporate bond returns are improving quite a lot beyond equities so far this year, and the pricing out of those arbitrages will probably take place prior to the equity part.

Zack Kembar

I agree with Daren with respect to volatility. We have come from a long period where volatility was low and money was cheap and people enjoyed high levels of leverage. In the last year, we have seen volatility explode with an accompanying contraction of liquidity and people dialing down their risk tolerance.

As volatility traders, we want to see market movement and pricing disparities, where we can buy options we feel are cheap and sell options that are overvalued.

For example, we might look at Korea vs. Japan, or perhaps the Aussie dollar vs the yen. The asset doesn't matter as much as how the asset moves in relation to another asset where there has been an interesting correlation. Our strategy has relative value as its essence. Going back to what Daren said before about correlation, everyone wants non-correlated returns when the market is going down, but when you have a relative value volatility portfolio, it doesn't automatically follow that you always perform great when the market is tanking and volatility is going up unless you are leaning long across your spectrum of assets.

I think that over the past year, the world has gone from a very high-risk taking, OTC and complex derivatives world to the opposite extreme. People seem focused much more on listed markets now. Transparency is at a premium for people -- they are asking questions such as what's the overall exposure, can I see it on the screen, who's the administrator, who's the legal, and how is the infrastructure maximized to secure and protect the business. I don't think that two or three years ago people were asking those types of questions.

I think this move to a more transparent and lower-risk environment actually suits strategies like ours because we want to trade primarily in listed or listed look-alike instruments. Historically, the people that traded volatility were bank prop desks and volatility desks within multi-strategy hedge funds. With the landscape now changing, I think that the opportunities for us have grown.

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We see spreads remaining wide, with volatility at quite elevated levels. We agree that long-term volatility is probably going to come down to some lower level, but right now, we are in no-man's land. We have come from a level of extreme volatility; now we are somewhere in the middle. I think the middle is interesting and allows us to capitalize on relative value and a more "listed" and transparent framework.

For the first time for probably the last 15-20 years, the true disappearance of liquidity is starting to create considerable opportunities for trade finance related strategies. Historically, banks provide probably around 85% of the entire money used in trade finance, and the remaining 15% are equally divided between funds, insurance companies and private investor equity.

For the first time, we have seen a true contraction and disappearance of that banking liquidity in the trade finance market. Even if you look back at the Asian crisis, sure there was suspension of the liquidity, but within a reasonable period of time the banking liquidity was mostly restored. This recovery is not so obvious this time.

Christian Stauffer



Christian Stauffer

Our fund is a bit different, because we are not operating in an organized market (stock exchange, OTC) like Daren or Zack. We are involved in trade finance, which is more tied to the real economy; short term secured financing flow of physical goods going from point A to B in the most simple manner.

But also here, the opportunities are increasing. For the first time for probably the last 15-20 years, the true disappearance of liquidity is starting to create considerable opportunities for trade finance related strategies. Historically, banks provide probably around 85% of the entire money used in trade finance, and the remaining 15% are equally divided between funds, insurance companies and private investor equity.

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For example, if the coal price went from 160 to 75 and at the same time if you lost 50% of your trade finance availability, you can still maintain volumes. Moreover, you are probably in a scenario where the volume has gone down as well. The challenge in the near future will most likely be that the price of goods will rise faster than the pace at which true liquidity will come back.

Therefore, we are anticipating the net effect to be in the market in the near future. It's difficult to say if it will be in 6 months, 9 months or 12 months, I don't have that crystal ball. But we are convinced this will create even more opportunities for funds like us, as long as you are not trying to control large market shares of the business. We are voluntarily refraining from being a market share player in order to keep the business liquidity available for our investments.

The challenge for such strategies are the current cash returns. In a strategy like trade finance, any single dollar which is not invested is a zero cash return. The ability of the manager to have

visibility on sustained capital together with the investment opportunities will determine a manager's optimization of the performance.

We are pretty upbeat, having already delivered 6% last year and 8% the year before with no negative month and a very low volatility. The strategy is uncorrelated to the other markets and class of assets and the driver of the performance is mostly a lot of work from the team.

Daren made a very good point before saying it is vital for an investor that he, and the manager, need to know what each other wants and can do. If a manager does not have the support in terms of sustainability of the capital, it becomes difficult to do a good job to optimize the performance and the investments.

Dermot Butler

I agree about the cash question. I think it was Warren Buffett who said that, "Saving cash is like saving sex for your old age." What a lot of people tend to forget is that hedge funds on the whole weren't that risky - it was the long-only's that were risky. They were the ones who got carved up 50%.

The majority of hedge funds did reasonably well, of course excluding those that were the wrong way around in sub-prime or got credit wrong because they had no idea what their OTC derivatives consisted of - both of which applied to the banks and other investors as well. I would say that even last year, hedge funds - long-short structures or arbitrage etc. - which historically had created alpha and maintained capital, as a group, certainly achieved 15 to 25% alpha last year, except for those that masqueraded as long-only funds.

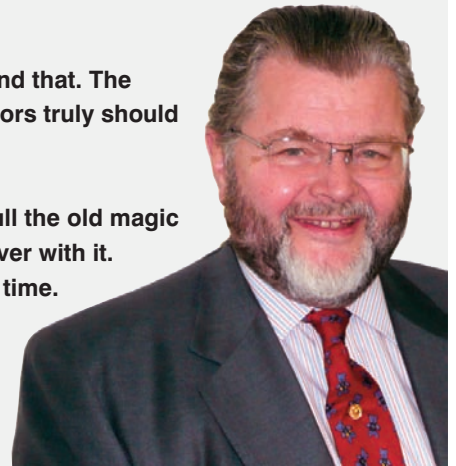
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They lost money and that upset an awful lot of investors, but there are factors behind that. The whole banking and liquidity crisis and the devastating consequences, which investors truly should try to understand.

I don't think you can blame the hedge funds for the fact that the banks suddenly pull the old magic trick of taking the tablecloth away, but this time they even took all the china and silver with it. So there was no money left at all, and overnight everything went down at the same time. Panic selling ensued and that's why a lot of hedge funds that may have been very well structured lost money last year, but they only lost 15% or 20% as opposed to 40% or 50%.

Dermot Butler



They lost money and that upset an awful lot of investors, but there are factors behind that. The whole banking and liquidity crisis and the devastating consequences, which investors truly should try to understand. When Alfred Winslow Jones started this whole game in 1948, or whenever it was; he went long and he went short. He reduced the profitability by doing that, but he reduced the risk by probably a greater percentage than profitability. It does, of course, rely on good analysis, and assuming the analysis was good, the only way to make it really profitable, again, was to leverage it. Leverage has been a core component of all hedge funds ever since.

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I had a conversation, (to be fair it was by proxy somebody else had the conversation and they told me), with one of the leading pension fund consultants, asking what their reaction was to hedge funds in 2009. The consultant said pension funds that invested in hedge funds took some time to think over Christmas, and realized the scenario that I just told you. They were upset they had lost money, but it was not really the good hedge fund managers' fault. They had actually only lost half of what they might have lost if they stayed long in equities – which meant positive Alpha..

So you had investors and consultants who still felt reasonably bullish about hedge funds, but ironically, they had to liquidate positions, due to the relative outperformance of the hedge fund component, the portfolio composition has changed and they needed to scale back the hedge fund proportion to the old levels. That was unfortunate; but in time they should be able to rewrite their mandates.

Actually those investors who weren't invested in hedge funds are looking at the events quite positively and expect to come into hedge funds, as Han Seng expressed it here, around the third quarter.

Daryl Ee

Given the negative performance of hedge funds last year, I think there's a bit of apprehension right now amongst Asian investors. The hedge fund industry also has to contend with negative press associated with the Madoff scandal. Some Asian investors had allocations to Madoff. For example, a few big institutional investors in Korea were mentioned in the mainstream press as being investors in Madoff-related feeder funds.

The media has made a lot of noise about massive redemptions faced by the hedge fund industry. However, not much coverage has been on the technical angle to some of these redemptions. For instance, some structured products had to systematically sell-down their underlying hedge funds as these structures were being unwound. Also, we've heard that there were some institutional investors who had to redeem from their hedge fund holdings to fund capital calls from their private equity investments. Fund-of-hedge-funds also had to trim their underlying hedge funds to fund currency hedging losses for non-USD denominated share-classes. So the bottom-line here is that there were other technical factors at play behind industry redemptions and not just disgruntled end investors per se selling down their hedge fund holdings at their own volition.

Daryl Ee



Overall, I believe there will be a period where hedge funds have to rebuild trust and show that they are able to once again generate uncorrelated returns. In addition, a lot more education and communication is needed. Collectively or individually, hedge funds have to play a larger role in educating investors, to shed more light on the realities and technicalities of hedge fund investing.

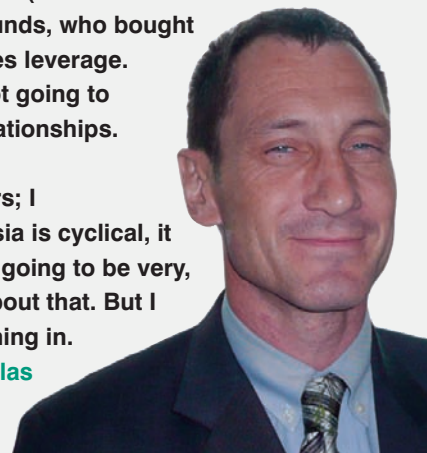
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For people following these discussions from outside Asia, may I underline that the Asian investor base is not particularly “hedge fund sophisticated”. There are some very large institutions in Asia, and there are some very high caliber people, and financially aware experts around. But generally speaking, when you sell a hedge fund product into Asia, you are selling to people that are not intuitively, instinctively comfortable with hedge funds. If you talk to an U.S. endowment, they have 15 to 20 years of experience allocating to hedge funds; in Asia, that history is not there.

Large chunk of Asian demand for alternatives came through private banks. The private bank risk manager looked at the recent performance of hedge fund aggregates which, up to 2008, had a very low volatility and therefore looked like a ‘safe’ asset. So the credit committees signed off on applying leverage to private clients’ hedge fund portfolios. As a result, the industry ended up with a group of sophisticated and professional investors (hence unprotected by distribution regulations), who still did not really understand hedge funds, who bought portfolios of hedge funds, typically through fund of funds, with three times, four times leverage. And clearly that was a recipe for all sorts of unhappiness last year. That money is not going to come back quickly, and to be honest, probably neither are those private banking relationships.

The Asian hedge fund industry is going to produce some great performance numbers; I completely buy the argument that there are massive inefficiencies at the moment. Asia is cyclical, it is volatile, and if you are prepared to commit to Asian hedge funds right now, you're going to be very, very well compensated over the next two to five years. I have absolutely no doubt about that. But I don't think Asians are going to play in that party - it is going to be global money coming in.

Peter Douglas



Peter Douglas

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The capital in Asia has not been institutionalized for very long. It can be misleading - when hedge fund marketers or managers fly in from London or New York or Connecticut, they will be talking to clearly high caliber people who are internationally educated, but they haven't internalized the hedge fund industry, because they haven't been there long enough to experience the longer-term track record, and operational characteristics, of hedge funds

I agree with Dermot that last year the hedge fund industry actually delivered superbly for its investor base, but here you had more of a universe of investors who had mentally penciled in the concept that hedge funds were the part of their portfolio which was never going to go down. And also, because they never had to go through the details, the small print, they also had also assumed that this was the part of the portfolio where they could always get their money back each and every month if they wanted it.

The other big (probably larger) bulk of assets in Asia came in to hedge funds through the private banking industry. One of the big changes over the last ten years between the last crisis and here and now, has been the growth of the Asian private banking industry.

So, in the ten years since the Asian crisis, we have had a huge growth and very aggressive penetration of private banks; in particular those based here in Singapore, which has become a major wealth management center. The default model for a private bank trying to gain market share rapidly is to be more clever, more aggressive, offer better products, and over recent years it also has been by offering more leverage to its clients.

As a consequence, a large chunk of Asian demand for alternatives came through private banks. The private bank risk manager looked at the recent performance of hedge fund aggregates which, up to 2008, had a very low volatility and therefore looked like a 'safe' asset. So the credit committees signed off on applying leverage to private clients' hedge fund portfolios. As a result, the industry ended up with a group of sophisticated and professional investors (hence unprotected by distribution regulations), who still did not really understand hedge funds, who bought portfolios of hedge funds, typically through fund of funds, with three times, four times leverage. And clearly that was a recipe for all sorts of unhappiness last year. That money is not going to come back quickly, and to be honest, probably neither are those private banking relationships.

So the perception that Asian investors have of hedge funds is noticeably more tainted than the impression I get from talking to comparable investor bases in the US and to a lesser extent in Europe.

In my view, the Asian hedge fund industry is going to produce some great performance numbers; I completely buy the argument that there are massive inefficiencies at the moment. Asia is cyclical, it is volatile, and if you are prepared to commit to Asian hedge funds right now, you're going to be very, very well compensated over the next two to five years. I have absolutely no doubt about that. But I don't think Asians are going to play in that party - it is going to be global money coming in.

Daren Riley

Asia plays its part by stopping buying, and because the consumer stops buying, the current accounts will turn positive. Therefore, you will start seeing an improvement of financial liquidity. I am not referring to leverage - I mean, things are terrible - but actually the liquidity starts to improve. That's what improves the market, but it is not the hedge fund investor - that is how I would look at it.

And then the foreigner comes in noticing that the current account is actually strong. There is a net buyer of the currency, and that in itself their dollar can then create more liquidity, and subsequently it takes off.

I am not disagreeing in any way with what Peter says, but there is a natural healing process in

Asia plays its part by stopping buying, and because the consumer stops buying, the current accounts will turn positive. Therefore, you will start seeing an improvement of financial liquidity. I am not referring to leverage - I mean, things are terrible - but actually the liquidity starts to improve. That's what improves the market, but it is not the hedge fund investor - that is how I would look at it.

And then the foreigner comes in noticing that the current account is actually strong. There is a net buyer of the currency, and that in itself their dollar can then create more liquidity, and subsequently it takes off.

I am not disagreeing in any way with what Peter says, but there is a natural healing process in Asia when the marginal investor, the foreigner, has gone.

Daren Riley



Asia when the marginal investor, the foreigner, has gone. This sequence of events is what we are seeing. The real economy, the demand for goods slow, then the current account moves positive despite falling exports, which is terrible for domestic earnings, but that then allows the foreign investor to come in and buy an intrinsic value or yield. Foreign money flows therefore strengthen that currency, and then the Central bank decides whether the currency will be allowed to firm, or they will allow money supply to expand. This is the healing process which we are starting to see.

Prof. Melvyn Teo

Recently, a lot of the focus has been on liquidity, and I like to make a distinction between certain kinds of liquidity. Traditionally, we are dealing with market liquidity, which means the ease of buying a stock without generating a big price impact. But the liquidity issue we are seeing now is driven also by funding liquidity, and that is where all the commonality comes in.

When you have a big event like the subprime crisis, market liquidity goes down, and when you try to buy a stock, price impact goes up. At the same time because your returns have been falling, investment banks try to clamp down on leverage ratios, margin calls are coming in, investors pull out money, then you have a funding liquidity problem. Both these effects feed on each other and I think the funding liquidity effect has been driving a lot of hedge fund problems last year.

On top of that, given the amount of money that has been flowing to the hedge fund industry over the last 4-5 years, I think a lot of funds have been getting into a very crowded space. I'm not sure about Asia, but at least in the U.S., convertible arbitrage funds have been facing these problems.

Arbitrage spreads have also come down because of the crowding. Hence leverage has to be increased to maintain the same return. When you have a funding liquidity situation, this compounds everything and a lot of funds just lose money in these firesale situations.

Obviously, now there is big aversion to illiquidity; people are averse to buying illiquid stocks, averse to buying illiquid bonds. Obviously, the reward for investing in these securities will go up, and as we mentioned, emerging market securities are typically very illiquid. If people are averse to illiquidity, risk premiums for emerging markets stocks should improve over the next couple of years.

That's a good point on liquidity. I would like to finesse it slightly.

Peter Douglas

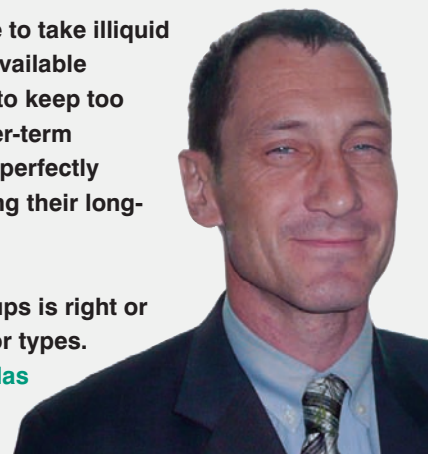
Anybody with enough wrinkles understands that market liquidity in Asia is always provisional, and Daren's comments are absolutely right. If you are trying to run a billion dollars of long-short equity in Asia, you are sailing into very stiff headwinds, even at the best times, in my opinion. But that's not a new story if you understand Asia.

What we learned last year, which was generally not appreciated enough, was that it wasn't appropriate to commingle investors with different liquidity demands. There were investors who actually wanted to take that illiquidity premium, mixing with investors that had a need for liquidity, and that created all sorts of problems.

The larger, long-term investors saw an environment where it was perfectly legitimate to take illiquid positions as liquidity providers; they in fact expected their managers to exploit the available opportunities - so these investors became genuinely upset that their managers had to keep too much cash, or liquidate positions, to fund shorter-term investors. Conversely, shorter-term investors like intermediaries, funds of funds, or some of the family offices, who had perfectly legitimate needs for liquidity, were upset that managers were, in their eyes, protecting their long-term investors at their expense.

I am not taking any sides here, I am not saying that either one of those investor groups is right or wrong, but I would hope that the industry learned last year not to commingle investor types.

Peter Douglas



But on the investor side, we're seeing a clear dispersion of liquidity appetite. One of the key learnings from last year relates to the very different characteristics of investor liquidity.

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I am not taking any sides here, I am not saying that either one of those investor groups is right or wrong, but I would hope that the industry learned last year not to commingle investor types. Either you are running money for long-term investors, or you are running money for short-term investors. If you mix the two, sooner or later it is going to go pear-shaped.

Daren Riley

One way to manage this going forward would be for certain strategies to issue different fund tranches with different liquidity, as one way to differentiate and segment the client base in order to better match the liquidity profiles.

Han Ming Ho

Regarding liquidity issues, I think quite a lot has been discussed by Peter and Daren in the resulting restructuring at the fund level. Separately, I've also seen some "movement" and restructuring in the relationships that managers have with service providers notably with prime brokers and custodians in the context of counterparty risks.

Separately and standing at the other end of the table, from an investor standpoint, we see a significant development recently from the big heavyweights. The 800-pound gorilla is in the form of Calpers or the endowments, who have started to review the relationships they have had over the long-term with their existing hedge fund partners.

I have seen a memo from Calpers that talks about revisiting hedge fund fee structures, as well as looking deeply into the corporate governance issues at the fund. One query is whether the structures that we often take for granted, the fee structures, will the 2 and 20 model hold? Should performance fees crystallise over 12 months instead of over a longer term?

So quite apart from liquidity of assets, the question and maybe pressure from investors today is whether the old world that we understand and are familiar with will and should continue to exist. It's something that we are keeping an eye on.

One fund of funds has actually raised its hand and said "we are not going to adopt line by line with what Calpers is asking, because we are not Calpers but we are definitely going to take some ideas off that memo".

So it's definitely something that we are keeping an eye on and which makes some Asian based hedge fund managers who take US tax exempt monies quite worried.

Christian Stauffer

I think there are two things that we will probably change. There must be a clear understanding, probably much deeper than what it was lately, between the investor and the manager.

First, it's documented, but there must be a true understanding of the investor about what the manager is doing. And then also from the manager to fulfill, obviously, what he has to fulfill under his mandate. The second thing is what Daren was saying about how much money you run for whom. I think that's probably what was a big problem last year at some point. The manager needs to have consistency in his investor base, and the least possible mismatch. It is also prudent to think that it should not be running a too large allocation, neither should he represent himself a too large investment for the investor.

Han Seng Low

We have been undergoing a fairly intensive exercise over the last 3-6 months reviewing managers and looking for people who have proven to be able to deliver good performance over a full cycle. We expect to be deploying funds to two managers over the new three to six months.

We are not capital constrained in any way, and we think that this is a very good opportunity for us. Let me add here that we have looked at managers globally but have decided to focus our

investments on managers running Asian strategies. This is a result of both resources limitations and us being able to better understand the strategies and the risk being taken by the managers here.

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In the current environment, I can get meeting time with managers who in the past could not or would not give me time of day. There was no capacity and they didn't want to talk to you: "How much money do you have? Less than 20 million? Don't bother, I have clients here who have 100 million and I am talking to them...." So forget about it. In addition, you couldn't really get much diligence done as an investor with certain funds. "The DDQ? Forget about DDQ, I will give you one hour. I am telling you how I am doing it, and if you are not smart enough to understand me, keep your money. ..."

Han Seng Low



Our process requires us to spend a lot of time with the manager, understanding the strategies that they execute, and the risk that they take to generate the returns. If we don't understand them, then I rather not invest.

The second issue is that we need to have managers that have a good track record over an up and a down period. For example, although many Asian hedge funds claim to be really good equity long/short shops, we note that it is really very difficult to add a lot of value on the short side in Asia, and in some markets it is actually very difficult to execute these short strategies. Compounding this problem, some managers also tend to go into small-cap and mid-cap on the long side and the reality in Asia is that it is very difficult to hedge the small and the mid-cap. The instruments tend to be only available for large-cap. This is just part of the reality of Asian equities market, so we need to really understand how the managers execute their strategies given these limitations.

I don't have too much of an issue with paying fees as an investor as long as it is within industry norms. We are happy to pay fees for funds that deliver returns, and if they are learning, then they should pay us the fees... We don't like paying the manager's tuition fees, if they are learning then they should pay us instead of us paying them.

I had mentioned that we find the environment is very interesting now to increase our allocation to hedge funds. I agree with Peter and also Daren that now is probably a good time to be allocating money in to Asia, but I am not only referring to the investment attractiveness or a timing of the market. What is more important for me is that now, as a hedge fund investor, my ability to get comfortable with a fund and a manager has improved significantly.

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So that is part of the past, at least now you can talk to managers, they have a proven track record that allows you to see who really understood the markets. You can now examine the connection between the opportunity set and their strategy and the risks being taken, how they had generated value. On top of that, you have time to talk to the managers, develop a relationship - and also there is capacity in the fund.

Melvyn, you mentioned before your research on information asymmetries and the advantages of proximity to the markets, can you share with us your findings?

Prof Melvyn Teo

We simply looked at whether managers had head or research offices in their investment regions. This study was done on Asia, so the various regions are Asia ex-Japan, Asia including Japan, etc.

Basically you have groups: managers who are invest in Asia from the U.S. or U.K., versus funds who do the same but with Singapore, Hong Kong, Tokyo or Sydney as a base. We looked at who was outperforming whom, and what were the reasons behind this.

It turns out that for a hedge fund manager, there is a distinct informational advantage to being located near the investment markets or having a research office there. The spread historically is about 3.7% risk adjusted, but it is coming down a little bit.

Of course, people are asking me “why doesn’t it just go away, why don’t all the foreign hedge fund managers investing in Asia, set up shop here and arbitrage away this informational advantage?”

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Prof Melvyn Teo



I think the reason is the hedge funds want to be close to their investors. As the bulk of the hedge fund investors are in the U.S. or in Europe, a manager may opt to stay close to his investors and maintain a good a relationship. They may still be reluctant to set up a significant operation in Singapore or Hong Kong to invest in Asia. They would rather invest from where they are.

We found that this advantage is extremely important in emerging markets for funds investing in small stocks and for funds with illiquid positions. As far as a hedge fund manager is concerned, it helps to be close to his investments. When we examine if proximity has a similar effect for the hedge fund investor, we could not confirm that.

It turns out that hedge fund of fund managers can be based anywhere in the world, and they will do just as well. It seems that a fund of funds manager does not have to monitor his investments that closely - after all he is investing in managers and not directly in securities. If a fund of funds manager travels to Asia for example, to visit managers once a quarter or every six months it seems good enough.

Zack, you represent the fund here in Singapore as an offspring of a larger U.S. fund. Can you tell us a little bit how you came to that decision and how was it for you to set up your firm here?

Zack Kembar

The Asian experience is actually rooted in the CVs of the people in our office here. In my case, I had spent most of the 90s in Japan; in the late 90s I was part of the Goldman Sachs equities division and had the opportunity to visit many clients based in Asia, in addition to those who traded from Europe and USA. Ferrel Daste, our head of marketing, had been managing Capital

Introduction at DB in Asia and was also a GS alumnus that I had worked with in the USA. Both of us had known Paul Britton, the founder of Capstone, for over 8 years. When we talked to Paul about setting something up an office in Asia, he clearly wanted to do this with people that he had close personal relationships. In addition, he wanted the players to have been in the business for a while and have experience on the ground in Asia (versus just hiring some people in NYC to work on an Asia platform).

We hired a team that came from a proprietary division of one of the investment banks in Hong Kong that had extensive Asian experience as well. So even though Capstone is mainly a U.S. operation and originated there, we have many people from all over. The founder, Paul, is from London and grew up as a floor trader on LIFFE and in Amsterdam. I'm Canadian, Ferrell is from the U.S. and our Asian trading team is a mix of North American, Singapore and Chinese members.

In addition, we like the fact that we have a large infrastructure in the U.S that supports us operationally. They help us with trade processing, technology, etc., as we evolve. Our goal is to adopt the Capstone style in the U.S. and modify it in order to best reflect Asia. I think the U.S. markets in equities, for example, is much more of a listed marketplace, where people see active screen prices and enjoy a high level of transparency. The Asia markets tend to be much more mixed. I think there is definitely more of an OTC market in Asia – especially with respect to equity derivatives – and that means less liquidity and more difficult price discovery and there is not a large listed market for single stocks. In Tokyo, for example, the TSE has been talking about improving liquidity for a long time, yet almost everything trades OTC.

I think the crisis and and liquidity contraction has limited the markets and products available. Given the changing environment, I think both banks and hedge funds would like to see listed markets trade more actively in single stock options. Although you have liquidity in the indexes, you don't see this with respect to single stocks, which is important for long/short asset managers who are arguably 80% of the investment community. And with the emergence of new strategies like volatility, I think there will be increasing demand for listed products.

Matthias Knab

Is this demand being answered? What is the Tokyo Stock Exchange or others doing here at the moment?

Zack Kembar

They do actually have listed stock options in Tokyo, they just happen to be extremely illiquid and nobody has really stepped up to make significant markets.

Right now, most of the liquidity in Tokyo and in Hong Kong and Korea in single stocks is happening off exchange. It could be listed lookalikes or a structured product, but most of it is OTC, and the Tokyo authorities are now getting very serious about forming a group of market makers that will create liquidity in single stocks, which I think will be fantastic.

Matthias Knab

Let's look briefly at the evolution of Singapore as a marketplace, as a destination, as a jurisdiction. What are your observations? How is Singapore evolving, what's happening here in respect to the market infrastructure or regulations, and also, how is the investor base evolving?

Peter Douglas

Singapore has evolved very successfully already over the last four or five years. The regulatory environment here is one of the most pragmatic in the world and has created a sensible environment for running hedge funds.

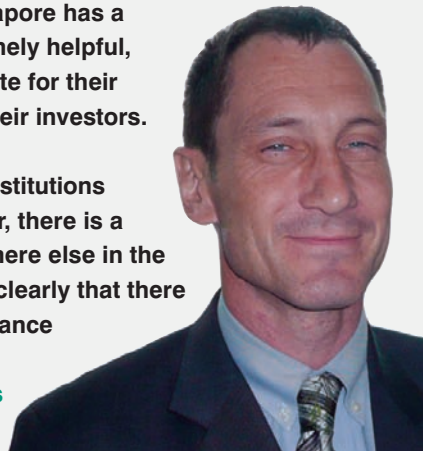
The majority of hedge fund investors are professional allocators who have very sophisticated manager assessment and due diligence processes, and expect nothing from regulators. Singapore has a regime where a manager can elect, if they want to, not to be regulated. This is extremely helpful, because it allows managers to put in place a compliance process which is appropriate for

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However, for those managers that are servicing institutions, perhaps public sector institutions elsewhere, perhaps European institutions that need to deal with a regulated manager, there is a regulatory environment in place here, which is as stringent and demanding as anywhere else in the world. That strikes me as being extremely sensible. Singapore has understood very clearly that there is a bifurcation in the industry's regulatory needs, and it has struck a very healthy balance between facilitating, and regulating, the industry.

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The rest of the infrastructure here is fine. Most hedge funds are principal-directed businesses, and most principals in the hedge fund industry are mid-career professionals with choices, who can decide to live pretty much wherever in the world they want, and Singapore offers a good lifestyle. If you are a global nomad, it's probably the easiest place to bring up a family of anywhere in Asia (unless you happen to speak Japanese, in which case Tokyo would be a close competitor for lifestyle).

I will let the managers talk about the financial infrastructure, because GFIA invests in managers, not markets. Perhaps Han Ming, we might get you to talk a little bit about how you see regulation developing here, as it seems the MAS may be reviewing how they administer the exempt regime. I am not sure that there needs to be a rapid evolution in respect to regulations – I get the impression that most market participants feel that Singapore has pretty much got it right.

Han Ming Ho

Yes, that's right, the regulator here has followed a very sensible approach in recognising and distinguishing the different businesses and requirements of a long only traditional mutual fund manager and that of a hedge fund manager.

If you ask me to gaze into the crystal ball – do I think the MAS will retain what's worked very well here? My guess is yes. I think they have seen the markets respond positively to the local regulatory and tax environment for fund managers. Just by looking at their surveys which they publish every year, the AUM figures are exponentially increasing, for example. I suspect it may have dipped for 2008, but this is due to market reasons that we all are aware of.

Regarding the exempt regime, the MAS is recognizing the evolution of the hedge fund industry here. I think their mandate six, seven years ago was basically to kick start the process, and one of the biggest things that they have done is to create a suitable environment, at least from a

regulatory perspective, to start business.

The second factor which has really helped are the tax exemptions available here. As you are probably familiar with the incentives available, managers here can apply for a concessionary corporate tax rate of 10% subject to MAS approval which is lower than the 17% rate from 2010 year of assessment. Also, if the fund is Shariah compliant, this can go further to 5%, giving managers good reason to raise monies from Shariah investors.

In terms of creating the right regulatory environment, the right tax environment, we can check both boxes affirmatively to the MAS - these two have been delivered. But moving on, with the critical mass of fund managers now active and based in Singapore, many managers are looking to set up their follow-on funds: fund number two or three, or funds adopting different strategies. These managers are interested in establishing the funds themselves in Singapore and one of the reasons being investors recognizing Singapore as a regulated jurisdiction, with good fund managers, good service providers like administrators and law firms which provide the support that an institutional investor is comfortable with.

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However, the problem is that there are not many legal structures available. The positive thing is MAS recognizes this, so they are pushing new legislation forward. There is a new Limited Partnerships Act in place under which a fund can be set up as a limited partnership. This is good for investors who are familiar with LP structures, for example the U.S. taxable investors. I understand that the MAS is also looking at new legislation which provide for the creation of open-ended fund vehicles in addition to the LP structure.

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If you look at the financial industry incentives that were announced in late January by the Finance Minister, the bulk of it is extremely positive for the fund management industry. The dreaded 80-20 rule which became 30-50 last year, has now all gone away with the "enhanced tier scheme". The new budget and the recent announcements have given more clarity and further enhanced the types of investments in which a fund would enjoy tax exempt status related to the income. Generally you can say that the authorities are giving out more incentives to fund managers.

I mentioned that a couple of years back, the MAS's mandate was to generate critical mass and bring the managers to Singapore. I believe their next mandate would be to retain the factors which attract managers and to explore the establishment of Singapore as a fund domicile. This means to

create more synergies within the industry here, which apart from fund managers, also includes the private wealth management industry. Things could fall nicely together, where one plus one ends up much greater than two.

Peter Douglas

Any comments on thematic inspections?

Han Ming Ho

Let me put on my AIMA hat now - the MAS has given us the heads-up that they would be knocking on exempt fund managers' doors to perform scheduled on-site audits. However, the assurance they gave us was that firstly, this is not a witch-hunt. Second, through the survey and visits they hope to understand the lay of the land much better, and thirdly, it's not a knee-jerk reaction to the markets.

I think it will be a sizable task for them to run down the entire fund manager list from A to Z, which is what they said they will do. The sense that I get is that the MAS is not set on course to nit-pick and I believe they really want to understand what the potential risk issues are in some existing operations - if there are any - and they want to identify and hopefully avoid these before any potential blow-up.

There will be issues in the way they carry out and execute this rather big exercise, but they are quite open about the whole process. We are meeting with them separately, where they will be carrying out closed-door discussion with AIMA and hedge fund managers. Here managers can raise questions if they are interested in finding out more about the survey.

Daryl Ee

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Examining events of the recent past, one would remember the wave of short-selling bans in September 2008 which started in the U.S. and U.K. These bans even spread to Asia as regulators attempted to bring order to the markets. During that trying period, Singapore and Hong Kong both resisted implementing any outright bans on short-selling, exemplifying their market-friendly approach to regulation.

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There has been a lot of "competition" between Singapore and Hong Kong in terms of developing their respective financial centers - you can watch a bit of game theory at play here. This is good because this spurs pro-industry developments. I believe in 2002, both jurisdictions allowed retail sales of hedge funds, the first jurisdictions in Asia to explicitly do so.

Dermot Butler

Ireland introduced a retail hedge fund of funds product with a minimum investment of €25,000. I think that was about six or seven years ago, and I am not sure if one single fund has been formed.

We chose Singapore for a number of reasons as an administrator, and we have a different objective to fund managers. Basically, we felt that the government in Singapore was much more proactive. I would not say the government was against us in Hong Kong, just more like indifferent or ambivalent, whereas in Singapore they were definitely proactive.

Singapore at the time was cheaper, which is always useful. I think that educationally the staff we have here are very focused, very disciplined - not particularly entrepreneurial, but I didn't want any entrepreneurs in an administration company any way. I have always felt that the Hong Kong entrepreneur was more interested in Happy Valley and the stock market.

Before coming here, we also looked at Sydney. Sydney is in my view, by far and away the most attractive place to work, but you have to be prepared to pay high taxes and cope with very high living costs. So Singapore won hands down.

From an outsider's point of view, I don't think many people in Europe, which is where I come from, would trust the Hong Kong government - because now it is basically China - as much as they trust the Singapore government. I would say we perceive Singapore to be politically more stable.

We opened here in Singapore in April 2007, and at the beginning of last year I had to go to Hong Kong. That was the first time I really noticed the pollution. With the majority of hedge fund managers being somewhere between 30 and 45 years old, those that are married all have a trophy wife - she may not have been when they first married, but she is now - and she is not going to bring up Justin and Jemima there, when she can't see Kowloon from the Peak - so she demands Connecticut, Fulham Road or Singapore.

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So I think some managers come to Singapore because of the environment, and others may come out of Tokyo, where there has an adverse tax effect on managers. Altogether, Custom House has been very happy here, and even comparing it to the other places we operate from, it is one of the more effective places.

I wanted to address the 2008 events that the industry is still sort of suffering from, particularly the Madoff scandal. Yes, rightfully, everybody is terrified and still nobody knows where all the money went, but it seems that all this could only happen because of a lack of due diligence. Investors got sucked in because "that guy" was invested and "this friend", and people just started to feel comfortable without actually having done any due diligence, which was very bad. But that was their fault, not the fault of the industry.

Also - You cannot stop a dedicated crook. The dedicated crook is not interested in regulations and he does his thing knowing the regulations are there. Sometimes I think they have a death wish, but that is speculation, I am not a psychologist.

Following Madoff, you could see some sensible reactions from the market place, and of course you could say we strongly support the approach of Swiss banks like UBP and Edmond de Rothschild who stated they will not invest in any self-administered funds. Obviously, we are targeting the self-administered funds in the US at the moment. The irony, and all of us need to be aware of that, is that Madoff never had a fund. It wasn't a hedge fund, so it never had an administrator in the first place, but - and this is a big "but" - all those feeder funds had very big administrators.

Daren Riley

Sometimes people asked me why did we move to Singapore? We moved to Singapore in February 2007 after my business partner Jeff and I spent about a decade or so in Hong Kong. For about six

months, we looked around the world and also checked with a number of people from the financial industry, asking for their views and experiences about the best place to locate and how to go moving, setting up etc.

For us, the primary aspects in favor of Singapore was its independence as a city-state in Asia, it was cost competitive, and over the preceding three to four years, there was a big leap forward in terms of the various service provisions in Singapore relative to Hong Kong, whereas historically it had materially lagged Hong Kong. That was changing quite fast, and therefore very positive.

As a comment from the professional world, we have found it difficult to find people who are well qualified and experienced but want to take risk, who are Singaporean. It hasn't been easy either who aren't Singaporeans, but to find those is also there. We would very much like to employ more Singaporeans - not that we are a massive employer, but we are expanding - because it helps with our own stability of our business.

On a personal level, I think there is a big difference between schools in Hong Kong and Singapore. The international schools in Singapore do not take local students, whereas in Hong Kong they do. What that means is that the international schools in Singapore have a more transient population in both the teachers and the students, which undermines the quality and the ability for the institution to develop.

Daren Riley



From a family perspective, the environment was there and the administrative environment as well was very positive. From a macro point of view, obviously China was growing, but so was India as well. My sense is that India has actually helped Singapore become more important than it was before, whereas obviously Hong Kong is vitally important geographically as well.

We love Hong Kong - it is in many ways probably a slightly better shop window, but with regards to Singapore we have enjoyed a good service provision here, at a professional level and personal level.

However, as a comment from the professional world, we have found it difficult to find people who are well qualified and experienced but want to take risk, who are Singaporean. It hasn't been easy either who aren't Singaporeans, but to find those is also there. We would very much like to employ more Singaporeans - not that we are a massive employer, but we are expanding - because it helps with our own stability of our business.

On a personal level, I think there is a big difference between schools in Hong Kong and Singapore. The international schools in Singapore do not take local students, whereas in Hong Kong they do. What that means is that the international schools in Singapore have a more transient population in both the teachers and the students, which undermines the quality and the ability for the institution to develop.

In Hong Kong, local students can attend international schools, which provides a bedrock of a core substance. It also provides a peer group of parents to pressure from the outside to help develop the school itself, and in many ways possibly the better schools in Singapore are local schools, if only they could have the same term times. So there is a difference here in terms of the education, and addressing this could help the educational sector in Singapore to be as good, if not better, than in Hong Kong.

Prof Melvyn Teo

There is a saying, "hire your risk manager from Singapore, hire your trader from Hong Kong" and it turns out that's what one of the largest Singapore based hedge fund does. Probably one of the reasons why people are finding it hard to find traders in Singapore who are Singaporeans, is because Singaporeans have a very high aversion to risk, for some reason. I think it's part of our education.

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Prof Melvyn Teo



Peter Douglas

It could also be a consequence of having spent two years in the Singapore National Service - wearing a uniform and doing for two years exactly what you are told....

Prof Melvyn Teo

To verify this we probably have to study those who went overseas and didn't do national service versus those who did...

There is another saying about the regulatory framework, that it takes six months to set up shop in Japan, one month in Hong Kong, two days in Singapore, which is of course a bit exaggerated.

However, as we mentioned, the friendly regulation and framework has allowed a lot of small funds to start up shop in Singapore. So initially, we were populated by mainly small funds and it was a very diverse group. You have macro funds, you have equity long/short, you have now all sorts of funds here. I believe in Hong Kong you have a much more strategy-specific group, to a large extent, of equity long-short funds focusing on Asia and Greater China.

As a result of the broader diversification, Singapore based funds seem to have weathered the storm better than Hong Kong. If you look at the Eurekahedge database, over the last year, performance has been roughly the same for Hong Kong-based versus Singapore-based funds. But the attrition rate for Singapore based funds is about 13% versus about 22% for Hong Kong. That could mean that there is a lot more strategy risk for Hong Kong based funds than for Singapore based funds.

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Han Ming Ho

Regarding the saying referred to by Melvyn about the set-up periods in the different jurisdictions - I am not sure where that saying comes from, but I think Zack would agree, six months to set up a shop in Japan can be considered short, and to do it in one month in Hong Kong is close to impossible, because you need a license in Hong Kong if you don't qualify for exemptions available there. You need to go through the SFC for the licence and we are really looking at about four months for Hong Kong, which is why a lot of managers come to Singapore, all other factors being the same.

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Zack Kembar

We have just gone through the exempt manager application process. I think "exempt" can be a bit of a misnomer. While on the one hand, you certainly don't have this intense regulatory scrutiny as you would have in the U.S. or somewhere else as a regulated manager, you do have to fill in a lot of paperwork, provide a lot of information. We also had one-on-one personal meetings with the MAS and talked to them about our business. We can confirm Dermot's experience that the MAS people we met were very friendly and motivated to help us. We felt like we were in a partnership with them. That was really interesting, because with just nine people at the moment, we are a small firm, but still they really wanted to help us in anyway they could.

But still, the process itself took probably a couple of months, because you have to assemble a lot of information, you have to get your office ready, put a business plan together and give the authorities a sort of a map of what you intend to do. I see it rather as light regulation rather than no regulation, and I would believe that a lot of people misunderstand that.

Let me also share some background why we had chosen to set up an office here. Our senior people had come from Tokyo, Hong Kong, and Singapore. I had been in Tokyo, and from a cultural and life-style perspective, I think Tokyo is probably the most livable city in Asia; there you have four seasons, a really interesting culture, a fascinating city and all sorts of things to do.

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I think the problem with Tokyo is that you seem to have a very capricious and random regulatory environment that is hard to understand – it seems to come from all corners and can be very Draconian. You also have a very big cultural difference, which we didn't feel here. In addition, the tax regime is very high. Finally, in Tokyo, if you are not a native speaker, it's very difficult to get around and that can be tough for families. The schools I think are a challenge.

With respect to Singapore vs Hong Kong, Singapore has clean air, an interesting mix of a colonial culture with a Malaysian and Chinese culture, and is a real melting pot. It is right in the center of Asia, which also makes travel easy. Combine that with the regulatory environment and the fact that you have a large peer group of people from all over the world here that are involved in asset management, administration, banking, legal, and so on. Singapore has a deep pool of people and talents. Singapore took people from Hong Kong, but also took everybody from Tokyo.

Last year on Bloomberg, a fund manager said "will the last person to leave Tokyo please turn off the lights?" I don't mean to be knocking Japan – I love Tokyo, I lived there for nine years – but they have made it difficult. This is a hard enough business, and when you throw in the taxes and everything else, it's a very easy decision to come to Singapore.

Peter Douglas

We can identify at least 25 Japanese hedge funds run from Singapore, and the oldest hedge fund in Singapore is in fact a Japanese hedge fund.

Melvin, very interesting your comments about attrition.

We are always being asked about hedge fund closures in Asia. If you look at the various databases, it looks like there were over a hundred hedge funds that closed in Asia last year. But the picture isn't actually that gloomy.

First of all, last year there were no blowups in Asia in 2008. This is of course also because of inefficient markets here, most Asian hedge funds do not tend to use a great deal of leverage, which means you are unlikely to get investment blowups.

The worst we had was actually the year before, in 2007, when some CDS-focussed strategies went wrong in Australia, but in 2008, nothing. We saw funds closing down, generally because commercially the fund was too small to be viable. There was also some oversupply with a lot of investment bankers who jumped into hedge funds over the last four or five years with high compensation ambitions, who were disappointed and gave up to do something else. Probably no great loss there!

We also saw a smaller number of large global managers who had come in towards the latter end of the bull cycle, with big budgets and big expectations. So when they were disappointed, they also

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We are seeing the new wave of startups, which is exactly what we saw post the Asian crisis. Talking about the Asian crisis, you have to remember that to a certain extent, we've seen this movie before here in Asia, or at least we saw the prequel! Of course, comparing the crisis then with today's, it is always different, but there was a very comparable set of circumstances. A lot of the great names of the Asian hedge fund industry were actually set up around the end of the Asian crisis. They were very small for a number of years, before they finally attracted attention and started to gain critical mass. Look at funds like Artradis in Singapore, or LIM or ADM in Hong Kong - a lot of what are now the biggest established managers actually started as small boutiques post the Asian crisis, running very small amounts of money for quite long periods.

Peter Douglas



went home. We see that in every Asian cycle, whether it's commercial banks, investment banks, securities firms... late over-investment and then early retreat.

At this time however, we are seeing the new wave of startups, which is exactly what we saw post the Asian crisis. Talking about the Asian crisis, you have to remember that to a certain extent, we've seen this movie before here in Asia, or at least we saw the prequel! Of course, comparing the crisis then with today's, it is always different, but there was a very comparable set of circumstances. A lot of the great names of the Asian hedge fund industry were actually set up around the end of the Asian crisis. They were very small for a number of years, before they finally attracted attention and started to gain critical mass. Look at funds like Artradis in Singapore, or LIM or ADM in Hong Kong - a lot of what are now the biggest established managers actually started as small boutiques post the Asian crisis, running very small amounts of money for quite long periods.

The opportunity costs of starting a small firm, for somebody with experience now are very low, because there are no big-buck jobs to be had in big firms. The operational costs of setting up a business in a deep recession is wonderful as your input costs are very low. And in whatever market segment you are in, there are huge dislocations, and managers see big opportunities. So if you can find a small amount of capital, the performance fee on that is going to make a very good return for the next few years. It's no surprise that manager formation is strong currently, and within the crop of managers that start this year and next, will be the next clutch of great managers.

At GFIA, we tend to focus on right-sized strategies, so we talk to a lot of small and mid-sized managers. We are seeing a lot of activity at the moment from people either starting up or planning to start up soon. Possibly this year will be the year of the startup in Asia....

Matthias Knab

What strategies do you see coming up?

Peter Douglas

All sorts of strategies. Asian equity long-short accounts not for 80% but more like 60%-65%. So there's already good dispersion of strategies. Now, right across the board managers are finding dislocations and opportunities, and we see a very broad range of strategies starting up.

Dermot Butler

I think we are going to see new funds, in fact we are already seeing them all over the world.

I still revel in the fact that when we took on Winton, they started with four million dollars and it took about six years before they got up to maybe \$50 million, and then in just a few years they got up to \$5 billion. Although that obviously is not every fund we have on the books, but is a model to go for.

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Zack Kembar

One of the things that's exciting about the hedge fund industry is that it tends to be populated by entrepreneurs, and that's very different than say the investment banking or the banking industry or the larger corporate structures - both in Asia and globally.

We could all observe how the investment banks completely changed the way that they are doing business. Consider the Deutsche Bank leverage of 30:1, or Goldman Sachs bragging that they have

taken their leverage ratio from 25:1 down to 16:1 -- if you had a hedge fund group that said, "we are leveraged 15:1", everyone would take their money out. So not only the investment banks and banks, but also the large corporations, in many parts of the world, tend to fire, cull staff and break down their businesses in a recession. This means that, in effect, they are selling at the lows and when the market is really hot, they are hiring everybody and buying at the top.

There are all these opportunities, including dislocation, with the whole environment changing so rapidly - but I think you have to have the courage, and you have to have the small, nimble kind of organization and cost base that will allow you to capitalize on these opportunities. If you are an enormous institution, it won't work.

Looking at the people that come through our doors to set up a fund, we find that the typical profiles now are much different from let's say two years ago. Then, we used to have ex-traders or ex-bankers that were paid a \$5m to \$10m bonus and they said "we could do this on our own", which they often did, to their credit, and raised \$50m or \$100m in the good times riding the bull markets and basically made money.

But in the last two quarters, you have that correction of the hedge fund market, if I could use that term, and only the persons that could generate alpha and produce absolute returns are still standing.

I still see a lot of startups coming through the doors - we are still very, very busy. The profile of the new hedge fund managers as compared to 24 months ago is however different. First, they have a well-thought and good business plan.

Second, they tend to have a backer; either in the form of incubator monies or they have at least committed seed capital sometimes in the amount of \$25m to \$50m. They understand what managing a hedge fund business means, they have thought about who they are going to hire.

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Second, they tend to have a backer; either in the form of incubator monies or they have at least committed seed capital sometimes in the amount of \$25m to \$50m. They understand what managing a hedge fund business means, they have thought about who they are going to hire. The irony from all the lay-offs we've seen in the markets is more traders and bankers having nowhere else to go, leaving the entrepreneurial ones to come out and to do their own thing.

The managers we see are very optimistic. Themes we have seen include distressed assets, but we also meet managers who think assets are at cheap valuations. There is also traction in the global macro theme.

With the downturn of 2008, if you are in the game and still have a fund to run, most managers

have to fight minus 15% or minus 20% to get back to zero. The startup managers start right there at zero, and they are telling the service providers "thank goodness, your fees were too high last year and we didn't launch, but now we are going to start and we are going to get capital in to start at zero, a position much better than some of our existing competitors ..."

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