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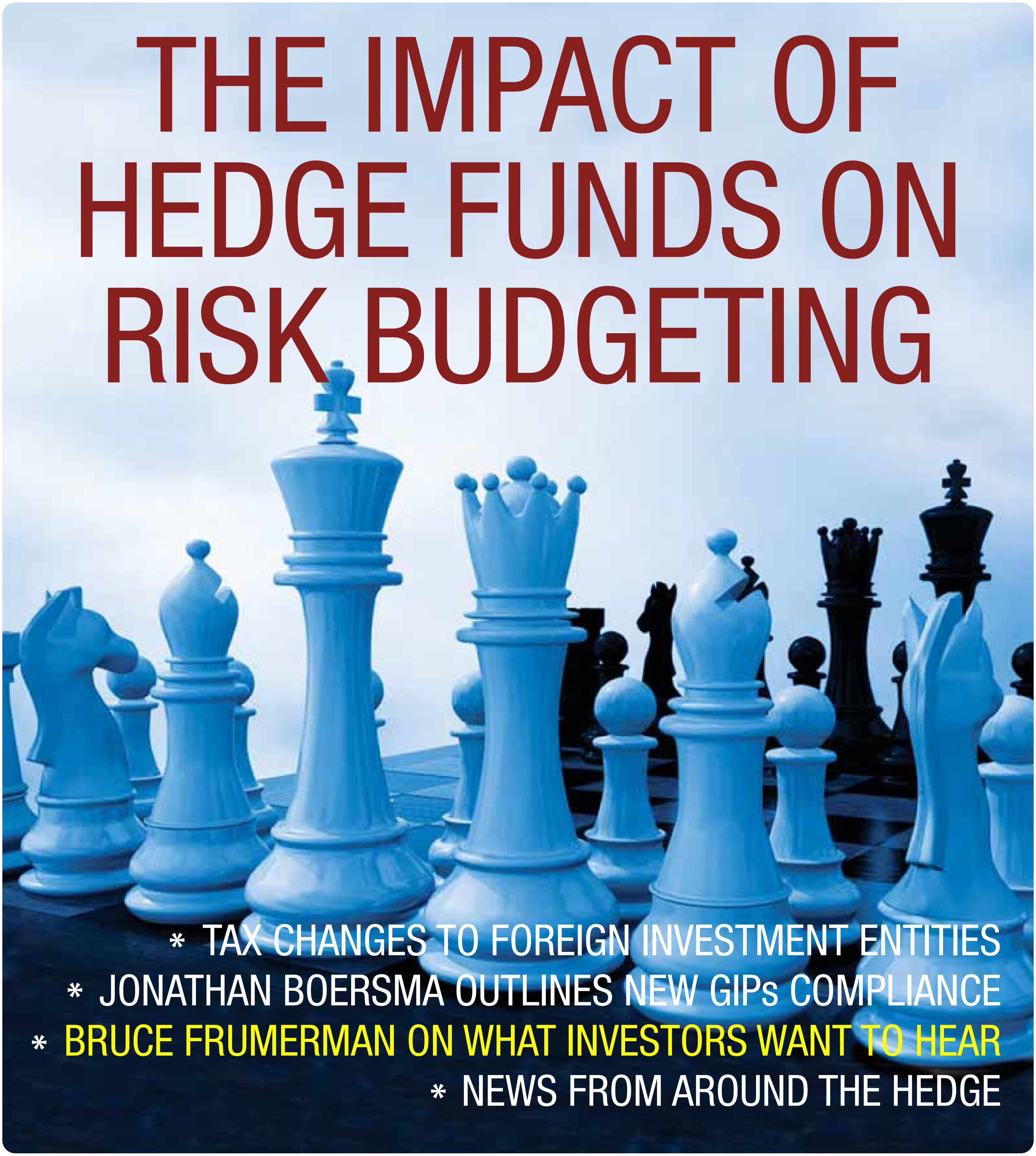
A MONTHLY REVIEW OF HEDGE FUNDS & ALTERNATIVE INVESTING MARCH 2010 VOLUME 10 ISSUE 3



THE IMPACT OF HEDGE FUNDS ON RISK BUDGETING

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Tell Investors What They Want to Hear & Out-Market Your Hedge Fund Competitors

Bruce Frumerman asks “Are you providing the right information?”

Bruce Frumerman
President
Frumerman & Nemeth Inc.

In January 2010, two surveys were released in which institutional investors show that hedge funds are not telling them what they want to hear. Your hedge fund can improve its ability to out-market competitors if you apply the survey revelations to your communications marketing.

What investors want to hear

The two surveys published in January that should be of interest to all hedge fund firms are the annual Global Hedge Fund Investor Review by Prequin and the SEI report, The Era of the Investor: New Rules of Institutional Hedge Fund Investing.

In the Prequin survey institutional investors were asked to name and rank their key considerations when choosing a hedge fund manager. The #1 response given was “Understandable / Transparent strategy”.

For the SEI survey, the biggest challenge institutions said they faced in hedge fund investing was “Transparency”. “Educating the Board” came in second. “Performance” came in third.

Additionally, over 70% of the investors SEI surveyed reported requesting more detailed information from managers than they did a year earlier. Did your hedge fund make an effort to provide more information last year than in the year before? And if so, were you providing the right types of additional information?

As SEI observed, “investors are intent on understanding a firm’s culture, investment strategies and operations. To remain competitive, fund managers will need to be proactive in enhancing their transparency, investor communications and reporting.” What did investors declare as their top-ranked selection criteria? “People, investment philosophy and the process for generating alpha.” There is something that my communications and sales marketing consulting firm has seen over the past year that the SEI survey also documented: the term transparency has taken on a wider connotation. SEI’s survey participants were expressing concern with transparency as it applies to investment process, as well as portfolio holdings, third-party administration and custody. “Investors want sufficient communication and reporting to assure them that hedge funds are generating alpha from a consistent approach that is in line with the fund’s stated strategy,” the report observed. Investor reporting and communication have emerged as key aspects of manager quality and differentiation, SEI noted.

What this means for fund managers

In this post-crash, post-Madoff world, having institutional-quality operations management at a hedge fund, with third-party administrators, custodians, et al, is no longer a fund differentiator; it’s just part of doing business. Although performance still matters, it has become tertiary to the key differentiator and value-add: a hedge fund’s investment process.

The institutional contacts that hedge funds market to have recognized that it is not enough for them to think that a fund and its manager are acceptable. They found they need to be able to communicate to their own constituents – investment committee members, other members of the family office, the clients whose money wealth managers may want to allocate to the hedge fund – just why they are recommending investing with one manager and not another with similar performance.

But that is easier said than done. Understanding and buying into the investment process of a hedge fund – a key element of the subjective part of institutions' due diligence vetting – is reliant upon how cogent, compelling and clear the hedge fund is in telling its story. As the Prequin and SEI survey results demonstrate, this is a key area that hedge funds have to better address in their marketing efforts.

Make this marketing intelligence work for you

Most hedge funds are communicating too little about how they manage their portfolios. Don't let your hedge fund be one of them. Instead, reevaluate and elaborate on the storyline you use to educate and persuade people to understand and buy into the process you follow in managing your hedge fund. Map out what topics you need to be addressing in greater length as well as how to communicate what you have to say in a more linear storyline.

Three pages of bullet points within a twenty-five page flip chart presentation are not good enough; nor is a pitch book/flip chart as your sole or primary leave-behind marketing collateral. Institutional investors have made it clear that they must re-tell your hedge funds' investing process story to their constituents. It is your responsibility to make their job as easy as possible. You can do this by providing marketing collateral that includes a full written explanation of the process you follow in managing your portfolio. This buyer-focused communications will, in turn, help your firm be perceived to be the more defensible decision over similarly performing competitors who ignore this communications marketing step.

Build a buyer-focused storyline that can pass muster with an interested, sophisticated and skeptical prospect. Make it clear enough to also teach and sell less sophisticated investment committee members on your fund and its investment process. This storyline for your fund should be applied with consistency to your marketing materials, your verbal pitch presentations, your DDQs, RFPs and Letters to Investors.

Don't forget to rehearse your portfolio manager, sales person and third-party marketer in telling your new, more elaborate storyline so they can do so smoothly and without fear of contradicting each other from one prospect meeting to the next.

Tell institutional investors what they want to hear and you fill both the information gap and differentiate yourself from your competition. *

Bruce Frumerman *is president of Frumerman & Nemeth Inc., a New York-based communications and sales marketing consultancy that helps financial services firms create brand identities for their organizations and develop and implement effective new marketing strategies and programs. His firm's work has helped money management clients attract over $7 billion in new assets, yet Frumerman & Nemeth is not a third party marketing firm. Bruce has 30 years of experience in helping money managers to develop buyer-focused positioning strategies to differentiate them from their competitors; create more cogent and compelling sales presentations and marketing materials to better tell their story; and use media relations marketing to help establish a branded identity for their organization by generating third-party endorsement for the expertise of their people, the value of their services and the quality of their products. He has authored many articles on the topic of marketing money management services and is a frequent speaker on the subject at conferences for hedge fund managers, institutional, mutual fund and Separately Managed Accounts money managers and Third-Party Marketers. He can be reached at info@frumerman.com, or by visiting www.frumerman.com.*