THE LONG VIEW

JOEL PRESS
says don't believe the hype

"DESPITE THE ABUNDANCE OF NAYSAYERS, I HAVE REASON TO BELIEVE THINGS AREN'T AS BAD AS SOME SUGGEST"

If you believe everything you read and hear about the hedge fund industry, it would seem the sector faces one of its most difficult years yet. The new year has been ushered in by articles bemoaning 2012 performance, accompanied by myriad commentators sounding off on how long investor "patience" will last. If you add in the Mathew Martoma case and the prospect of more SEC action against hedge funds, reasons to be hopeful recede further still. But despite the abundance of naysayers, I have reason to believe things aren't as bad as some suggest. Furthermore, 2013 looks set, in my view, to be an excellent year.

First, performance wasn't as bad as many are accusing. The average advance of around 6% recorded by Hedge Fund Research is not representative of an industry dominated by the biggest firms, who tend to harvest the best gains. The 20%-plus advances recorded by Dan Loeb, Ricky Sandler and Crispin Odey, sector heavyweights either side of the Atlantic, show that the big names can still deliver. And these industry indices don't factor in volatility, capital preservation and risk, which are additional key concerns for investors.

Inflows will continue to be strong. Despite perceptions of a mixed last five years, investors have continued to increase their allocations to the hedge fund industry and that won't change in 2013. For many pension funds, hedge fund investments offer more stable and consistent returns than equity markets.

The start-up scene will be strong in the US, where interesting seeding opportunities have developed, but less so in Europe. The instability stemming from the sovereign debt crisis has made for a tough asset-raising environment and we are years away from a robust start-up market there. But in both the US and Europe, talent is going to be an interesting issue this year as waves of high-calibre professionals depart a shrinking banking sector in search of hedge fund opportunities. Hedge funds are going to be able to cherry-pick the best for themselves. The flipside is that many talented individuals could be left sidelined, with the sector absorbing only those it truly wants.

Mergers and acquisitions will continue in high volume among venders to the hedge fund industry as these businesses build ever more sophisticated businesses through partnering with rivals. While smaller admins are perennial takeover targets for their larger cousins. Do not be surprised if we see more deals among the top ten – the GlobeOp/SS&C and Goldman Sachs/State Street deals of 2012 may yet be trumped this year.

In prime brokerage, there may be more consolidation among smaller players but the established larger banks will continue to dominate. Out of these, Goldman Sachs and J.P. Morgan seem in my view to be doing especially well.

There is much, therefore, to be positive about in the next 12 months, although ongoing SEC cases highlight the fragility of the sector in the face of a relentless, 24-hour media news cycle. Firms can be damaged by being named in stories even when they have not been accused of insider trading misconduct. The industry has to get round press negativity and I would urge people to hold their breath and not make their minds up until the full legal eventualities have been decided. Facts matter.

But on the whole, reasons to be positive far outweigh the negative this January. The hedge fund industry is filled with talented, dedicated people and I expect it to prove the critics wrong over the course of 2013. ■

JOEL PRESS is the founder of Press Management

THE WEEK IN QUOTES

"SOONER OR LATER THE PERFORMANCE WILL SPEAK FOR ITSELF AND EVENTUALLY THERE HAS TO BE SOME OUTFLOWS FROM LARGER CTAS"

Peter Kambolin, CEO of New York-based Systematic Alpha Management (SAM), believes size is becoming a hindrance for some CTAs

"INVESTORS HAVE FINALLY WISED UP TO THE FALLACY OF THE 'HOT LAUNCH'"

HFMWeek reader, as part of this week's State of the Industry survey

"THE COMPANY DISTORTED, MISCHARACTERISED, AND OUTRIGHT IGNORED LARGE PORTIONS OF OUR PRESENTATION"

Pershing Square's Bill Ackman, who called Herbalife a "pyramid scheme" during an in-depth December presentation, responds to the nutritionist firm's defence of its business model