

Investment Monitor

Summer/Autumn 2004

www.peritus.co.uk

Welcome



Welcome to the latest edition of the Peritus Newsletter intended for our Trust and Private Clients around the world.

James Day

Krug to be won

We will shortly be launching a customer survey. All respondents will be entered into a draw where two winners will receive a bottle of Krug champagne. We of course respect your time and privacy and will keep the survey short but equally, if you do not wish to participate please let us know.

Charity - Budding photographers required!

Christmas may seem a long way away but we are already looking for a festive snow filled image and if any of you budding digital photographers have some high quality scenes, we would be delighted to see them. We would be happy to pay £200 to you or a charity of your choice and of course give full plaudits to you on the card itself.

E-Mail delivery

If you would prefer to receive our newsletter by e-mail, please let us know at james.day@peritus.co.uk. Equally, if you know of other people who would like to receive a copy, we would be glad to hear.

Breaking News

Peritus have now moved to larger premises. For our new contact details please see below.

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MULTI MANAGER HEDGE FUNDS - MASSIVE FUND DEMAND - IS THE BEST ALL OVER?

UK pension funds are now jumping on the bandwagon of hedge fund investment. Once again, it raises the question what their Consultants have been doing for the last 20 years but that aside, how will the hedge fund industry cope with the demand and what does it mean for investors?

Capacity for some managers has always been an issue. Most managers negotiate capacity for new funds when they first invest and it is essential to know what future capacity your multi style manager has to invest new funds without diluting performance.

One well known manager invests 50% of their client assets into new hedge funds. This ensures that they can grow but with what certainty of performance? Another, purchased an entire hedge fund company which included good and bad funds just to secure capacity.

Many Hedge Fund companies have developed the means to grow but what about their performance? If world class hedge fund managers are as rare as good equity managers, what happens to returns if these managers close their funds to new business because they are swamped with new money?

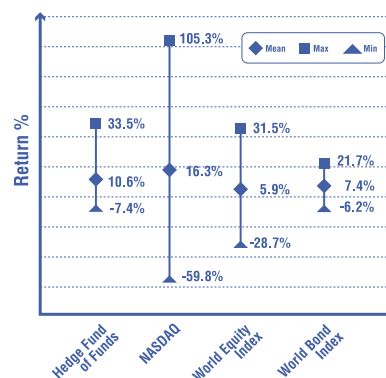
Like it or not, returns will diminish and risks will increase.

Many strategies such as Arbitrage are capacity constrained. Blending different strategies manages risk. Having access to fewer strategies results in less diversification and higher risk. In addition, as the demand for capacity increases, so good managers will be able to dictate terms often resulting in less due diligence and higher risks.

So risks will increase but why should returns fall for multi managers? The problem is not one of identifying good hedge managers but that the number of hedge managers or capacity needed to satisfy the very large flow of funds, forces managers to spread their assets to a sub optimal choice. The results are diluted by less good managers because of capacity issues.

Finally, fees at hedge fund level and multi manager level are rising and good managers know they can dictate terms. In rare cases, fees have risen from 2% for management with a performance fee of 20% of a certain defined gain to 3%-4% for management and performance fees of 40%! Similarly, the multi managers are aware that they are a rare breed as well and are raising or not negotiating their fees. The end result is higher fees with lower returns for the investor.

Performance - Hedge vs Bonds and Equities 1990 - 2002 rolling yearly returns



Are we worried? YES. Our analysis shows that it is very rare and difficult for Private Clients or Institutional Investors to truly know their multi managers. This means that there will be some unpleasant performance, fee or risk surprises which emphasises the importance of thorough manager research. ●

SHOULD TRAIL FEES BE ABOLISHED?

Why does the UK and Europe not have a champion of the masses in the form of Elliot Spitzer? Granted, there is surely a purpose behind his fervour but what would a European Investment Champion attack? The list is too long and will help pad future Peritus' Newsletters however one area, sensitive to us, are Mutual Fund and Investment Manager Trail Fees.

Peritus never receives retrocessions or any form of inducement. Every penny and cent offered to us is passed to our clients.

However, our concern is how do other clients know what trail fees are available and whether their Trustees have negotiated as good an investment relationship as the Trustee next

door? The result is that there is not enough transparency in the Investment industry and ultimately, the client loses out.

The sequence begins with the Investment Manager or Fund – Just like any industry, incentives can be offered to Investment Managers or Trustees to buy their product. Trustees use their purchasing power and market knowledge to secure better terms, which often results in wide differences in pricing for the same investment product. Clients therefore need to understand what the Trustee has negotiated on their behalf.

Trustees can therefore differentiate themselves by highlighting how they work in the interest

“It is not the strongest of the species that survive, nor the most intelligent, but the one most responsive to change.”

Charles Darwin

of clients by securing superior terms and thus reducing overall costs directly or indirectly to the account. We would like to see, very simplistically that each investment product should come with two transparent fee choices. A lower fee 'Institutional' offering and a higher 'Retail – Trail Fee' offering. Trustees could clearly secure the optimum terms and the result would be happier and more satisfied clients. ●

“Chance is always powerful. Let your hook always be cast; in the pool where you least expect it, there will be fish.” Ovid

ARE MANAGER AWARDS VALUELESS?

Every year, there are many Investment Manager or Mutual Fund awards ceremonies with prizes bestowed on the great and the good. The winners then place great effort in highlighting how prestigious their success has been in all their marketing efforts and sales staff promote their wares announcing that this award is further proof of their skills in managing money.

Many of you will know that we are quite cynical about the merit, value and reliability of awards and manager rankings. In many cases they purely look at past performance or fail to take into account the Investment Quality, process or soft aspects of a firm. Large companies which have marketing Dollars or many funds often win.

Last year, in seeking to further bring together the leading experts in the field, PAM (Private Asset Manager Awards) invited Peritus to join the judging panel for the annual PAM awards because of our strong focus on qualitative manager analysis and our wide ranging knowledge of consistent managers.

Since 2001, the awards have had a blend of Quantitative and Qualitative analysis whereby the judging panel use their expertise to focus not only on past performance but also on areas such as investment process, service and reporting.

It is our hope that by participating in this forum we can widen the universe of managers who participate and in time, create a more global perspective on suitable managers. This very much fits within our mission 'to enhance the investment experience clients have in the management of their wealth'. ●

ETHICAL AND PASSIONATE STAFF REQUIRED!

Your continued confidence in our approach means that having found new larger premises we are looking to recruit more staff. The staff we are looking for are like the Tortoises on the Seychelles, a rare and endangered species.

We are looking for free thinkers, not afraid to challenge the accepted investment and relationship wisdoms of old. These are the people who stand up for their clients and care passionately about results. These are the people who hark to the old days when putting your client first with good fair fees was what resulted in the success of the firm. Dilbert, Alex Masterley and Martin Lukes are painful but humorous reminders of the world we live in and which new recruits would wish to leave behind!

The salary will be fair but the rewards high. Equity and personal empowerment is the glue and honey we offer all staff. We are looking for two exceptional people to build our team.

- A Global Portfolio Manager Analyst who recognises the Herculean challenge of finding excellent managers. A keen forensic mind and a willingness to constantly challenge accepted thinking are essential.
- A Relationship Officer who is personable, has a thirst for knowledge and who appreciates that to earn the trust of up to 40 clients takes time, commitment and regular communication. ●

ARE YOUR INVESTMENT MANAGERS MOVING OFF COURSE?

Many Trustees and Private Clients have a good process for evaluating the past performance of their managers but may not have the time, skills or know-how to assess the suitability of a specific manager. Peritus Investment Consultancy provides one off reviews of investment managers.

Manager concerns arise when past performance, talk on the street or structural changes present doubts about the wider risks, particularly, when investing in less well known managers. Our reports assess the team, company, investment process, operational and compliance procedures as well as the philosophy and values of the company. ●