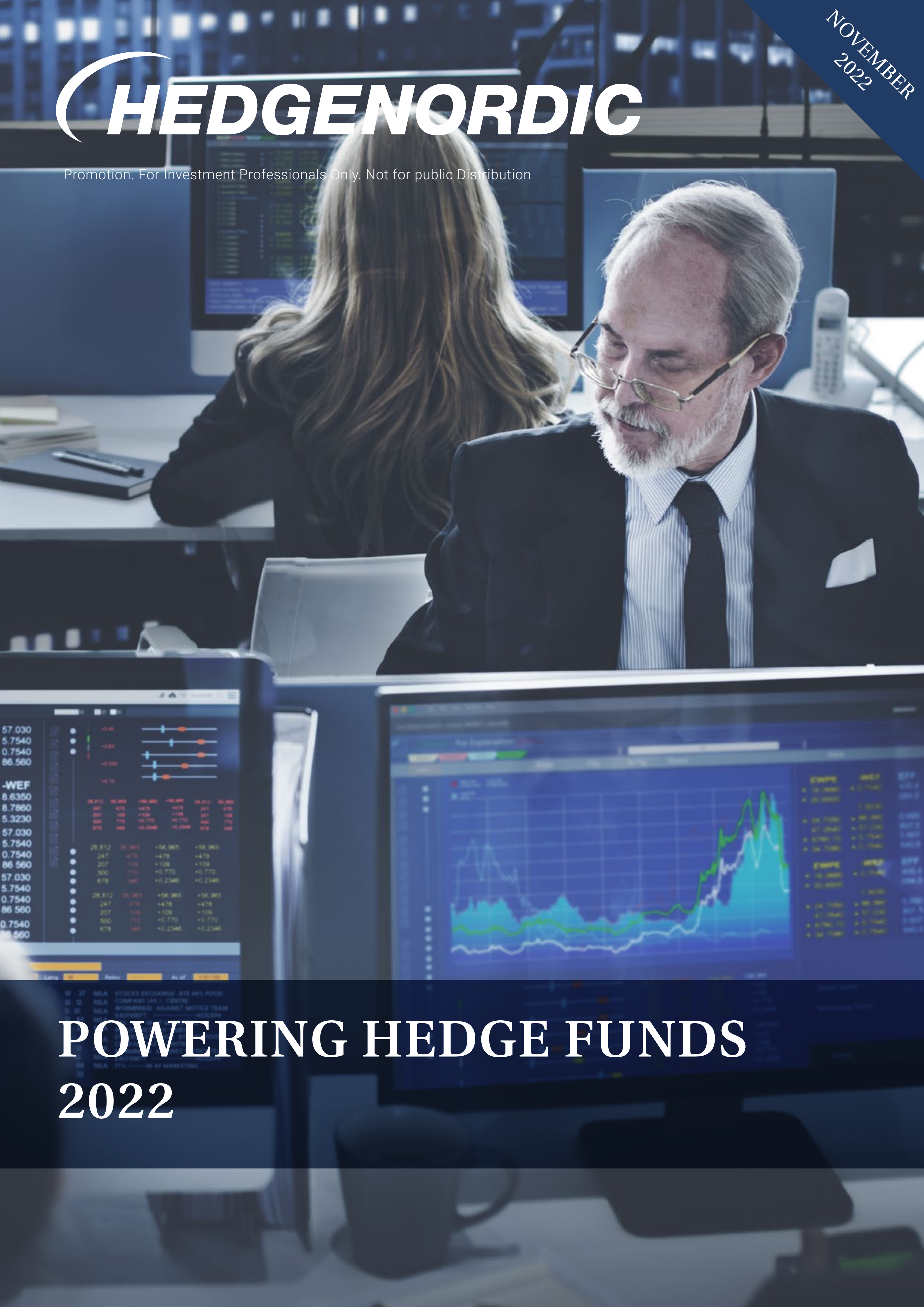

HEDGENORDIC

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POWERING HEDGE FUNDS 2022

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INTRODUCTION

HedgeNordic is the leading media covering the Nordic alternative investment and hedge fund universe. The website brings daily news, research, analysis and background that is relevant to Nordic hedge fund professionals from the sell and buy side from all tiers.

HedgeNordic publishes monthly, quarterly and annual reports on recent developments in her core market as well as special, indepth reports on "hot topics".

HedgeNordic also calculates and publishes the Nordic Hedge Index (NHX) and is host to the Nordic Hedge Award and organizes round tables and seminars.

CONTACT:

Kamran George Ghalitschi
Nordic Business Media AB
Kungsgatan 8
SE-103 89 Stockholm, Sweden
Corporate Number: 556838-6170
VAT Number: SE-556838617001

Direct: +46 (0) 8 5333 8688
Mobile: +46 (0) 706566688
Email: kamran@hedgenordic.com
www.hedgenordic.com

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Editor´s Note …

with a little help from my friends …

As managers focus on risk-adjusted returns, creating new products to meet growing investor demands and meeting the obligations of the everchanging regulatory landscape, there is an increasing need for trusted and skilled hedge fund services partners to support them with the day-to-day operations.

While some areas have always been covered by outside, third-party providers, the recent years have also seen the outsourcing of some operations of portfolio management that had traditionally been key and critical internal departments. The hedge fund space is also often at the forefront within the financial industry embracing technology, or indeed new technologies in their operations, be it front-, back- or mid-office – as well as all other elements not involved in trading and portfolio management. Technology has become a critical enabler for hedge fund managers and the service providers that support them.

Managers increasingly rely on sophisticated front-office solutions to help achieve market-beating risk adjusted returns. Meanwhile, automated and integrated middle- and backoffice infrastructures deliver the operating and compliance efficiencies hedge funds need to curb costs and maintain their profitability in an era of tightening fees.

In this publication "Powering Hedge Funds," HedgeNordic aims to investigate how hedge fund managers can act even smarter, gaining time and efficiency doing what they are there for, namely creating uncorrelated returns for their investors. We want to highlight what service providers do for managers, what they could do and what is actually needed to make a hedge fund work. In short, we want to showcase the "Intel inside" equivalent for the hedge fund space.

One additional aspect to investigate is how far the hedge fund industry, particularly in the Nordics, has come with embracing new – and old – technologies, and where there are still areas of improvement. We aim to showcase some concrete solutions that can make managers' and investors' daily jobs and routines more efficient, streamlined and cost effective and aim to give potential end-users smart options to their requirements, or even open doors they were unaware existed.

The publication starts off with guide on "How to Start a Hedge Fund: 5 Steps for Setting Up for Long-Term Success" by Michael Hutner from SS&C Eze. Conor Daly and Hugh O'Dea from Goldman Sachs proceed to provide insights into "Optimising Currency Hedging for Funds and Share Classes."

Johan Björkholm from Swedish fund hotel AIFM Group tells hedge fund and other fund managers to "Focus on What You Do Best" and let fund hotels take care of their entire laundry list of responsibilities. Declan Quilligan of Citco Fund Services then discusses "How Global Asset Servicers can Power Regional Hedge Funds."

In "Saxo Bank: 30 Years of FinTech Innovation," one can learn more about Saxo Bank's scalable platform that is always seeking to adapt and stay ahead of the curve. Mathias Österberg goes on to share more insights into how Finnish fund solution provider GRIT Governance is "GRIT-ting the Finnish Hedge Fund Industry" by setting out on the mission to "help the daring build legendary investment businesses" in Finland and beyond.

"Are you ready for Institutional capital?" asks Edgefolio's Rowen Pillay, who puts forward some guidance for emerging fund managers seeking institutional capital. In "Fund operations: The explosion of algorithmic trading," Ryan Guichon from RBC Investor & Treasury Services provides his insights on how fund operating models are evolving to align with today's dynamic market environment. experts from Novus round up the publication with more insights into "An Allocator's View on Effective Hedge Fund Marketing."

Happy reading!

Kamran Ghalitschi

PUBLISHER, HEDGENORDIC

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BY MICHAEL HUTNER – SENIOR VICE PRESIDENT, GENERAL MANAGER, SS&C EZE

How to Start a Hedge Fund: 5 Steps for Setting Up for Long-term Success

Throughout my 22 years at SS&C Eze, I've seen my share of shifts in the market. Here is one worth noting: a report by Hedge Fund Research reports that more than 600 new funds were launched in 2021 - the highest number of funds in four years. Others are noticing, too. The Alternative Investment Management Association and Eze partner Cowen provide a detailed analysis of this trend in their "Emerging Stronger: The Next Generation Manager Survey."

Their research found declining costs to be a significant factor driving the increase in the number of hedge funds starting up. In fact, the breakeven point for hedge funds has dropped 25 percent, partly due to reduced headcount and reductions in travel and office expenses brought on by the pandemic.

Additionally, allocators are now more willing to consider managers with less than $100 million in assets under management or those with a track record of fewer than three years, breaking down another barrier to entry.

But this openness does not mean allocators are willing to invest in just any new fund. In the report, over 80 percent cite concerns over operational due diligence, poor administration standards, and lack of transparency as barriers to investment.

If you are considering taking advantage of these trends and starting a hedge fund, you must first prepare to address potential concerns. Here, I share insights gleaned from more than two decades of experience in financial technology on how the right partners can help you address these concerns and set you up for success.

1. SET YOUR COURSE – START WITH A DETAILED PLAN

Begin by making a business plan that outlines your investment strategy and the costs involved in running an efficient and institutionally sound operation.

At this point, you'll also want to think about how you'll market your fund. You'll need to develop a compelling name that attracts investors and create a pitch book highlighting your investment objectives, strategies, and who is running the show. The pitch book is an investor's first look into how you run your fund, so you want to get it right.

Getting up and running will likely take longer than you think. On average, hiring the right personnel and setting up all the partnerships you'll need, including legal entities, auditors, and prime brokers can take six to nine months. Having a plan and your end vision in mind will help ensure things stay on track.

2. MEETING INVESTOR OPERATIONAL DEMANDS WITH HELP FROM THE EXPERTS

As I mentioned, allocators' most significant barriers to hedge fund investments are now due diligence, poor administration standards, and lack of transparency. Navigating evolving regulatory requirements and settlement changes while managing your firm's operations becomes increasingly complicated. Luckily, help from the right experts can make managing your fund operations successful regardless of complexity.

When choosing these experts, research and hire the best service providers you can find. Look for vendors and professionals with long track records of success in the industry who can work with you beyond launch as a long-term partner.

Once in place, put this team of experts to work. Before you enter due diligence, most investors will expect to see:

- Legal and tax infrastructure completed for jurisdictions in which you will operate.
- Connections to prime brokers who can provide capital introductions essential to fundraising.
- A technology operations system handling trading, accounting, reconciliations, etc.

- Proper certification for all vendors, demonstrating that they uphold rigorous, globally recognized standards.

Addressing Security Concerns with Global Security Certifications

Investors want to know their money is safe and your operations are seamless and designed to mitigate risk. As such, security should be a primary consideration when establishing these third-party provider relationships. When choosing solutions, systems, partners, and vendors, ensuring they meet the highest global standards for security is essential.

ISO certification is the best way to ensure vendors employ strong security practices. For example, at SS&C Eze, our frameworks uphold the highest international standards – ISO certification 27001, the gold standard for keeping client data safe and confidential, and ISO 27018 and 27017, signifying that our cloud services uphold the most rigorous privacy standards.

3. BEYOND DUE DILIGENCE: CHOOSING PARTNERS FOR LONG-TERM GROWTH

Your goal in starting a hedge fund is to achieve long-term growth. Doing so requires working with trusted partners who will continue to support you on your path long after launch.

So how do you know if a provider is a partner for growth? This type of provider will have specific distinct characteristics.

Service is the most important characteristic to look for in a vendor. From onboarding and implementation to day-to-day support for your front- to back-office, you need to know your vendor can provide fast and personalized service from day one. Also, be sure your service partnership can expand to accommodate your needs as your business grows.

In addition to scalable support, your provider should offer flexible and configurable solutions that will not only meet your current needs but expand and grow as your needs evolve.

At a minimum, your solution should be built using an elastic infrastructure and employ APIs that empower you to extend the value of your investment through integrations with current and future platforms.

To scale even more seamlessly, choose a vendor with an app store or marketplace of plug-and-play applications. This type of service lets you expand your investment ecosystem quickly when the time is right, without the cost and hassle of vetting and onboarding additional vendors.

4. CRITICAL QUESTIONS TO ASK WHEN SELECTING A HEDGE FUND TECHNOLOGY PARTNER

Often, hedge fund founders don't make necessary considerations or factor in growth when choosing a technology operations system provider. Instead, these firms simply settle for the vendor with the lowest proposal price or that meets only their day one requirements.

To avoid buyer's remorse, compare the goals of your fund with the technology the provider is offering.

Start by looking at your business plan and answering the following:

- What's my ultimate size goal? What technology will I need to accommodate a hedge fund of this size?
- How big do I envision my firm getting? How much mobility should my technology system have across offices and jurisdictions?
- Do I want to go after larger investors, and will I adjust my fee structure to accommodate them?
- What strategies do I want to run, and how much flexibility do I need to be able to introduce new asset classes?

Next, evaluate whether your technology partner can help you achieve your goals. Asking these questions can help you make your assessment:

- Are you a partner I can trust? What is your track record in the industry, and how do I know you take the technological and operational risks seriously?

Michael Hutner
General Manager and Senior Vice President
SS&C Eze

- What is the size of your service and support organization? Do they have expertise in specific areas of my business? Can I always get someone on the phone if I have an issue? What is your experience helping firms like mine grow?
- Are you capable of supporting the asset classes, jurisdictions, and strategies I have defined for my fund today, and any ideas I have for the future?

If the vendor can't answer these questions satisfactorily and grow with you to accommodate your desired path, the TCO is far greater than the low up-front cost.

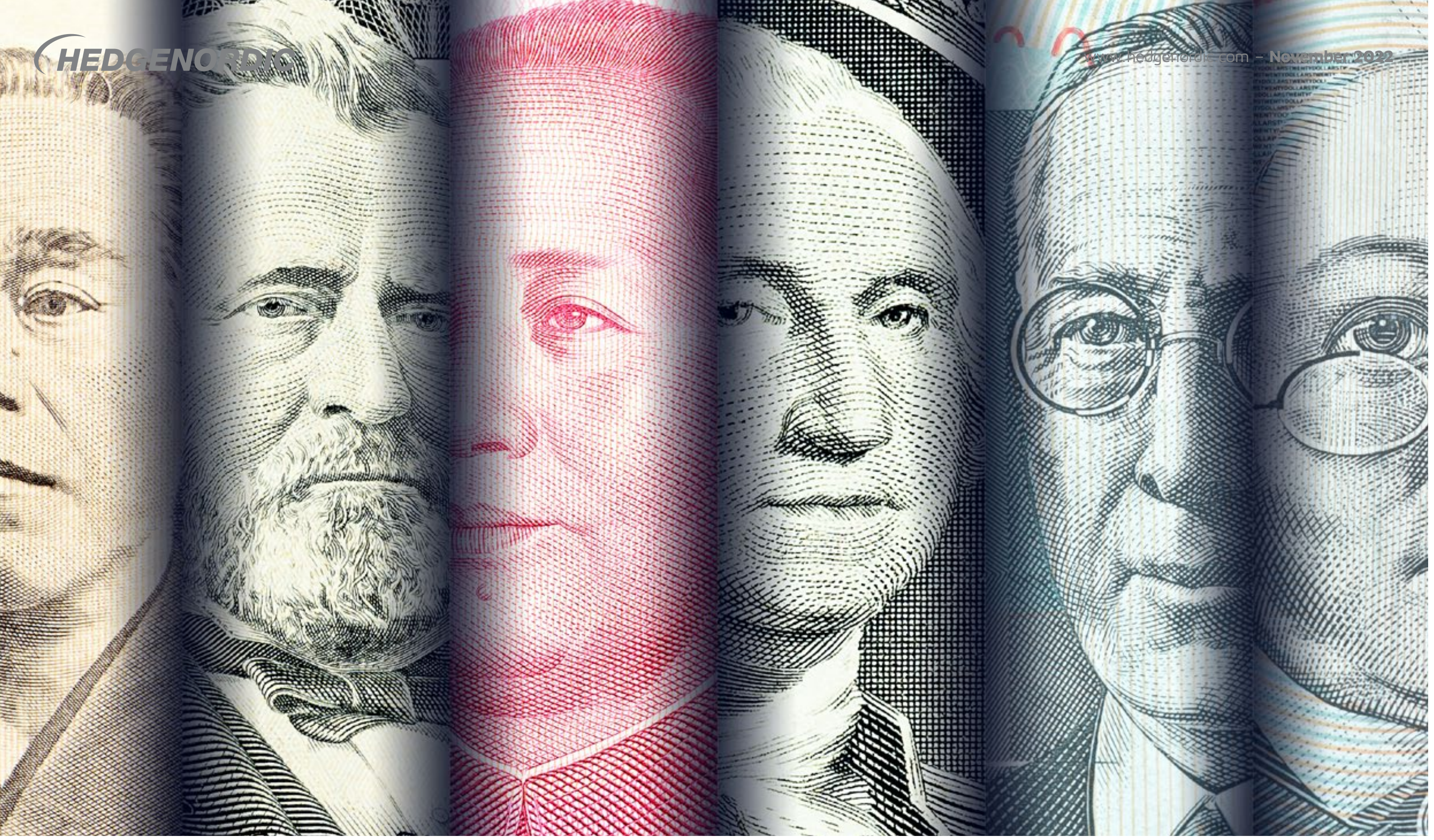
Additionally, inquire about your vendor's system delivery options. A cloud-hosted system with a scalable, elastic infrastructure is best. Flexible, modern cloud technology allows you to access your systems and deliver returns, regardless of location or market volatility. Cloud-hosted systems also provide critical connections in today's hybrid work environment.

Choosing a technology provider that offers the scalability and adaptability to handle your workflows of today – and the future – sets you up for operational success and saves you the cost and hassle of switching providers down the line.

5. DON'T WAIT – GET AHEAD OF THE COMPETITION

Hedge fund managers shouldn't wait until after launching their fund to implement critical investment operations.

Making a plan, finding the right partners, and adopting scalable, reliable, and secure technology creates an institutionalized infrastructure that sets your hedge fund up for success. In doing so, you are better prepared to address any potential investor concerns, and having the right technology from the start sets you ahead of your competitors.



Optimising Currency Hedging for Funds and Share Classes

By Hamlin Lovell – HedgeNordic

> "Practicalities on the post trade side were an obstacle in the past, but thanks to the proliferation of things like cloud computing, APIs and common standards on margining and credit risk, it is now possible to match all settlements within one vertical."
>
> Conor Daly

Regulators have long advocated for an unbundling of foreign exchange services. New technological advances enable an open architecture approach to selecting FX providers and counterparties. "Practicalities on the post trade side were an obstacle in the past, but thanks to the proliferation of things like cloud computing, APIs and common standards on margining and credit risk, it is now possible to match all settlements within one vertical. Systems and protocols such as CLS, FIX and Swift were created to standardize processes and democratize access to markets," says Conor Daly, FX Solutions Strats and EMEA head of eFX sales at Goldman Sachs. There should now be a level playing field for everyone, even if some deliberate or unintended barriers to fair and equal competition do remain.

The inertia, factor long-standing relationships and, occasionally, restrictive contracts might lead some asset managers to view the default option as bundling currency hedging with other services from providers such as administrators, custodians, depositaries, or prime brokers, which may also be balance sheet lenders. Yet a tender process, such as an RFP/RFI exercise may identify a dedicated currency provider as more competitive. This can be in terms of anything across pricing, best execution, operational efficiency or reporting requirements. A currency specialist can dovetail with existing service providers: "we provide seamless post-trade connectivity with third party custodians, prime brokers and portfolio management systems," says Daly.

Smaller and newer funds might be particularly keen to lighten their operational burden, and be anxious to reduce the chances of any operational mishaps around FX hedging, which can be an existential threat for a neophyte manager. "Disjointed FX workflows caused by having too many counterparties, platforms and agreements can be a challenge for smaller teams. Some clients lack the technology or IP for managing currency risk efficiently," says Hugh O'Dea, Vice President of FX Sales at Goldman Sachs, who covers FX in the Nordics and other regions.

The Goldman Sachs Passive Currency Overlay (PCO) offering has hundreds of clients covering a broad spectrum in terms of AUM size and fund structure complexity. In the Nordic region, clients include many featured by HedgeNordic, including some of the largest household names and newer firms starting with little assets, who may also be using Goldman's leading equity financing resource. The unit is taking a constructive view on the longer-term growth prospects of some start-ups: "we work with them from day one to provide content, technology and expertise that helps them to scale up," says Daly.

PCO focuses on portfolio currency hedging, share class hedging and FX cash management, and reduces the operational workload inside asset managers. PCO aims to ease operational burdens and risks for COOs, Treasurers, Portfolio Managers and Heads of Operations and middle office managers, whilst also improving governance structures.

The three most common criteria for selecting FX providers are pricing, best execution and operational efficiencies but their relative weighting can vary between clients. "Some earlier stage funds require a lot more support with engineering, operations and regulatory items. STP is a priority for many," says Daly.

AUTOMATION, ELECTRONIFICATION AND APIS

There is a lot of scope to automate undesirable aspects of currency risk management, such as data keying and handling or trade bookings. However, risk management will often retain an important human touch. "Electronification of FX markets hasn't meant fewer humans: on the contrary, it's meant more

Conor Daly
FX Solutions Strat & EMEA Head of eFX Sales – Goldman Sachs

humans, serving more clients, doing more valuable things with their time," points out Daly, who has been active in electronic FX for 13 years.

For execution, the blend between algorithmic and higher touch execution will vary partly with the currencies traded. Goldman's Systematic Market Making (SMM) unit helps the firm to deliver a hybrid risk management approach. "Currencies with better pre-trade price transparency and active, central limit order books are easier to deliver higher levels of systematic market making to," says Daly.

The open architecture is powered by technological advances, that are in a sense plumbing and wiring: "APIs reduce friction to collaboration," says Daly. FIX protocol APIs are widely used for execution, portfolio management and post-trade processes. Meanwhile, restful APIs can also help to access data services such as market data for back-testing. The entire client onboarding process can also be expedited through APIs, which are embedded in client portals or websites and share data in real time.

MARGINING, STRATEGIES AND OPTIONS

Approaches to currency hedging will vary with criteria including the investment strategy, types of collateral and leverage. Generally, cash and top grade government bonds are acceptable collateral.

Margin is negotiated on a client by client basis, informed by timely data on NAV and exposures. "We look to incorporate our clients' requirements regarding credit terms wherever possible," says Daly. This can be a moving target with SAC-CR and regulatory changes underway. "Where illiquid strategies, such as private equity or private debt and real estate, have less cash and liquid assets on hand, GS has a number of alternative solutions to traditional spot and forward FX hedging programmes to assist clients," adds Daly.

MARKET COVERAGE

Goldman Sachs turns over tens of billions of dollars of notional per day and can source liquidity through interbank markets. Currency market coverage is wide and includes an extensive franchise in emerging market currencies, including NDFs, and Goldman takes pride in maintaining access through turbulent markets.

INTERNALISING AND NETTING

Goldman Sachs FX overlay platform assist clients to achieve execution cost reduction through netting (whereby both sides of a transaction could be crossed at or near the mid, thus avoiding part or all of the bid/offer spread). This can be achieved within the same fund and across portfolios, where the rate benefit is distributed in a volume weighted manner to treat all funds fairly and ensure correct reporting and downstream settlements. "Clients of GS particularly like this netting capability, where they operate look through hedging across their portfolio and share-class hedging needs," according to Hugh O'Dea.

In addition to this, Goldman Sachs, as an FX flow house, is focused on internalization, and minimizing the market impact of trades. "Risk intermediation is one of our most important functions as a partner to our clients," according to Daly.

COUNTERPARTY EXPOSURES AND RELATIONSHIPS

PCO clients have counterparty exposure to Goldman Sachs acting as principal, directly and/or via clearers or prime brokers – and the systems can coordinate amongst multiple clearers and PBs. "PCO takes the raw exposures, regardless of where they sit, nets them down to the smallest possible delta, hedges and then manages the cashflows back to prime brokers and custodians," says Daly.

Beyond spot FX, this requires an ISDA and CSA with Goldman Sachs. "In recent years, standardization of documents and streamlining of processes have made the onboarding process less onerous and less daunting than 5 years ago," according to O'Dea.

CURRENCY CHARGING BUSINESS MODELS

Clients pay for PCO via trade execution on the platform. In contrast, Daly has observed some other

Hugh O'Dea
Northern Europe FX Sales – Goldman Sachs

currency providers charging a variety of fees including management fees, administration installation costs, and other execution costs that can be difficult to benchmark. "We have also seen per transaction booking fees, which do not make sense in a world of scalable straight through processing," he argues.

The most egregious practices observed have probably been opaque currency reporting without any time stamp, which could make it difficult or impossible to ascertain if best execution has been obtained – and could thus be the most expensive "hidden fee."

BENCHMARKS AND TCA

Best execution is a nuanced and multi-dimensional concept where price is only one among many criteria. "PCO has quantitatively demonstrated best execution versus a variety of benchmarks, such as WM Fixing, BFIX and Siren FX. The choice of benchmark is partly determined by fund valuation points," says Daly.

Various third party TCA providers can be used. Many are already on the menu and connected to GS and clients are also able to select different providers.

REBALANCING THRESHOLDS AND HEDGE RATIOS

Costs are partly influenced by trading frequency, which in turn depends on rebalancing thresholds and hedge ratios. Clients can weigh up the benefits of more accurate currency hedging against the extra transaction costs it entails; GS PCO provides back-testing analytics to support clients with their decisions in this regard.

Rebalancing thresholds have generally been between 0.50% and 5%. "In 2022, with increased levels of FX volatility, clients have been reviewing them more often and gauging them against peer group practices," says O'Dea. Where hedge ratios are not fixed, in effect a variable hedge ratio is an active wager and a form of active currency overlay and managers do have discretion to express these views.

> "Electronification of FX markets hasn't meant fewer humans: on the contrary, it's meant more humans, serving more clients, doing more valuable things with their time."
>
> Conor Daly

AIFM: "Focus on What You Do Best"

By Eugeniu Guzun – HedgeNordic

> "Emerging fund managers want to focus on their strategy and investors, but are often overwhelmed by the increasing regulatory complexity and structural matters."

No start-up can succeed without a great business idea. Beyond that, there are many factors and details determining whether the idea can be turned into a successful venture. For a hedge fund business, as much as any other business, the main ingredient of success lies in its concept, its investment strategy. Although many hedge fund start-ups are exceptionally skilled at investment strategy, setting up a fund, let alone a hedge fund, is not an easy undertaking.

"Emerging fund managers want to focus on their strategy and investors, but are often overwhelmed by the increasing regulatory complexity and structural matters," Johan Björkholm, the deputy-CEO of Swedish fund hotel AIFM Group, discusses the challenges faced by fund start-ups. There are a lot of nuts and bolts that need tightened on the journey of building a fully operational and sustainable hedge fund business. "The laundry list of responsibilities for

Johan Björkholm, deputy-CEO – AIFM Group

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"In my world, the risk-reward ratio should steer fund managers towards a fund hotel such as AIFM."

up-and-coming managers may seem intimidating, and can even deter some away from wanting to start their own fund business."

While not necessarily providing a road map for certain success, fund hotels can provide the infrastructure needed to successfully launch and run a hedge fund start-up. "By seeking outside know-how and operational infrastructure, these professionals benefit from having a team "holding their hand" to ensure a structurally sound fund launch and to help navigate continual management once up and running," says Björkholm. "The fund hotel set-up can enable the emerging fund manager to truly focus on their core capabilities while enlisting a "one-stop shop" to fulfill all obligational functional areas related to accounting, administration, compliance, risk, legal, etc.," he elaborates.

AIFM has managed to build a completely customizable suite of solutions that covers everything one would need to set up and run a traditional fund, alternative fund or hedge fund, ranging from corporate services and guidance on how to create a suitable business structure to daily administration and risk management services. "It is very difficult to procure each of these individual functions if you have no experience to distinguish a solid service provider from a less experienced one," explains Jared Fein, Fund Operations Specialist at AIFM. "Navigating these decisions takes time and manpower, and serve to distract from the most critical concerns – the investment strategy and capital raising."

This fund hotel set up enables fund managers to leverage AIFM's already-in-place operations infrastructure in the face of an ever-changing compliance and regulatory framework. "Running a fund can be overwhelming with all the systems needed, organizational requirements, and connections to the outside world such as distribution channels and investor reporting," considers Björkholm. The fund launch-related challenges facing the next generations of fund managers are getting starker with the increasing legislative requirements and increasing barriers to entry. "AIFM provides the entire infrastructure needed to meet these requirements, making it almost as simple as pressing a button."

In the face of an ever-changing business environment and regulatory landscape, AIFM takes an open architecture approach to building a tailored ecosystem for each client. "Rather than a "one size fits all" approach, AIFM offers customization that can fit the needs of any case," explains Fein. "This offering allows for the managers of the fund to cut out waste of services not needed as well as ability to use the core competencies of the manager and AIFM to build a strong relationship that can be expanded and contracted based upon need."

OUTSOURCE OR DO EVERYTHING IN-HOUSE?

Nordic hedge fund managers, especially emerging managers, are increasingly turning to outsourcing various functions as a cost-effective alternative to building out expensive specialized internal teams and infrastructure. "I would find it hard to motivate the general risks but especially the costs related to finding and hiring the appropriate personnel to run a fully-fledged fund management business with all functions in-house," argues Johan Björkholm. "Fund managers generally create value for investors in the actual fund management, not by running a fund management company."

"No matter how much expected or committed capital there is at inception, establishing an organization that will manage one or more hedge funds entirely in-house can be an expensive and risky endeavor," reckons Björkholm. As professional money managers, hedge fund managers are in the business of searching for and investing in attractive risk-reward opportunities. The same risk-reward concept can be applied in the decision-making process of building out a fund management business. "In my world, the risk-reward ratio should steer fund managers towards a fund hotel such as AIFM," says Björkholm.

A PLATFORM FOR EVERYONE

AIFM services and collaborates with a wide range of strategies, with the types of strategies ranging from non-conventional asset classes such as physical art and Baltic forestry to more familiar asset classes such as equity, private equity and private debt. "By remaining neutral and operating on a case-by-case basis, we're able to cater to any and all strategies," he elaborates. "AIFM prides itself on being the only fund manager in Sweden with approval to manage according to all available investment strategies."

The types of strategies launched by emerging managers reflect investor interest and demand in the prevailing market environment. "Investment strategies interest tends to follow market movements," elaborates Björkholm. "We have gone from a lot of real estate-related requests, to mortgages, crypto currencies and tech," he continues. "In the current market environment where it feels like almost all asset classes are depreciating, alternative investment strategies such as hedge funds are gaining traction."

Hedge funds of all shades have struggled to keep up in the bull market during the decade of quantitative easing after the financial turmoil of 2008. "Following a strong stock market since the Great Financial Crisis, my view is that hedge funds have struggled with popularity," reckons Björkholm. "But maybe it's time for a hedge fund renaissance?" If that happens, fund hotels such as AIFM are ready to take on board all duties discharged by emerging fund managers, who can instead just focus on successfully running their investment strategies undistracted.

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Facing a New Frontier: How Global Asset Servicers Can Power Regional Hedge Funds

By Declan Quilligan,
Head of Hedge Fund Services –
Citco Fund Services (Ireland) Ltd.

The last two years accelerated change in our industry in a way that no one could have anticipated. Whilst the solutions and stop gaps introduced to keep funds running were successful during the pandemic and its aftermath, they also served to highlight inefficiencies within established and trusted operating models.

While the catalyst for this accelerated change will hopefully stay firmly in the rear-view mirror, we are in a place where the industry has already evolved significantly.

As managers increase diversification across asset classes, move into hybrid strategies and access a wider range of investment vehicles, the volume of data being exchanged between funds and asset servicers has reached new highs, and the complexity of asset-servicing of alternatives will only continue to grow.

Long gone are the days of providing month-end NAV calculations, with the industry now focused on offering truly front-to-back office services, and tailored, outsourced solutions. The challenge from here is to keep the foot on the gas.

MEETING COMPLEXITY WITH INNOVATION

With delivering returns to their investor base front of mind for hedge fund managers, they need a partner that understands the nuances and complexities of day-to-day transactions and the impact these have on their portfolios.

Whether covering complex loan activity or enhanced agency services for syndicated and complex transactions, experienced and knowledgeable staff at asset servicers must work in parallel with software and systems to tackle these challenges. As such, outsourcing this digitization is crucial to the streamlining of managers' businesses.

From removing paper from the initial subscription and capital commitment process to helping managers score their portfolios against environmental, social and governance (ESG) metrics, there are various tools either available or in development that can help with this process. At Citco, we have a three-year digitization program geared towards a "touchless" future – designed around our intention to minimize human interaction with data and automate regular processes. Whilst we are always in the business of 'doing', automation allows us to add value by using our teams as analysts and strategists, rather than just processers.

One of the biggest technology enhancements we have implemented is the successful transition of our Æxeo® platform to the Amazon Web Services (AWS) cloud. The data lake we have since been able to set up in AWS provides clients with on-demand access to their data through an API, giving them flexibility and accuracy in a timely fashion. The move to the cloud was a significant milestone for the Citco team – marking one of the largest accounting transactions in history, and the largest within the alternative investment sector – and is the forward-thinking innovation that underpins our client-centric approach.

However, it isn't all technology of today. Natural Language Processing (NLP), a branch of artificial intelligence, has been around in some form or another for the last fifty years, and focuses on how

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computers can be used to analyze natural language to extract information. We already use a combination of robotic process automation, business process management applications and AI, with over 30 RPA processes currently in place performing basic tasks across all clients.

This base technology is being enhanced all the time, and as it improves it provides more and more use cases for asset servicing. From improving the client experience through data extraction, to speeding up NAV finalization, the positive impact on Service Level Agreements is unquestionable.

THE NEXT FRONTIER

These innovations, however, are concerned primarily with the collation of data. Whilst this is an acknowledged challenge, the new frontier is increasingly how that data is used and – crucially – how it is protected.

With data from multiple sources, data management tools are emerging as a solution that will help fund managers tackle the wealth of data crossing their desks. By providing transparency, they can unearth inefficiencies in existing processes allowing for adaptation and improvement, driving real business value.

With this efficiency comes the added advantage of addressing security risk. As our world becomes increasingly connected and reliant on data, ensuring security is critical. As online trading becomes more prevalent, it becomes necessary for processes to incorporate security methods such as dual factor authentication, watermarked documents, and digital certificates embedded in documents that are tamper-proof once signed.

It is through collaborative platforms that servicers can meet managers' needs to have data securely acquired and stored, as well as permitting managers to communicate electronically with their existing investors, as well as potential new clients. This cutting-edge technology is already in high demand, and we would expect that to continue to pick up pace throughout 2023.

> "Whilst we are always in the business of 'doing', automation allows us to add value by using our teams as analysts and strategists, rather than just processers."

FUELING THE FUTURE

Today, there are demands on managers to deliver returns in a world where those very returns are challenged. In turn, the opportunity for asset servicers is simple – help managers to spend less time on administrative duties so they can achieve their objectives for end investors.

There is widespread growth of outsourcing like this in many areas of the world, including the US, UK and Asia. However, some regions – like the Nordics – are yet to embrace this trend so emphatically. Managers in the Nordic region have been less eager to leverage such services, opting instead to either continue to work in-house, or partner with regional providers.

The drawback to this is that regional providers may not have a global footprint, and this can often delay operations outside of the Nordics. In an industry whereby regulation is becoming increasingly more complex, and the importance of data intensifies, we believe that Nordic funds are likely to move away from this local approach, increasingly turning to global service providers who can provide everything under one roof. This is likely to be particularly pertinent when it comes to areas such as middle-office services, where it increasingly makes sense to have treasury, collateral and cash management carried out by one provider who has full oversight of managers' cash positions.

To continue to bring value to clients, our expectation is that asset servicers will in turn need to pitch themselves as one-stop-shops for clients' needs. It is this simplification for businesses that could be one of the biggest growth areas in asset servicing going forward.

At Citco we have a nimble, independent structure, digitized technology processes and a culture of dedication to client service, so if clients do seek an all-in-one solution from a single provider, we are well placed to provide that.

> "Managers in the Nordic region have been less eager to leverage such services, opting instead to either continue to work in-house, or partner with regional providers."

Saxo Bank: 30 Years of FinTech Innovation

By Hamlin Lovell - HedgeNordic

"When we launched in 1992, we were a FinTech before the term was even coined. Being a FinTech is part of our DNA. The only constant is change," says Stanislav Kostyukhin, Commercial Owner of Direct Business at Saxo Bank, headquartered in Copenhagen.

> "Especially alternative investment funds and smaller hedge funds are reaching out to us now because they need to trade a wider range of instruments, and want more operational efficiency."

The firm takes pride in its Danish roots and entrepreneurial culture, but is always adapting and staying ahead of the curve. Saxo now has a global footprint of 16 offices. We serve and onboard institutional partners from our offices in key financial centers, including Denmark, the UK, Amsterdam, Singapore, Australia, Hong Kong and Switzerland. There are clients in 160+ countries, and client assets total over DKK 640 billion (EUR 85 billion). Saxo globally now has over 2,500 employees covering more than 65 nationalities.

Saxo caters to a broad range of clients, from retail to high-net-worth individuals, banks, brokers, family offices, and various asset managers including hedge fund managers – in the Nordics and globally. The firm has 850,000 clients, including over 200 white-label partners, which include some of the world's biggest banks and financial institutions such as Banca Generali, Old Mutual, Standard Bank and Mandatum.

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“We service clients in a very different way to traditional banks and brokers.”

“During 2021, we welcomed more than 263,000 new trading clients. It took us twenty-five years to amass the first DKK 100 billion in client assets, whereas it took slightly more than four to gather an additional DKK 540 billion. We have a very efficient setup for onboarding, integrating and servicing our clients,” says Casper Andreas Andersen, Global Head of Products and Services.

The platform is very scalable in part because most of the execution is electronic, albeit with some manual safety filters for regulatory checks and market impact. The systems can easily cope with 500,000 trades on a busy day or a million on some extra hectic days.

Saxo has a growing roster of more than 300 hedge fund and financial intermediary clients. “Especially alternative investment funds and smaller hedge funds are reaching out to us now because they need to trade a wider range of instruments, and want more operational efficiency. They do not want to have to deal with integrating different counterparties, execution systems, stock lenders and calculating margins,” says Daniel Bergman, Associate Director of Institutional Sales.

Systematic and quantitative funds, which seek standardization and speed of execution, are especially attracted to Fix API for execution, and the execution offering is geared towards electronic trading. “A suite of in-house execution algorithms is part of the package, including TWAP, VWAP, icebergs and customized plug and play algorithms including low latency and fully scripted options that can be used for high-frequency trading. Furthermore we are having more than 200 million OpenApi request /day,” points out Andersen.

A small share of trades is handled manually, including some securitized derivatives that cannot be traded electronically.

INTEGRATED OFFERING

The package goes well beyond execution: “it is often most efficient to bundle execution and clearing with custody, order management and settlement. Most clients benefit from a full end-to-end package. We aim to be a one-stop shop offering end-to-end coverage and want to be the primary broker,” says Kostyukhin.

“However, the architecture is also open enough to accommodate clients’ own CSD setups,” points out Andersen. Additionally, Saxo can complement other banks and brokers. “We service clients in a very different way to traditional banks and brokers,” he adds.

With a broad range of services in the catalogue, such as end-of-day files, a dedicated platform for case management, state-of-the-art performance reporting and simulation tools for back-testing of trading strategies, Saxo offers institutional partners an integrated solution that allows them to focus on what really matters: running their strategies as seamlessly and efficiently as possible.

CASH AND SYNTHETIC CHOICES FOR EQUITIES

Saxo Bank offers both a traditional cash prime brokerage setup and a synthetic CFD offering that allows clients to obtain leverage with the leverage wrapper that suits their needs best, according to Andersen. “Short positions are available synthetically and fully funded positions can be lent out via our Securities lending program,” he adds. Securities can be located internally or from third parties.

“The pros and cons of synthetic versus cash depend on the strategy, execution costs and ease of integration,” elaborates Andersen. “The most active traders will often find it cheaper to use CFDs. Those seeking to earn from stock lending will use cash.”

EXTENSIVE AND GROWING MARKET COVERAGE

Saxo is mainly focused on more liquid markets that are easier to automate and the coverage has grown both through organic initiatives and various acquisitions over the years. The universe includes 20,000 cash equities and other instruments in 28 countries; 7,000 ETFs and 15,000 mutual funds. Listed derivatives in over 40 global markets cover exchange-traded futures, options and single stock options. There are over 300 futures and 3,000 listed options.

Saxo is famous for its foreign exchange offering that helped to make the firm’s reputation at the start 30 years ago. “This includes over 180 crosses on the platform, which access liquidity from the largest financial institutions. We have FX options for more than 40 crosses as well as forwards,” says Andersen. “We are seeing growing interest in currency trading with the Euro below parity,” adds Kostyukhin.

Saxo also rolled out a crypto-FX offering in 2021 with fully automated trading. It trades the largest 3 cryptocurrencies, including Bitcoin (BTC), Ethereum (ETH) and Litecoin (LTC) against major fiat currencies such as USD, EUR or JPY. Furthermore Saxo offers a dozen+ crypto based ETNs .

There are over 5,000 fixed income instruments and Saxo shops around for the best prices, automatically sending out indications of interest to multiple market maker parties. “We have state-of-the-art execution. Historically the market was rather opaque but we are now bringing more transparent price discovery,” says Kostyukhin.

Market coverage includes some of the most volatile and best performing commodities in 2022, such as German and Nordic electricity, as well as natural gas listed on Nymex, Dutch TTF Gas listed on EEX and Henry Hub in Chicago. The Eurex-listed carbon emissions contract is also traded. Formost of these, Saxo has created CfD-equivalent contracts which allow for trading in smaller sizes.

Saxo sometimes trades as agency and sometimes as principal. “For securitized derivatives, we need to make our own prices and give clients access to superior liquidity. Thanks to the BinckBank integration, we have become market leaders in products such as turbos and constant leverage certificates, which can be very popular in Middle and Southern Europe as well as Asia. There are local rules on maximum leverage,” says Andersen.

LEVERAGE, MARGIN AND RISK MANAGEMENT

Leverage is bespoke to the client, but Saxo does not compete on the lowest margin rates and highest leverage. "We have made a conscious choice to be ahead of the curve, including on regulation. For instance, the Australian regulator, which once allowed 400 times leverage, recently copied ESMA's European restrictions on leverage. We have always been conservative so we were immediately compliant with the new rules," says Christoffer Sagild, Senior Director and Head of Risk.

Saxo has developed proprietary models for margin and exposure calculations, monitoring risk limits, and stress testing. The packages vary with markets traded and wrappers. "There can be some degree of netting between delta one and options exposures. There can also be a more portfolio-based approach, netting over product wrappers, where we offer more holistic portfolio margining. It all depends on how a portfolio is structured. Overall, our netting is probably much more conservative than some more aggressive players," says Sagild.

Saxo Bank's award-winning platform is helping hedge fund managers to broaden their portfolio diversification and also enhancing operational efficiencies through its integrated solutions and electronic execution. It also offers the convenience of trading by phone, tablet or laptop from any location, which fits in very well with post-Covid hybrid working patterns. Saxo's nimble, global and substantially automated business model is thriving in the volatile markets of 2022. The offering will continue to expand, and can sometimes add markets in response to client demand. With hedge fund industry assets now around $5 trillion, Saxo is currently a relatively small player but it is looking forward to a strong and long runway of growth.

> "We have state-of-the-art execution. Historically the market was rather opaque, but we are now bringing more transparent price discovery."

Mathias Österberg, CEO
GRIT Governance

GRIT-ting the Finnish Hedge Fund Industry

By Eugeniu Guzun – HedgeNordic

Finland has historically had the lowest number of active hedge funds among the Nordic countries. High barriers to entry, ranging from high start-up costs, complex idea-to-launch processes to regulatory hurdles, can be the all-encompassing answer to the question of what has suffocated growth within the Finnish hedge fund industry.

Finnish fund solution provider GRIT Governance, with its roots at the oldest hedge fund manager in the Nordic region – Estlander & Partners, has set out on the mission to "help the daring build legendary investment businesses" in Finland and beyond by lowering barriers to entry. "Typically, new managers have great, at times unique ideas when it comes to investment strategy," observes Mathias Österberg, the CEO of GRIT Governance. "They have asset-raising capabilities in their core team, and possibly potential seed investors lined up," he continues. "But the "now what?" question that comprises the next step of the build-your-investment-business process is at times overwhelming."

By partnering up with trusted and experienced fund solution providers, investment managers can speed up the idea-to-launch process and hit the ground running. "Having the ability to tap into the experience and connections of someone who has started dozens of funds over the years is a great way to get a picture of the road ahead," explains Österberg, who has been at the helm of GRIT Governance since its spin-off from Estlander & Partners' hedge fund business in 2019. "Aspiring managers that value opportunity cost and want to hit the ground running, find it most efficient to bypass the hurdle of building everything from scratch."

REGULATION AS AN OBSTACLE

While emerging managers may be well-placed to start a new fund based on their career and experience, setting up a fund or a hedge fund can be a long and arduous task. Regulatory hurdles – or lack of understanding of regulations – have often been cited as one of the biggest deterrents for emerging managers thinking about launching a new fund. "It would be easy to sweepingly conclude that increased regulations represent a barrier to entry," reckons

"Having the ability to tap into the experience and connections of someone who has started dozens of funds over the years is a great way to get a picture of the road ahead."

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Österberg. "However, the regulations themselves are fairly straightforward to understand for people that have been within the industry for a number of years."

"The true murderer is the psychological barrier that these regulations create," emphasizes Österberg. Where do I start, which regulations are relevant to me, and what happens if I get something wrong are just some of the questions popping up in the heads of emerging managers. "This series of questions kill a lot of the enthusiasm before you even get to evaluating the economic viability of your idea," considers Österberg.

The main appeal of partnering with an experienced fund hotel or fund solution provider is that investment managers can focus on their main areas of expertise by letting someone else handle the groundwork. Already-established fund managers are increasingly starting to see the benefits of partnering up with fund solutions providers as well, observes Österberg. "Not so much for cost-saving reasons," he argues, as many managers run their operations very streamlined to their needs. However, "they see the need to clear the table from distractions" to avoid the headache and constant need to stay on top of upcoming regulations that may or may not impact them.

GRIT'S DNA AND EVOLUTION

"Staying atop of existing and upcoming regulations is a challenge for both established and emerging managers," points out Österberg. In addition to the primary duties of maintaining and growing clients' investments, fund managers face an extensive laundry list of administrative tasks and duties when running an asset management business. "There are a bunch of other issues that are or can be challenging depending on your background and existing systems," points out Österberg. He refers to everything from creating compliant processes for investor onboarding, transfer agency, reporting to investors and authorities, connection to platforms, to the more mundane but just as important to get right; striking NAVs and handling investor practicalities. Fund hotels, however, can help fund managers get their affairs in order.

GRIT Governance's fund services platform has been born and developed under the umbrella of Estlander & Partners, and has, therefore, been involved in running and servicing the systematic quant-driven hedge funds within Estlander & Partners. "We come from a CTA, market-making and hedge fund background with a history of building and maintaining in-house systems all the way from the 90s, and own funds since the early 2000s, so we're somewhat of natives within the derivatives and high trading intensity world," asserts Österberg. GRIT Governance has gradually broadened its scope to serve cash equities and similar plain-vanilla investment strategies.

> "The true murderer is the psychological barrier that these regulations create."

"Our current funds are split quite evenly between hedge funds and equity funds or fund-of-funds, where the hedge fund side has a clear tilt towards systematic derivatives-based investment strategies," summarizes Österberg. Having built a comprehensive infrastructure for both AIF and UCITS funds, GRIT Governance can service a wide range of investment approaches, much less so fixed-income-focused strategies. "If I have to look for a weak spot, I'd put my finger on bond strategies," acknowledges Österberg. "Our systems can handle them, but our thinking hasn't quite adopted the world of bonds," he explains. "Proper high-frequency trading (HFT) with tens of thousands of lines per day would also need a bit of extra consideration before onboarding."

MINIMUM VIABLE SIZE AND NEW COMPETITION

One of the most important reasons for engaging in a fund hotel outsourcing, besides streamlining the day-to-day complexity to focus on core competencies, is to reduce fund administration costs. "Businesses are different, some start with a larger AUM with little view to raise additional assets, whereas some start with 'founders&friends' capital only but with a very detailed marketing and asset raising plan," says Österberg.

"There are a lot of factors that affect your costs, but as a rule of thumb: as long as your AUM is below €10 million, someone in the chain is working for free," considers Österberg. "We review setups on a case-by-case basis rather than having a fixed minimum AUM as basis for qualification, and in the cases where we've come to the conclusion that honest feedback on the viability of your investment business idea is in order, we've given such feedback."

Hedge fund start-ups face an uphill battle to gain a foothold in the sizable and mature hedge fund industry and differentiate themselves from an already-diverse crowd. Therefore, GRIT Governance observe a trend of new managers being more innovative in the face of stiff competition. "Due to our background and network, we've always had a predisposition for managers with a more innovative approach. Or maybe the predisposition goes the other way around," says Österberg. "One thing that has popped up quite prominently lately is a new generation of managers that want to differentiate themselves from the old-school 3-piece-suit kind of wealth management," he emphasizes.

New managers know how to individualize their offering, know how to market on social media, have high expectations on end-user experience throughout the process, and demand the same from their providers," according to Österberg. "They are clearly on to something, and if the stuffy older managers don't watch their backs, the new generation of managers are going to attract a big piece of the flow over the next few years."

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Emerging fund managers: Are you ready for Institutional capital?


Rowen Pillay, Co-Founder & CEO - Edgefolio

By Rowen Pillay - Edgefolio

Congratulations. You're 3 years into your journey as an emerging hedge fund manager. Only the strongest have survived, and your fund is one of them.

3 YEARS IS A MILESTONE FOR ALL HEDGE FUND MANAGERS

- Three years is a common prerequisite for institutional investment, and the minimum timeframe requirement for a listing on Morningstar. [1]

- Most emerging fund managers fail within three years. You should be proud that you've braved the odds and are still here…

- Especially tough during two bear markets and the worst pandemic for over a century!

However, now the really exciting and challenging opportunities begin. All successful emerging hedge funds will be looking to leverage their three year survival to increase their AUM. Institutional capital is inevitably an essential part of this.

Institutional investors have greater resources, impact and influence on the market and the assets they invest in, therefore –

- You need to figure out your strategy's true capacity, then when and how you're going to prospect professional investors.

- Institutions rarely invest with solely their own money; this means grappling with the considerably more robust governance and due diligence requirements of their clients, customers and shareholders.

- Bigger portfolios also mean bigger allocations, leading to higher initial subscriptions than HNW, wealth managers or family offices.

BEFORE MARKETING FOR INSTITUTIONAL INVESTMENT, DEFINE YOUR IDEAL INVESTOR

Before you pitch, or even start to plan your roadshow, get your sales and marketing team to create a 'Buyers List' of your ideal institutional investors. Make sure they consider the following criteria:

- Who will they be? Corporate pension providers? Public pension providers? Sovereign wealth funds?

- What sort of expertise do these investors have in your sector? How might this impact their DDQ processes?

- Are they investing in your competitor's funds?

- How much do they typically invest in emerging funds of your size?

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- Will they be able to give you your ideal amount when you need it?

- What's the time zone of the company's main office(s). If your key contact operates in a very different time zone, this might make it harder to arrange meetings.

ONCE YOU'VE CREATED A LIST OF IDEAL BUYERS, GET READY TO PITCH YOUR EMERGING FUND

Leverage and grow your network through LinkedIn, attend in-person or online conferences, send great prospecting emails, and write thought leadership content that will appeal to your ideal investors.

The way you engage, get investors to feel confident about you, and build relationships, are just as important as the technicalities. You want them to get enthusiastic about working with your team before they commit any capital to your fund.

FIGURE OUT HOW TO ANSWER THE 'WHY YOU?' AND 'WHY YOUR FUND?' QUESTIONS

Hedge funds must differentiate themselves to survive.. Focus on developing a consistent narrative to avoid confusing your investors. They need to understand what the opportunity is, and how you, as an emerging fund manager, can take advantage of it.

- What makes you, your strategy and your team investable?

- Why should this investor pick you and not thousands of other fund managers?

- Research your competition and peers rigorously so you can confidently differentiate yourself from other emerging funds.

BE PREPARED FOR TOUGH QUESTIONS ABOUT YOUR EMERGING FUND'S PERFORMANCE

You need an exceptional track record and a coherent investment strategy which can withstand intense scrutiny. An institutional investor will quickly become sceptical if your claims don't correlate with the data.

For example, if you market your emerging fund as generating consistent alpha, and the majority of the companies you invest in are US-based equities, an institutional investor would expect you to outperform a reliable market index, such as the S&P 500. Contrast that to if, from March 2020 to December 2021, your fund grew by 50% and had significant exposure to US tech stocks, that would be a substantial underperformance compared to the S&P 500's exceptional 100% growth during that same period.

The lesson here: know your stats and contextualise them confidently.

BE TRANSPARENT ABOUT YOUR EMERGING FUND

Institutional investors need to know their capital will be safe in your hands. So be honest: if you took a risk that didn't pay off, how did you analyse and evaluate?

Other topics that might be on your institutional investors' checklist:

- Tax: What are the tax implications of investing in your emerging fund? Your investor will need to look at any potential pitfalls and tax issues they might be exposed to. Be prepared to address concerns.

- Diversity: More institutional investors are asking investment managers about their commitment to diversity, equity and inclusion (DEI). Research by Credit Suisse has found that firms with women strongly represented in their senior management enjoy a diversity premium consisting of higher spare price returns. Hedge funds are frequently criticised for their lack of diversity, yet 9 out of 10 hedge funds surveyed by the AIMA said improving DEI was 'very important' or 'important' for sourcing talent. Less than 5% of hedge fund managers have a formal DEI initiative, so those that do could stand out against their competition.

- ESG: Similarly, more institutional investors are demanding to see ESG incorporation. How do you screen the assets you invest in? Have you generated alpha from integrating different types of ESG factors into your portfolio? Do you know which ESG issues your ideal investors are most concerned with when considering emerging funds for their portfolios?

REMEMBER: YOU'RE IN THIS FOR THE LONG HAUL

Expect to meet with your prospective investor(s) several times over the course of 6-12 months. That's because it's normal for institutional investors to meet with hundreds of fund managers each year. Many also need to strategically adjust their portfolios before they can re-allocate any capital, so timing is everything

So be patient and disciplined. Focus on building your relationships first.

FIVE WAYS A DIGITAL FUND MARKETING PLATFORM CAN HELP YOU SECURE INSTITUTIONAL INVESTMENT FOR YOUR EMERGING FUND:

- Use the best-in-class technology and tech stack

Institutional investors will expect your investor relations platform to be just as robust as that of a seasoned investment manager. Fortunately, with Edgefolio's FundPortal, you can streamline your tech stack in an all-in-one client communications platform.

- Make sure your investors can get the information they need, when they need it

Being transparent is vital for building trust. That's why FundPortal allows your investors to access all the documents and data they need to scrutinise your fund's performance.

- Scale your business development

Growing an emerging fund is never a smooth process. Fortunately, with Edgefolio, you can harness the power of an investor portal, dataroom, CRM, behavioural analytics, peer analysis, email campaigns, and more, all from a single fund marketing platform, to deliver consistent AUM growth and retention.

- Tell your story through marketing

Without effective, consistent and engaging fund marketing content, you'll find it harder to manage your long-tail of prospects and build relationships with your ideal institutional investors.

- Attract more investors – raise more assets – make more money

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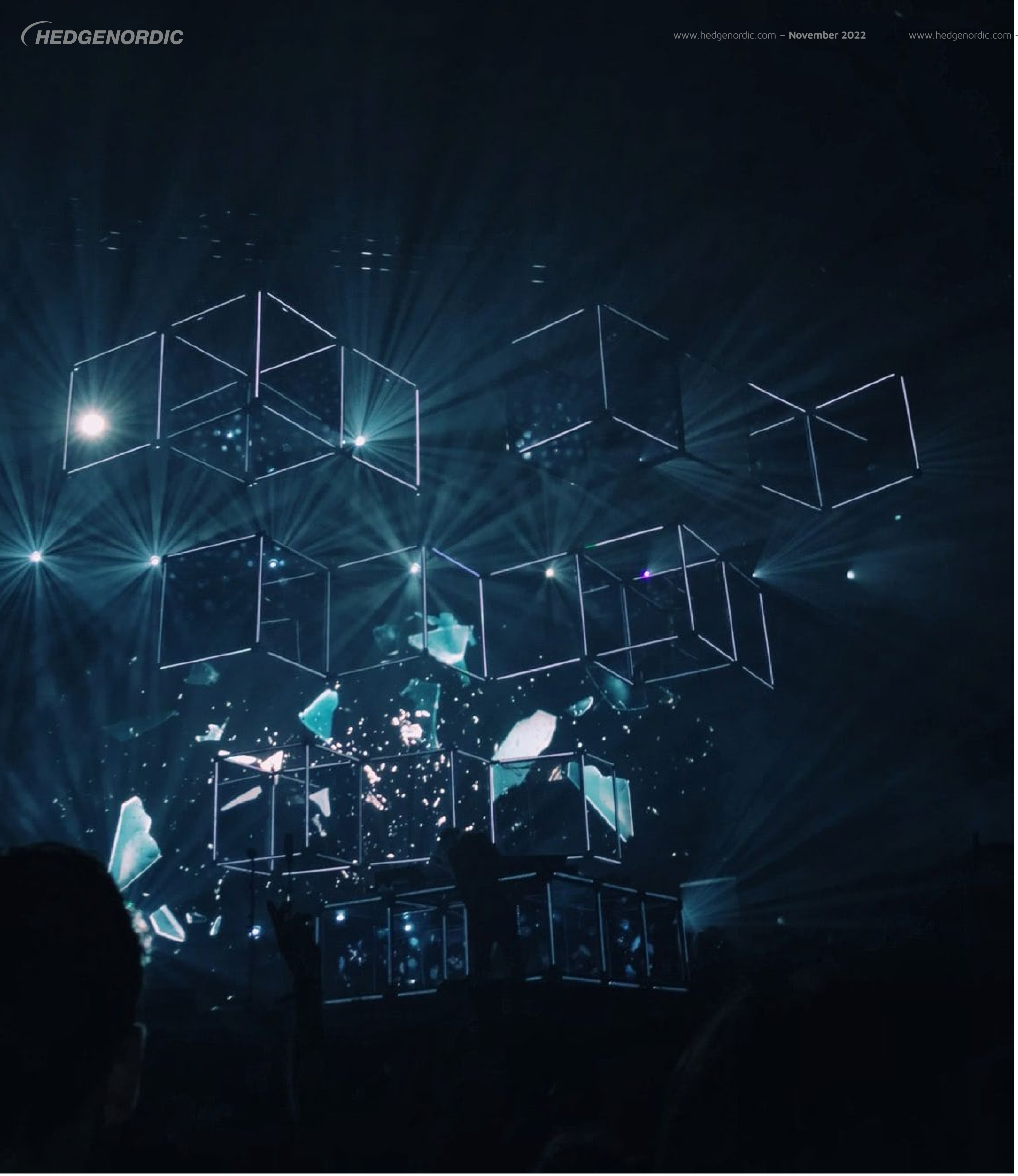

Fund operations: The explosion of algorithmic trading

As financial markets become increasingly efficient and faster-moving, fund managers are having to adapt their operating models accordingly. Technology plays a key enabling role in this evolution, as does the human element. Both need to be managed optimally and rebalanced to get the best results. Ryan Guichon, Product Head for Fund Administration & Accounting Services at RBC Investor & Treasury Services, provides his insights on how fund operating models are evolving to align with today's dynamic market environment.

ADAPTING TO ALGORITHMIC TRADING AND PASSIVE STRATEGIES

The popularity of new investment vehicles driven by algorithmic trading systems is exploding. These system-driven investment strategies are bringing about significant change to the fund operating model. This change requires the development of new inter-connected systems to keep execution of the investment strategies "between the lines"—much like how a self-driving car keeps passengers safely on the road. According to Guichon, a big part of the change requires an understanding of data science within middle- and back-office functions, enabling fund managers to take a step back from execution and focus on oversight.

"Index funds, for example, have a relatively simple coded strategy, which is to say: 'This is the list of instruments that we will be investing in, given to us by the index engineering team, and we will rebalance these positions on a set cycle.' The investment strategy has been simplified to such a degree that complexity has arisen in other parts of the fabric—the trading strategy. With the efficiency of today's markets and increasing liquidity challenges, the window to get in and out of investment opportunities is shorter, which is driving a change in how funds oversee their models. The market no longer provides time to oversee each individual trade, so the models require built-in risk-governance mechanisms that you then oversee, rather than looking at each individual trade. It's all about taking that step back."

MANAGING THE HUMAN ELEMENT

While much is made of the importance of technology in driving these changes, Guichon emphasizes that the human element cannot be overlooked. "As change occurs, people will be asked to apply their expertise in different ways, in different settings and working with people who have unfamiliar competencies. Clear communication is needed to provide employees with context for the change: Why is it happening? What will it deliver? How will I fit into the new system?"

Guichon says it is important for employees to understand that change is about applying their tools in a different setting. It involves helping them to understand that the nature of their work is going to change, and why this is a good thing.

"For example, take someone involved in fund accounting who historically enjoys getting into the ledger entries and reviewing them for valuable insights. If this is no longer a requirement, because the ledger entries are happening so quickly that the review process needs to be automated, then the person's role may become overseeing the exception system that runs the review process. Or they may get pulled into a new area where they can apply their skills and experience in a slightly different context. Making the effort to clearly communicate the rationale and benefit of change will make it easier to sell that change and get buy-in."

ADOPTING DISCIPLINED DATA MANAGEMENT

In an environment of increased automation, effective management and documentation of data

"A big part of the change requires an understanding of data science."

"For employees, change is about applying their tools in a different setting."

transmission and lineage are more important than ever, says Guichon. "As you change your systems, you need to understand how data moves between your front, middle and back offices, and institute best practices for documentation, control mechanisms, and data and system architecture.

At the core of this is detailed documentation of every critical process and system that touches your data. Over time, the people who developed the systems will move on to other projects or jobs, so you require the documentation to understand why a system was set up the way it was, and how any changes will impact your data and other systems within the overall architecture. Otherwise, you run the risk of projects that never end and stall other impactful investment opportunities."

To support the increased pace of change within fund operations, Guichon recommends a modular approach to system development and data management. "I'm a big proponent of purpose-built architecture, where you have individual systems built to execute specific functions. This allows you to measure success more easily—with a data model built over time to power future learning applications. You can also pull old systems and slot in new ones more efficiently, providing greater freedom to adapt to new demands on your operations, whether it's a new regulatory requirement or a new investment product with unique data requirements."

KNOWING WHERE AND HOW TO FIND VALUE

Guichon notes that tackling operational change can be overwhelming, adding that a clear understanding of a project's value and success metrics goes a long way toward selecting the right projects.

"With pretty much everything on the table, it can be challenging to know where to start. Markets are changing very quickly, and there's an expectation of responsiveness and adaptability, but change for the sake of change is a misguided approach. It's important to evaluate projects based on the value they will bring. Understanding a project's value and communicating how to measure the value is key. There need to be clear gates and success criteria for a well-directed process of change."

Ryan Guichon, Product Head for Fund Administration & Accounting Services – RBC Investor & Treasury Services

"Change for the sake of change is a misguided approach."

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An Allocator's View on Effective Hedge Fund Marketing

By Shaunak Amin and Joe Peta – Novus

"Bud Fox, I look at a hundred deals a day. I choose one."

Gordon Gekko after a pitch from a prospective broker.

Despite the hilariously outdated technology props and some extinct jargon, Oliver Stone's Wall Street is still revered by financial industry insiders. Even today, more than 25 years after its release, Wall Street is regarded as a realistic depiction of the industry largely because the film nails the dynamics of some important relationships in the business.

Take the above quote, for example. Fund managers are perpetually being pitched. Sell-side analysts fill portfolio manager's voice mails and inboxes with research ideas. Bankers want to bring their traveling roadshow to the buy-side office to pitch the latest company issuing paper. Today's fund managers, just as Gordon Gekko implied, know how irritating it can be to face a bombardment of pitches that all look alike.

And yet, based on our discussions with allocators (endowment, pension, fund of funds or the like), when the tables are turned – when the hunted becomes the hunter – and managers need to do their own fund raising, many of them forget that very lesson.

Allocators who interview hundreds of managers each year tell us that it's paramount for managers to distinguish themselves. One sure way not to do that is for managers to tell potential investors that they "have an edge" without accompanying evidence.

From the perspective of a hedge fund looking to raise capital, it can be perplexing to think about how allocators are making decisions about investing capital. One wonders if there is a clear path to moving things forward, and could one have improved the chances of getting a follow-up meeting? Let's find out by getting into the minds of allocators.

SILLY BUT TRUE

- Allocators will prioritize a fund that is "soft-closing" vs. a fund that is perpetually open. It helps to have phases when you exclusively meet with allocators and other phases when you are focused on investing. It builds up demand. Deadlines help.
- Playing hard-to-get works.
- The biggest influence on investors' opinions of a hedge fund is the opinion of other investors. There are very few who simply decide for themselves.

When an allocator hears about your hedge fund from a peer at another firm, you've already done the heavy lifting. To this point, it can help to have a mind map of who knows who. Similarly, the same effect can cause one allocator to redeem when someone else is redeeming.

- The story is what people remember.

- Like it or not, your fund is "bucketed" in a particular strategy/style in the allocators' book. Knowing your "bucket" helps anticipate questions.

HOW CAN A HEDGE FUND HAVE AN EFFECTIVE FIRST MEETING THAT RESULTS IN A FOLLOW UP?

In a typical year, an allocator meets with hundreds of hedge funds. Most first meetings tend to be centered around topics like pedigree, research process and edge, ideas and theses on those ideas. After an allocator has 20 of these meetings, the story starts to sound the same. This routine does not give an allocator a true sense of what makes a manager unique. An open-ended meeting is often ineffective and results in no clear next step.

> "For the first meeting to be effective, a hedge fund must articulate its value proposition to prospective allocators. Numbers and actual unadulterated statistics are more impactful than esoteric conversations around processes"

Skill-set	***Evidence***
Security Selection	High batting average and win/loss ratio at the portfolio level and for different slices of portfolio (sector, market cap, geography). Both absolute and relative (portion of return coming from security selection) ratios are relevant.
Expressing Conviction	Proof that position sizing has added value over time. What is the return on invested capital on smaller names vs. core names? Offer a return comparison to an equal-weight portfolio.
Market Timing	Proof that managing net exposures has added value.
Category Allocation	Proof that being in the right sector/sub-sector/asset class/geography has added value.
Trading	How much of the total return is attributable to trading? How do actual returns compare to a zero-turnover portfolio?

A better way to differentiate your value proposition

One of the most common questions an allocator is trying to answer is "What's the edge?" While the question itself oversimplifies investing and carries some implicit assumptions, a simplistic, unsupported answer like "Our edge is security selection/research" by itself does not hold much weight. Talking about one or two high-conviction names does not really answer the question either.

For the first meeting to be effective, a hedge fund manager must clearly articulate the value proposition to prospective allocators. Numbers and actual unadulterated statistics are more impactful than esoteric conversations around processes. For example, if research and security selection are indeed core drivers of returns, a more thoughtful answer would involve statistics that prove a manager is actually a good stock picker. One approach to highlight persistent security- selection skills would be to lay out batting average and win/loss ratios by sector/market cap/position size/liquidity or any other category that is most relevant. The table on the previous page lists a variety of skill-sets and how to present evidence of their existence.

Consider that for the first meeting to be effective, it is important to share with allocators:

1. The true value proposition, supported by skill-set-centric results.

2. The elements that differentiate your fund from other hedge funds.

What not to focus on in the first meeting?

The risk in covering too much in the first meeting/call is that allocators spend 90% of the time on a topic that makes up less than 10% of the book and is not core to the overall strategy. These topics could be P&L derived from IPO's or a few private positions that make up a tiny portion of the book. This is often unintended and it should be avoided.

The goal of the first meeting is to take baby steps to get to the second meeting; spending too much time on a small portion of your book can derail the conversation.

WHAT IS EFFECTIVE HEDGE FUND MARKETING?

The world of marketing has changed, and it's critical for managers to rethink how they communicate with investors by taking a moment to see things from the investor's point of view.

Investors today have access to more information than they can effectively consume. They are being bombarded by emails, marketing brochures, pitch books, and bold claims from managers competing for their capital. Increasingly, this sort of "push marketing" is having less impact on investors who have heard it all before. To be competitive in today's environment managers need to differentiate themselves by clearly demonstrating their value to the investor through data-supported narrative.

An increasing number of innovative managers have evolved their marketing efforts by tapping technology and data analytics to help them quantify the value they deliver. Through the use of portfolio intelligence tools, they have gained an edge in raising and retaining capital.

Demonstrating their skill and highlighting the drivers behind their investment process, these managers can substantiate their claims and win the trust of investors along with their capital. In the meantime, managers who continue to rely on subjective claims alone will be at a significant disadvantage, even if they are as skilled as they claim.

Here are four specific steps to take your marketing to the next level:

1. Focus on what makes you unique

Investors are looking for unique opportunitiesnot another "fundamental I/s" fund. Focus on your key differentiators and connect them to your background and expertise.

2. Align your message with the objectives of your investors

Investors from pensions to funds of funds are faced with criticism of putting up with sub-par returns, paying high fees and not fully grasping the complexities and risks of hedge funds.

Whether they are looking for uncorrelated sources of returns, absolute returns, or alpha, it is your job to understand investor needs and challenges.

3. Talk about your "fund" as a business

Besides running a portfolio, you are running a business, and investors are keen to understand the strengths and challenges of your organization.

Organizational structure is often highlighted in marketing documents but few talk about organizational 'health'. What is the reason the fund was launched? What are your beliefs and guiding principles? If you are clear on those and you dedicate time to them in your messaging, you are more likely to attract strong, long-term partners who share your values.

The rest of the article will focus on our final point – and one we feel is most critical in separating effective marketing from mediocre. It is the ability to show value rather than just tell folks about it.

4. Show, don't tell

A picture is worth a thousand words. In our day and age, it's worth a lot more since no one has the time to read a thousand words but they are happy to quickly glance at a chart and discover the insight for themselves. Of course, it's critical which data you choose to visualize.

> "Fund managers need to be able to stand out not just by telling investors
>
> what they are good at, but by 'showing' or proving their value proposition
>
> in a compelling, easily retained way."

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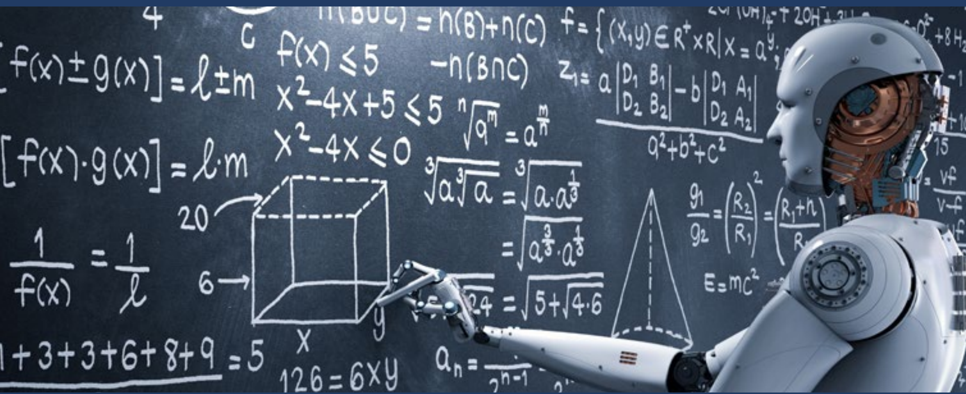

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