

Hedge Fund Industry “Blind Spots” Persist

(Press Release) - Northern Trust Hedge Fund Services survey shows hedge fund managers and institutional investors grappling with longstanding and emerging industry issues

Amid the rapid growth of the hedge fund industry and the complex regulatory climate following the financial crisis, hedge fund managers and institutional investors have differing views on transparency and independent controls, according to a new survey by Northern Trust, a leading provider of services to some of the world's largest asset managers and institutional investors.

An overwhelming majority of managers (90 percent) believe that all or nearly all of their investors are satisfied with the level of transparency they receive. However, about half (55 percent) of investors say they seek higher levels of transparency than they currently receive.

Investors place such value on transparency that many are willing to pay for it. Among those investors who desire more transparency, 78 percent say they would accept a 1-to-3 basis point increase in management fees to support the operational costs for such reporting.

Regarding the issue of independent controls, there is a perception gap between the level of independent oversight investors value and the controls managers actually have in place.

- While 96 percent of investors indicate independent verification of cash processing is extremely or somewhat important, only 44 percent of managers say they have independent controls on cash.
- Additionally, 43 percent of investors say independent checks on portfolio risk calculations are extremely important, yet only 13 percent of managers employ such independent controls.

“Despite the ongoing push for transparency, a majority of hedge fund investors are still seeking more insight into their investments,” said Peter Sanchez, CEO of Northern Trust Hedge Fund Services. “Bridging the transparency gap goes beyond costs. It requires a balance where investors get the reports they need while managers retain ownership of their unique strategy. We believe providing insight into risk is one approach to bridging that gap.”

Regulation: Helping or Hurting?

Increased regulation in the wake of the financial crisis has played a role in reshaping the hedge fund industry and increasing the operational demands on hedge fund managers. Surprisingly, a majority of managers (59 percent) and investors (53 percent) feel some regulations have helped reduce the likelihood and severity of another financial crisis. But the industry continues to have skeptics, as 40 percent of investors and 34 percent of managers say regulations have done nothing to prevent a future crisis.

Priorities: Managers vs. Investors

Over the next five years, hedge fund managers and investors are in agreement on the need to recruit and retain top talent. However, while issues related to regulation and fund operations are top priorities for investors, few managers agree.

- About half of investors (56 percent) and managers (45 percent) rank the recruitment and retention of talent, as either their number one or two priority.
- Many investors also highly rank regulation (46 percent), including regulatory reporting and investor due diligence, and operations and internal infrastructure (56 percent) as a number one or two priority. However, less than a third of managers rank regulation (26 percent) and operations (30

percent) similarly.

“As the hedge fund industry becomes dominated by institutional investors, managers must continue to invest in their operations and infrastructure to meet the growing needs of these investors,” said Sanchez. “The strength of a fund’s operations is evolving into a key driver of success as it allows managers to adapt more quickly to the ever-changing regulatory climate and address the transparency demands of their investors.”

About the Survey

Northern Trust Hedge Fund Services in partnership with Asset International conducted a global hedge fund industry survey of more than 100 hedge fund managers and 300 institutional investors in North America, APAC and EMEA on topics including past and future priorities, transparency, operational controls and independent oversight and regulation.

Managers’ assets under management ranged from more than \$10 billion (23 percent of respondents) and below, with investors’ assets ranging from more than \$10 billion (40 percent of respondents) and below.

About Northern Trust

Northern Trust Corporation (Nasdaq: NTRS) is a leading provider of wealth management, asset servicing, asset management and banking to corporations, institutions, affluent families and individuals. Founded in Chicago in 1889, Northern Trust has offices in the United States in 19 states and Washington, D.C., and 20 international locations in Canada, Europe, the Middle East and the Asia-Pacific region. As of December 31, 2014, Northern Trust had assets under custody of US\$6 trillion, and assets under management of US\$934 billion. For 125 years, Northern Trust has earned distinction as an industry leader for exceptional service, financial expertise, integrity and innovation. Visit northerntrust.com or follow us on Twitter @NorthernTrust.

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