

Global Association of Alternatives Investors

Position Paper
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The last decade has seen a rapid growth in alternative investment strategies, accompanied by an equally rapid interest in the area by plan sponsors. The emergence of Alternatives as an asset class has been spurred by two clear factors

- a more progressive business compensation structure where true skill is rewarded by performance fee alignment, and
- the development of skill based strategies which seem to be relatively uncorrelated with the industry standard asset classes – equity and fixed income.

However, as the market for alternatives has developed very rapidly, there are still various anomalies in the overall market structure, partially because of the fragmented nature of both the investors and the hedge fund managers. On the hedge fund side, a facet that is often cited is that a very small number of large hedge funds account for a significant portion of the total assets of the industry. The repercussion of this fragmentation is that there is wide spectrum of hedge funds in the market – with good skill and with poor skill, with crowded standard strategies and with unique but complex strategies, with the business stamina to weather downturns and those without, and with the bargaining power to determine various facets of the investment management contract or without.

A less known fact is that the plan sponsor market is equally fragmented, wherein a small number of large pension plans and endowments invest a significant portion of their asset base in alternatives. The repercussion of plan sponsor fragmentation is the sustenance of various anomalies in the alternative space.

These anomalies span various topics such as:

- fees of hedge funds and the competitive position of plan sponsors for high fees
- gates, lockups, side pocket investments and investment transparency
- excessive risk taking in hedge funds and blow up risk
- the variation in investment risk control in portfolios which have complex trades.
- the skill actually offered by fund of funds to justify a second layer of fees.
- misconceptions around what is alpha, what is beta and whether they are the same or different.
- The value of active versus passive investments and their comparison to short extension 130/30 strategies and hedge funds.
- the value of illiquid strategies compared to a liquid marked to market portfolio.

While there are several forums that have debated these issues, we find that there is often a reluctance to debate these topics freely as the participants in these forums are from across the industry from opposite sides of the fence, (plan sponsors, hedge fund managers and consultants) and have very different views due to the impact that it can have on their business position. Further, in almost all cases there are regulatory and

organisational constraints which would hinder the actual implementation of ideas on these topics.

As such, we feel there is a need for an association of plan sponsors in the industry which can function purely as an intellectual think tank on such issues, without having any objective from a regulatory lobbying perspective, or from an implementation perspective. This has been our *raison d'être* for starting the Global Association of Alternative Investors (GAAI).

The objectives of GAAI are as follows:

- to create a association network of plan sponsors who invest in the Alternatives space, from across the world who can share ideas on subjects of mutual interest. In order to create a situation where there is no misalignment, we aim only to have members from end investors such as government and corporate pension plans, insurance companies, and endowments.
- to foster innovation of new ideas and be an intellectual think tank in the area.
- to create forums where the plan sponsor community can share learning between themselves and learn from others in academia and research.
- to generate momentum from a plan sponsor perspective to increase market efficiency in the business model of alternative managers.

What we do not aim to be is

- a lobby group for regulatory purposes
- a forum which combines hedge fund managers, consultants and plan sponsors
- a conference organiser
- an academic journal publisher
- a formal training or certification institute, or
- a forum where members will share the perspective of their respective organisations.