Hedge fund industry overview

Davide Serra

SECTION 1

Hedge fund performance and volatility

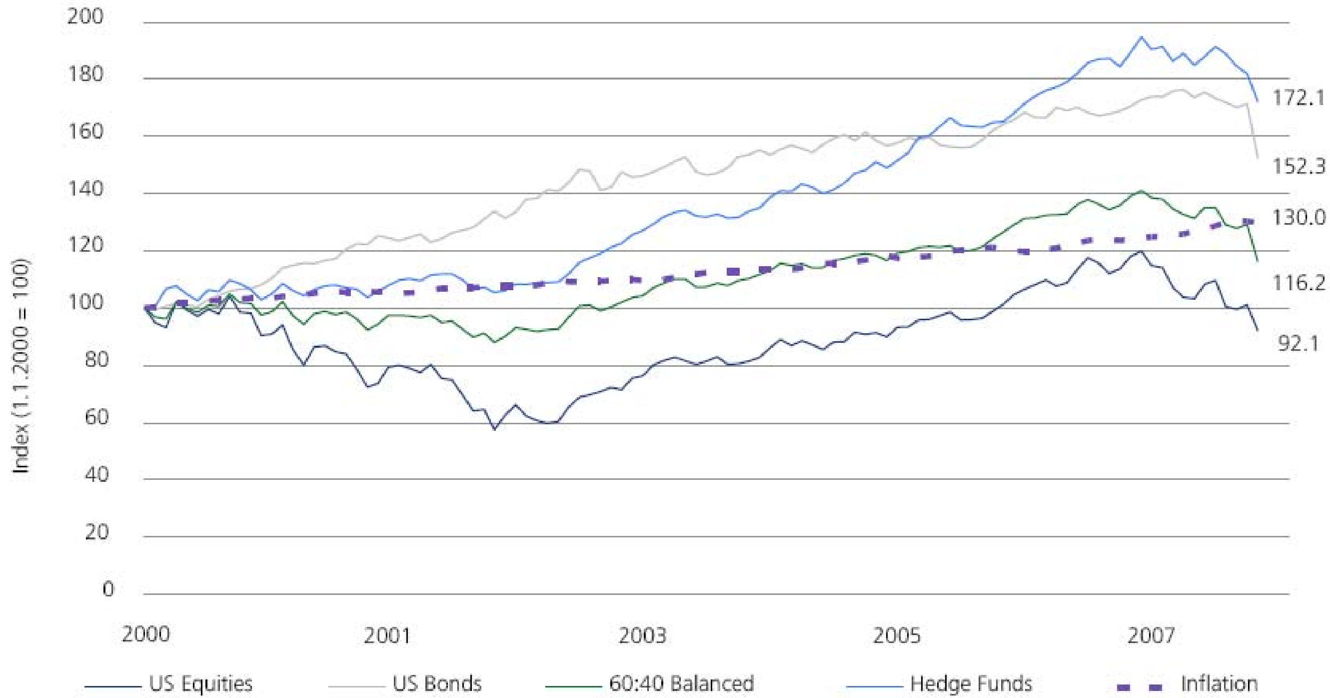
Historical hedge fund performance

HFRI fund weighted composite index—performance analysis since 1990

Index	12-month		3-year annualised		5-year annualised		10-year annualised		Since 1990 annualised	
	Net return	Standard dev	Net return	Standard dev	Net return	Standard dev	Net return	Standard dev	Net return	Standard dev
HFRI FWC	(9.10)	8.43	4.43	6.62	7.00	5.82	9.32	6.92	12.57	6.85
S&P 500 w/ dividends	(21.96)	14.75	0.22	11.38	5.16	10.34	3.06	14.37	8.84	13.97
FTSE 100 Index	(24.19)	20.00	(3.63)	13.73	3.68	11.71	(0.32)	14.10	3.83	14.28

Source: HFR Global Hedge Fund Industry Report—Third Quarter 2008

Absolute performance this decade



Source: UBS Alternative Investment Solutions, Thomson Financial.
Based on total USD total returns returns from January 2000 to September 2008. Equities: S&P 500; Bonds: Lehman US Aggregate Corporate A; 60:40 Balanced: 60% equities, 40% bonds, monthly rebalanced; Hedge Funds: HFRI Fund Weighted Composite; Inflation: US CPI.

A comparison of Long-Only vs. Hedge Fund portfolios

Balanced long-only portfolio compared to HFRI Fund of Funds Composite Index (Jan-90–Oct-08)

Balanced long-only portfolio

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD	LTD
2008	-3.1	0.6	0.7	1.9	0.4	-4.6	-1.4	-1.5	-7.5	n.a			-13.9	6.8
2007	0.2	0.6	1.2	3.1	0.9	-0.7	-0.1	0.7	3.8	2.5	-1.3	-1.0	10.2	8.0
2006	3.2	-0.2	0.9	2.7	-1.3	-0.4	0.7	2.0	0.6	2.6	2.6	0.5	14.6	7.9
2005	-1.8	1.9	-1.6	-0.6	0.3	0.2	1.7	1.2	0.8	-2.2	1.6	1.8	3.2	7.5
2004	1.1	1.1	0.2	-2.9	0.9	1.3	-2.1	1.2	1.7	2.6	4.5	3.0	13.2	7.8
2003	-1.3	-0.5	-0.1	5.8	5.2	0.4	0.0	1.1	2.6	3.4	1.6	5.3	26.0	7.4
2002	-2.5	-0.3	2.5	-0.6	1.2	-1.8	-4.6	0.9	-6.1	4.3	3.3	-0.9	-5.1	6.1
2001	1.1	-5.1	-5.0	4.3	-0.9	-2.2	0.2	-1.4	-5.0	1.5	3.0	-0.7	-10.1	7.1
2000	-4.2	0.0	5.3	-3.7	-1.2	3.0	-2.3	1.7	-3.3	-1.5	-2.8	2.4	-6.9	8.8
1999	1.0	-2.9	2.6	2.4	-2.9	2.1	0.7	0.0	0.0	3.1	1.2	4.7	12.4	10.5
1998	2.1	4.4	2.2	1.2	-0.6	1.5	0.0	-6.9	3.2	6.3	3.1	3.7	21.6	10.3
1997	-0.3	0.4	-1.5	1.7	4.7	3.5	2.6	-4.1	4.2	-2.3	0.6	0.7	10.3	9.0
1996	0.7	0.1	0.9	1.3	0.1	0.7	-1.4	0.9	2.6	1.2	3.9	-1.2	10.2	8.8
1995	-0.1	1.9	4.9	2.7	1.6	0.2	3.2	-2.4	2.7	-0.5	2.5	2.3	20.6	8.6
1994	4.3	-1.2	-2.8	1.8	-0.2	0.3	1.5	1.7	-1.4	2.3	-3.1	0.7	4.0	6.3
1993	0.9	2.1	4.1	3.5	1.6	-0.5	1.3	3.9	-0.7	1.6	-3.7	3.4	18.8	6.9
1992	-1.9	-1.1	-3.2	1.2	3.5	-0.9	1.0	2.5	-0.6	-2.6	0.4	0.9	-1.0	3.2
1991	3.1	5.6	-3.0	1.0	1.4	-4.2	3.7	0.7	3.0	1.4	-2.0	6.4	17.8	5.4
1990	-3.4	-3.0	-3.9	-1.0	7.6	0.3	1.7	-5.9	-5.9	7.2	-0.3	1.7	-5.8	-5.8

HFRI Fund of Funds Composite Index

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD	LTD
2008	-2.9	1.4	-2.7	1.0	1.7	-0.8	-2.7	-1.4	-6.3	-7.3			-18.0	8.1
2007	1.3	0.8	0.8	1.7	2.1	0.7	0.3	-2.2	2.2	3.1	-1.5	0.5	10.3	9.9
2006	2.9	0.4	1.7	1.8	-1.9	-0.6	-0.2	0.7	0.1	1.7	1.9	1.7	10.4	9.9
2005	0.0	1.4	-0.6	-1.4	0.2	1.4	1.7	0.8	1.5	-1.4	1.7	2.0	7.5	9.9
2004	1.6	1.1	0.5	-0.9	-0.9	0.2	-0.6	0.0	0.9	0.8	2.6	1.5	6.9	10.1
2003	0.8	0.3	0.0	1.2	2.1	0.7	0.2	0.8	1.2	1.5	0.6	1.6	11.6	10.3
2002	0.5	-0.3	0.8	0.6	0.4	-0.9	-1.3	0.3	-0.5	-0.2	0.8	0.7	1.0	10.2
2001	1.9	-0.7	-0.4	0.7	0.9	-0.1	-0.4	0.2	-1.6	0.9	0.4	1.1	2.8	11.0
2000	1.5	5.2	0.2	-3.4	-1.6	2.8	-0.2	2.0	-1.2	-1.0	-1.5	1.4	4.1	11.8
1999	1.4	-0.2	2.1	3.3	0.8	2.8	0.7	0.1	-0.1	1.3	4.9	6.9	26.5	12.6
1998	-1.0	1.9	4.0	0.9	-0.9	-0.6	-0.2	-7.5	-2.6	-2.0	1.4	1.6	-5.1	11.1
1997	3.6	1.7	-0.8	0.4	1.8	2.5	4.6	-0.3	2.8	-1.4	1.1	1.1	16.2	13.3
1996	2.7	-0.6	1.0	3.1	1.5	0.4	-1.9	1.5	1.3	1.6	2.3	0.7	14.4	12.9
1995	-1.3	-0.1	1.4	1.5	0.9	0.6	1.7	2.3	0.8	-0.5	1.2	2.2	11.1	12.7
1994	1.3	-2.3	-2.3	-1.1	0.4	0.8	0.2	1.3	0.8	-1.0	-1.0	-0.5	-3.5	13.0
1993	0.9	2.2	1.5	2.3	2.1	2.8	2.4	1.8	0.3	2.3	0.4	4.8	26.3	17.6
1992	1.3	1.2	0.8	0.1	0.3	0.4	0.8	0.5	2.5	1.7	0.3	1.8	12.3	14.8
1991	0.4	0.0	3.5	-0.8	0.8	1.2	0.5	1.3	1.8	0.6	0.1	4.5	14.5	16.0
1990	0.1	1.3	2.1	0.9	0.5	2.2	3.1	1.6	2.8	1.6	0.0	0.1	17.5	17.5

Return below -4%
Return between -4% and -2%
Return between -2% and -1%

Source: UBS Alternative Investment Solutions, Thomson Financial

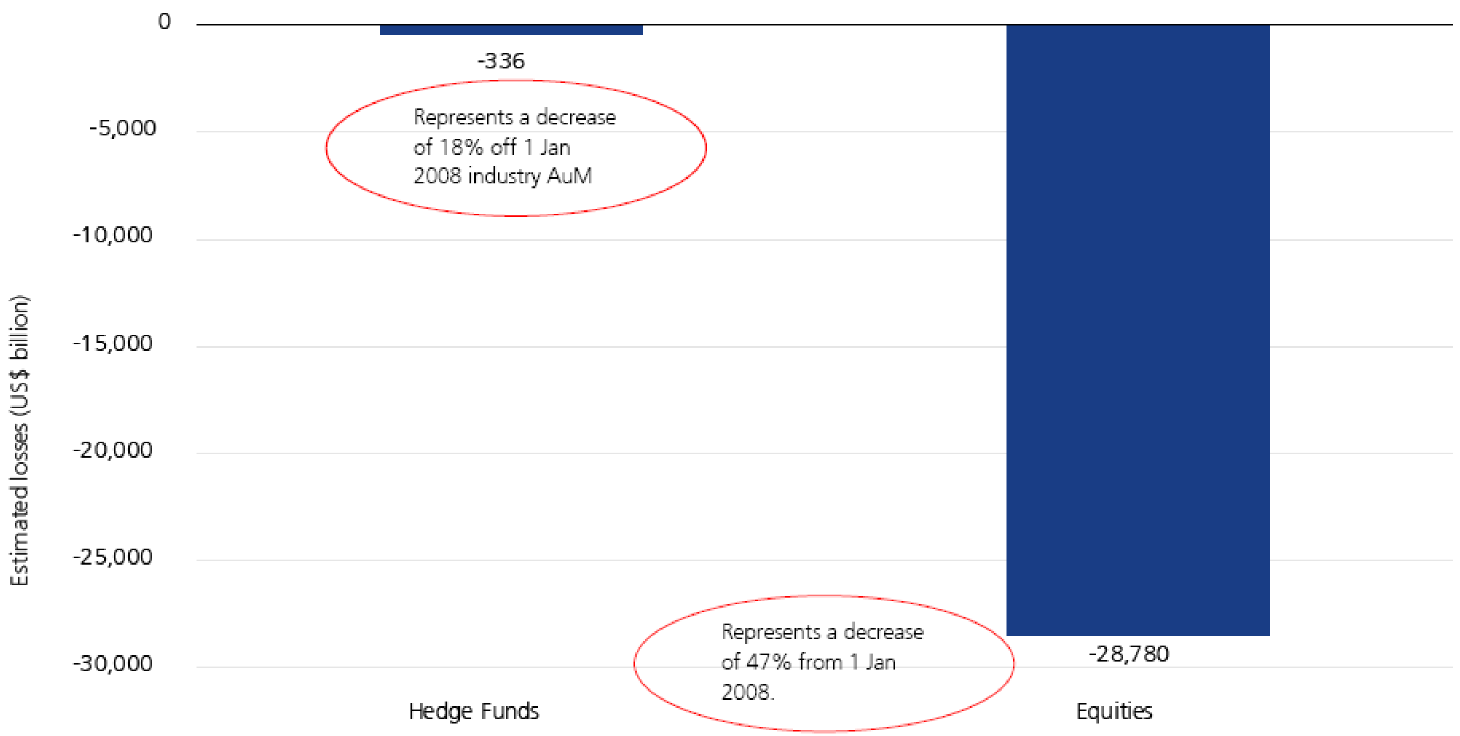
Note: LTD stands for life to date and is the CARR (Compound annual rate of return) from January 1990 to Oct '08. The balanced portfolio is based on 60% MSCI World Total Return Index and 40% JPM Global Government Bond Index, rebalanced monthly. The long-only portfolio is gross of fees while the HFRI Fund of Funds Composite Index is a proxy for a hedge funds portfolio net of two layers of fees

SECTION 2

Wealth destruction and the recovery path

Wealth destruction

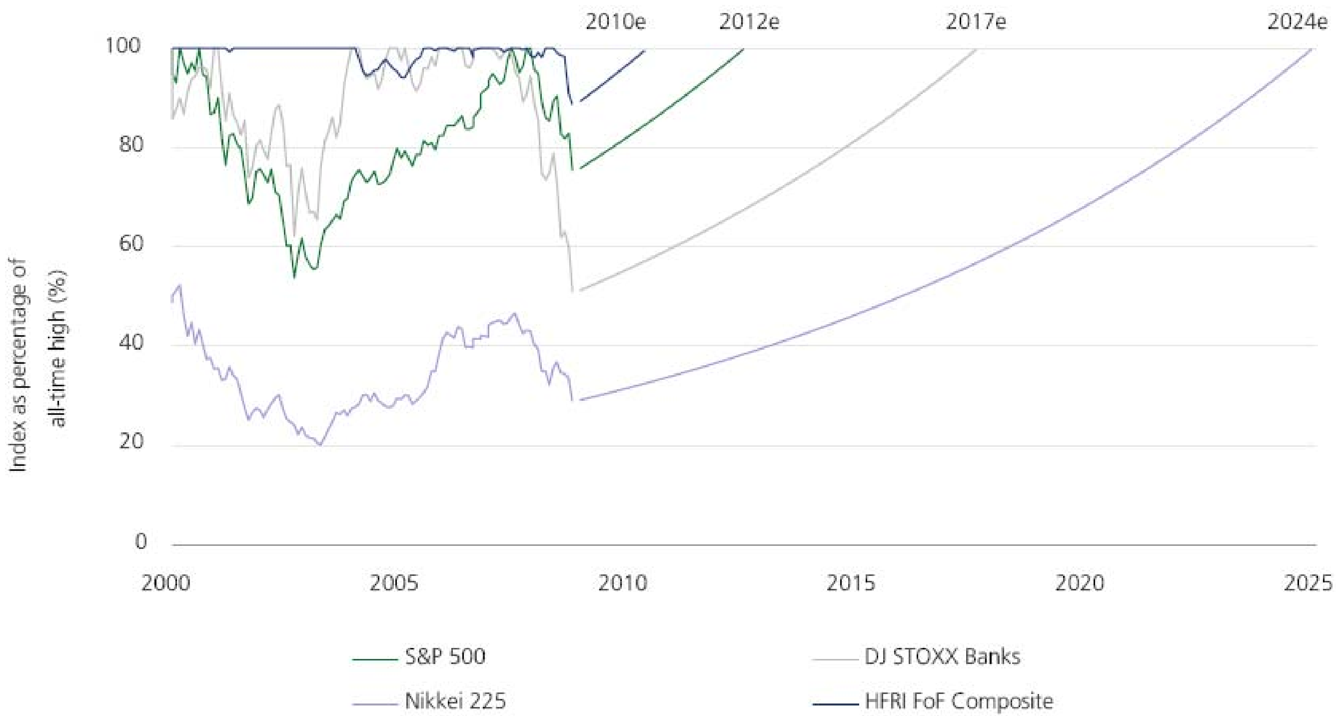
2008 Estimated losses in perspective



Source: UBS Alternative Investment Solutions, Bloomberg
Hedge fund component calculated by applying an 18% decrease to industry assets according to HFRI of $1.72 trillion. 18% is the estimated drop in the HFRI hedge fund composite index since 1 January 2008. Equities loss from the "Bloomberg World Exchange Capitalisation Index", in US$. Estimated losses in US$ billion to 11 October 2008

Digging out of the hole

Drawdown and potential recovery at 8% return p.a.

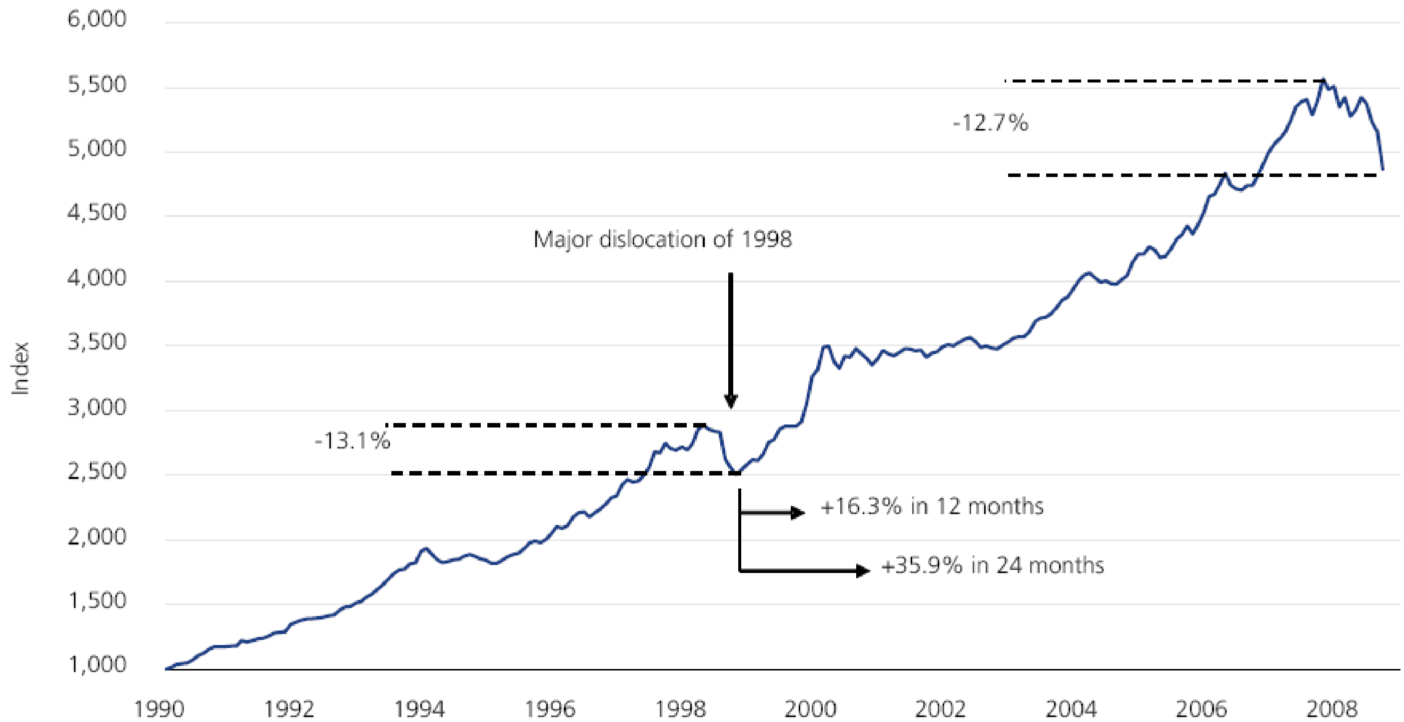


Source: UBS Alternative Investment Solutions, Thomson Financial

Hedge fund dislocations—a good entry point?

"Be fearful when others are greedy, and greedy when others are fearful"—Warren Buffett

HFRI Fund of Funds Composite Index

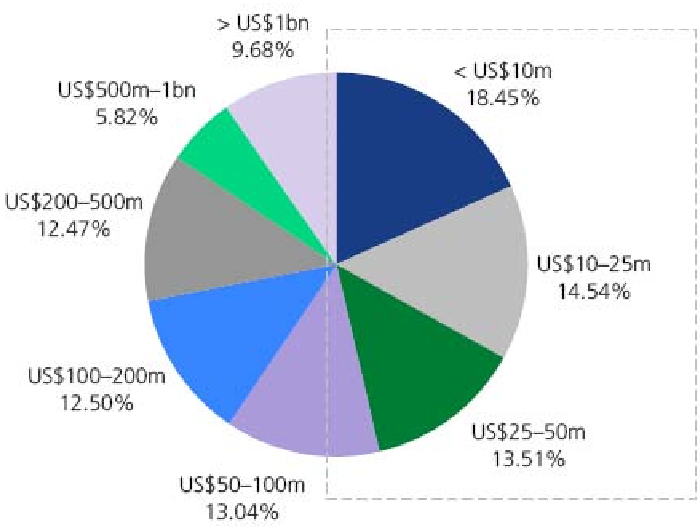


Source: UBS Alternative Investment Solutions, Thomson Financial
September 2008 inclusive

Distribution of industry assets by fund AuM tier

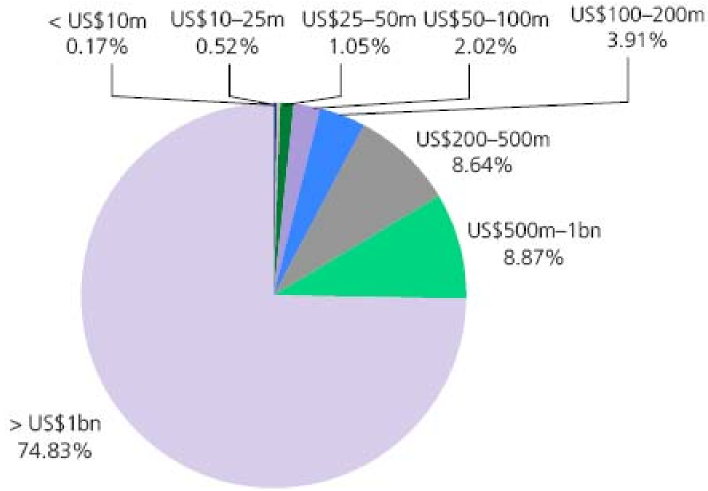
The number of funds in the HF industry is set to experience significant change in 2009 …

By number of funds



Source: HFR Global Hedge Fund Industry Report—Third Quarter 2008

By fund AuM size



Source: HFR Global Hedge Fund Industry Report—Third Quarter 2008

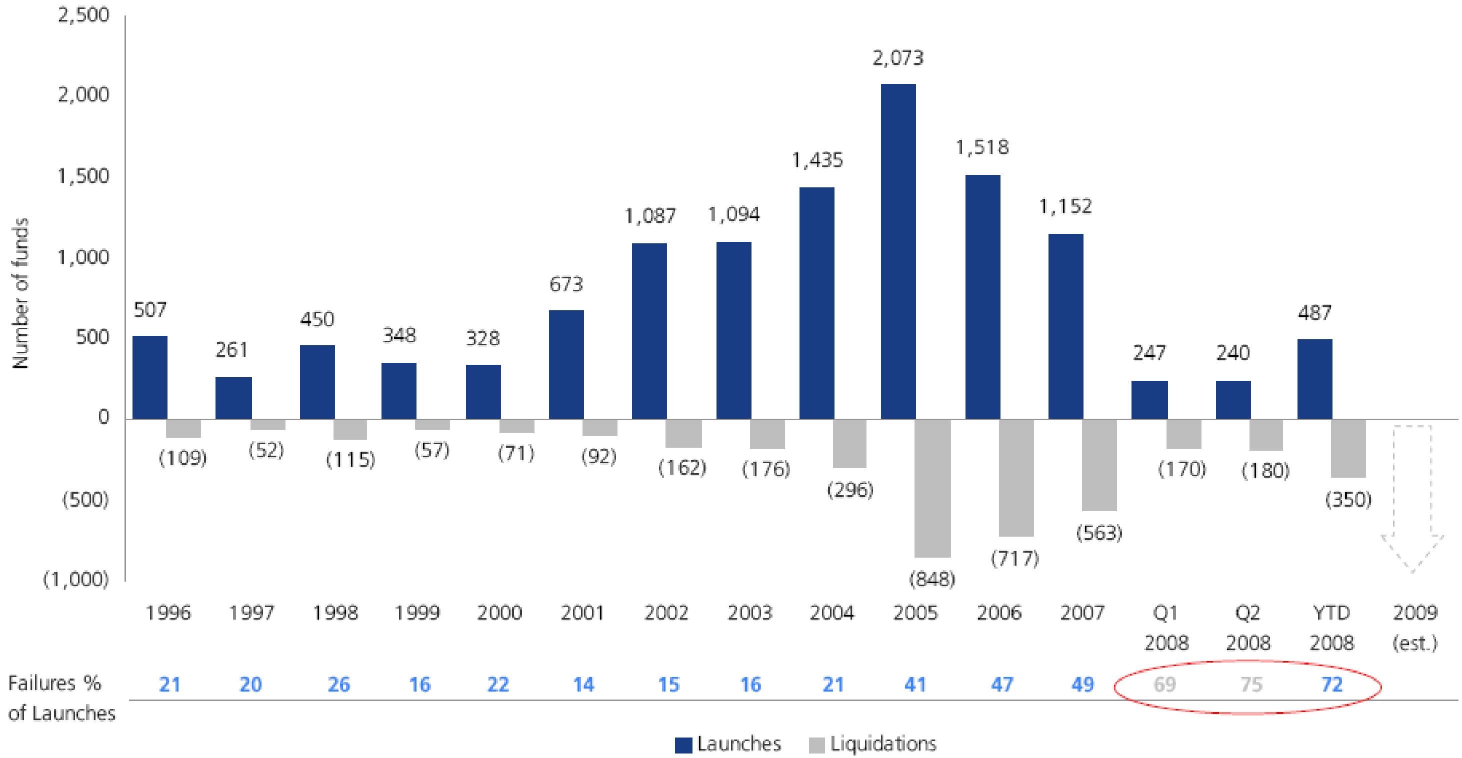
… with those with asset less than US$50m most in danger of disappearing

SECTION 3

Industry growth concentration and mortality

Estimated number of funds launched/liquidated: 1996 to Q2 2008

The mortality rate of funds is expected to rise to the highest level since the conception of the industry



Source: HFR Global Hedge Fund Industry Report—Third Quarter 2008

Note: Due to lag time in notification of fund launches and liquidations by fund managers, HFR only estimates through prior quarter

Why FoF's make sense for the unsophisticated investor

Access to the blue-chips, diversification and lack of selection skills are likely reasons why an unsophisticated investor should go for a FoF

Five reasons

1. Lack of necessary fund selection skills
2. Access to "Blue-Chip" funds only through FOF
3. True diversification only likely through FOF
4. Management of HF portfolio would be overly onerous
5. Generally better liquidity offered to investors through FOFs rather than HFs

Diversification characteristics of hedge fund vehicles

Manager diversification \ Strategy diversification	Yes	Some	None
Yes	Balanced Fund of Funds		
Some		Concentrated Fund of Funds	Strategy Baskets
None		Multi-Strategy Hedge Funds	Single-Strategy Hedge Funds

Source: Ineichen, 2008