OPALESQUE



Opalesque Round Table Series '12

LONDON

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Editor's Note

Two days before the 2012 London Olympics open, we present you the Opalesque 2012 U.K. Roundtable. We found that not only athletes have been traveling to London lately, but *"every single week groups of financial services companies from China are visiting us. They come here for fact finding and looking to do things, just like the Japanese did in the 80s. History does not repeat itself, but it does rhyme. The Chinese are great students of history, they study the mistakes the Japanese made and are in general a lot more cautious...."*

Life time opportunities

Read in this Roundtable details about the **three sovereign Chinese wealth funds** – how do they differ, and which one of them has started the first investments in fund of funds? **Can an offshore Renminbi market develop in London**, like the Euro bond market in the 80s, the Japanese dollar warrant market in the 90s and ADR and GDR markets in the 2000s?

The **dislocations** that are going to take place over the next ten years in **banking and insurance** (via **Basel III, Solvency II**) are going to create **opportunities that we may never see again in our lifetime**. Third Point and Paulson have launched reinsurance companies with significant amounts of capital, and Steve Cohen's SAC has announced one. Read how to set up such vehicles in order to benefit from the deleveraging in banking and insurance.

Traditional hedge fund strategies are challenged

A lot of hedge fund strategies have become much more difficult to assess considering the bimodal tail risk (depending upon the outcome of the European crisis), particularly directional hedge fund strategies. Significant tail risk may be a consequence of a stroke of a pen, as opposed to an economic outcome. Is it true that a lot of start-up managers are missing these tidal changes in the markets and promote strategies and styles that made money in the 2005 to 2007 period, but may fail going forward?

The Roundtable discusses strategies that have the potential to continue making money for investors, like G10 rates strategy, global equity relative value, U.S. municipal bond market strategies, arbitrage strategies including statistical arbitrage and idiosyncratic opportunities in Structured Credit.

The German Mittelstand Opportunity

One example of an idiosyncratic and specific story which is rather independent and not necessarily correlated to the broader market environment focuses on German mid-sized companies (or "Mittelstand": mostly privately owned German mid cap companies largely manufacturing and engineering export oriented goods). **In a secular shift that will probably last for 5-10 years until there is a new financing order, roughly 5,000 companies will have to re-arrange about 1,000 billion euros of financial debt** on their balance sheets in order to adapt to the changes in corporate lending and banking in Germany. As those firms are forced to move away from bilateral short term facilities towards multilateral and longer term instruments (for which there are secondary markets), huge opportunities come up in German high-yielding corporate credit.

The Opalesque 2012 U.K. Roundtable, sponsored by Eurex, Bingham and Taussig Capital, took place June 28th in London with:

- **Blaine Tomlinson,** Founder, Financial Risk Management (FRM)
- **Laurie Pinto,** CEO, North Square Blue Oak (NSBO)
- **Dr. Paul Netherwood,** Co-Founder, Beach Horizon
- **Basil Williams,** CEO, Concordia Advisors
- **Mark Hoffmann,** Portfolio Manager, Robus Capital Management
- **Christopher Leonard,** Partner, Bingham McCutchen
- **Joe Taussig,** Founder, Taussig Capital AG
- **Renaud Huck,** Senior Vice President, Eurex Group

Cover Photo: London Bridge

The Roundtable discussion offers additional insights and intelligence about:

- **Which hedge fund strategies have been successful for institutional fund of hedge funds manager FRM?**
- **What is behind the successes of FRM's seeding business?** The combined multi-manager business of Man and FRM will manage $19bn: **What does the new unit aim to achieve?**
- **How do systematic strategies cope with today's markets?** What should be considered when designing systematic trading strategies?
- **Will there be a massive M&A cycle coming soon?**
- **What are the new trading opportunities going forward? Will the Deutsche Mark, Frank, Lira, Drachma come back?**
- **How do exchanges handle the mandate given by global regulators to move OTC clearing to central counter parties (CCPs)?**
- **Where is collateral protection heading?** With new regulations, it is estimated that 1.7-2.2 trillion dollars of collateral will need to be posted by buy side firms, hence protecting these assets in the event of the default of a clearing member will be of utmost importance.
- **Opportunities or Nuisance?** What are some of the new regulations European managers will have to cope with?

Enjoy the read!

Matthias Knab

Director Opalesque Ltd.
Knab@opalesque.com

Participant Profiles



(LEFT TO RIGHT)

Dr Paul Netherwood, Renaud Huck, Joe Taussig, Basil Williams, Mark Hoffmann, Christopher Leonard, John Holton (Bingham), Blaine Tomlinson, Laurie Pinto, Matthias Knab

Introduction

Renaud Huck
Eurex Group

My name is Renaud Huck. Based in London, I am a Senior Vice President at Eurex Group where I am responsible for U.K. institutional investor relations.

Eurex Group includes six businesses and by working together, each of these businesses play a key role in the financial industry. The value we bring to the market is our unique business model that covers the entire process chain in derivatives and securities trading. There is no other exchange group that covers trading and clearing, risk and collateral management, market data and IT under one roof. We are the experts in what we do.

At Eurex Group my role is to reach out to the buy side, be they asset managers, hedge funds, high-frequency algo firms and also sovereign wealth funds to provide greater opportunities to the buy side.

Paul Netherwood
Beach Horizon LLP

My name is Paul Netherwood. I am one of the Founding Partners of Beach Horizon LLP, a London-based CTA.

Beach Horizon is a systematic fund manager that trades a portfolio of global commodity, financial and foreign exchange markets with a larger weighting to commodities than many CTAs. The firm was founded by David Beach, Sanjeev Lakhanpal and I in 2005. It was originally part of Beach Capital Management which was run by David who has over a 20 year track record in fund management. I started my career at AHL in the early 90's.

Laurie Pinto
NSBO

I am Laurie Pinto. I am the Chief Executive of a group called NSBO. We are based between London and Beijing.

Blaine Tomlinson
FRM

I am Blaine Tomlinson, founder of FRM. We are a global hedge fund investment specialist managing around $8 billion in client assets, most of which are from pensions and other institutional investors. Recently we agreed to integrate our operations with Man Group's Multi-Manager business to create the largest independent funds of funds group based in Europe, which will operate under the FRM name.

Christopher Leonard
Bingham McCutchen

I am Christopher Leonard, a Partner in Bingham McCutchen's investment management group. Bingham's investment management practice spans financial centers in the US, Europe and Asia and offers legal advice and support to investment managers of all types across those continents. My particular focus is on advising institutional and hedge fund asset managers on UK and European financial services regulatory issues.

Mark Hoffmann
Robus Capital

I am Mark Hoffman working for Robus Capital as Portfolio Manager. We run a credit opportunities strategy in the German speaking countries based out of London and Frankfurt. We are the first fund to focus on the German Mittelstand investing across the whole credit spectrum: liquid to illiquid, private to public, bilateral and multilateral as well as special situations and distressed opportunities.

Basil Williams
Concordia Advisors

I am Basil Williams. I am the CEO of Concordia Advisors. Concordia is an alternative asset manager, founded in 1993, focusing on relative value strategies in the rate, credit and equity markets.

Joe Taussig
Taussig Capital

I am Joe Taussig of Taussig Capital. We partner with fund managers to create reinsurance companies that result in permanent capital and generate a considerable amount of assets for their sponsors. Furthermore, they are virtually certain to outperform the fund manager's funds. The best known of these types of reinsurers are Berkshire Hathaway and Greenlight Capital Re. However, Third Point, Paulson, and SAC have launched similar companies this year.



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Matthias Knab **2012 hasn't been an easy year so far for investors and asset managers. How are you analyzing and adapting to this market?**

Basil Williams: **We have been conservative in our risking taking across our strategies so far this year given the macro backdrop. On an ex ante basis, our risk is running at about 65% of target. We manage assets in three strategies - a G10 rates strategy, which focuses on micro relative value trades in Germany, the US and the UK. We also manage a global equity relative value strategy which is a pairs-trading strategy in companies that have multiple classes of listed equity. For example, we trade holding companies against their listed subsidiaries and voting shares against nonvoting shares. In the third strategy we look at opportunities in credit, focused on the U.S. municipal bond market.**



Why have we picked these strategies as opposed to others? Over the years Concordia has been involved in both CB and quantitative strategies, and credit and merger arb. I think our feeling coming out of the crisis is that the strategies we focus on currently are as close to uncorrelated and unique within the space as you might find. They tend to be less affected by particular macroeconomic events.

Clearly, we are living in a world of what can be called bimodal tail risk, depending upon the outcome of the European crisis. A lot of strategies have become much more difficult to assess considering this tail risk, particularly, directional hedge fund strategies. Significant tail risk may be a consequence of a stroke of a pen, as opposed to an economic outcome, and that causes us to be quite cautious.

Basil Williams

We are seeing good opportunity in traditional fixed income arbitrage; a lot of prop capital has left the street. Why are we focusing on the credit relative value opportunity manifested in the U.S. municipal bond market, which is in a state of transformation? It used to be a very high quality, rate-based market. It is becoming a credit based market, as the creditworthiness of the issuers has declined. Less than 40% of the market is AA or better compared to about three-quarters five years ago. This results in a lot more opportunity for credit alpha in a space that traditionally has not displayed those characteristics. While still retail dominated, the U.S. municipal bond market is going through a transformation, and when you go through broad transformations in the market, they usually create good trading opportunities.

Mark Hoffmann: **We focus on corporate credit in Germany where there is also very specific kind of story developing. There is a secular shift in the way German mid-sized companies (or "Mittelstand" – mostly privately owned German, mid cap companies largely manufacturing and engineering export oriented goods) finance themselves, moving away from the banks towards alternative providers of capital, away from bilateral short term facilities towards multilateral and longer term instruments for which there are secondary markets. If you read the newspaper, Germany's economy is one of the sounder ones in Europe, and certainly the economic fabric in terms of industrial backbone is probably one of the more robust ones. However, less well publicized is the fact that the German banking system is not in that good a shape. Traditionally, Germany's economy relied on what was called the "three pillar banking system", which were Landesbanken, Cooperatives and the private commercial banks like Commerzbank and Deutsche Bank.**

Each one of those three pillars has become weaker. That is to a certain extent related to the financial crisis – which brought banks down globally - but for the specific system in Germany the break down was bound to happen sooner or later anyway, as it was not sustainable that German banks were lending to sub-investment-grade companies at rates as low as 50 basis points over EURIBOR (on the flip-side decades of cheap capital from this banking system were

probably partially responsible for there being such a large number of world-leading privately owned well-invested mid-sized companies in very capital intensive businesses).

Probably some 24 months ago, these mid-sized German companies needed to start looking for financing elsewhere as banks were not able to provide new loans or even extend existing ones. Hence, a local debt capital market started to emerge in Germany with various instruments that have names a bit difficult to pronounce in English like Schuldscheine and Genussscheine. You also have smaller bonds – which are actually called "Mittelstand bonds" which come with German documentation and are only placed in Germany, and we expect further evolution of existing and development of new instruments as well.

We invest in German high-yielding corporate credit as the space is undergoing a massive shift. We are talking about roughly 5,000 companies with about 1,000 billion euros of financial debt on their balance sheets – a significant part of that needs to and will be shifted away from bilateral bank financings to multilateral capital market instruments. A curiosity is that historically many firms had bilateral, working capital facilities, but based on a term called BAW or "bis auf weiteres" broadly translated as "to be cancelled at any time", meaning the financing was terminable at any point. The companies now realize that this is not a healthy condition at a time when banks want to reduce their books.

This development or broader shift in financing has just started, and it is such an enormous shift as you have to move the financing order all the way from the left to the right. It does create inefficiencies, dislocations and distortions, and that is basically what we are investing in. We expect this secular shift to last for probably 5-10 years until there is a new financing order.

Of course, the current issues in the broader European financial markets and the European sovereign debt crisis help us, because it produces more volatility and stress in the system, and generally creditors like us get paid better (i.e. higher coupons) than you would in a more stable environment. However, unlike for conventional distressed or special situations funds, the European crisis is only a side show and not our investment thesis: the opportunity set we are focusing on is an idiosyncratic and specific story, and is rather independent and not necessarily correlated to the broader market environment.

Mark Hoffmann



So to finally answer the question, 2012 has so far been good to us as we saw our investable universe increase dramatically by a flood or new instruments coming out – loans, bonds, Schuldscheine – and prices generally moving in our direction. The domestic German and Austrian markets continue to produce more paper which is interesting to us and we are also seeing companies (after decades of cheap money) accepting to pay higher coupons or margins on their debt.

Blaine Tomlinson: The global markets are very challenged, and this is not likely to change soon. Fixed income yields are very low and equity markets are range bound. Equity market upside is capped by the uncertain macro environment and their downside is currently limited by central bank intervention.

Hedge funds in aggregate are not having an easy time, but on a relative basis we still hold our view that hedge funds are better suited than long only to protect capital and to generate returns, particularly during times like these.

Within the individual hedge fund strategies we have always had a strong focus on relative value and arbitrage type strategies. Since the 2008 crisis we have seen many opportunities in this sector. At the simplest level, these strategies make money through providing liquidity. With banks withdrawing from proprietary trading, there is less competition for good trades and as a result arbitrage and RV returns have been much more attractive. Specifically,

statistical arbitrage has been very successful for us, though there are constraints in terms of high quality capacity.



We also look at dispersion in the markets and what that means for hedge funds. For some time now, equity markets have been driven by technical rather than fundamental factors. This has made it difficult for fundamental equity long-short managers to outperform. On the other hand, there is still dispersion in credit markets, and so credit managers can profit from better security selection on the long and short side.

We also see some idiosyncratic opportunities, for example Structured Credit. We have liked the strategy for a while now because of its asymmetric payoff profile and because the market dynamics in both RMBS and CMBS are somewhat asynchronous with traditional markets.

Blaine Tomlinson

Laurie Pinto: It was quite obvious for anyone watching after 2008 that the existing model, the old structure of the markets, is in a serious challenge. I am not sure if anybody in 2008 would have predicted the issues would carry on that long and that painful for many. One clear outcome from the crisis is that a situation has been established where the world is falling into a divide between the haves and have-nots. There are countries that have got cash and have got a banking system and there are areas that have not.

We are seeing a continuing trend of money coming out of Asia and China that potentially could have massive implications for the way money is run in the West. That, in general, has been the premise of our firm. Obviously, the Chinese domestic market is the second biggest on earth. They are just about to start having foreign hedge funds in China and it is an area where we are involved.

Apart from the politics, a concern we have is that a lot of stocks have correlated for a very long time now. Stock markets have all moved as one up and down, and it has been very difficult for stock pickers generally or any value-based investors to make money.

Unfortunately, quite a few of the arbitrage strategies have shown to be interest rate correlated despite any way they track it up, and that made it a bit more difficult making money there. I do expect a massive rise in the M&A cycle very soon. The Goliaths will take over the Davids, as they have the biggest balance sheets since World War II.

There are a lot of big groups with cash, and they are waiting to see Europe clarified. Then they are going to buy equities, because compared to their historical values they look very cheap. Unfortunately, it is very difficult to take such stakes in the current macro environment.

Laurie Pinto



In the short-term the global markets will also have to deal with pockets of protectionism, which has started to creep into the world from Latin America. There is a trend of protectionism now across different parts of Europe, and it contributes to a pretty unfair playing field. You could say that protectionism is still having some positive effects on London as a business center and a place to do business, but ultimately for capitalism it is a very bad thing.

Matthias Knab **Laurie, you mentioned how Asian money is affecting the global financial markets, can you elaborate on that?**

Laurie Pinto: In China, there are effectively three sovereign wealth funds. There is the CIC, which is the big one everyone reads about. There are actually two CICs, the CIC and CIC number two which invests internationally and has pretty high profile overall, buying water assets in the U.K. and making big statements to buy more infrastructure assets in Europe.

Then there is another entity called SAFE, the State Administration of Foreign Exchange. This is the unit that owns the U.S. treasury position; it has about $3 trillion of assets. Unfortunately for them, they are accounted in Renminbi and they have to deal with a domestic inflation. So, it is quite difficult for them to do much overseas at this stage.

The third one is called NSSF, the National State Securities Fund - China's equivalent of CalPERS. China has started domestic savings plan for pensioners. This fund has currently $500 billion and is predicted to double over the next four years. It is just starting to make its first investments in fund of funds. Like any emerging market, once the Chinese start to become middle class, they will start saving money. 500 million people have moved into cities, the savings industry will be a huge business.

This industry is very new in China. The first mutual funds were started in 1998. The first licenses issued and money put into QDI and QFI was in 2004. Therefore, if anyone tells you they have been doing it longer than eight years, they are significantly exaggerating.

While there is tremendous distribution opportunity, the early joint ventures were not a success. There are certain traps in that business in the China region. A lot of groups have gone out there in search of the Holy Grail and come back with a fistful of business cards, but no business.

When it comes to business, fortunately the Chinese are very pragmatic people. If you have a domestic inflation and you have got cash, you either have to use it or lose it. The Chinese have been looking to buy assets, buildings, infrastructure, companies, IP, pretty much anywhere in the world where people allow them.

For example, the African Resource Trade is well documented, and China has established incredibly strong business ties with Germany in the last few years. Just look at the approach that German politicians have used to doing business in China and compare it to the U.K. Angela Merkel goes to China, she takes a stack of books, DVDs on German philosophy, and spends two days with Hu Jintao. David Cameron goes to China, spends four hours, lectures them for an hour-and-half on Tibet human rights, and wears a Poppy [on the lapel to honor British war veterans]. If you think from a Chinese point of view, whom do you want to do business with? The way Germans historically have done business, including their manufacturing, is very suited to China's growth.



From a British point of view would be focusing more on the service economy. Those 500 million people which have moved into cities will all need healthcare services, financial services, and these will play very strongly to the strengths of London and other financial centers during the next stage in the economic development.

Laurie Pinto

A lot of these ideas are not originally mine, but was also the behind the thinking when Anthony Bolton moved from Fidelity London to Fidelity Hong Kong, which has been well documented. Fidelity looked at the development of the middle class over the last 200 years, and every time a country reaches an average personal income of $5,000 per capita, their stock market pretty much exponentially takes off. When Bolton left London, China's average was $4,850. While his logic was based on a lot of empirical data, the timing may not have been fantastic because the Shanghai index has fallen from 6000 to 2200, but it is not clear whether that domestic index really reflects China.

Paul Netherwood: What are the new trading opportunities going forward? Deutsche Mark, Frank, Lira, Drachma? CTAs have always thrived on long-term macro change and a breakup of the Euro would be a good example of that kind of change if it were to happen. 2008 was a banner year for CTAs as the world went through significant macro economic change. CTAs were the only asset class delivering returns that year. Since then, however, the whole world has been pretty static and stagnant in terms of directional activity. There have been directional moves, but they have been relatively short-lived and often reversed quite quickly, often on a statement from a central bank or from an EU politician.

That makes it a difficult environment for CTAs, which to a certain extent rely on long-term volatility. Economists around the world are concerned about levels of European Debt and that policy statements from EU politicians are just short-term solutions that just keep "kicking the can further down the road". At some point there could be a tipping point, which may manifest into either in stable Europe or a collapsing Europe. Short-term solutions will no longer be an option and Europe will be faced with tough choices on fiscal and political union. At that point, CTA strategies will probably do quite well, irrespective of which direction the markets go. However, it's not just Europe where opportunities may arise. For example, an event that seriously affects energy supplies, such as a blockade of the Straits of Hormuz, or weather patterns that severely limit crop production. These type of events would create significant price moves.

We do not try to make predictions on what will occur. One of the advantages of systematic strategies is that you are divorced from fundamentals and rely purely on price action.

One of the reasons that government intervention appears to be a factor in CTA returns at the moment is that there is not much else going on in the world. Prices seem to have little potential on the upside due to poor global growth potential and the downside is seen as limited because it appears the governments have a greater will to intervene to prop up the markets.

This has the effect of creating a range bound environment which can be difficult for many managers. History has shown that these periods rarely persist and it's unlikely that this is the new market norm. There has always been intervention in the markets whether it's been interest rate setting or currency restrictions but often these form one of the many influences in market direction. But when there is not much else going on it can appear that intervention is the dominant influence in the markets.



Will this state last? You can never predict what will happen in the next 5 years. Could we have predicted the Iraq War, the 2008 credit crunch 5 years ago? We have no way of knowing what event will occur that will drive directional activity. The approach with systematic programs is to design mechanisms to adapt to changing market conditions and be ready to catch new directional moves while managing risk. Our strategy evolves through new research, but we only deploy research that has consistent behavior in many market environments not just the one at a given moment in time.

Paul Netherwood

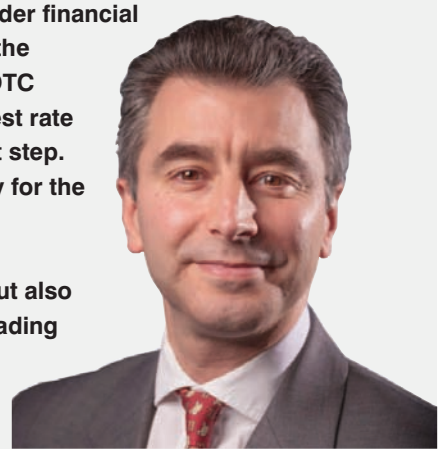


Mark Hoffmann: Probably we as an emerging manager ourselves are not best placed to comment on other new launches, however, from our perspective especially, in the high yielding credit space, there have been various new fund launches and new local teams assembled by mostly large hedge fund organizations from New York.

Additionally, for us it seemed that the obstacles for launching a new fund manager increased substantially. Pre 2008 from my perspective it seemed that everyone who knew how to handle a Bloomberg terminal and came from one of the big investment banks was thrown money at to launch a new hedge fund. Investors nowadays ask for an institutional infrastructure, high quality service providers, management teams that worked and produced an outstanding track record in the past, high transparency while generally the fees have come down, especially on the management fee side. And it feels like the quality and amount of questions and meetings increased while the average ticket size came down.

Renaud Huck: When talking about the uncertainties within the political and the broader financial framework, you can also add to that the changes on the regulatory side. In light of the current regulatory landscape and the mandate given by global regulators to move OTC clearing to CCPs, at Eurex Clearing we have decided to offer OTC clearing on interest rate swaps during the second half of this year and are looking at equity options in a next step. There is a vast need from the marketplace to mitigate counterparty risk - particularly for the buy side.

This is not only to save them from the potential default of their clearing members, but also specifically to protect their collaterals and to bring capital efficiencies to the post-trading process.



Renaud Huck

Christopher Leonard

From our side as an international law firm with a strong focus on the global financial industry, I can recognize and relate to a lot of what the group has been discussing.

In terms of fund and capital raisings, we are seeing the most significant activity in Asia. We have opened an office in Beijing this year, and this office together with our well established Hong Kong and Tokyo offices, have been very successful in supporting and advising investment managers seeking to take advantage of these Asian opportunities.

As Renaud was mentioning, people here in London and across Europe are trying to understand the flood of regulatory change that is coming down the line. We have been looking, just as he has, at the EU market infrastructure rules and of course the trading rules and structural rules that apply to hedge funds, which are really changing the dynamics of the way in which our clients are running their business in Europe. There is an awful lot of legal change that has to be synthesized, understood, and applied. On the one hand, that change makes the utilization of capital more expensive but it may also create investment opportunities.



As a lawyer, I feel a little sorry for, but greatly admire, my clients as they face this deluge from the legal and regulatory side. I am here to help them, but they and their organizations have to put into practice system changes to reflect the new rules and, moreover, adapt their business models to best operate (and prosper) in the new landscape.

In very short order, our clients are having to deal with various new regulations. We have mentioned the market infrastructure rules, there are the new short selling rules coming into force on 1st November that will impose certain disclosure requirements and prohibit European managers from shorting EU equities and sovereign debt on a naked basis, changes to regulatory capital rules and the Alternative Investment Fund Management Directive, which of course is going to have a massive impact on the way that the

Christopher Leonard

business is structured and funds are marketed in Europe. We have been working within the MiFID framework for four years now, but this Directive is also currently subject to review and will be broadened in scope. Market abuse regulations and directives are also being looked at again, with a view to tightening the rules, and we can expect that the instruments and markets that these rules apply to will be extended.

It is also the case that not only are regulations increasing, but the regulators themselves are becoming more proactive and interventionist. For example, the UK FSA has transitioned from what was known prior to 2008 as a light touch regime to being a proactive, quite aggressive regulator, as we have seen with increased market abuse prosecutions and the FSA's investigation of LIBOR rate-fixing.

Mark Hoffmann We chose our regulator to be the Financial Services Authority here in the UK as we were of the impression that they have a better brand internationally than the German authorities. After having passed the application process with the FSA in a very short time frame, we were really impressed by the amount of work and the depth of the general process.

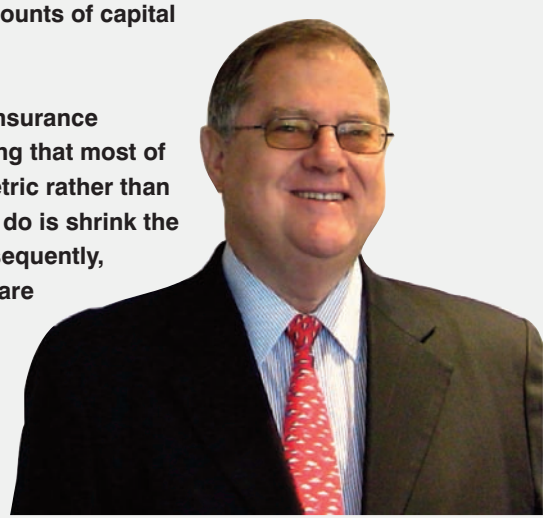
Joe Taussig: There are four words that get me really excited these days - Basel III, Solvency II. The dislocations that are going to take place over the next ten years in banking and insurance are going to create opportunities for those willing to seize them that you will never see again in your lifetime.

Some of these opportunities can be described as crossover opportunities. For example, two of our clients come out of huge bank prop trading desks that are being marked for obsolescence, and both of them are making a substantial splash moving into the life insurance business. And when I say substantial, I mean to say these are multi-billion dollar moves.

The opportunity surrounding insurers is that they have a perverse incentive to buy short duration, high grade, fixed income securities in a long-only strategy and hold them until maturity to avoid mark to market. Consequently, they sell products with the time value of money based on those bonds. However, that business case is no longer viable. If you want to study this, look at The Hartford, which is a well-known, well-respected old-line insurance company whose salesmen for the last couple of years sold fixed annuities with 3%, 4%, and 5% crediting rates against bank deposits before yielding less than 1%), when the 10-year bond is 1.5% and the 30-year bond is 2.5%. Every time they made a sale, they were losing money. Arguably they need to shut it down, but then again they were afraid they would put the salesman out of business if they would not have a product to sell and would lose their ability to distribute the rest of their products. Now the Hartford is in serious trouble.

These ex-bank prop traders that are looking to take these massive books off their hands, and the bogey they have to exceed - if you think of it as a high grade fixed income trading operation - is 3%. If they can beat 3% a year, it is a winner. Most of those guys believe they can, and so there are massive amounts of capital moving into this into this model.

The big idea here is that banks have to deleverage on the asset side and insurance companies are going to have to deleverage on the liability side. I am betting that most of the top managements will usually turn on capital charge as the primary metric rather than the profitability of the business or the product. The last thing they want to do is shrink the company, because that affects executive comp at the highest levels. Consequently, what they will do instead is shrink the things that make it appear that they are big and serve as the base for executive compensation reasons, and they will, if you would, regurgitate things that are very valuable to people who are opportunistic.

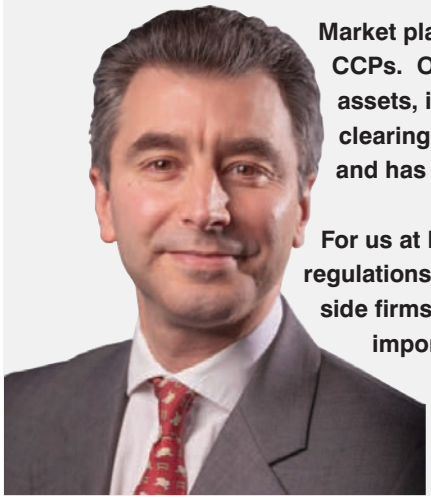


Joe Taussig

Some people involved with that will have to change their behavior. Obviously, a prop desk going into the life insurance business can be viewed as a huge change, but it's already happening on a broader scale. If you just look at this year, Third Point and Paulson have launched reinsurance companies with significant amounts of capital. Steve Cohen has announced one. Again, they are going to be picking off the dislocations that are occurring in the insurance business that are a result of the deleveraging that is taking there.

Solvency II is going to put tremendous stress on capital in the insurance business. As I said, historically the bogey is about 3% per year, so if as a fund manager you are good at what you are doing, if you think with a high degree of confidence you can generate 3% per year in any five-year rolling period of time, this is a business you might want to consider. If you are just average at underwriting, you can produce mid-teen, low 20 percent ROEs pretty readily.

Renaud Huck: We can see how changes create opportunities, and this is happening globally, whether you look at the Dodd-Frank Act in the U.S. or European Market Infrastructure Regulation (EMIR) in Europe. I definitely agree with Joe that Basel III and CRD IV will impact banks significantly in terms of their capital requirement and the size of their balance sheet going forward.



Market players will also benefit from the regulators' drive to shift markets towards using CCPs. One area where we're concentrating heavily is protection and portability of client assets, i.e. for a buy side firm, what happens to the collateral you have deposited with your clearing member should they default? Our Client Asset Protection solution addresses this and has seen a lot of interest.

For us at Eurex Clearing, collateral protection has really become a big topic. With new regulations, it is estimated that 1.7-2.2 trillion dollars of collateral will need to be posted by buy side firms so protecting these assets in the event of the default of a clearing member will be important to such firms. In addition, the ability to easily port these assets is also important.

Renaud Huck

The danger is to fall into the classical trap where you shift away from one risk but become exposed to another one. The collateral protection issue is definitely more global and more important, purely because this is the blood of the industry. All those securities that the buy side spent millions buying need to be protected, not only because this will allow them to do business, but also to ensure that there is capital efficiency for the entire industry.

Matthias Knab **How do you at Eurex address this vital collateral protection? What are some of the solutions you offer or are working on?**

Renaud Huck One aspect is how you structure your OTC clearing offering. At Eurex Clearing, we ensure that these collaterals are fully segregated in a central depository account which neither the clearing member nor the exchange would be able to access. In case one of the market players was to default, the buy side client will not be impacted as the collateral sum would remain protected in the depository account.

Blaine Tomlinson We've talked about collateral and the significance of counterparty risk, but also re-hypothecation falls into that category. I would like to hear your views on those issues, because as hedge fund investors we are, obviously, concerned about these risks which are often understated and underappreciated.

Renaud Huck Definitely. One of the major concerns of the buy side is if we have litigation, what do you do with those collaterals and how do you isolate them?

In fact, we asked ourselves, what is the solution we are going to bring to the industry? We decided to broaden the offering on the collaterals that we accept. Collateral transformation is commonly used by the sell-side, and we do not think that it was appropriate for a clearing house to be in that field. Additionally, we thought that we had a better and more innovative offering to bring to the marketplace.

So, the first thing we asked is: what is the best benchmark of collaterals' list that could be accepted? We chose the ECB Eligible List of Collaterals, but nevertheless we are rather strict in what we want. For example, we are not going to take the fifth tranche, which is ABSs.

The four tranches are the ones we take as collaterals, 25,000 ISINs. Obviously, cash is king. We also accept corporate bonds and gold certificates. By the same token, we also accept sovereign bonds, but we monitor them constantly because we do not want to have too much of one issuance. So, we have decided that we will not take more than 25% of any outstanding issuance and as far as cash equity is concerned, no more than 5% of the free float.

Nevertheless, going forward with the need of collaterals, which are going to be sucked within the industry and within the clearing houses, there is going to be a bottleneck situation, and two important questions within the industry are whether there will be enough collateral, and what tomorrow's collateral will be.

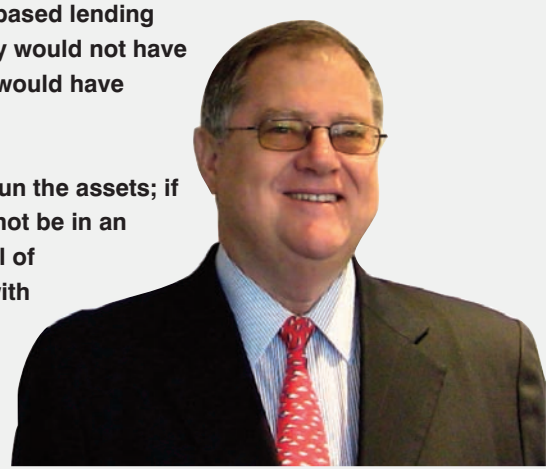
Paul Netherwood I want to add something to what Joe was saying before about Basel III and Solvency II. Our asset raising has in fact been impacted by Solvency II as insurance companies that would have allocated a lot more to alternatives are having to rein that back in. That means we are already seeing the effects of that, even though the regulations have not come into force yet. As Institutions are already deciding the appropriate size of their alternative investments due to Solvency II leverage restrictions.

Joe Taussig There is an incredible irony in all of this. A lot of times, I will argue with analysts in the banking and insurance businesses that run money in sector funds. I ask about the target return they suggest to their investors. Let's just assume it is 10%. And then I suggest they take their ten favorite banks or take their ten favorite insurance companies and superimpose that 10% just on the equity, and going back the last five years, I will bet their second five will run to the top five, it is just that simple.

Laurie and others here talked about the increasing business of non-bank lenders. I also believe that lending is a huge opportunity, but they should do it as banks! If you look at all those asset-based lending funds that got locked up in the crisis, arguably if they had been banks they would not have had those problems. Not only would their returns have been higher, they would have been tax efficient if you are an US investor.

If you start an insurance company, the investor acknowledges you get to run the assets; if you do not, you have to compete for them. Swiss Re is levered 6:1; it cannot be in an equity strategy. To give you an example, Swiss Re has 30 times the capital of Greenlight Re and 500 times the employees. Something cannot be right with that. I mean, they cannot move down to our market levered six times, because in 2008 you would be out of business.

Joe Taussig



Basil Williams: **I am a little less sanguine about the opportunity being created by the regulation and more concerned about the frictions.**

As an alternative asset manager, the impact of an increase in regulation on our business is significant; a number of new regulations are heavy-handed. For example, the US Treasury has a regulation now that we have to sign a document every year to state what foreign accounts we happen to be a signatory on. In our case, we have about 16 different fund structures and those fund structures could each have six different banks accounts so once a year I sit there and sign 96 pieces of paper that say, I am signatory on these bank accounts. Now, that is a small example of it, but I am not sure as to the real value of this information to the US Treasury.



This bureaucratic nuisance is one aspect, but what really concerns me more is the friction that is being put into the system on the investment side as a result of centralized clearing, for example. We are big fan of it, but the cost of centralized clearing versus the OTC trading is material to certain trading strategies.

The increase in bank regulation is another concern. Banks have been through their prime brokerage operations a significant provider of finance to hedge funds. Those have been extremely profitable businesses for banks. In fact, prime brokerage is a business where banks have historically taken very few, if any losses. That said, the new regulation is going to increase the cost of capital, which means the banks will increase the spread they demand from their hedge fund clients.

Basil Williams

So, again, the question I worry about is that notwithstanding the creation of opportunities through new sets of inefficiencies and the need to restructure and move assets off balance sheets, the regulations also create a lot of friction on existing businesses that can permanently change the economics of those businesses.

Laurie Pinto: **I totally agree with that. I have never seen a period where I have seen so many things manipulated in financial markets as there is now. It is pretty hard to pick a market that is not affected in one way or another. Some of the measures taken obviously don't work at all - just look at the ban on short selling, did it really stop the markets going down or are the market forces in the end stronger than politics? When politicians mess in the market, in the first place they create uncertainty; with uncertainty you get less activity; with less activity you get less economic growth; with less economic growth you get greater unemployment, and soon you may end up getting civil unrest and revolution.**

It seems to me that now everyone is fiddling around the edges, messing around with the rules, changing this, changing that. But capitalism really is about trying to get things done and making money for the greater benefit of everyone, and all the dance around about the rules and regulations and the huff and puff about it is a total waste of time, if not outright counter-productive. As an industry, regulations and compliance created this extra bureaucracy with thousands of jobs, which to a certain extent can be admired, but it all comes at the expense of investors.



Another concern of mine is around the emerging manager space in general and I will be interested in Blaine's take on this because he is a lot more experience than me. When I see hedge fund managers starting up now, it seems to me they present and promote strategies and styles that made

Laurie Pinto

money in the 2005 to 2007 period. They are great managers focusing on what I believe are bad strategies, simply because they are not taking into account that we now all live and invest in what has become a manipulated environment. Many of those strategies are just poor from a risk-reward perspective, and I am really concerned that people still believe that some of these old styles and strategies will still serve them in the current environment.

Given how the western world has moved more left wing in terms of intervention, regulation etc., I believe a lot of the start-ups are totally misguided in the current environment, and they still carry on. I think the actual alternative in alternatives has largely gone, because the hedge fund community has not really adapted itself for the changed world we are in. We can blame the bankers, because everyone else does and why should not I, but probably we have to blame the whole industry infrastructure.

Blaine Tomlinson Putting aside the political question for now, I have a somewhat different view in terms of hedge fund outlook.

Of course, I do agree that the hedge fund industry is facing a number of challenges. We are facing the same challenges as all investors are facing. For example at FRM we essentially represent many millions of private investors whose money is invested by our pension fund clients. We help pensions manage their money and construct portfolios to help them meet their liabilities.

The challenge is always how to generate the returns to meet those liabilities. Clearly, the environment is difficult and managers are challenged in a number of different ways. But I have not lost confidence in hedge funds. One of the great things about hedge funds is that they are dynamic businesses - often run by smart, entrepreneurial people. The best hedge funds adapt to the environment, and their investment strategies are highly flexible, allowing that adaptation to happen rapidly. I believe we are seeing this adaptation across a number of different firms. They are learning to make money in range bound markets, where of course it is not that easy to make a profit.

A specific example of this is the traditional equity long short hedge fund. Before, a manager may have only looked at fundamental factors and ignored macro environment or technical factors. But nowadays, we see managers starting to focus on all three factors. They are having to be flexible and adaptable in how they approach investments.



Other strategies are having to adapt through re-focusing their strategies on different geographic markets. Specifically, with macro trading, Europe and the US are very policy constrained. So we're focusing on macro managers who trade emerging markets where there is still scope to anticipate directions and trends. And as I mentioned earlier, other strategies like relative value and arbitrage are actually seeing their opportunities increase since 2008 as their bank competitors – proprietary trading desks - are being closed or downscaled.

So in looking for returns, the decisions we make are a mix of strategy decisions and localized opportunity. It is not easy in this environment, but there are return opportunities out there.

Blaine Tomlinson

Matthias Knab **What else do you see on the emerging manager side?**

Blaine Tomlinson: We have been running a seeding business since 2007 and most of the investments have been successful, with a handful being very successful.

We look for smart, entrepreneurial people who need either seed capital or acceleration capital to achieve scale, and once we invest, we can also positively influence or give guidance as far as good governance and best practice.

The point in seeding is that one has to be very selective in terms of the strategies. Do we think a particular strategy is going to work and do we think these are the best people available to make that strategy work? Several of the strategies we have seeded have been idiosyncratic or distinctive in nature, as we want something that is not dependent on market beta.



For example we seeded a credit fund lending money to corporates; that strategy has been very successful. Also we seeded a quantitative fund focused on Asian markets that is generating excellent returns.

Laurie is right that traditional strategies do not suffice anymore, so just having a value view, or a technical view is often not sufficient to achieve returns and survive in today's markets. But a good number of managers are putting idiosyncratic strategies to work within traditional markets. These are among the niches to look for uncorrelated sources of return.

Blaine Tomlinson

Paul Netherwood: I also believe Laurie is right about some strategies that may have worked perhaps before 2008, but not since. Certainly strategies that relied on cheap financing and leverage betas are strategies that don't work as well in this current environment. What is important for strategy designers and strategy builders like myself is to be very careful not to curve-fit strategy designs to localized conditions. Instead, we aim to pick up on persistent behavior that occurs over very long time spans.



When we design strategies, we know that there will be market conditions that do not always work in favor of the strategies and they will go through periods of drawdown. Every strategy goes through cyclical behavior and some cycles can be very short and others quite long. But you do not necessarily want to change your strategy every time a current cycle does not necessarily suit your model. A strategy designed in this way will then be just chasing the current environment and can run the risk of just missing it. It then also runs the risk of missing a future move that the previous model may have been perfectly set up to grasp.

Of course, you do want to deploy certain adaptive changes to your strategy where your research shows it will be persistent perhaps in multiple environments rather than always changing it to make it work for the present.

Paul Netherwood

Renaud Huck I wanted to come back to a point that Basil was making earlier about fairness becoming a big theme in the industry.

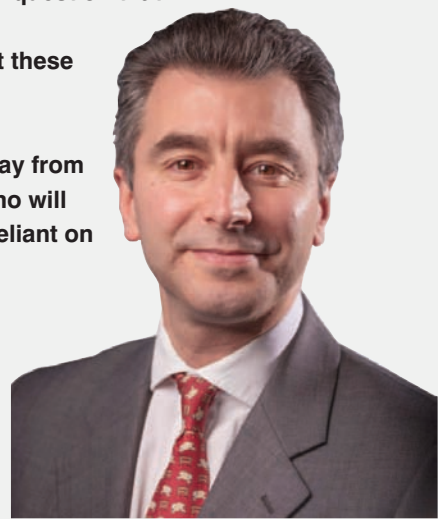
With regulators globally forcing the entire industry to embrace clearing and the use of CCPs, what will be the cost of clearing? This is a fair question, because it is certainly going to have an impact and we are now entering this

unchartered territory. In our OTC clearing offering we do not charge for the actual infrastructure. Eurex Clearing will only charge for the trades which are cleared.

But nevertheless from what we can observe there may be potential for regulatory arbitrage in the marketplace, in terms of the cost of clearing. For example, a trade that a buy side firm would do with a U.S. counterparty could potentially drag them under the Dodd-Frank Act, while at the same time for the same price a trade with a European counterparty would not. I think that this is one potential situation that could arise once these changes are implemented.

What perhaps the regulators did not consider is that the shift to a CCP will definitely have side effects and some of them would be considered negative. For example, it may force small institutional investors to exit the OTC market, purely because they will have to go more towards exchange-listed products to get the same asset exposure. That is the first thing.

OTC clearing will definitely be too expensive for these smaller structures. The other question that we will have to raise is: will there be sufficient capacity within the banks to clear for everybody? I do not think it is going to be possible. I think that banks will also limit these transactions and introduce clearing capacity limitations.



So, small institutional investors will be forced to go towards other markets to go away from the OTC world. But it will be the same potentially for second and third tier banks who will not have the internal structure and the capacity to do it on their own, leaving them reliant on the same top tier banks that do not have total capacity limitations.

So, I think that while the big principle of shifting towards CCP might be, on paper, a good way to mitigate risk, it also opens the door to significant side effects, which are potentially as big as the risk that they are trying to address in the first place.

Renaud Huck

Matthias Knab **Unintended consequences.**

Renaud Huck Exactly.

Matthias Knab **What else do you see happening in the UK?**



Laurie Pinto: Despite all those issues we've been talking about, generally my view is that it's the best time ever to be doing business here. We got the Olympics this year, every single nationality on earth is moving here which is great for property prices, we have a stock market open for business and a rational semi pro-business government. The bad news is we are part of Europe, whether we like it or not, and our economy is linked to all the problems there in one way or another. So, while unfortunately there are a few dark clouds, I still am incredibly optimistic about our business in London and the financial service industry generally.

In my view, the big development over the next 12 months will be the offshore Renminbi market here, and how it is going to grow. This is a massive business

opportunity for London. Unfortunately, I have been already a number of years in this business... I have been around in the 80s when we developed the Euro bond market, which was a massive job creator and wealth creator for the UK government. With the 90s came the Japanese dollar warrant market. In the 2000s we had the ADR and GDR markets, and hopefully in this decade we will be having the offshore Renminbi corporate market. I f we do, it is a magnificent opportunity for the UK. I am pushing for it very strongly and hope that market will be established here. It would be a massive industry for the hedge fund industry, financial services generally, and great for the UK PLC.

Matthias Knab **What would be the roadmap or steps towards the establishment of such an offshore Renminbi market in London?**

Laurie Pinto To have an offshore market you need deposits. Currently, in the UK, there are no deposits, so there is no real offshore Renminbi market. But the first products are being developed here. The first dim sum bond issues in London happened about two months ago in London. All other dim sum bonds were done in Hong Kong. Another thing we need for that market will be the backbones and clearing systems. Historically, London has been very strong in that regard and can build on a tremendous expertise and brain power in these areas.

Christopher Leonard In addition to all those advantages of London described by Laurie, I would also add the benefits of English law and the English courts which are both generally recognized as commercially sophisticated, open and transparent and available to entities and transactions of any nationality. Notwithstanding the change in culture since 2008, there is an awareness in government and at the regulator of the dangers of regulatory arbitrage and of the need to ensure that UK law and regulation is not more restrictive than that of the other major financial centers.

Joe Taussig And London's got a big time zone benefit. You can play Asia, you can play the US, you can play Europe, you have reasonable working capital at hand, there is no other place in the world you can do that.

Laurie Pinto Correct, we could not have placed ourselves in a better spot. The UK government, George Osborne, has been working really hard at this and the UK Treasury has a number of task forces working on it night and day trying to get this done.

But what people forget is it is the Chinese election year this year, so there are a number of big political issues. We just had the Dalai Lama here, which obviously is not good for moving some things forward in the short-term. Also, if you look at the Chinese banks based in the U.K., they are at the very early stages of their development

Every single week we have groups of financial services companies from China visiting us. They come here for fact finding and looking to do things, just like the Japanese did in the 80s. History does not repeat itself, but it does rhyme. The Chinese are great students of history, they study the mistakes the Japanese made and are in general a lot more cautious. Their early investments of financial services companies quite frankly were mixed, not necessarily structurally but from a timing perspective. They invested in Blackstone just at the wrong moment and unfortunately in Morgan Stanley just before 2008.

So, while not all of their investments were an immediate success, the Chinese are taking a long-term view, and I believe they can soon grow to a significant size and force here in Europe. In my view the financial services industry here should welcome them, because they come with capital and enormous distribution, which will create substantial opportunities. Therefore, I am actually very bullish on London and the financial services industry here.

Laurie Pinto



Paul Netherwood: Unfortunately, the UK is facing some quite strong regulatory head winds from the EU. There are a number of incoming Directives in the pipeline, one of the more significant being AIFMD. We are still waiting for the final Level II text to be published, but it seems that much of the lobbying that was done by the industry and which was acknowledged by ESMA and incorporated into their proposals at the end of 2011 has been rejected by the EU Commission and was not included in their draft implementing rules which were released earlier this year.



The publication of the final Level II regulations has been delayed, so it is a matter of wait-and-see, but I view this coming regulatory framework negatively, there are a lot of protectionist rules around like the requirement for EU domiciled custody arrangements and so on. A lot of these regulations will add considerable costs and difficulties to the trading process and as Basil correctly said, have become a nuisance for UK based financial firms.

We, as a firm, might opt to not apply for an AIFMD passport in order to avoid becoming subject to a lot of the more irksome provisions, even though that may restrict our marketing in the EU. It seems that some EU regulators here are not friendly to the growth of alternative investments.

Paul Netherwood

Renaud Huck

I will definitely agree with Paul in the sense that there is regulatory uncertainty. From a business perspective, companies function better when there is regulatory stability.

Nevertheless, like Laurie, we remain very optimistic for the industry. We do believe CCP clearing for the OTC space will be a great opportunity for the market place overall. I do not think the question is whether you want to embrace it or not as in the end it will simply be mandated, so we as an exchange and a clearing house have to get on with it. At Eurex Clearing, our duty is to offer segregation models and working solutions for the buy side.

The bread and butter of an exchange is to create attractive exchange-listed products. We have recently launched OAT bond futures with tremendous success and liquidity and are, all in all, rather optimistic about the opportunities for our client base.

Matthias Knab **Blaine, what do you think does the future hold for the fund of funds industry?**

Blaine Tomlinson: There will always be a role for funds of funds because of the diversity and complexity of the hedge fund industry vs. long-only managers. Also, for institutional investors, they are looking to achieve specific risk and return profiles that complement their other investments, which requires additional analytics and expertise to understand hedge fund strategy dynamics, forecast returns and construct portfolios of hedge fund investments. This isn't to say that direct investors cannot do it, but in my experience the best resources in the industry, by a long way, reside in the top funds of funds groups. Investors who want to outsource some or all of the aspects of their hedge fund investing, or who just need some help with their direct investing programs will often look for the best expertise, and so there is an ongoing demand for what we offer.



All this being said, the fund of funds industry is recalibrating and regrouping in terms of how it provides that expertise to clients and how it demonstrates

Blaine Tomlinson

value. For example, at FRM one of the things we do is use our global research team to provide access to the mid and smaller size managers who are beyond the research capabilities of most consultants and direct investors, and we use our size to negotiate better fees and terms which are passed on to clients. We also do a lot of work building customized portfolios for clients or helping clients with their direct investing programs. Sometimes these elements come together, for example when we constructed a customized portfolio of investments in small managers for a large investor who was otherwise investing directly.

To some extent I think fund of funds is an outdated name for firms like ours, as it implies a single product. Groups like ours aren't just product providers, we work with clients to come up with solutions and also have a very important role in hedge fund research, sharing of expertise and client education. Essentially we assemble deep resources and expertise in hedge fund investing and make those available to clients in a number of ways.



Mark Hoffmann: I don't fully agree with that. Historically, analyzing hedge funds was more complex due to all funds being structured as offshore companies. Today, alternative investment strategies can be structured onshore as well. A lot of structural complexity is obsolete. We also offer a Luxembourg domiciled absolute return fund and while the strategy is more complex than a benchmarked long-only product, investors are capable and appreciative. We also found that when it comes to understanding new investment opportunities family offices can often be more willing to listen and learn than funds of funds.

Mark Hoffmann

Matthias Knab In May Man Group announced it would acquire your firm, FRM. The combined multi-manager business will manage $19bn. Can you give us more details about what FRM and Man will want to achieve together?

Blaine Tomlinson: There were two things driving our decision to integrate our operations with Man's Multi-Manager business, which are scale and fit.

One of the things we are seeing in the fund of funds industry is the importance of scale. Competition is intense, and so firms that can deliver incredible resources and breadth of capability are going to do best. We'll have a very large and global investment team which can provide great access and expertise in every facet of hedge fund investing around the world. Very few firms will be able to match this. Scale also allows us to come in as a larger investor with hedge funds, essentially aggregating client assets to negotiate better fees and terms on their behalf.

With Man also there was a unique fit. We brought a well regarded institutional quality process and client base, and Man brought cutting edge capabilities with a proprietary managed accounts platform and analytics with position level data. So when we combine capabilities, it is going to result in a very extensive and differentiated set of products and solutions, but it also should improve how we manage our existing commingled portfolios since we'll have more real time data and ability to quickly shift positions due to the MAC platform.



Blaine Tomlinson

Matthias Knab **Do you see more consolidation in the fund of fund industry?**

Blaine Tomlinson: Yes, I do. As I've implied, the need for consolidation is there as scale is getting to be so important. FRM has always been a large firm within our industry with over 100 staff in a half dozen or so offices, but even for us we saw the advantage of building on our capabilities.



Some funds of funds will be successful as focused niche players, but for many others, who are looking at serving institutional investors who want well resourced partners, scale is important.

I think one of the things holding back consolidation is the question of fit. It isn't just about combining assets, but combining teams and capabilities where you and your clients have a high degree of confidence that it will work. One of the things with Man, other than the strategic fit, was a unique situation with Luke Ellis leading their Multi-Manager business. Earlier Luke had spent a decade helping build the business at FRM, and therefore he knew both businesses very well.

Blaine Tomlinson

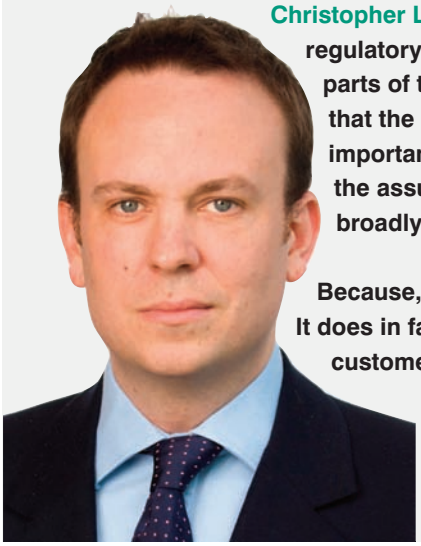
Matthias Knab **How much of your fund of funds business is in customized portfolios? At what asset size do you see investors usually switch to customization?**

Blaine Tomlinson

Today, we are about 70% product and 30% customized. The customized segment is higher growth, but that said there is still projected growth in commingled products.

When it comes to the question of either going into a commingled fund or having a customized portfolio, it comes down to a decision on both sides. The usual threshold for a customized portfolio is around $100 million, but that does not mean to say that you can't do it at smaller levels. For example, an institution may start off with $50 million or $75 million, but the anticipation is to finally run $200 million or $300 million.

Matthias Knab **What other trends and developments you want to comment on?**



Christopher Leonard: I would like to add a few more comments on the developments on the regulatory front, what they mean for the industry and how best to deal with them. Significant parts of the UK's financial services framework is derived from European law. It is no secret that the hedge fund industry has few friends in the European politic. So, it is incredibly important that the industry stands up for itself and, picking-up on your point Blaine, counters the assumption within many European legislators minds that the financial services industry broadly, but hedge fund managers especially, have no particular social value.

Because, the reality is that the hedge fund industry plays a vital role in the capitalist system. It does in fact provide social benefit to underlying investors (ultimately, in many cases retail customers in the form of pensioners) and to what has become known as the 'real economy' in terms of the professional and expert allocation of capital, protection of capital, growth of capital. I think that the industry has to get out there and say that both within the UK and Europe and to encourage (and to support) the UK government to be at the table in Europe and making that argument.

Blaine Tomlinson It is a challenge for regulators to harmonize regulation. Hedge funds will have to accept the fact that increased regulation is going to happen. Most of them are regulated in one way or another, and I believe one of the challenges will be to avoid the regulatory arbitrage Chris has also spoken about.

There are less visible issues such as re-hypothecation that we as investors are sensitive about. This is an important issue for investors and managers to understand; and while it is not in the spotlight, it is out there and needs to be better understood.

Basil Williams I would echo what Blaine said. We spend a lot of our time on ensuring we work within the regulations. We have a location here in London and in New York, and over the past we have had an office in Asia as well, and from a business and operations perspective our trades flow towards the least restrictive regulatory environment - provided that counterparty exposure management, collateral management and related aspects are appropriately covered.

Probably the biggest concern I have today, is not what is happening in the UK, but what is happening in the US. A lot of the US regulations seem to be very US bank-centric with risks pushing more business Europe's way, if not appropriately modified. Dodd-Frank is far from finalized, and Mr. Dimon's testimony over the last two weeks has put that back in the spotlight. Unfortunately, I don't think the US regulators are looking at the issues at hand on a global basis. At the same, time, the political pressures to do something fast and to protect the US banks will probably result in an uneven playing field for some time to come.

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