AIMA AUSTRALIA ANNUAL FORUM 2017

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Stuart Roden with Jack Inglis

TOP FOUR TIPS FOR SUCCESS IN FUNDS MANAGEMENT

"THERE ARE ALWAYS REGULATORY ISSUES BUT WE CAN DEAL WITH THOSE. BUT WHAT WILL DETERMINE WHETHER WE DO WELL IS OUR PEOPLE. IN THE LAST 10 YEARS, WE'VE TAKEN ON ONLY TWO NEW FUND MANAGERS, ALTHOUGH WE'VE PROBABLY SEEN 70-80. IT'S VERY HARD TO FIND GOOD PEOPLE.

There are four things you need to be good at to be a success in funds management, according to Stuart Roden, the co-founder and chairman of Lansdowne Partners, the US$18 billion UK-based fund manager which has delivered an annual average return of 13 per cent since inception in 2001.

Interviewed by Jack Inglis, the global chief executive of AIMA, at the AIMA Australia Annual Forum 2017, Roden said the most important things for fund managers to have were:

- "Some creativity". You need people in the firm who "think differently". Roden believes you can recognise that in someone when you meet them. "It's how they observe life," he said.
- "Good analysis". This is a more common trait than creativity. An analyst who thinks like a businessman is better than one who doesn't, he said. They have to be good at modelling data and verifying whether something is good or bad value.
- "Risk management". You have to put a portfolio together so that it makes sense for clients. "We've had two bad years in 20," Roden said. "Risk management starts from the clients' objectives taking into account volatility and likely drawdowns."
- "Ongoing monitoring". You have to keep asking questions of the investment decisions, you have to forget about your entry price and try to be as dispassionate as possible. "All our teams are small, four or five people, who sit together… I'm a great believer in a team approach," he said, "but that doesn't mean consensual management. Emotionally, it's probably the trickiest. It's difficult to admit you are wrong."

Filling in for the unavailable AIMA Australia chair, Paul Chadwick, for the regular "fireside chat" at the Forum, on September 12, Inglis asked Roden why he stepped down from managing money to take up the chairman role at the successful firm this year.

The answer: "I had run money for a long time," Roden said. "And I wanted to work with some of the younger fund managers. We have four other portfolios and I wanted to make sure we had a firm with certain values that I think are important. I wanted to make sure that every employee believed in that.

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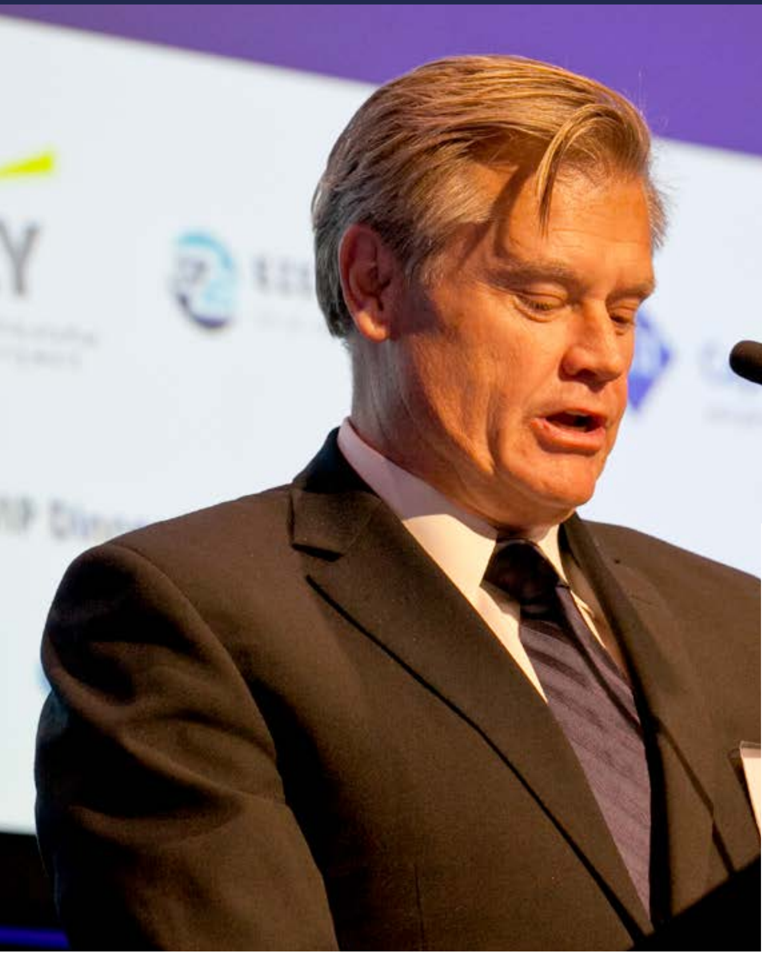

Michael Gallagher

MESSAGE FROM AIMA

The AIMA Australia Annual Forum 2017 has again set a 'high watermark' with a record number of sessions and speakers addressing an ever-growing range of issues shaping alternative investing.

Global industry leaders such as Dr Sushil Wahdwani, Thomas Weber and Stuart Roden presented a rounded perspective on the quantitative and fundamental approaches to non-traditional alpha against a backdrop of unconventional policies, rising ESG interest and growing levels of risk within markets.

This year we introduced an operations and regulations stream that ran concurrently with the main forum, attracting a strong contingency, reflective of how critical these issues are for de-risking and optimising outcomes for investors.

The Forum's 'outperformance' is consistent with other metrics that paint a stronger year for hedge funds, with inflows, performance and local AIMA membership all on the rise in 2017.

Special thanks to the support of our sponsors, members of AIMA's executive committee and industry volunteers that make the Forum accessible, constructive and enjoyable for the industry. New ticketing system Humanitix proved highly efficient and helped raise ticket fee donations to children's cancer charity Redkite.

Thanks also to our global CEO, Jack Inglis, for once again heading Down Under and this year jumping into the 'fireside chat' hot seat in Paul Chadwick's absence. We were also joined by Michael Bugel and Kher Sheng Lee from AIMA Hong Kong and Singapore, reflective of the Forum's firm place on the industry's international calendar, and Australia's importance to AIMA's global network.

Planning for next year is already underway with two quality key notes lined up for the AIMA Australia Annual Forum 2018, which will of course stay true to the Forum's charter, "by the industry for the industry".

Michael Gallagher, General Manager AIMA Australia

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Asked what he worried about most, he answered: "There are always regulatory issues but we can deal with those. But what will determine whether we do well is our people. In the last 10 years, we've taken on only two new fund managers, although we've probably seen 70-80. It's very hard to find good people."

Inglis observed that Lansdowne had spawned several other funds management firms set up by former employees, to which Roden replied: "If we don't have a place for them, I try to give them every support. It's much harder now to start a firm with $50-100 million or less. I don't want people at the firm who are unhappy."

> THE FED HAS RESPONDED VERY QUICKLY TO ANY WOBBLE IN RATES... WHILE THIS MAKES A RECESSION LESS LIKELY IT ALSO MAKES THE EXTENSION OF A [UPWARD] TREND LESS LIKELY.

Sushil Wadhwani

WHAT STRATEGY FOR THE FUTURE?

The best of three scenarios for the global macro scene to benefit alternatives strategies is also the most likely: that the US Federal Reserve finally normalises interest rates and this is followed by the European Central Bank and "maybe in my lifetime", the Bank of Japan, according to keynote speaker Dr Sushil Wadhwani.

The chairman and co-chief executive of Wadhwani Asset Management, admitted that "a number of strategies, such as macro, risk premia, and trend-following [momentum] have performed poorly since the global financial crisis, compared with traditional long-only strategies".

There were various reasons for this, Wadhwani said. Low interest rates meant that 'carry' opportunities shrank, because dispersion declined. Trading to short rates became less profitable, while other asset prices were also impacted.

But, what he thought was the most important reason was that policymakers' actions crimped asset prices. "The Fed has responded very quickly to any wobble in rates," he said. "While this makes a recession less likely it also makes the extension of a [upward] trend less likely."

The high correlations between asset classes since the GFC limited the opportunity set for alternatives managers, therefore limiting their ability to take risks. High correlations were particularly hurtful for trend-following strategies.

"In the US, the recovery is in its 100th month. The data back to 1987 [a market crash year] shows the longest recovery period to be 130 months," he said.

The three scenarios he imagines are:

- That the Fed normalises rates, followed by Europe and Japan. This will "benefit most strategies".
- There is another recession. The business cycle slowdown coincides with another crisis and policymakers have limited ammunition to fight it. In such a scenario, trend followers may do well but carry trade managers will suffer.
- More of the same: a continuation of the post-GFC world with lacklustre growth and central banks failing to make headway would mean that alternatives strategies would face a tough time.

His tip for investors was to look for strategies that may be okay across the range. Value, sentiment and non-trend strategies might be good examples to look at, he said. "You need a diversified strategy."

ESG PROVIDES ADDITIONAL OPPORTUNITIES FOR ALTERNATIVES MANAGERS

Ian Woods, Joanna Nash, Philippe Jordan and session chair Jeff Dunn

ESG principles are being integrated into most institutional clients' portfolios and, increasingly, the portfolios of investors through the wholesale and retail markets. How do alternatives stack up incorporating ESG processes? The answer is: it depends.

There is more to ESG than just screening stocks, says Ian Woods, the head of ESG research at AMP Capital. Applying a "positive screen", where the manager makes an active decision to include stocks to provide an additional risk/return benefit based on ESG principles is relatively easy with traditional fundamental portfolios – even long/short ones. But with systematic investing, such as smart beta portfolios there are more challenges. A lot of the issues to address require more data, he said. In private markets investing data was particularly difficult to source.

Australia, New Zealand and Europe were leading the way incorporating ESG into their strategies, according to Joanna Nash, the head of ESG investments in Australia at BlackRock. "In every RFP we do, the client asks us about ESG," she said.

But because of the nature of alternatives investing not all strategies are suitable for ESG integration. Philippe Jordan, the president of CFM International, said that with "trading strategies" – such as trend following – ESG tended to apply additional impact costs which were problematic. "It's probably only the 'G' which ads persistent value," he said. "In aggregate, the stats for the 'E' and 'S' are very poor… The best news about ESG is that the reverse is also true. That is, it doesn't take much value away. Unless you need to trade – then you are taking value away."

Thomas Weber

ALTERNATIVE RISK PREMIA AS AN ALPHA ENHANCEMENT

Alternative risk premia strategies are gaining popularity as a complement to both traditional fundamental strategies and high alpha-seeking strategies. But they will not replace alpha, according to Thomas Weber, a leading exponent.

Weber, the CIO and a co-founder of LGT Capital Partners, a big European alternatives manager, said that alternative risk premia (ARP) strategies helped investors to focus on alpha as a complement to other strategies and also as a tool to help negotiate fees. ARP strategies tend to be cheaper than fully active management.

He said that more than 300 risk premia factors had been "discovered" between 1964, when CAPM (the capital asset pricing model) was developed, and now. The main ones used by either specialised team or more diversified quant managers were: value, carry, momentum and defensive (such as low volatility). "But not all risk premia are what they promise to be," he said. "ARPs vary over

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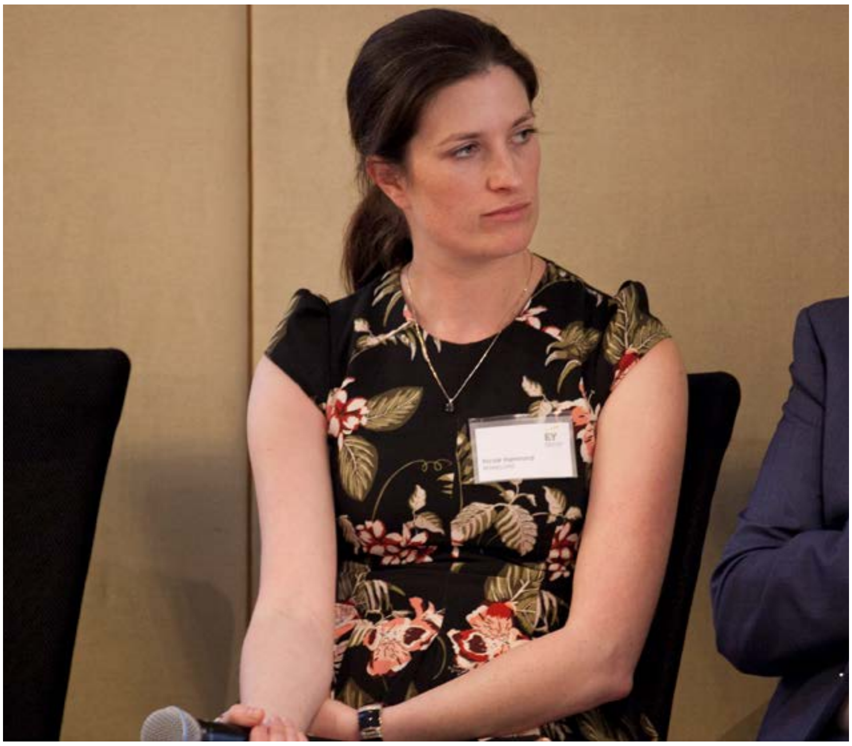
time and they are not homogenous. They don't provide consistent performance.

He said one of the issues that investors needed to keep in mind was that there could be "investor crowding" into risk premia. In the last couple of years, he said, there had been significant inflows. For instance, in 2016 there had been about US$15 billion in inflows into quant strategies in a general environment of net outflows.

Investors should remember August 2017, when a number of quant strategies suffered significant falls in returns. Goldman Sachs' market neutral fund lost 23 per cent in the month and the firm described the situation as "the best market-entry point ever". But a couple of years later the fund was quietly closed.



Nicole Hammond

HOW LICS CAN HELP REDUCE OPERATIONAL COSTS

LICs are becoming more popular with alternatives-style managers and one reason for that is they represent a way to save costs for operations and reporting.

Two of the speakers at a breakout 'Operations and Regulations' session at the Forum – Paul Mason, the COO of Montgomery Global, and Tim Bolger, the COO of Watermark Funds Management – spoke of the benefits of LICs, after initial prospectus costs and listing fees.

"We're looking at setting up a listed fund which will eliminate some of the costs and problems associated with unlisted funds," Mason said. For example, rating firms were becoming more expensive, he said, and they were requiring regular updates after an initial rating.

Bolger added that you did not need a three-year track record with an LIC, although managers normally had that and more from other funds. Nor did you need to provide daily pricing of the underlying investments, which may be unsuitable for some strategies, particularly in the alternatives space. But good communications is necessary to avoid them trading at a discount to the NTA of the underlying investments. "Our LICs are like toddlers," Bolger said. "We have about 15,000 shareholders in the three [LICs] and they are hungry for information. Those that trade at or above their NTAs generally are the ones which communicate better with their investors. We do two investor roadshows a year and we can see, time and again, that the shares will trade up afterwards."

Cathy Young, director of outsourcing provider Attentus Fund Solutions, said there was now a number of companies, including hers, doing middle-office outsourcing for start-up managers. In her view, unless a start-up outsourced those functions, it would have to have at least two people inhouse to do the work.

But costs associated with start-ups could become a burden too. Nicole Hammond, head of investment operations at multi-affiliate manager Bennelong, said that the firm tended to "bank roll" a team for about three years before it became profitable. "I don't think we'll incubate another startup," she said. "We'd prefer managers which have been operating for at least three years. That seems to be an acceptable benchmark."

John Claisse

HOW TO RETAIN A FIRM'S MOST IMPORTANT ASSET

"OPERATIONAL DUE DILIGENCE STAFF ARE CRITICALLY IMPORTANT IN AN INCREASINGLY REGULATED WORLD. THEY ARE BECOMING THE BACKBONE OF AN INVESTMENT MANAGEMENT FIRM.

The global hedge fund industry now manages over $3 trillion in assets. But pinpointing a firm's most important asset when looking through the lens of that much capital is a very difficult task. However, John Claisse the chief executive of Albourne Partners, an influential advisor for alternative investments, and Richard Quigley, of Goldman Sachs Asset Management, explained their thoughts on the topic.

What was overwhelmingly espoused was that talented, high quality staff are the most important assets. Attracting the right talent has become very difficult. To compound this further, hedge funds (and the wider investment and finance community) are faced with large technology firms poaching the high-end talent. There is an arms race for high quality candidates and the finance community is having to adapt. "Demand for high quality staff within alternatives managers has never been higher" said Richard Quigley.

However, between "the changing environment and fee compression the financial health of funds is not as strong as it was 10 years ago".

The question therefore remains, how can firms continue to attract young graduates and talented individuals?

It is important to remember that a one size fits all approach will not yield the best results when exploring a firm's decision to hire and fire. A manager has to think about the entire organisation, not just the investment side or front office. "It is a very different decision when you are hiring someone for a team of 5 versus a team of 100. Talent retention is seeded deeply into the culture of a firm and the culture affects every facet of the firm, including compensation" according to Claisse. Whilst compensation for talent is certainly important, pure economics is not a great indicator of retention.

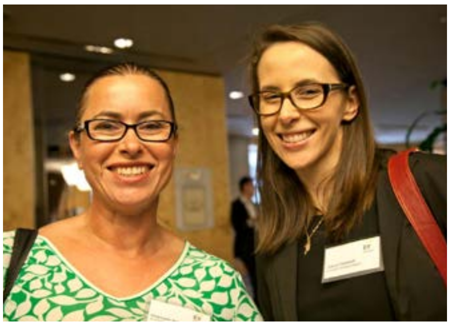
There has recently been a push for higher compensation and increased attention on the operation due diligence employees of a firm. "Operational due diligence staff are critically important in an increasingly regulated world. They are becoming the backbone of an investment management firm" said Claisse.

One of the key changes to the hiring process over the past 10 years is the use of internships. "We predominately hire graduates who have already interned with us before. This was not something that was so prevalent 10 years ago" said Claisse.

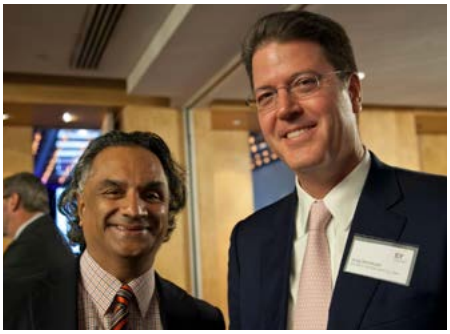
CAUGHT DURING THE BREAKS...

Jeremy Brugmans, TMF Group, Jason Denisenk, Allen & Overy, and Jason Huddy, ARCO Investment Management

Darren Parnell accepted the CAIA education scholarship for colleague James Mitchell of Boronia Capital



Stephanie Nolan and Jelena Campbell, GI Asset Management



Jay Moghe, Deutsche Bank and Greg Donohugh, Double Haven

Jennifer Lyon, Macquarie Group, Stephanie Rickard, ASIC, Susan Blanche, Regal Funds Management and Nikki Bentley, Henry Davis York

CAUGHT DURING THE BREAKS...

David Whitby, Bennelong and Meredith Jordan, Platinum Recruiters

Derani Brewis, GMO and Elizabeth Chisholm, Wellington

Mohit Kabra and Declan O'Callaghan, both Deloitte and Kevin Razavi, Perpetual

Rachel Shirley, Alexander Funds Management, Melanie Woodward, Tactical Global Management, and Nicole Hammond, Bennelong

Bronte Golding, Bloomberg, Gaye Anable, ITG, and Emma Cullen-Ward, OneProfile

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ABOUT AIMA

AIMA, the Alternative Investment Management Association, is the global representative of the alternative investment industry, with more than 1,800 corporate members in over 50 countries. AIMA's fund manager members collectively manage more than $1.8 trillion in assets. AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programmes and sound practice guides. AIMA works to raise media and public awareness of the value of the industry. AIMA set up the Alternative Credit Council (ACC) to help firms focused in the private credit and direct lending space. The ACC currently represents over 80 members that manage $300 billion of private credit assets globally. AIMA is committed to developing skills and education standards and is a co-founder of the Chartered Alternative Investment Analyst designation (CAIA) – the first and only specialised educational standard for alternative investment specialists. AIMA is governed by its Council (Board of Directors). For further information, please visit AIMA's website, www.aima.org.

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