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## **The Edhec European Alternative Multimangement Practices Survey**

**Sponsored by Fimat, Global Fund Services**

**London – December 11, 2003.** Edhec Group, the largest of the major French Business Schools, has published the results of an extensive survey into Alternative Multimangement (Funds of Hedge Funds) in Europe. Conducted over the second half of 2002 and supplemented by analysis and interviews during 2003, the survey took in 61 respondents together managing some €136bn at July 31, 2002.

The overall aim of this major survey is to shed light on an increasingly significant section of the global alternative investment industry, to examine new trends and changing attitudes among fund of hedge fund managers and investors, and to provide a statistical basis for recommendations on new or improved practices. A key theme of the survey is the continuing evolution of the European hedge fund industry in the face of increasing institutional interest and investment.

Highlights of the Edhec Survey were presented at a morning press conference in London, by Noël Amenc PhD, Professor of Finance, Edhec Business School, supported by Jean-René Giraud, C.E.O. Edhec-Risk Advisory and Gregoire Dechy, Executive Business Developer, Fimat, Global Fund Services. Electronic copies of Professor Amenc's presentation, carrying permission for the republication of extracts (with attribution to Edhec/Fimat) are available from Victoria Thomas ([victoria@rostronparry.com](mailto:victoria@rostronparry.com)).

Among the core findings and recommendations related to European Funds of Hedge Funds, are:

- **INVESTORS.** In European funds of hedge funds, high net worth investors still represent the main category of investors but institutional investor allocations are growing rapidly
- **DIVERSIFICATION.** The growing importance of institutional investors is leading to a greater concentration on diversification rather than absolute return, a greater emphasis on benchmarking and a requirement for greater attention to be paid to operational risks.
- **INDICES.** The use of indices (for benchmarks) is not problem free: Indices suffer from numerous biases, mostly related to the absence of regulation of the publication of performance and composition. Furthermore the selection/construction methods involved in creating an index tend to create the performance rather than the strategies covered. (The survey lists pairs of indices showing the measurement variance for different strategies over a five year period – for example, for long/short

equity investment, the variance between the two extreme index measurements is 22.04%).

- **OPERATIONAL RISKS.** The increasing importance of institutional investors and their desire to protect themselves against operational risks is resulting in greater attention being paid to these types of risks, which represent the most significant source of hedge fund failures. The study however reveals how challenging it might be for funds of hedge funds managing less than \$200-\$300 million to undertake a satisfactory operational due-diligence both in terms of skills and economics.
- **QUANTITATIVE/QUALITATIVE APPROACH.** Only 13% of respondents combine a quantitative approach with a qualitative portfolio construction approach, even though it is the only method that allows scenarios on extreme market conditions to be taken into account while, at the same time, disciplining and formalising the manager's intuitions.
- **FUND OF FUND SIZE.** The number of funds within European funds of hedge funds (or managers within multimanager funds) is significantly above the optimal academic findings as only 18% of respondents hold FoHF that include fewer than 15 funds.
- **PERFORMANCE EVALUATION.** 82% of respondents consider the Sharpe ratio and only 4% calculate an Omega ratio, despite the fact that the latter is more appropriate for the alternative universe.
- **DATABASES.** Performance databases play a central role for 67% of the respondents, even though these databases contain numerous biases and it is easily shown that the choice of database, and thus the choice of particular biases, condition the performance of the funds selected.
- **DUE DILIGENCE.** Small funds of hedge funds have economic problems with regard to undertaking a formal due diligence process. The survey suggests that the costs of a due diligence process cannot be sustained by FoHFs with assets under management that amount to less than 200 million US dollars.
- **THIRD PARTY CERTIFICATION.** While studies on the failures of hedge funds have shown that certification of their performance significantly reduces the failure rate, it should be noted that only 13% of the respondents have implemented certification by an independent third party.

Please note that the bullet point summary above is only a selection of points arising from the Edhec survey, and that all survey points are sustained by statistical analysis.

### **Edhec Business School**

With 90 permanent professors and more than 3,000 students spread over two campuses in Lille and Nice, the Edhec Group is in fact the largest of the major French business schools.

Established in 1906, Edhec has been one of the top five business schools in France for several years.

The Edhec Risk and Asset Management Research Centre carries out major research programmes in the areas of asset allocation and risk management in both the traditional and alternative investment universes.

### **About Fimat Group:**

Global Fund Services is part of Fimat Group's prime brokerage and alternative investment services business line. Global Fund Services is a proud sponsor of this independently produced

academic report by the Edhec Business School, where the views expressed in the report are those of the authors.

The Fimat Group has a global network of 20 offices and is a member of more than 40 of the world's largest derivative exchanges and 10 stock exchanges. The Group provides global clearing and execution services to institutional users of derivatives and securities markets worldwide. Companies of the Fimat Group cover markets that account for 80 percent of the volume of all major exchanges. They offer clients access to over 500 individual interest rate, bond, currency and equity products as well as 220 individual commodity contracts, covering the full spectrum of metals, energy, grains and soft commodity products.

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