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FINANCIAL NEWS

at GAIM

‘Internationally, there is considerable demand for long-short Japanese equity funds’

Charles Beazley, Gartmore

Asian hedge fund industry

Funds investing in India returned annualised gains of nearly 44% last year, writes Fionnuala Synnott

Investors are exploring the potential of hedge funds based in the Asia-Pacific region as successful US and European managers come up against capacity constraints. Assets managed in the region now top $60bn (€49bn), according to industry estimates, and are expected to reach $85bn by the end of the year.

Performance last year was disappointing compared with 2003, with the ABN Eurekahedge Asian Hedge Fund Index gaining almost 9% compared with 27% the year before, but growth remains robust.

Alexander Mearns, director and chief operating officer of Eurekahedge, said: “While the rate of growth of the industry has slowed from the explosive 50% increase in numbers we saw in 2003 to around 25% growth in 2004, we believe that this is indicative of a rapidly maturing industry.”

The region’s hedge funds are increasingly popular with investors in Europe. Swiss investors accounted for 40% of asset flows into the region’s funds last year, with UK and US investors contributing 25% each, according to Eurekahedge.

Mearns said there is a growing interest in Asian hedge funds from US investors, while Japanese institutions are increasing allocations to single-manager strategies in the region.

He added: “There is also an increasing demand for emerging market hedge funds, particularly in Asia. The China and India growth stories are attracting a lot of investor attention from the US, and the rest of emerging Asia is firmly on the radar of European investors looking to diversify portfolios with quality managers.”

Funds investing in India were top performers last year, returning annualised gains of 43.85% on average.

There are still plenty of opportunities for institutions looking to include Asian hedge funds in their asset allocation.

Start-up funds appear regularly. There were 22 launches of funds in Asia including Japan last year, according to Eurekahedge, up from 14 the year before.

Japan has been a focus of attention. Research by Eurekahedge found the strongest asset flows in 2004 were to Japanese funds, at 41% of all flows to the region, totalling almost $8.2bn. Assets in Japan-focused funds have increased by almost 82% since 2003.

Charles Beazley, head of institutional and alternative investments at Gartmore, the UK fund manager, said: “Internationally, there is considerable demand for long/short Japanese equity funds,” adding that the level of institutional investor demand far outweighs the number of institutional quality funds on offer.

Derek Stewart, a director at Mellon Global Alternative Investments, said the Japanese hedge fund market has changed dramatically in the past decade.

He said: “In 1996, there were only two or three hedge funds in Japan. Whereas before, it was mostly foreigners who ran hedge funds in Japan, there has been a recent growth in the number of domestic hedge funds and there are signs that the Japanese market is entering an innovative phase.”

Operators desert Hong Kong for Singapore’s lighter regime

Singapore has eclipsed Hong Kong as the top location for hedge fund start-ups in Asia-Pacific with 19 fund launches in 2004.

This is largely due to the shorter time it takes managers to register as investment advisers in Singapore and explains why big US funds such as Tudor, Everest and Moon Capital have decided to operate out of Singapore rather than from Hong Kong.

Singapore accounted for 20% of the new launches in the Asia-Pacific region in 2004, as opposed to 13% for Hong Kong. But Hong Kong still remains well ahead in terms of total assets under management, with about $9.3bn being managed from the city compared with Singapore’s $2.8bn.

‘New institutional investors cannot access the top 10 managers in Japan and it is difficult for them to penetrate the market’

Derek Stewart, Mellon Global Alternative Investments

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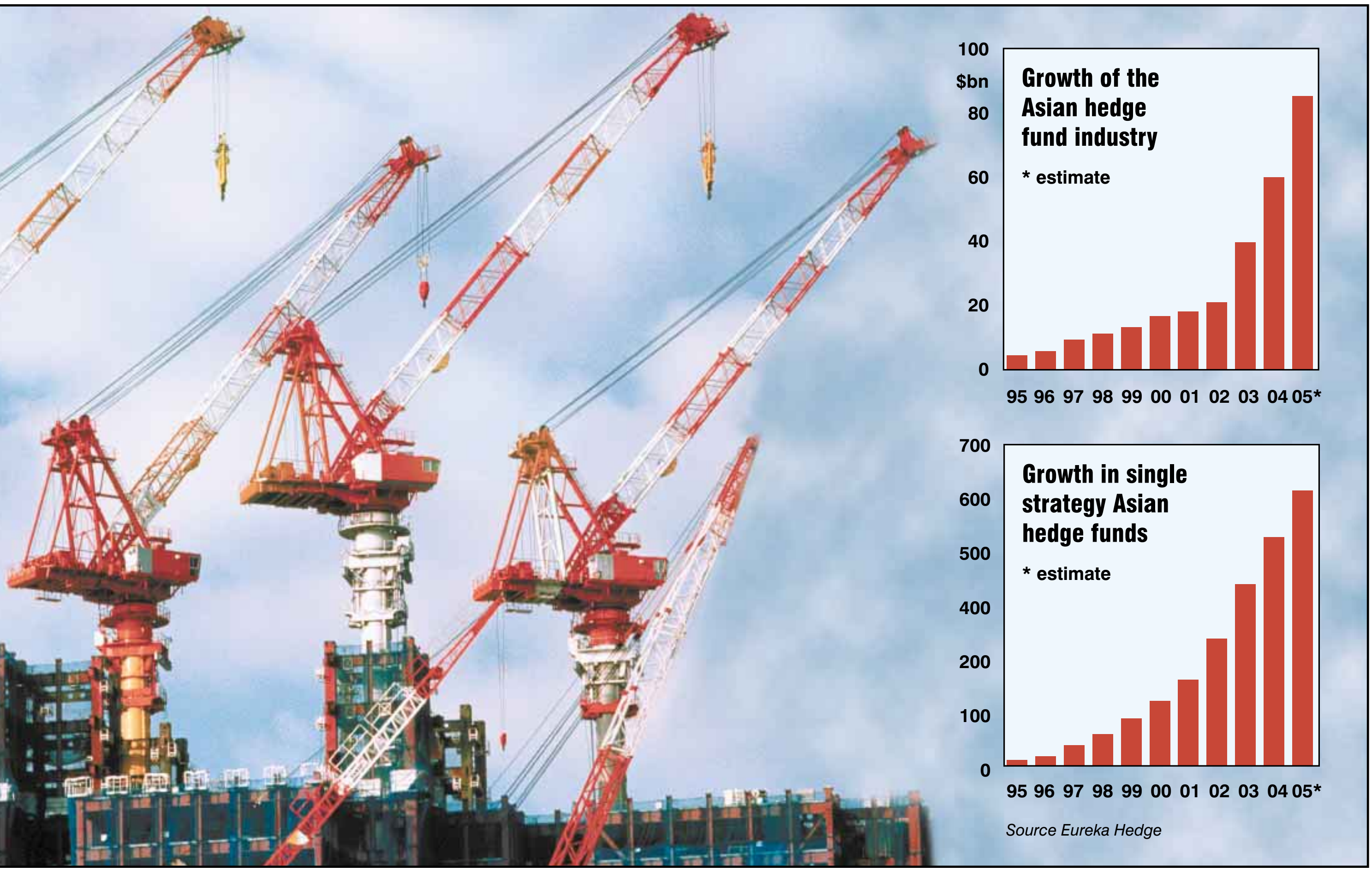
builds momentum



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There is a growing interest in Asian hedge funds from US investors, while Japanese institutions are increasing allocations to single-manager strategies in the region

Investors were initially slow to commit to Japan following a decade-long equity bear market. Stewart said: “In 2001 and 2002, institutional investors could have had their pick of almost any Japanese hedge fund but most held off investing until after 2003, when the Japanese market performed well relative to other global markets. This led to a rush for capacity in these funds.”

Many of the managers selected by the Mellon Nippon Absolute Fund, a fund of funds, have already reached capacity. Stewart said: “New institutional investors cannot access the top 10 managers and it is difficult for them to penetrate the market.”

Derek Doupe, executive director, fund of hedge funds at Schroders, expects to see new entrants in the market. He said: “There are tremendous opportunities in Japan. The restructuring of so many companies means more potential for long/short equities and event-driven strategies in particular.”

However, the of managers is not necessarily as high as investors would like, said Stewart. “Few good fund managers stuck out the bear market. Consequently, there was a significant drop-off in the quality and experience of the management teams.”

While long/short equity funds have traditionally dominated the hedge fund sector in Japan there are increasingly diverse opportunities for investors.

Mearns said: “There remains a strong predilection among Asian hedge funds for long/short equity strategies, with almost 60% of the universe falling under this category in 2004. But the domination of long/short strategies is expected to diminish as the number of proprietary traders launching macro funds, commodity trading pools and multi-strategy arbitrage funds increases.

“The impressive performance of distressed debt and event-driven strategies in the last two years means these approaches are also likely to be considered by new Asian funds.”

Stewart said that with hostile takeover activity emerging in Japan, and foreign predators entering the market, special situations, distressed debt and merger arbitrage funds are likely to see increasing activity.