

Finding a Home for Nordic Hedge Funds

Stockholm (HedgeNordic) – Luxembourg and Ireland hold a dominant role as European fund domiciles and together account for hosting about half of all funds domiciled in Europe. The Nordic countries are different in this respect, at least when it comes to Nordic hedge funds. These are much more likely to keep their funds and management close to home. HedgeNordic interviewed a group of Nordic managers in an attempt to understand the decision-making process used to select their fund domicile.

Where are Nordic hedge funds domiciled?

Almost two-thirds of the hedge funds included in the Nordic Hedge Index (NHX) are domiciled in their respective home markets. This could be partly attributable to the dominance of Swedish-originating funds in the NHX, most of which are domiciled locally because of the Swedish society's familiarity with fund investing. Sweden has the highest proportion of fund investors in the world, with the Swedish Investment Fund Association reporting that eight out of every ten Swedes have savings in funds even beyond their fund-based premium pension savings. Most Swedish funds may find the local market sufficient for their fund-raising ambitions. Domiciling a new fund in Sweden, therefore, is a cost-effective solution for funds fishing in their local ponds, explains Stefan Gavelin, CEO at Swedish Adrigo Asset Management.



Stefan Gavelin

"We mainly target Nordic investors, and I think one driver for choosing Luxembourg over Sweden is if you are targeting international investors, as they tend to look for a structure that they are familiar with," Gavelin tells HedgeNordic about the decision to domicile Adrigo Small & Midcap in Sweden. "Another important point is that we feel that the Swedish structures are fair to investors when it comes to the fees paid by the fund or by the fund management company. Foreign-domiciled funds tend to be more expensive for investors as more administrative fees are allowed to be charged to the fund," in Gavelin's opinion. "The most essential factor, however, was time to market," reckons Gavelin. "We have been planning to launch another hedge fund for some time and prepared the permit with the Swedish FSA in advance. Once we had finalized details on how the new fund would invest, we contacted the Swedish FSA for approval to amend the fund articles. This enabled us to launch quickly."

A fundamental consideration in the choice of fund domicile is the nature of target investors. The local focus of Nordic-originating hedge funds can partly explain the reason behind setting up locally. Around two-thirds of the 104 Swedish hedge funds included in the NHX are domiciled in Sweden. The same proportion of locally-domiciled funds as in the group of the 19 Finnish index members. In contrast, and more in line with other European markets, approximately only half of Danish and Norwegian hedge funds are domiciled in their respective home countries. Differences in legislation, especially when it comes to the marketing of investment vehicles, is the most likely explanation for the percentage difference between these two blocks.

Luxembourg and Ireland are the domiciles of choice for Nordic hedge fund managers who do choose to leave their home shores. Around 37 percent of the hedge funds included in the NHX are domiciled in non-Nordic countries, with the majority being domiciled in the Grand Duchy of Luxembourg (62 percent). These numbers are true for the fund and share class that is listed in the Nordic Hedge Index. There is likely some distortion as managers may have various funds in multiple jurisdictions, offsetting our statistics.

Why do most Nordic managers choose Luxembourg?

The implementation of the Alternative Investment Fund Managers Directive (AIFMD), which allows the cross-border distribution for alternative investment funds following a home state approval, increased the attractiveness of European onshore domiciles at the expense of offshore domiciles and reduced the range of attractive choices to two: home domicile and onshore domicile in another European jurisdiction.

The choice of fund domicile represents a critical decision for fund managers. Fund managers will evaluate a number of criteria including tax efficiency, costs, distribution channels, reputation, time to market, ability to implement their investments strategies, among others. A number of Nordic hedge fund managers, however, suggest that soft factors such as personal experience with a certain jurisdiction tend to influence the choice of fund domicile rather than objective considerations such as tax environment or cost of doing business. But more importantly, the familiarity of both Swedish and international investors with Luxembourg as an international fund hub appears to explain the tendency of Nordic fund managers to choose Luxembourg at the expense of other options, such as Ireland.



Sean George

Sean George, CIO at Strukturinvest Fondkommission, tells HedgeNordic they had to choose between two rather equivalent options - Luxembourg and Ireland - when launching the Hamiltonian Global Credit Opportunity Fund in the May of 2018. "We mostly focused on the available fund structures offered by these two jurisdictions and did not put too much emphasis on criteria such as taxes or costs because there were no big differences between the two jurisdictions," he says. George states that both Luxembourg and Ireland advertised they allowed for a faster time to market, "but I could not tell which side was right since we decided to go for Luxembourg in the end." "The deciding factor then was that Swedish investors are more accustomed to Luxembourg than Ireland." The partner at another Nordic hedge fund requesting to stay unnamed corroborates George's view, with recent data from the Association of the Luxembourg Fund Industry, ALFI, showing that 59 percent of cross-border funds registered for distribution in Sweden are domiciled in Luxembourg.

The team running the mentioned fund also had to choose between Luxembourg and Ireland for their fund's domicile, but their previous experiences led them to select Ireland as a fund domicile. "Although managers can now set up a Reserved Alternative Investment Fund (RAIF) without CSSF approval, my past experience of being stuck in the approval process played an important role in our decision making," says the partner.



Joakim Stenberg

Joakim Stenberg, a founding partner of Nordic Cross Asset Management, tells HedgeNordic they had a very clear idea of how to set up their range of recently launched funds. “We wanted our products to be alternative, offer daily liquidity, and incorporate ESG factors from the beginning,” said Stenberg. “Since fund hotels in Sweden do not have experience with alternative UCITS and given that we wanted to be able to target non-Swedish investors, too, in the longer term, we made the decision to domicile our funds in Luxembourg,” says Stenberg. While three of the four hedge funds managed by Nordic Cross are domiciled in Luxembourg as UCITS, the fourth, Nordic Cross Credit Edge, was set up as a special fund in Sweden as the fund’s strategy employs more complex instruments than possible in a UCITS structure. Nordic Cross did not consider other fund domicile options, arguing that the choice was based on their previous good experience with Luxembourg and the recognized distribution capabilities offered by this jurisdiction.



Michael Petry



Erik Lundkvist

The choice of fund domicile is an easy decision for hedge fund shops which already have an existing fund structure in international fund hubs. Erik Lundkvist, Chief Investment Officer at Coeli Asset Management, and Michael Petry, head of hedge funds at Danske Asset Management, tell HedgeNordic that the primary reason behind domiciling their freshly launched hedge funds in Luxembourg was that their firms already had an existing platform in the Grand Duchy of Luxembourg.

Conclusion

Domicile selection is no easy task for hedge fund managers because of the wide range of factors influencing the choice of domicile. The nature of target investors plays a central role in the selection process of fund domicile, but personal experience with a certain jurisdiction is certainly important to many hedge fund managers launching new funds as well. Investor comfort, distribution channels, and time to market are also found to constitute important decision factors in the process of choosing fund domiciles. The familiarity of Swedish investors with Luxembourg represents the main reason why most foreign-domiciled Nordic hedge funds are domiciled in the Grand Duchy, and the so-called

network effect will most likely enable Luxembourg to maintain its dominance in the Nordic hedge fund industry going forward.

Picture: (c) RTimages—shutterstock.com