

Edhec Hedge Fund Days Conference

London, February 15th, 2006, 09:00-09:45

Presentation of the Programme

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Programme Presentation

From a Sell-Side to a Buy-Side Perspective

- With currently almost one trillion US dollars in assets under management, hedge funds have seen impressive growth over the past decade.
 - From an initial phase, where some high net worth individuals invested in hedge funds, the industry moved into the mainstream as more and more institutional investors have started allocating to, or at least looking at, hedge funds.
 - The interest from institutional investors comes at a time when they are trying to find alternative solutions to recover after having been dramatically affected by downturns in the equity market.
- Hedge funds have mostly been sold to investors on the basis of their (abnormal) performances.
- This conference is intended to shed some light on the emergence of a new approach to hedge fund investing with characteristics better suited to the needs of institutional investors.

Why Invest in Hedge Funds?

HF offer Attractive Risk-Return Trade-Offs

- Hedge funds have become a key ingredient in investors' asset allocation due to their strong performance.
- HFs, however, are not absolute return vehicles that deliver stable performance regardless of market conditions.

	Convertible Arbitrage	CTA Global	Event Driven	Equity Market Neutral	Long Short Equity	Funds of Funds	MSCI World Equity	Lehman Global Treasury
Ann. Mean Return	9.24%	8.17%	11.25%	9.41%	12.11%	9.68%	6.33%	-0.17%
Ann. Volatility	4.10%	9.22%	5.73%	2.19%	7.24%	5.88%	14.91%	2.83%
Sharpe Ratio*	1.76	0.67	1.61	3.38	1.40	1.31	0.29	-0.77
% of months with neg. returns	21%	44%	21%	7%	31%	31%	45%	44%
Minimum monthly return	-3.19%	1.17%	-8.86%	-1.07%	-5.52%	-6.16%	-13.92%	-2.20%
Sortino Ratio*	2.27	3.67	1.52	5.98	2.39	2.01	0.39	-1.02
VaR (95%)	1.46%	3.63%	2.31%	0.20%	2.42%	1.78%	7.36%	1.43%
Maximum Drawdown	8.21%	11.68%	10.93%	1.07%	10.75%	7.08%	48.02%	9.60%

Why Invest in Hedge Funds?

HF Returns, too, are Exposed to Risk Factors

- Different hedge fund strategies exhibit different exposures with respect to broad systematic risk factors.

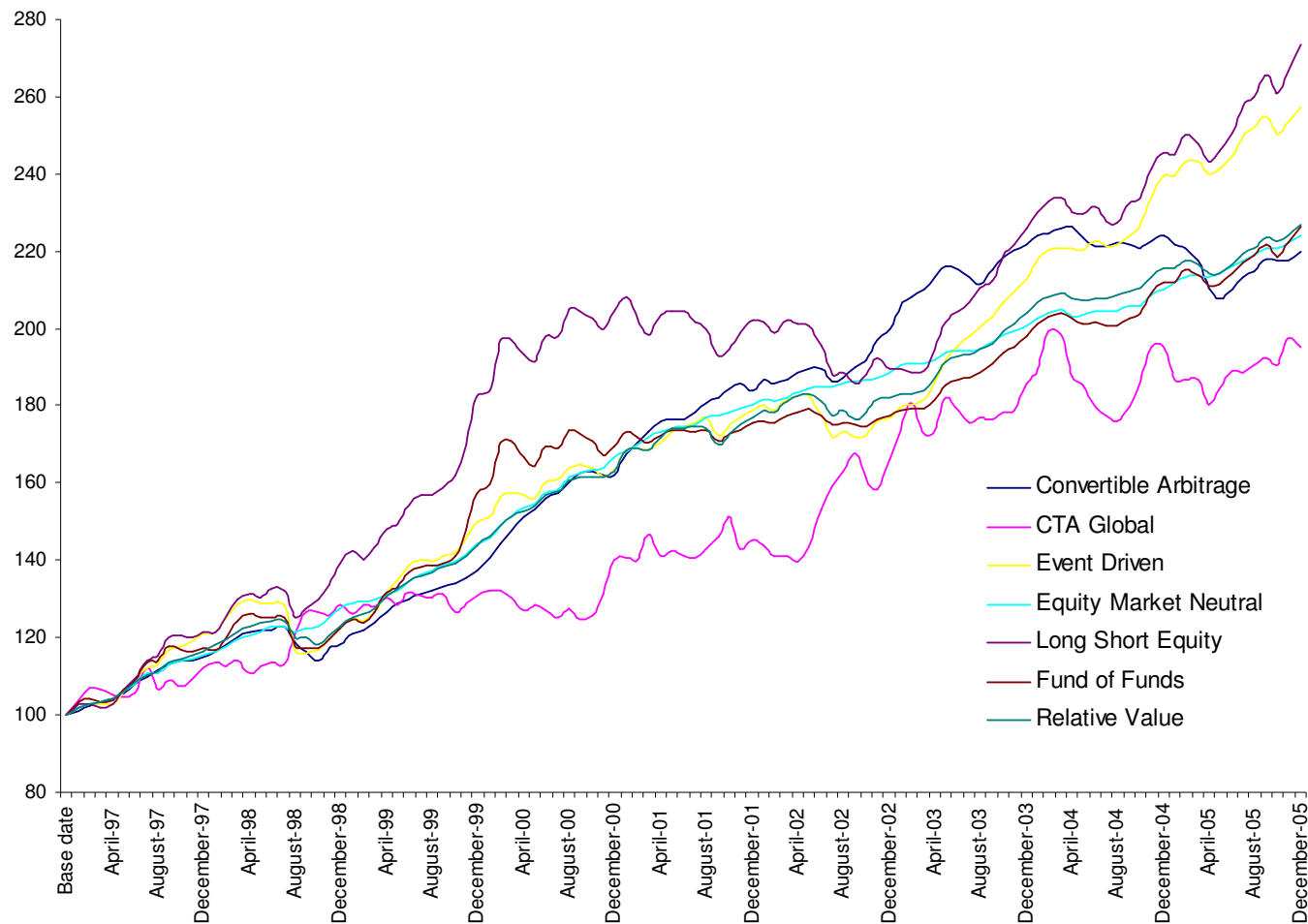
	Equity Factors					Bond Factors					Others Factors
	Implied Volatility (VIX)	Change in implied volatility (VIX)	Value versus Growth	Small Cap versus Large Cap	S&P500 return	Term Spread	Credit Spread	Bond Return	Historical Volatility Bond Return	T-Bill 3 months	Commodity Index
Equity Market Neutral				+	++	--	--	+		++	
Convertible Arbitrage										+	
Long/Short Equity	-	--		++	+++		--				
CTA Global	+							++	-		+
Event Driven	--	--		++	+++		--		-		

Sample period: 01/1997 to 12/2005. Edhec Hedge Fund indices are used for the different hedge fund strategies. Series have been adjusted to account for the presence of serial correlation. Single regression analysis is first used to isolate factors with significant impact. Only the significant factors indicated. + is used to denote a long exposure, and - is used to denote a short exposure. The presence of ++ and +++ (respectively, -- and ---) signals that the long (respectively, short) exposure is relatively strong.

Why Invest in Hedge Funds?

Absolute versus Relative Returns

- Hedge funds are not absolute return investment vehicles.



Sample period: 01/1997 to 12/2005. Edhec Hedge Fund indices are used for the different hedge fund strategies.

Why Invest in Hedge Funds?

Alphas versus Betas

- Hedge fund returns = Betas (normal returns generated from exposure to rewarded risk factors) + Alphas (abnormal returns due do manager's skill)
- Two types of betas
 - Traditional betas: exposure to return on stock and bonds – arguably lower exposure for HFs compared to MFs
 - Alternative betas: exposure to other equity related factors (small cap vs large cap spread, growth vs value spread, volatility, etc.) and other bond related factors (term spread, credit spread, etc.), as well as other factors (commodity, FX, etc.)
- Two types of alphas
 - Alpha emanating from picking skills
 - Alpha emanating from factor timing bets
- In brief (more on this later):

HF Returns = Traditional Equity Factors (TEF) + Traditional Bond Factors (TBF) + Alternative Equity Factors (AEF) + Alternative Bond Factors (TBF) + Other Alternative Factors (OAF) + Alpha

HF's and the Core-Satellite Approach

Core-Satellite Approach

- The trend towards an increase in institutional investors' allocation to hedge funds re-enforces the need for questioning the role of hedge funds in the overall allocation.
- The distinction between alpha and beta benefits is perfectly coherent with the modern *core-satellite* approach to institutional money management.
- This approach advocates a clear separation of a core portfolio managed passively from one or more very actively managed satellites
 - Allows for better cost efficiency
 - Allows for better use of active risk budget

HF's and the Core-Satellite Approach

Hedge Funds and the Core-Satellite Approach

- One (good) reason for investing in hedge funds: Alpha benefits
 - Because hedge fund managers are not subject to the same kinds of constraints that affect long-only investment, they can maximize the potential for alpha for a given level of skills.
 - This legitimates the role of hedge funds as natural candidates for entering the satellite fraction of an investor's portfolio.
- Another (better) reason for investing in hedge funds: Beta benefits
 - Because hedge funds are exposed to risk factors different from long-only managers (so-called *alternative betas*), they allow for i) good diversification benefits when mixed with stock and bond portfolios, and ii) access to rewarded sources of risks that are not easily accessible otherwise.
 - As such they should rightfully enter the design of the core portfolio.
- Optimizing alpha and beta benefits of hedge funds is the real challenge
 - These questions are the focus of this two-day conference.
 - Issues of implementation and risk management are critical.

Programme Presentation

Morning and Afternoon Plenary Sessions, Feb 15th

- (9:45-11:00) The question of the value-added of funds of hedge funds
 - Presentation of the results of an exclusive global study of the long-term performance of 100 top funds of funds
 - Determinants of the performance of fund of funds strategies
- (11:30-13:00) Capacity and sustainability effects in the alternative industry
 - Are growth and industrialisation of the alternative investment industry affecting the performance of funds of hedge funds?
 - Is recent lower-than-expected performance due to cyclical or structural factors?
 - Measuring the capacity effect: academic and industry answers
- (17:30-18:30) Using hedge fund indices to implement allocation to the various hedge fund styles
 - Addressing the inherent biases in indices
 - Reconciling investability and representativity
 - Building funds of indices

Programme Presentation

Afternoon Streams, Feb 15th

- Asset Allocation Stream (14:30-17:00): Asset Allocation as a Value Proposal
 - What concepts and techniques are available to increase the added value of asset allocation in the alternative universe?
 - Tactical style allocation in the alternative universe.
- Fund Picking Stream (14:30-17:00): New Tools for Fund Picking
 - Advanced techniques for measuring hedge fund performance.
 - How much is enough?
 - Reconciling the top-down method with fund picking.
- Risk Management Stream (14:30-17:00): The Value-Added of Risk Management
 - Taking into consideration the specific risks of hedge funds in the portfolio construction phase
 - Managing the operational risk of hedge fund investments

Programme Presentation

Morning Workshops, Feb 16th

- (8:45-10:15) Workshop A: Critical Factors of Operational Due Diligence
 - Conducted by Theo Nijssen and Mark Vandertoorn (Fortis)
- (8:45-10:15) Workshop B: The Benefits of Managed Futures
 - Conducted by Valere Costello (Invesdex)
- (8:45-10:15) Workshop C: Risk Transparency for Hedge Fund Investors
 - Chaired by Olivier Le Marois (Riskdata)
 - Conducted by Adil Abdulali (Protégé Partners), Benjamin Mouté (New Finance), Yves de Naurois (Independent Risk Monitoring Ltd)
- (8:45-10:15) Workshop D: Including HF Strategies in Institutional Portfolios
 - Conducted by Patrick Fenal (Unigestion)
- (8:45-10:15) Workshop E: Structured Alternative Investment
 - Conducted by: Rémi Genlot, David Escoffier, Laurent Le Saint (SGCIB)

Programme Presentation

Morning and Afternoon Plenary Sessions, Feb 16th

- (10:40-12:45) Institutional investors' expectations with regards to alternative investments
 - Presentation of an exclusive Edhec survey
 - Investors' perceptions and expectations with regards to new trends and new products in the alternative universe
- (14:00-15:15) Portable beta and alpha packaging
 - Integrating hedge funds in a core-satellite approach tailored to institutional investors
 - From the delivering to the packaging of alpha
- (15:45-17:00) New requirements in terms of reporting, performance and risk measurement for hedge fund investments
 - What are the most frequently used indicators for HF risk and performance? Results from an Edhec survey of leading practitioners
 - Edhec recommendations for fund of hedge funds reporting