FP INVESTING

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Hedge funds' growing season

'Successful hedge funds are all about risk control'

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Off The Record

If the number of conferences on a topic is any indication, then hedge funds will be the next big thing in investing.

For instance, Merrill Lynch Investment Managers is hosting a gathering next month on hedge funds. In the same month the Institute for International Research is holding a session, while the Strategy Institute recently hosted 250 brokers and managers. And yesterday Frank Belvedere of William Mercer spoke to the Toronto Society of Financial Analysts on alternative investments including hedge funds.

It's not as if hedge funds aren't available here. There are a number and more are in the works.

But typically they are the preserve of those who have at least $150,000 to invest, given they are sold via a private placement.

One fund, Mackenzie Alternative Strategies Fund, which outsources management to Tremont Investment Management, has already been launched, while the talk is that work is proceeding on more offerings geared to retail investors with smaller minimums.

And some of the players have expanded. For instance Hillsdale Investment Management, which has been around since 1996, has two aggressive hedged products to satisfy what it terms "the demand for predictable, yet non-correlated returns." Leverage of up to twice equity is allowed.

Chris Guthrie, one of the founders, said "these funds target a mid-market exposure and are designed to both preserve capital in down markets and participate as markets rebound."

Hillsdale now has six products on offer, three in C$ and three in US$. Of the six, two are long only; the other four allow short selling. Total assets under management are about $15-million.

Naturally, Guthrie makes the case that the recent flurry of activity represents a real trend. "The general availability of risk-adjusted performance data has finally tilted the playing field in favour of good hedged product."

And he believes institutions will increase their exposure to this area. It has hired John Motherwell, formerly with CIBC World Markets in Singapore, to help market to the institutions.

Guthrie makes the case "successful hedged funds are all about risk control." He argues managers must be willing to frequently lose money on short positions in order to deliver on the promise of low correlation and low risk within the clients' portfolios.

"A manager must have significant risk-adjusted return on the long side even before attempting to play on the short side. It is the gap between long and short which creates the return, but it is the consistency of the gap which controls the risk," said Guthrie.

So what's the performance like?

At the end of April, Hillsdale's Canadian aggressive hedged fund was up 17% over the past 12 months while the total return from the TSE 300 was down by 14%. The fund owned 30 stocks, was short 30 stocks, with 64% of the fund allocated to the longs and 36% to the shorts.

Since last July (or inception) the U.S. Aggressive Hedged is up by 3% while the S&P 500 index is down 12%.

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