

## Performance Update

<b>Fund of Hedge Funds Indices</b>	Dec	Nov	YTD	2005	2004	2003
EDHEC Fund of Funds Index	1.72%	1.85%	11.21%	6.80%	7.07%	11.46%
HFRI FoHF Composite Index	1.72%	1.87%	10.35%	7.49%	6.86%	11.61%
CISDM Fund of Funds Index	-	1.61%	7.45%	6.47%	7.12%	10.23%
InvestHedge Composite	-	1.54%	6.98%	7.07%	6.15%	9.34%
Altvest Sub-Index: Fund of Funds	1.75%	2.11%	10.30%	7.68%	7.39%	11.12%
Eurekahedge Fund of Funds Index	1.80%	1.75%	9.98%	7.72%	6.84%	11.61%
Barclay/Global HedgeSource FoF Index	1.79%	1.65%	9.43%	6.91%	6.65%	10.44%
<b>Average FoHF Indices</b>	<b>1.76%</b>	<b>1.77%</b>	<b>9.39%</b>	<b>7.16%</b>	<b>6.87%</b>	<b>10.83%</b>

<b>Investable Hedge Funds Indices</b>	Dec	Nov	YTD	2005	2004	2003
CS/Tremont Investable HF Index	1.71%	1.13%	9.51%	3.61%	5.31%	11.04%
MSCI Hedge Fund Invest Index	1.19%	1.28%	7.63%	4.68%	3.10%	14.70%
HFRX Global Hedge Fund Index	1.58%	1.54%	9.26%	2.72%	2.69%	13.39%
FTSE Hedge Index	1.24%	0.56%	6.08%	2.60%	3.12%	12.36%
<b>Average Investable HF Indices</b>	<b>1.43%</b>	<b>1.13%</b>	<b>8.12%</b>	<b>3.40%</b>	<b>3.56%</b>	<b>12.87%</b>

Numbers prior to the date of inception of the Investable Indices are pro forma. Fees may not be included.

<b>Fund of Funds of Hedge Funds</b>	Dec	Nov	YTD	2005	2004	2003
PrimFund Diversified (net of fees)	1.54%	1.73%	9.43%	7.78%	8.39%	13.68%
PrimFund Growth (net of fees)	2.11%	2.99%	13.73%	9.38%	15.69%	20.75%
PrimFund Opportunity (net of fees)	2.13%	3.04%	21.49%	17.02%	17.13%	25.09%

Inception of PrimFund Diversified was July 2004, of PrimFund Growth April 2005, of PrimFund Opportunity September 2006. The simulated data prior reflects the net performance of a weighted composite of the targeted fund managers net of fees. All numbers shown are for illustration purposes only and are no guarantee of future performance.

## Industry News

### Hedge funds attract record inflows in 2006

**HFR**

According to data released by Hedge Fund Research (HFR), the hedge fund industry attracted a record \$126.5 billion in new money in 2006, helping to swell total assets under management to a record \$1.43 trillion, a 29 percent increase from year end 2005. The strong fund flows represent a dramatic rebound from 2005's relatively subdued pace of \$46.9 billion, which at the time was the smallest flow since 2001. Notably, the \$15.8 billion inflow in the fourth quarter was significantly below the pace set in the first three quarters of the year.

The HFRI Fund Weighted Composite Index returned 5.4 percent in the fourth quarter and 12.85 percent for all of 2006, the best annual result since 19.55 percent in 2003. As it has for the second consecutive year (and three out of the last four years) the HFRI Emerging Markets Index led the industry in performance, adding 10.7 percent in fourth quarter to return 24.3 percent on the year. M&A dependent strategies such as Event Driven and Merger Arbitrage increased by 15.3 percent and 15.7 percent respectively. Short Selling was the only strategy to see negative returns for both the quarter and the year, losing 1.64 percent in the fourth quarter and 1.47 percent for the year.

Funds of funds saw net new flows of \$3.89 billion in the fourth quarter, marking the fourth straight positive quarter for funds of funds after two consecutive quarters of outflows to end 2005. For the year, funds of funds brought in \$49.7 billion in net new assets compared to \$9.5 billion in 2005 and \$33 billion in 2004. Globally, there is \$547 billion invested in funds of funds. Fund of fund performance was up 5.36 percent in the fourth quarter, and 10.35 percent for the year.

### Fund of funds managers fear new correction

Fund of funds managers remain wary of another bumpy year for global equities. The latest Citywire fund of funds survey shows managers are generally divided on whether North America is the place to be, even though all managers are united in their belief that the dollar will continue to fall next year. The majority of managers are also unsure of whether they can outperform next year and a large majority believe a severe correction may be on the way.

### **US hedges to be hit with first net outflows ever**

Hedges focused on U.S. markets will see net redemptions for the first time ever in 2007 as investors shift money to emerging-markets managers, especially traders specializing in China, according to an annual survey of the \$1.4 trillion industry by Deutsche Bank. U.S. focused funds are likely to see outflows of 8% this year, while managers specializing in China could experience a 39% jump, Deutsche Bank found in a poll of investors with more than \$900 billion in hedge funds. Other emerging-markets managers focused on other parts of Asia and Latin America could also see inflows of at least 13% in 2007.

Highlights of Deutsche Bank's Fifth Annual Alternative Investment Survey: 1) Investors rank the best performing investment strategies for 2007 - 18% rank long/short equity as the top performing strategy, 13% rank macro and 12% rank event-driven/relative value strategies as top performers. 2) Some strategies will see a dramatic growth of assets, such as merger arbitrage, which is predicted to have a 20% increase in assets based on portfolio rebalancing. Others, such as credit arbitrage, will see outflows of as much as 13% of current assets. 3) According to investors, hedge funds that invest in China are going to see a huge jump in assets; Deutsche Bank predicts inflows of more than 38% of current investment levels to these funds. 4) Emerging Asia is predicted to be the top performing region for the second year in a row. Pensions, government organizations, endowments and foundations are particularly interested in this region, with more than half of these respondents indicating that they will increase their exposure to the region. 5) During 2006, the number of investors willing to accept longer lock-ups surged. More than half are willing to accept a lock-up of two years or more, a figure that has more than doubled since 2005. 6) Investors are not enthusiastic about hedge funds adding private equity components to their traditional hedge fund offerings; 39% of investors feel that it is a bad idea for hedge funds to make private equity investments.

### **Deutsche Bank**

### **Richest Americans reduce exposure to hedge funds**

The very richest Americans have soured somewhat on hedge funds. Households with a net worth of \$25 million or more, not including primary residence, reduced their exposure to hedge funds significantly in 2006. Just 27% of those households owned hedge funds last year, down from 38% in 2005, according to a new Spectrem Group report. That represents a decline of 29% in a year that brought some well-publicized challenges for the industry. The Ultra High Net Worth segment as a whole, representing households with a net worth of \$5 million or more, saw total hedge fund exposure fall to 14% in 2006 from 17% in 2005. The decline was most prevalent among the wealthiest subset of this group, the \$25 million-plus households.

### **Spectrem Group**

## **Advisor/People News**

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### **UBP appoints Head of Alternative Investment Research for Europe and Asia**

UBP announced the appointment of Gideon Nieuwoudt as Head of Alternative Investment Research for Europe and Asia, and Deputy Head of Alternative Investment Research. Gideon Nieuwoudt will join Union Bancaire Privée London in April. He was formerly Senior Investment Consultant with the investment consulting firm Watson Wyatt, where he had been employed since 2000, first in London and then New York. In that capacity he has advised numerous institutional clients on the definition and implementation of their absolute return investment strategies, mainly in the field of hedge funds.

### **South West Capital Partners team joins Gottex**

Gottex Fund Management purchased South West Capital Partners and the team, led by Francis Campeau. The team, which includes Muri Rhee, Arnaud Massenet, Peter Foley CFA, Tomasz Szuka and Richard Kooi will focus on asset based strategies. Francis Campeau joins Gottex as a Managing Director, reporting to J.P. Bailey, Senior Investment Partner.

### **EFG International to buy PRS Group for undisclosed sum**

EFG International announced that it has reached an agreement to acquire PRS Group from its main founder. PRS Group currently manages approximately US\$ 2.5 billion in high net worth clients' assets, which are primarily invested in proprietary funds and proprietary funds of hedge funds.

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### **Proctor Acquires Minority Stake in Circle T Explorer**

Proctor Investment Managers LLC, which makes private equity investments in, and provides sales and marketing expertise to, boutique investment managers, announced a strategic partnership with Circle T Explorer Asset Management LLC, a New York City-based fund of hedge funds firm which offers a specialized emerging managers strategy. Under the partnership agreement, Proctor has acquired a 24.9% minority equity interest in Circle T Explorer and has become its strategic sales and marketing partner. Circle T Explorer currently has approximately \$110 million in assets under management. As a result of the investment by Proctor, Circle T Explorer will now operate as an independent company.

### **Castlestone appoints new CEO**

Castlestone announced the appointment of Dennis Burger as Chief Executive Officer of Castlestone Management. Dennis previously held the position as Director of Distribution and Marketing for Old Mutual International. Dennis brings with him extensive experience of more than 20 years in the financial services industry covering life companies, asset management, distribution and marketing.

### **Collingham hires new portfolio manager**

Collingham Capital Management announced that Ameet Patel has joined the firm as a Portfolio Manager, bringing with him expertise in the equities space. Ameet previously worked at Lehman Brothers, as a sell-side equity research analyst covering stocks in a range of sectors over a five year period. Ameet qualified as a CFA in 2005, earned an MSc in Finance from the London Business School in 2001, a Diploma in Actuarial Science from City University in 1998, and a BSc in Mathematics and Management from Nottingham University in 1997.

## **Product News**

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### **Hedge fund of funds created by Old Mutual**

Old Mutual Asset Management started a hedge fund of funds that invests with new and small managers. Managed by OM subsidiary Larch Lane Advisors, the Old Mutual 2100 Emerging Managers Fund will make investments with hedge fund managers with less than USD400 million in assets under management and track records of less than three years.

### **Stillwater Capital Makes Ripples With New Offshore ABS Fund**

New York-based Stillwater Capital Partners launched The Stillwater ABS Fund, a Cayman Islands-domiciled fund of funds, with \$10 million in initial equity. The fund will invest in approximately 20 single-strategy managers all within the asset-backed securities space.

### **Parker Global launches investable Forex Index**

Parker Global Strategies (PGS), who have tracked FX managers since January 1986 in their widely published Parker FX Index, announced the launch of their first investable foreign exchange index -- PGS FX Alpha Edge. PGS FX Alpha Edge is designed to capture alpha available in the global currency markets, as well as to provide a return stream with low correlation to equity, fixed income, commodity markets and most hedge fund strategies.

## **Academic/Research**

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### **The Geography of Hedge Funds**

This paper analyzes the relationship between the risk-adjusted performance of hedge funds and their proximity to investments using data on Asian hedge funds. They find, relative to an augmented Fung and Hsieh (2004) factor model, that hedge funds with a physical presence (head or research office) in their investment region outperform other hedge funds by 5.28 percent per year. The local information advantage is pervasive across all major geographical regions and investment styles, but is strongest for Emerging Market and Event Driven funds. These results are robust to adjustments for fund fees, serial correlation, backfill bias, and incubation bias.

**Melvyn Teo**

**Conditional Performance of Hedge Funds: Evidence from Daily Returns**      **Li, Kazemi**

Using daily returns on a set of hedge fund indices, they study (i) the properties of the indices' conditional density functions, (ii) the presence of asymmetries in conditional correlations between hedge fund indices and other investments and between hedge indices themselves, and (iii) the presence of market timing skills in the indices. They use the SNP approach to obtain estimates of conditional densities of hedge fund returns and then proceed to examine their properties. In general, a nonparametric GARCH(1,1) model appears to provide the best fit for all strategies. They find that the conditional third and fourth moments are significantly affected by changes in the current volatility of returns on hedge fund indices. They also examine changes in the conditional probability of tail events and report significant changes in the probability of extreme events when the conditioning information changes. These results have important implications for models of hedge fund risk that rely on probability of tail events. They formally test for the presence of asymmetries in conditional correlations to determine if there is contagion between hedge funds and other investments and between various hedge fund indices in extreme down markets versus extreme up markets. They do not find strong evidence in support of asymmetric correlations between hedge funds and other investments, while They find evidence in support of asymmetric correlations between some hedge fund indices. Finally, they find strong evidence supporting the presence of market timing skills in these indices. However, they argue that our findings are more likely to be because of long-volatility positions held by the managers rather than because of their market timing abilities. Further, they claim that the presence of option-type returns as explanatory variables are not likely to correct for this problem. They use market timing results concerning returns on a simulated portfolio to support this conclusion.

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