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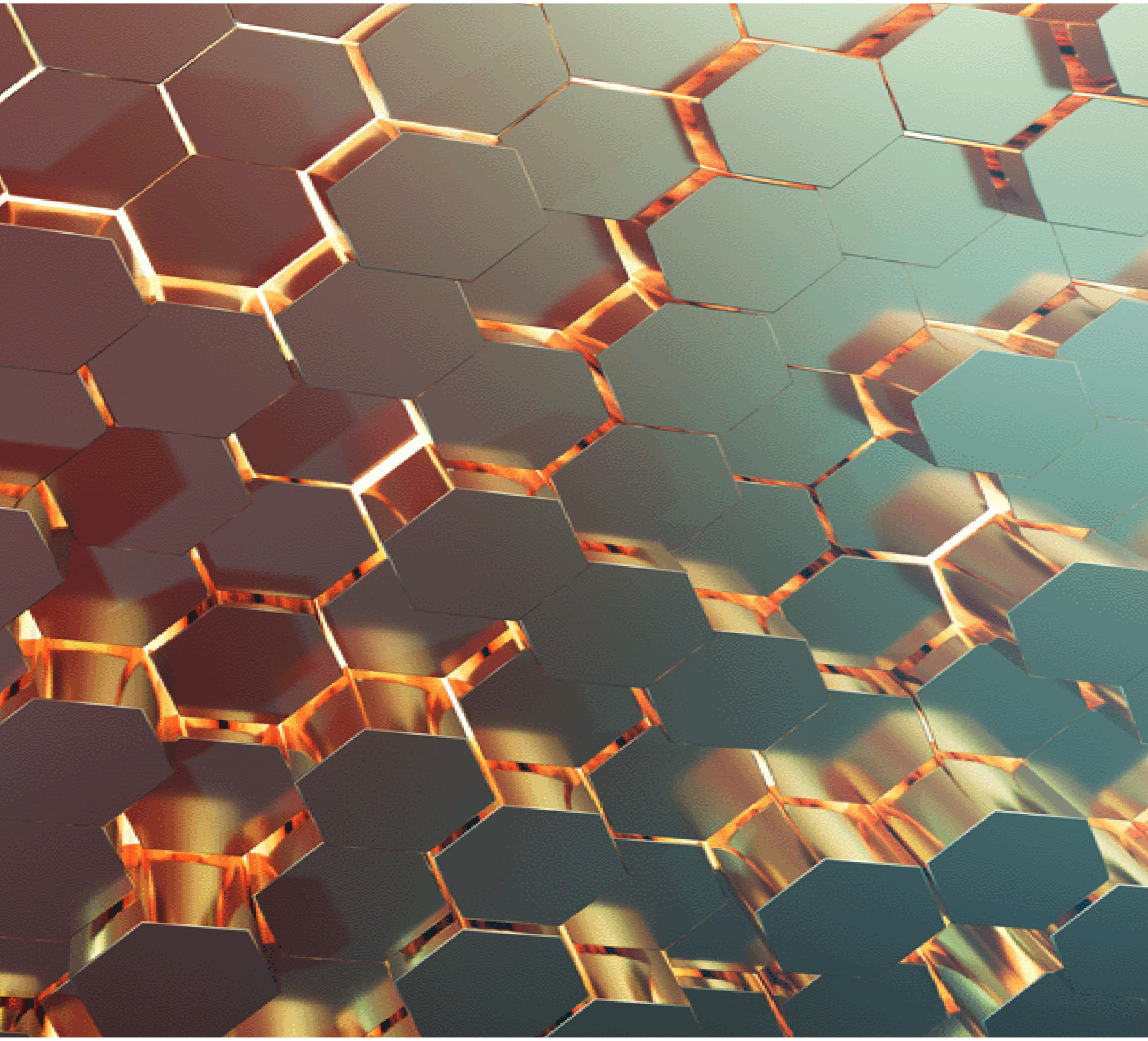


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MESSAGE FROM AIMA'S CEO

I am delighted to share our 122nd edition of the AIMA Journal. We are dealing with great uncertainty – the coronavirus pandemic has caused unprecedented social unrest and economic disruption. Our thoughts are with those people who have been impacted by this terrible virus around the world.

During these times of crisis, we are grateful to our members who have contributed to this edition of the AIMA Journal, providing key information on how the industry is shaping under current developments.

The publication starts with an article from **Broadridge** which compares how the hedge fund industry has fared during the current crisis relative to what happened in 2007-2008. The discussion focuses on fund flows. It concludes that, although the pandemic has inflicted some short-term damage to the hedge fund industry, the longer-term prospects for the sector are bright – as investors continue to need strategies that can deliver uncorrelated risk-adjusted returns.

BardiCredit then explores how the venture capital (VC) industry is changing and, importantly, how it may look once the pandemic measures are reversed and things go back to normal. One of the key takeaways from this insightful article is that the VC investment vehicles can become lower cost investment products focused on thematic ideas which appeal to a wider audience of investors.

Meanwhile, **Espresso Capital** provides a great risk-reward analysis of venture debt. This article particularly argues that young technology businesses, with great products and strong potential, struggle to attract finance that is not prohibitively expensive. Venture debt presents a solution for these businesses and an opportunity for investors who are searching for extra yield and are happy to put their capital at work for longer periods of time.

Remaining with private markets, **State Street** discusses how new technologies are enabling more investors to access opportunities in private equity, private credit, real estate, and infrastructure – areas which have traditionally been sold to a select group of highly sophisticated investors.

Maples Group presents two interesting articles. One of them is an analysis of how COVID-19 is impacting Jersey's investment fund industry. It focuses on emergency laws, business continuity processes, data and cybersecurity risks, marketing considerations and corporate governance in times of crisis.

The second one covers the opportunities that Asian markets offer for institutional investors: positive long-term economic growth, stronger rule of law and the increasing need for higher yielding assets.

We then turn to **CME Group**'s detailed analysis of how changes in investor expectations about future events impacts on market volatility. The article offers an insightful discussion on narrative economics, Bayesian inference and how to analyse market sentiment. Given the volatile times that we find ourselves in, this article is timely and incredibly relevant.

As policymakers all over the world continue to respond to the ongoing healthcare crisis, compliance requirements are likely to remain a top priority for the alternative investment management industry.

In this edition of the AIMA Journal, we present readers with a wide range of articles analysing various regulatory and compliance challenges that both hedge fund managers and their clients need to keep in mind.

As such, **ACA Compliance** provides an update on the inevitable replacement of LIBOR with other interbank reference rates.

Meanwhile, **Buzzacott** presents a debate on the right amount of regulatory capital that financial service providers have to hold in order to protect themselves and their clients during turbulent times.

Additionally, **EY Australia** reflects on the regulatory changes that are coming from Australia and which will have a much broader impact on fund managers worldwide.

Furthermore, **Deacons** provides an overview of how the Hong Kong hedge fund industry is impacted by the growing on-site inspections conducted by the Securities and Futures Commission. This provides readers with six common compliance deficiencies that their team observed during mock audits of hedge fund clients.

Deloitte highlights that despite increased uncertainty, Bermuda remains an attractive location to set up a fund, offering robust regulatory infrastructure and an extensive network of financial professionals.

Staying within the realm of laws and regulations, **Dechert LLP** explains how the line between hedge funds and private equity funds is becoming increasingly thinner. They argue that even if hedge funds and private equity funds have been fundamentally two distinct investment propositions, since the global financial crisis of 2008 a convergence between the two has been consolidating. The catalyst appears to be an increase in allocation to less liquid investments.

Last but not least, we turn to the topic of ESG. **Man Group**'s article explores the impact of COVID-19 on the growing ESG-investing market. It argues that there are three reasons of why allocations to ESG products are likely to continue despite recent market turbulence: firstly, it explains that ESG investment vehicles have performed well for investors in recent years; secondly, there are still opportunities within this universe at attractive valuations; and thirdly, the drivers behind ESG are long-term and still very much in place.

I hope you will enjoy the latest edition of the AIMA Journal. Please don't hesitate to share your thoughts and let us know if you are interested in contributing to any future editions.

Jack Inglis
Chief Executive Officer, AIMA

CORONAVIRUS CRASH: FUND-FLOW LESSONS FROM THE FINANCIAL CRISIS

Eric Bernstein
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As we approach what is likely to be one of the steepest recessions and economic contractions in living memory, it is inevitable that some asset managers will start panicking.

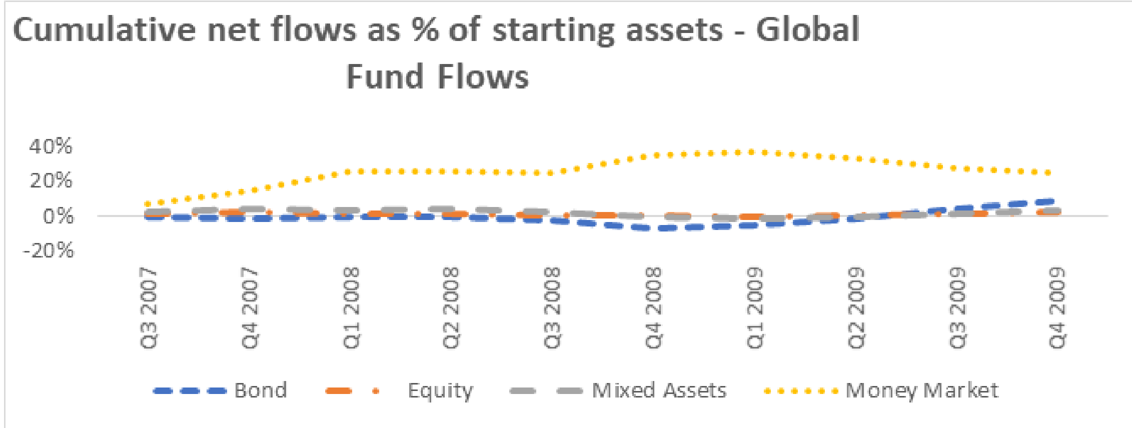
The volatility has sapped performance across many asset classes, heightening fears about the likelihood of mass client redemptions at traditional and alternative asset managers.

However, it is crucial that investment firms reflect on previous crises as these can shed light on how things might play out for global fund demand.

Admittedly, past market performance is not a guide to future returns, but fund sales are also driven by emotion. While each crisis has its own nuances, there is often a degree of similarity in investor behavior. Take the 2008 financial crisis, for example. From its zenith in 2007 to its nadir in 2009, the S&P 500 fell 50%. For many managers of alternative and traditional funds, that was an extraordinarily painful period.

Revenues dissipated while clients withdrew vast sums of capital, causing overall assets under management (AuM) to drop precariously.

For some managers, this was fatal. But the 2008 crisis was also notable for the speed at which the asset management industry recovered itself. With investors desperate for returns, they put their money into funds, especially those with diversified return streams.



Source Broadridge GMI, Radar Europe and Fund Buyer Focus

The above chart is indicative of the pace of this resurgence. Of the four asset classes identified, bond funds suffered the most in terms of declining sales and withdrawals, incurring a 7% loss of assets. However, bond funds were back in positive net sales territory (on a cumulative basis) within two years, illustrating the brevity of the disruption. In the case of money market funds, these actually continued to attract capital throughout the crisis as they were viewed as being a safe haven. It was only after the crisis receded that the cash in money market funds was reallocated into more rewarding asset classes.

Hedge funds are facing short-term challenges too as a result of Covid-19, but institutional investor appetite will eventually recover. Covid-19 wrong-footed a number of hedge funds to begin with, and performance initially suffered. As a result, hedge fund AuM dropped by $366 billion at the end of Q1 to $2.96 trillion, a steep decline from its record $3.32 trillion[1]. It also prompted investors to pull $33 billion from hedge funds in Q1, making it the biggest quarterly outflow since the financial crisis when $42 billion was withdrawn. Despite the gloomy projections, there is reason for optimism, especially if we benchmark current events against 2008. In 2008, hedge funds went on to beat the market, and investors returned in even greater numbers. Hedge fund performance in April 2020 was at levels unseen in more than a decade, and this achievement will have been noted by return-hungry institutional investors.

Why the future is bright for hedge funds

So who will be the managers that thrive in this adversity? In 2008, the firms that enjoyed success were the ones who had the foresight to diversify their businesses. An over-reliance on a single strategy proved detrimental for many managers during the last crisis, but things have improved markedly since. Nowadays, hedge funds are more diversified with managers pivoting towards multi-asset class strategies, including infrastructure, private debt and private equity. Such diversification not only helps hedge funds attract a wider spectrum of investors, but it can protect their businesses during sharp downturns.

Simultaneously, the hedge funds in 2008 that paid diligent attention to operational risk management also fared well when markets normalised. Fortunately, most hedge funds now take operational risk very seriously, evidenced by the ease in which the industry adjusted to working from home without much disruption. Those hedge funds whose business continuity plans (BCPs) are found wanting are expected to see withdrawals. Conversely, managers - who prior to Covid-19 - invested time and effort into their operational resiliency and risk management programmes are likely to be rewarded with further inflows.

1 Hedge Fund Research (April 22, 2020) Hedge fund assets fall as market volatility surges on pandemic uncertainty

Additionally, the hedge funds which have been open and maintained regular dialogues with clients will be the primary beneficiaries when Covid-19 subsides.

Pre-2008, the industry was criticised for being opaque with investors, many of whom would receive performance updates on a quarterly basis, if that often.

Post-crisis, the hedge fund model institutionalised itself partly as a result of the huge inflows that came from major pension funds, sovereigns and insurance companies. With that, hedge funds were forced to become more transparent and communicative with clients.

These much-improved transparency standards will serve hedge funds well when institutional investors start allocating capital once again. If hedge funds are to win mandates, they need to evolve with the times. This latest crisis is a stark reminder of the importance of digitalisation.

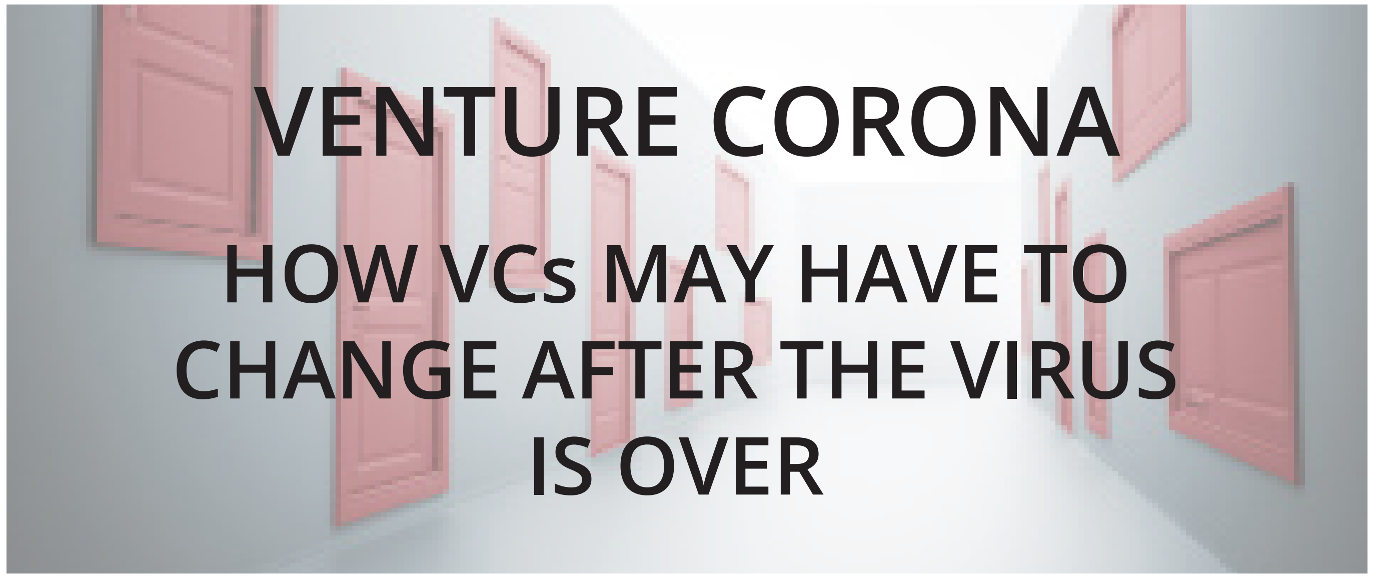
Fortunately, a number of hedge funds have transitioned away from manual processing towards something more automated, which has had a positive impact on client reporting.

As investors increasingly embrace technology, it is critical their fund managers do so too.

If hedge funds are to accumulate more assets in the future, they need to digitalise the investment experience by ensuring performance and operational reports are available in real-time or near real-time in a compatible, user-friendly format that can be accessed via a mobile phone or smart tablet device.

Lessons learned

Covid-19 will lead to short-term pain in the funds industry, but there is reason for optimism. Past crises have shown that flows bounce back relatively quickly. Moreover, the hedge fund industry has made some impressive strides since 2008 by becoming more diversified; communicative; digitalised and better risk-managed. If performance is robust and superior to that of public markets, then investors will return.



VENTURE CORONA

HOW VCs MAY HAVE TO CHANGE AFTER THE VIRUS IS OVER

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Marc Andreessen sure knows how to make headlines. His latest article It's Time To Build really hit a nerve with the virus struck America.

It says exactly what you'd expect it to: we (the Americans and the West more generally) should start building and creating again. Though, arguing that the lack of masks and corona tests speaks to America's "smug complacency" may be a tad populist (no country can be prepared to treat all its people at once; nowhere, not even China), the main point of his argument sticks: the West has grown used to live light—offshoring the building, while relishing in consumption and experiential living.

Rightly or wrongly, Andreessen goes on saying that the problem isn't money. After all, the U.S. government just said to push $2 trillion into the economy. But how can it not be? Andreessen talks about gleaming skyscrapers, highly automated factories and hyperloops, and asks why there is no will to build these things?

The invention and creation of these technologies has to be funded first, and the money would have to come in no small part from venture capitalists.

This could be a problem. Reaching for stars is in the VCs' mandate. They are supposed to invest in companies that have the potential to become value outliers—the next Facebook(s). So, you see they don't invest in hard stuff. As we know, it was Marc Andreessen who said "software is eating the world."

A lot of the things that VCs invest in keep that light Western life going. Something would have to happen to make VCs invest in the building—hardcore (decades) long-term investment themes. The question is, is that something the coronavirus?

When the global markets plunged by 30% in March, people woke up to the realization that this is indeed a very deep crisis.

Economists, investors and market commentators began discussing if this crisis—the global coronavirus crash—will prove deep enough to change the world and how. That discussion slowly graduated to a more mainstream audience, until it became widely accepted that we may never go back to the office or on an airplane.

Though some of the doomsday prophecies about eternally impaired spending habits should not be taken all too seriously, it is certain that the virus will have a lasting effect on how we function as a society.

Some things will get slower like ever-present health checks (few could have imagined the extent of airport checks before 9/11), others will get much accelerated like the trend toward remote working.

Zoom's user base has grown from 10 million to 200 million in the space of weeks, and in response, Facebook just launched its own video app. In some areas of the U.S. like the virus struck New York, demand for houses in suburbs has grown by 70%.

These are not short-term trends. In fact, they can make our lives much more efficient. Think about it: take away the daily commute and millions of square feet of rented office space and you have a fundamentally more efficient society.

It wouldn't happen without the virus. It takes a crisis to force us to do things we know we could have done for years. And it is the same with VCs.

The crowding of the VCs in light themes—the Uber(s), Snap(s) and Airbnb(s)—was reactionary. The 2008 crisis brought about disillusionment with the system, a desire for lighter life of soul-searching, not building. The global coronavirus crash exposed that we need things to fall back on—better systems and hard technology that VCs better react to just like they had done before.

One of the reasons why Andreessen's very own **fund a16z** rose to prominence is that, born out of the 2008 crisis, they reformed what a VC is, repurposing venture capital into an agency-like institution. This crash could give rise to more innovation, which is certainly needed.

For, though VCs are thought of as the disruptors, they themselves have not been disrupted yet. They remain investment vehicles for billion-dollar institutions and a few super-wealthy with opaque manual processes which often yield (but remain undetected) below average performance.

For starters, in tandem with the virus struck digital-only world, VCs could embrace digitalization a bit more.

There are now neat virtual dashboards that can help VCs automate the reporting and monitoring, some of which are funded by the VCs themselves like Vestberry.

Opening their funds to more investors by, for example, changing the subscription process to a digital form, thus saving time and legal costs could be seriously impactful. VCs could become lower cost thematic investment vehicles for larger investor audience, and, in the words of Marc Andreessen, "all contribute to building."

ASIAN MARKETS INSIGHT: PERSPECTIVES FOR US INSTITUTIONAL INVESTORS

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The 21st Century has been declared by some to be the Asian Century. During this period, Asia is anticipated to dominate global growth and become the centre of world activity based on long-term demographic trends and a projected shift in global economic power. Two decades into this period of Asian ascendancy, the opportunities for US institutional investors are significant.

Asia is already home to more than half the world's population, housing 21 of the world's 30 largest cities and soon it will represent half of the world's middle class. Analysis by the Financial Times[1] shows that Asian economies will become larger than the rest of the world combined during 2020.

A report by the Asian Development Bank[2], outlines a historic rise in Asian production to account for over half of global output by 2050. During that period an additional two billion people will attain living standards equivalent to those in the US and Europe.

Some US investment luminaries have long extolled the virtues of placing Asia at the centre of portfolio construction and Asia is consistently identified by institutional investors as a region for increased exposure to both hedge and private equity fund strategies.

But many investors seeking exposure to the region may have questions regarding operational and regulatory standards.

Expert Viewpoint

Real GDP growth projections for the region serve to highlight the scope of the Asian opportunity. According to the OECD[3], GDP in Emerging Asia is set to grow annually on average by 6.1% in 2019-23.

Southeast Asia is forecasted to grow by 5.2% over this period, which is an even faster rate than seen in 2012-16.

China's GDP growth, though slightly slower than the recent past, is anticipated to still post an impressive 5.9% average growth in 2019-23.

Additionally, medium term growth for India is projected at 7.3% and within the ASEAN 5, the Philippines and Vietnam are projected at 6.6% and 6.5% respectively. By contrast, The Conference Board[4] forecasts average annual GDP growth for the US at 2.0% for 2020-24 and just 1.5% for Europe over that same timeframe.

It's clear from these projections that the growth outlook is heavily skewed towards Asia in the years ahead and that growth differential will only increase as Asia's relative population growth and labour productivity dynamics kick in.

Against the backdrop of Asia's impressive growth profile, it is no surprise that opportunities in the region are on the radar of US institutional investors. In addition to Asia's encouraging demographic picture, there are also diversification benefits.

Equity markets in the region have been at different stages in their market cycle than those in the US.

China's Shanghai Composite Index made a significant market peak in June 2015, experienced a bear market and bottomed in January 2019.

From a valuation perspective, stocks in most Asian markets, including the Shanghai Composite and Hang Seng Index, are trading at the low end of their

1 Reed, John and Romei, Valentina. The Asian century is set to begin (March 25, 2019). The Financial Times. https://www.ft.com/content/520cb6f6-2958-11e9-a5ab-ff8ef2b976c7.
2 Asia 2050: Realizing the Asian Century (August, 2011). Asian Development Bank. https://www.adb.org/publications/asia-2050-realizing-asian-century.
3 OECD Economic Outlook for Southeast Asia, China and India 2019. https://www.oecd.org/development/asia-pacific/01_SAEO2019_Overview_WEB.pdf
4 The Conferenced Board Global Economic Outlook 2018-2019. https://www.conference-board.org/data/globaloutlook/Global-Economy-Forecast-Projection.

historic private equity multiple ranges and offer compelling value.

This compares with the US equity market that experienced the longest bull market in its history where stocks prior to topping in January and February 2020 were trading at Shiller Cyclically Adjusted Price to Earnings (CAPE) Ratio levels only seen just prior to the market crash in 1929 and during the Dot-Com Bubble.

Progressive structural reforms that will take hold in China over the next year will also provide significant support for market gains and economic growth.

Due to the growing maturity of the investment fund sector in the region, the financial centres of Hong Kong and Singapore have seen a wave of high profile and successful hedge fund and private equity launches over the last decade.

These launches included funds from international investment professionals with strong track records who spun out of their former shops.

These entries effectively forced the market to adopt a more institutionalised approach to fund management in order to meet the standards expected by US institutional investors and attract more capital to the region.

A notable characteristic evident in these spin-outs is that while the portfolio manager is often able to generate strong performance, they tend to need some assistance in terms of their middle-to-back office functions in order to meet institutional investors' standards.

"There is ample opportunity in China and greater Asia," said Tim Barrett, Associate Vice Chancellor at Texas Tech University and Chief Investment Officer of the Texas Tech University System Endowment Fund.

"At the Texas Tech University System endowment, we focused our first direct relationships in private credit six years ago, followed by Pan-Asia equity market neutral, relative value and market neutral fixed income strategies.

Most recently, we have added to our private equity portfolio via Pan Asia buyouts and Chinese Venture Capital.

Bottom line, across the board there is higher persistent alpha across strategies as these markets are just beginning to institutionalise."

Jonathan Mandle, Co-Managing Partner at Corrum Capital offered a similar perspective. "At Corrum Capital, we believe the growth of the middle class in Asia is a compelling long-term investment opportunity," he said. "Currently, we are active in the aircraft leasing space, which is not specifically dedicated to the region, but has significant exposure to Asia broadly given the growth of the demand for air travel and the need for substantial aircraft in the region to support this growth.

We see the growth in both business and tourism travel across Asia, which is increasing much faster than many other parts of the world. Our aircraft leasing company recently opened a regional office in Singapore to better service our airline customers in Asia. In addition, the sourcing and security of food is also an interesting trend that provides a tailwind for our trade finance thesis and related companies."

Opportunities in Asia – On the Ground Insights

Asian markets are generally considered less efficient than the equity markets of the US and Europe with less broadly available security analysis. These inefficiencies present significant opportunities for investment funds who can take advantage of active management or may have particular insight in specific sectors of the economy.

US markets by contrast are largely seen as efficient, so for that reason some investors simply opt for index funds, but that's not the case in Asia. A broad range of hedge fund managers in the region has demonstrated success in consistently outpacing market benchmarks and exploiting a vast array of untapped opportunities relative to the US and Europe.

Against this backdrop, we are seeing a greater number of US institutional investors seek to take advantage of these opportunities by placing capital with successful hedge fund managers in Asia who have demonstrated an ability to generate significantly better performance than their counterparts in the US. Golden Pine Capital is just one example of a China focused hedge fund which has a spectacular three-year track record of beating the broad market in China. Established in 2016 by CIO Dr. Peng She, Golden Pine's AUM is currently around US$270 million, with approximately 70% of that from institutional investors.

The long / short equity fund with a Greater China focus on sustainable and high quality growth companies has produced annualised returns of 21% since inception and registered positive returns in 9 out of 11 sectors, being awarded the Barclay Hedge Award of 2018 and HFM Hedge Fund Asia Award of 2019 for the number one performing fund in its category in the Pacific Rim.

Another Asian asset manager that has had significant success both in terms of performance and in attracting and retaining world class investors is Ichigo Asset Management.

A long only, Japan-focused fund, Ichigo started with US$19 million under management in 2006 and now has assets under management of approximately US$8 billion from mainly US and European endowments and charities.

Charles-Lim Capital ("CLC"), based in Hong Kong and Singapore, similarly has had significant success in terms of performance and in attracting such prominent investors. A long only firm investing globally with a focus on Asia, CLC has grown from US$6 million in 2010 to over US$1 billion in AUM.

In private equity, we are seeing US institutional investors participating in funds with AUM above US$500 million with an investment focus on China and other markets in the region.

In terms of what is happening on the ground, private equity in the region continues to be characterised by a buoyant fund raising and deal making environment. We have also witnessed strong returns from higher value exits.

The Rules of Engagement

From a US institutional investor perspective, there is significant demand for exposure to Asia.

For some newer investors there may, however, be questions and some education required regarding the most opportune markets and how to tap into the best managers with the right strategies.

There are also issues for investors to consider related to business practices, cultural nuances, the rules of engagement and the level of corporate governance in less familiar locations.

While performance and diversification are always critical when considering an allocation, US institutional investors looking at Asia are also looking for managers who have robust risk, legal and compliance and operational controls in place.

Some questions over corporate governance standards may present additional challenges for US institutional investors to overcome. With each Asian market going through different stages of development it is hard to make sweeping generalisations on overall corporate governance in Asia.

The language barrier can also present additional challenges for both US investors and for Asian managers looking to raise US institutional capital to grow their business and can make it difficult to explain a strategy to a potential investor.

Leveraging the Asian Century

In highlighting the diversification benefits of adding Asian alternative strategies to investment portfolios, US institutional investors stand on the threshold of what may be a highly rewarding opportunity.

From an alternative investment standpoint, Asian funds offer something different for US institutional investors and may be better positioned for outperformance with the potential for an enhanced risk-reward profile.

Please visit the [Maples Group's website] for more insights into Asian markets and the resources and support available for managers and investors looking to do business in this rapidly expanding market.

EXAMINING THE DYNAMICS OF SHIFTING EXPECTATIONS

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Every volatility episode is unique, as the pandemic is demonstrating. Some last longer than others. Some have greater magnitude. They all have different underlying or fundamental causes. In essence, all volatility episodes are driven by the shifting nature of narratives and market expectations about the future and changing degree of confidence that market participants have in their expectations.

Consequently, what we want to examine are the dynamics behind the way the shift in expectations leads to volatility in the markets. That is, in this research we are not looking at the fundamental cause of a volatility episode, we are analyzing the nature and characteristics of the evolution of expectations.

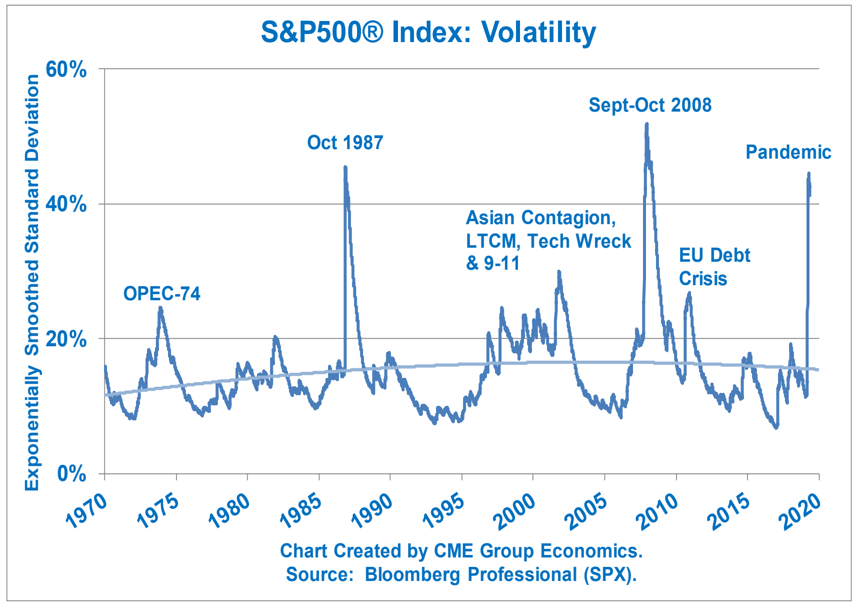
To accomplish this task and to present a clear concept of the dynamics of shifting expectations, we want to link together the topics of narrative economics, Bayesian statistical inference, and quantitative market sentiment analysis.

To anticipate some of our key conclusions, our research makes the case that:

• Expectations shift because the prevailing narrative changes. What matters are the stories people are willing to internalize, to believe, and to tell to others. This is an essential concept of 'Narrative Economics'.
• Bayesian statistical inference offers a very intuitive approach to assist in adding data-driven analysis to our interpretations of narrative economics.
• Appreciating that market sentiment plays a large role and that expectations in a volatility episode are typically not normally distributed, we present some of our research on developing quantitative tools to measure and assess risk distributions as market sentiment shifts from one environmental state to another.

The research views expressed herein are those of the author and do not necessarily represent the views of CME Group or its affiliates. All examples in this presentation are hypothetical interpretations of situations and are used for explanation purposes only. This report and the information herein should not be considered investment advice or the results of actual market experience.

Fig 1 - Equity Volatility Episodes



Narrative Economics and Market Expectations

From our perspective, the key to understanding market volatility is to appreciate that it is about the narrative, and the narrative often evolves rapidly as we sort through an irregular stream of news and noise.

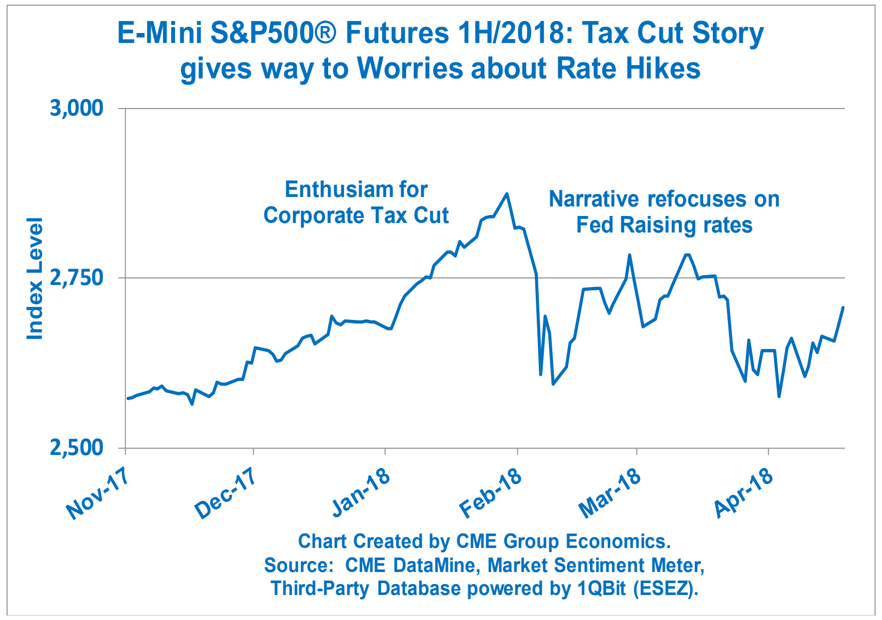
The School of Narrative Economics, led by Nobel Prize winner Robert Shiller (Narrative Economics, Princeton University Press, 2019), argues that expectations are not necessarily about the data. Expectations are grounded in the stories that people are willing to internalize, to believe, and to share on social media and repeat to others.

The stories that gain traction will be picked up by the main stream media and given a swift acceleration into the psychology of market participants.

More importantly, stories may change with each news cycle. The change in the narrative is what can influence how expectations shift and has large implications for understanding the twists and turns in market prices that we measure and observe as volatility. We will take a quick look at one case from the past, just to illustrate the concept, and save a few other examples for a little later when we discuss market sentiment and the pandemic of 2020.

To illustrate our concept, we travel in time to late 2017 and January 2018. Then, the narrative of interest for US equity market participants was all about corporate tax cuts, which were passed into law in December 2017. From February 2018, though, the prevailing narrative influencing US equities shifted abruptly to focus on the Federal Reserve's guidance that a sequence of rate hikes were coming. Our key takeaway is that the dynamics of the changing narrative was one of the key factors driving the rise in market volatility.

Fig 2 - S&P 1H-18 Taxes



Bayesian Inference and its Applicability to Analyzing Market Dynamics

Narrative Economics shares an interesting common intellectual thread with Bayesian inference statistical theory. With narrative economics, how the storyline changes with the arrival of new information is critical to analyzing market volatility.

Bayesian statistical processes are all about analyzing how new information both changes one's expectations of the future and one's confidence in that view. The common thread is the focus on how to update one's views by integrating new information into one's prior views, or we should say, the prior narrative.

Bayesian inference starts with two inputs. First, one develops a 'prior' hypothesis, which is essentially a view about what may happen in the future and one's confidence in that view.

This initial expectation may be based on experience, a theory, or just a naïve estimate.

If little or no data is available, a Bayesian simply makes a reasonable judgement. Second, there is a level of confidence associated with the expectations. Initial confidence levels are often very low.

Each news item or new data point allows a Bayesian to update the view and the probability the view is accurate. In the Bayesian world, having a view or expectation always comes with a probability attached so one can evaluate the likely accuracy of the expectation. Put another way, making a market forecast and not providing a level of confidence is not allowed in Bayesian statistics.

Think about building an economic model and trying to specify the parameters of the model or the coefficients to attach to the critical features or factors in the model. The Bayesian view would be that the parameters of an economic model are likely to vary through time.

Treating model parameters as time-varying puts the focus on how to incorporate new information into one's view (or model) of the economic system. Importantly, the Bayesian approach is comfortable with the common problem of a lack of data.

Bayesian statisticians can start with little to no data, develop a view based on experience or expertise and then let the new data confirm or shift the interpretation.

Consequently, when faced with a dynamically evolving narrative or with a switch from one formerly influential narrative to a newly developing one, our research preference is to develop Bayesian-inspired methods for analyzing new data so we can stay on top of the risk management challenges associated with the dynamics of changing expectations and episodically volatile markets.

Thoughts on Quantitatively Assessing Market Sentiment States

Our last line of analysis is to discuss our approach to quantifying the impact of a changing narrative on the sentiment of market participants which, in turn, may have large implications for financial risk management.

One approach is to incorporate text searches from the Internet to better track the rise and fall of narratives. We applaud this area of research as potentially extremely promising, even as we acknowledge the challenges that come from every volatility episode and every narrative being different.

Our initial approach goes in another direction and focuses on the actions market participants take as they respond to the changing narratives that shift market expectations. That is, our emphasis is on what market participants actually do, rather than on what they say, which is similar to what economists call 'revealed preference'.

Working with the quantum software company, 1QBit, we have tried to develop a quantitative approach to identifying different sentiment states for markets.

Arbitrarily, we ended up with four sentiment states: (1) 'complacent' with few worries and is relatively rare (~12%), (2) 'balanced' with a level of worry typical of a given market and is extremely common (~75%), (3) 'anxious' with a wall of worry and is relatively rare (~9%), and finally (4) 'conflicted' representing a very rare (~4%) yet extremely important to recognize sentiment state where there are two reasonably probable and very different scenarios embedded in the expectations of market participants.

We use a variety of features of market-participant activity to derive our risk probability distributions which are associated with different sentiment states.

Among others, our features include comparing put to call options volume, observing the relative calm or intensity of intra-day prices swings, comparing short-term and long-term historical volatility with current implied volatility from the options markets, etc.

One of the critical objectives of our research was to develop a quantitative method that was distribution-independent and could even represent bi-modal and other skewed distributions of price expectations that were decidedly not similar to bell-shaped curves and normal distributions.

And, while we do not explicitly incorporate Bayes' formula, we also spent considerable time thinking about how to incorporate Bayesian-inspired ideas to handle new data and improve the signal from some quite volatile and not so stable data sets.

By way of illustrating our research, which is at a very early stage, we will take a look at two cases: US-China trade tensions in 2019, and then the pandemic of 2020.

In our first sentiment example, we will study the US-China trade tensions case. Early in the spring of 2019, the trade tension news was a drumbeat of positive information flowing from both Washington and Beijing that a deal could possibly be coming soon.

Unfortunately, in late April and early May 2019, the negotiations became more acrimonious and talk of a quick deal faded. The trade narrative shifted to focus increasingly on whether there would be a deal soon or no deal at all.

This was reflected in our 'Market Sentiment Meter', which shifted to the extremely rare 'conflicted' state. The 'conflicted' state involves a bi-modal risk distribution, which we interpret to mean the narrative is weighing two very different scenarios (i.e., deal or no-deal) with the potential for shifts in the relative probabilities towards or away from one or the other scenarios with each news cycle.

Fig 3 - S&P 1H-19 Trade

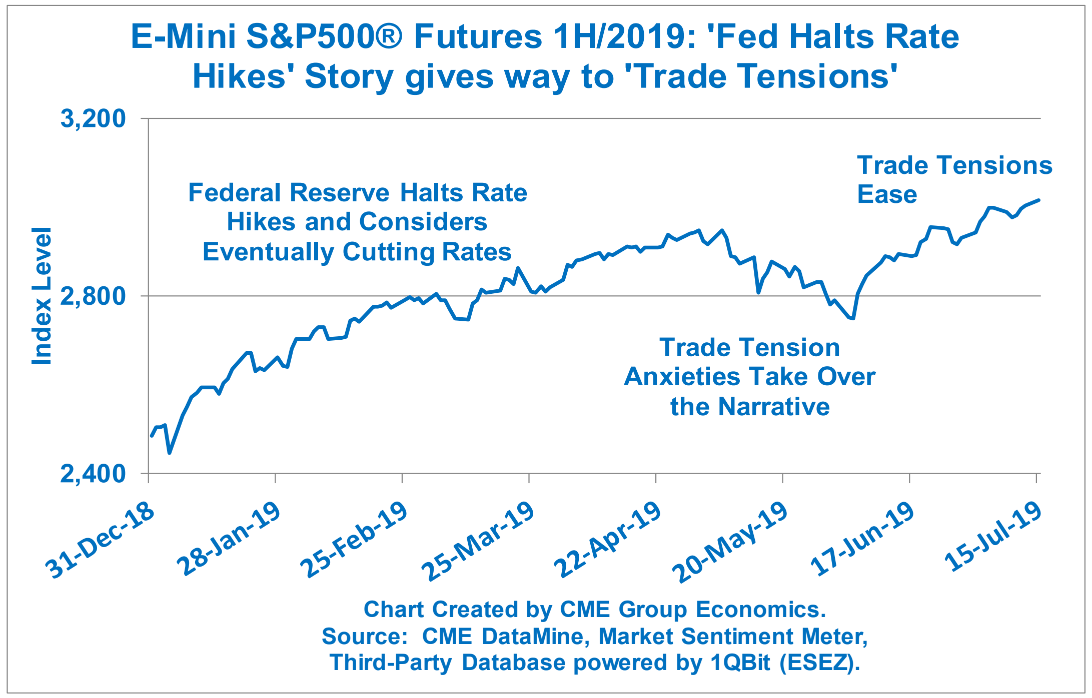
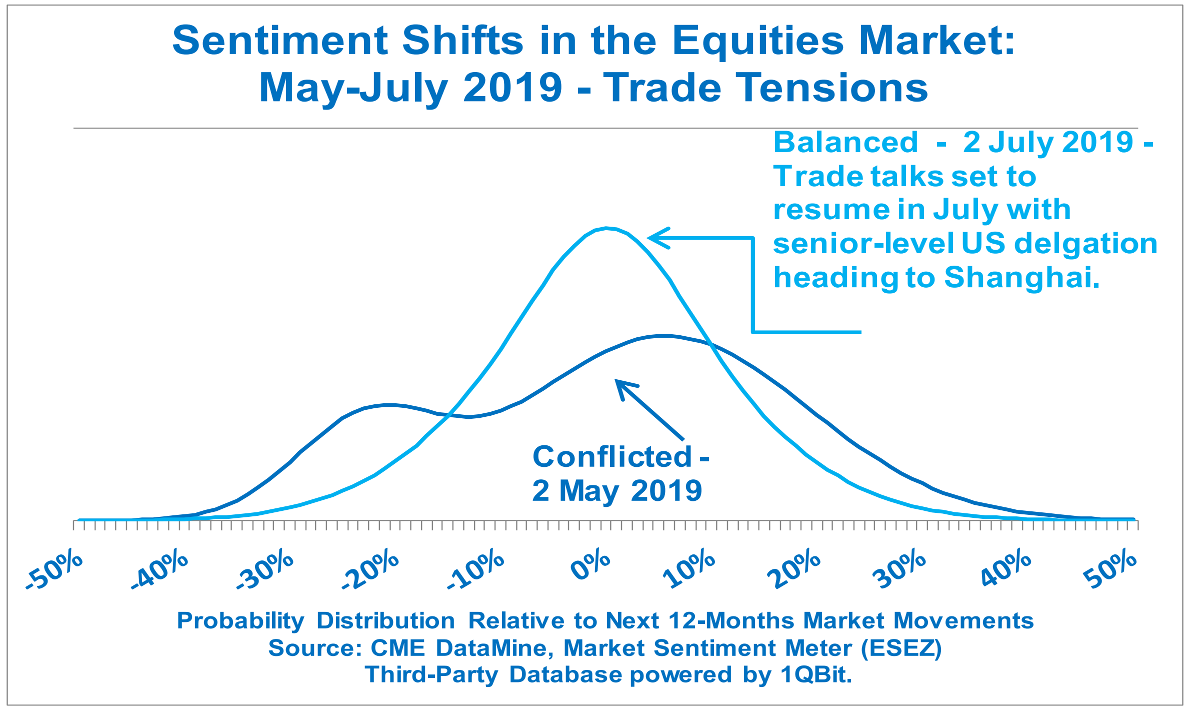


Fig 4 - Trade 19-07-02



For our second illustration, we examine interesting shifts in the narrative coming from the evolution of the pandemic. The COVID-19 virus broke onto the scene in mid-January 2020 initially as a China-only narrative. US equities reflected a 'balanced' sentiment state during the early stages when the narrative was mostly about China.

During the weekend of February 22-23, 2020, the news and the narrative shifted to a global focus, and shortly thereafter our Market Sentiment Meter showed that US equities had entered an "anxious" sentiment state, reflecting a sharp increase in worries about the future.

Then, as the narrative developed into an even more worrisome storyline, focused on the serious ramifications of shutting down travel, tourism, restaurants and bars, and generally depressing global demand for goods and services, US equity markets entered bear market territory in early March 2020.

The narrative went through several more evolutions.

Equities hit the bottom of the bear market sell-off on March 23, 2020, as the narrative shifted to reflect the degree of asset price support that the Federal Reserve (Fed) was willing to provide, with announcements of current and forthcoming purchases of US Treasuries, Mortgage-Backed Securities, Corporate bonds, and Municipal bonds.

Effectively, the Fed was promising multi-trillion-dollar support for the entire spectrum of the US fixed income marketplace. Equities rallied from their low points on the back of the "Fed has the markets back" narrative.

Fig 5 - S&P Q1-2020 COVID

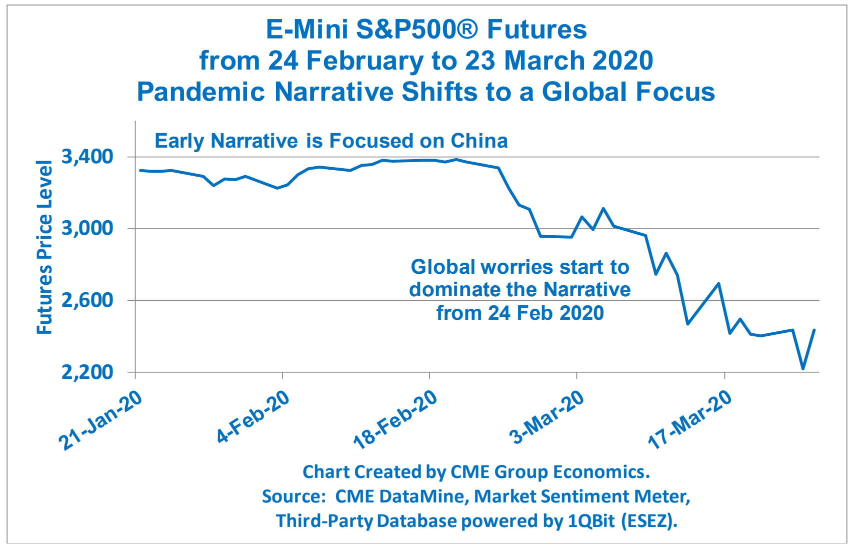
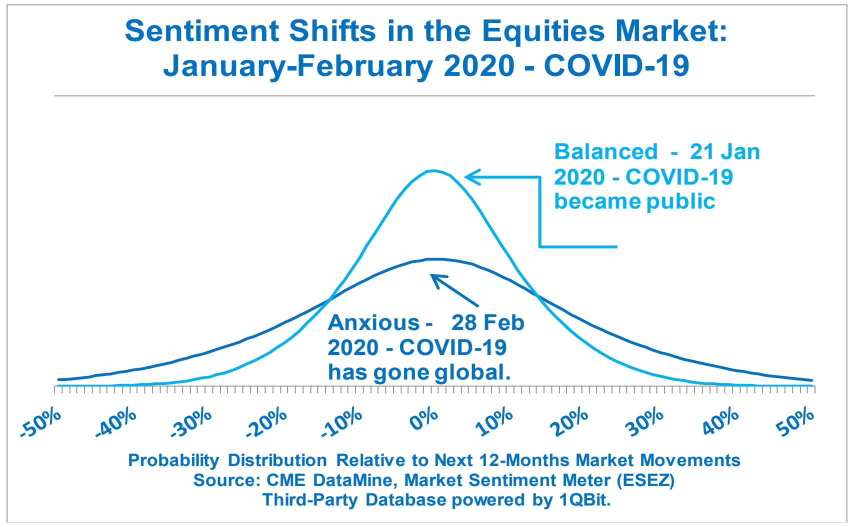


Fig 6 - Virus 20-02-28



Then, in the second half of April and into May 2020, equity markets developed competing narratives. One narrative was positively focused on economies in countries and states in the US starting to re-open their economies.

A second narrative was more pessimistic as it focused on the massive unemployment and the likelihood that further corporate layoffs, due to weak demand even as economies re-opened, would make for a very long and drawn out rebuilding phase.

The conflicting narratives suggested that while the Fed could calm the volatility in markets, there were limits to the upside on equity prices while the economy was still digesting the bad news on unemployment and the likely extremely slow path to recovery.

Work in Progress

We are careful to note that our research is not necessarily predictive. In all of our examples, anyone paying attention to equity markets would have known that sentiment had dramatically changed.

Our objective is to attempt to quantify the price expectations and the expected risk distribution, and especially to appreciate when the expected risk distribution is decidedly not bell-shaped and displays significant asymmetry or even a double-humped shape.

That is, we may all know the sentiment state has changed, but can we quantify the new sentiment state in a manner that allows for comparisons with the past, with metrics that can be inputs in risk assessment systems, and hopefully can improve our financial risk management?

We note that all of the original data, the calculated metrics, and a discreet data version of the hypothetical expected risk probability distribution is available from 2012, daily, through CME Group DataMine for eight products: E-Mini S&P, US Treasuries, Euro FX, Gold, WIT Oil, Natural Gas, Corn, and Soybeans, powered by 1QBit.

This is a storyline in development, and we hope for more improvements.

Our research to date has been illustrative and highly informative, and we think the thread of intellectual curiosity from Narrative Economics, to Bayesian-Inspired methods, to our Market Sentiment Meter, is a path worthy of future research.

Importantly, from a practical quantitative perspective, we move intellectually in a consistent manner from the interpretation of narratives in terms of their impact on market expectations to a quantitative assessment of market sentiment states which are independent of embedded distributional assumptions, may be compared to past episodes, and offer the potential to improve our risk management processes.

Fig 7- S&P 1H-20 COVID

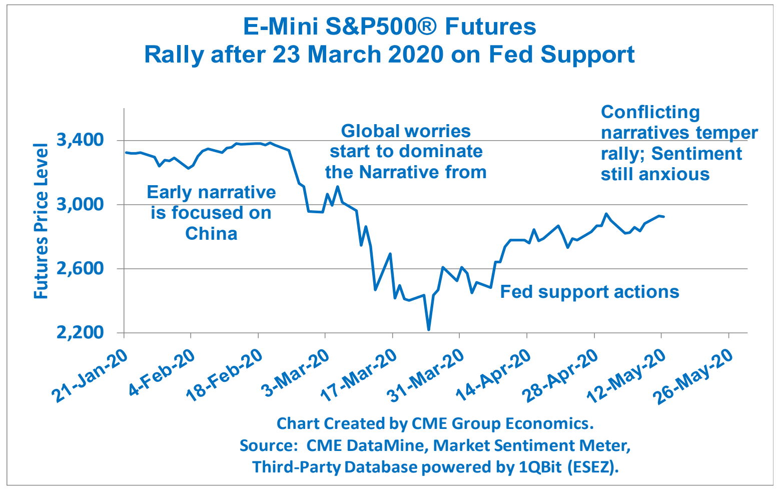
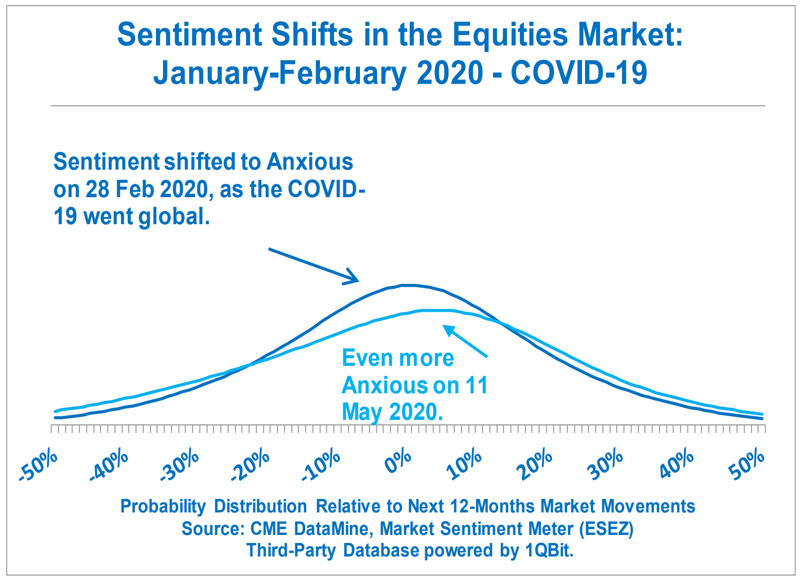


Fig 8 - Virus 20-05-2012



LIBOR NO MORE: HOW ALTERNATIVES MANAGERS SHOULD IMPLEMENT THE TRANSITION

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In recent months, we have seen a barrage of co-ordinated messages from the UK authorities to chivvy the industry into action to ensure minimal disruption and mitigate any associated conduct risks arising from the termination of LIBOR by the end of 2021.

On 16 January 2020, the FCA, the Bank of England and the Working Group on Sterling Risk-Free Reference Rates ("RFR Working Group") published transition targets for 2020, stating that "firms need to accelerate efforts to ensure they are prepared for LIBOR cessation by end-2021" and adding that "2020 will be a key year for transition".

This was followed on 27 February 2020 by a Dear CEO letter from the FCA to all asset management firms, setting out their expectations for managing the transition.

The background to replacing LIBOR

Two primary reasons lie behind the case to replace the London Interbank Offered Rate ("LIBOR") as the key benchmark for wholesale borrowing: first, since the financial crisis there has been a structural decline in the use of the interbank market as a source of funding; second, the setting of LIBOR incorporated a fragile system for the quoting of rates which was perceived to be vulnerable to manipulation.

In April 2017, the RFR Working Group recommended a reformed version of the Sterling Overnight Index Average ("SONIA") as the long-term replacement of LIBOR for sterling markets under the administration of the Bank of England.

SONIA is anchored to an active and liquid market in wholesale overnight rates and is perceived to offer a much more robust proxy to the risk-free rate.

There has also been international coordination in generating replacement benchmarks in the other key currencies currently employing LIBOR: US dollar, Euro, Swiss Francand Japanese Yen. Thus, we move to the Secured Overnight Financing Rate ("SOFR") for US dollars; the Euro Short-Term Rate ("ESTR") for Euros; the Swiss Average Rate Overnight ("SARON" for Swiss Francs; and the Tokyo Overnight Average Rate ("TONAR") for Japanese Yen.

What are the UK authorities' immediate priorities?

The targets announced by the RFR Working Group in January are intended to support a smooth transition to SONIA and other alternative rates and include some specific milestones for asset managers –we take "milestone" to mean somewhere between guidance and obligation:

- From 2 March 2020: market makers should switch from LIBOR to SONIA for sterling interest rate swaps, so asset managers should now take new positions in the latter where possible.
- End of Q3 2020: for asset managers to cease investment in sterling LIBOR products which mature beyond 2021, as well as launching new products or performance fee measures which are linked to LIBOR.
- Q1 2021: the target date for asset managers to have significantly reduced exposure to sterling LIBOR products in their client portfolios.

What are the FCA's chief concerns?

Beyond achieving a smooth transition to SONIA and other relevant benchmarks without significant market disruption, the FCA identifies a number of key conduct risks during the implementation period. Firms' LIBOR transition plans thus need to take account of the following:

- **Product performance:** whether legacy LIBOR exposures in client portfolios will perform as expected, particularly after the end of 2021.
- **Product governance:** whether any new products with LIBOR exposures will adhere to the principles of the product governance rules (for example, whether the charging structure is sufficiently transparent and understandable).
- **Planning and accountability:** whether firms have established proportionate transition plans which have been agreed by their governing bodies (including appropriate accountability and updated Statements of Responsibility submitted to the FCA).
- **Clients' best interests:** whether firms are proactively replacing LIBOR-exposed instruments within their portfolios with those that reference alternative rates and/or amending the constitutional documents of existing products which in some way reference LIBOR to include fall-back provisions.
- **Conflicts of interest:** whether firms are mis-representing past performance, even if advertently, and whether clients are being disadvantaged by adjustments in performance fees.

What are the main challenges for asset managers?

Credit strategies clearly are likely to contain the most significant exposure to LIBOR referenced products and hence present the greatest challenge, but the following checklist will be relevant in some degree to other strategies as well:

- **Loan documentation:** for any sterling or other LIBOR-based credits, a review of the underlying documentation such as the loan facility agreement should be undertaken to identify if a replacement for LIBOR has already been identified. This can then feed into portfolio income monitoring tools to ensure accurate interest calculations (always helpful when calculating interest coverage tests for instance).
- **Loan agency role:** managers engaged in the rapidly expanding direct lending space, who have taken on the loan agency role for floating sterling loans, will have to identify the new base rate and ensure that those rates can be set in accordance with the criteria in the agreements (e.g.x days before reset date). This will also most likely have to be agreed with the borrower.
- **Interest rate hedging:** hedging out interest rate risk, swapping interest rates,or engaging in perfect asset swaps, are also potential areas of particular focus in identifying LIBOR replacements. Any alterations to such agreements may need discussions with counterparties to identify the ideal replacement.
- **Other operational issues:** firms should review all outward payment streams to investors to ensure that no payments to investors are based upon, or reference, LIBOR. These include tranches of the CLOs, credit-linked notes, or references to LIBOR as part of a return hurdle.

What other steps are the UK authorities taking to accelerate the transition?

The Bank of England has been at the forefront of additional measures to encourage market participants to get ahead of the switch, recently announcing that:

- It will publish a compounded SONIA-linked index from July 2020 which will help firms construct compounded SONIA rates in an easy-to-use, consistent format.
- It is consulting on the publication of daily "screen rates" for specific period averages of compounded SONIA rates, thus removing the need for agents to perform these calculations.
- It plans to increase the haircuts on LIBOR-linked collateral which it lends against from October 2020.

Will Covid-19 affect the timetable?

At the moment, the UK authorities are sticking with their message that firms cannot rely on LIBOR's existence beyond the end of 2021. The Bank of England, the FCA and the RFR Working Group are issuing regular updates, most recently a statement on 29 April. In this they acknowledge the challenges presented by the current operating environment which they recognise may affect some interim milestones.

What are other regulators saying?

As mentioned earlier, the replacement of LIBOR across major currencies has been a multi-national endeavour.

Of particular interest is that the SEC's Office of Compliance Inspections and Examinations ("OCIE") highlighted exposure to LIBOR as one of its exam focus areas in 2020: "OCIE encourages each registrant to evaluate its organization's and clients' exposure to LIBOR, not just In the context of fall-back language in contracts, but its use in benchmarks and indices; accounting systems; risk models; and client reporting, among other areas."

Similarly, the Hong Kong Monetary Authority wrote to local institutions in March 2019 to remind them of the risks associated with the transition to alternative reference rates.

The difference with the UK is that US dollar assets typically reference LIBOR whereas HK dollar assets reference the Hong Kong Interbank Offered Rate ("HIBOR"). The Hong Kong Dollar Overnight Index Average ("HONIA") has been designated as the appropriate replacement.

What should firms be doing now?

1. Establish a project team to plan and oversee the transition (front office, legal, operations, investor relations, compliance).
2. Get sign-off from the governing body including allocation of senior management responsibility.
3. Educate the front-office in the broader considerations in making the switch to LIBOR alternatives.
4. Engage operations team on identifying and mitigating embedded LIBOR exposure.
5. Brief legal on updating product and investor documentation.
6. Brief investor relations on any amendments to product information and marketing materials.
7. Ensure risk teams take into account the impact that the proposed changes will have on the market and whether they need to consider changing their scenario analysis or model testing as a result.
8. Keep clients appropriately informed of such changes as they are developed and implemented.
9. Monitor compliance with regulatory obligations and FCA priorities.

Plan, Conserve, Maintain, Assess, Update

REGULATORY CAPITAL IS IT ADEQUATE FOR THE TIMES AHEAD?

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The financial services sector, like most industries worldwide, are in the midst of assessing the impact of COVID-19 on their business and future strategies.

In addition to the operational challenges triggered by the outbreak, the need to re-budget inevitably impacts on regulatory capital requirements. It is arguably more important than ever to not lose focus on the pillars that were established for regulated businesses to cope with times of crisis.

The Regulator's expectations remain the same; that firms must have adequate financial resources to protect their businesses, and more importantly, customers. This means taking necessary steps to preserve capital in the light of potential demands on liquidity.

On 17 April the FCA provided an update on financial resilience for FCA solo-regulated firms, with a clear message that it expects all firms to plan ahead, conserve capital, maintain capital adequacy, assess liquidity and update ICAAP and wind-down plans:

- Plan – Firms should plan ahead and assess their position for the foreseeable future
- Conserve – Firms need to consider setting aside regulatory capital
- Maintain – Ensure that capital adequacy is maintained and identify possible deficit situations going forward
- Assess – Firms must assess their liquid resources available and ensure that they have sufficient working capital to meet their obligations
- Update – Firms should revisit and update their ICAAPs and wind-down plans to ensure that these assessments are relevant to the current market conditions.

What does this mean at a practical level?

Adequacy of financial resources, capital and liquidity is reported through the regulatory returns submitted to the FCA on a periodic basis. In addition to this, the FCA expects firms to conduct, at very least on an annual basis, an 'internal capital adequacy assessment process' or 'ICAAP' to further analyse and quantify the risks that a business faces.

Within the requirements and in addition to the above, however, is the rule within GENPRU 1.2.26 – Requirement to have adequate financial resources which states:

A firm must at all times maintain overall financial resources, including capital resources and liquidity resources, which are adequate, both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due.

This puts an ongoing responsibility on firms to monitor their position and have measures in place to ensure that no breaches occur on the capital adequacy and liquidity adequacy fronts.

What should firms be doing now?

Identify and Assess

It is more important than ever before to identify and assess their risks from an operational and financial perspective and ensure that they have the appropriate documentation in place in order to demonstrate continuity of their business going forward.

> **"Adequacy of financial resources is designed to:**
> **• enable firms to remain financially viable and to provide services through the economic cycle**
> **• enable an orderly wind-down without causing undue economic harm to consumers or to the integrity of the UK financial system "**
>
> **Ref: FCA's CP19/20 – Assessing Adequate Financial Resources**

In particular firms should focus on the critical revenue drivers and business lines such as management/advisory fee arrangements and how these may be affected in the current environment and certain stress scenarios, including business areas subject to the greatest risks, e.g. if a sudden large volatility in the currency market will lead to unexpected losses; business areas subject to the greatest risks.

From an operational perspective, firms should examine their current infrastructure, resources or third parties upon which they heavily depend. It is essential that the firm's agreed (qualitative and quantitative) risk appetite and risk thresholds are reviewed, and that the relevant compliance monitoring and reporting processes are in place.

Firms need to ensure that these assessments are documented sufficiently, and that their governance arrangements include clearly defined responsibilities amongst their identified Senior Managers.

Actions
To assess the above factors, firms should, if they haven't already done so, implement the following actions as soon as possible:
• Prepare realistic financial projections for 2020 as granularly as possible and compare them with actual results on a month by month basis. Use the projections for a detailed estimate of capital adequacy so that all potential breaches can we avoided. Liquidity requirement as explained further needs specific monitoring as well.
• Incorporate stress testing within the monitoring process which is representative of the real scenarios faced by the firm.
• Construct a Risk Register or matrix which clearly articulates the likelihood of occurrence of all types of operational and business risks, specific controls that can be allocated to those risks, identify senior managers with ultimate responsibility towards the monitoring of those risks and quantification of capital required to address the risks. This drives the Pillar 2 capital framework and the FCA expect firms to have documented this diligently.
• Prepare or update wind-down plans as per the FCA's guidance. This is discussed in detail later on in this article.

For most managers, the above components should already be included within the ICAAP, Firms should consider updating the ICAAP as soon as possible so that it is current, real-time and complete.

The FCA's view

In the event that the FCA decides to review a firm's current operational effectiveness, the FCA will consider if a firm has:
• taken reasonable steps to identify and measure its risks.
• taken a forward-looking approach to risks and how these develop through the economic cycle.
• appropriate systems and controls and human resources to measure risks prudently at all times.

• accessed adequate capital to support the business, and that client money and custody assets are not placed at risk.
• resources which are commensurate with the likely risks it faces.

In theory, your ICAAP should discuss a scenario that is catastrophic at a performance and operational level. It is important to include a detailed discussion about a pandemic so disastrous to the business continuity of the firm and the actions that the firm would take in such a situation.

Meaningful and robust stress testing needs to be part of your ICAAP. An event like this can trigger not just a significant drop in revenues and assets, but may also test the operational resilience that firms should articulate within their ICAAPs and business continuity plans.

Cash is king but cash is not capital

There is often confusion in the difference between the capital in the business and the liquid assets available. In order for capital to be eligible Tier one capital must have all the following characteristics:

• it is able to absorb losses.
• it is permanent or available when required.

> "Firms should consider 'what if' scenarios and estimate the potential impact. This is to determine the amount and type of financial resources needed to put things right when they go wrong."
>
> Ref: FCA's CP19/20 Assessing Adequate Financial Resources

• it ranks for repayment upon winding up, administration or similar procedure after all other debts and liabilities.
• it has no fixed costs, that is, there is no inescapable obligation to pay dividends or interest.

The most common forms of eligible tier 1 capital are ordinary share capital and share premium, members' capital (for LLPs) and audited retained earnings. However while capital may be put into a business to meet its working capital and regulatory capital requirements, it can often be tied up in illiquid assets such as fixed assets and deposits and also get eroded if there are continuous losses.

Liquid assets are cash and cash equivalents but cannot be considered as capital until specifically designated as 'regulatory capital'. In addition, not all current assets can be treated as liquid assets; the general norm under MiFID being that assets that can be converted into cash within 90 days are considered 'liquid'.

Firms authorised under AIFMD also have a requirement of ensuring that their 'Funds under Management' requirement can be met through liquid assets. There is an additional challenge for such firms in that liquid assets under AIFMD are those that are cash convertible within 30 days.

It is therefore essential that firms assess their balance sheets, in particular given the current situation, to ensure that the regulatory capital of the business is backed up by sufficient liquid and recoverable assets.

Hope for the best but plan for the worst

The FCA Handbook includes detailed guidance under **Regulatory guides - WDPG** which sets out its expectations from firms to document the process they intend to follow for an orderly wind-down.

Guidance states that besides having a clear-headed and prompt decision-making ability, it is important to articulate a wind-down plan at an operational level.

The starting point of the wind-down timeline is the decision and the end point is the successful cancellation of the regulatory permissions but the 'planning' is all about the numerous tasks and challenges in between.

The key questions that the plan should address are as follows:

• What is the estimated length of the wind-down period
• What resources (both financial and non-financial) would be needed to implement it?
• Who needs to be available to assist the firm in winding-down?
• How would the firm deal with redundancies and, conversely, which employees need to be retained with special financial arrangements?
• What systems (e.g. IT systems) need to be available to the firm during the winding-down?
• Will the firm need to engage professional advisors to wind-down?
• Has the firm considered the implications for any overseas offices and branches?

To conclude, it is essential to have a robust wind-down plan which gives a clear picture on governance process, operational analysis, estimated revenue/ costs schedule and resource assessment.

If you need to discuss capital adequacy planning or update your ICAAP documentation and wind-down plans, please get in touch at enquiries@buzzacott.co.uk

MEETING IN THE MIDDLE: CONVERGENCE OF HEDGE AND PE

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Historically, hedge funds and private equity funds occupied two distinct realms within the alternative investment funds industry; hedge funds typically being structured as open-ended funds pursuing generally liquid and public investment strategies, and private equity funds typically being structured as closed-ended funds pursuing generally illiquid and private investment opportunities.

A 'convergence' of the two structures accelerated following the 2008 financial crisis as managers moved into less liquid credit strategies. Traditional hedge fund managers have been increasingly pursuing longer-term, more concentrated and less liquid investment strategies as part of, or as a supplement to, their primary strategies.

Conversely, traditional closed-ended private equity and private credit managers have been increasingly seeking to access a new source of capital and investor base through the offering of more liquid and shorter-term private strategies through open-ended vehicles. This article sets out the approaches taken to fund and product structuring in this hybrid space to meet the needs of the investment strategies and opportunities described above.

Types of Hybrid Fund Structures

There are generally two types of 'hybrid funds'; closed-ended, or 'private equity lite' hybrid funds, and open-ended, or 'evergreen' hybrid funds.

Closed-ended or 'private equity lite' hybrid funds

A typical closed-ended fund would require investors to commit their capital for a minimum period of time, usually at least three to five years, and often up to ten years.

There are pre-agreed dates on which the fund will stop making new investments (i.e., the end of the 'Investment Period') and be wound up (i.e., the end of the 'Term'). A closed-ended hybrid fund typically has a much shorter Investment Period and Term than a more traditional closed-ended fund and will typically have fewer closings (i.e., typically no more than one or two).

The manager receives a carried interest only upon the disposal of the fund's investments, but in many cases only after all the fund's capital has been returned (i.e., at the end of the Term).

Where a fund is approaching the end of its Term and has yet to dispose of certain investments, the manager may have the right to extend the Term (in order to sell the assets at a more favourable price) and thereby restrict distributions to investors.

As investors have no redemption rights during the fund's Term, managers have certainty over their available investment period. Accordingly, in the private equity space, these structures may be suitable for managers seeking to 'house' a small number of investments and/or investors. They may also be appropriate for certain private credit strategies, for example, a direct lending strategy making a small number of short-term loans.

Open-ended or 'evergreen' hybrid funds

In an 'evergreen' hybrid fund, the liquidity terms utilized are often similar in their impact to the 'private equity lite' hybrid fund (e.g., investors will have no redemption rights for a fixed term - their investment will be 'locked-up'). However, there are key distinguishing factors:

- Structure of the manager's compensation. An evergreen fund offers more immediate financial rewards than a 'private equity lite' hybrid fund due to the different compensation structures. Evergreen funds typically provide for annual performance based compensation on realised and unrealised gains, as opposed to a carried interest upon the disposal of the investments and return of the fund's capital. There is generally no clawback of the performance fee in the event of subsequent losses.

- Ability to continuously market the fund and receive further capital. Evergreen funds are open-ended and therefore managers can continuously market the fund and raise capital at any time. In light of the less liquid nature of the strategy being pursued, a manager might utilize a draw-down and commitment structure, thereby allowing the manager a reasonable period of time to source and allocate capital to investment opportunities without diluting investment returns.

Key Characteristics of an Open-Ended Hybrid Fund

As it is difficult to define a 'hybrid fund' due to the variation of terms across asset classes, it is more practicable to identify and discuss common terms and mechanisms that are found in a fund structure which, when combined, create a 'hybrid fund'.

Funds pursuing longer-term and less liquid strategies, or housing less liquid assets within the fund's portfolio, need to incorporate mechanisms to ensure that the liquidity of the fund matches, as closely as possible, the liquidity of the underlying assets within the fund's portfolio. We deal with some of the key mechanisms used below.

Lock-up periods

Hybrid funds will typically have lock-up periods which provide some certainty as to the capital available to invest. Lock-up periods can be structured as 'hard' locks or 'soft' locks, the latter allowing investors to redeem or withdraw their investment subject to a redemption or withdrawal charge. Soft-locks are more commonly used as a mechanism to help ensure longevity of capital (regardless of the investment strategy), whereas hard-locks are often utilized as a mechanism to help align investors' investment term to the liquidity applicable to the underlying strategy of the fund.

An increasingly common feature of hybrid funds is the inclusion of rolling lock-ups, whereby if investors do not redeem/withdraw at the end of a lock-up period, they are automatically rolled into a new lock-up period. The length of the lock-up period may depend on the liquidity of the underlying strategy, and different classes might be set up with different fee arrangements (whereby the longer the rolling lock-up period, the higher the fee discount).

Gates

A gate limits redemptions from the fund by reference to the net asset value of the fund (a 'fund level gate') or the net asset value of an investor's investment in the fund (an 'investor level gate').

A typical gate would prevent investors from redeeming more than 25% of the fund's net asset value on any dealing day. The investor level gate works in the same way by reference to the investor's investment in the fund.

The purpose of a gate is to avoid situations where the fund is forced to sell a significant proportion of its assets at an undervalue to the detriment of the investors as a whole.

It also seeks to avoid concentration issues, whereby the non-redeeming investors are left with the fund's less liquid assets (where the more liquid investments are realised to meet the redemption requests of the redeeming investors). Investor level gates might also be used as a way to align investors' investment behaviour with the long-term nature of the investment strategy (even for more liquid strategies).

Fund level gates may be perceived negatively by some investors and can have unintended consequences in times of financial turmoil. In the financial crisis in 2008, fund level gates were blamed for encouraging investors to submit standing redemption requests, even where they did not want to redeem from the fund (so as to avoid being the last investors left holding the fund's least liquid assets). As a result, investor level gates are often favoured, given that they focus an investor's behaviour on its own investment/redemption intentions and not on those of other investors.

The fund documentation should state whether deferred redemptions are treated pro-rata to new redemption requests or in priority to new redemption requests. Treating redemption requests in priority to new investment requests may also encourage a run on the fund.

Side pockets

Hybrid funds may use side pockets to separate a fund's illiquid assets from its more liquid investments (either in respect of a specific investment opportunity or problematic assets). Once designated and placed into a side pocket, the relevant asset is accounted for separately from the assets in the fund's main portfolio. The investors remain invested in the side pocket until the asset is realised (even if those investors redeem from the main fund). Fees would typically be applied to the side pocketed assets separately to the main portfolio.

The use of side pockets to deal with problematic assets has often been viewed negatively by investors due to the potential for misuse. Managers have in the past been accused of overvaluing side pocketed assets, leading to higher fees from investors and the hiding of unrecognised losses. Some managers have also been accused of using side pockets to prevent new investors from participating in a particular investment opportunity (thus avoiding investment returns from certain assets being diluted).

Investors may be more comfortable with the use of side pockets in funds where they are used for the purpose of actively pursuing specific and less liquid investment opportunities (often referred to as 'special situation investments'). These investments are often limited to a specified percentage of the fund's net asset value. Investors generally seek clarification as to the maximum length of time the 'special situation investment' will be imposed.

Frequency of redemptions/ withdrawals

Open-ended hybrid funds usually offer monthly or quarterly liquidity. To stereotype, US investors tend to be more comfortable with less liquidity compared to European investors, many of whom are used to the minimum twice-monthly liquidity (often daily or weekly) offered by UCITS.

Managers pursuing less liquid strategies would need to consider whether monthly liquidity is appropriate taking into account other liquidity management tools, including redemption notice periods, lock-ups, gates etc. A quarterly (or even semi-annual) redemption/ withdrawal dealing day might be more appropriate.

Redemption/withdrawal notice period (e.g., 30, 60, 90, 120 days)

The notice period for redemptions/withdrawals should be guided by the time it would take the fund to realise investments (both liquid and illiquid) to meet the redemption/ withdrawal request (in a way which does not require such investments to be sold at an undervalue to the detriment of the fund and its investors).

Liquidating SPVs and in specie redemptions/withdrawals

In the event of redemptions, hybrid funds often provide for investors to receive assets in specie directly from the fund or, alternatively, to receive interests in a special purpose vehicle ("SPV") used to 'house' an illiquid asset until it is sold. The establishment of an SPV should be carefully considered, in particular to avoid any regulatory and tax issues.

The SPV will ordinarily be established in the same jurisdiction as the fund to avoid double taxation. The SPV should also be structured to avoid unworkable investor consent rights over the operation of the SPV.

Co-Investments and One-Off Investment Opportunities

Managers pursuing a range of alternative strategies have also increasingly turned to co-investment and/or single-investment structures to take advantage of single name (or similar) investment opportunities which are not suitable for a manager's existing investment products, whether due to the type or liquidity profile of the relevant asset(s), or due to capacity or concentration limits imposed on existing investment products.

This may be particularly relevant to special situation and distressed investment opportunities. Where such investment opportunities arise, a manager would need to determine whether such investment is also appropriate for its existing fund(s).

If so, the manager would need to determine how to allocate the relevant opportunity between the existing fund(s) and the co-investment vehicle and on what terms (including as to size of investment and timing of entry and exit).

The manager should consider its trade allocation and conflicts of interest policies to ensure that all investment vehicles are treated fairly and equitably with respect to such investment.

The manager will also need to determine whether the opportunity to participate in an investment outside of the existing fund(s) will be offered to all current investors (often a key side letter point). Depending on the types of investors that are participating, an appropriate structure for the co-investment vehicle will then need to be created.

Co-investment arrangements are often structured on a one-off basis through standalone SPVs or partnership structures (which is common in the private equity space).

Alternatively, managers could establish an umbrella structure, allowing for multiple investments to be pursued on a periodic basis. An umbrella structure typically offers a cost and time efficient route to market for managers pursuing investment opportunities on a relatively regular basis.

This has been particularly common in the credit space as managers have sought to take advantage of special situations or distressed opportunities arising.

THE CASE FOR VENTURE DEBT

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Technology companies can create tremendous value, but to do so they require capital to fund their early development.

Unfortunately, they often struggle to obtain that capital from traditional lenders, and instead find themselves relying exclusively on equity funding that can be expensive and impose unwelcome restrictions. To avoid these challenges, many tech businesses are turning to venture debt. Not only is venture debt an attractive alternative for entrepreneurs, as we'll see, it also offers compelling, differentiated returns for investors.

Venture debt demystified

Software and other technology companies often need capital to fund their sales, marketing, and product development activities.

Since GAAP frequently treats these as expenses, young companies typically report negative operating margins as they grow, which can impede access to traditional debt financing.

The fact is that banks are ill-equipped to gauge the future profitability of rapidly growing enterprises with negative incomes, and their lack of tangible assets makes asset-based financing virtually impossible.

It's because they can't access traditional financing that so many high-growth tech businesses look to equity providers for funding. But what founders and CEOs usually discover is that equity capital comes with caveats. Selling equity can dilute founders' upside economics, while liquidity preferences and other mechanisms increase downside risk. Equity backers typically also demand managerial input, reducing founders' control and strategic flexibility.

To be clear, equity is the right starting point for almost every business plan. Nevertheless, relying on it exclusively often leads to suboptimal results.

Another option that allows businesses to augment their capital base, while enjoying a more efficient capital structure and greater flexibility, is venture debt.

In fact, debt can be a very effective way to fund the runway necessary to reach profitability, allow more flexibility around the timing of valuation events, and help founders reduce the amount of equity required thereby decreasing dilution.

Underscoring the point, the use of venture debt has increased in recent years as those benefits have become more widely understood. Today, it accounts for between 10 and 15 percent of total venture capital invested in a given year (approximately $8 billion to $12 billion annually).

Investors benefit from high yields and diversification

Venture debt typically generates high yields, but the coupon is only one of the benefits these assets can afford investors. While the interest rate on venture debt is particularly eye-catching in a zero interest rate environment, the drivers of that rate are even more important from a portfolio management perspective.

High yields, in this case, don't just reflect higher underlying risk. The return profile is also driven by the underwriting process for venture debt, which differs from the way that loans to mature companies are priced in some important respects.

Large, mature companies have credit metrics that are easily compared against their peers, and the price of their credit — expressed as a spread over the risk-free rate — is transparent.

The market for that lending is therefore reasonably efficient, and prices for given borrowing categories will often respond in lockstep to changes in the macro environment.

By contrast, venture debt is more idiosyncratic. Young tech companies lack long financial histories, and their growth rates make extrapolating from the records that they do have impossible. Investing in them is about gauging the people running the business as much as it's about mechanically analyzing financial statements, rendering read-across comparisons difficult.

Beside the fact that growth companies' credits are hard to compare to one another, lenders aren't competing on price alone. A host of other factors are important to growth companies, including:

- The reputation of a firm's principals
- Their records with other entrepreneurs
- The personal chemistry between teams

All of these inform a borrower's choice of financial partner. This gives lenders more leeway around pricing than they'd have with mature borrowers. The result is that the underlying credit isn't the only thing driving yield.

In short, the market for mature companies' debt is more efficient and transparent than the venture equivalent. The variables that drive pricing are comparatively well understood and predictable, which implies a somewhat homogeneous market for similar instruments — they will tend to move together as the environment changes. Since venture loans are constructed on a different basis, they provide a degree of structural diversification for investors.

SaaS growth rates underpin lending

The structural differences between the underwriting processes outlined above are likely to endure, suggesting that the yield gap between conventional and venture loans will persist. However, venture debt is also attractive for other reasons, including the borrower universe. While some tech companies — chip manufacturers, for example — look a lot like traditional industrial concerns, a software company's business model is different in many important respects.

Business software was historically sold via a one-time perpetual license fee, sometimes with a smaller recurring maintenance fee.

Today, by contrast, cloud-based software is sold on a monthly, quarterly, or annual subscription basis. The installed base represents a very reliable annuity stream, with extremely consistent revenues and high contribution margins. And, the reliability of those revenues is complemented by a very steep growth profile.

Virtually every business in the world is shifting its software from on-premises to the cloud. In fact, 73 percent of companies plan to make their business systems completely software as a service (SaaS) based by the end of 2020.

This is a multi-decade, secular shift that is driving enormous growth for SaaS companies. Just consider that while on-premises solutions are only growing at 8 to 9 percent, SaaS revenues are growing by an average of 25 to 30 percent.

Any investment in acquiring SaaS customers can therefore generate tremendous returns, even if near-term cash flows look challenging. In our experience, SaaS companies typically have to spend $1 on sales and marketing to acquire $1 of annual recurring revenue. The negative cash flow that is reported in that first year looks very different in subsequent periods, as the development and sales expenses have already been funded, and run-rate margins can approach 80 percent over 8 to 10 years.

Given those metrics, software companies can create $3 to $5 in enterprise value from every $1 invested in sales.

Software business models also afford downside protection

The potential for such efficient value creation (and the rapid natural deleveraging that follows) allows loans to be structured at comparatively low LTV ratios. Not only that, the downside protection that this gives investors is augmented by other factors.

The underlying businesses tend to be quite recession resilient. Accounting systems and marketing automation platforms, for example, are typically mission-critical. Even in economic downturns, companies don't get rid of their core software subscriptions.

In addition, the sales function in a SaaS company is a growth driver, which affords its managers a degree of cost control that doesn't exist in other business models. If a traditional business generates the same sales in consecutive years, it will report 0 percent growth.

Conversely, a SaaS company that reports equivalent unit sales in years one and two has doubled in size. If it doesn't generate any sales at all, it will report flat year-over-year revenues.
This is a very powerful revenue model, and that power is amplified by the ease with which customers can adopt and implement SaaS software solutions compared to on-premises products.

Although software companies have never been subject to the same capacity constraints that manufacturing businesses operate under, SaaS models affords them even greater potential for growth.

While the upside benefits of this model are obvious, it also offers an underwriter substantial downside protection. Specifically, sales spending can be cut significantly without really affecting the current revenue base. If business conditions merit it, there is flexibility to cut costs within the business and to harvest the existing cash flow stream, implying much greater coverage for debt than the reported P&L might suggest.

Stakeholder alignment is also important. Loans should be underwritten against realistic risk appraisals, and an understanding of the support that the company's equity sponsors can provide. Managing shareholder relationships so that support is given when needed can be a critical element in a lender's risk management process.

Properly structured and managed, venture debt therefore combines a number of attractive characteristics for lenders. The structural characteristics of the origination and underwriting processes form a constructive basis for pricing and other terms.

Moreover, many of the potential borrowers have business models that, while not conforming to traditional underwriting characteristics, are tremendously well suited to support debt.

Higher yields reflect structural differences between venture debt and other corporate lending

Venture lending can generate higher yields than other classes of corporate debt. But it is a mistake to think of the yield purely in terms of the risk of the underlying credit.

The link between risk and yield is much less mechanical in venture debt than in other credit markets, and many other factors influence pricing and returns.

The result is that a properly constructed venture debt portfolio can provide investors attractive returns relative to underlying risk and offer an important source of diversification within an income mandate.

CAN COVID-19 INTERRUPT THE ESG TREND?

Will COVID-19 and its associated bear market interrupt the move towards responsible investing? While a cynic would say yes, we would disagree for three reasons: ESG as a factor has performed well through this coronacrisis, we don't think the area is in bubble territory and we believe the long-term structural tailwinds remain in place.


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Will COVID-19 and its associated bear market interrupt the move towards responsible investing ('RI')? The cynic would say yes: the growing trend of responsible investing using environmental, social and governance ('ESG') criteria is likely to be put on the back-burner because of the bear market.

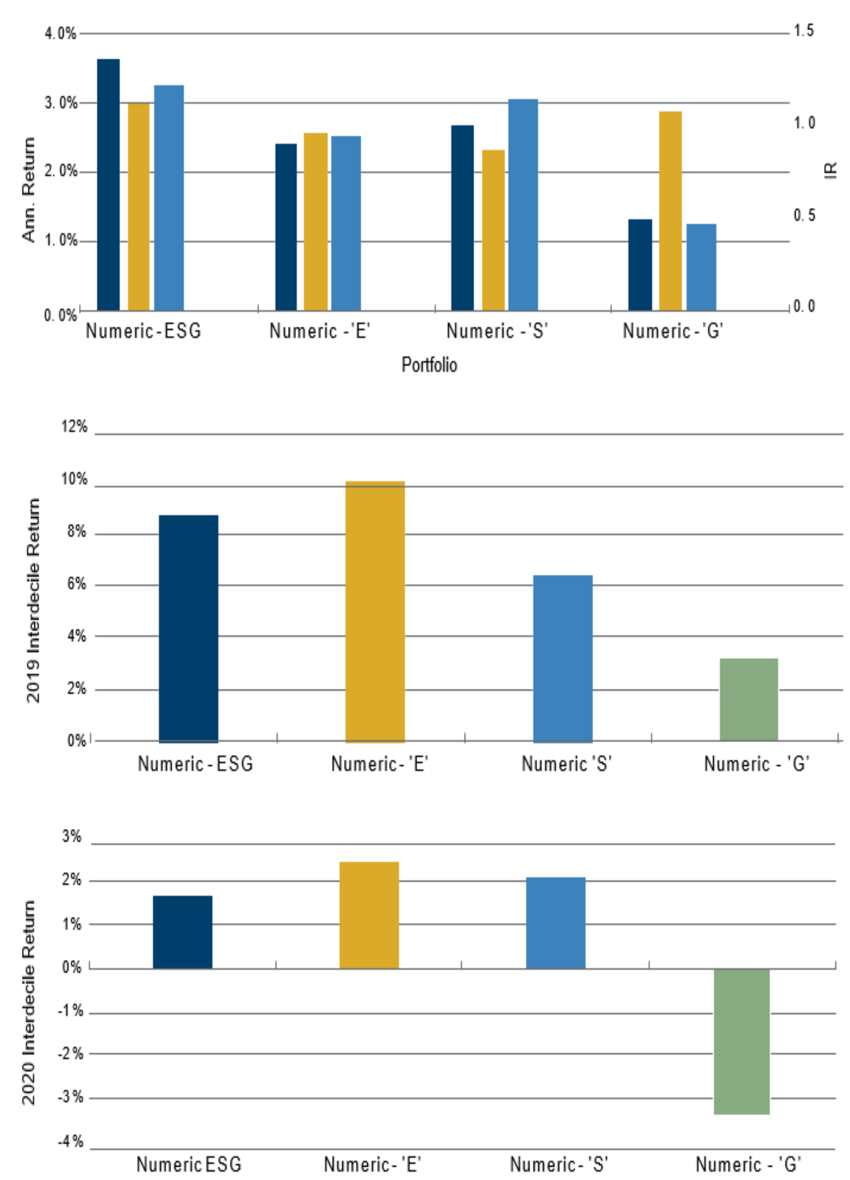
Indeed, history would support this position. During the 2008/09 bear market, for instance, investors demoted climate change and 'green' issues right towards the back of the priority queue. However, we would disagree with this cynic for three reasons.

Why the Cynics Are Wrong: Performance, No Bubble and Structural Drivers

First, ESG factors have performed well in 2019 and in year-to-date in 2020.[1] This can, for instance, be observed by looking at the MSCI ESG Leaders indices. However, we observe it in a more precise manner ourselves. Man Numeric has developed a set of ESG alpha signals, using a range of data providers, and its own quantitative adjustments.

1 Through to 31 March.

Figure 1. Man Numeric ESG Performance – Simulation 2012-19 (top), 2019 (mid), 2020 YTD (low)



Source: Man Numeric; As of 31 March 2020.
The ESG model spreads shown are provided for illustrative purposes only, do not represent any product of Man Numeric, and should be considered hypothetical. Hypothetical results have inherent limitations and should not be relied upon. Model results are gross of any fees and expenses that would be charged in an investment product.

> "He're is a good chance, in our view, that this theme is one of the dominant factors of the coming decade, at the end of which it may well have taken bubble-like proportions.
>
> However, for now a bubble cannot be detected"

Figure 1 shows the performance of these signals in the historical simulations, in 2019 and year-to-date in 2020 (annualised). It can be noted that the driving ESG themes in 2019 and 2020 were 'E' and 'S', which have more recently become a focus of corporate management. On the other hand, 'G' – which has been viewed at the only legitimate ESG factor by some – has lagged. We view ESG factors as elements that can help achieve good risk-adjusted returns.

And obviously, the need for return has by no means lessened due the bear market and the COVID-19 crisis.

Second, we find no evidence that the growing ESG attention has reached bubble-like proportions. In fact, quite the contrary. There is a good chance, in our view, that this theme is one of the dominant factors of the coming decade, at the end of which it may well have taken bubble-like proportions.

However, for now, a bubble cannot be detected. For instance, Empirical Research calculates that stocks held by ESG funds are not at a significant premium to other stocks (Figure 2). Additionally, while 2019 showed good inflows into ESG funds, it only amounted to net USD20 billion, which is very small in comparison to all flows and market cap.

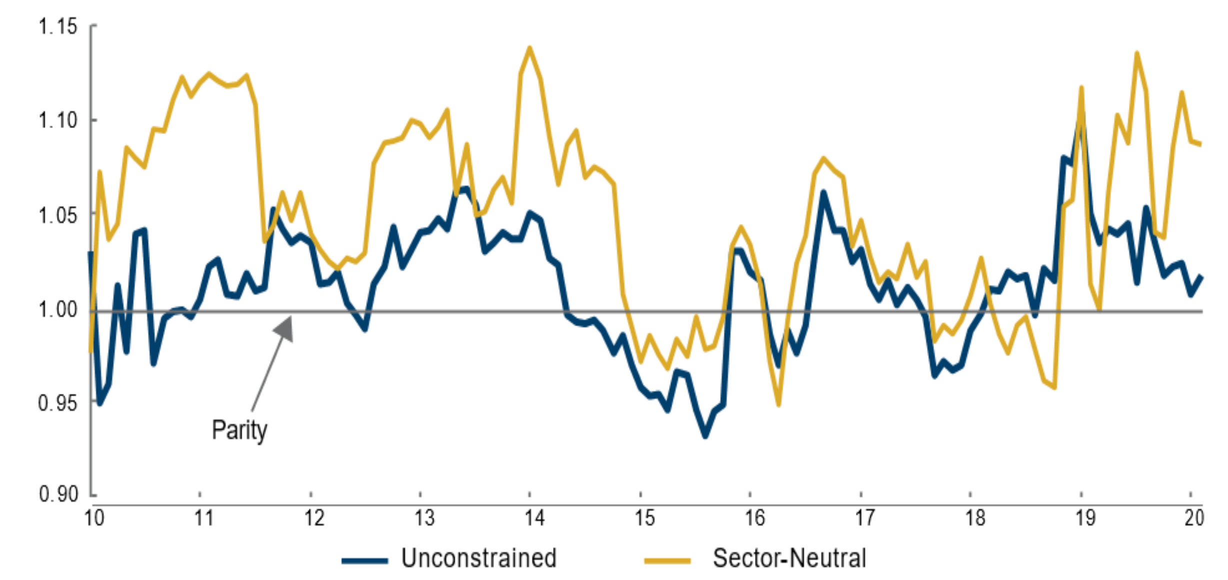
Third, some of the driving forces behind responsible investing are very much long-term structural drivers, not short-term cyclical drivers.

These include, but are not limited to: diversity and inclusion to achieve better decisions; climate change as a large existential threat that needs to be addressed; and governance structures to ensure incentives are aligned with all stakeholders.

Conclusion

As such, we don't feel that there is a bubble in RI, and don't expect retrenchment from the ESG leaders compared to the broader market. RI has moved on since 2008 – and so should our views.

Figure 2. Empirical Research ESG Premia



Source: Empirical Research Partners Analysis; As of 31 March 2020
ESG fund ownership is the share of a stock's capitalisation owned by ESG ETFs. Capitalisation-weighted data.

AUSTRALIAN REGULATORY CHANGES IMPACTING GLOBAL FUND MANAGERS

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Australia is in the midst of a number of regulatory changes that are impacting local banks, fund managers, financial advisers, insurance providers and superannuation funds following the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

While most of these regulatory changes will impact local Australian entities, this article focuses on a couple of changes that will impact global fund managers wanting to do business in Australia.

New Foreign Financial Services Providers licensing regime

The Australian Securities and Investments Commission (ASIC) has been undertaking a comprehensive review and consultation of the Australian Financial Services (AFS) licensing regime for Foreign Financial Services Providers (FFSPs) looking to carry on financial services activities in Australia, including marketing their offshore funds or providing portfolio management services to Australian clients. This impacts FFSPs currently relying on the existing sufficient equivalence relief and new FFSPs looking to enter the Australian market.

On 10 March 2020, ASIC released the updated version of Regulatory Guide 176: Foreign financial services providers (RG 176) following extensive consultation with industry and overseas regulators.

The updated RG 176 provides guidance on the new AFS licensing regime for FFSPs providing financial services to Australian wholesale clients. The new licensing regime has two key elements:

- Foreign AFS licence: a new foreign AFS licensing regime for FFSPs.
- Funds management relief: a limited licensing relief for providers of funds management financial services seeking to induce eligible Australian users.

Foreign AFS licence

An FFSP that is authorised by an overseas regulatory authority that regulates the FFSP under a "sufficiently equivalent" regime is eligible to apply for a foreign AFS licence.

ASIC has expanded the list of "sufficiently equivalent" regimes to now include Denmark, France, Germany, Hong Kong, Luxembourg, Ontario Canada, Singapore, Sweden, the UK and the US. ASIC will continue to assess applications to extend the foreign AFS licence to cover additional overseas regulatory regimes.

The updated online application and the licensing regulatory guides released in April allow FFSPs to apply for the new foreign AFS license.

The application process for a foreign AFS licence is intended to be more streamlined than a standard AFS licence application, and an FFSP holding a foreign AFS licence will be exempt from certain obligations that apply to AFS licensees, such as financial requirements.

However, a foreign AFS licensee will still be subject to several obligations including, to have in place adequate arrangements for management of conflicts of interest and risk management systems.

Funds management relief

The newly introduced funds management relief is narrower in application than what was initially sought by the industry and so may be of limited use. The funds management relief only provides relief for the conduct of "inducement" activities.

If an FFSP is otherwise carrying on a financial services business in Australia (e.g. because of ongoing financial services being provided after the initial "inducement" activities) then it is likely that they would fall outside the scope of the funds management relief and a foreign AFS licence is required unless another applicable exemption can be relied on.

The funds management relief also no longer references a 10% cap on the gross revenue generated from the provision of the funds management financial services in Australia or a requirement for the assets being managed to be located outside of Australia which were part of ASIC's original proposal.

Transition period

The transition period allows FFSPs to continue to rely on their existing sufficient equivalence relief for another two years (until 31 March 2022) provided that the FFSPs have notified ASIC of their reliance on the sufficient equivalence relief and was able to rely on the relief on 31 March 2020.

Next steps

- If you are relying on the sufficient equivalence relief, you have two years (until 31 March 2022) to transition into the new regime.
- Assess your activities (or intended activities) in Australia to confirm whether you are able to rely on the funds management relief or other licensing relief.
- Prepare to apply for a foreign AFS license. If you are considering applying for the foreign AFS license, we recommend you do so as soon as you can, given ASIC's service charter provides that ASIC aims to complete 70% of applications within 150 days, and 90% within 240 days. This means it may take up to 8 months or longer after the application is lodged for you to obtain the foreign AFS license.

Updated ASIC Regulatory Guide 97

In the last few years, ASIC has been making significant changes to the fees and costs disclosure for superannuation funds and managed investment schemes in the prescribed product disclosure statement (PDS) provided to retail clients.

On 29 November 2019, ASIC released an updated version of Regulatory Guide 97: Disclosing fees and costs in PDSs and periodic statements (RG 97), following an external independent review of the fees and costs disclosure regime.

The updated RG 97 makes major changes to the fees and cost disclosure regime for products distributed to retail clients. Australia is different to most other jurisdictions in that hedge funds can be offered to retail clients as well as wholesale clients. The changes to the fees and costs regime includes simplifying some of the previous complexities with the fees and costs disclosure. The new fees and costs disclosure requirements will apply to PDSs issued on or after 30 September 2020.

Key changes

- Re-formatting the fees and costs summary to distinguish between ongoing annual fees and costs and member activity related fees and costs.
- Removing the requirement to calculate and disclose property operating costs and borrowing costs.
- Specifying that all performance fees are to be calculated based on an average of the previous five financial years. Superannuation

funds and managed investment schemes are also required to disclose performance fees information for each of its underlying funds, however ASIC has indicated that it might revisit this given concerns around confidentiality.
• Clarifying that fees and costs in PDSs must be shown gross of tax and without adjustment in relation to any tax deduction available.

Considerations for global fund managers

Global fund managers will need to be aware that superannuation funds and responsible entities of registered managed investment schemes will need to implement the updated RG 97 fees and costs disclosure regime for all PDSs with an issue date that is on or after 30 September 2020.

Accordingly, fund managers may receive requests from superannuation funds and responsible entities for fees and costs information calculated under the previous RG 97 disclosure regime as well as the new RG 97 disclosure regime.

Design and distribution obligations

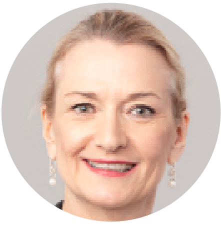
The Australian Government has passed new legislation introducing new design and distribution obligations (DDOs) as well as product intervention powers. The DDOs will come into force in April 2021 and will affect all managed fund products that target retail clients, while the product intervention powers are immediately effective.

The DDOs and the product intervention powers are aimed at ensuring that funds are targeted and sold to the right consumers, and where funds are inappropriately targeted or sold, ASIC will be empowered to intervene in the distribution of the fund to prevent harm to consumers.

The DDOs will require issuers to:
• Identify target markets for their funds and prepare target market determinations having regard to the features of funds and consumers in those markets.
• Select appropriate distribution channels.
• Periodically review distribution channel arrangements to ensure they continue to be appropriate.
In addition, distributors will be required to:
• Put in place reasonable controls to ensure funds are distributed in accordance with the identified target markets, and
• Comply with reasonable requests for information from the issuer in relation to the fund's review.

The views reflected in this article are the views of the authors and do not necessarily reflect the views of the global EY organization or its member firms.

HONG KONG HEDGE FUND MANAGERS: OBSERVATIONS ON REGULATORY COMPLIANCE



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In recent years we have seen an increase in the Securities and Futures Commission (SFC) conducting on-site inspections of SFC licensed corporations. In 2019 alone, the SFC conducted 350 on-site inspections, a rise of 19.8% from the previous year.

One regulatory focus of note is senior management accountability, and statistics demonstrate that the SFC has little hesitation in holding individuals accountable for non-compliance.

In this article, we share six common compliance deficiencies observed during our recent mock audits of hedge fund clients. These audits were conducted to help clients prepare for an SFC inspection. In sharing our observations, we encourage firms to conduct a gap analysis between these deficiencies and their own operations.

FMCC and Code of Conduct

While conducting these mock audits, we identified a number of instances of non-compliance with relevant provisions of the SFC's Fund Manager Code of Conduct (FMCC) and the Code of Conduct for Persons Licensed by or Registered with the SFC (Code of Conduct). The FMCC is applicable to all fund managers, including those involved in the management of authorized and unauthorized collective investment schemes. While the FMCC and Code of Conduct do not have the force of law, a breach is likely to have an adverse effect on the SFC's view of the defaulting entity or individual's fitness and properness to hold an SFC licence and may result in disciplinary action.

Observation 1: Insufficient measures in recording MNPI

A portfolio manager may become privy to material non-public information (MNPI) when conducting due diligence on listed companies. While perhaps only a few fund managers set out to deliberately breach insider trading laws, a fund manager may nevertheless end up on the wrong side of an investigation due to the lack of robust compliance procedures to prevent the misuse of MNPI.

Our mock audits revealed that:

• while hedge fund managers sometimes obtain MNPI about listed companies through frequent contact with the management of these companies, smaller hedge funds in particular do not maintain a central system to record and store attendance notes of telephone calls, interactions and meetings with these companies; and
• some hedge fund managers do not regularly review electronic communications between their employees and third parties from listed companies to detect any potential misuse of MNPI.

The FMCC requires firms to establish, maintain and enforce policies and procedures to prevent market misconduct and insider trading. We recommend that firms take a more proactive approach in managing MNPI risks. At a minimum, a firm should have a central electronic recording system of MNPI, which must be periodically reviewed against the firm's trading activities and personal trading activities of its employees.

Observation 2: Lack of measures to demonstrate appropriate use of soft dollars

Over the years, we have seen best execution and soft dollar arrangements being a common topic in SFC inspections and enquiries. Following MiFID II in January 2018, and the SFC's own report on the thematic review on best execution published in the same period which saw many firms directing orders to brokers offering more attractive soft dollar arrangements, we expect the SFC to pay even more attention to firms' controls in this area.

The Hong Kong regulator permits the use of soft dollar arrangements; but the FMCC puts the onus on the licensed firm to ensure that such arrangements will not adversely affect the firm's ability to deliver best execution.

Our mock audits revealed that:

• some hedge fund managers do not have policies and procedures in place to evaluate broker performance and the use of soft dollars provided by brokers; and
• of the firms with policies and procedures in place, some do not periodically evaluate their use of soft dollar arrangements, or are unable to demonstrate that they perform such an evaluation.

While a fund manager may consider all relevant factors in its broker selection exercise, without proper policies and procedures and records documenting broker evaluations, it will be difficult to convince the SFC that broker selection is not primarily based on soft dollar inducements.

Observation 3: Failure to maintain records of suitability assessments

Suitability remains at the top of the SFC's agenda, it being named a priority in both its current and previous annual reports going back several years. Under paragraph 5.2 of the Code of Conduct, licensed firms must determine whether a product they are selling is a complex product. If a product is a complex product, the licensed firm cannot sell it to an individual investor, whether a professional or not, unless the licensed firm is satisfied that the product is suitable for the investor.

In 2018 and 2019, we saw the SFC take three notable disciplinary actions against licensed firms for deficient selling practices. In total the firms were fined HK$24.6 million. Given that the SFC has repeatedly communicated its concerns on this topic, it has limited patience where firms continue to fall short.

Our mock audits revealed that:

• some firms do not keep proper records explaining why the funds they manage are suitable for their investors, having considered their needs and circumstances; and
• some firms have not kept sufficient documents in relation to identification and risk assessments of investors.

Firms need to implement safeguarding systems to demonstrate suitability, and to automate and streamline that documentation so that investor information, interactions with investors, product due diligence, risk profiling assessments and professional investor assessments are recorded and regularly updated. Adequate record keeping is the best way, and in many cases the only way for a firm to demonstrate compliance.

Observation 4: Lack of records to show eligibility verification of CPIs

Certain investor related protections set out in paragraph 15 of the Code of Conduct, including the suitability assessment, can be waived for corporate professional investors (CPIs). However this waiver is not automatic; a licensed firm must conduct a formal assessment to verify that the investor is a CPI. The assessment criteria is set out in paragraph 15.3A of the Code of Conduct. It is principles-based and the SFC's FAQs assessment of Corporate Professional Investors includes a non-exhaustive list of factors to consider when performing the assessment.

Our mock audits revealed that while all firms performed CPI assessments, some hedge fund managers do not keep sufficient records. When the SFC conducts an inspection, its officers will ask for an audit trail of enquiries made and information obtained as part of the CPI assessment. In the absence of sufficient documents, it will be difficult to demonstrate to the SFC that the CPI assessment has been properly conducted.

Observation 5: Lack of records to support investment rationale

As part of the investment decision

making process, portfolio managers often meet with potential target companies to obtain business updates.

Our mock audits revealed that during or after these meetings, it is common practice for a portfolio manager to take personal notes.

However, some hedge funds do not maintain a central system to collect, record and store these notes. These personal meeting notes form an important part of the documentary evidence substantiating investment decisions and during routine inspections, the SFC will often ask for such evidence.

Observation 6: Insufficient monitoring of personal trading activities

The SFC actively pursues breaches of internal control failures. In fact, of the total fines of over HK$413.3 million imposed by the SFC in the final quarter of 2019, HK$408.8 million resulted from disciplinary actions concerning internal control weaknesses. A number of these actions resulted from failures to put in place adequate systems and controls to detect and prevent illegal activities, including short selling and cross trades by employees using their personal trading accounts.

The FMCC requires fund managers to establish appropriate policies and procedures governing personal account dealing (PAD).

Our mock audits revealed that:

- some firms do not strictly follow their own PAD policies and procedures. For example, employee personal account statements are not periodically reviewed to ensure that trades have been pre-cleared as required; and
- listed securities flagged for MNPI are not always placed on a restricted trading list.

We recommend that hedge fund managers actively monitor personal account trading activities to ensure compliance with the firm's PAD policy.
The SFC will not hesitate to discipline senior management for such failures. In mid-2019 the SFC suspended the licences of two senior management staff for a period of six months for failing to adequately supervise and implement effective controls in relation to personal trading activities.

Conclusion

We recommend hedge fund managers to review their policies and procedures, with an eye toward what the SFC would look for during an inspection. There is no bright line test as of how much effort is sufficient, but erring on the side of caution, particularly in areas that the SFC has highlighted in its thematic inspections and enforcement actions should help to narrow the expectation gap and reduce non-compliance risks.

THE IMPACT OF COVID-19 ON JERSEY'S INVESTMENT FUNDS INDUSTRY

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On 9 May 2020, Jersey marked the 75th anniversary of its liberation at the end of World War II. The world now faces a different battle against an invisible enemy, the coronavirus ("COVID-19"), which is causing a devastating impact on human life and health, and the global economy.

This article considers the impact, challenges and issues faced by the Jersey funds industry as a consequence of COVID-19.

Emergency Laws

In the battle against COVID-19, Governments worldwide, including the States of Jersey, introduced emergency laws to address public health concerns and imposed non-essential travel restrictions, physical distancing and lockdown measures ("COVID-19 measures"), primarily to protect human life and health, contain the rapid global spread and reduce the burden on healthcare systems.

The States of Jersey has also relaxed regulations to facilitate the redeployment of healthcare staff, the use of alternative premises for healthcare and established an emergency fund for the crisis.

COVID-19 measures have had a substantial impact on Jersey's funds industry, but it is difficult at this stage to assess the overall financial impact.

Business Continuity

COVID-19 has presented unprecedented challenges, forcing Jersey funds businesses to implement their business continuity plans ("BCP") and focus on the health and safety of management and staff, including their physical and mental well-being.

Business and working practices have completely changed with the majority of businesses fully transitioning to remote working operations. This has led to an increased use of technology for internal and external meetings with video conferencing proving crucial to maintaining contact and conducting day-to-day business.

Policies and procedures should be reviewed and adapted to support these operational changes and risk assessments should be conducted on corporate governance, risk management, financial resources (including capital and cash flow), outsourcing, employees, IT and cybersecurity.

Data and Cybersecurity

Due to remote working and an increased reliance on technology, IT systems, servers, networks and data are more at risk for cyberattacks.

IT systems, networks and security should be closely monitored and recorded. Risk assessments should be conducted to assess loss of data, privacy breaches, cybersecurity and IT system and network failures.

Marketing

COVID-19 measures have restricted fund raising activities and virtual meetings have replaced investor face-to-face meetings.

Offering documents should now include disclosure and risk warnings on COVID-19's impact on investment objectives, valuations, liquidity and past performance. Existing fund documentation should be reviewed and updated with COVID-19 statements included in periodic reports and accounts.

Investor Take-On

In 2019, the Jersey Financial Services Commission ("JFSC") revised its AML / CFT handbook to allow the use of electronic identification ("E-ID") as an alternative to original 'wet-ink' documents to show evidence of identity from electronic sources, including phone apps capturing information, documents and photos, as long as certain identified risks are considered and effectively managed.

With COVID-19 measures, it has been difficult to follow the usual identification procedures where investors are unable to have 'face-to-face' meetings or provide 'wet-ink' certified copy or notarised documents. Jersey fund managers and administrators have been able to use E-ID where permitted by their policies and procedures. Policies and procedures should be reviewed to include the flexibility to use E-ID, appropriate risks identified, and risk management procedures included.

Corporate Governance

Jersey-based funds and managers are usually 'managed and controlled' in Jersey to maintain tax residency. If a manager conducts 'fund management business' in Jersey, it must be 'managed and directed' in Jersey to comply with economic substance.

Constitutional documents typically require meetings to be quorate in Jersey and restrict telephone or video conference attendance from a country prejudicing tax residency.

Due to COVID-19 measures, Jersey funds and managers have made changes to their usual operating practice for holding quarterly board meetings or ad hoc emergency meetings. If it is not practical to amend constitutional documents, alternate directors can be appointed.

The Jersey Comptroller of Revenue issued guidance to reassure companies who were making temporary adjustments to their normal operating practices to mitigate the effects of COVID-19, that it would not regard them as failing to meet the economic substance test.

A company that usually holds board meetings in Jersey will now be allowed to temporarily hold virtual meetings for directors to attend. Additionally, the Jersey tax residency of a foreign company managed and controlled in Jersey will not be affected by any temporary changes.

Constitutional documents should be reviewed to check meeting procedural requirements and that the tax authority for the country of a particular director's residence has issued similar guidance.

Regulatory

Recognising the challenges faced by Jersey's funds industry, the JFSC has provided a level of flexibility and taken a pragmatic approach.

Application forms for forming new entities are submitted using the Registry's online portal. The Registrar will accept documents signed by electronic signature, scanned signature or by email confirmation. Certificates and approvals are emailed or made available on the portal.

For Jersey regulated businesses including funds and managers, the JFSC has extended regulatory filing deadlines, allowing three months for audited accounts and 20 days for fund statistics returns. The JFSC encourages regulated businesses to deal openly and co-operatively with it and will require them to take a proactive approach to business continuity and raise any concerns or risks at an early stage.

Liquidity Management

Due to the extreme market volatility, some Jersey open-ended funds are experiencing liquidity issues as concerned investors submit redemptions requests. Jersey funds and managers are having to consider 'tools' available to them to manage liquidity, taking account of the interests of exiting and remaining investors and any reputational damage risks. The liquidity tools might include the following:

(a) Redemption gates to enable a fund to control the timing of redemptions, allowing assets to be sold in an orderly manner to fund redemptions;

(b) Suspending redemptions for a period of time to prevent a 'run' on the fund;

(c) Distribution in specie of assets made by a fund to satisfy investors' redemption requests, avoiding the need to sell assets and pay sale costs;

(d) Redemption charges deducted from redemption monies payable to investors, representing a pro-rata share of the asset sale costs; and

(e) Side pocket entity to which illiquid or 'hard to value' assets are transferred, issuing shares or interests to relevant investors.

A fund's liquidity should be regularly reviewed and monitored. Constitutional and offering documents should also be reviewed to check if liquidity tools are available.

Contracts

The financial impact of COVID-19 may cause Jersey funds or their managers, investors, lenders or service providers, who may be experiencing liquidity or cashflow concerns, to review whether their contracts can be terminated or their performance delayed or discharged. A contract may include the following clauses:
(a) Force majeure clause: Relieves the parties from performing their contractual obligations when an act of God or certain circumstances beyond their control arises, making performance impracticable, illegal or impossible; and

(b) Material adverse effect ("MAC") clause: Allows a party to terminate a contract where a specified event, condition or change is (or reasonably expected to be) materially adverse to the operations, business, assets or financial condition of party or asset.

Investors might seek to delay a capital call payment, or see if they can be excused or excluded from an investment. Key service providers might look to delay or be excused from performance, vary service levels or even terminate their services agreement.

A buyer might look to terminate a sale and purchase agreement relying on a MAC clause where the asset value has substantially fallen. If a financial covenant or MAC clause in a loan agreement is breached or triggered, the lender will ask a fund to remedy (if capable) the breach and, in default, take enforcement steps. Insurers could refuse cover or to pay a claim, seeking to rely on a force majeure or MAC clause.

Whether COVID-19 triggers these clauses will depend on the precise wording in the relevant contract which should be carefully reviewed.

Transactions

Due to COVID-19 restrictions, as an alternative to 'wet-ink' signatures, the use of electronic signatures to sign documents for completing transactions has become more prevalent.
Under the Electronic Communications (Jersey) Law 2000, if parties agree, a contract may be formed by electronic communication and signed using an electronic signature. If statute requires 'wet-ink' signatures, electronic signatures will suffice as long as the method used identifies and shows approval of the signatory.

Some documents cannot be signed electronically, such as a registerable power of attorney or a power of attorney to be given by an individual, which are required to be signed in the presence of a witness, which is difficult with physical distancing. Constitutional documents and documents being signed, should be reviewed to check if electronic signatures are allowed and for any power of attorney to consider.

Lessons Learned

Jersey's funds industry will reflect on the impact of COVID-19. Businesses will evaluate their BCPs and IT systems in light of working practice changes and consider if any lessons can be learned and improvements made. It will be important to review relevant documentation and, where appropriate, update to cover the issues and matters highlighted in this article.

Maples Group Jersey

Maples and Calder (Jersey) LLP is the Maples Group's law firm in Jersey. As part of an international organisation with 18 locations worldwide, our lawyers and professionals have seen how many of the issues impacting Jersey have similarly impacted other jurisdictions where we operate. We have therefore gained a unique insight into legal and regulatory trends which will benefit our Jersey clients.

THE PRIVATE MARKET REPUBLIC?

How Collaboration and Technology Are Enabling a Trillion Dollar Opportunity

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Private market funds, such as private equity, private credit, real estate and infrastructure, have traditionally been sold to institutional investors.

That's starting to change as institutional flows into private investments plateau, pushing private market funds toward a fresh source of investment: high-net-worth investors.

In the US alone, the affluent and mass affluent segments control more than $16 trillion investable assets.[1] If private markets capture just 5-10 percent of those assets, it would represent between $800 billion and $1.6 trillion in assets under management.

Recognizing the opportunity, private fund managers and large asset managers are beginning to strategically tap into this universe through wealth management channels.

Regulators are also taking an active interest. In an April 2019 interview at the U.S. Chamber of Commerce, SEC Chairman Jay Clayton spoke about his desire to give retirement investors greater access to private funds.

Two months later in June, the SEC put out a call for ideas to 'simplify, harmonize and improve' regulations surrounding the sale of non-public investments. This potentially transformative initiative could result in amended rules, greater access to products and more secondary sale options.

The Individual Investor Opportunity

Increased access to private market funds comes at an opportune time for individual investors. The public markets are shrinking. Between 1996 and today, the universe of listed companies in the US stock market declined by roughly 50 percent[2].

The entry of abundant new capital in the late-stage venture market has helped organizations stay private longer. It is likely that many of the unicorns (private companies with $1 billion+ valuations) going public today are already further along their growth trajectory than similar companies that went public a decade or two ago.

Gaining a clear entry path to the private markets will position individual investors to access companies' strong pre-IPO growth potential.

The private markets are likely to appeal to individual investors looking for products with a higher steady yield than what fixed income currently offers, a better risk-adjusted return than public equities, and diversification from the ups and downs of public markets. With the right education, purchasing private market products can be simple and convenient. And with the right technology platform, investors can access their account and statements in an intuitive way that's similar to mutual funds and public securities.

The Hurdles of a Democratized Private Market

Better education and a stronger understanding of private market products will be critical so that investors can make informed decisions and investment advisors are prepared to advocate for their clients, and so that both groups have the opportunity to build their command of unfamiliar terminology and concepts.

Investors, advisors and managers also need reliable tools to model complex portfolios that include alternatives to demonstrate how certain asset classes can shift a portfolio's risk and return profile.

What's more, fund sponsors and wealth managers face challenges in alternative investment fundraising, including the administrative burden of managing small-dollar investments, as well as a complicated and error-prone subscription process. In addition, there is limited visibility into the book-building process, as well as privacy and data security concerns.

It will also be important for managers to accurately estimate operational hurdles that can occur as they trade high volumes but smaller tickets. Collaboration and technology will be critical to connecting the private market ecosystems and improving the flow of information. Scalable and flexible solutions will help remediate a fragmented market driven by disparate players and a lack of standardized distribution processes.

Unlocking the Registered Investment Advisor Market

Extending the availability of private funds has the potential to be a win-win, offering managers access to fresh capital and giving investors an opportunity to add new asset classes to their portfolios.

Yet the market is struggling due to a lack of agreed-upon standards for documents, terms and structures, and poor connectivity between investors and service providers. In a sense, today the private funds space is where the mutual fund industry was 25 years ago.

Much like mutual funds, standardizing client onboarding and creating a more transparent distribution process will add significant value.

That's why State Street and iCapital Network (iCapital) have teamed up to provide solutions for private market sponsors distributing registered products through wealth management and other distribution channels.

State Street offers specialist fund administration and registered transfer agency services to private market fund managers who are actively launching new products and distribution channels.

iCapital brings an end-to-end solution to manage alternative investments that helps advisors simplify operations and improve the investor experience. Together, we support participants — managers, distributors and investors — throughout the investment ecosystem by offering a modular solution to help clients better understand alternative investment fundamentals, market trends and opportunities.

This partnership can accelerate the launch of a registered product for a private fund manager whose infrastructure is built for institutional investors by simplifying the launch process and vendor due diligence.

With a centralized view that offers full transparency along the fundraising continuum, managers can see investments at every stage of the process and can analyze data by fund or advisor. The benefit to the end investor is an end-to-end digital way to monitor the lifecycle of their investments.

By streamlining the on-boarding, qualification, servicing and reporting of the high-net-worth advisor and investor market, fund managers and investors can diversify their business in a way that is scalable, transparent and secure.

Important Information

1 Cerulli US Alternative Products and Strategies
2 iCapital Network, "The Private Equity Market in 2019," Nick Veronis and Tatiana Esipovich, January 2019.

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Past performance is not indicative of future results. Alternative investments such as those described are complex, speculative investment vehicles and are not suitable for all investors.

An investment in an alternative investment entails a high degree of risk and no assurance can be given that any alternative investment fund's investment objectives will be achieved or that investors will receive a return of their capital.

This industry information and its importance is an opinion only and should not be relied upon as the only important information available.

BERMUDA: A REGULATORY UPDATE AND FUND STRUCTURE PRIMER

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Bermuda has a long and rich history as a financial center, supporting both the asset management and insurance industries.

With recent regulatory milestones achieved, now is a good time to review the investment management and fund framework supported locally.

Bermuda's Position as a Global Financial Center

Bermuda's key strengths, as detailed below, include (i) its position as an experienced global financial center; (ii) the quality of its service providers; and (iii) a solid well-respected regulatory environment that adheres to international requirements.

Bermuda is a strategic global financial center with sophisticated infrastructure and human capital to support various types of professionals in the financial sector, from managers of traditional hedge funds to private equity, venture capital, collateral managers and insurance managers.

This marketplace was developed, and is continually refined, by talented professionals who are experts in their respective fields. There are long-established business partners on the island including globally recognized banks, lawyers, accountants, corporate service providers and administrators working together with the investment manager community to drive world class innovation in the local industry, including fintech innovation.

Recent changes in legislation have affirmed Bermuda's commitment to responsiveness and quality. The Economic Substance Act 2018 and the Economic Substance Regulations 2018 were enacted in response to a scoping paper issued by the European Union's Code of Conduct Group (Business Taxation) in June 2018.

Further, effective December 2019, Bermuda enhanced its regulatory framework, including amendments to the Investment Funds Act 2006 (IFA). The EU's Economic and Financial Affairs Council (ECOFIN) confirmed in February 2020 that Bermuda had met its commitments given to the EU to implement legislative changes that comply with the EU's tax governance principles ahead of the deadline, and had accordingly been discharged from the review process.

Bermuda is globally respected for its leadership and proven record on compliance and transparency. In January this year, Bermuda's regulatory regime has been assessed by the Caribbean Financial Action Task Force (CFATF) and the global inter-governmental Financial Action Task Force (FATF). The results of these assessments continue to confirm Bermuda as having some of the highest international standards when it comes to combatting money laundering and the financing of terrorism and proliferation.

Bermuda Funds Landscape

The Bermuda legislation provides flexibility and options for global asset managers to meet their offshore investment business objectives. Investment funds may be structured and organized under Bermuda law in the following ways:

- Company limited by shares
- Limited partnership
- Limited liability company (LLC)
- Segregated accounts company
- Incorporated segregated accounts company (ISAC)
- Unit trust scheme

Companies, partnerships, LLCs and unit trusts that meet the definition of an investment fund as stated in the IFA are either Authorised (further classified as Institutional, Administered, Specified Jurisdiction Funds or Standard Funds (for retail investors)) or Registered (further classified as Private, Professional Class A, Professional Class B Funds or Professional Closed Fund) and thus regulated by the Bermuda Monetary Authority (BMA).

Authorised funds are classified based on criteria such as minimum investment and/or sophistication of the investor base. Investors seeking enhanced, yet efficient, supervision tend or prefer to invest into an authorised fund.

Professional funds are either Class A or Class B. In both cases, reporting requirements are met by filing an annual certification with the BMA. The qualification criteria differs between the two classes as it relates to the appointment of the investment manager.

Professional Class A funds must appoint an investment manager for the fund who is either:
• licensed under the Investment Business Act 2003;
• authorized or licensed by a foreign regulator recognized by the BMA; or
• carrying on business in or from Bermuda or in a jurisdiction recognized by the BMA, being a person who has gross assets under management of an amount that is not less than $100 million; or is a member of an investment management group that has

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consolidated gross assets under management of an amount that is not less than $100 million.

Closed ended funds (private equity) can be established as either private (less than 20 investors) or professional closed funds and audit waivers are available where the BMA considers it appropriate to do so.

The new Incorporated Segregated Accounts Companies Act 2019 allows for the creation of segregated accounts with separate legal status.

This allows both open and closed-ended strategies to be housed in the same vehicle, benefiting from synergies and cost and operational efficiencies while enjoying statutory ring fencing (assets of individual segregated accounts, or cells, are not available to the creditors of any other cell).

Given the separate legal personality, separate accounts may appoint different boards of directors. ISAC structures can be useful for master/feeder structures (one account can invest into another account within the same structure) and for family office structures.

It is not a requirement for investment funds to either have economic substance in Bermuda or to have a local audit or a local director.

Officers and service providers must be fit and proper persons. That being said, the Big Four accounting firms have a large presence on the island and the Institute of Directors continues to broaden and strengthen the independent director talent pool in Bermuda.

As managers look to implement ESG initiatives and consider "green" valuations, the Bermuda Stock Exchange (BSX), a fully electronic offshore securities market, has launched an Environmental, Social and Governance initiative that aims to empower sustainable and responsible growth for its member companies, listings and the wider community.

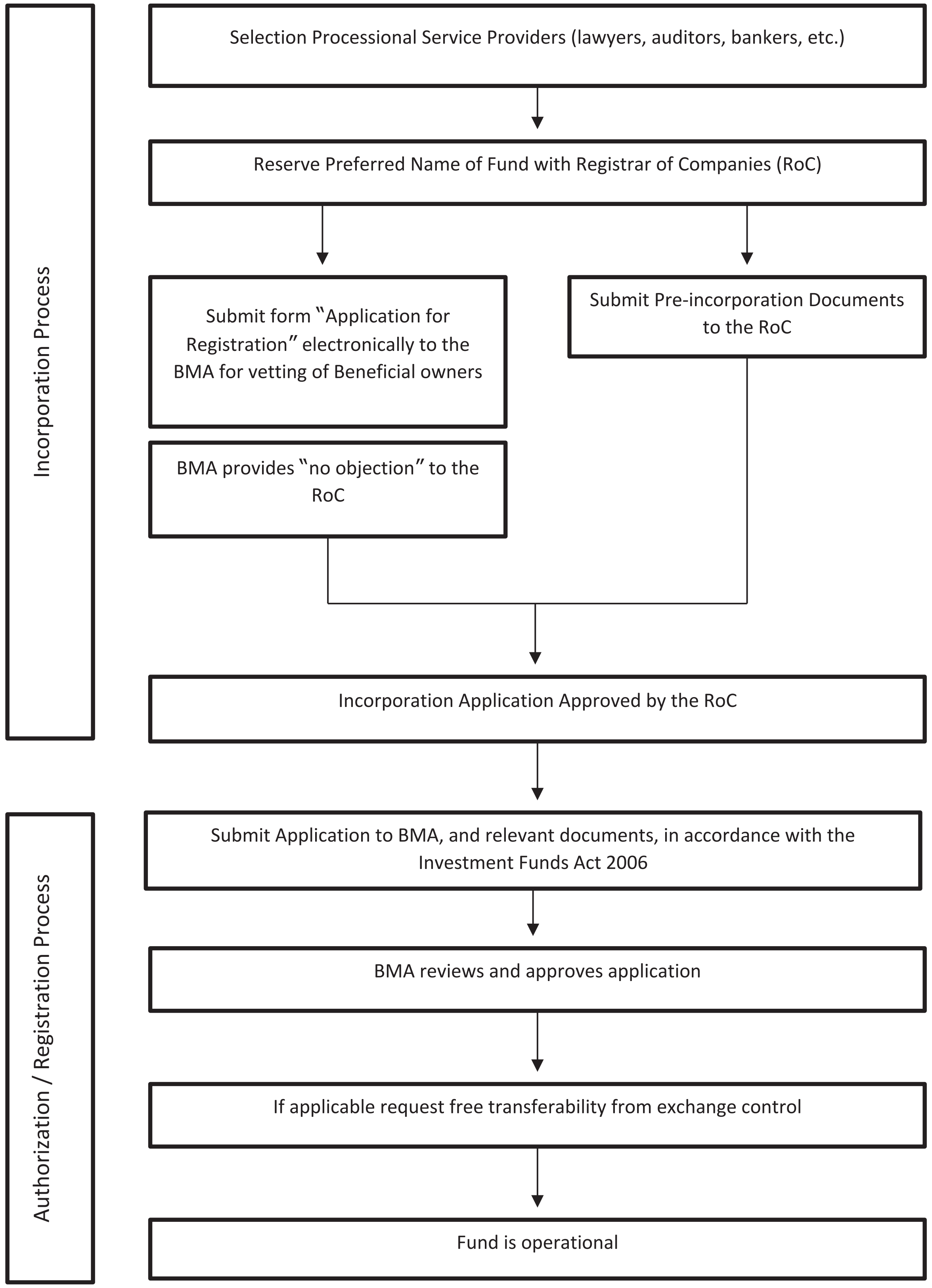
The BSX is the world's leading exchange for the listing of Insurance-Linked Securities (ILS) which are acknowledged as sustainable development investments.

Conclusion

Bermuda provides a wide variety of different legal structures to allow fund managers to meet their investment objectives in a recognized and respected regulatory environment.

How to set up a Bermuda fund structure

The following chart is reproduced courtesy of the BMA, the Bermuda Monetary Authority



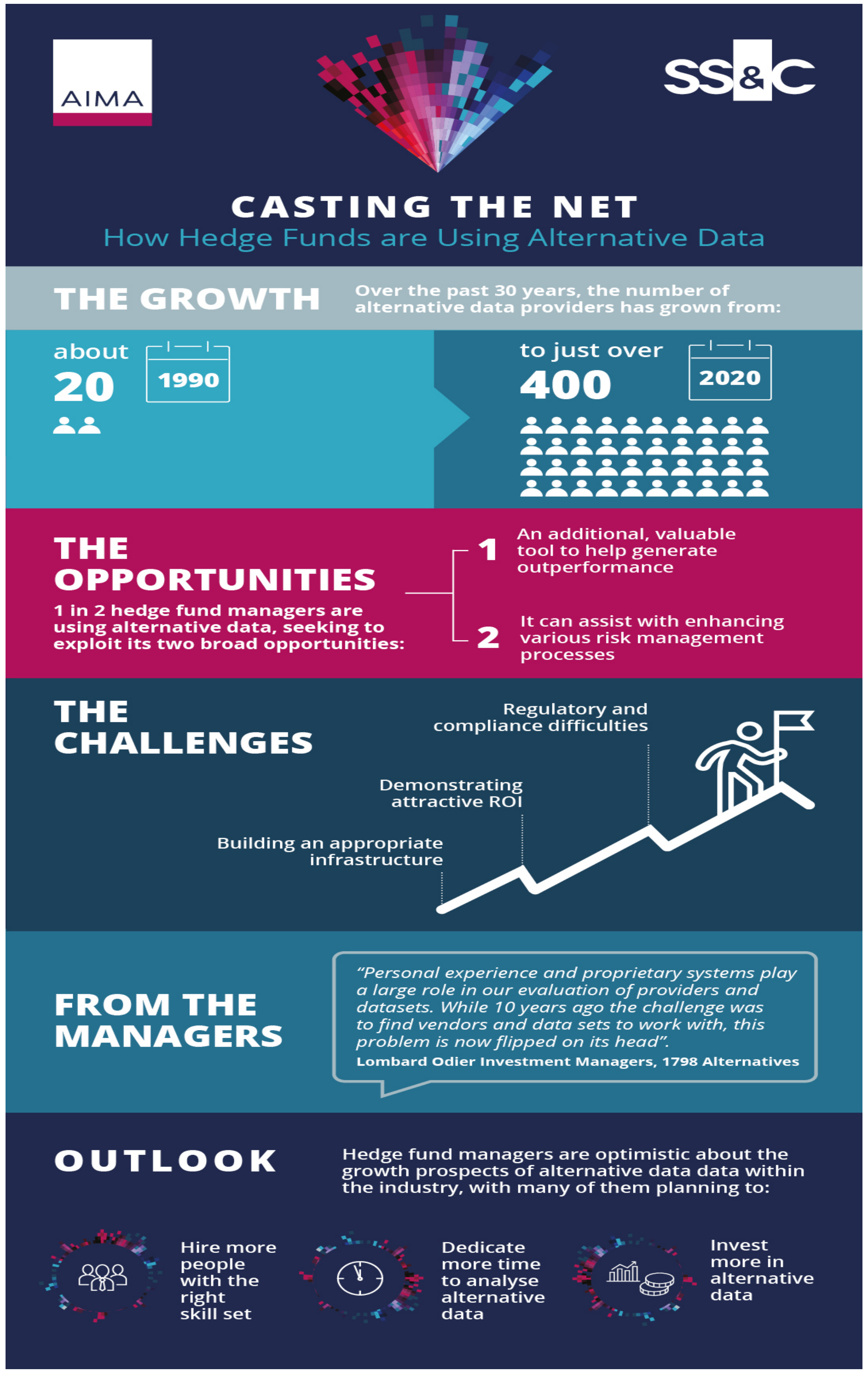
HOW HEDGE FUNDS ARE USING ALTERNATIVE DATA

The global economy and financial markets are always changing. With them, the information that hedge fund managers can gain from analysing the world around them also evolves. Consequently, the tools needed to extract data from such information need to adapt – successful investing, irrespective of what strategy or style one employs, depends to a good extent on gaining and maintaining a legitimate information edge over the rest of the market.

To put it differently, for hedge fund managers to meet the investment needs of their clients, they need to have a greater understanding of how the world functions than their competitors.

Central to this new way of thinking is the emergence of alternative data. In recent years, enabled by the technological advancements across a number of industries, accessibility to alternative data sets has improved tremendously: with a growing number of alternative data providers, hedge fund managers now have access to a large number of non-traditional data sources, such as satellite imagery, social-media trends and weather patterns.

The infographic on the opposite page provides insight to AIMA's latest research publication which examines hedge funds use of alternative data. You can read it here



AIMA Virtual Events

AIMA continues to deliver varied programme of events via virtual platforms. Click through to learn more.

AIMA members can watch past virtual events on-demand. To search for playbacks, visit www.aima.org

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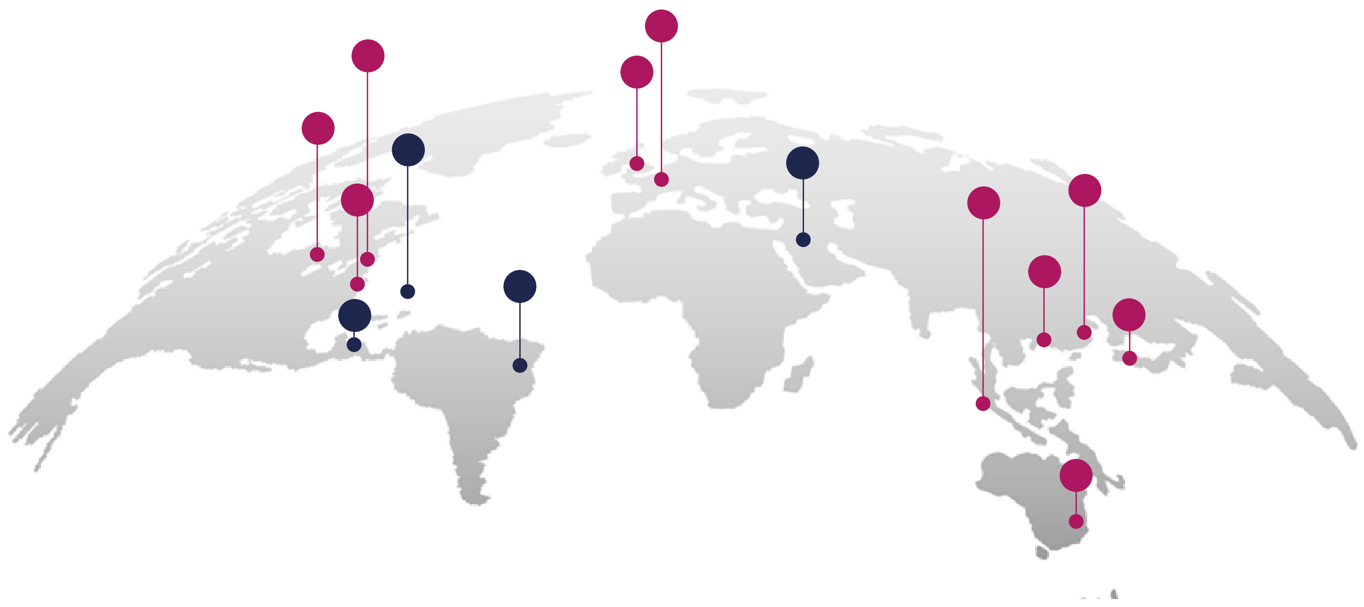

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