World Knowledge Forum 2012

CFA: Be More Realistic on Hedge Funds

On Tuesday, October 9th, 2012, a panel discussion on the complex issues surrounding hedge funds in global markets took place at the 13th World Knowledge Forum.

Anthony Scaramucci, Managing Partner of SkyBridge Capital, began his formal remarks by stating, "These products are safe, as long as there is institutional due diligence in the process."

Mr. Scaramucci was joined on the panel by Dominique Strauss-Kahn, the Former Managing Director at the International Monetary Fund, Peng Chen, CEO of Dimensional Fund Advisors Asia Pacific, Christian Edelmann, the Asia Pacific Region Head of Oliver Wyman, and Ochi Tetsuo, CEO and Managing Partner at MCP Asset Management Company Limited.

Mr. Scaramucci discussed the positive nature of hedge funds, saying that they have done much to "mute overall volatility" and have consistently outperformed the bond markets by 15 to 20 percent.

On the other hand, he explained why some people might be apprehensive about the industry. "The media has scared the general public away from hedge funds. 95% of the industry is doing a good job," Mr. Scaramucci said.

He followed up by saying that the media only focuses on "people that made a billion, people that lost a billion, and people that stole a billion." Aside from the media, central banks also need to be careful with how they react to hedge fund set-backs, as an over-reaction causes the public to shy away from hedge funds.

"The best managers have the ability to come back," Mr. Scaramucci said.

Mr. Edelmann continued, "There are a certain amount of risks, and who is the best owner of risks? Hedge funds over banks." He briefly added that hedge funds are not interconnected like banks, and do not have the problems that large banks have witnessed in the recent global crisis.

"Because of slow growth and the political situation, people are afraid of taking a risk," Mr. Tetsuo added. He then focused on the reality of world markets, political risks, and due diligence. Mr. Tetsuo talked about how election years in China and the U.S. will have an effect on the markets, and that once these are settled, there will be a measure of calm.

He said that of the three major sectors, governments had the worse balance sheets, while corporations enjoyed much more cash on hand. Acknowledging this, Mr. Tetsuo also stressed the need for clients to exercise the highest level of due diligence before selecting a manager.

The session then shifted to focus on issues of transparency, due diligence and the future of hedge funds.

Mr. Chen said that the only guaranteed winner in hedge fund investment was the hedge fund manager. For investors, he said, "The game is becoming a zero sum game. If you win, someone else needs to lose big.”

He also openly questioned the ability for managers to evaluate their own performance and how they market themselves to customers. Returns are the major focus of hedge funds but “60 to 70 percent are tied into market factors,” rather than hedge fund manager performance. The panel agreed that this particularly was a major problem with managers' pay being directly tied to activity.

"The highest producing managers tend to be making money," Mr. Scaramucci countered. He echoed that while compensation may be an issue, it was important for managing partners to be invested in their own hedge funds, which will avoid overly risky investing.

"Investors need to demand more transparency," Mr. Chen said. He and all of the panelists agreed that customers must conduct a high level of due diligence before selecting a firm to invest with.

Regulation of hedge funds was also a topic of discussion.

"Hedge Funds are parts of the market and there are no problems with that. The problem is the models are easy to work with, and those models are wrong," Mr. Strauss-Kahn stated. He said central banks should play the role of an "architect" and that they should not add strong regulations that could stifle hedge fund investment.

Mr. Strauss-Kahn added that governments should be concerned with who the "losers" are in the market because it would be very important for policy makers to understand which sectors would be losing money.

Closing out the discussion, the panel touched on the future of hedge funds in Korea and elsewhere.

"The people that will do the best here will be a part of the educational process," Mr. Scaramucci said. He directly commented on the future of the young hedge fund industry in Korea, and how investor education will be crucial to producing successful managers and investors.

Still, Mr. Scaramucci was confident that from within Korea’s fledgling hedge fund industry, a superstar would arise.