

Hedge Fund Marketing In The Recessionary, Post-Madoff Environment

Woodfield's President and CEO Frank Franiak was speaking recently with an industry colleague, **Bruce Frummerman** of the New York-based communications and sales marketing consulting firm, [Frummerman & Nemeth Inc.](#), about the changes we've seen 2008 bring about for hedge fund firms. Bruce's observations and insights about new business marketing resonated with us, as they reflected some of the same issues we see hedge funds struggle with today in order to stay in, and grow, their business.

Here's part of their conversation.

Frank: What has the recessionary, post-Madoff environment changed for hedge funds?

Bruce: As I know you've seen, arms-length administration, record keeping and reporting oversight have gone from being "nice to have" to "need to have." Today's hedge funds can't afford to do without a firm such as Woodfield, both to handle operations-related tasks and to serve as a tangible demonstration of taking fiduciary responsibility for their investors. Also, more regulation is coming. These are the changes and challenges that have been, and will continue to be, covered by the press. However, while operations-related issues present business management challenges, they are not going to be the key selling points of tomorrow that will differentiate one hedge fund firm from another.

Another change is that the selling cycle has grown longer. We're seeing a few reasons for this. Many investors remain unsure where to next allocate their alternative strategy investment dollars. "Trust only after verifying due diligence" is becoming more the rule than the exception. And today's investors require a greater "comfort factor feeling" that they understand more about how the manager of a hedge fund they're considering thinks and invests than they had in the past.

So, you're seeing a shift in the traditional marketing touch points of reference in telling a hedge fund's story.

Bruce: That's right. Hedge funds battle to stand out from one another by communicating about the key due diligence factors that investment committees discuss behind closed doors: performance, pedigree and process.

But 2008 has crucially changed both what hedge funds have to report and the marketplace's perceptions about what hedge fund managers have to say regarding these topics.

Performance for 2008 was negative for most hedge funds. While their average relative returns weren't as bad as the S&P 500 Index, managers who delivered positive absolute returns were few and far between. For fund managers who have been around for a while, this means they now also have to live with the resulting domino effect of deteriorated three- and five-year performance track records.

Historically, when they didn't have a good performance story to tell, many managers would rely on having a good pedigree story to fall back on. Unfortunately, the value of having a pedigree, from the investors' perspective, has also come into question as a result of the Madoff scandal. At least for a while, the value of a quality pedigree--where you were before and what you have done in the world of investing--is going to be overshadowed by prospective investors asking themselves, "But can we trust them?"

That brings us to process, which has also become more suspect. This isn't just thanks to the Madoff scandal. True, we are in an environment where the few bad apples have made investors increasingly suspicious of money managers. But, that aside, after suffering a year of big losses, financial advisors and investment committees are under greater pressure to have the next fund managers and strategies they choose to receive their new investment allocations be very defensible decisions! A great number of strategies that investors thought were sound did poorly last year, so managers under consideration this year have a tougher job of convincing to do.

So, the biggest communications marketing change the recessionary, post-Madoff environment wrought for the hedge fund manager is the need for a more detailed explanation about investment process.

When you're speaking with hedge fund managers now about this communications challenge, what's the first thing you tell them?

Bruce: Avoid being vague. It's surprising the number of money managers who are.

You and I have been speakers at hedge fund industry conferences where we've heard investment consultants and financial advisers talk to hedge fund managers about this. Investors and their gatekeepers don't have time to perform detailed due diligence on all of the funds out there in their screening, so the short cut they take is to look first for reasons to reject a manager.

Sure, there are obvious red flag issues that may qualify as reasons for a hedge fund's marketing materials to get moved from a prospect's inbox to the reject pile, but being vague can get your marketing materials pitched into the bin just as quickly.

Two common grounds we hear are a commodity-like lack of differentiation from the pack and reasons to doubt the efficacy of a manager's claimed strategy. These impressions tend to be formed when the prospect is given too little information to go on. I find the culprit is often a hedge fund's vague-sounding explanations about its investment process.

This is more often the result of poor communications skills than because managers are trying to keep confidential a truly proprietary element of their portfolio management. But forgiving and being willing to overlook a manager's lack of good communications skills are not the first things that will come to mind for prospective investors who are presented with hazy explanations about how a portfolio is being run.

From our vantage point at Woodfield it appears that there are differences in the ways some hedge funds are running their portfolios now compared to before the crash. Are you finding hedge fund managers addressing this more in their marketing?

Bruce: That's a good point. Investors recognize that while it takes some time to come out of a recession, the current economic environment is a temporary one. So, they want the next hedge fund manager they select to have a thoughtful plan for running the portfolio now and for the post-recessionary economic environment that will follow.

Unfortunately, the storylines and marketing materials of many hedge funds that we're seeing don't make mention of how they plan to navigate their portfolios through market recession to market

recovery. Those fund managers that do will help engender a comfort factor among prospects and further differentiate themselves from their competition. The hedge funds that think they can wait until they are asked such questions in, say, a finals presentation, will find they may never get that far.

Speaking of finals presentations, there can be a lot of meetings with individuals--consultants, investment committee members and the like--before a fund can even get to the stage of presenting to a group of final decision makers. What counsel are you giving hedge funds to improve their odds of making it to a finals presentation?

Bruce: Don't get lost in translation! In almost every case a prospect who is pitched in a sales meeting is going to be retelling what he knows about the hedge fund to others involved in their decision making process. He will be speaking to an investment committee, a spouse, an accountant or an attorney. And he will be retelling the hedge fund's story to that person or group. So, one of the important sales missions a hedge fund has is to reduce the odds that a prospect will mess up retelling its story.

A fund's marketing materials are what tell its story when the manager is not there and are what a pitched prospect will pass on to colleagues when that fund is under consideration. A full and clear, buyer-focused explanation about the investment process and how the manager thinks can improve a fund's odds that it has differentiated itself from its competition and reduce the odds that the prospect will mess up retelling its story to others.

Performance aside, what would you say are the keys to hedge fund marketing success?

Bruce: Today, more than ever, success in attracting investors is dependent upon a hedge fund's ability to educate and persuade people to be aware of and buy into how it invests. Achieving this requires developing a cogent and compelling way to best tell the investing story with consistency, applying it to sales and marketing efforts and obtaining third-party endorsement for and increased awareness of the firm's investing process. Do these things and--as long as you're delivering performance that's within the ballpark of acceptance--you'll be able to out-market more of your competitors.

Thank you, Bruce!

About Bruce Frumerman

Bruce Frumerman is president of Frumerman & Nemeth Inc. (www.frumerman.com), a 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. Their work has helped money management clients attract over \$7 billion in new assets, yet they are not third-party marketers.

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