



2010 Key Trends in Asian Hedge Funds

Eurekahedge September 2010

Introduction

The Asian hedge fund space, which includes funds that are either based in Asia or investing in Asia, has been one of the fastest growing sectors in the global hedge fund industry since 2000, both in terms of assets and number of funds. However, the industry has also gone through difficult periods and diverse phases. After witnessing tremendous growth in the first eight years of the decade, Asian hedge funds went through a lean period in 2008 and early 2009 amid the global financial downturn and widespread redemptions. However, the industry rebounded in 2H2009, posting excellent returns and attracting more capital – the Eurekahedge Asian Hedge Fund Index was up 26.79% in 2009, the strongest yearly return on record for the index.

Figure 1 shows the growth of the Asian hedge fund industry since 1999.

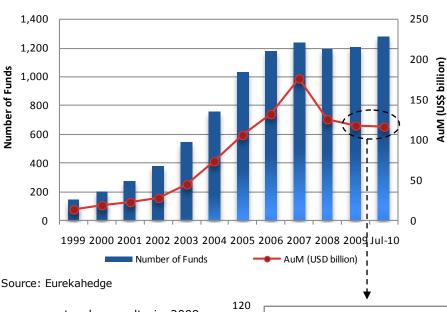


Figure 1: Growth of the Asian Hedge Fund Industry

After posting some spectacular results in 2009, Asian hedge funds have witnessed mixed returns and subdued subscriptions in the first seven months of 2010¹. While the last year ended on a high note with excellent performance and strong asset flows, a spike in risk aversion and volatility in global markets during the first half of 2010 translated into marginally negative performance (July YTD) and weak asset flows. As of July 2010, the size of the Asian hedge fund industry stands at US\$116.9 billion, which is more or less the same since the start of the year.

115
110
105
100
Way-10
Way-10
AuM (US\$ billion)

Source: Eurekahedge

¹ While we have not included August numbers in the research, our most recent data shows asset flows to be negligible – which is often the case for August.





Industry Make-Up and Growth Trends

Asset Flows

The first seven months of 2010 have yielded slightly negative asset flows of US\$1.2 billion from the Asian hedge fund space as investor confidence has been low through most of the year. Concerns over the European debt contagion spreading to emerging markets and Asia have also had a negative effect on market sentiment while fears of a double-dip recession have not subsided. In this environment, managers have found it hard to raise capital for their funds while investors have been cautious about the volatile markets, choosing to hold their allocations on the whole. However, if markets stabilise into an upward trend for the rest of the year, we anticipate greater inflows to the sector with Q4 expected to witness the strongest assets flows this year.

Table 1a shows asset flows and performance-based growth in Asian hedge funds since the start of 2008. Table 1b shows the growth in Asian hedge fund launches in 2009 and 2010 through asset flows.

Table 1a: Asset flows across Asian Hedge Funds (US\$ billion)

Month	onth Net Growth (Perf)		Assets at end	
2008	(26.0)	(23.6)	126.4	
Jan-09	0.1	(9.1)	117.4	
Feb-09	(0.2)	(4.7)	112.5	
Mar-09	0.6	(4.6)	108.5	
Apr-09	1.3	(5.1)	104.8	
May-09	3.6	(2.6)	105.8	
Jun-09	0.4	(0.2)	106.0	
Jul-09	1.6	0.5	108.1	
Aug-09	(0.2)	1.7	109.7	
Sep-09	1.0	1.2	112.0	
Oct-09	(0.0)	2.8	114.7	
Nov-09	0.9	1.0	116.7	
Dec-09	0.9	(0.1)	117.4	
2009	10.1	(19.1)	117.4	
Jan-10	(1.2)	(0.6)	115.7	
Feb-10	(0.2)	(0.7)	114.8	
Mar-10	2.2	(0.1)	116.9	
Apr-10	0.9	(0.4)	117.4	
May-10	(2.4)	0.7	115.6	
Jun-10	(0.3)	(0.2)	115.1	
Jul-10	0.8	0.4	116.2	

Note: All figures are in US\$ billion.

Source: Eurekahedge

Table 1b: Asset Flows across Asian Hedge Funds (US\$ billion)

Average AuM Growth in Asian Hedge Fund Launches through Asset Flows				
Year Total Growth Growth per Month				
2009	81%	6.75%		
2010	4.71%			

The Asian hedge fund sector witnessed strong asset flows in the last six months of 2009, gaining US\$7.2 billion through net subscriptions amid rising market sentiment. Comparatively, assets in Asian funds of hedge funds have remained low and have not seen any growth after losing nearly 60% of their total assets during the global financial crisis after reaching a peak of US\$87.8 billion in December 2007.





Figure 2 shows the relative growth in Asian hedge funds and Asian funds of hedge funds over the last two years and a half.

100% 90% 80% 70% 60% 50% 40% 30% Oct-08 Oct-09 Apr-08 Asian Funds of Hedge Funds AuM Asian Hedge Funds AuM

Figure 2: Relative Growth of Asian Hedge Funds and Funds of Funds

Source: Eurekahedge

Table 1 (on the previous page) demonstrates an interesting correlation between one month's negative performance and the net redemptions of the following one or two months and vice versa. Figure 3 shows the monthly net flows displaced by three months plotted against the Eurekahedge Hedge Fund Index. This seems to suggest that investors have subscribed two to three months after periods of positive performance and redeemed two months after periods of negative performance at corresponding magnitudes to the underlying performance. Whether this truly suggests that investors are 'trendfollowing' or a simple statistical manipulation is open to some debate.

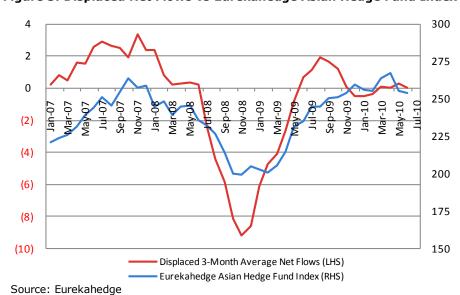


Figure 3: Displaced Net Flows vs Eurekahedge Asian Hedge Fund Index





Another interesting perspective is the high proportion of assets allocated to larger funds as opposed to medium-sized and small funds. Table 2 shows that in 2010, the largest 20% of funds manage nearly 80% of Asian hedge fund assets, an increase of more than 7% over the last six years. The biggest jump of nearly 2% occurred in 2008 when a significant number of smaller funds were forced to close due to losses and heavy redemptions. Larger funds, on the other hand, were able to handle the crisis better given their larger asset base.

Table 2: Proportion of Assets in Large Asian Hedge Funds

Percentage of Asian Hedge Fund Assets in the Largest 20% of the Funds				
Year % of Assets				
2005	72.8			
2006	74.0			
2007	76.1			
2008	78.9			
2009	79.2			
2010	79.8			

Fund Population

The first half of 2010 has seen launch activity picking up in the Asian hedge fund space, with the total number of hedge funds now standing at 1,278, exceeding the previous maximum of 1,240 seen in 2007. The 125 Asian hedge fund launches in the first seven months of the year represent a return to the healthy growth seen before 2008. The strong launch activity witnessed so far in 2010 is a result of growing interest in Asia due to greater growth potential in the regional economies as well as developments in the regional hedge fund service provider industry, making it easier for managers to set up their funds in the region. Other factors include increasing availability of complex financial products in the Asian markets, lower set-up costs as compared with the West, desire for large hedge fund investing institutions to diversify into Asia and efforts from Asian governments to attract global managers.

350 300 250 Launches / Closures 200 150 100 50 0 July 2010 YTD 2006 2005 2008 2007 Launches ■ Closures

Figure 4: Asian Hedge Fund Launches and Closures

Source: Eurekahedge





Lifecycle of Asian Hedge Funds

This section explores the trends in the average ages of hedge funds and statistically looks into whether there is any truth behind the common myth that the average lifespan of a hedge fund is 4 to 5 years.

16%
14%
12%
10%
8%
6%
4%
2%
0%
<1 <2 <3 <4 <5 <6 <7 <8 <9 <10<11<12<13<14<15<16<17<18<19<20<21<22

Figure 5: Historical Lifespan of Asian Hedge Funds

Lifespan of a Hedge Fund (in Years)

Source: Eurekahedge

Figure 5 shows the population of live and dead hedge funds according to their age as at 30 August 2010. We include dead funds in this analysis to counter the survivorship bias which would be inherent if this distribution was based entirely on live funds. The age-wise population of hedge funds demonstrates leptokurtic properties or positive skewness, showing that while most of the hedge funds are concentrated around the median age of 3.7 years, there are outlier funds that have been around for a long time and hence, increasing the mean age to 4.6 years.

Table 3 shows that the average life of dead funds² is increasing over the years. This suggests that managers are increasingly able to develop successful strategies and hence, last longer by earning performance fees while also raising enough capital in the early years to hit their survival threshold.

Table 3: Average Life of Dead Funds over the Years

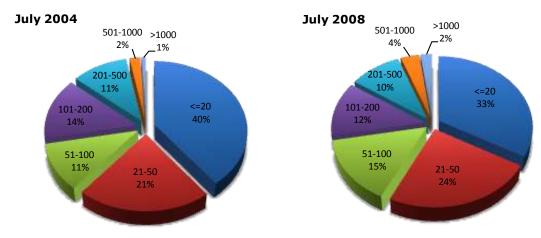
Year of Liquidation	Average Life (Years)
2002	2
2003	2.6
2004	2.6
2005	2.6
2006	3.6
2007	3.4
2008	3.6
2009	4.3
2010	4.7
Average	3.3

 $^{^2}$ It is worth noting that dead funds can be dead for positive, negative and neutral reasons – not just because of poor performance.

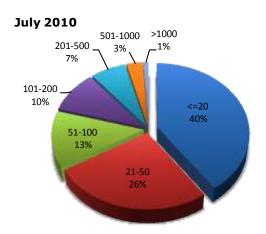


Fund Sizes

Figures 6a-6c: Breakdown of Asian Hedge Funds by Fund Sizes



Source: Eurekahedge Source: Eurekahedge



Source: Eurekahedge

The breakdown of the Asian hedge fund sector according to different fund size tranches shows some significant changes in the composition of the industry over the last few years. These changes are reflective of the growth in the Asian hedge fund space both in terms of asset flows and performancebased gains.

Figures 6a-6c show the composition of the Asian hedge fund sector by fund size in July 2004, July 2008 and July 2010. The industry, though still young, was in a phase of rapid growth in 2004 – and this phase continued until mid-2008. During this time, the number of small hedge funds with US\$20 million or below fell by 7% as most of the small funds grew significantly through healthy asset flows and strong performance-based gains. At the same time, Figures 6a-6c show that there were more than 800 funds launched during this period and since Asian funds tend to start relatively small, it can be deduced that most of the funds in mid-2008 with assets less than US\$20 million were new start-ups while those funds that had started earlier grew in size and got 'promoted' into the next fund-size category.

Since July 2008, however, as the credit crunch and the subsequent financial crisis took its toll on hedge fund assets, the industry composition has changed back to its pre-2005 days. In fact, currently, the number of relatively smaller hedge funds, managing US\$50 million or less, has increased to 66% of the Asian sector.

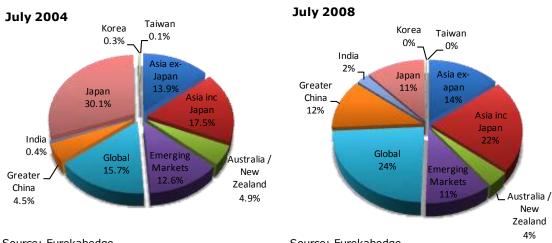




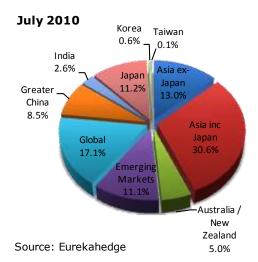
Geographical Mandates

The composition of the Asian hedge fund sector in terms of the geographic mandates of the managers has also witnessed significant changes over the years amid the growth of funds and development of the regional industry.

Figures 7a-7c: Changes in the Geographic Mix of Asian Hedge Funds by Assets under Management



Source: Eurekahedge Source: Eurekahedge



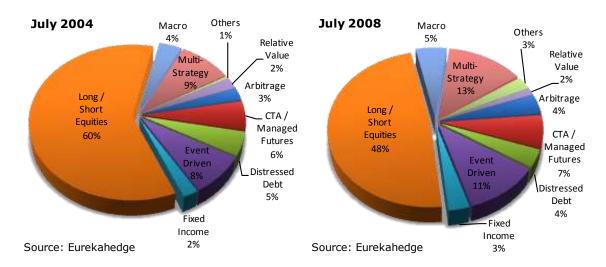
While some trends were reversed after the global financial crisis, the trend towards greater geographical diversification has continued through July 2010. In July 2004, global-mandated funds made up 15.7% of the sector – this number has now expanded to 17.1%. This is primarily due to two reasons: a) funds with a broader geographical mandate did not suffer as much as regional or single-country funds during the global financial crisis and b) most global-investing funds have significantly increased their allocations to Asia in the recent years due to the strong growth in the regional markets and continued growth potential.

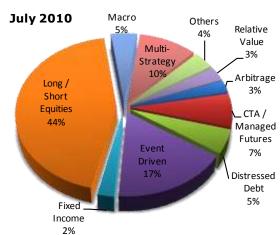
On the other hand, Japan-mandated funds have lost nearly 70% of their share of the Asian hedge fund universe in the last six years. This can be attributed to the exceptional growth in Asia ex-Japan hedge funds and three consecutive years of negative returns (2006, 2007 and 2008) by Japanese funds which led to investors allocating greater capital to the growth regions.



Strategic Mandates

Figures 8a-8c: Changes in the Strategic Mix of Asian Hedge Funds





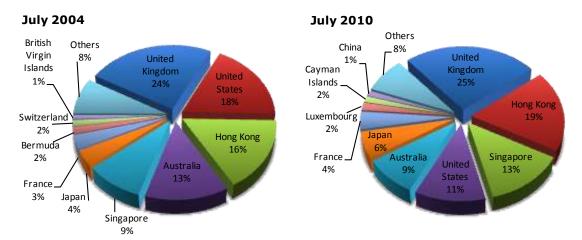
Source: Eurekahedge

In terms of strategies, the Asian hedge fund sector has witnessed some strong movements over the last six years, as shown in Figures 8a-8c. The most important trend has been the decrease in the share of long/short equity funds from 60% of the sector to 44%. However, this is not a sudden change in the aftermath of the global financial crisis; instead, this is a sustained trend through the years which can be attributed to the increasing availability of other strategies in the regional hedge fund space, greater access and easing of restriction in markets such as China and India, and the availability of more complex financial instruments in Asian markets.



Head Office Location and Fund Domicile

Figures 9a-9b: Head Office Location by Number of Funds



Source: Eurekahedge Source: Eurekahedge

In terms of hedge office locations of Asian hedge funds, the United Kingdom continues to hold the top spot as the share of US-based funds decreased. The trend suggests that a significant number of the older Asian hedge funds were set up in the US initially since the Asian hedge fund centres were not fully developed in terms of an investor base as well as service providers and financially trained workforce.

Within Asia, Hong Kong continues to be the dominant hedge fund centre while Singapore also gained some ground. Although Hong Kong did lose some of its market share as the global economy went through the financial downturn, it still accounts for more than 250 hedge funds as it was among the first in Asia to boast a wide-range of hedge fund service providers and investors, making it an attractive location for managers to set up shop in.

Channel Others Guernsey Islands 1% 1% Mauritius 2% Bermuda Cavman 3% Islands Ireland 59% 5% United States 6% British Virgin Islands Australia Luxembourg 6% 7%

Figure 10: Fund Domiciles by Number of Funds

Source: Eurekahedge

In terms of fund domiciles of Asian hedge funds, the Cayman Islands still rule the roost, with 59% of the managers choosing the location to set up their hedge funds. Cayman offers friendly regulation as well as ease of fund set-up, featuring a large number of service providers, such as law firms, accounting firms, and administrators – and with tougher regulations being introduced in the US and Europe, we expect an increase in the number of Cayman-domiciled funds.





Fee Structure

Table 4: Asian Hedge Fund Fees

Year	Performance Fees (%)	Management Fees (%)
2000	19.48	1.49
2001	19.75	1.47
2002	19.82	1.54
2003	18.61	1.47
2004	19.75	1.58
2005	19.42	1.73
2006	18.78	1.62
2007	19.08	1.84
2008	18.86	1.68
2009	17.94	1.66
2010	19.22	1.56

Table 4 shows the changes in the fee structures of Asian hedge fund launches over the last decade and although management fees have remained similar, performance fees witnessed a decrease in 2008 and 2009 as the managers responded to calls from investors to lower their performance fees. However, the average performance fees in 2010 Asian hedge fund launches are back above 19% amid a recovery in the sector.

Service Providers

This section looks at the service provider industry in Asian hedge funds – it must be noted here that this analysis is based on data reported by hedge funds to the Eurekahedge database on a biannual basis.

Prime Brokers

Table 5: Prime Brokers - AuM Share of Asia-Focused Hedge Funds

2007					
Prime Broker	Share				
Morgan Stanley	26.62%				
Goldman Sachs	26.49%				
UBS	9.15%				
Bear Stearns	9.13%				
Deutsche Bank	7.50%				
Credit Suisse	6.60%				
Merrill Lynch	3.77%				
Citigroup	3.23%				
Fimat	0.53%				
Man Financial	0.09%				
Others	6.89%				

2010					
Prime Broker	Share				
Morgan Stanley	23.9%				
Goldman Sachs	21.6%				
JP Morgan	16.9%				
Credit Suisse	9.00%				
UBS	8.40%				
Deutsche Bank	7.90%				
Citibank	3.40%				
Bank of America Merrill Lynch	3.30%				
Barclays	1.50%				
Newedge	1.40%				
Others	2.60%				





Table 5 shows the top 10 prime brokers by hedge fund assets. The changes observed in the Asian hedge fund prime broker industry suggest a move towards greater diversity versus three years ago. Before the collapse of some large financial institutions, two prime brokers accounted for more than 50% of Asian hedge fund assets; however, currently the space has more equitable distribution among the large institutions. It should be mentioned here that before the financial crisis, it was the prime brokers that had put in measures for counter-party risk; however, since then, fund managers have also become wary of their dependence on prime brokers and have diversified their businesses across the different service providers. Furthermore, the share of 'Other' has also decreased, suggesting that managers prefer working with well-known and financially stable prime brokers.

Table 6 shows the share of prime brokers among the top performing (1st quartile) hedge funds, going by 2010 performance.

Table 6: Prime Brokers' Share of Top Performing Asian Hedge Funds (1st Quartile)

Prime Broker	Share
Goldman Sachs	13.5%
Deutsche Bank	12.9%
Morgan Stanley	10.7%
Citi	10.7%
Credit Suisse	10.7%
UBS	9.0%
Bank of America Merrill Lynch	3.9%
Newedge	2.8%
JP Morgan	2.8%
BNP Paribas	2.2%
Others	20.8%

Administrators

As with prime brokers, the trend among the hedge fund administrators has also moved towards greater diversification. The most noteworthy trend is a drop in the share of assets administered by 'Others', which includes in-house administration. The primary reason for this shift is the emphasis on regulations and transparency - no investor is ready to invest with managers who do not have the proper risk controls in place and reputed third-party administrators.

Table 7: Hedge Fund Administrators - AuM Share of Asia-Focused Hedge Funds

2007	
Admin	Share
HSBC	32.17%
CITCO	10.76%
State Street	4.94%
Citigroup	4.11%
Goldman Sachs	3.36%
PNC	2.91%
JP Morgan	2.40%
Morgan Stanley	2.03%
Fortis	1.98%
Northern Trust	1.95%
Others	33.39%

2010					
Admin	Share				
HSBC	22.30%				
State Street	20.30%				
CITCO	11.90%				
BNP Paribas Fortis	4.11%				
IFCE	2.90%				
Daiwa	2.80%				
Viteos	2.50%				
Citigroup	2.50%				
SS&C	2.50%				
Admiral	2.20%				
Others	21.50%				

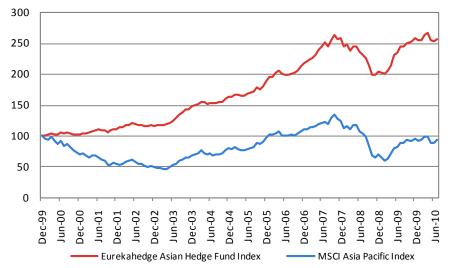




Performance Review

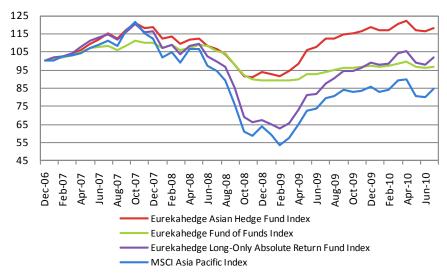
Asian hedge funds have outperformed underlying Asian stocks significantly since 2000 as shown in Figure 11. The Eurekahedge Asian Hedge Fund Index gained 157% since inception while the MSCI Asia Pacific Stock Index lost 6% over the same period.

Figure 11: Performance of Asian Hedge Funds and Equities in the Last 10 Years



Sources: Eurekahedge and MSCI

Figure 12: Performance of Asian Hedge Funds and Other Investments over 5 Years



Sources: Eurekahedge and MSCI





Hedge funds have consistently outperformed underlying markets over time, but there were distinct periods at which hedge funds delivered significantly better results. For example, Asian stock markets experienced a drawdown of 53% during the 2000-2003 period while Asian hedge funds were up 48% during the same time. Additionally, during the 2008 economic slowdown, hedge funds lost 25% of their NAVs on average while Asian stocks plummeted by 56% (MSCI Asia Pacific Index). This highlights the resilience of the Asian hedge fund industry during economic downturns and why they can be important additions to investor portfolios. Asian hedge funds have also performed better than other alternative investment classes in the region such as funds of hedge funds and long-only absolute return funds as shown in Figure 12.

Figure 13 highlights the superior risk management capabilities of Asian hedge fund managers. The average annualised standard deviation of the Eurekahedge Hedge Fund Index is 6.8%, much lower than the 16.6% for Asian equities. Managers kept portfolio volatility to less than 15% on average while the comparative figure for the underlying markets is 37% in April last year.

As such, not only have Asian hedge funds outperformed the underlying markets in the long and medium terms, they have done so with lower volatility, delivering consistent risk-adjusted returns as per their mandate.

Figure 13: 12-Month Rolling Standard Deviations of Asian Hedge Funds and Equities

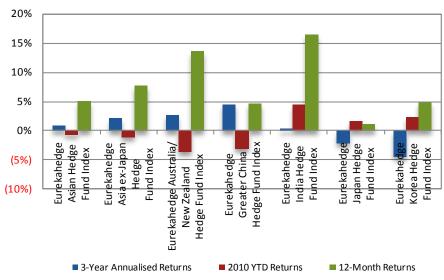
Source: Eurekahedge





Geographical Mandates

Figure 14: Performance of Asian Hedge Funds across Geographic Mandates



Source: Eurekahedge

Looking at the performance by regional mandates, India-focused hedge funds are the top performers in 2010 as well as over the last 12 months. The Eurekahedge India Hedge Fund Index returned 4.45% July YTD (which is 2.1% more than the Indian SENSEX Index) and delivered gains of 16.4% since July 2009. Most of the Indian hedge funds are long/short equities as shown in the graph. The managers have not only been able to capture the upside in the markets, they have also protected capital through the volatility of 2010.

The other two regional mandates that performed positively this year are Korea- and Japan-focused funds, which have achieved healthy returns of 2.3% and 1.6%, respectively, (July YTD). Japanese long/short equity managers, who form the bulk of the Eurekahedge Japan Hedge Fund Index, have performed especially well this year, beating the benchmark Nikkei 225 Index by 11.1%.

Over the longer time period, Greater China hedge funds dominate the landscape. Their stellar performances in 2007 (up 55.7%) and 2009 (up 45%) compensated for the 25.9% loss in 2008 and also for the subdued returns this year. Overall, managers investing in Greater China have performed exceptionally well over the past decade. Excellent growth and strong economic fundamentals have created an extra depth of liquidity in the region, giving hedge fund managers more opportunities to profit using various trading styles. The Eurekahedge Greater China Hedge Fund Index has gained a massive 736% since its inception.





Table 8: Performance across Asian Geographic Mandates

	EH Asian Hedge Fund Index	EH Australia / New Zealand Hedge Fund Index	EH Greater China Hedge Fund Index	EH India Hedge Fund Index	EH Japan Hedge Fund Index	EH Korea Hedge Fund Index
12-Month Returns	5.04%	13.57%	4.62%	16.43%	1.10%	4.76%
3-Year Annualised Returns	0.82%	2.67%	4.52%	0.32%	-2.20%	-4.46%
3-Year Annualised Standard Deviation	10.95%	11.86%	16.34%	26.14%	7.52%	12.26%
2010 YTD Returns	-0.74%	-3.56%	-3.08%	4.45%	1.61%	2.28%
2009 Returns	26.71%	41.52%	45.31%	53.62%	7.17%	9.47%

Strategic Mandates

14%

12% 10% 8% 6% 4% 2% 0% (2%) istressed Debt Hedge Driven Hedge Fund Index Eurekahedge Asia Long/ Arbitrage Hedge Fund Eurekahedge Asia Fixed Income Hedge Fund Eurekahedge Asia CTA Eurekahedge Asia Event Short Equities Hedge Strategy Hedge Fund **Eurekahedge Asia** Eurekahedge Asia Hedge Fund Index Eurekahedge Asia Mac **Eurekahedge Asia Mul** (4%)Hedge Fund Index **Fund Index Fund Index**

■ 2010 YTD Returns

■ 12-Month Returns

Figure 15: Asian Hedge Fund Performance (Strategies)

Source: Eurekahedge

■ 3-Year Annualised Returns

Most strategic mandates across the Asian hedge fund space have witnessed broad gains in 2010 July YTD. Managers deploying trades in the fixed income space are the best performers so far in the year, with distressed debt hedge funds leading the way. In the first seven months of 2010, the Eurekahedge Asia Distressed Debt Hedge Fund Index has gained 6.15% - which is twice as much as what the same group of hedge funds returned for the whole of 2009 - primarily due to a positive outlook on emerging market debt. Distressed debt investing is also the most profitable hedge fund strategy worldwide in 2010 and investors have injected more capital into distressed debt hedge funds than any other strategy.





Asian fixed income hedge funds have also fared well in 2010 - the Eurekahedge Asian Fixed Income Hedge Fund Index is up 4.6% this year. Top performing fixed income themes have been those focused on high-yielding issues while the funds utilising leverage to amplify their gains have also delivered excellent returns. Comparing the returns of fixed income hedge funds across the globe, Asia ex-Japan fixed income hedge funds are the top performers with double-digit YTD gains of 11.3%.

Long/short equity is the only negative Asian strategy in 2010, primarily due to the unpredictable volatility seen in the underlying equity markets. Since long/short equity managers form the bulk of Asian hedge funds on an equally weighted basis, their negative returns have also pulled the overall sector performance into the red. However, hedge funds have still outperformed the underlying markets in the year - the Eurekahedge Asian Hedge Fund Index is down 0.43% as opposed to a -1.12% loss in the MSCI Asia Pacific Index (July YTD).

Table 9: Performance across Asian Strategic Mandates

	EH Asia Arbitrage Hedge Fund Index	EH Asia CTA Hedge Fund Index	EH Asia Distressed Debt Hedge Fund Index	EH Asia Event Driven Hedge Fund Index	EH Asia Fixed Income Hedge Fund Index	EH Asia Long/Short Equities Hedge Fund Index	EH Asia Macro Hedge Fund Index	EH Asia Multi- Strategy Hedge Fund Index
12-Month Returns	4.17%	4.36%	11.57%	9.66%	11.97%	4.15%	4.81%	3.96%
3-Year Annualised Returns	3.48%	13.21%	1.43%	4.74%	5.15%	-0.29%	4.05%	1.53%
3-Year Annualised Standard Deviation	5.69%	6.18%	4.60%	8.93%	8.19%	11.83%	5.12%	8.74%
2010 YTD Returns	0.98%	0.23%	6.15%	3.89%	4.56%	-1.97%	1.52%	-0.20%
2009 Returns	14.68%	18.40%	3.06%	24.05%	21.45%	27.88%	14.25%	19.86%