

Performance Update

Fund of Hedge Funds Indices	Sept	Aug	YTD	2004	2003	2002
EDHEC Fund of Funds Index	1.59%	0.79%	4.83%	7.07%	11.46%	1.25%
HFRI FoHF Composite Index	1.42%	0.84%	5.05%	6.86%	11.61%	1.02%
CISDM FoHF Diversified Median	1.11%	0.76%	4.78%	7.52%	10.04%	0.65%
CISDM FoHF Niche Median	-	0.72%	4.11%	8.33%	10.62%	1.99%
InvestHedge Composite	-	0.79%	3.63%	6.12%	9.28%	1.99%
Altvest Sub-Index: Fund of Funds	1.48%	0.80%	5.45%	7.39%	11.12%	1.23%
Eurekahedge Fund of Funds Index	1.49%	0.80%	5.02%	6.62%	11.49%	2.09%
Barclay/Global HedgeSource FoF Index	1.61%	0.84%	4.98%	6.61%	10.36%	1.79%

Investable Hedge Funds Indices	Sept	Aug	YTD	2004	2003	2002
CSFB/Tremont Investable HF Index	1.21%	0.52%	2.92%	5.31%	11.04%	5.67%
MSCI Hedge Fund Invest Index	1.15%	0.41%	2.82%	3.10%	14.7%	5.30%
S&P Hedge Fund Index	0.97%	0.54%	2.54%	3.95%	11.12%	4.14%
HFRX Global Hedge Fund Index	1.11%	0.43%	1.42%	2.69%	13.39%	-
FTSE Hedge Index	0.75%	0.23%	1.26%	3.12%	12.36%	2.05%

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

Fund of Funds of Hedge Funds	Sept	Aug	YTD	2004	2003	2002
PrimFund Diversified	1.13%	0.47%	5.17%	8.39%	13.68%	-

Inception of the fund was July 1st 2004. The simulated data prior reflects the net performance of a weighted composite of the targeted fund managers

Industry News

Hedge fund assets swell 30% in a year

Investors have increased the amount of money in hedge funds by 30 percent in the past 12 months, to \$1.37 trillion as of the end of September, according to a survey of 44 fund administrators by Hedge Fund Manager Magazine.

The gain in assets was spread evenly across the world, with 58 percent of the money invested on behalf of U.S. clients, 24 percent for Europeans and 5 percent for Asian customers. The \$1.37 trillion figure applies to funds overseen by a single manager, the so-called single-strategy funds. Assets in funds of hedge funds, which invest in a range of single-strategy funds, rose 33 percent, to \$709 billion.

Assets pulled from fund of hedge funds

HFR

Investors pulled more than \$1bn from funds of hedge funds in the third quarter, according to Hedge Fund Research. This compares to inflows of \$3.5bn in the second quarter and \$6.2bn a year ago. And inflows to hedge funds themselves are the lowest for more than a year. And HFR said that new flows to hedge funds slowed to \$9.4bn in the quarter – down from \$10.9bn in the second quarter and \$16.9bn a year ago.

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European schemes shun hedge funds

European pension funds have not followed through on expectations that they would increase their use of hedge funds and private equity, according to new research from Greenwich Associates. "Many institutions have been talking quite forcefully about venturing further into these asset classes, but in practice most have continued to dabble," the firm said. It said allocations to hedge funds and private equity have remained flat at about 1% of assets for each of the past three years.

Restrict access to hedge funds, eliminate FoFs: David Swensen's suggestions draw ire

David Swensen, who as Yale University's chief investment officer has made ample use of hedge funds over the years, aroused ire by suggesting investor access to hedge funds should be further restricted to prevent more industry-damaging blow ups.

Swensen, a well-known industry figure has been credited with stellar returns at Yale's \$14 billion investment portfolio, said in a New York Times column that regulators should "prohibit unsophisticated players from participating in hedge funds." Swensen also called for the elimination of fund of hedge funds

Advisor/People News

Ibbotson leader joins Azimuth Trust

Ibbotson hedge fund head Ezra Zask has joined Azimuth Trust Co. He joined the New York company after installing a fund of hedge funds program at Ibbotson. Zask said his role at Azimuth Trust would focus on business development. Prior to Ibbotson, Zask founded his own CTA firm. He has also worked as a professor.

Fortis forges multi-manager arm for international push

Benelux investment giant Fortis is creating a new multi-manager funds powerhouse which will target the UK, the US and Asia. Fortis is combining all the existing multi-manager elements of its business, notably those of the MeesPierson private banking arm and the retail funds business of Fortis Investments. The new unit, Fortis Multi-Management, will start life in the New Year with combined assets of €6 billion. That total includes traditional long-only fund of funds, fund of hedge funds and fund of private equity funds. Products will be run by a 32-strong team.

Pilarski to leave Dow Jones Indices

Kevin Pilarski, director of alternative strategies and derivatives at Dow Jones Indexes, is planning to leave the firm on November 4th. Pilarski is a recognized expert and speaker on hedge fund indexing. Along with the Dow Jones Hedge Fund Index business, he was responsible for derivative revenues at Dow Jones and ran the credit default swap indexing business known as DJ CDX. His immediate plans are unknown.

PRS Group adds investment professional

PRS Group announced that Martin Loeser has joined the firm's alternative investment team as a Portfolio Manager. Prior to joining PRS, he was Senior Investment Analyst at Ivy Asset Management in New York. At Ivy, he was directly responsible for sourcing and selecting new equity managers, with a focus on emerging managers. Previously, he was a Vice President at The Mayfair Group and Senior Analyst at Tower Capital, conducting manager due diligence, risk management and portfolio management for each firm's fund of hedge funds program.

Andre du Plessis joins Watson Wyatt Investment Consulting

Andre du Plessis, the ex-chief executive of Coronation Fund Managers, is to join Watson Wyatt Investment Consulting as a senior investment consultant. Du Plessis, who has a background in fund management and investment banking, joins from Coronation Fund Managers (the institutional Funds of Hedge Funds business) where he was Chief Executive for the past three and a half years.

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Bucephale strengthens team

The Bucephale Group announced that it broadened its management structure with the additions of Robert Weir and Geoffroy Perret, who were named Senior Portfolio Managers, of Luc Deblue, elected Chief Financial Officer, and of Stefano Arcidiacono, in the position of Quantitative Analyst and Head of Information Technology.

Arden lands Ex-Deutsche ARS executive

Fund of funds firm Arden Asset Management hired Natalie A. Birrell as a managing director. She joins from Deutsche Bank, where she was managing director and chief operating officer for the firm's Absolute Return Strategies Group. ARS manages US\$10 billion, as does Arden.

At Deutsche Bank, Ms. Birrell was responsible for the day-to-day operations of the hedge fund group, including developing, implementing and managing products; strategic planning; fund administration and client service; technology; and risk management, according to a news release from Arden.

Product News

Clade launches the South African investable Hedge Fund Index

Clade Investment Management announced the launch of the South African Investable Hedge Fund Index (SAIHF) and a range of investable index products tied to this index. The SAIHF is the first product that allows investors to access this attractive investment class at a low cost and without incurring significant fund specific risk.

The SAIHF is a capital weighted index of South African hedge funds. It contains four strategy specific sub-indices: Fixed Income, Long/Short Equity, Market Neutral and Arbitrage Trading.

Pro-Hedge launches new multi-manager energy fund

Pro-Hedge Funds has launched its diversified Pro-Hedge Multi-Manager Energy Fund, the first such fund to be launched in Canada. Specializing in the North American Energy and Utility sectors, the fund is widely diversified in its strategies, sectors and security types, and is designed to take advantage of this top performing energy sector while significantly lowering portfolio volatility.

SGAM to open hedge fund range in U.K.

Societe Generale Asset Management is set to open its funds of hedge funds range in the U.K.. The range will include SG's three main global fund of hedge funds—an equity hedge fund of funds, a relative value fund of funds and a global macro fund of hedge-funds. These funds already have a five-year track record in the U.S.

HFR and Barclays Capital to launch dedicated Emerging Managers platform

HFR Asset Management announced the launch of the first ever Emerging Managers fund of hedge funds on a controlled infrastructure platform. The HFR Emerging Managers Fund will initially comprise 21 funds each with two years or less of tenure. Barclays Capital has an exclusive arrangement to offer structured products on the Fund which will be the first time principal protected notes have been issued on a dedicated Emerging Manager fund of funds.

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Academic/Research

Factor Modelling and Benchmarking of Hedge Funds: Are Passive Investments in Hedge Funds Possible?

L. Jaeger

The hedge fund industry is starting to recognize (however slowly) that a main part of its returns corresponds to risk premium rather than market inefficiencies, i.e. from "beta" instead of "alpha". This has some implication for the industry, among which the most striking is the endeavour to construct investable benchmarks for hedge funds on the basis of an analysis of the underlying systematic risk factors and a subsequent replication of the corresponding risk premium with generic trading systems. The question touches further on the sense and nonsense of the currently marketed investable versions of hedge fund indices. If possible, investable benchmarks constructed by a joint venture of financial engineers and quant groups based on risk factor analysis and replication offers a valid, theoretically more sound, and cheaper alternative to the currently offered hedge fund index products, especially as the latter reveal themselves more and more as questionable from a theoretical as well as practical standpoint. This article reflects on this most recent discussion within the global hedge fund industry about the "beta versus alpha" controversy, investable hedge fund indices, and finally capacity issues. It illustrates how the current research activities in the quant groups of the large investment banks and financial academic centres might turn the hedge fund industry upside down in coming years. This article offers a follow up discussion on the broader treatment on the subject in the author's book "Through the Alpha Smoke Screens: A Guide to Hedge Fund Return Sources".

The Benefits of Hedge Funds in Asset Liability Management

Martellini, Ziemann

This paper examines the benefits of including hedge funds for investors facing liability constraints. They cast the problem in a stochastic surplus optimisation setup where hedge funds are treated as a complement, and not as an addition, to traditional asset classes, which alleviates the concern over ex-ante modelling of hedge fund returns, a notoriously difficult challenge given the short history and complexity of these alternative investment styles. Their conclusion is that, when added to bonds and stocks, suitably designed portfolios of hedge funds can allow for significant benefits in an ALM context, as can be measured in terms of reduction of the expected mismatch between assets and liabilities. This impact is more pronounced when the relevant objective turns to extreme risks. In fact, they show that the probability of extreme deficits (value of the assets falling below 75% of the value of liabilities) can be reduced by as much as 50% by allocating not more than 20% to hedge funds.

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