



India-focused Hedge Funds in for Long Haul

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It is no secret that emerging markets hedge funds, specifically those focused on India, fell from their apex last year and took a beating along with the rest of the industry. Funds of all strategies and sizes dropped between 28% and 88% during the course of the year.

However, hedge fund managers who lived through the carnage of 2008 say that there are brighter days ahead in India for those investors willing to ride out the storm.

Nowhere to Hide

Ridaa Murad, co-founder of the Veda Multi-Strategy India Fund, a fund of hedge funds which launched in September, said managers who suffered the most last year were the ones with the large side pocket investments because, "when the liquidity crunch came, they were in no position to do anything with those (side pockets)."

Real estate was also a tough space to be in; and quite a few funds with either direct exposure to land acquisitions or to publicly-listed companies also suffered drawdowns, according to Murad. Another strategy that fared poorly was private equity in the public markets (ie having long-term investments in public companies), which worked really well in 2007 but was hammered because holdings that were not listed on the index and could not be hedged, were sold without any regard for valuations.

Murad's own fund lost 26.52% through December, compared to the BSE 500 Index, which was down 68.8% for the year. Firm co-founder Bradford Matthews said while the firm is not happy about the negative returns, given the market dislocation, he believes the fund has done what it set out to do: Give investors returns from multi-asset classes while experiencing 50% less of the downside volatility than the index, while at the same time capturing a disproportionate amount of the upside volatility.

Changes? What Changes?

Going forward, Murad foresees an increase in India-focused long-biased funds for investors who want index-plus exposure, more long/short portfolios geared toward typical hedge fund investors, and more hybrid private equity/hedge fund products for endowment type investors.

For its part, Murad said the firm isn't making any changes to its portfolio, which houses direct lending, debt lending, convertible arbitrage and distressed debt. It is also keeping its fees the same – 1% for management and 10% for incentives. The fund has a 1-year lockup with quarterly liquidity thereafter. Up to one-fifth of the fund can be invested in non-liquid assets.

Buy and Hold On

"We told our investors that if they're not looking to invest in India for three years, then they shouldn't put money there at all," said Murad, who admitted that finding new investors is very hard because they have lost faith in the region and are sitting on the sidelines.

Gautam Prakash, founder of Bethesda, Md-based Monsoon Capital, echoes Murad's sentiments.

"India was more the flavour of the day for these investors in previous years and they tended to buy high and sell low when they should have been doing the opposite," said Prakash. "Looking at month-to-month returns in India may not be wise. We remain bullish on the 10-year picture of where India's going."

Prakash declined to comment on Monsoon's performance but said export-oriented companies and infrastructure companies generally fared poorly last year. The firm runs a liquid private equity strategy, a real estate private equity fund and a hedge fund.



"The Indian mid-cap market was down some 75% in dollar-terms last year, so almost everything was down," said Prakash. "The other factor impacting the firm's performance was the rupee's depreciation against the dollar."

This year, Prakash said Monsoon is taking a more defensive posture by reducing its gross exposure to export-oriented companies, focusing more on liquid names in the mid-cap space.

This article was first published in VC Circles' Deal Outlook 2009, which focuses on dealmakers and investment in India.

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