Hedge funds reach out to advisors to improve reputation

Techniques range from trips and financial incentives to sharing information

Monday, November 12, 2007

By Rosemary McCracken

In an effort to buck a reputation as the black hats of the investment world, hedge funds are using everything from money incentives to manager access to win advisors' business.

One obvious way to grab advisors' attention is to get them in front of the funds' managers. Toronto-based **Robson Capital Management Inc.** , for example, sets up visits to the offices of its funds' portfolio managers in New York and Miami. **Man Investments Canada Corp.** , also of Toronto, arranges due-diligence trips for advisors to Chicago, which is the North American head office of its British parent, Man Group PLC.

According to the funds, these visits are far from easygoing junkets. Man Canada's CEO, Toreigh Stuart, calls the trips "intense, 12-hour days" that revolve around meetings with managers, both in person and via video conferences with its other centres.

And these trips aren't offered as freebies; advisors pay their own costs. "We chalk them up to continuing education or due-diligence expenses," says an advisor in Toronto. "And that's how it should be. A firm that offers to pay is showing desperation. I wouldn't go near it."

For Christopher Kruczynski, an advisor and partner with **Mar-chand-Kruczynski Group**, an investment-management group in St. Catharines, Ont., affiliated with ScotiaMcLeod Inc., meeting with a hedge fund's managers is a prerequisite to buying into it.

"My upbringing in the industry has been to meet with managers to get a feeling for how they are doing business," Kruczynski says. "My preference is a due-diligence visit on-site to discuss their strategies and the guidelines they follow. A lot of them will show you their positions on a given day. I appreciate that it might not be the same position the next day, but it gives me an idea."

Jim McGovern, CEO and managing partner at **Arrow Hedge Partners Inc**. in Toronto, admits not all hedge fund managers are willing to discuss what they are buying and selling. "On the other hand, advisors can take comfort from the fact that [the fund manager] keeps reviewing every position in the portfolio," he says, "and we're happy to show the underlying risks."

Kruczynski isn't afraid to pepper the managers with questions, and he wants to know the portfolio manager's track record. "I like to see a manager who's been through a full market cycle," he explains. "You're seeing a lot of managers who have left the big shops for the boutiques — usually because they weren't allowed the scope they wanted. I like them to put in the time they need at the new firm to develop their strategies."

He also wants to know how much of the manager's own money is in the funds.

Indeed, while face time with managers and exhaustive due diligence are important, money talks, too. Most hedge funds charge investors a 20% performance fee on profits generated beyond a certain benchmark. Many hedge fund companies — but not all of them — allow advisors to share in the fund's performance by giving them part of the performance fee.

"The advisor's performance fee is usually about 10%," Kruczynski says. "This is an additional incentive for advisors to do due diligence on a hedge fund. Your compensation is aligned to it, whereas you can recommend a great or a not-so-great mutual fund and receive the same trailer."

Not only do the trips, lunch and dinner presentations, symposiums and cross-country road shows give advisors a chance to learn about hedge fund managers' strategies, the funds also use them to cement ties with advisors through personalized relationship-building, similar to what advisors are doing with their own clients.

“Our relationships with advisors are an inch wide and a mile deep,” says Chris Fontana, director of sales at **Front Street Capital Corp.** in Toronto. “Few of them use us. But those who do, use us a lot.”

“It’s continuous outreach,” adds James Fox, director and vice president of sales and marketing at **Sprott Asset Management Inc.** in Toronto. Sprott just completed a fall road show that brought managers out to meet advisors in Victoria, Vancouver, Calgary, Edmonton, Toronto, Ottawa and Montreal. Until Sprott hits the road again in the spring, it will keep up contact with advisors through monthly e-newsletters, quarterly updates and market commentary from its managers on its Web site.

Although hosting advisors at managers’ offices is one approach, some hedge funds prefer house calls — allowing them to meet with advisors and their clients on their own turf. Toronto-based **J.C. Clark Ltd.** doesn’t offer due-diligence trips but instead sends its reps on the road to meet advisors. “We’re travelling a lot, bouncing in and out of advisors’ offices,” says Sean Wynn, director of marketing at J.C. Clark. “We focus on what advisors are doing. Do they have hedge fund exposure? And if so, what is their weighting? We run the market correlation numbers. If the market is up, we tell them we’re not necessarily going to go up with it. Or is their exposure limited to principal-protected notes?

“We’re also talking to the people running hospital endowment funds about how hedge funds can smooth out the edges in times of market volatility — when they still have the obligations to meet,” he adds.

Quadrexx Asset Management Inc. of Toronto is another firm that makes house calls — and these days, that usually means heading west. “We normally go to the advisors’ offices with presentations we have tailored to their individual businesses,” says Miklos Nagy, CEO of Quadrexx. “Of course, these are the advisors who want to listen to us.”

Nagy finds hedge funds a hard sell to advisors in Ontario, largely because of sophisticated inves-tor rules. In Ontario, investors must have $150,000 to invest in a fund or be an “accredited investor” with $1 million in financial assets or annual income of $200,000 for the past three years (or $300,000 in annual household income). But in Alberta, Saskatchewan and Manitoba, individuals with annual incomes of $75,000 or $400,000 in net assets are considered eligible investors.

“Advisors and investors in Al-berta, in particular, are also open to new ideas, new products,” Nagy says. “There’s lots of new money in the province and investors don’t have preconceived investment ideas, because in the past they may not have had much money to invest.” Quadrexx does about 40% of its business in Alberta, he adds. **IE**