

SEPTEMBER 1, 2015

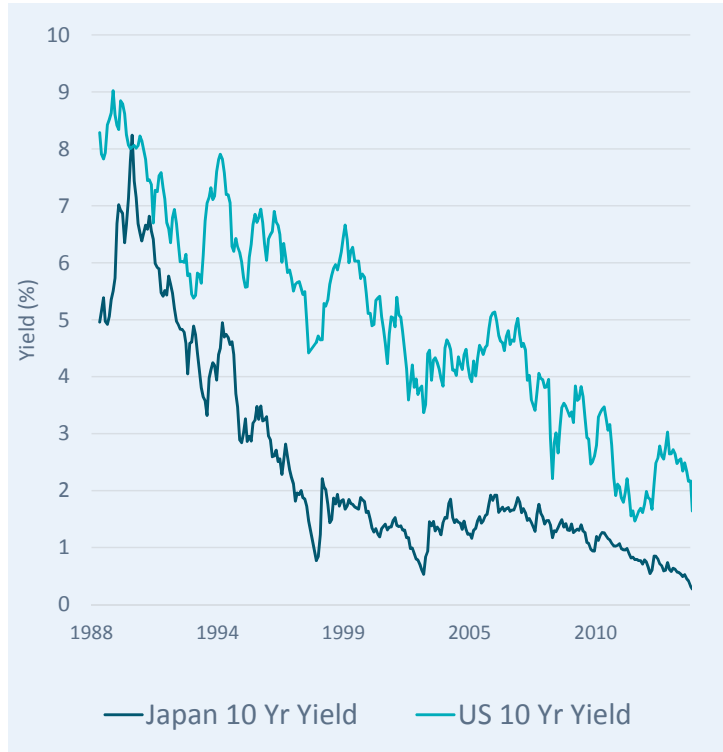
Shelly Heier & Jim Vos from Aksia, LLC

**Using Hedge Fund Alpha Strategies to Improve Portfolio Construction**

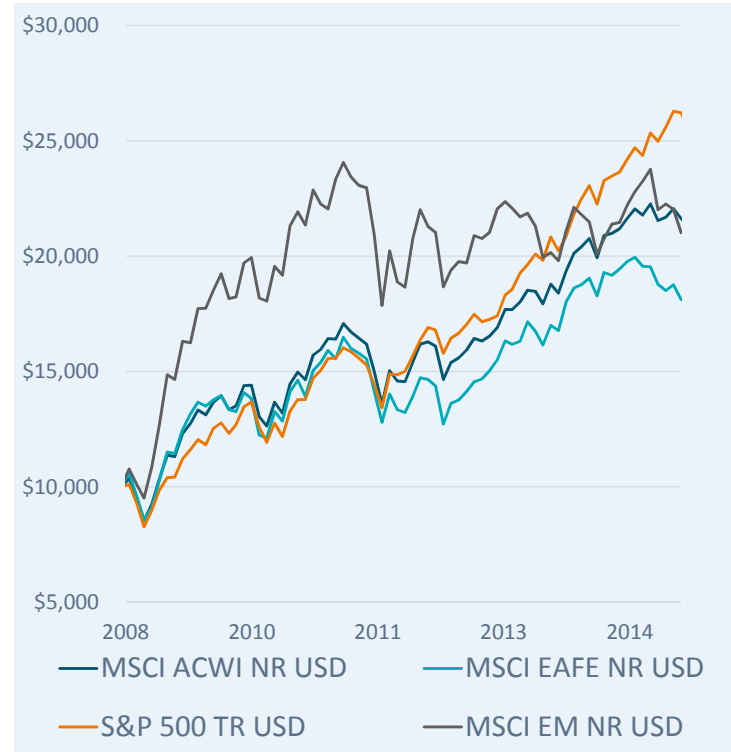
**2015 Client Summit**  
**True North**



# Why we favor hedge funds today



Sources: Bloomberg, MSCI, Standard & Poors

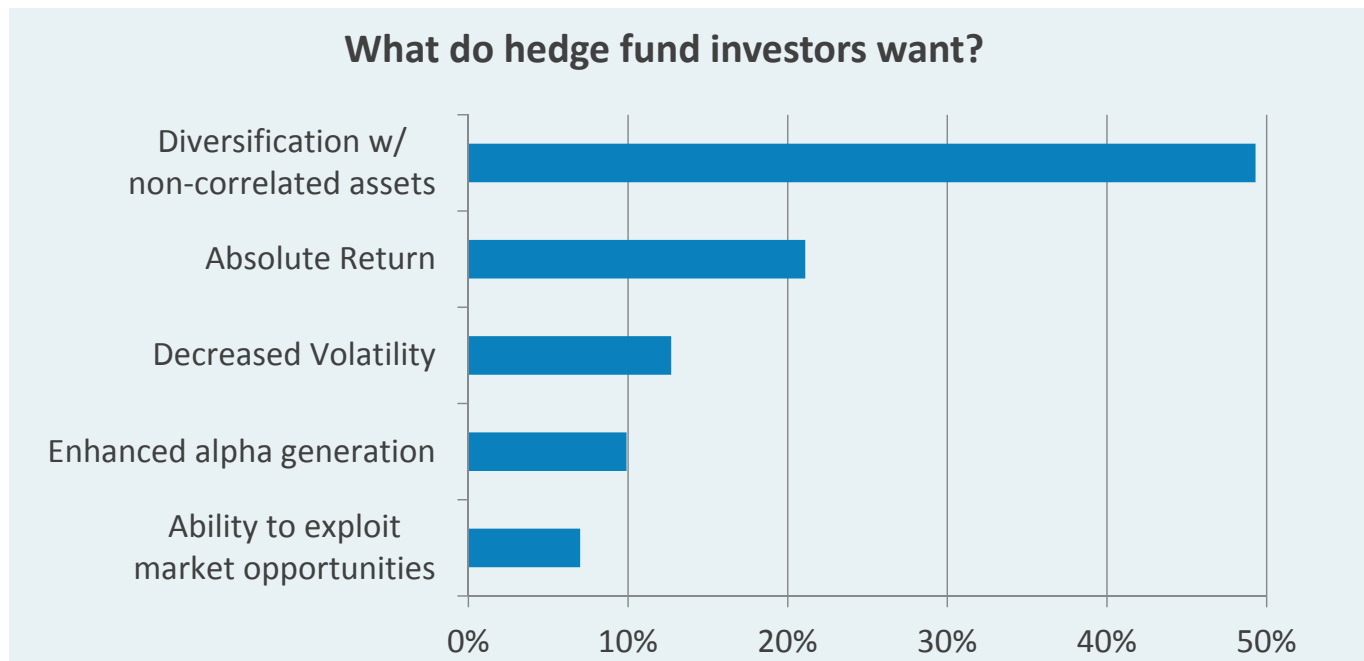


End of the 30-year  
bull market in  
bonds?

Cresting of six-year  
bull market in  
equities?

# The role of hedge funds

## The low correlation promise



Source: SEI Hedge Fund Investor Survey

# Calpers to Exit Hedge Funds

Pension Plan to Shed \$4 Billion Investment to Simplify Its Assets, Reduce Costs

By **DAN FITZPATRICK**

Updated Sept. 15, 2014 7:59 p.m. ET

The largest U.S. public pension plan is getting out of hedge funds as part of an effort to simplify its assets and reduce costs, a retreat that could prompt other cities and states to consider similar moves.

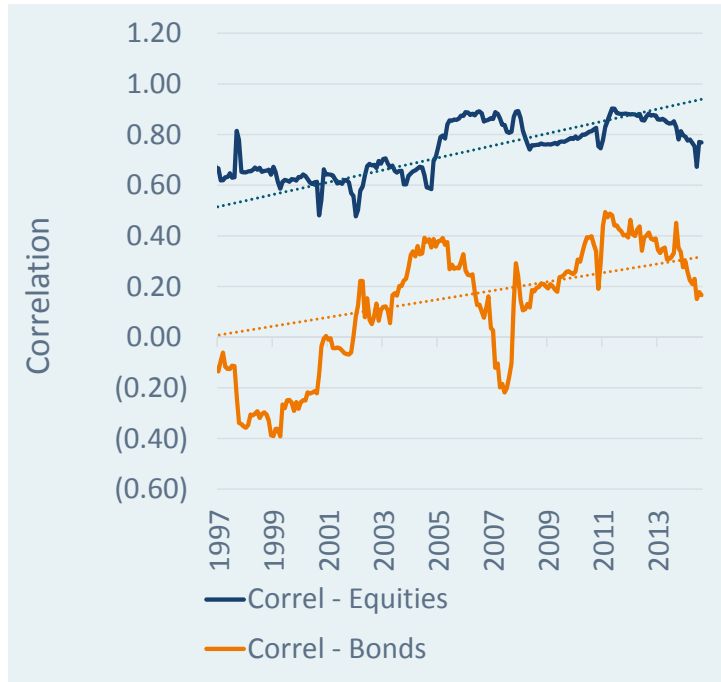
The California Public Employees' Retirement System said Monday it would shed its entire \$4 billion investment in hedge funds over the next year.

The pension known by the abbreviation Calpers, which manages \$298 billion in investments and benefits for 1.6 million current and retired police officers, firefighters and other public employees, is a bellwether for investment trends at other public plans. Any shift it makes will likely influence others because of its size and history as an early adopter of alternatives to stocks and bonds.

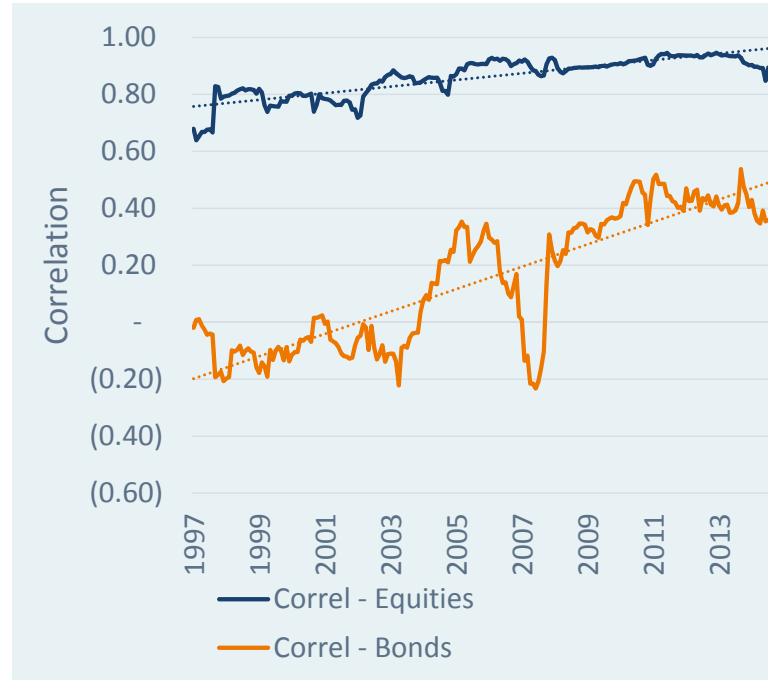
# Diminishing benefits?

Aggregate hedge fund correlation versus stocks and bonds

HFRI FUND OF FUNDS COMPOSITE



HFRI FUND WEIGHTED COMPOSITE

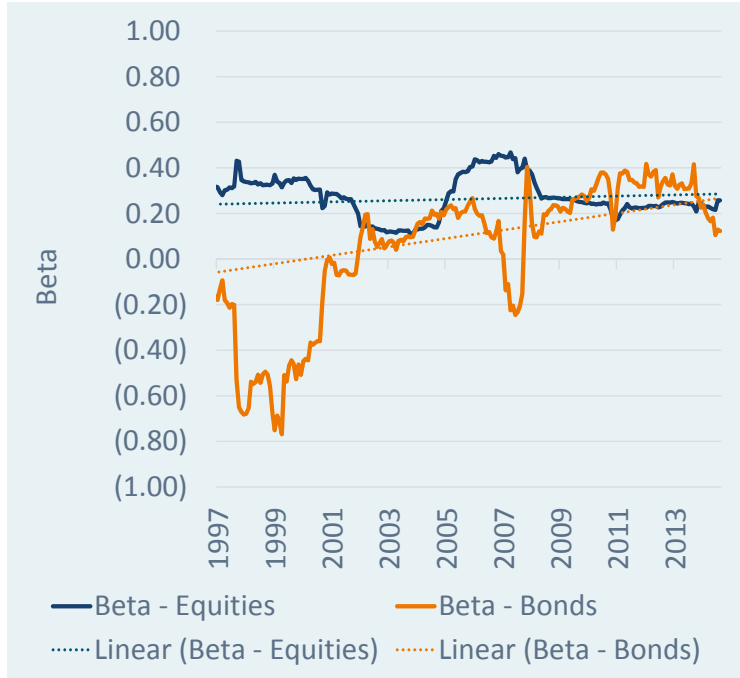


Source: Bloomberg, HFR, Barclays, MSCI, Verus. Equity returns represented by MSCI ACWI, while Bonds were represented by the Barclays Global Agg

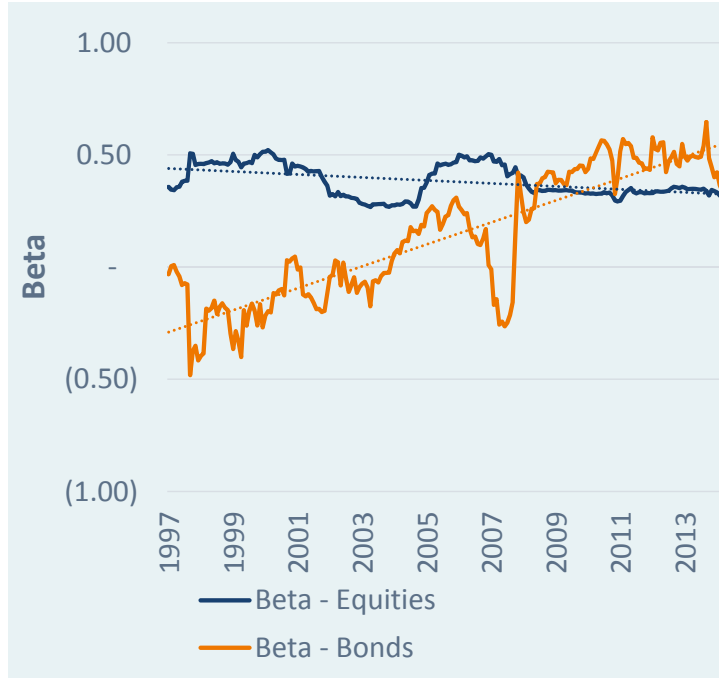
# Diminishing benefits?

Aggregate hedge fund beta versus stocks and bonds

HFRI FUND OF FUNDS COMPOSITE



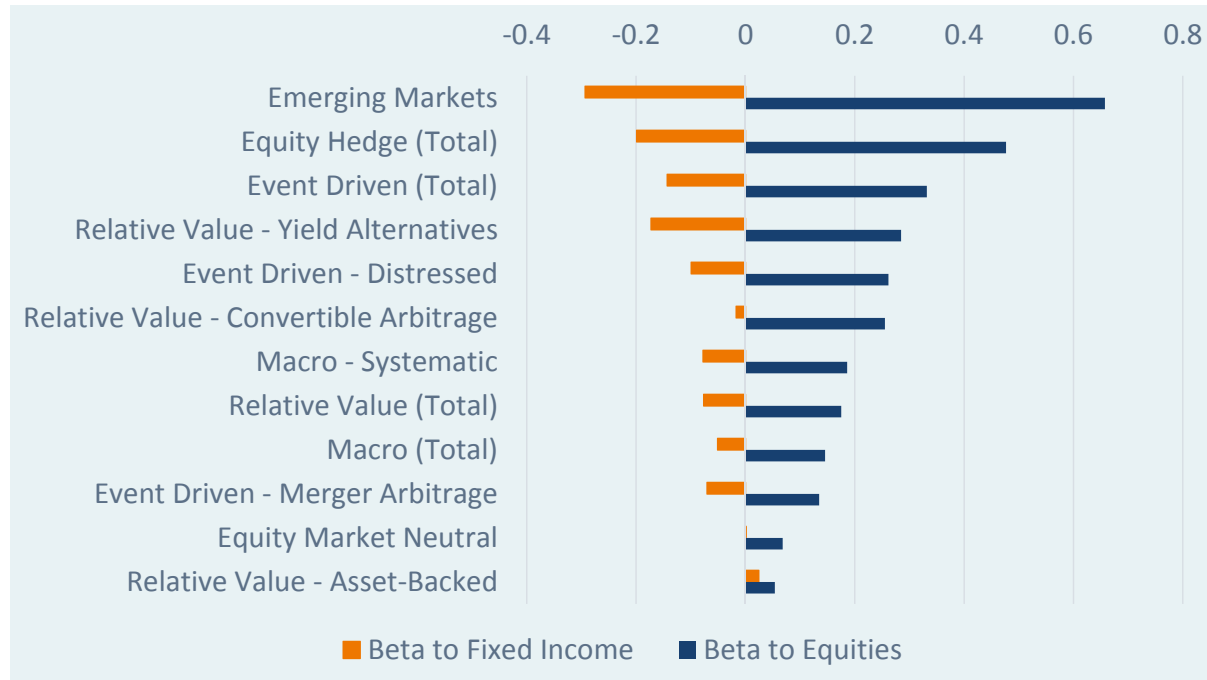
HFRI FUND WEIGHTED COMPOSITE



Source: Bloomberg, HFR, Barclays, MSCI, Verus. Equity returns represented by MSCI ACWI, while Bonds were represented by the Barclays Global Agg

# Disintegrating the aggregate

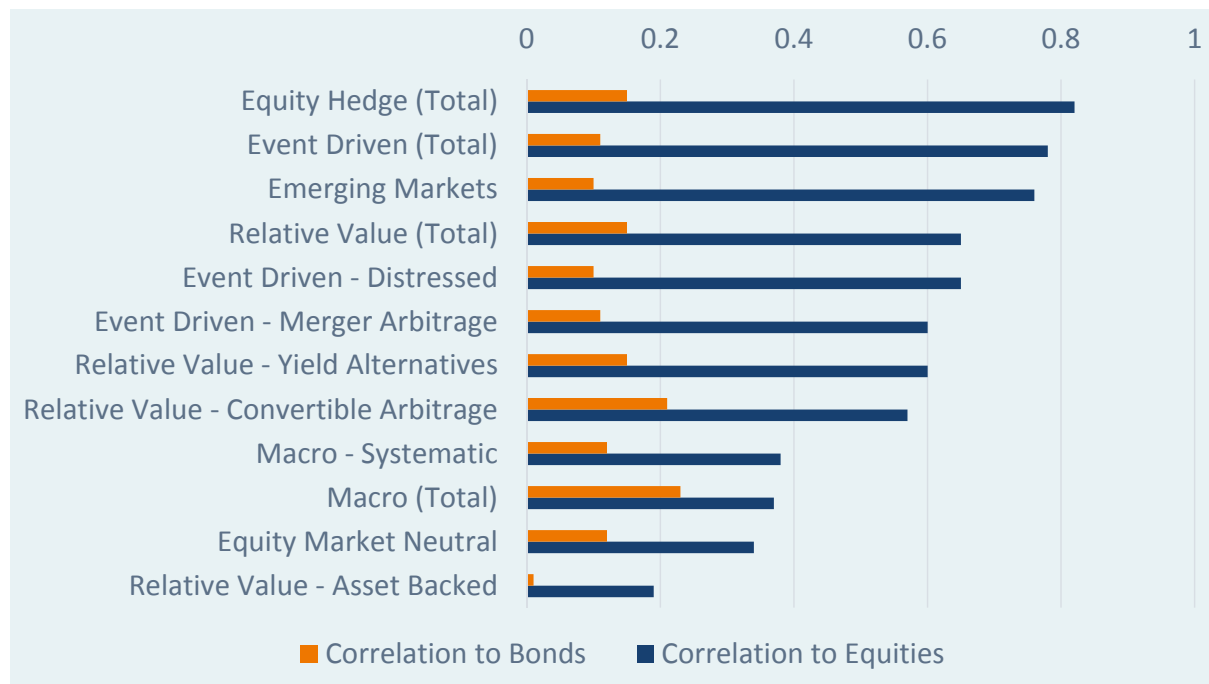
Benefits and diversification capacity vary by strategy



Source: Analysis uses MSCI ACWI and BC Global Agg. MSCI, Barclays, Bloomberg, HFRI, Verus. Data from January 1995 to June 2015.

# Disintegrating the aggregate

Benefits and diversification capacity vary by strategy

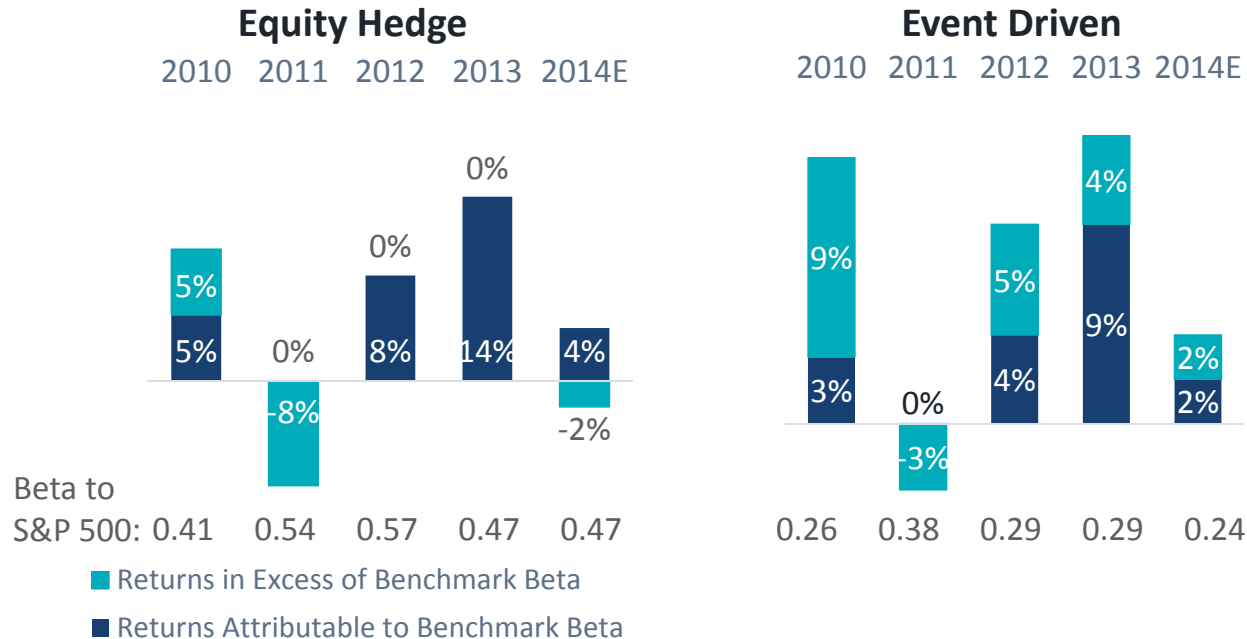


Source: Analysis uses MSCI ACWI and BC Global Agg. MSCI, Barclays, Bloomberg, HFRI, Verus. Data from January 1995 to June 2015.



# Adding alpha

Barclays Capital Solutions study based on HFR returns

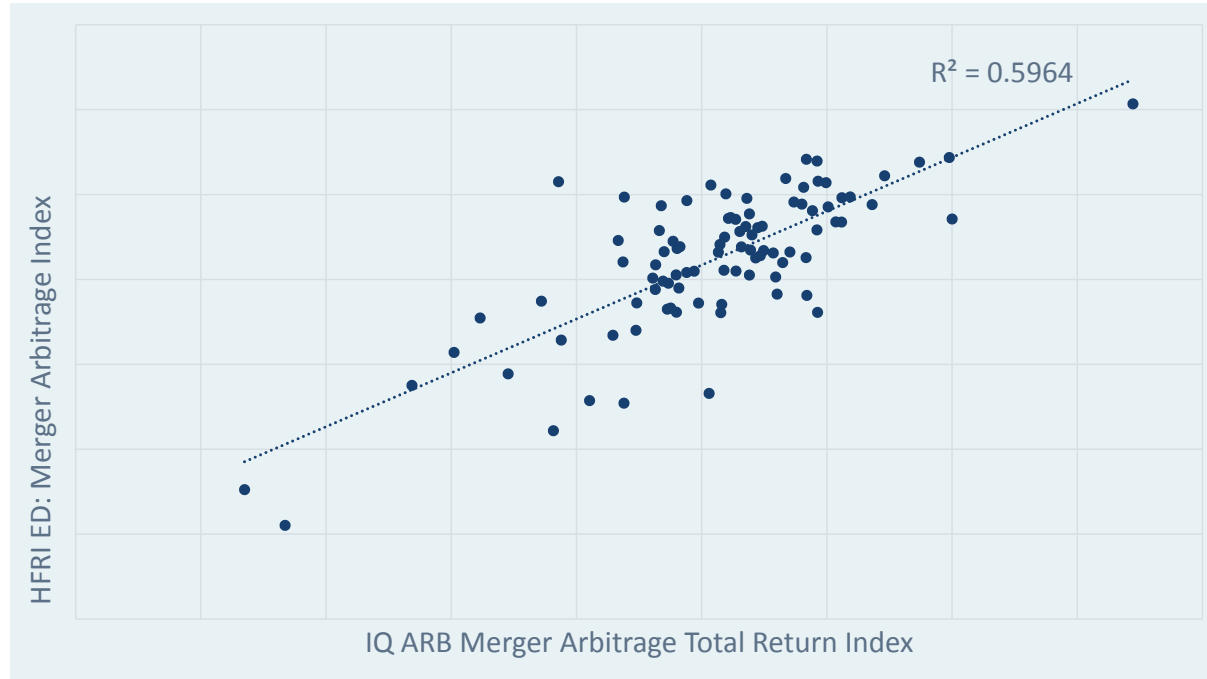


Source: Barclays Capital Solutions, January 2015 "What Lies Beneath: 2015 Global Hedge Fund Industry Trends and Allocation Outlook"

[http://www.barclayscommunications.com/CapSol\\_Publications/520593/WhatLiesBeneath\\_USL.pdf](http://www.barclayscommunications.com/CapSol_Publications/520593/WhatLiesBeneath_USL.pdf)

























# Hedge fund “beta”




Certain strategies rely on premia that are widely documented and understood...



Source: HFR, IndexIQ, Bloomberg, Verus

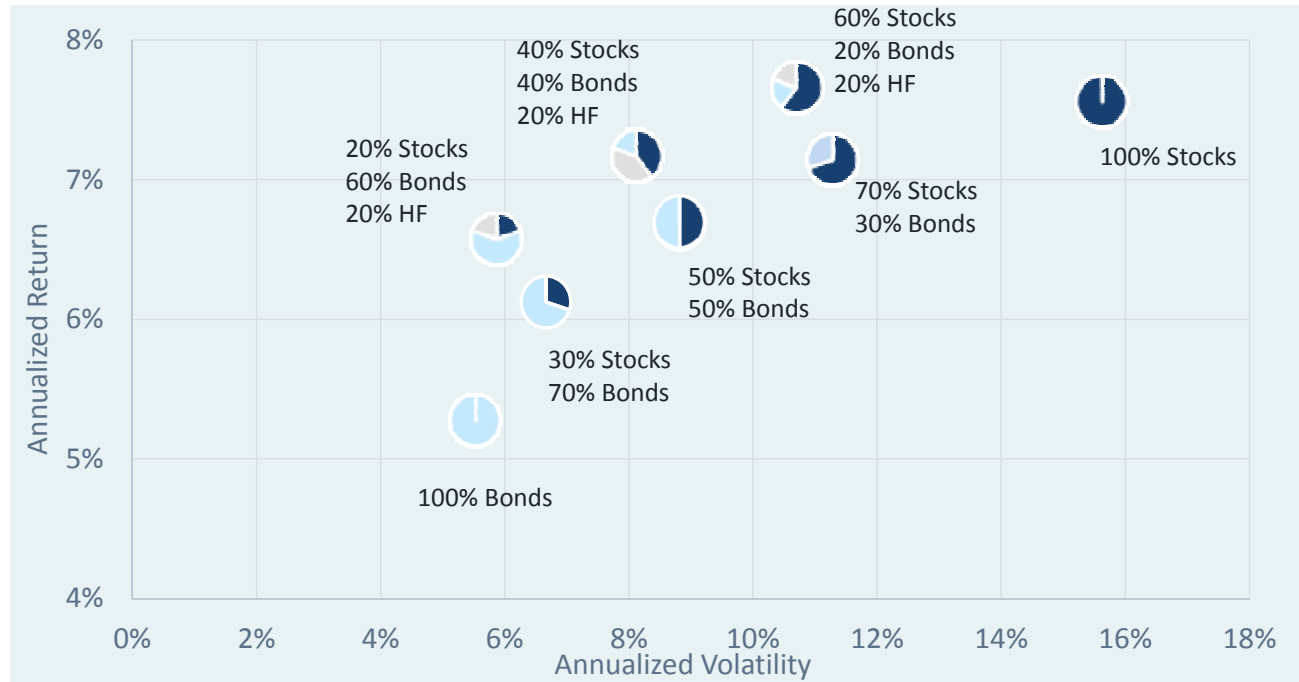
# Finding alpha... and finding impact

	Strategy	Return-Enhancing	Risk Reduction	New Risk Factors (Diversification)
Equity Strategies	Long-Short Equity			
	Market Neutral			
	Short-Biased			
Macro Strategies	Global Macro			
	Managed Futures			
Arbitrage Strategies	Event Driven			
	Convertible Arbitrage			
	Fixed Income Arbitrage			

 High Impact  
  Moderate Impact  
  Low Impact

# The impact of hedge funds

Historical risk and return (1995-2015)



Source: Bloomberg, Barclays, MSCI, HFR, JP Morgan. Data from January 1995 to June 2015.

# Seeking alpha: FOF or direct?

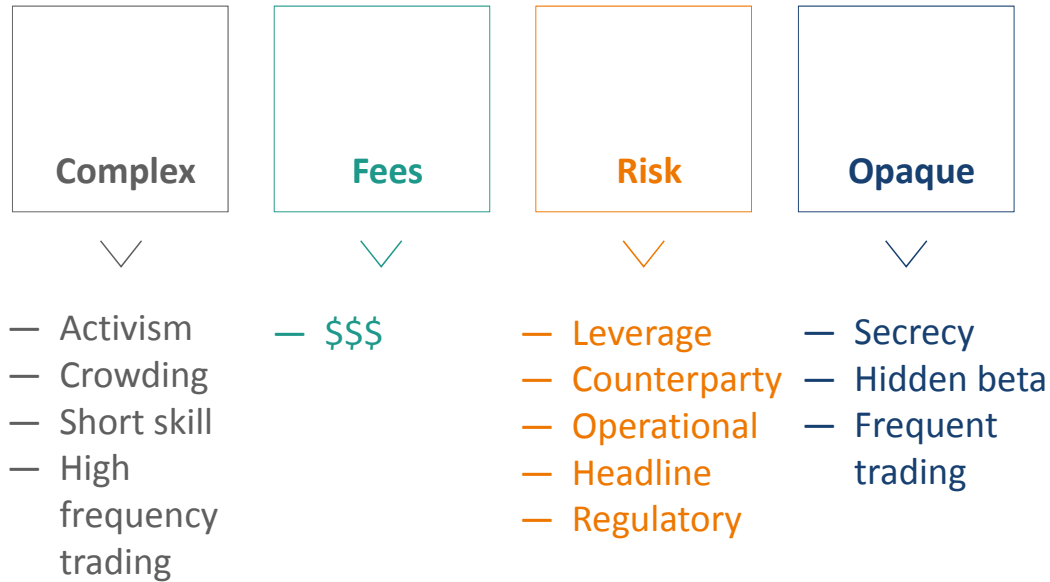
As much a governance decision as cost decision

Key considerations include:

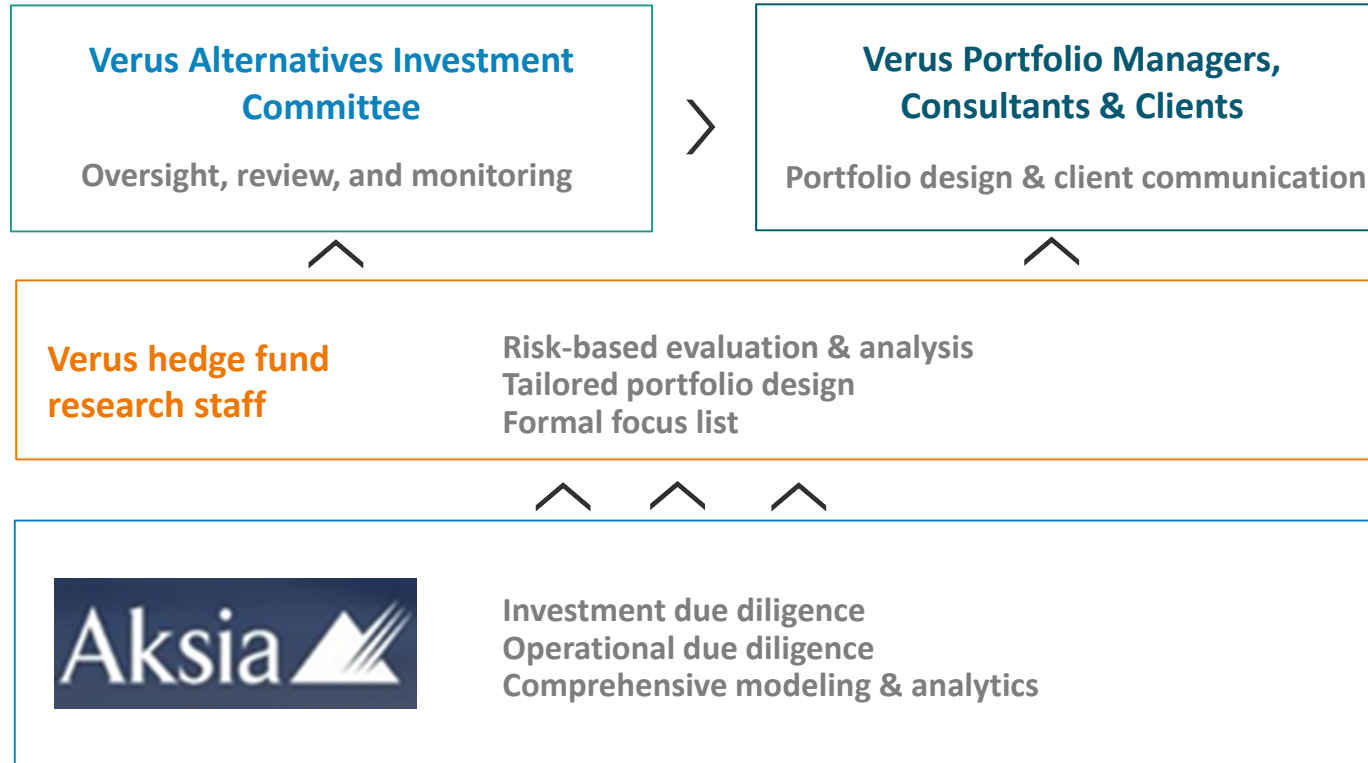
1. Unbiased top-down expertise for designing portfolio strategy
2. Bottom-up expertise for evaluating and selecting managers
3. Independent expertise for evaluation of operational risks of managers
4. Administrative bandwidth for portfolio implementation and maintenance



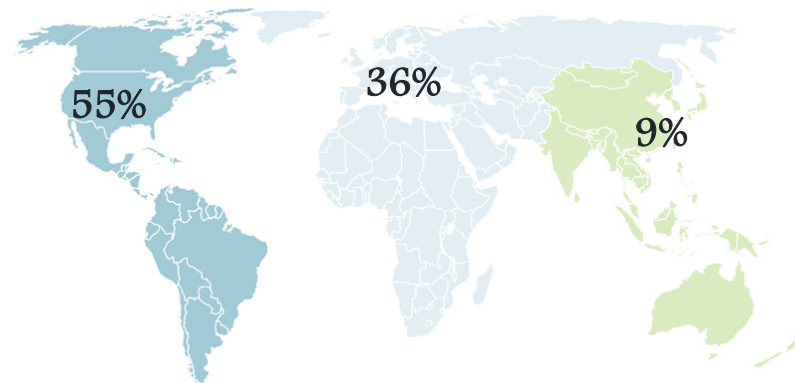
# Hedge funds are not without challenges



# Verus hedge fund solution



# Aksia professionals



Total Staff	95
Research Staff	57
Average Assets Under Advisory Committed to Hedge Funds:	\$1,280* mm
Total Clients : Total Staff	.7 : 1
Monitored Funds : Operational Due Diligence Staff	12 : 1
Monitored Funds : Investment Due Diligence Staff	8 : 1

\* Data as of August 2015. This includes advisory clients only and represents a conservative estimate of the assets our clients have committed to allocating to hedge funds based on most recently available information. Number is not inclusive of clients who do not disclose hedge fund allocations to Aksia.

# Research coverage

	Insight Reports <sup>1</sup>	ODD <sup>2</sup>	IDD <sup>3</sup>	Monitored <sup>4</sup>
Long/Short Equity	188	393	206	82
Event Driven	169	165	121	65
Relative Value	137	173	104	54
Tactical Trading	76	180	123	50
Multi-Strategy	25	57	47	24
<b>Hedge Funds</b>	<b>595</b>	<b>968</b>	<b>601</b>	<b>275</b>

*\*Data as of August 2015*

*1. Figures represent investment programs on which an investment insight report has been completed.*

*2. Figures represent investment programs on which operational due diligence has been performed. Both onshore and offshore funds of the same program count as one.*

*3. Figures represent investment programs on which investment due diligence has been performed. Both onshore and offshore funds of the same program count as one.*

*4. Figures shown represent total number of investment programs on which we perform ongoing monitoring. Both onshore and offshore funds of the same program count as one.*

# Investment due diligence

## Strategy

- History & background
- Investment strategy overview
- Investment risks
- Capital allocation
- Research / inv. process
- Firm and fund structure

## Team & Structure

- Key staff and dependencies
- Staff turnover
- Compensation structure
- Alignment of interests
- Firm ownership structure

## Risk

- Risk management philosophy
- Risk management team
- Asset liability / mismatch
- Risk exposure, leverage and financing
- Quantitative risk analysis





# Operational due diligence

## Infrastructure & Operational Process

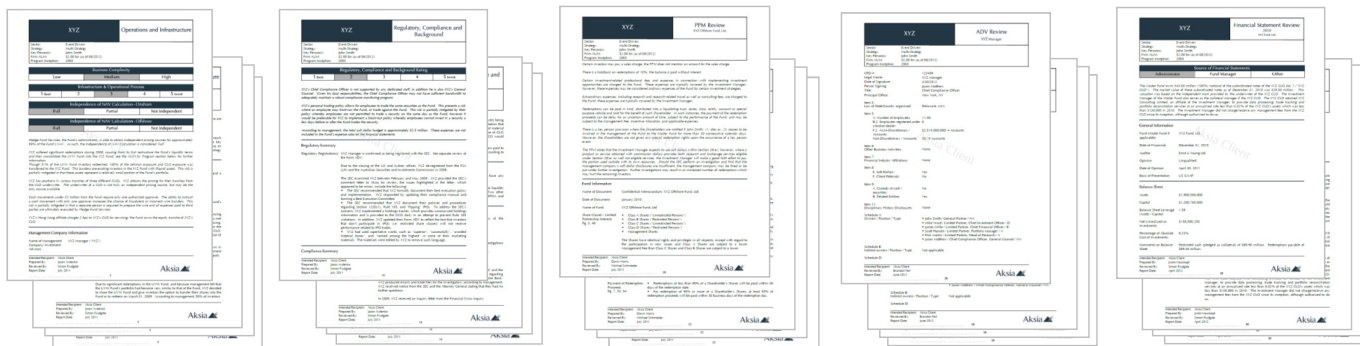
- Competence of key staff
- Counterparty relationships
- Independence of NAV
- Review of trading systems
- Cash management process

## Regulatory, Compliance & Background

- Regulatory registrations
- Compliance culture & approach
- History of examinations by regulator(s)
- Background checks on key employees
- Historical violations
- Conflicts of interest

## Document Review

- Specialist review of:
- Financial statements
  - Offering Memo
  - Form ADV



# Risk framework

Risk Exposures

Risk / Return Profile

Risk-Based Position Sizing

Public Holdings

Alpha Analysis

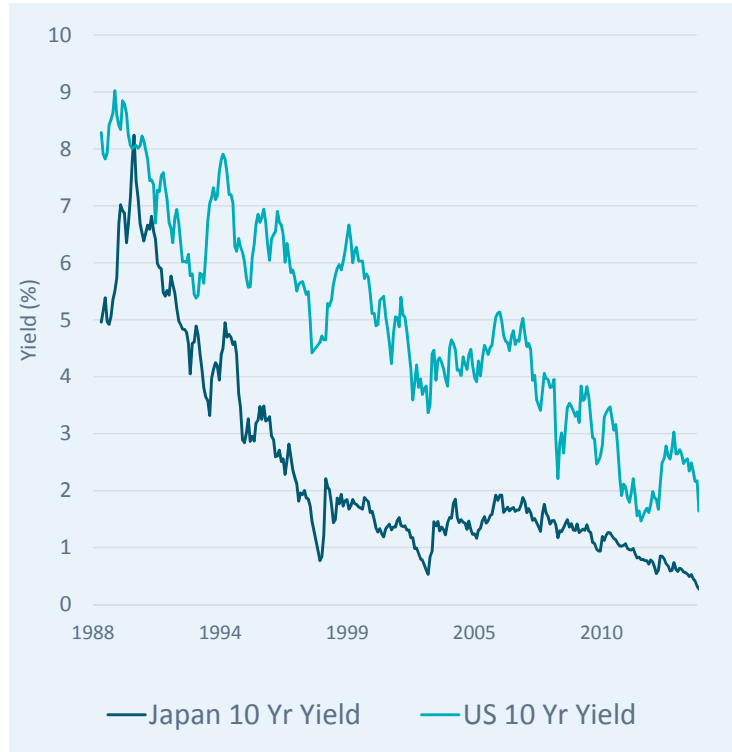
Factor Replication

Liquidity Mapping

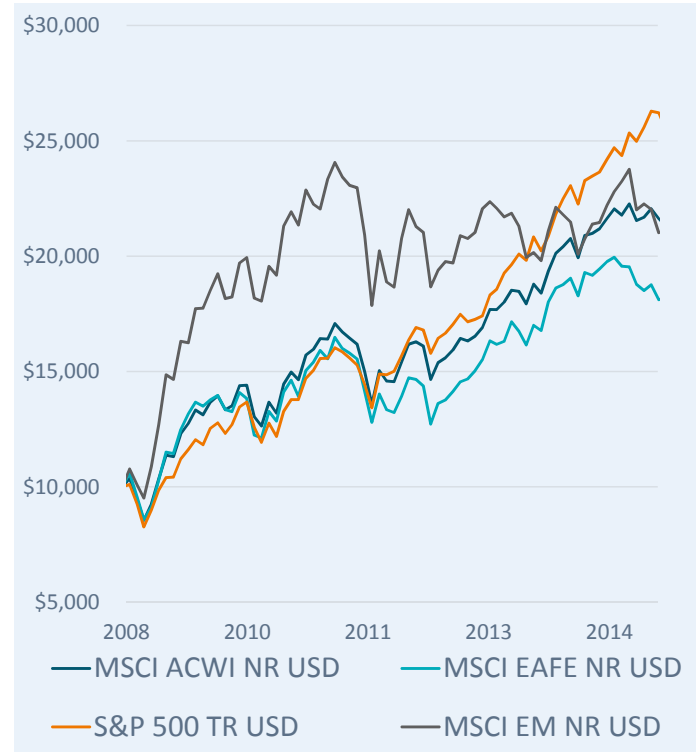
Active Management Attribution



# Why we favor hedge funds today



Sources: Bloomberg, MSCI, Standard & Poors



End of the 30-year  
bull market in  
bonds?

Cresting of six-  
year bull market  
in equities?



























# Questions?



# Thank you



# Every asset class has a role

	RETURN ROLES				DIVERSIFICATION & VOLATILITY ROLES		
	Benefit from GDP Growth	Earn Risk Premium	Produce Stable Income	Hedge Against Inflation	Low Absolute Volatility	Low Corr. To Other Assets	Reduce Portfolio Volatility
Public Equities							
Fixed (Credit)							
Hedge Funds <i>(Perceived role)</i>							
MAGNITUDE	 High	 Med-High	 Medium	 Low	 None		