OPALESQUE

Opalesque Round Table Series '11

NETHERLANDS

Editor's Note

Welcome to Opalesque's first Netherlands Roundtable!

Amsterdam is unique in that its financial history dates back to early-17th century, when equity trading was invented. According the Holland Financial Centre, a public-private organization, the financial crisis has offered a chance for the Amsterdam Metropolitan Area to regain a lead that it had lost, especially by offering added value in the form of skills and expertise. One of which can be found in pension fund management services, others come in the shape of financial logistics and sustainable financing.

And of course, there is the nascent hedge fund industry, which now claims more than 30 single hedge funds, and for which the country created an accommodating vehicle, namely the FGR (fund for joint account). Dutch hedge funds, which manage approximately $20bn in mostly long/short equity (HFN) and managed futures strategies, are subject to the ordinary rules relating to investment institutions. And Dutch taxes are easy – also for expatriates.

The Roundtable, which gathered some of the industry's most esteemed members of the local hedge fund industry, gives us a complete portrait of it, including the popular strategies, fund structures that are in demand, initiatives done for emerging managers by seeding platform IMQubator, investor-bases, the relationship between pension funds and hedge funds, and the regulatory environment.

For example, find out why:

The environment has become worse for Dutch pension funds to invest in hedge funds
The pension fund boards need to fully understand the strategies, regulators tend to classify hedge funds as riskier than equity, and pension funds have become short-term investors.

The Netherlands is a very favourable fund domicile and few know about it
Fore example, the 2007 Financial Markets Supervision Act provides the regulatory environment in which the investment manager, not the fund, needs a license – which means hedge fund managers can launch several funds without needing to license them. The country also has a friendly tax regime for investment funds.

The participants
- **Wouter Ten Brinke,** Theta Capital Management
- **Ivo Jenniskens,** Providence Capital
- **Mark Baak,** Finles Capital Management
- **Willem de Vlugt,** Evaluation Capital
- **Jeroen Tielman,** IMQubator
- **Robert Vennegoor,** Custom House Fund Services (sponsor)
- **Dr. Randolph Roth,** Eurex (sponsor)

also discuss:
- The demand for tailor-made products
- The challenges encountered by funds of hedge funds
- Hedge fund managers' reaction to the current market uncertainties
- What is being done to preserve and to raise capital
- The Dutch fund structure known as the FGR
- Amsterdam's place within the changing regulatory environment
- Who is affected by ongoing market regulation initiatives such as MiFID, MIFIR and EMIR
- The misconceptions about what a financial transaction tax could do
- Amsterdam as a happy place for foreign finance professionals

The Opalesque Netherlands Roundtable took place October 2011 in Amsterdam and was sponsored by Custom House and Eurex.

Enjoy "listening in!"

Benedicte Gravrand
Senior News Editor, Opalesque Geneva

Cover Photo: Blooming tulip fields in Holland

Participant Profiles

(TOP TO BOTTOM)

Dr. Randolph Roth, Willem de Vlugt, Wouter ten Brinke, Mark Baak

Benedicte Gravrand, Jeroen Tielman, Ivo Jenniskens, Robert Vennegoor

Introduction

Willem de Vlugt
EValuation Capital Management

My name is Willem de Vlugt and I am managing partner at EValuation Capital Management. We manage the EV Smaller Companies Fund, a €70 million long/short equity fund with a focus on Benelux and German small and midcaps. The fund is long-biased, has a stock picking approach and was started about five-and-a-half years ago. Since inception the fund has generated a return of 53% with an average net exposure of 50%.

Mark Baak
Finles Capital Management

Mark Baak, I am the Head of Portfolio Management at Finles Capital Management. We select hedge funds and focus on professional investors like insurance companies, private banks, wealth managers, family offices and pension fund. Finles Capital Management was founded in 1977 and we currently offer tailor made hedge fund solution, hedge fund consultancy and fund of hedge funds.

Robert Vennegoor
Custom House Fund Services

My name is Robert Vennegoor, I head the operation of Custom House Fund Services in the Netherlands. Custom House Fund Services provide independent fund administration and Depositary services to 540 alternative investment funds and sub-funds, throughout the world.

We are a true global player with centralized computer processing and seven operations from Chicago to Singapore, covering 18 hours 5 days a week. This allows us to always provide our services in time and also assures business continuity if something happens, wherever in the world.

Also, we provide project management and hands-on support and assure as such the smooth set-up and (re-)structuring of investment funds.

Wouter ten Brinke
Theta Capital Management

Wouter ten Brinke, Managing Partner at Theta Capital Management. We manage about $600 million in a range of three funds of hedge funds and managed accounts, based in Amsterdam, Netherlands. We are celebrating our 10th anniversary this year.

Jeroen Tielman
IMQ Investment Management

My name is Jeroen Tielman. I am the Founder and CEO of IMQ Investment Management which is the manager of the IMQubator Fund. IMQubator is a seed investor in hedge funds set up by experienced investment professionals who just have started their own investment management company. We have €250 million in assets under management from APG. We have made eight commitments so far and two to go, and are currently raising additional capital.

Dr. Randolf Roth
Eurex Exchange

My name is Randolf Roth. I am Head of Market Structure at Eurex Exchange.

Ivo Jenniskens
Providence Capital

My name is Ivo Jenniskens. I am an Investment Manager at Providence Capital. Providence Capital is a multi-investment office for ultra-high-net-worth individuals, charitable foundations and endowments. We focus on fiduciary asset management, investment consulting and family office services.

Benedicte Gravrand **Could you tell us about the investment opportunities that you are seeing at the moment.**

Willem de Vlugt We focus on Europe and more specifically on the Benelux and Germany.

In the longer term perspective we believe equity valuations are currently very low, in particular in Europe which is trading at a Price/Book of below 1 versus the U.S. at 2. Most fund managers are underweight equities and within that, underweight Europe. If politicians manage to create some stability going forward, then it is quite obvious Europe is where allocations should increase.

Willem de Vlugt

I see many good opportunities in our geographical focus area going forward.

Mark Baak We expect that the markets will remain unstable and volatile for the foreseeable future. In an environment like that we prefer hedge fund strategies like global macro, managed futures and trading oriented managers. We are also advising our clients to shift part of their long-only equity exposure to long/short equities funds to lower risk. Willem's fund is a good example.

Wouter ten Brinke As an investor in hedge funds and from a top-down perspective, we would be most bullish on credit-based strategies for one, because they tend to do well in weak growth environments. But we are seeing more dominance in both the corporate credit side and within asset-backed securities. On the structured credit side, there are tremendous opportunities for skilled long/short managers. Looking at the regulatory influences on both these markets, hedge funds are particularly well suited to eventually, on a two or three year period, take advantage of these opportunities from the long/short perspective.

So credit, distressed ABS, distressed corporate credit, and trading strategies are the main opportunities.

Jeroen Tielman Now is really a buyer's market for seeders investing in emerging manager hedge funds.

There are a lot of talents coming to the market right now and there is still scarcity of capital. So this is the right moment as an investor to get exposed to this market segment. It is also a good time to align interests between investors and hedge fund managers; the seeding stage is the best moment in hedge funds' lifecycle to get these interests aligned.

Jeroen Tielman

In general, despite the slightly negative sentiment around hedge funds, this is a good time to look at skill-based asset classes and absolute return asset classes that hedge funds represent as an alternative to long-only investment strategies.

Dr. Randolf Roth We experience some volume increase based on the current high volatility. For us, as a financial derivatives exchange, the most exciting asset class is probably volatility derivatives, which proved to be a useful risk management tool when the market started to drop.

As we are as well the leading marketplace for European fixed income derivatives, we closely observe the developments of the European bond markets and in particular most recently the Italian bond market as the Eurozone's government bond spreads may continue to widen because of credit issues. Based on these developments, we recently extended our fixed income offering by launching Euro-BTP Futures covering all available terms.

Dr. Randolf Roth

Ivo Jenniskens

Within the hedge fund space, we are looking primarily at global macro, already mentioned by some here in the panel. In general, insurance is becoming very expensive and risk is becoming cheaper. But if you look at long-term equity valuations, take the Schiller P/E, equity is still not cheap. We do however use shorter term indicators for trading opportunities around the long term view. In the credit markets, high yield spreads are widening and becoming an opportunity in our view.

Benedicte Gravrand

What is the outlook for your own strategies or the strategies that you deal with? Are you planning on starting new products?

Willem de Vlugt

We only manage one fund and I do not see that changing in the near future, so all our efforts go into executing our long/short strategy.

I am optimistic about the outlook for our fund. From an investment perspective, we are quite happy with the names we have in the portfolio, which should also do well in a low growth environment. At the moment it is all about capital preservation and managing risk in a macro dominated environment. As stated before, if politicians succeed in creating some form of stability, we can focus on fundamentals again.

With regards to growing the assets under management I am optimistic as well. When investors consider a long/short fund or any other type of fund, investors will look at how the fund performed in 2008 and now also how it performed in 2011. Asset gathering should become easier if a fund passes both tests. Our fund has done well in preserving capital in 2008 and so far this year as well. Should inflows accelerate then we will start thinking about soft closing the fund.

Mark Baak

We expect inflows into hedge funds in general will continue.

We are also seeing more demand from professional investors for tailor-made products or tailor-made solutions. The tailor-made solutions may not come as traditional fund of funds, but as mandates or as a tailor-made hedge fund search or as hedge fund consultancy.

Mark Baak

Robert Vennegoor

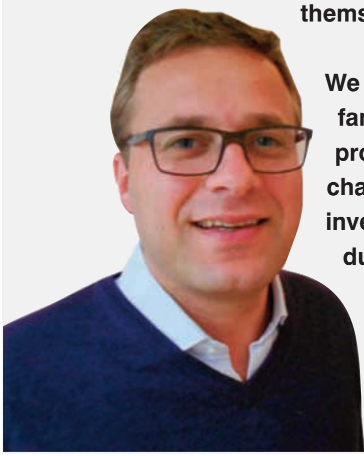
Custom House focuses on providing full administration to about 540 investment funds and managed accounts of all strategies and all over the world. We continuously invest in our systems, in our business processes and in our staff to become the best alternative investment fund administrator of the world.

Apart from that, we a develop value added services with a focus supporting the risk management function. We already provide asset verification services, collateral management services, and also do shadow accounting in this respect.

Wouter ten Brinke

We have no specific plans to launch new products in the near future.

We run a couple of fund of hedge fund vehicles and the current sentiment is fairly biased against hedge funds and it is even more biased against fund of hedge funds. That means that fund of hedge fund managers will just have to prove themselves and attribute their added value a lot more than they have done in the past.



We have been running managed accounts or customized portfolios of hedge funds for our family office clients for ten years now. So, the system that we have is very well suited to provide the breakdown of the added value that we deliver. This will be one of the main challenges for the fund of hedge funds industry going forward. Whether that means that investors go into the managed account route, pick their own funds, and leave the operational due diligence to others or whether they go through UCITS vehicles or any other type of structure, the fund of hedge funds managers will need to prove their added value a lot more and they will need to be able to adapt to such an environment.

Wouter ten Brinke

Over the past two, three years we have been seeing a lot of organizations that have not been able to adapt to the new situation, but I am pretty confident that in the next two or three years, we will see a couple of survivors who will turn out to be quite strong in that area.

Jeroen Tielman

As far as expected returns are concerned, several sources of research, including a recent study we have made, indicate that emerging managers when compared to mature hedge fund managers have an outperformance on average of 200-300 basis points. Barclays did some research this year indicating an even a higher outperformance.

We strive for capital preservation. This year certainly is a test. At the same time, we have a long term return objective of 700 basis points over EURIBOR excluding seeding and asset raising economics.

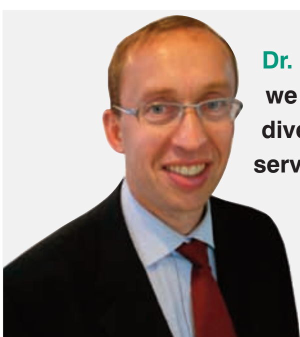
When we seed a fund we typically invest $25 million, commit with a three-year lock-up and take a 25% stake in the management company of the emerging manager.

We want close our current fund to new investors around the end of this year. We aim to get an additional $100 million in our current fund which we will use as acceleration capital, meaning that some of our existing managers will get an additional ticket in return of us getting some additional equity.

In 2012, we want to set up our next fund.

Jeroen Tielman

The other thing we are working on is a collaboration network of specialized placement agents, as we feel that emerging manager funds need assistance with fund raising, as the fund raising climate is very difficult.



Dr. Randolf Roth: Our focus regarding our product and service offering is twofold: on the one hand we aim to increase our offerings at the exchange level to provide investors appropriate and diverse investment opportunities. On the other hand, we are increasing the efficiency of our service offering on the clearing side.

To mention two examples: first, we rolled out the initial phase of our client asset protection model. Client asset protection allows for greater transparency and legal safety on the treatment of client positions and pledged assets in the event of a clearing member default. In

the current phase, we are targeting Non-Clearing Members. In a next step, we are addressing mainly the buy side needs i.e. those firms which are not members.

Second, we will be introducing Eurex Clearing Prisma - a new portfolio based risk and margin calculation methodology - which will raise the benchmark of adequate risk assessment of our members.

In terms of products, we focus on meeting the G20 goals regarding the extension of central clearing to a broader range of OTC products.

So, while we continue to list new products for trading and extending our clearing service offering, one main push is about expanding the CCP clearing offering to standardized OTC products such as interest rate swaps.

Ivo Jenniskens We manage for our clients a highly diversified portfolio of liquid assets - so not only fund of hedge funds.

But we are looking to increase our hedge fund exposure this year or the beginning of next year.

We have always demanded very high transparency with respect to the underlying funds. In addition, we are currently working with our fund of funds managers on factor analysis. We want to know in advance how the managers expect their funds to behave in certain market environments. It is still quite new for some of them, so we work on that together.

Ivo Jenniskens

Outside hedge funds, we have a very substantial cash position. The areas we are looking to increase our exposure to are emerging market debt, local currency, high yield bonds (which I mentioned earlier), and also commodities after further corrections take place.

Benedicte Gravrand **A lot of you have mentioned concerns with capital preservations and capital raising. What is being done to preserve and to raise capital? Do you see trends that hedge funds are following to do so, such as more transparency and lower fees?**

Willem de Vlugt: To preserve capital, we lower both our gross and net exposures. In particular in the last few months we lowered our gross exposure too as fundamentals do not play a role whatsoever and it is purely macro and sentiment/momentum that drive the stock markets. For us, this is not an environment to invest in with high conviction and we therefore wait until the moment we can focus again on the fundamentals.

Capital raising at this moment is difficult, but it is purely down to the market environment. Although timing is less important when investing in long/short funds specifically, investors in general try to time it anyways and wait for a more favorable moment. The performance of hedge funds have shown that, in spite of 2008, timing is less crucial to overall performance. Although we continue to see inflows, we expect them to accelerate as soon as the stock market environment becomes more stable.

Mark Baak

When it comes to capital raising, I agree that transparency and providing information are of great importance to get there.

I have never met an allocator who became more negative when he spent a lot of time on meeting hedge funds and knowing more about the hedge fund world. So for us as hedge fund selectors, that is the biggest task.

As for capital preservation, a lot depends on the mandate. If the mandate is to outperform the equity markets then you could allocate to long/short equity funds with a variable net-long or to long-biased funds like Willem's fund. The goal of these funds is not to preserve capital in every single time frame but to minimize the downside as much as possible. When you are down 4% like Willem's fund is, in an environment when the European equity market is down 15 to 20%, this is very attractive for investors (as an alternative to long-only equity investing). By limiting the downside to a maximum of one-third of the market and targeting two-thirds or more of the upside of the market, the expected return in substantially higher for long/short equity compared to the equity indices. The shift from long-only equities to long/short equities will be one of the most powerful moves allocators will make in the years to come.

Mark Baak

When a client has a very strong focus on absolute returns, it is important to make specific strategy and manager calls. One of our clients, a single family office, gave us such a specific mandate and we have been successful in achieving the set goals. While the broad hedge fund market is down about 5% this year, the mandate we manage is up +5%. So the mandate's requirements are also very important for preserving capital.

Robert Vennegoor

Following a number of fraudulent incidents during the credit crunch and in anticipation on the EU AIFM Directive, in our capacity as Depositary we have noticed an increasing demand for our independent oversight of the compliance of the investment management process with the Fund documents. Besides, the Boards of the Dutch pension funds more often seek independent oversight of the collateral management and of the fund accounting and valuation process.

Custom House has a sizeable and independent Depositary activity that by nature provides these oversight services and as such attributes to more transparency at investor level and to more control over the investment management process.

Wouter ten Brinke

It is a very challenging environment to raise capital for the whole hedge fund industry, even more so for the fund of hedge funds industry.

Luckily we have been able to get some fairly decent gross inflows this year, around 20% of starting year AuM. However, some of that went in our new fund. All the other assets have almost exclusively come into tailor-made products. We are currently working with a couple of larger investors to set-up a new product which effectively gives the investor a bit more discretion and leeway; the investor can on a discretionary basis select specific hedge fund styles and strategies, and at the same time effectively outsource the whole process of investment, due diligence and operational due diligence to ourselves.

This is just another reflection of the increased demand for transparency and control that investors are demanding. It is more on the portfolio construction side rather than the operational side (within managed account platforms); and I expect products and services like this will continue to develop going forward.

Wouter ten Brinke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Jeroen Tielman For hedge funds to raise capital in this challenging climate, they must show investors that they respond to their needs and therefore get better aligned. Greater transparency about risks and liquidity are two of the needs we frequently hear being mentioned by investors.

Emerging managers, have some increased operational risks in the first year of operation and we are reducing this risk by having them locate in the same office as where we are located in order to do a better guiding and monitoring.

Liquidity needs to be synchronized so that the liquidity promised by the fund matches the underlying liquidity of the investments. As a seeder, we want to see full transparency and clear communication about that by the investment manager.

Jeroen Tielman

So in summary, capital raising is important for new products to address some of the design flaws, and hedge funds should be very clear about what they promise to their future investors.

Ivo Jenniskens From our perspective, capital preservation is achieved through broad diversification. Apart from hedge funds, we also allocate to cash, bonds and other asset classes. Even in 2008, when people said diversification did not work, the interest rate on cash deposits with Dutch banks was still 5% and Eurozone government bonds returned more than 9%. So, there were definitely places to hide and preserve capital.

If we look specifically at the hedge fund exposure, I fully agree with Mark that it depends very much on the reason you are buying the hedge fund exposure for. If we buy it as a substitute for equity long-only, of course there is a certain sense of capital preservation, but that is not the main aim. When markets go down, as in 2008 when equity markets went down 40% and equity long/short funds lost 20%, then that is still seen as protection. But on the other hand, we have some very conservative funds of hedge funds which are still making positive returns so far this year.

As an allocator, we very much look for alignment of interests, when the manager has "skin in the game". Other obvious things are transparency and underlying liquidity in combination with the liquidity provided to us and, of course, independent operations where tasks like administration etc. are all separated from the investment manager.

Ivo Jenniskens

Benedicte Gravrand **The Dutch pension fund industry has a great reputation, and manages around €700 billion. How tied is it to the hedge fund industry? Do pension funds invest in hedge funds, do they invest in Dutch hedge funds? If they do, what do they want? If they do not, who invests in Dutch hedge funds?**

Ivo Jenniskens From what we have experienced with a pension fund as one of our clients, the regulatory environment in the Netherlands is not very positive for pension funds to invest in hedge funds.

This pension fund was invested in hedge funds. Despite the fact that they outperformed the markets, including in 2008, the pension fund had to sell almost its entire hedge fund exposure because the regulator, the Dutch Central Bank, sees hedge funds as a higher risk than equity. Pension funds have to keep more collateral for hedge funds, it weighs heavier in their risk budget than for equity. The regulator says to those who are invested in hedge funds, "we do not know what these hedge funds are exactly doing" and the pension fund should know that. For smaller pension fund Boards it is almost impossible to have enough knowledge.

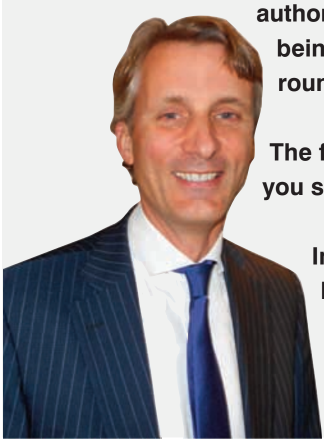
Ivo Jenniskens

If you do not have sufficient know-how internally, you have to hire a separate risk management company to monitor the hedge funds risk exposure in addition to the fiduciary manager who does the allocations. The additional monitoring leads to another layer of costs. Our experience is that the environment has become worse for pension funds to invest in hedge funds in the Netherlands.

Jeroen Tielman I agree with most observations there.

There is a bifurcation as far as pension funds are concerned. The largest pension funds continue with their exposure and slightly increase their exposure in hedge funds in general.

The other pension funds are very hesitant with any increase in exposure to hedge funds. Part of that is not only the regulatory aspect, but also the governance aspect. The highest level of decision-making unit within the pension fund consists of trustees, who are, as required by law, representatives of the employer and representatives of the employees. They are not necessarily specialists in alternative investing. They have to approve the investment strategy of the pension fund, which is prepared by professionals and the CIO. Trustees feel the pressure from the regulatory authority for being more in control, and the effect of all this is that the investment strategy ends up being adjusted to the capacity of the trustees, whereas it should obviously be the other way round.



The funny thing is that the opportunity costs of not having the exposure in hedge funds – which you should have – is not being measured and people are not being held accountable for that.

In addition there is a challenge for the hedge fund industry in general to present itself in a better way to the general audience and show that managers are not opaque or greedy or totally after their own interests.

Jeroen Tielman

Mark Baak Parts of the Dutch Pension Fund industry are very sophisticated and experienced hedge fund investors. The biggest pension funds have internal teams that are dedicated to hedge fund selection.

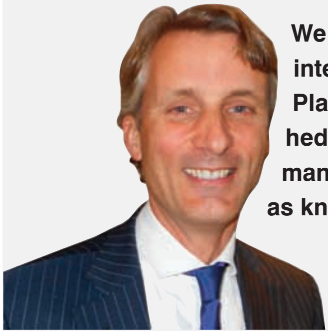
Given the fact that most of the 31 Dutch hedge funds are not big enough to accept €50+ million tickets, they usually don't have big allocations from Dutch pension funds as these pension funds are conservative when it comes to investor concentration. But a big fund like Transtrend (AuM of about $10 billion) probably has several Dutch pension funds as investors. AEGON spin-offs Saemor and Pelaros are big enough to absorb larger allocations and have an institutional infrastructure and background. So I would not be surprised to see Dutch hedge fund allocations for these funds this year as well.

Mark Baak

The smaller Dutch hedge fund typically receives allocations from insurance companies, private banks, wealth managers, (single) family offices and High Net Worth individuals.

Benedicte Gravrand **Who are your investors, Jeroen?**

Jeroen Tielman Currently only APG. As our next investors we see insurance companies, sovereign wealth funds and for example family offices in Europe and the Middle East.



We do not have contact at this moment with U.S. pension plans, but several of them are interested in the space we are operating in. Recently for example, the Massachusetts Pension Plan announced that it would like to have an exposure of between 5% and 10% to emerging hedge fund managers (that was one of the first few concrete examples I saw where emerging managers are recognized as a separate asset class). They are further ahead of the curve as far as knowledge is concerned.

Jeroen Tielman

Also, in the Far East and in China, I see an interest for specialized hedge fund products.

Wouter ten Brinke

About Dutch pension fund activity in hedge funds, I agree with the two former speakers about the Boards needing to be in control, i.e., needing to understand what they actually invest in, which makes a lot of sense before you make any type of investment. But it has been a very important driver.

Probably this is driven or is driving some of the interests that we are seeing in our new pool structures, which effectively means that some of the pension funds are looking at hedge funds not necessarily as an asset class with an overall absolute return objective. Pension funds look at hedge funds as an alpha engine within their traditional asset classes. The way that we have responded to that is by giving these investors access to our long/short managers, for example. The whole pool of long/short managers has about 15, 16 single hedge funds. Pension funds can allocate into this pool from their equity allocation, as opposed to either deciding whether to take it out of their fixed income or equity allocation for example and invest in hedge funds as an asset class, because they want alpha within an asset class.

It has been a discussion over the past 10, 15 years in the hedge fund industry, but we are seeing some tentative moves into this area and this is driven by the desire to understand more what hedge funds really are and what they do.

My second remark about pension funds in the Netherlands investing in hedge funds is that I have observed that the investment horizon of pension funds has shortened significantly over the past couple of years, to a large degree due to regulations.

If you, as a pension fund, need to have a 105% funding ratio and you have a shortfall below that ratio of 105%, depending on what your relationship with the regulator is, you probably have between one, two or three years to come up with a recovery plan. That effectively makes pension funds short-term investors.

Wouter ten Brinke

I have spoken to various pension fund CIOs, and one of them six months ago said publicly that as one of the larger pension funds, she had now become a short-term investor.

Clearly, this type of regulation does not support a long-term view in any kind of asset allocation. So, as a result I would expect a lot of the pension funds would be fundamentally constructive towards hedge funds; they have not done anything or will not do anything precisely because the regulator does not allow them to take a medium-term timeframe, beyond two, three years.

Benedicte Gravrand **Who are your investors?**

Wouter ten Brinke

We have been in business for ten years. I would say three-quarters of our investor base is Dutch-based, one-quarter is Switzerland plus UK. We are increasingly going outside of Holland and within Benelux.

We are building a little bit in Germany, although that brings with it specific challenges in the hedge fund arena. Our investors are still predominantly Dutch. Going forward, we will focus on a lot more than we have done over the past five years on the Dutch institutional arena, whether it be pension funds, insurance companies or larger institutional asset managers.

Robert Vennegoor

We attend approximately fifteen meetings of institutional unit holders in investment funds each year. Following the weak financial markets and the regulator's demand for more control during the past years, Dutch pension fund managers certainly have become more cautious in their investment process; their appetite to allocate to hedge funds is little at present.

On the other hand, I have seen a very positive development in the further professionalization of the people that represent pension funds at these meetings over the past 2 years. Moreover, the Dutch pension fund sector consolidates rapidly. These developments will impact the capabilities in a positive way and eventually the appetite to invest in more complex fund and asset classes.

Apart from this, we should not forget that there also have been pension funds that just have continued to actively manage their hedge fund exposures over the past few years. For example, the Dutch second largest pension fund, PGGM (managing around €142 billion in assets) is in the process of concluding the restructuring of its allocation to fund-of-hedge funds. It now invests directly in hedge fund and takes responsibility for the selection and monitoring of its own hedge funds investments.

Robert Vennegoor

Mark Baak

At Finles, we focus on insurance companies, (single) family offices, private banks, wealth managers and pension funds.

When we look at pension funds, we see most of them are well equipped to invest in hedge funds; especially the bigger ones who have dedicated teams selecting hedge funds.They know what they are doing and have been doing it for quite some time. I do not expect that to change.

Most smaller pension funds don't have dedicated hedge fund selection teams as yet. Investing in fund of funds is a solution for them, or using managed account platforms to outsource some of the due diligence tasks. They can also use other forms of outsourced due diligence and consultants. So the tools are available, it is up to them how to use them.

We are talking about the asset side at the moment, but for pension funds, the liability side is obviously why they are forced to have a short-term focus. Especially with the swap curve moves we have seen last year and this year. To make sure that pension funds can let go this forced and extreme short term focus to some extent, the liability side needs re-thinking. An alternative to the daily swap curve could be a fixed discount rate or something like a 5 year moving average.

Mark Baak

Willem de Vlugt

About what Wouter said on the coverage ratio, the whole system forces pension funds to sell low, as they are forced to sell equities when the coverage ratio decreases, and buy high, when coverage ratio increases following stock market rallies. So they really need to get their knowledge about hedge funds up to speed, as timing is of less importance with hedge funds and therefore offer a solution to their problem.

Due to our size of €70 million, we currently have no pension funds as clients, our investor base is mainly comprised of families, family offices, wealth managers and high net worth individuals.

Benedicte Gravrand **With regards to regulation, a lot is changing in the European Union as you well know. How are you preparing for those regulatory developments? Could you also tell me about the Dutch regulatory system?**

Robert Vennegoor I am not a lawyer or tax advisor and a Fund may want to seek the professional advice of an advisor but I believe that it is generally accepted among Dutch lawyers, tax advisors and auditors at the Financial Mile district (the 'ZuidAs') that the Netherlands represents a very favorable fund domicile. Few investors and investment managers outside the Netherlands know this.

In 2007, the new Financial Markets Supervision Act was introduced in the Netherlands and replaced legacy laws with a modern regulatory framework.

This Act provides the regulatory environment in which the investment manager - instead of the fund - needs a license. The implication of this change is that the licensed investment manager can launch a second fund and another one without prior consent of the regulator. Apart from that there are legal structures for funds that are very flexible and can meet all typical hedge fund requirements.

Moreover, the regulator has become much more open, accessible and transparent in its decision making. Even, upfront ruling or advice can now be sought. Besides, a fund is eligible for full exemption from supervision if for example the required minimum nominal investment exceeds €50,000 or its equivalent (as of 1st January 2012: €100,000).

For investment managers that require a 'light' supervision, in July 2011, the voluntary supervision regime was introduced, which is beneficial for the investment managers who seek capital from foreign institutional investors that require to be supervised. The voluntary regime provides less hassle in terms of regulatory requirements, but at the same time the fund officially is supervised.

Besides, the Netherlands has very favorable tax regimes for investment funds, without being qualified as a tax haven. There are opaque tax regimes for investment funds that are eligible for protection under the 100 or so double tax treaties that the Netherlands has in place. There also are tax transparent fund regimes in which the investors take care of their own taxation – this may be favorable for, for example, pension funds that may have important tax exemptions. And there is a fully exempted tax regime for investment funds. Under this regime no tax is due at all. But this regime typically is not protected under a double tax treaty either.

Robert Vennegoor

Apart from this, the Netherlands applies the so-called participation exemption through which (subject to specific conditions) dividend income is not taxed for corporate income tax. In case of doubt about the taxation of the fund, an investment fund or manager may request advanced tax rulings to deal and conclude on any uncertainty.

To conclude, I believe that Luxembourg and Ireland simply are ahead in their marketing. Dutch and foreign investment managers though now tend to discover the favorable conditions of the Netherlands as a fund domicile. There are two very large investment managers in Netherlands whose funds are currently domiciled in Luxembourg and who now seriously contemplate setting-up master structures in the Netherlands and reform their Luxembourg structures into feeders, thus benefiting from the Dutch favorable fund regimes and protection under the double tax treaties on the one hand, and the Luxembourgish name recognition and distribution capability on the other hand. It is my experience in the investment management industry that once one gives the example, others will follow.

Robert Vennegoor

What I have learned from foreign investment managers is that they appreciate the Netherlands providing a very stable legal and tax environment and a fairly conservative approach.

At Custom House Fund Services we have a specialized Fund Formation desk with a strong knowledge about the common on- and offshore jurisdictions for investment funds and with project management capabilities. The Formation Desk assists investment managers under the final responsibility of their lawyers and tax advisors in exploring the most efficient jurisdiction for the domiciliation of their particular funds as well as in the smooth set-up of these funds.

Wouter ten Brinke

We have an example on the role of the regulator here in the Netherlands.

About a year and a half ago, we showed our interest to the regulator in listing one of our fund of hedge fund vehicles on the Amsterdam Stock Exchange. Around about twelve months later, we were able to list the fund (on 1st of March this year).

Our seed investors were happy and we were also quite happy to be in on this, because the regulator definitely proved they were able to be very constructive in the discussions, as regulations did not easily allow a structure like this to be listed and to be traded the way we wanted it to be traded. The regulator came-up with some fairly creative solutions, and we appreciated it.

We launched that product which was specifically designed for a couple of seed investors (one is a foreign investor) who wanted to have a little bit more scrutiny, an additional layer of supervision, even if we already have our licenses and our funds are registered and licensed in the Netherlands. The listing on the Amsterdam Stock Exchange did provide an additional layer of supervision.

The interesting thing is that we are currently working with one large institution which is active across Europe and which is looking at our Amsterdam-listed vehicle specifically with the idea of dealing with the regulatory pressures of the AIFM Directive.

Wouter ten Brinke

Although we had set-up the vehicle for a select group of Dutch investors - that is where we see most growth in the short-term - now we also have interests from foreign investors, because of these regulatory pressures coming out of the rest of Europe, and the listing on the Amsterdam Stock Exchange could potentially help them deal with these issues. I think that is an interesting development going forward.

Jeroen Tielman

As far as regulation of fund structures is concerned, we encourage a light regime. We see demand for that; there are foreign institutional investors who feel more comfortable about a lighter regime for institutional products than having no regulation at all for professional investor products.

Regulations, as far as portfolio construction, risk management and the custody of assets of hedge funds are concerned, I think it is important for the hedge fund industry to become more self-regulatory to prevent Madoff-type blow-ups, which could lead to rule-based restrictive “reactionary regulations.”

Also, hedge funds are being sold, instead of being actively bought by institutional investors. Investors should become more explicit in what they expect from hedge funds, how they would like to see the fee structure, the alignment, the transparency, etc. Their needs should become more leading in the design of hedge funds, as it is important to stay ahead of the curve and to avoid reactionary rule based regulation. It serves the industry better to have principle-based regulation.

The funds we have seeded are domiciled in the Netherlands, in Jersey, Luxemburg, and Dublin. The main reason for this is that our Dutch FGR structure is not well known abroad. Technically, the FGR structure is great, it is comparable with institutional structures in Dublin and Luxemburg, but unfortunately it is less well-known.

Jeroen Tielman

Benedicte Gravrand The FGR is said to be the most common fund vehicle used in the Netherlands. Can you tell me more about this structure?

Robert Vennegoor: I am not a lawyer, but I believe that it is commonly accepted that the FGR is, as Jeroen said, a very flexible structure that can meet the requirements of the hedge fund industry.

FGR stands for "fonds voor gemene rekening" or "fund for joint account" in English. It is not a legal entity but a contractual fund; the contract is between the investment manager and the Depositary. The fact they there is a Depositary involved is just to separate the assets from the investment manager vehicle and to protect the investors against unlawful alienation by the investment manager.

Robert Vennegoor

Depositaries, like Custom House, typically provide safekeeping services to avoid unlawful alienation of assets and perform oversight over the investment manager to make sure that it acts in compliance with the prospectus and the marketing material of the Fund. Custom House is a recognized Depositary in the Netherlands and its Depositary services are SAS70-II certified.

A FGR can be tax-transparent as well as tax-opaque. If it is tax-transparent, it may be interesting for institutional investors who now have favorable tax condition on investor level, like pension funds, or for those investment managers who may prefer to leave the tax payment to the high net worth individuals who act as investors in such a fund.

As for other opaque structures, the FGR is eligible for protection under around 100 double tax treaties that the Netherlands have entered in.

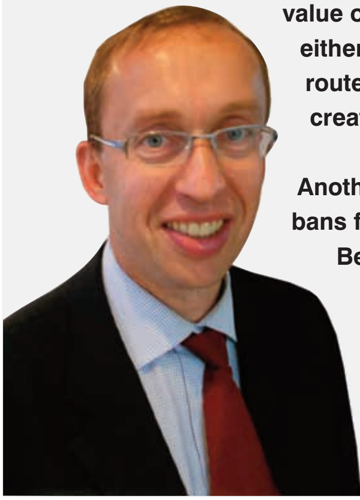
Mark Baak We try to be on top of regulation as much as we can. For the AIFMD, we are a member of the soundboard of the Ministry of Finance, which is quite a professional and efficient vehicle. As a result the Dutch are leading at the moment when it comes to the implementation of the AIFMD.

When comparing the impact of the AIFMD to the issues pension funds have with the regulator and issues insurance companies will have with Solvency II, the AIFMD impact seems very limited.

Dr. Randolf Roth: There is a number of significant market regulation initiatives ongoing which affect us, the most prominent being MiFID, MIFIR and EMIR.

We welcome two elements of the proposed new regulation in particular; one is the expansion of transparency to derivatives and other so-called "non-equities" such as bonds or structured finance products. We also fully support that all marketplaces arranging multi-lateral trades will be recognized as trading venues and therefore be regulated. For example, inter-dealer brokers which organize markets in a broad range of derivatives will be recognized as marketplaces, more specifically as an Organized Trading Facility (OTF), and accordingly need to fulfill the general transparency requirements. For example that should help create a safer environment for liquidity providers in options, where a large part of the business is arranged by brokers. If those liquidity providers find more transparency in the market, they will respond by providing a better service level to our markets, ultimately to the benefit of the buy-side.

Our biggest concern about regulation is the impact of MiFID I on equities, which is a much more fragmented market place. Fragmented market means on the one hand competition, which obviously is a good thing. On the other hand, it also means fragmented liquidity and a lot more opportunities for those who seek to monetize on the value of their customer flow by redirecting this flow to special purpose vehicles where they can either internalize flow or facilitate payment for order flow arrangements. As customer flow is routed away from the transparent, liquid market places, overall market quality will be reduced creating a vicious circle.



Another piece of legislation that created a lot of uncertainty in Europe was the short-selling bans for certain financial and insurance stocks, introduced ad-hoc by the French, Italian, Belgium and Spanish regulators on August 12th. The scope of these bans was highly problematic as it (a) left significant room for interpretation and (b) was much further reaching than the previously introduced German short-selling ban and the proposed short-selling regulation for Europe published by the European Commission in September 2010.

Dr. Randolf Roth

To give an example of the August uncertainty: we had a situation where, in a falling market European asset managers did not dare to use the European benchmark derivatives to hedge their downside exposure. The reason was that the affected instruments accounted for 6-7% of the EURO STOXX 50 market cap and as they had already underweighted those stocks, they were concerned that the regulator would come to the conclusion that they synthetically go short in short-selling-ban-affected stocks, if they used EURO STOXX Futures to hedge their mainly-long-portfolio.

Looking at the results of the ad hoc introduced short-selling ban, Credit Suisse conducted in October an analysis finding the short-selling ban did not slow down the decline of share prices but increased volatility and decreased liquidity in the affected stock.

Benedicte Gravrand **The European Commission recently proposed a tax on financial transactions. Could you give us your take on that?**

Dr. Randolf Roth That is also an interesting development with a potential devastating impact.

There are two misconceptions about the financial transaction tax. The first one is that the tax is going to reduce the profits of high frequency and proprietary trading firms, and has no meaningful impact on the buy-side as the tax is just a little extra cost which might as well be absorbed by the broker. However, the cost itself is actually substantial. If you look at derivatives, take the DAX-Futures example, the all-in trading and clearing exchange fee is around 30 cents. A broker would charge his client an all-in fee of around €1.50. Both numbers are in sharp contrast to the tax of about €15. This is ten times the broker commission and 50 times the exchange fee. Clearly the broker cannot absorb the tax, resulting in a substantial impact on the buy-side.

The second misconception is that our markets will by-and-large continue to exist as today. Looking at a simple market model, there are liquidity providers and liquidity takers. The latter group I have discussed above. Looking at the liquidity providers and staying with the DAX-Future example, a highly profitable liquidity provider would generate revenue of €1. This would cover all of its cost and generate a healthy profit. It is obvious that with a financial transaction tax of €15 there are few choices left for the liquidity provider. As a result, either the market structure will "break down" or the market will relocate to other jurisdictions.

Dr. Randolf Roth

Ivo Jenniskens

Regarding the AIFM Directive, we monitor the developments closely. It is part of our selection process. All managers we currently invest in already comply or have already stated that they are going to comply with the AIFM Directive.

Willem de Vlugt

I agree with previous speakers that regulatory actions are usually reactive and provide a lot of extra work. But in the end regulation does create some form of level playing field.

We have a license and are subject to the supervision of the Financial Markets Authority in the Netherlands, hence we follow all developments and we can react upon them fairly easily. However, maybe specifically to the Netherlands, there could be some developments which would make it more difficult for smaller outfits and start ups to comply or carry the cost. This is a trend which can be worrisome because it restricts the supply of new funds, but in general we welcome regulation.

Benedicte Gravrand

There are grave concerns about the European economic climate at the moment. How do hedge fund managers who invest in Europe fare in that environment?

Mark Baak

I was talking to Wouter six months ago and we both agreed then that the macro environment was very challenging. We hoped that managers would bring market risk down faster than they have done.

Hedge fund managers themselves were negatively surprised by the inability of political Europe to come to a solution. Had they known, they would have taken down risks much faster than they did. The environment is so uncertain right now that nobody is taking much risk, which is disturbing financial markets. A disturbed financial market slows down economic growth.

The entrepreneurial mindset of hedge fund managers differs though. Each year, we see more managers launching than quitting. We don't limit ourselves to the Dutch market, we invest in hedge funds all over the World. But we have a good view on what is happening in the Netherlands because we coordinate the Dutch Hedge Fund Index at Finles Capital Management.

Mark Baak

Currently, the index has 31 constituents, which is an all-time high. The Index is growing quite a bit, because when we launched the Index two-and-a-half years ago the hedge fund index had 17 constituents and now is has 31. Part of the growth has come from initiatives like IMQubator, but the excellent network of service providers easily facilitates the growth.

Willem de Vlugt: European managers have lowered their gross exposure. There is high volatility and we have read a lot about the so-called risk-on risk-off. So it is much more about managing your exposure, your market risk, rather than focusing on alpha generation.

Willem de Vlugt

Wouter ten Brinke

Wouter ten Brinke: Building a little bit upon the Mark's observation, European banks have been following the establishment.

At the launch of the Euro in 1999, most European bank managers expected the politicians to live up to the agreements that were made at the time, i.e., the stability and growth pact and similar agreements. A lot of European bank management teams were completely surprised by the inability of politicians to deliver and to live up to the implement and maintain these agreements.

Similarly, a lot of hedge fund managers were more recently surprised by the inability of European politicians to do something about the situation when things went wrong. It is my observation that it was predominantly U.S. long/short managers who were surprised - they were surprised to a much larger degree than a lot of European based hedge fund managers; that is a clear distinction.**

Secondly, what are we seeing in Europe? Not everybody is risk-off. We have some fairly big allocations to a couple of larger credit managers, global or U.S. based or European based, and they are just dying to buy these distressed portfolios of mortgages, corporates and exposures in European banks. However, up until now there has been very little volume simply because the banks do not want to take the write-downs, and it is averaging the guesstimates of the managers that we work with. There is still a 20 percentage point difference between the price that these managers are willing to bid for the assets and the price at which the banks might be willing to sell. So, until we cross that 20 percentage points price gap there is not going to be a lot of selling by banks and there is not going to be a lot of buying by hedge funds. It is a big opportunity that the whole credit industry and the hedge fund industry are watching.

Wouter ten Brinke

Jeroen Tielman In general, investors including hedge funds have been very clear about the problems of sovereign debt; they laid bare what the real problems were instead of believing politicians, as we all did.

In times of crisis and turmoil, skill-based investing like hedge funds is the place to be instead of long-only strategies. A lot of investors have been hurt by the volatility of their long-only exposure and once more they have realized that the nature of their liabilities is not related to whatever equity or bond index. Their liability of capital return targets are by nature more absolute return related instead. This really could be an opportunity for hedge funds in general.

The irrationality and the unpredictability of political behavior is a complex situation. This complex element however might deter some hedge funds to be active at this particular moment in time. But there might be hedge fund strategies benefiting form this situation by looking at the market from a behavioral finance point of view.

Jeroen Tielman

To cut the long story short, these moments are certainly an opportunity for hedge funds. If you want to benefit from it, get out of long-only strategies; hedge funds are a better alternative.

Ivo Jenniskens I am surprised to hear from Wouter that hedge fund managers were taken by surprise by the lack of political guidance to the crisis in Europe. To the contrary, I would have been shocked if European politics had come up with a swift total solution. Our hedge fund managers have generally taken off risks in the different strategies. On the fund of funds level, managers are for example also decreasing their exposure to equity long/short.

In general I expect new opportunities to arise and, as earlier mentioned, we are doing a search for additional fund of funds managers, including funds with a higher risk profile.

Benedicte Gravrand **Dutch asset manager APG said in the past that the Netherlands was a much happier place than the UK. And Mercer ranks Amsterdam highly. What is the work environment like here?**

Willem de Vlugt I fully agree. Amsterdam is a very good place to run a hedge fund. I started five-and-a-half years ago together with my colleague; we resigned at the end of 2005 and five months later we were up and running. Our fund is also set up as an FGR account.

Mark Baak: In the Netherlands, we were the first in the world to trade equities as the first ever share could be bought in 1606. We have a culture of investing. And we have a large pool of capital, not only from pension funds and insurance companies, but also in general as the Netherlands is quite a wealthy place. So investing has been a big part of our history.

And the global surveys indicate that the country is a good place to have a business, to raise kids, it has good infrastructure, solid service providers etc.

Robert Vennegoor: The Amsterdam stock exchange is the oldest in the world. In 1602 the Dutch East India Company was the first company in the world that went public and the Netherlands therefore became the cradle of the global share trading. In1978 Amsterdam incorporated the first options exchange in Europe which today is still leading in the field of equity options and equity index options and the second in the field of derivatives.

Then and now, Amsterdam represents a vibrant environment for the financial industry.

Robert Vennegoor

The Netherlands is currently successfully preparing for the future. Regulatory-wise, the regulators anticipate on the most current market requirements. Recently, the PPI (the Premium Pension Institution)-regime has been adopted and implemented allowing the Netherlands to support defined contribution pension schemes, complementary to the existing defined benefit schemes. As a result, the Netherlands can continue to leverage and further build on its retirement management competence to become the number one retirement management competence center in Europe. I believe that over 100 applications for the PPI regime were filed, meanwhile.

What Mark said earlier, the Netherlands is well in advance in comparison with other EU jurisdictions with regards to the implementation of the EU AIFM Directive. As such, the Netherlands is motivated and well prepared for a vibrant near future.

And apart from that, I think that greater Amsterdam provides an exciting and international environment to work and live with your family. It provides favorable personal income tax conditions for expats and all the support and facilities that an international community typically requires.

In this respect, to learn more about the Netherlands one may check the website of the Holland Financial Centre foundation which contains a lot of interesting information.

Wouter ten Brinke

That's apart from the great weather that we tend to have between the 1st and the 15th of May every year (we have two weeks of great weather here in Amsterdam, that's about it).

As a Dutch and Amsterdam-based investment manager, an allocator to hedge funds over the last 10 years, we find that a lot of other investors have been doing it for much longer. We have a long experience here with investing.

As was mentioned before, there is a huge asset base which we draw from. We also have a lot of experience with the requirements that institutional investors ask of their service providers, whether it be hedge funds directly, fund of hedge funds or other investment managers.

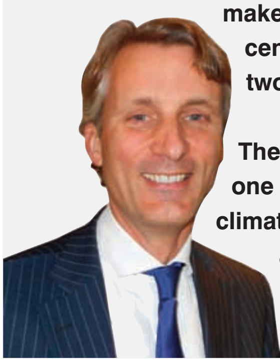
Standards in terms of requirements for transparency, governance, etc. are extremely high. I am finding that a lot of managers - especially U.S.-based managers and probably even more UK-based managers - find this environment very challenging. But they actually find it challenging to live up to these expectations and requirements.

Wouter ten Brinke

Similarly, having dealt with these requirements and these levels of transparency for a long time, for ten years now, I see this coming out of Holland and moving abroad; in some specific cases, we are actually ahead of the curve. A large Dutch insurance company which recently visited a couple of New York-based (several billion plus) fund of hedge funds managers, said in a tier feedback that in terms of the investment infrastructure, the managers could not live up to what we have, especially in terms of the process that is built around that infrastructure.

Going forward in the next couple of years, it will be very beneficial for Dutch based investment managers to move abroad. We do have a competitive advantage there. And it is related to science, but more to experience.

Jeroen Tielman: **We have a 30% tax rule for foreign professionals moving over to the Netherlands. So that would make Amsterdam, for them at least, a very happy place. There is a lot of activity in the new financial center at the Amsterdam Zuidas where our office is located. We have within half a square kilometer two of a lot of service providers, financial institutions in addition to several nice restaurants.**



The cost of living is Amsterdam is low in comparison with places like New York and London. We are one train stop away from the airport, so going to London is an easy day trip. Also the business climate, which is not only stimulated by the Dutch government and the Holland Financial Centre, but also the Municipality of Amsterdam, is very welcoming and receptive to foreign talent.

Jeroen Tielman

Dr. Randolf Roth Having only lived in Frankfurt, London and Chicago, I have an outside view on Amsterdam.

Besides it being a very nice place to visit, it is also a very good breeding ground for trading talent. We get more volume from the Netherlands than from Germany despite the fact that Germany is obviously a much larger country and that it is our home market.

Dr. Randolf Roth

From my perspective also the regulatory environment in the Netherlands is a positive factor, as the regulatory authority AFM seems very reasonable and balanced in its approach.

Ivo Jenniskens I agree with Willem. When we set-up our business, the regulators were very cooperative and we were able to do it in a relatively short period of time. We experience a positive attitude.

On the happy part, I have been living in Amsterdam for 18 years and within the Netherlands I am not going anywhere.

In general, the Dutch are quite open-minded, and able to speak foreign languages, which helps a lot when doing business. For our business, it helps that we have big pension fund pools for which many managers from all over the world, travel to Amsterdam. This gives us a relatively easy opportunity to meet these managers whenever we want.

Ivo Jenniskens