



Opalesque Roundtable Series '16

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Editor's Note

Talent level and strategy diversity remain as high as ever in Connecticut hedge funds, but managers wary of tax, overregulation

Connecticut, often referred to as the “Silicon Valley of Hedge Funds,” remains one of the leading hedge fund centers in the world. Lifestyle benefits give Connecticut advantages over New York and other metropolitan areas, while local managers still have access to talented, experienced market professionals, and benefit from the flow of investors in and out of the metro area.

The 2016 Opalesque Connecticut Roundtable exhibits the historical prevalence of talented managers residing in the region, and also the emergence of specialized new strategies that continue to populate the local hedge fund landscape. It is this depth in the talent pool and variety of managers that make Connecticut such a hotbed for global investors in accessing reliable alternative investment managers. This year's Roundtable presents a deep dive and valuable insights into five unique strategies, and displays the depth of specialization and market expertise available in the region. These strategies include:

Catastrophe Risk Investing, accessing insurance-linked risks through catastrophe bonds and collateralized reinsurance contracts

Fixed Income Long-Short Strategy, trading liquid credit markets while operating through the **lens of an equity perspective**

Renewable Energy Long-Short Strategy, focusing on Environmental, Social and Governance (ESG)

Small and Mid-Market Asset-Based Lending, providing capital to small and medium-sized businesses

The industry's only dedicated **REIT Activist Strategy**, bringing an activist component to publicly traded real estate and real estate-related securities.

However, local industry veterans also warn about the adversary effects of current state tax structures, which have become burdensome for principals. The state of Connecticut should reconsider these structures, which were favorable in the 1990's and drove growth in the industry, but now would be forcing many managers to reconsider their geography. Although access to investors and intellectual capital are very attractive elements of the region, if operational costs remain too high, a lot of managers and a lot of wealth may leave the area.

Another industry concern the panelists discuss in depth is the overregulation of the alternative investment industry. Unintended regulatory-driven outcomes are numerous, including extremely high operational costs and barriers to entry for new managers. The suppression of a new generation of managers has a downside for investors, who often cannot get high levels of alpha from the largest fund managers, and cannot access this new generation because smaller managers are not able to stay in business, despite good returns.

The Opalesque 2016 Connecticut Roundtable, sponsored by Maples Fund Services and moderated by Opalesque's Greg de Spoelberch, took place in Stamford, Connecticut, with:

1. Brett Houghton, **Managing Principal, Fermat Capital Management**
2. Craig Melcher, **Co-Founder and Portfolio Manager, Land & Buildings Investment Management**
3. Jason Brandt, **Regional Head of Fund Services, Americas, Maples Fund Services**
4. Jeff Haas, **COO, Old Hill Partners**
5. Mark Fishman, **CIO, Aesir Capital Management**
6. Richard Rankin, **COO, Managing Director, Ardsley Partners**

The group also discussed:

- What do investors look for in each of these unique strategies? (pages 7-9)
- What are the specific capacities for these highly specialized strategies? (pages 23-25)
- Bond market pitfalls: What an equity lens can tell you about market downgrades (page 10-11)
- How to best short fixed income securities (pages 11-12)
- How does a REIT Activist Strategy unlock value? (pages 12-13)
- Why catastrophe risk investing is a defensive positioning (page 8)
- How capital in catastrophe risk grew from \$1 billion of invested capital in the late 1990s to \$70 billion today (page 22-23)
- Why do insurance underwriters actually hope for losses occasionally? (page 16)
- Why the big banks have exited from small and mid-market lending (pages 14-15)
- With a high shutdown rate for emerging managers, what parameters do fund administrators gauge when onboarding clients? (page 22)
- How service providers also needed to become huge “data warehouses” (page 18)
- The unintended consequences of increased regulation in the alternative investment industry (pages 19-22).

Enjoy!

Matthias Knab
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Participant Profiles



(LEFT TO RIGHT)

Richard Rankin, Jason Brandt, Jeff Haas, Mark Fishman, Craig Melcher, Brett Houghton, Greg de Spoelberch

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Introduction

Brett Houghton
Fermat Capital Management

My name is Brett Houghton. I am a Managing Principal of Fermat Capital Management, which is based in Westport, Connecticut. Our primary investment strategy focuses on generating returns from insurance-linked risks, and we access those risks through catastrophe bonds and collateralized reinsurance contracts. This means that we are not in the business of generating returns for our clients through credit, equity, or commodities markets fluctuations, but by effectively risking investor capital to losses as a result of extreme catastrophic events. Our investors are compensated for that risk through the insurance industry. There is a tremendous demand for capital to be injected into the insurance industry to protect against these types of extreme events, and there is not enough insurance industry capital to cover the large concentrations of wealth and property in catastrophe prone areas. Our strategy is very specialized and the asset class is uncorrelated to traditional markets.

The main sources of capital shortage in the insurance industry where you can derive excess returns are hurricanes in Florida and earthquakes in California and Japan, because that is where you have large real estate exposures and relatively frequent incidence rates of large catastrophes. In those areas you can have actual events which can cause losses to the industry that outstrip the capitalization of the entire insurance industry. External capital is therefore needed to provide additional loss capacity for the industry.

As an outside investor, one of the main benefits of our strategy is that it is diversifying risk for a pension fund, family office, or individual investor. The asset class is uncorrelated to most of their other holdings, but still offers an attractive excess risk premium, so it is a nice source of uncorrelated returns in an investor's portfolio.

Jeff Haas
Old Hill Partners

My name is Jeff Haas, I am the Chief Operating Officer of Old Hill Partners. We are located in Darien, Connecticut and focus on private credit investments. More specifically, we engage in asset-based lending, and our strategy primarily provides capital to small to medium-sized businesses throughout the United States. In a world where traditional public fixed income investments have provided minimal yield for investors, private credit, partially due to illiquidity, can provide an attractive risk adjusted return for investors. Additionally, an advantage that private credit can offer to investors is an uncorrelated asset class which has far less volatility than the publicly traded markets, and in Old Hill's case can provide cash paying yield to investors.

Mark Fishman
Aesir Capital Management

I am Mark Fishman, the Chief Executive Officer and Chief Investment Officer of Aesir Capital Management. We have a fixed income focused long-short strategy. Our firm spun out from Diamondback Capital in 2012, so between the two different firms our core team has now been together for over eight years. I have roughly 30 years of investment management industry experience first as a traditional asset manager then in 1999 I transitioned to the alternative investment arena.

Our approach is interesting because we trade the liquid credit markets while operating through the lens of an equity perspective. We focus on fully understanding what is going on in the markets from an equity perspective in terms of themes, trends, and market capitalization. We then overlay our credit metrics onto that market research to create a portfolio which has better market characteristics on the long-side and conversely worse market characteristics on the short side. We are trying to effectively short candidates that have a declining risk profile and assets which are being downgraded, and to hold a core position of bonds that are getting upgraded because they are in the proper sectors.

What we do not do is buy yield, so we frequently actually run a negative carry portfolio. Going back to our equity perspective, we are looking for a catalyst of price change rather than carry as being the primary focus of our return.

This is a core attribute of our long-short equity approach which is applied to the fixed income markets.

Our goal in difficult markets is to ensure we utilize our liquidity to maintain a good Sharpe ratio and provide risk-adjusted returns. Over the last 3 plus years since inception of the Aesir Credit Funds we have had a Sharpe ratio over 3, which we are quite proud of. What we try to do is to make sure that when things are a little bit less choppy and challenging than they have been recently, that we are able to deploy our capital effectively and drive significant returns. What we are looking for is alpha that is generated from our strategy, and not from leveraged beta.

Craig Melcher
Land and Buildings Investment
Management

My name is Craig Melcher, and I am the Co-Founder and Co-Portfolio Manager of Land and Buildings Investment Management. We founded our business in 2008, and we invest in publicly traded real estate and real estate-related securities. Our fund invests globally on a long-short basis, but our investments are principally in the US.

We seek to capitalize on pricing inefficiencies in the public markets where companies are trading significantly above or below the private market value of their real estate. Our investment universe is over \$2 trillion in market capitalization, creating a large, liquid universe to generate alpha.

On the long side, we invest in companies we have identified that are trading at significant discounts to the value of their real estate. In addition to our traditional and event-driven investments, we utilize select activism to unlock value at companies via operational improvements and / or strategic alternatives and have undertaken 12 such campaigns since 2012. We are the only real estate hedge fund with a significant activist component to its strategy, which we believe differentiates us from our peers.

On the short side, we principally short companies we find to be inferior, which can be over-leveraged, own lower quality real estate, employ a poor management team and where we identify companies trading at significant premiums to the underlying value.

Richard Rankin
Ardsley Partners

My name is Richard Rankin, and I am the Managing Director and Chief Operating Officer of Ardsley Partners. Ardsley Partners is one of the oldest hedge funds in the United States. We manage equity long-short strategies, the longest-tenured of which was launched in 1986 by Philip Hempleman. The firm's primary areas of focus are healthcare, technology and energy. Over the past decade we have been tilting our energy exposure towards renewable energy.

In 2006, we launched a standalone renewable energy fund called the Ardsley Partners Renewable Energy Fund. This is an Environmental, Social and Governance (ESG) product that is seeing increased investor demand from not only the pension allocators, but also ultra-high-net-worth investors, family offices, and some state plans and sovereign wealth funds. The renewable energy strategy and that sector will be my main area of focus for our discussion here today.

Jason Brandt
Maples Fund Services

My name is Jason Brandt. I am the Regional Head of Fund Services for the Americas at MaplesFS. I represent Maples Fund Services, the fund administration arm of the Maples group which also comprises law firm, Maples and Calder, Maples Fiduciary and Maples Private Client Services. I have oversight for our service, relationship management and business development teams in North America out of our Boston office.

Maples Fund Services has been around since 2005 and currently has over USD\$55 billion in assets under administration. We operate in key onshore and offshore financial centers and offer a wide range of services including accounting, middle office, risk reporting and administration to clients that include investment management firms, institutional investors and global financial institutions.

We recognize that regulatory requirements and demands from institutional and high net worth investors have put tremendous pressure on fund managers and we take a dynamic approach to developing products and solutions that help alleviate some of the operational burden.

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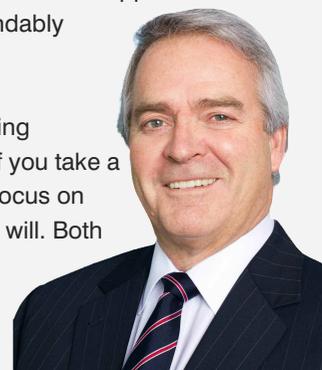


All of the managers at this table have fascinating and distinctive strategies. I would like to hear about your investor bases. What are investors looking for when they invest in your fund, and what opportunity sets do you provide that they can take advantage of?

Richard Rankin: Regarding ESG investing, there has been a significant interest across the allocator community to take into account environmental, social and governance considerations. Recently we have been hearing more about movement in the endowment and foundation world called “Divest-Invest”. The movement was initiated by some foundation and endowment boards which advocated for a highly level of impact or sustainability accountability by the managers they were investing with. This movement was catalyzed on certain college campuses with students lobbying their investment to divest from fossil fuel and carbon-producing assets, and to invest in clean energy instead. They exerted significant pressure on these institutions to go fossil-free. In practice however, there was no real incentive for the CIOs of these endowments and foundations to do so.

Prior to the recent selloff in crude oil, natural gas and global energy stocks, the equity sector had been one of the top performing sectors within the S&P for an extended period of time. That was certainly stimulated in large part by the demand from China. So, the traditional energy sector had been a top performing sector for a number of years and the opportunities in publicly-traded renewable energy companies was somewhat limited. CIOs were therefore understandably reluctant to divest away from the sector.

Today there is a visible and continuing movement into ESG-related investment opportunities, including increased dialogue and discussions on a periodic basis between major issuers and their advisors. If you take a look at the financial reports of publicly-traded companies over the past decade, there is increasing focus on their social responsibility and sustainability efforts. These are so called impact-oriented efforts if you will. Both ESG and impact investing are trends that I believe will continue as the Millennials take more responsibility for managing assets.



Mark Fishman: At this point our fund is closed, so we are not allowing any inflows, and we will not open the fund until the end of 2016. We currently have a stable group of investors who are more institutionally based, along with a small group of family offices and ultra-high net worth investors who have known us for a long time.

Our institutional investors have been with us for many years, and we are now getting inquiries from a number of endowments and well known family offices. We are lucky to be in that position, especially after 2015 when a lot of funds had a very difficult year and we were able to have a positive return. Our extensive track record, size, and strong performance have opened up a lot of doors, but we have agreed that we will not officially start marketing until mid-2016 and will not accept new money until the end of the year.



Jeff Haas: Right now we are seeing a great deal of interest in illiquid opportunities, like the private credit opportunity managed by Old Hill. Investors have started to realize that there is an illiquidity premium that can be extracted from specialized investment activities like private credit. Our particular strategy focuses on capturing that premium.

One of the things that I try to communicate to people is that when you talk about private credit, you really have to narrow down where the specific opportunity fits within a very broad private credit landscape.



Are you looking at a cash flow-oriented opportunity where you want to capture a multiple of EBITDA? Or at the other end of the spectrum, are you looking at an asset-based lending opportunity where you focus on loan-to-value considerations? Is it a senior secured debt opportunity, or a mezzanine opportunity? Is it small balance, large balance, sponsor-driven or non-sponsor driven type of deal? Within the private credit spectrum there are many different verticals that investors can access.

There has been a lot of capital raised and deployed in the sponsor-driven, cash flow-oriented, large balance type of lending opportunity. That space has definitely seen a lot of activity. We at Old Hill think the best opportunities are on the opposite side of the spectrum, because we look primarily at small balance deals. We tend to focus on transactions that are sub-\$25 million and have a maturity of up to 4 years. Depending on the asset and the structure of the transaction, we will structure our deals with loan-to-value ratios of 35% to 85%. In most of our transactions we are able to generate coupon-related activity of anywhere from the high single digits to the mid-teens, with probably another 1 to 3 percentage points added to our return in the form of traditional lending fees associated with loan origination, pre-payment draw down, etc.

Sometimes when an investor hears about those returns they automatically want to shift us into a different risk bucket, but the reality is that probably 600-700 basis points of that return is due to the illiquidity of the opportunities in our space. You are going to continue to see opportunities like that because there has been a fundamental shift in the United States in terms of access to traditional capital, especially for the smaller companies. The big banks have essentially exited from small and mid-market lending. We have indeed seen a lot of capital get raised at very low yield for bigger companies, but you have also seen a steady deterioration of small companies' access to traditional bank capital over the last 15 to 20 years. That is partially why there such attractive rates of returns that can be generated within private credit opportunities.

For investors looking for low volatility and a steady double digit type of return, there is a definite opportunity in certain segments of the private credit space to do that.

Brett Houghton: The investor base for insurance risk exposure has evolved somewhat over time. Our firm has been around since 2001, so we have a roughly 15-year history in the space and have been able to observe the changes in the industry. Large international pension funds were definitely the early adopters of accessing exposure to insurance risk. They are extremely sophisticated entities, and very early on they recognized the strong value of diversification that insurance risk exposure provides to their portfolios. We had a couple of large pension fund clients who came onboard very early on in the lifecycle of the firm, and who effectively bought out our capacity until about 2010.

Since that time, the market in general and also our footprint has continued to grow quite substantially. Eventually, we got to the point where the size of the market and our capacity within the market outstripped the demands of our early core clients. As a response, we broadened things out with a number of commingled funds, a UCITS fund, and also with British Virgin Islands-based offshore fund which we market through a company called Global Asset Management (GAM), which is based in Zurich and London.

The investor base for those products has been dramatically different. Those newer investors have primarily been family offices with high-net-worth footprints, and also foundations. What is interesting is that many of those clients also tend to be international, and the main trend we see is that they are not looking for returns in the teens. They use our strategy as more of a defensive positioning asset within their portfolios. Now, catastrophe risk investing may seem somewhat counterintuitive to that defensive perspective, but once you get under the hood of our strategy and really understand what goes into it and how the return stream behaves, it becomes quite clear why investors look at our area as a defensive investment.



We have seen a little bit of investor rotation with the recent market volatility, as some of the longer term investors have looked to allocate away from lower yielding investments and looked instead to distressed high yield or other energy equity investments to potentially generate higher returns. However, we are receiving a lot of new inflows from entities with similar profiles to our traditional client-base, who observe the choppy markets and are not looking to increase their risk exposure in the current environment.

In summation, investor interest in the space has never been higher. Catastrophe risk investing is a \$70 billion market and has been growing at a consistent clip of about 10-15% per year over the last 15 years.

Craig Melcher: The types of investors that look at our strategy range across the spectrum from large endowments, pensions funds and foundations to smaller family offices and high-net-worth investors. The source of that allocation from these organizations can differ; sometimes it comes from the real estate bucket of this entity who wants to dedicate a portion of their allocation to publicly traded real estate stocks rather than buy private buildings. The demand can also come from the larger equity long-short component of one of these allocators, where they see the return stream that we have generated and recognize us as strong alpha-generators. These will invest in our strategy based on the return stream, and the low correlation of our returns to various market indices.



Greg de Spoelberch

I would like to take a deeper dive into your strategies, talking about day-to-day activities and what kind of opportunities you have and how the strategies operate. Mark, with your 32 years of market experience and well-established track record, tell us more about how you generate returns.

Mark Fishman: I started in this business working with a quantitative equity firm up in Boston named Batterymarch, so I started off looking at equity sectors, industry groups, and individual stock components. I was looking at factors like relative value, expected betas and empirical betas, and observing whether or not I saw actual price performance in comparison to what was expected. The experience gave me an understanding of equity teams; specifically how and why they pick stocks, and of traditional and quantitative matrices of correlated and non-correlated analysis.



I moved on to Bank of New England and began working in fixed income because the move was the next intuitive step, where we were applying equity views to liquid credit portfolios. What we found was that we did a very good job of avoiding most of the mistakes in the market. In the long-only credit world of bank portfolios, if you can avoid the mistakes that are also represented in the indices, for example, you will achieve significant outperformance. I was fortunate to work with some very good teams early in my career, and to gain a great deal of experience from talented professionals.

Greg de Spoelberch

Can you whittle down specifically on what you mean by mistakes in the indices and market?

Mark Fishman: I absolutely will, through both an early lesson in my career that drove my philosophy, and through a more broad view of the bond market and flaws in the indices. I ended up at State Street Global as a Senior Portfolio Manager overseeing all of the fixed income portfolios, and I can give you a concrete example which helped to shape my investment philosophy and perspective. We had a very large bond position in one of the automakers before it went bankrupt, and I went to the equity team and asked them about their views on that specific equity. Their blunt reply was that they would not buy it. The stock was trading at about \$8 a share, and I asked them to give me a reason why not. Did they see an issue with valuation, forward outlook, or market share? Would they buy it at \$3? They said that they would not buy it at any price. Everybody who likes a story owns as much of it as they can, and everybody who does not like the story is not going to buy it at any price, either higher or lower, if the fundamentals are too negative.

We focused on the feedback from the equity team, which was a huge red flag for us, and took a long look at the company's credit history. The bonds had started with a single-A rating, and they were now rated triple-B at the lowest edge of investment grade. The ratings were clearly going the wrong way, and State Street's short term funds also happened to be one of the largest providers of short term funding of this company through its participation in short-term credit facilities, which raised another set of concerns.

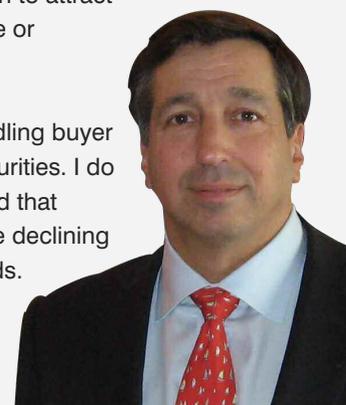
After more extensive analysis, given that outlook I got all of the relevant parties together and we ended up terminating that short-term credit facility within an appropriate time-frame, which gave the automaker time to find other credit partners. We also fully exited our bond positions. About six months later that company had the highest yielding bond in the investment grade matrix, so if you did not own it you gave up a lot of yield and got less return. However, when the bonds were subsequently downgraded, their value decreased by roughly 25 to 30 points. By avoiding that downgrade we did give up a little yield, but we did so to obtain a far more stable price performance. So the lesson is that in the liquid credit markets I want to fully understand all of the components of what we have in our portfolio. As I said earlier, one of the ways we find alpha is by going sector to sector and analyzing expected earnings versus realized earnings. That metric is a key indicator for us.

As some additional background on how the bond market works and our approach, take a 10-year public corporate bond, for example. Fixed income market professionals will say that they can define the duration of the bond, and the convexity feature is relatively defined as well; but when a bond goes from investment-grade to non-investment grade the price goes down appreciably. The market misses the negatively convex payoff nature of credit. That is definitely one of the biggest fixed income market pitfalls. People model the convexity related to interest rate moves but underappreciate the negatively convex payoff related to spread or credit moves. The payoff in credit isn't symmetric. The downside pain is a lot greater than the upside gain. A lot of market players fail to recognize the key indicators before a downgrade, and do not act until it is too late. They can therefore get killed by the market. Our equity approach and research in combination with our fixed income analysis helps us to recognize those downsides and position accordingly.

Historically, a bond that falls from single-B to triple-C has about a two-thirds probability of going into default. Every time a bond goes further down that spectrum, it has an increasing illiquidity profile. It has to give more yield and you have fewer people who will buy it, so it becomes less and less liquid.

If somebody is trading in private and illiquid fixed income, they are buying bonds with the appropriate premium, which provides a lot of extra yield in comparison to the public market. When you have a bond that is coming from the public world and becoming increasingly illiquid, it has to gap down in price to give a yield which is high enough to attract other investors' interest. However, because those bonds have declining metrics, rather than stable or improving metrics, they become increasingly more abandoned and less liquid.

Our goal is to be short those increasingly illiquid securities because we recognize there is a dwindling buyer base. The negative price performance is what we are trying to capitalize on by shorting those securities. I do not find that you can effectively find the best opportunities by looking solely at bonds. I have found that usually you find best fixed income opportunities when you look at equities of companies that have declining market capitalizations and then cross-reference those numbers with credit history and credit trends. Then you move on looking at relative performance from the equity side. If I can combine those metrics, it gives us a list to start from before we do the deeper dive.



We have a variety of quantitative analysts and several fundamental analysts on our staff to support and inform our traders, who have been trading and managing portfolios on average for over 20 years. We prefer professionals who have personal experience operating in the savings and loan crisis along with the 2008 financial crisis, and who did a good job of not getting destroyed during those periods. My view is that a little bit of gray hair does lead to better sleeping at night.

On the long side we are looking for the opposite kind of characteristics as the short side. We want companies who have an improving credit profile, and who are in sectors where we want to be thematically. Richard's discussion of ESG and clean energy rings a bell with me, because these are improving themes and stories of where America and the world are going. We want to be involved with companies that can model out better earnings and experience organic growth.

We are also looking for companies that have a responsibility to their debt holders, where they prioritize their financing and want their bonds to be upgraded. Securities that have excellent management, strong economic tailwinds, and an increase in liquidity profile comprise the core of our longs positions.

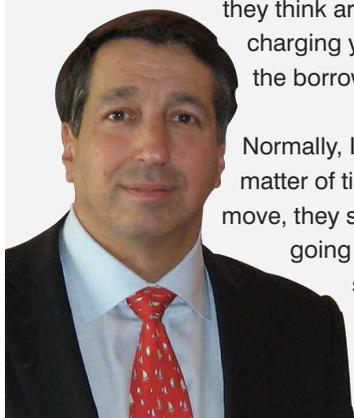
Because we are liquid, we can play a number of simple roles that very few other people really can. When something is not working and the markets are choppy, we can actually get smaller. With this kind of volatility in the market, we can indeed get whipsawed, as most of us do, but we are willing to get whipsawed to protect principal during really challenging times. If we are losing money, the overall balance sheet of our portfolio is reduced, and we sell the problems that spring up.

We do not need a lot of leverage or a huge balance sheet. What we do need is to have very defined risk parameters for the overall portfolio, so that when we are losing money we are reducing our positions, and when we are making money we are increasing the position sizes. Because of that philosophy we do have higher transaction costs because we will trade more and have to pay for bid-offer spread, but for the 16 years we have been on the traditional buy-side we were a top outperformer. That outperformance includes my periods with State Street Global, Mitchell Hutchins, and Columbus Circle. Since I went to the hedge fund space back in 1999, I have had only one negative year in this strategy. Every year besides that we have been able to generate positive returns with a consistently high sharpe ratio. That ratio has been one of my greatest priorities and sources of pride.

Richard Rankin

What is your cost to borrow on the short side? We have seen that due to the volatility in our sector, the cost to borrow has been and is quite high. While there may be a number of opportunities on the short side, the cost of being there is increasingly expensive; so, when it comes to the short side, there's also a real need for a catalyst to unlock value, correct?

Mark Fishman: Absolutely, our trades have to be thematic and catalyst-driven to fit into our equity long-short overview. When a stock is heavily shorted, the cost of the borrow goes way up. Market participants look at some of the energy companies that they think are going out of business, and you either cannot borrow those securities or the counterparties are charging you very high amounts. In fixed income, we can face that situation as well, and if you cannot get the borrowed security you simply cannot buy into that trade.



Normally, I make sure I can get a term borrow and get bigger in the position, because it is usually just a matter of time before the bonds move to the downside. What is interesting with bonds is that when they move, they shift 10 to 30 points. You must therefore have high conviction, because you know that you are going to be bleeding for a while with your carry before the desired movement occurs. Most of our shorts tend to be early shorts, so counterparties who do the securities lending have no problem lending us the bigger names like Exxon, because it is a triple-A bond. However, it took me two weeks to sell 10 million of those Exxon bonds, so even the highest grade bonds can present liquidity issues at times.

People asked me why I was trying to sell Exxon bonds. Last year Exxon did an \$8 billion bond issuance because they did not have the free cash flow to pay out their dividend. They went to the bond market and borrowed the money in order to distribute that payment. The price of oil last year was higher than this year, so we came to the simple conclusion that if they did not have the money last year to pay that dividend, what are their options this year? One of the rating agencies also recently put a negative outlook on that company. This is just intuition, but Exxon probably wants to issue more debt through a bond deal, and is trying to figure out how to do it and with what maturity. If I look at where the bond is trading now, and where it would have to come to market with a new \$8 billion deal in the coming year, I am betting that the bonds issued last year are going to get cheaper. I do not think that the company is going out of business, so I will use the new issue at a significant discount to cover that short and move on.

That is just one example, but a lot of these bonds in general are just collateral. The secret is making sure that you are not simply jumping on everyone else's short, and if you execute the short trade early, you make sure that you utilize term borrowing. If you do not use term borrowing, you end up getting absolutely crushed with borrowing fees.

Greg de Spoelberch

Craig, tell me about your strategy and your opportunity sets.

Craig Melcher: Prior to launching Land and Buildings, my partner Jonathan Litt and I ran the REIT sell side research team at Citigroup. Consequently, our portfolio is built with a bottom-up approach because fundamental analysis is a major part of our backgrounds. What is unique about the real estate space is that we are able to value the buildings a company owns within a pretty tight range in most situations. So, when a stock is trading appreciably above or below that level, we can find opportunities on both the long and the short sides.

On the long side, there are three strategies that we employ in order to make money. The first is what we call our traditional strategy. When we find a high quality company with strong fundamentals that is trading at a cheap value relative to its private market value, we will buy the public stock with the projection that it will be able to close the gap relative to the actual asset value. That traditional approach comprises the majority of the number of investments we undertake.

The second component of our long portfolio is our activist investments. We have run 12 activist campaigns since the second quarter of 2012 where we have generated over 40% annualized gross returns on completed investments. Our goal in these situations is to work collaboratively with the management teams and boards of these companies to formulate a strategy to close the discount between the stock price and the actual asset value of the companies. We have run proxy contests seeking new representation on the boards in situations where we have not been able to work together with management teams. We have effected change in all of our activist situations, including several companies that have been sold, and several others have enacted changes to their capital allocation strategies and management teams, which has helped close the value gap.

The third category of our strategy is event-driven and is a smaller component of what we do. Our real estate expertise allows us to identify and analyze dislocations in the market surrounding events such as mergers, spin-offs and management changes and determine whether or not we want to invest in such opportunities.

On the short side, our investments principally revolve around identifying and shorting what we call inferior companies and overvalued companies. Inferior companies are those with inferior balance sheets, substandard management teams, and lower quality real estate with inferior supply/demand characteristics. What we have seen over our careers is that these companies generate inferior earnings growth and fail to grow their net asset values at levels that are commensurate with their peers. Overvalued companies are companies that the public markets are giving a valuation that is well above the underlying values of the real estate.



When we identify those companies, if there is any misstep, whether it is a bad acquisition or a management change, there is a great deal of room for that stock to fall back to the actual underlying value and we can capture that spread. The final category of shorts are hedges to long investments, principally activist investments to reduce exposure to a given property type or geography.

Greg de Spoelberch

You mentioned you are essentially the only fund in your universe that employs an activist strategy. Are there other activist funds that touch the REIT space or do something similar?

Craig Melcher

There are no other dedicated real estate activist funds. There are other larger activist funds that have been involved in certain real estate companies, but real estate is not their primary line of business to our knowledge.

Greg de Spoelberch

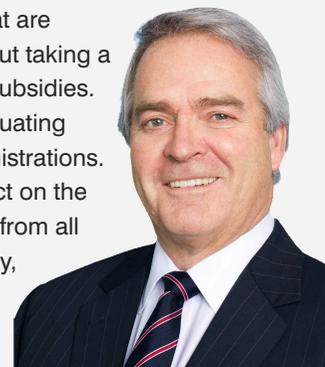
How do you choose a board when you are implementing change in a company?

Craig Melcher: Over time we have developed a great network, including many former real estate executives. These are professionals who mostly have held senior roles running companies. They have been through multiple market cycles and have the experience to formulate a clear, independent perspective in order to catalyze value. Quite often we will look to an executive who was the CEO or CFO of a REIT, or someone who ran a large portfolio that invested in REITs. We also select individuals outside of the real estate space that we believe can add value to the company.



What is important is to first identify what the issue is at a company that is causing the discounted valuation, and then we can find the right people to help address that issue. If inferior operations and bad capital allocation are the problem, then when we think about the individuals to nominate to that board, we will identify individuals that have expertise in that area. That individual can provide the knowledge and leadership to improve the operations or capital allocation decision making. We tailor our recommendations in order to find the right person to fix whatever issues we think are causing these stocks to trade at discounts.

Richard Rankin: While we have 'gone activist' a couple times since inception, activism is not a priority. The Ardsley Partners Renewable Energy Fund is an equity long-short fund that focuses its investments on companies that are seeking to solve global energy and natural resource problems. We invest in these companies without taking a lot of technology risk, and we prefer to buy companies that are cash flowing without the benefit of subsidies. The renewable energy sector has been colossally volatile, predominantly as a consequence of fluctuating commodity prices and the sentiment surrounding policies of both domestic and international administrations. Regarding the domestic sphere, both state and federal level administrations can have a huge impact on the market for renewable energy thus driving volatility. The amount of subsidies provided to the sector from all quarters seems to ebb and flow, and the impacted or beneficiary securities tend to trade accordingly, and are highly correlated to policies.



Our team looks at a universe of about 500 names which are fossil free and would qualify for our strategy. We are looking for companies that have organic growth and that are priced reasonably well regarding their peer group. We divide those companies by sub-sector, not just by GIC. The team utilizes an extensive fundamental research process for each stock which includes sub-sector analysis and macro considerations. The portfolio manager ensures, that from a risk perspective, the portfolio is not over-weighted in any specific sub-sector which might be negatively affected by commodity price fluctuations, government subsidies (or lack thereof), new invention and technology dislocation. The fund does short companies in the sector as well, but as I mentioned earlier, in order to effectively do so we generally look for a short-term catalyst because our cost to borrow in this volatile sector is high.

The Ardsley investment team is comprised of nine analysts, three of whom are dedicated to the renewable energy strategy. While we do indeed invest globally, we are a domestically focused fund with roughly 70-80% of our investments going into US companies, and 20-30% deployed out of this country.

Wall Street coverage and research resources in the renewable energy sector are somewhat limited. We compile all of those sources and external coverage to subsidize our own fundamental bottom-up research.

Jeff Haas: At Old Hill we focus on the private credit space, so our lens is slightly different than some of the other strategies that have been presented here today. We consider ourselves more or less a full service originator and lender to these small businesses, so we need the necessary infrastructure in place to support all of our internal activities. A number of our employees wear several hats, and we start out by having small teams focus on the sourcing of transactions. We typically do not participate in transactions that have been originated outside of the Old Hill name. Besides the sourcing of transactions, we do our own analysis and due diligence on the underlying investments. There can be a lot of similarities in structuring each deal, but each also has unique properties so you can see a wide range of different lending opportunities. To a certain extent there are also private equity components to what we do in terms of deal origination and analysis.

Once a deal has been structured and a term sheet executed then the full-fledged due diligence on a company begins. Our teams are sent out for on-site visits to the particular borrower's location. We look at whether or not the financial controls are in place, and the underwriting standards are reviewed. Sometimes we actually loan to smaller lenders, which is more or less a wholesale activity, and for that kind of deal the underwriting components are critical. In all cases, typical background checks are conducted, including criminal and credit checks for the executives.

When we are getting involved with a company we want to take steps to ensure that the borrowers are seasoned and have significant experience, where either the company itself or the individuals running the company have a certain level of expertise in their field. We also need to make sure that there is proper alignment of borrower and lender interests in place, which means that the loan-to-value ratio is appropriately structured with the borrower, and that there is capital at risk from the underlying borrower itself. That capital risk from the borrower is a key determinant in ultimately determining the appropriate loan-to-value for a particular asset. After our due diligence functions are carried out, the legal documentation and negotiation processes are completed, and we can finally fund the transaction.

The time frame for the identification of an opportunity to the actual funding of a transaction can take anywhere from six to eight weeks on the quicker side, to three to five months on the slower side. However, that is not where the work stops, because what is most important for us is the underlying activity and monitoring of the transaction after a deal closes.

That is why it is so important that we make the right decisions going into a transaction. We monitor and service of all of our transactions in-house, so a firm like ours must have a platform in place to originate, structure, service and monitor the transactions. Old Hill has such a platform in place and has been involved in lending since 1996.

The opportunity that we are really trying to take advantage of, which I alluded to earlier, is the regulatory shift in the United States. Companies come to us and ask why they are not getting a facility from a traditional bank.



This is because the banks have gradually pulled back and exited from the mid and small market lending space. Recent legislation and the Dodd-Frank regulatory requirements have made it increasingly difficult for traditional banks to engage in a lot of this activity unless it is done at a very large level, so scale is very relevant. Most of these companies are too small for traditional banks to consider, and I can tell you why.

If I engage in a \$20 million facility for a particular borrower and on day one they are only drawing down \$2.5 million for a transaction, if I am a private entity there is no issue from a regulatory capital point of view. On the other hand, to provide that loan under the same circumstances a bank would have to put forth \$20 million of regulatory capital. It is obvious why they are not engaging with these smaller companies and lending into this space; because it does not make any sense for them. From an asset-based lending point of view, we can take advantage of that regulatory inefficiency which is pushing into the banking space. I will re-emphasize that smaller companies are borrowers that have been most impacted by traditionally banks exiting the lending landscape, and interesting enough these are the exact companies that desperately need this capital, which is why Old Hill focuses on this segment of the market.

When you look at the economy from a job creation point of view, smaller companies account for over 60% of the new job growth in the US. They are significant contributors to Gross Domestic Product, so our strategy and others like it have a huge impact for the future well-being of this country. Even though the economy has recovered somewhat since 2008, these organizations need access to capital, and you are not seeing nearly enough capital spending. Regardless of what the publicly reported employment numbers are, employment and wage growth are also below where they need to be, and that is a direct result of the reality that many of these companies are still not getting the capital that they need in order to grow.

We focus primarily on transactions here in the United States, where there are a ton of opportunities because of the environment I just described. We recognize the range of private opportunities outside of the US, but we have a strong grasp of the collateral perfection issues and bankruptcy laws within the US, and there are sufficient opportunities domestically. All of my transactions are cash paying, so they do not have a Payment in Kind (PIK) component to them, which means that in a world where yield is quite hard to find, what we are able to do for an investor is to provide an attractive yield that is cash paying and offers a pretty constant return on capital over multiple years.

Brett Houghton: It is certainly interesting to hear about bank regulatory capital influencing returns in the asset-based lending space, because a key factor that drives return opportunities in the insurance risk space are insurance company capital requirements.

To give you all some background, insurance companies are regulated by the National Association of Insurance Commissioners (NAIC) here in the United States, and also receive ratings from rating agencies including AM Best, S&P and Moody's. They are also regulated in Europe through the Solvency II Directive. Regulatory requirements put a great deal of stress on these companies, because they consume a great deal of equity capital in the case of a catastrophic event. Regulators are primarily concerned with the insurer's ability to pay all of its claims, and in the case of catastrophic events they are quite conservative in terms of how much capital or external risk transfer the industry is required to maintain in order to ensure that claims are paid in the event of a large catastrophe.

The average headline return or coupon in the catastrophe bond space is currently about 5% over cash. About 2% of that represents the actual quantitative or actuarial expectation of loss on a particular bond. We are talking about assuming risks of loss or default on these securities, which are expected to only occur about once every 50 years. Recurrence of the 1906 San Francisco earthquake or Hurricane Andrew would be some examples of events likely to cause losses to existing catastrophe bonds, because catastrophe risk only includes extreme events which can potentially cause hundreds of millions of dollars in losses for traditional insurance companies. In effect, we are getting on average a 3% excess return over that 2% actuarial risk of loss, which amounts to a total of 5% over the cash coupon.



What really drives that return premium is the cost of equity in the insurance space. You have to think about these risks and how much equity capital they consume for the insurance industry in order to account for potential losses in the hundreds of millions of dollars; that is the real driver of the return generating capability within the insurance risk investing space. The types of risks which provide the highest excess returns are the ones that cause the most marginal equity capital for insurance companies.

If you think about the difference between what we refer to as peak peril risks versus diversifying risks, it is quite dramatic. Insurance companies tend to be maxed out on the peak peril risks that they are able to take. When you look at Florida hurricanes, California earthquakes, and even New York, New Jersey Shore, and Connecticut hurricane exposures, there is so much real estate and insurance value in those regions that the industry is already maxed out relative to the capital that they have. They therefore look to counterparties like ourselves (through the issuance of catastrophe bonds) to mitigate that risk.

For example, look at the situation where a developer builds a new hotel in Florida and they go to AIG to get a policy for \$50 million of coverage. If AIG's capacity is full, they would have to put up another \$50 million in capital to cover this policy. From the regulatory capital standpoint, that new policy attracts a full marginal unit of capital, so there is a lot of excess charge that is going to go into their premium calculation for that exposure.

On the flip side, if you want to build a hotel in Wisconsin and you go to AIG to buy the same policy, they will have to put up zero marginal capital to provide you with that insurance policy, because there is nowhere near as much exposure in Wisconsin. The way that the capital models work, the insurance companies are not going to have to increase the amount of equity value that they have against their book of business to protect against these kinds of extreme catastrophe risks in less-concentrated regions.

When we look at investing in insurance risk for our clients, all insurance risk is equally diversifying to some degree. The key is not to look for too much diversification within the space, but instead to look at the space itself as diversifying to your overall holdings. Within the sector, an investor wants to maximize the amount of excess returns they can get over the risk of loss. That does lead to a relatively more concentrated book of risk exposures relative to the industry, but over the long run if you are able to generate enough excess return over the actuarial risk of loss that you are taking, you end up with a much higher expected excess return in the long term. Part of the reason for that is because the cost of capital fluctuates with its scarcity.

If you think back to Hurricane Katrina, that was the most devastating event that we ever experienced from an economic standpoint, resulting in a roughly \$45 billion industry loss. In the aftermath of that event, it did cause the cost of capital in the insurance industry to spike up dramatically. Our return making potential spiked from the cash plus 5% range to the cash plus 9-11% range. Those returns persisted for about a three year period of time, because it takes time for the industry to regenerate that capital when they have suffered heavy losses on a particular event. During that time frame, the elevated cost of capital actually allowed our strategy to recoup those losses and make them back in a fairly short period of time.

In Katrina we had an approximately 8% drawdown in August of 2005, but our returns in 2006, 2007, and 2008 were roughly 8%-9% over cash on average per year during that three year period, so we made back the drawdown quite quickly. If you talk to insurance underwriters in the space, they will quietly tell you that they actually hope for losses occasionally, because over the long run you get paid more for having taken the loss and then earning it back by charging higher premiums in the aftermath. Thematically, the concept is somewhat counter-intuitive, but that is how the industry works.

Greg de Spoelberch

You are essentially hoping that you do not get hit with multiple catastrophes for a couple of years in a row, because that kind of anomaly would put you out of business. Is that correct?

Brett Houghton

That is exactly right. If you had the 1906 San Francisco earthquake one year and then the next year you had a recurrence of Hurricane Andrew, the performance would be down too much to be able to recover in a short period of time. It's not an out of business situation however, since capital will be so scarce in that environment that investors who stay committed to the sector would be well compensated for continuing to provide capital to back these risks. The multi-event risk you are referring to is so far out in the tail that the probability of that type of sequence of events is probably a 1 in 10,000 or 1 in 20,000 years scenario.

Richard Rankin

Brett, who are you seeing out there competing with you in this market?

Brett Houghton: The market basically follows the 80/20 rule. 20% of the managers have probably 80% of the assets under management. We are usually going up against four or five different managers with longstanding experience in the space for some of the larger, higher quality mandates. The way organizations come to market with their funds varies a little bit. Some other managers will try to approach the market from the traditional insurance company perspective, where they seek to assemble a portfolio of risks that are essentially equally weighted among 10 or 15 different regions or zones throughout the world.

What is interesting about that approach is that it parallels the way that the insurance capitalization rules work, because the insurance industry favors an equally weighted, nicely diversified set of exposures. That is the way that the industry minimizes capital charges relative to the business that it takes on.

However, the end effect of that approach is to create a competitive dynamic where insurance and reinsurance companies and some fund investors fight against each other for the diversifying risk, and drive the premium rates down. In many cases they even drive the premium rates below the actuarial risk of loss, simply for the privilege of having top line premium income, which appeases the equity analysts. The type of managers in our space who use that approach have a different set of metrics that they are trying to optimize, whereas from our perspective we focus solely on a pure risk-reward tradeoff

If we are looking to maximize returns for investors in the long term, our view is that we should be focusing more heavily on peak peril risks, which have the most attractive excess returns associated with them. Our portfolio is structured to favor those risks. While there is a heavier tail risk from a downside perspective, year in and year out our returns are much higher because peak peril risks attract a much higher capital charge and we therefore get paid a lot more for taking those risks.

We tend to outperform our peers by about 150-200 basis points in exchange for a 10 point heavier tail at the 1 and 100 year point. If you think about how that math works, we have a 10 point worse loss with an expected recurrence rate of once every 100 years, but we are making that back every seven to eight years in terms of excess return. That is because of the insurance regulatory framework that imposes these high capital charges on peak peril risks. Investors that gravitate to us understand that tradeoff, and they are willing to live with a bit more volatility within their allocation to the insurance risk space.



Greg de Spoelberch

Do you also focus on weather risk?

Brett Houghton

If you think of hurricanes as weather, we do. We do not utilize so-called weather derivatives, which focus on rainfall or temperatures. There are no capacity issues within the insurance space for those kind of risks, and so they do not attract any excess capital charge as a result.

Mark Fishman

Do you do a lot of work with the Bermuda-based catastrophe reinsurance issuers?

Brett Houghton

Yes, they are major issuers of catastrophe bonds. They also enter into private over-the-counter derivatives contracts with investors such as ourselves, so they are one of a range of sources for how we generate investment opportunities.

Greg de Spoelberch

Jason, give us your perspective on regulatory changes and the range of managers you are working with. It is a whole new world out there, so could you please give some additional insights how else regulations have and are changing the industry?

Jason Brandt: The industry has evolved significantly over the last ten years and regulatory compliance has become the top priority for managers today who now bear a much greater operational burden. Quite frankly, that has been a benefit for us at Maples Fund Services because managers are increasingly looking to outsource those responsibilities.

The wave of regulation has indeed been daunting, from FATCA and Annex IV a few years ago to the new Common Reporting Standards ("CRS") which are being implemented this year. In conjunction with recent demands from investors, managing internal systems of reporting and compliance has never been more important for managers.

The funds industry, however, is just now beginning to comprehend the full scope of the technological challenges brought on by all of this regulation. The issue is that all of these regulatory efforts involve massive amounts of data that needs to be collected, aggregated, calculated and submitted on an ongoing basis. The frequency of filings, in particular, has promoted us to invest significantly in our technology in order to be able to meet these new requirements. As a result, we've become more of a data warehouse that can take information, manipulate it and then file accordingly based on a jurisdiction's specific requirements.

At times it can be quite difficult to mine all of this data so we have had to evolve our processes and procedures internally and have adapted to the new environment alongside our clients in order to support them most efficiently. We have been on the leading edge of many dynamic initiatives as an industry and as new regulations have come on board and this approach has made us well positioned to support our clients and add significant value for a fund.



Greg de Spoelberch

Are you seeing more prosecution or more fines for regulatory lapses?

Jason Brandt: There has definitely been an uptick in enforcement and there are more complex factors coming into play that managers have to worry about. The SEC is obviously much more active in the alternative investment and hedge fund space. The new Anti-Money Laundering ("AML") and Know Your Customer ("KYC") rules have put a great deal of attention on screening client-bases and potential investors.



FinCEN, the Financial Crimes Enforcement Network, has been investigating managers who are not properly performing their AML and KYC processes and imposing significant fines. This is true even for funds within the US who need to strictly follow their own internal procedures. There have already been significant penalties with regards to operational and reporting failures and we can expect to see more fines being levied moving forward.

Greg de Spoelberch

All of the experts in this room have a great deal of experience in the alternative investment industry. What are your insights about the changes to the industry environment from a compliance and regulatory standpoint, and what effect are these new operational costs having on the industry and the new generation of up and coming managers?

Mark Fishman: The end result is that those regulatory changes raise the barriers of entry for new players, which is a shame for investors. In conjunction with those regulatory pressures, you have to look at the generation of more experienced alternative managers and also current investor perspective to draw insight into the current environment.

Most successful people, the best managers, have over the years really stuck to their knitting and their core area of expertise. No manager can run any product at an infinite size, although I'm sure they would like to, and most managers who have an alternative strategy have to accept the fact that, whether they will admit it or not, they do have a natural capacity. As a fund gets bigger, we all hear investors say that they are not receiving the same alpha return. That is absolutely true. But what allocators do receive in sticking with those larger managers is a stable alternative platform in which they have confidence, and in whom they have developed trust.

When those investors find a manager who is really fantastic and small, they frequently want to observe that manager for five years before allocating to them money, and in doing so they often miss a good part of that manager's performance. So there is a tradeoff on the part of investors, where they have a comfort level and stability with bigger and more established firms, but the returns are usually not outstanding, and investors can definitely miss the alpha generation provided by up and coming funds.

If you are 30 years old, at that age you really are still just a kid with limited experience. If you are trying to put together a group of talented portfolio managers, it is extremely difficult to raise the money to even operate for the first two or three years. You need the ability to have a COO, a CFO, and a compliance person, because if you do not have that help or those functions in place, you do not have time to do your job of generating returns. With investors demanding more consistent reporting and communication, along with the regulatory pressures, there are significant barriers to entry right now.

My perspective is that what is affecting the entire industry and restricting this new generation the most is the noticeable public backlash against the alternative investment community, most specifically hedge funds. In my view that is ironic, I do not think that backlash was deserved. AIG clearly overleveraged their AAA bonds and caused far-reaching and pervasive problems during the credit crisis. A great deal of the major corporations also became overleveraged in their financing arms, and when they could not get funding it created a myriad of problems. The banks were bailed out, and hedge funds took advantage of trading opportunities, but so did all of the major mutual funds. Politicians and media members like to point fingers, and they would rather point fingers at hedge funds rather than investment companies that offer mutual funds and ETFs. Our industry was clearly the recipient of a lot of criticism. This public perception is still widespread and toxic to the alternative investment community, largely preventing younger managers from having a shot to succeed in raising capital.

Creating a culture of compliance for the entire industry. But think about the fact that the largest growth area of every major brokerage firm and bank today is compliance. These organizations are losing the people who generate revenue, and replacing them with a huge cost structure that adds nothing to the bottom line. They have to ensure that there is a compliance person reading every Bloomberg terminal and looking at every email, so there is a significant and palpable pervasion of fear in those firms, and it is having a negative impact on employee morale. One of the byproducts is again a higher barrier to entry in our business with counterparties, who are often afraid to take any calculated risks. Some added compliance procedures and regulation are beneficial, but a lot of it is counter-productive and is hurting the financial industry in general, along with growth in the alternative investment business.



Jeff Haas: We are a smaller firm, so we are forced to either bring those compliance and reporting facilities in house and have employees wearing multiple hats, or use a third party. If we choose the former, our staff can get stretched thin, and if we choose the latter it adds to our cost structure. Even if the regulator is trying to do a carve-out, where if you have a fund with a smaller AUM you are not regulated by the SEC, but then you will get regulated by the state anyway. The bottom line is that there is no real way to escape those issues. You have to be prepared to deal with all of these matters if you get into this business.

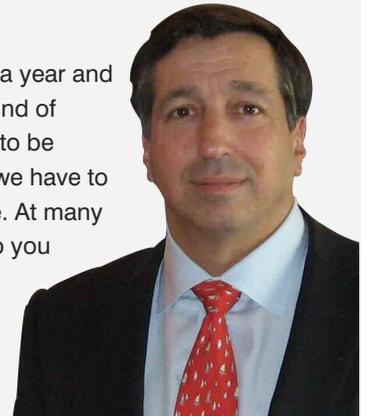


I agree with Mark, in that it is really a shame how much negativity has been directed at the alternative investment industry. Historically, there have been countless smaller funds which launched and became very successful here in Connecticut. It is almost impossible for a lot of the smaller guys these days due to the excessive cost structures and service provider costs. A lot of the seeding platforms that were around in past years have also disappeared, making capital very scarce. It is definitely enormously challenging for the new guys coming into the game.

Mark Fishman: We have a group of people here who are all very successful in their expertise. If you are a good investor, either you worked on the traditional buy side or you worked at a brokerage firm. All of us either traded or were a specialist with quantitative skills, but in either case we developed a defined professional expertise. We decided to live the American dream, which is to open up our own business, and on average I would bet that nobody here is working less than 50 or 60 hours a week, and most of us work on the weekends. As managers, we all take significant risk to open up our shops, we try to bring in people who believe in what we do, and we work extremely hard to succeed. If we succeed, instead of observers recognizing our accomplishment as an embodiment of the American dream as entrepreneurs, where we add to our economy by building companies and employing people, we tend to get demonized.

That perception is amazingly twisted, and people think that because you work at a hedge fund that you must obviously be a billionaire. Last year there were a bit over 800 new hedge fund launches but at the same time almost 700 funds closed. This is consistent with the reality that a high percentage of new hedge funds close up shop within their first few years, so the public really does not know the facts or have an awareness of the reality in our industry. If you succeed you can do very well financially, but we take risk in a market where it is challenging to succeed.

The last time I checked, the President and CEO of Yahoo!, Marissa Mayer, is earning \$37 million a year and is doing a terrible job. I am just curious as to why there is not more of a public backlash in that kind of situation. The point is that there seem to be other places in the economy where you are allowed to be rewarded even if you do not succeed in your job. In our business, that is not the case, because we have to put our reputations and capital on the line every single day, and performance numbers do not lie. At many levels the industry has been demonized as being the root of all evil, but you cannot let that get to you as a manager, because it is something that is out of your control. You just have to keep a good attitude and enjoy what you do, because all of us have a passion for our businesses. That is the advice that I would give to the next generation of managers.



Richard Rankin: I have a few points to add about the current environment and would like to build on some of my fellow panelists' contributions. Jeff's explanation of the consequence of regulatory changes in pushing banks out of small market lending resembles something we have experienced in our business. His point was that in a regulated traditional bank environment, the bank would need to impair their capital at some point to authorize a smaller loan. In our space, as a hedge fund, we carry cash as part of the strategy. Over the past year cash has become a regulatory impairment for prime brokers, effectively a liability on their balance sheet. Consequently, we have been forced to somewhat increase our fund's risk parameters by sweeping cash into another investment instrument, albeit a money market fund.



Again, this is a regulatory-driven outcome which may have been unintended by the lawmakers. Some additional risk gets passed-off to the fund itself and thereby to the underlying investors, amplifying Mark's point about the negative effects of these changes on the brokerage firms and financial industry in general.

I would also add that we have seen a proliferation of liquid alternatives strategies recently, which in some cases, seem to be higher risk products offered to less sophisticated investors. Some of that demand is likely driven by the desire for higher returns, because those returns have not been accessible through other products. Some of these liquid alternative products have gotten so large that the return opportunities, the primary motivation for the shift into these products, have in certain instances, largely disappeared.

Jeff Haas: Another development related to regulatory shift that illustrates the need to fill the lending gap in private credit is the emergence of a number of new players. Some are less well-known, but are issuing debt to both large and small corporate environments. The big banks do still play significant role in the game, but a lot capital is coming from alternative providers. Old Hill is set up as an asset management firm, but there are plenty of other companies that have been set up as specialty finance companies.

To give you some background, we all know that the consumer in the United States lives on credit. Prior to 2008, credit card securitization was a much healthier business. As the banks have moved away from riskier and small-scale lending, the credit card companies have done the same, and pulled back from issuing that type of credit. The result has been an explosion of specialty finance companies that are in the market and offering credit to consumers. We see it on the internet through peer-to-peer lending, and if a consumer walks into a Lowe's or Home Depot they can finance a product for nine months with no interest.

This niche kind of credit strategy is coming from specialty finance companies. They are not big corporations. They are small firms that have popped up all over the private market and thematically illustrate the growing shift from traditional market lending. This is a more permanent shift than people realize. What some market participants describe as the gray market, or non-bank market, is something that is here to stay. Therefore there are opportunities for investors to access a return stream that has traditionally been oriented toward traditional fixed income.



Jason Brandt: I can reinforce Mark's point, because he is spot on with his observations. Since the financial crisis, we have observed a decreasing number of emerging managers and far fewer fund launches because the barriers to entry have become extremely high.

From the fund administration perspective, the regulatory consequences for large financial institutions have forced quite a few banks to divest their fund administration businesses. Additionally, some of the larger independent fund administrators are beginning to more closely examine their bottom lines and weigh the cost versus the profit of servicing a particular fund. This, coupled with increasing consolidation, has caused significant disruption in the market. As a result, you are seeing the largest players getting bigger because they have the infrastructure in place that will allow them to continue to invest into their businesses. At the same time, some administrators are becoming more selective about the size and level of activity they need to see before engaging with a fund and have been forced to shed at least some of their small to mid-size clients given current market dynamics



For the smaller service providers, and by smaller I mean those that are in the US\$20-30 billion assets under administration range, it is difficult to continue to investing in infrastructure to keep up with regulatory and reporting changes. Transparency and operational due diligence demands from investors, which are now requisite services for a fund administrator, require huge investments so a lot of the smaller players are being forced to exit the market.

Fortunately for some of the smaller funds and new launches, there is a growing segment of mid-sized fund administrators that can provide them with high levels of service at a lower price point to support their entry into the market. In order to do that, you are going to have to make an investment into those client relationships at an early stage. We are happy to do that to help managers when they are getting started because we recognize the challenges that they face and realize that a minimal fee structure will hopefully help them to survive and grow their funds. As an administrator that provides a comprehensive core offering that can be customized with other ancillary services, we are also able to readily support a fund as it grows and evolves.

Greg de Spoelberch

Mark mentioned the rate at which funds shut down within the first year, and it is extremely high. How do you make a decision whether you are going to actually work with a fund, and invest that time and energy when they are starting out? What are the parameters that you examine when making that determination?

Jason Brandt: When individuals and teams are launching they are not going to have a deep pool of capital so it's important to consider a number of factors that can determine if they have what it takes to survive. We primarily assess the fund's historical performance and whether that performance is transferrable and if they are able to validate their ability to generate returns. Portfolio management experience is clearly a critical indicator of a manager's ability to succeed but most of the time managers are no longer simply running a portfolio. They are managing the business and everyone and everything that falls under that umbrella. Consequently, we have to screen for their business acumen and whom they will align themselves with in their third party outsourcing, including prime brokers, audit firms, law firms or outsourced compliance providers. All of those factors come into play because they determine the likelihood of long-term survival and success. Once you consider all of those components you are forced to take an educated guess when you forecast a person's success rate.

I often hear that a fund is going to launch on day one with US\$100 million, but then they end up launching with US\$50 million or less. It is very difficult to find that initial capital so you really are invested in their ability to survive, perform well and eventually grow. They need to have a strong business acumen and forward-thinking approach coupled with all operational and growth parameters modeled correctly in order to succeed. We work with the funds who we believe take all of those elements into account.

Generally, we will make that investment for the first year and after the first year we revisit the situation. We have to look at how much capacity they are taking from our teams and how often they are looking to us for consultation on various matters. We spend significant time with them reviewing how they have performed in that first year and that review process continues year over year where we often have to assess the fee structures.

Sometimes we must have those difficult conversations of whether or not we are going to bear the cost of the increase in our fees or if a manager is going to have to bring on somebody else internally to help the business move forward. Although we have discussed quite a few challenges for this next generation of managers, the environment as a whole does not have an overwhelmingly gloomy outlook and there are still a lot of good success stories out there.



Mark Fishman: Jason is right, but even if these managers do a good job it can sometimes be impossible for them to survive. Let's say a manager starts with \$15 million and makes 10% or even 20% in their first year. Most of the money that they make obviously gets returned to the investor. Then you have the cost associated with all of the regulatory elements you have to cover. There is no way that a manager with \$15 million and a 20% return in their first year can pay their bills. I am glad there are some service providers out there who recognize the environment and are facilitating the ability of these managers to continue to operate.



I will reiterate that the industry needs to be regulated, and we need to protect non-accredited investors. But the reality is that we have the interesting problem of who the regulators turn to for their expert advice. They look to the largest fund managers with the deepest pockets, and who have the most specific interest in perpetuating the status quo. Remember that Fannie Mae was the largest contributor to Super PACs before the 2008 crisis, and no one costs the government more than Fannie Mae. If you are a regulator, you have to start thinking about who the advisors are, what their motivation is, and how you are being helped. You have to protect Main Street, but you also have to be able to help keep the capitalism alive in the United States.

Greg de Spoelberch

Mark mentioned the concept of capacity, and how smaller funds can be more nimble and potentially more likely to outperform the market. What do you see as your capacity over the next year, or within the next few years? What is the number and how do you determine that?

Brett Houghton: From the insurance risk investing perspective, we have been either closed or soft closed essentially since existence when we originally launched in 2001. We had a couple of very large pension clients who were on-boarded in 2003, which was early in the lifecycle of the firm. As I mentioned earlier, they effectively bought our capacity through the 2009-2010 timeframe.

When we launched the commingled funds, we realized that you have to be very careful in a commingled fund environment, because if you have a strategy which is cyclical in terms of when you can deploy capital but you leave the fund open to investor flows, it can be very damaging to returns. This is particularly true if you are forced to hold cash for any meaningful period of time, because if you are a 500 basis points-over strategy like we are, those investor flows can really chew up your returns. To combat that problem, we manage investor inflows very specifically and very precisely, and only look to bring in capital during periods of time when we know we can deploy it effectively.

The new issuance in the insurance space is highly cyclical, and is focused around the end of the year and also in the April through June time frame before the annual start of hurricane season. Outside of the large issuance periods, if you get a big inflow you have to buy bonds in the secondary market, and people see you coming a mile away. We like to be on the other side of that trade, selling rich bonds to counterparties when they get investor inflows and are more desperate to deploy capital.

We have indeed lost numerous mandates over the years because we have refused to take money on an investor's timeframe. We have to be very disciplined about enforcing our own time frame for when we can take in money.

That being said, we do scale up as the market grows, and the good news about the insurance risk market is that people are migrating to the coasts at a very rapid pace, particularly in the United States. That means you are seeing a lot more real estate growth and development. As you guys know by now from our discussion, given the financing that you need to build these



developments on the coasts in these catastrophe prone areas, insurance is a critical component.

Looking at the numbers, the growth of these areas and demand for catastrophe insurance actually causes the peak peril loss making potential of catastrophes in the insurance industry to double once every 10 years. That is about a 7% compound growth rate, but the capitalization of the industry overall is only growing at approximately the rate of GDP. That means there is a huge gap that continues to grow, and that gap has driven growth from merely a cottage industry of about a billion dollars of total invested capital back in the late 1990s, to a \$70 billion AUM industry today.

We expect that compound growth rate to persist over the next 10-20 years. In summation, we expect these trends to continue, so our capacity remains at good levels. We just have to be very careful in terms of how we manage it. As I mentioned, AUM currently stands at \$5 Billion and should grow quite a bit over the next 5-10 years, but we have to manage that pace so we're able to deploy capital in a responsible way.

Craig Melcher: In terms of capacity for our strategy, our investment universe is about a 1,000 companies. The equity market cap of those companies is in excess of \$2 trillion, so we see very significant opportunity set and room for growth.



We often have investors asking about the scalability of the activist approach to our sector. We have been effected change at companies in that range in size from a \$500 million market cap to over \$10 billion market cap companies. We see opportunities to unlock value at a wide range of size of companies. A larger AUM would allow us to have larger percentage stakes, and when it comes down to a proxy contest, if we own 6% of a company versus owning 1% of a company, that means we have 6% of the vote that we know will be in our favor. A bigger size would allow us to be more effective winning the ultimate vote.

Mark Fishman

Is there a size at which you could get too big, so that the process of changing positions becomes more cumbersome rather than nimble?

Craig Melcher

Our AUM is currently north of \$200 million. Within the real estate space, some of our peers have been successful managing \$1 to \$2 billion. We think that for our business, an optimal next step would put us in the \$500 million to \$1 billion range. We would then seek to ensure that we can generate attractive returns for investors before revisiting the appropriate fund size.

Richard Rankin: Capacity for our renewable energy strategy at \$400-500million is somewhat limited, and for good reason. We believe that our returns would begin to diminish over that. We have liquidity parameters and concentration limits and do want some of the smaller cap names in our portfolio, which have solid growth potential, to move the needle. We are very careful and thoughtful in finding balance between reward and risk to obtain optimum results. At a larger size we would not be able to do that as effectively, so \$400-\$500 million is the limit.

Although renewable energy generates about 20% of global electricity, the aggregated market capitalization of all renewable energy companies versus the aggregated market capitalization of conventional energy companies sits at less than 5%. There is a significant arbitrage opportunity to establish market value parity between renewable energy and traditional energy based upon energy produced.



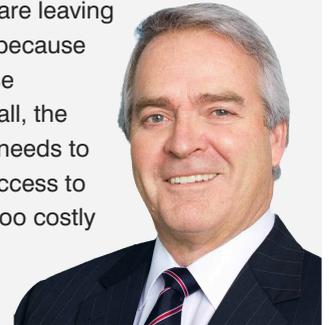


Mark Fishman: Although we are closed right now, we would cap our fund at \$2.5 billion. I have managed larger funds in the past, and from my experience I think that is the optimal size for a liquid credit fund. To reiterate my point from earlier, at some point you have to stop listening to the sirens screaming for more AUM, because you end up having to manage the portfolio very differently to accommodate for your size. You start leaving way too large of a footprint in the market with your trades. During periods of stress, it also becomes very difficult to maneuver the portfolio. If the fund is too large, even though you we are trading liquid products, you are moving the market too much in individual positions. Maintaining our liquidity and Sharpe Ratio are priorities for us, so \$2.5 billion is the point at which we would cap our fund.

Greg de Spoelberch

Connecticut is often compared to Silicon Valley in terms of the number of hedge funds here, and there is indeed a lot of credibility to this region. Do you find regional advantages in accessing investors or staffing your firms with talented people?

Richard Rankin: We are actually seeing a migration out of the state by a number of managers who are leaving for personal tax purposes. Connecticut really began to grow as a hedge fund center here in the US because of the favorable tax advantages when the industry was initially established about 25 years ago. Those competitive advantages, from a tax perspective, have begun to wane for successful principals. Overall, the region is still a hotbed for smaller start-ups and very attractive from a lifestyle perspective, but there needs to be some reconsideration by the state government if it wishes to encourage growth in the industry. Access to exceptional intellectual capital both locally and from New York is a very attractive element but if it is too costly to operate here managers, and a lot of wealth, will leave the area.



Mark Fishman: I agree with all of Richard's points. UBS had moved to a big facility out in Stamford, and in the last few years they met with the Mayor and the Governor because they wanted to stay in Connecticut. They were told that every effort would be made to help them, and to prevent them from leaving. We now know that the UBS building has only one floor that is filled, and even that will soon close down. The inability of the State of Connecticut to generate taxes from other sources has led them to try to aggressively tax much of the financial industry and other businesses. GE and UBS are leaving soon, and a lot of other major companies are starting to shift their focus to other regions.



From a lifestyle perspective, professionals in our space would much rather be in Connecticut than New York, and they can still reap the advantages of being close to the metro area. New York is the financial hub of the United States and is one of the three primary hubs globally, so you have experienced market professionals and access to that talent. The flow of customers in and out of New York makes it far easier to access investors as well.

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