Trials and Tribulations of Newbies in Stockholm

Stockholm (HedgeNordic) – As aspiring new fund managers dream of starting their new fund, they focus on how to develop a new attractive investment strategy which will generate superior risk adjusted returns. Quickly however, the prosaic reality hits them. in the current regulatory environment, how can they raise assets without a fund and how can they start a new fund without any assets?

Today more than ever, professional investors want more than a new strategy idea. They want a structure around it, a sound asset management business model, and this structure has a cost. How much exactly depends on the strategy itself and future ambitions.

Pre-AIFMD (Alternative Investment Fund Management Directive), it was easy to start up an alternative investment fund (AIF) in Sweden. "You used to be able to put together an AB (a regular limited liability company) and invest anyone's money in high-risk private equity-like targets in the North of Sweden for example", says Björn Wendleby at Magnusson. Wendleby has witnessed hedge funds births throughout his career, first at Finansinspektionen, the Swedish FSA, and as a lawyer from 2004. The protection for retail investors was virtually inexistent in this type of set up, but it made alternative returns available to many.

Alternatively, you could seek a license from the Swedish FSA to manage a special fund. Such a fund could seek exceptions from the traditional mutual fund-type license opening up for hedge fund-like investment features (leverage, use of derivatives, short-selling etc.) while marketing to quasi-retail investors. This was made possible in Sweden already in the second part of the 1990s, unlike in many other countries, where hedge funds were always reserved to qualified investors. The most famous pioneers of this opportunity were Brummer & Partners, who made alpha accessible to Swedish investors through their first fund, Zenit, already in 1996. Slowly but surely, the number of special funds started growing. According to Wendleby, perhaps 30 or 35 out of 800 registered funds were special funds in 1998, of which a few hedge funds. Their number culminated in 2007 when you saw a massive number of new funds, many of which are no longer active today. After the debacle that followed post Lehman Brothers, new openings slowed down sharply.

In the meantime, European regulators put their heads together to implement new rules meant to prevent a similar systematic meltdown in the future. UCITS IV rules came out in 2011 followed by the AIFMD in 2014. As a result, new levels of control were imposed on special funds, as well as other alternative investments like Private Equity and Real Estate managers, including those simple AB structures mentioned above. This meant additional protection for investors as well as a dramatic increase in costs, especially for smaller managers who lack scale to support the new imposed functions such as independent risk management. "The regulation is positive… mostly for lawyers", says Wendleby with a twinkle in the eye. "Seriously, I believe that all these levels of controls make products safer, but the regulator should go further in allowing more of the alternative investments to reach non-professional investors. As a non-professional, you can invest in an ELTIF (European Long-Term Investment Fund, a new vehicle recently approved by the European Commission) but not in a regular Real Estate fund."

The full article can be read on p.80-85 of the HedgeNordic Industry Report 2016