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The Hedge Fund Report Card

SOME FORMERLY INVESTOR-UNFRIENDLY FIRMS HAVE GROWN UP — AND THEY'VE GOT NEW, IMPROVED GRADES TO SHOW FOR IT.

By Stephen Taub

ILLUSTRATIONS BY NOMA BAR

After

founding his London-based hedge fund firm, The Children's Investment Fund Management U.K., in 2003, Christopher Hohn quickly earned a reputation for producing outstanding returns. But he later also became known for alienating his investors.

Hohn racked up annualized gains of roughly 40 percent in his firm's main fund during its first four years and built the firm, known as TCI, up to $19 billion in assets at its peak, in May 2008, with a staff that included 12 analysts. But after the fund posted a 43.1 percent loss that year, many of Hohn's investors — who were unhappy with the fund's unusually severe three- and five-year lockups — began fleeing en masse as their terms expired. By the end of 2012, assets had shrunk to $4.9 billion in the main fund, even though it posted an impressive 29.5 percent gain that year. Investors weren't the only ones eager to escape the firm: From 2009 to 2011 several analysts and the head of investor relations also left.

"We had strayed from being heavily invested in stocks with a high barrier to entry and a bulletproof franchise to weaker industries," Hohn now concedes. "Then we weren't fully invested in 2009. The team and the fund got too large."

So in early 2013, when *Alpha* published its annual Hedge Fund Report Card, in which investors are asked to grade hedge fund managers on a variety of factors, it wasn't shocking to see TCI ranked near the bottom, with an F grade. But by then Hohn had been working assiduously to turn things around. He had shrunk his group of analysts and began rewarding them as a team rather than on individual performance. He had hired a new head of investor relations, slashed fees, significantly loosened liquidity terms for investors and hit the road for a prolonged series of meetings with investors. For the first time in years, clients had access to TCI's investment team, and the firm set up a new online portal containing presentations and details about the fund's investments.

By the second half of 2013, Hohn began to see results. His fund gained about 14.5 percent in the fourth quarter alone, finishing the year up 47 percent, net of fees. Finally, after four years of no new money coming in, TCI was growing. By year-end 2014 its assets had jumped to $8.7 billion.

Clearly, investors took notice: TCI finishes in seventh place in *Alpha*'s annual Hedge Fund Report Card — up from No. 53 just two years ago — and is one of only 14 firms to earn an A grade. What's more, TCI earns an A in five of the eight individual categories on which investors were asked to rate their managers, gaining the No. 1 spot in two of those, Alignment of Interests and Transparency. Most important, peformance bounced back after 2008, with the firm's main fund posting annualized gains of 19.2 percent over the past five years. (TCI was up 8.9 percent in 2014.) "They have restructured, and their results are better," says a prominent hedge fund investor. "Hohn is one of the best equity investors in the world."

KEY FACTORS WHEN EVALUATING A HEDGE FUND

Scale: 1 to 10 (10 = most important)

RANK	FACTORS	SCORE
1	Alpha Generation	9.11
2	Risk Management	8.64
3	Alignment of Interests	8.57
4	Transparency	7.73
5	Infrastructure	7.28
6	Liquidity Terms	7.25
7	Independent Oversight	7.22
8	Investor Relations	6.44

Each year we ask pension funds, endowments, foundations, funds of funds and other institutional investors to rate the firms in our annual Hedge Fund 100 ranking of the world's largest hedge funds. (Only investors that had money in the 100 hedge funds in the 12 months before polling are surveyed.) Thanks to a strong response among investors surveyed, we were able to rank and grade 58 firms this year, up from 47 in 2014. (For more information on the methodology, see "How We Compiled the Rankings," page 22.)

TCI is one of several firms ranking near the top of this year's Hedge Fund Report Card that previously were among the most opaque in the hedge fund industry, especially before the financial crisis. Other examples include Chicago-based Citadel, which finishes third overall; Evanston, Illinois–based Magnetar Capital (No. 4); and three New York–based firms, Perry Capital (No. 5), Millennium Management (No. 6) and Two Sigma (No. 14). These were among the many firms that until the financial crisis felt it was a badge of honor — perhaps even a sign of success — to keep most information close to the vest.

This year's results underscore the continued institutionalization of the hedge fund industry. As firms have evolved from investing for wealthy individuals to managing money on behalf of public workers' pensions, endowments and charities, they have recognized the need to become much more accountable and responsive, investors say. This has meant implementing elaborate risk management systems and generally paying more attention to nonperformance-related areas, such as investor relations. These investments are reflected in the firms' improved standings in the Hedge Fund Report Card since the survey's launch in 2009.

Multistrategy giant Citadel exemplifies the shift toward more-investor-friendly policies. "We need to stay focused and provide what they need to report to their constituents," acknowledges Kenneth Griffin, Citadel's founder and chief executive.

But an additional factor has been driving hedge funds to better communicate with their clients and provide more detailed information: underperformance. In recent years the average hedge fund has regularly lagged various market indexes. Judith Posnikoff, a co-founder of Irvine, California–based fund-of-funds firm Pacific Alternative Asset Management Co., says that before 2008 no one talked about non-performance-related issues. The financial crisis changed that.

"I think performance is critically important," Posnikoff explains. "But I will pass on a top-decile fund for a fund with more-flexible and better terms and more transparency."

This year marks the first time that a non-U.S. firm — London-based Egerton Capital — has topped the Hedge Fund Report Card. Egerton, founded in 1994 by John Armitage and now-retired former Tiger Cub William Bollinger, has quietly become one of the best hedge fund firms few people know. Armitage "has never been a household name," says one hedge fund investor.

Egerton posted double-digit gains, ranging between 20 and 45 percent, in each of its first full six years. And in nearly 21 years, the firm has had only two losing years: 2008 and 2011. Egerton started to gain notice in the investment community in 2013, when its long-short fund returned 27.7 percent and its assets under management nearly doubled, to $13.2 billion. At the beginning of 2014, Egerton was the world's 43rd-largest hedge fund firm, up from No. 74 the year before. Today it manages $13.7 billion, according to its website.

Egerton's investors appear to be extremely satisfied. The firm is one of just three to receive A grades in seven of the eight Hedge Fund Report Card categories. (The other two are Silver Point Capital and Magnetar.) Egerton, which declined to comment on the results, tops the list for Liquidity Terms. It is tied with Glenview Capital Management for No. 2 for Transparency, ranks No. 3 for Investor Relations, is tied with Two Sigma for No. 3 in Risk Management and ranks No. 4 for Infrastructure.

This year Silver Point slips one notch to take second place. The Greenwich, Connecticut-based credit and distressed-debt firm, founded by Goldman Sachs Group alums Edward Mule and Robert O'Shea, earns an A in all but one category, Risk Management, in which it receives a B. "They are very good at understanding the credit markets and finding opportunities, especially opportunities not evident to a lot of the market," says one investor, who also lauds the firm for its strong investor relations team.

THE HEDGE FUND REPORT CARD 2015

RANK	FIRM (LOCATION)	WEIGHTED SCORE
GRADE A		
1	**Egerton Capital** *(London, U.K.)*	86.60
2	**Silver Point Capital** *(Greenwich, CT)*	86.19
3	**Citadel** *(Chicago, IL)*	85.13
4	**Magnetar Capital** *(Evanston, IL)*	84.39
5	**Perry Capital** *(New York, NY)*	84.06
6	**Millennium Mgmt** *(New York, NY)*	83.95
7	**The Children's Investment Fund Mgmt U.K.** *(London, U.K.)*	83.45
8	**Glenview Capital Mgmt** *(New York, NY)*	83.14
9	**Elliott Mgmt Corp.** *(New York, NY)*	81.93
10	**Canyon Capital Advisors** *(Los Angeles, CA)*	81.86
11	**Fir Tree Partners** *(New York, NY)*	81.78
12	**Adage Capital Mgmt** *(Boston, MA)*	81.13
13	**HBK Capital Mgmt** *(Dallas, TX)*	81.09
14	**Two Sigma** *(New York, NY)*	81.08
GRADE B		
15	**Senator Investment Group** *(New York, NY)*	80.89
16	**Davidson Kempner Capital Mgmt** *(New York, NY)*	79.44
17	**King Street Capital Mgmt** *(New York, NY)*	79.39
18	**Farallon Capital Mgmt** *(San Francisco, CA)*	79.23
19	**Highfields Capital Mgmt** *(Boston, MA)*	78.90
20	**Tudor Investment Corp.** *(Greenwich, CT)*	78.80
21	**Cerberus Capital Mgmt** *(New York, NY)*	78.67
22	**Bridgewater Associates** *(Westport, CT)*	78.28
23	**Wellington Hedge Mgmt** *(Boston, MA)*	78.27
24	**GSO Capital Partners** *(New York, NY)*	78.19
25	**York Capital Mgmt** *(New York, NY)*	78.10
26	**Marshall Wace** *(London, U.K.)*	77.98
27	**Viking Global Investors** *(Greenwich, CT)*	77.97
28*	**Maverick Capital** *(Dallas, TX)*	77.38
29*	**Pershing Square Capital Mgmt** *(New York, NY)*	77.38
GRADE C		
30	**Anchorage Capital Group** *(New York, NY)*	76.67
31	**Visium Asset Mgmt** *(New York, NY)*	76.60
32	**Winton Capital Mgmt** *(London, U.K.)*	76.59
33*	**Och-Ziff Capital Mgmt Group** *(New York, NY)*	76.48
34*	**BlackRock** *(New York, NY)*	76.48
35	**Third Point** *(New York, NY)*	76.25
36	**D.E. Shaw & Co.** *(New York, NY)*	75.89
37	**Jana Partners** *(New York, NY)*	75.01
38	**Taconic Capital Advisors** *(New York, NY)*	74.92
39	**Pennant Capital Mgmt** *(Summit, NJ)*	74.64
40	**ValueAct Capital Partners** *(San Francisco, CA)*	74.59
41	**Angelo, Gordon & Co.** *(New York, NY)*	73.49
42	**Pine River Capital Mgmt** *(Minnetonka, MN)*	73.15
43	**MKP Capital Mgmt** *(New York, NY)*	72.63
44	**Pacific Investment Mgmt Co.** *(Newport Beach, CA)*	72.26
45	**AQR Capital Mgmt** *(Greenwich, CT)*	72.23
46	**Lone Pine Capital** *(Greenwich, CT)*	71.28
GRADE D		
47	**Caxton Associates** *(New York, NY)*	70.07
48	**Avenue Capital Group** *(New York, NY)*	68.88
49	**Eton Park Capital Mgmt** *(New York, NY)*	68.75
50	**Fortress Investment Group** *(New York, NY)*	68.50
51	**Brevan Howard Asset Mgmt** *(London, U.K.)*	67.19
52	**Discovery Capital Mgmt** *(South Norwalk, CT)*	66.63
53	**Paulson & Co.** *(New York, NY)*	66.40
54	**Greenlight Capital** *(New York, NY)*	66.08
GRADE F		
55	**Cevian Capital** *(London, U.K.)*	65.69
56	**Mason Capital Mgmt** *(New York, NY)*	61.19
57	**Convexity Capital Mgmt** *(Boston, MA)*	60.29
58	**BlueCrest Capital Mgmt** *(London, U.K.)*	55.76

* Tie due to rounding, not an actual tie.

Citadel moves up from fifth place last year. It earns an A in six categories, a B for Transparency and a C for Liquidity Terms. The firm, founded by Griffin in 1990, has clearly placed its disastrous 2008 in the distant past. "We are in the business of creating alpha for our investors," Griffin stresses. "If you can't do that, you aren't providing what is fundamentally important."

Griffin also attributes his firm's rebound to risk management lessons learned from 2008, especially in regard to the repricing

of funding. He explains that from 2003 to 2007 Citadel took advantage of low funding rates to build a portfolio, which included convertible securities and high-yield debt, that suddenly became very expensive to unwind in 2008. "The portion of our portfolio that is tied to the price of finance is now far, far smaller," Griffin says.

As a result, Citadel's CEO insists that his firm would be in a very different position if another 2008-style liquidity crisis erupted. "Portfolio managers know where risk lies," he explains. "P&L attributes are like radar in a plane in a fog-filled night. In a downdraft [portfolio managers] know where they are and can get where they need to be."

After receiving a B in last year's ranking, Magnetar, founded by Citadel alumnus Alec Litowitz, returns to the near-top of the rankings this year — despite what one manager calls headline risk for its controversial role during the mortgage crisis, when regulators investigated its mortgage-trading activities. However, most investors, as well as regulators, have moved beyond the issue. The firm earns an A in all but one category, Alignment of Interests, where it receives a B.

Magnetar says generating consistent alpha across a variety of market conditions is the most important objective for the firm as it tries to achieve what it calls idiosyncratic returns. It also aims to build a strong risk management team; at the same time, it tries to match the liquidity requirements of each of its funds with their underlying assets, as part of alpha generation. Last, the firm emphasizes the need for a strong infrastructure to support all that.

"To be a robust firm, you need to build out a well-structured investment platform and infrastructure and engage with investors," Magnetar co-founder and president Ross Laser says in an e-mail. "From day one, it has been in our core DNA to build businesses, not trades."

Perry Capital rounds out the top five. This year the firm received an A in six of eight categories, including Investor Relations, where it topped all managers. Richard Perry, a former risk arbitrageur at Goldman, Sachs & Co., has transformed his firm from one betting on merger deals to one that is more of a special-situations maven. He also has slowly emerged from the shadows — speaking, for example, at the Delivering Alpha conference cohosted by Institutional Investor and CNBC.

"He has built a good firm," says one admiring investor. Although this client is concerned that Perry sometimes winds up in the society pages, given his firm's investment returns most investors don't seem bothered. The Perry Partners International fund lost more than 3 percent last year but posted double-digit gains in each of the previous two years.

TCI, Citadel and Magnetar aren't the only prominent hedge fund firms to learn serious lessons from the financial crisis. Before the global meltdown Two Sigma also seemed to take its investors for granted. All the firm provided to investors were its performance results, with no additional detail on portfolio construction or positions. So despite being up as much as 8 percent in some funds in 2008, Two Sigma suffered substantial redemptions the following year.

Former D.E. Shaw & Co. colleagues John Overdeck and David Siegel, who founded Two Sigma in 2001, began to seriously focus not only on serving clients better but on diversifying the firm's mix of investors. It looked to attract more institutional investors, such as pension funds, endowments and sovereign wealth funds, which typically have longer investment horizons than high-net-worth investors. Two Sigma began working hard to reach out to its investors, spending more on investor relations, infrastructure and risk management. These days the firm hosts a client conference each year, attended by dozens of its more than 700 employees.

It took a while, but investors have rewarded Two Sigma's effort. The firm jumps 12 spots in the Hedge Fund Report Card overall ranking, to No. 14, just making the A grade cutoff. The firm also grabs the top spots for Alpha Generation and Infrastructure and is tied for No. 3 for Risk Management. In last year's survey Two Sigma received a C overall, as well as an F for both Alignment of Interests and Independent Oversight and a D for Transparency.

Four firms — BlueCrest Capital Management, Cevian Capital, Convexity Capital Management and Mason Capital Management — receive an F overall and also take the lowest grades in many individual categories.

Mason Capital, a New York–based activist hedge fund firm founded in 2000 by former KS Capital Partners portfolio manager Kenneth Garschina and ex-Oppenheimer & Co. arbitrageur

Michael Martino, scores an F in six of the eight individual categories. Late last year the Rhode Island State Investment Commission, which manages a $7 billion public pension fund, confirmed it was pulling its $61.8 million investment in Mason, according to a report in the *Providence Journal*. The newspaper noted that the value of Rhode Island's Mason investment rose by an annual average of just 1.02 percent. "Over the three years the SIC has been invested, the fund has exhibited less return for the risk taken than expected given its prior track record," spokeswoman Ashley Gingerella-O'Shea said in a statement.

Boston-based Convexity Capital, a secretive hedge fund firm founded by former Harvard Management Co. CEO Jack Meyer, David Mittelman and Maurice Samuels in July 2005, receives an F in four individual categories. The firm, which uses complex relative-value and fixed-income-oriented strategies to try to beat a targeted benchmark, has been struggling for several years, with the founders telling clients it fares best during periods of high volatility. In mid-2013, Convexity's management team notified investors that it would not take any additional money until its performance improved.

London-based BlueCrest Capital gets an F in six individual categories. Founded in 2000 by former J.P. Morgan derivatives trader Michael Platt and William Reeves — the latter subsequently retired — it ranked as the fifth-largest hedge fund firm in the world at the beginning of 2014, with $32.6 billion, although that was down from $35.3 billion the previous year. In 2013 the firm was hurt in part by its systematic BlueTrend fund, which lost 11.4 percent in what was a tough year for many computer-driven hedge funds.

However, like others of its ilk, the BlueTrend fund rebounded in 2014, returning 12.7 percent. At the end of last year, BlueCrest spun off its computer-driven hedge funds into a new firm, Systematica Investments, which has more than $10 billion under management, according to a regulatory filing. It is led by Leda Braga, BlueCrest's former head of systematic trading.

London-based Cevian Capital gets an F in two categories, Liquidity Terms and Risk Management. Cevian's assets surged nearly 45 percent last year, to $13.3 billion, making the activist firm the tenth-largest hedge fund in Europe. It was founded in 2002 by former Custos alumni Christer Gardell, who served as chief executive at the Swedish investment bank from 1996 to 2001, and Lars Förberg, who was CIO there from 1998 to 2001. Two years ago Cevian earned two A grades, ranking third in Independent Oversight and seventh in Alignment of Interests, although it received an overall grade of C. Last year the firm did not receive enough votes to qualify for the ranking.

> "I think performance is critically important. But I will pass on a top-decile fund for a fund with more-flexible and better terms and more transparency."
>
> *Judith Posnikoff, Pacific Alternative Asset Management Co.*

Each year investors rank the eight attributes on which they are asked to vote. Once again voters rate Alpha Generation the most important factor when selecting a hedge fund. But managers define alpha differently. For example, Larry Robbins's New York–based Glenview Capital, which finishes fifth in this category, in a tie with Silver Point, thinks of alpha generation in terms

ALPHA GENERATION

RANK*	FIRM (LOCATION)	SCORE	GRADE
TOP 5			
1	Two Sigma *(New York, NY)*	9.50	A
2	Citadel *(Chicago, IL)*	9.30	A
3	Adage Capital Mgmt *(Boston, MA)*	9.17	A
4	Viking Global Investors *(Greenwich, CT)*	9.05	A
5	Glenview Capital Mgmt *(New York, NY)*** Silver Point Capital *(Greenwich, CT)***	9.00	A
BOTTOM 5			
53	Avenue Capital Group *(New York, NY)*** Caxton Associates *(New York, NY)*** Maverick Capital *(Dallas, TX)***	5.50	D
56	Mason Capital Mgmt *(New York, NY)*	5.43	F
57	BlueCrest Capital Mgmt *(London, U.K.)*	4.80	F
58	Convexity Capital Mgmt *(Boston, MA)*	3.83	F

* The full list is available at institutionalinvestorsalpha.com **Actual tie

RISK MANAGEMENT

RANK*	FIRM (LOCATION)	SCORE	GRADE
TOP 5			
1	Millennium Mgmt *(New York, NY)*	9.36	A
2	Elliott Mgmt Corp. *(New York, NY)*	9.03	A
3	Egerton Capital *(London, U.K.)*** Two Sigma *(New York, NY)***	8.86	A
5	Citadel *(Chicago, IL)*	8.84	A
BOTTOM 5			
54	Avenue Capital Group *(New York, NY)*** Discovery Capital Mgmt *(South Norwalk, CT)***	6.43	D
56	Mason Capital Mgmt *(New York, NY)*	5.71	F
57	Paulson & Co. *(New York, NY)*	5.67	F
58	Cevian Capital *(London, U.K.)*	5.40	F

* The full list is available at institutionalinvestorsalpha.com **Actual tie

of its ability to meet a yearly absolute-return target — in its case, 15 percent.

However, investors and allocators don't just want to see statistics. They want managers to articulate how they generate alpha. "I want to hear a clear philosophy for how they make their money," says Francis Frecentese, director of hedge funds at Bessemer Trust, a New York–based wealth management firm. "I want to hear a clear mission statement. I want it thought out what they do."

Risk Management is the second most important issue for investors. And if there is one person who's had to learn from risk management mistakes, it is Citadel's Griffin. However, the firm's investors seem to share Griffin's belief that Citadel has completely revamped its risk management profile: The firm receives an A in this category, ranking fifth.

Israel (Izzy) Englander's Millennium takes the top spot in Risk Management. "Millennium has a fundamentally tried-and-true risk process, which allows them to bring in many people," says one hedge fund investor. The multistrategy firm is known for its 150 individual trading teams.

"All I care about is how much risk is utilized and the return you are getting for it," says Charles Krusen, founder and CEO of Krusen Capital Management, a New York registered investment adviser that advises clients on alternative investments, including hedge funds and private equity.

Apparently, so does Paul Singer, founder of New York–based Elliott Management Corp.: He is said to regularly tell employees that the firm's objective is to not lose money. Elliott consistently tries to measure how much it can lose on a given investment. "We try to hedge or eliminate risk we can't control," says chief marketing officer Jaime Hobbeheydar. Elliott is second in Risk Management.

On the other hand, TCI received a D — its only poor grade in any of the categories — for Risk Management. Perhaps this reflects the firm's penchant for running a very concentrated portfolio, which now holds just ten to 12 meaningful stock positions. It is not uncommon for Hohn to take huge stakes in one company, such as when he devoted 18 percent of his assets to Airbus at the beginning of 2013. The stock wound up surging 92 percent that year. "We take risk and don't hedge it away," Hohn declares. "We don't hide it, don't apologize for it, and we understand it is not the taste for everybody."

John Paulson's New York–based Paulson & Co. is one of three firms that get an F in Risk Management. This may reflect the fact that the firm suffered steep losses in most of its funds in 2014 — its second lousy year since it posted triple-digit gains in 2007.

One prominent hedge fund investor says that before Paulson's seminal gains in 2007, which cemented the manager as a billionaire, his firm was much more risk-conscious. "Now it is about getting the option right," the investor says. "He's looking for a big hit. Some people feel managers don't take enough risk. But they must size it right."

Alignment of Interests, the third most important attribute, is a tricky issue. Most investors say they want to see the bulk of the net worth of the managers and their top people invested in the fund. Glenview's Robbins has 100 percent of his investable liquid net worth in his funds, and 22 percent of the firm's capital is internal money. Robbins even wants his employees to share this alignment of interests, so he pays all of them a base salary, as well as a discretionary bonus and profit-sharing units, which represent compensation directly tied to the net returns of the funds. "We like to say we are partners looking for co-partners," says Elizabeth Perkins, a partner and the firm's investor relations chief. Glen-

ALIGNMENT OF INTERESTS

RANK*	FIRM (LOCATION)	SCORE	GRADE
TOP 5			
1	**The Children's Investment Fund Mgmt U.K.** *(London, U.K.)*	9.36	*A*
2	**Glenview Capital Mgmt** *(New York, NY)*** **Taconic Capital Advisors** *(New York, NY)***	9.00	*A*
4	**Highfields Capital Mgmt** *(Boston, MA)*	8.89	*A*
5	**Pennant Capital Mgmt** *(Summit, NJ)*	8.88	*A*
BOTTOM 5			
53	**Convexity Capital Mgmt** *(Boston, MA)*** **Pacific Investment Mgmt Co.** *(Newport Beach, CA)***	6.33	*D*
55	**Brevan Howard Asset Mgmt** *(London, U.K.)*	6.31	*F*
56	**Fortress Investment Group** *(New York, NY)*	6.23	*F*
57	**Discovery Capital Mgmt** *(South Norwalk, CT)*	6.14	*F*
58	**BlueCrest Capital Mgmt** *(London, U.K.)*	3.90	*F*

* The full list is available at institutionalinvestorsalpha.com   **Actual tie

TRANSPARENCY

RANK*	FIRM (LOCATION)	SCORE	GRADE
TOP 5			
1	**The Children's Investment Fund Mgmt U.K.** *(London, U.K.)*	9.07	*A*
2	**Glenview Capital Mgmt** *(New York, NY)*** **Egerton Capital** *(London, U.K.)***	8.86	*A*
4	**ValueAct Capital Partners** *(San Francisco, CA)*	8.83	*A*
5	**Perry Capital** *(New York, NY)*	8.50	*A*
BOTTOM 5			
54	**Caxton Associates** *(New York, NY)*	5.88	*D*
55	**Greenlight Capital** *(New York, NY)*	5.80	*F*
56	**Mason Capital Mgmt** *(New York, NY)*	5.43	*F*
57	**Convexity Capital Mgmt** *(Boston, MA)*	5.33	*F*
58	**BlueCrest Capital Mgmt** *(London, U.K.)*	4.10	*F*

* The full list is available at institutionalinvestorsalpha.com   **Actual tie

INFRASTRUCTURE

RANK*	FIRM (LOCATION)	SCORE	GRADE
TOP 5			
1	**Two Sigma** *(New York, NY)*	9.57	*A*
2	**Citadel** *(Chicago, IL)*	9.51	*A*
3	**Bridgewater Associates** *(Westport, CT)*	9.21	*A*
4	**Egerton Capital** *(London, U.K.)*	9.14	*A*
5	**Millennium Mgmt** *(New York, NY)*	9.12	*A*
BOTTOM 5			
54	**Avenue Capital Group** *(New York, NY)*	7.14	*D*
55	**Greenlight Capital** *(New York, NY)*	7.00	*F*
56	**Paulson & Co.** *(New York, NY)*	6.83	*F*
57	**BlueCrest Capital Mgmt** *(London, U.K.)*	6.80	*F*
58	**Mason Capital Mgmt** *(New York, NY)*	6.29	*F*

*The full list is available at institutionalinvestorsalpha.com

INDEPENDENT OVERSIGHT

RANK*	FIRM (LOCATION)	SCORE	GRADE
TOP 5			
1	**Fir Tree Partners** *(New York, NY)*	8.80	*A*
2	**Silver Point Capital** *(Greenwich, CT)*	8.73	*A*
3	**Millennium Mgmt** *(New York, NY)*	8.71	*A*
4	**Citadel** *(Chicago, IL)*	8.68	*A*
5	**Perry Capital** *(New York, NY)*	8.50	*A*
BOTTOM 5			
54	**Pacific Investment Mgmt Co.** *(Newport Beach, CA)*	6.67	*D*
55	**Brevan Howard Asset Mgmt** *(London, U.K.)*	6.53	*F*
56	**Greenlight Capital** *(New York, NY)*	6.29	*F*
57	**Mason Capital Mgmt** *(New York, NY)*	5.71	*F*
58	**BlueCrest Capital Mgmt** *(London, U.K.)*	5.50	*F*

*The full list is available at institutionalinvestorsalpha.com

view is tied with New York–based Taconic Capital Advisors for second place in this category, trailing only TCI.

Transparency is the fourth most important factor among investors. PAAMCO's Posnikoff says her firm always demands position-level data; that way she knows precisely how her overall portfolio will be affected when she adds a new manager.

These days managers not only provide quarterly reports and discussions of their portfolio holdings, they send out monthly spreadsheets detailing overall exposures, in some cases by geography and industry. Some hold quarterly conference calls with top investors.

This is good enough for many investors, including Jonathan Hook, CIO of the Harry and Jeanette Weinberg Foundation, an Owings Mills, Maryland–based nonprofit that provides grants to organizations that help the needy. "We want to know where the general exposures are," explains Hook, who joined the $2 billion foundation last April after serving as CIO of Ohio State University. "Daily position exposure is too much information for our staff." Rather, Hook wants what he calls factor analysis: knowing where the biggest risks are.

For their part, many managers are reluctant to provide too much

> "The portion of our portfolio that is tied to the price of finance is now far, far smaller."
>
> *Kenneth Griffin, Citadel*

detail, especially if they are invested in assets other than highly liquid equities. "As we move to more-liquid assets, we are able to provide more transparency," says Citadel's Griffin. But, he adds, if a manager provides too much detail about its individual positions and stumbles, "other trading firms can take advantage of you."

Elliott keeps investors apprised of its major positions and the types of risks it is taking in its lengthy quarterly letters. The firm also provides monthly exposure reports. But Hobbeheydar says: "We don't make our entire portfolio available on our website. Even big positions are occasionally referred to in a descriptive way." Some managers — and investors — concede that if a manager did provide daily disclosures of individual trades, the investor would not know what to do with all of this information.

A top-rated firm must have top-notch infrastructure — at least, that seems to be what investors are saying given that most of the firms that receive an A overall in the Hedge Fund Report Card also get an A in the Infrastructure category. "Infrastructure is very important," stresses Mike Hennessy, co-founder of Chapel Hill, North Carolina–based investment adviser Morgan Creek Capital Management. Things can go wrong, so you want to make sure a firm has an "impeccable back and front office" with a separation of duties, he says.

In fact, investors want to be able to gauge the stability, and indeed the survivability, of the overall firm. PAAMCO's Posnikoff, for example, looks at the asset-raising experience of the hedge fund firm, and its expenses, then creates a mock business plan to determine its break-even point. She wants to know whether a manager needs to "hit the ball out of the park" to generate performance fees to support the overall firm's expense base.

Though not at the top of the list of important attributes, Liquidity Terms are still critical, as well as a tricky issue. Yet many managers, especially shareholder activists and those running less-liquid portfolios, have instituted two- and three-year lock-ups. Several funds even have five-year lock-ups.

Hennessy, however, says "liquidity is on us." He emphasizes that investors such as his firm should make sure the lock-up and redemption terms match the overall strategy of the fund. For example, many investors understand that certain strategies, such as credit, need a longer lock-up, but they doubt that many long-short equity strategies need more than the standard one-year lock-up and 30-day or quarterly notification for redemptions. Indeed, Citadel, which receives a C in this category, reduced its lock-up period as its portfolio became more liquid.

After 2008, Glenview — which this year receives a B for Liquidity Terms— cut its two-year lock-up to one year and maintained its quarterly liquidity. In 2013 it went to a soft one-year lock-up, meaning there is a penalty if an investor redeems in the first year.

Although several investors question why an activist needs a multiyear lock-up, investors like the Weinberg Foundation's Hook are willing to talk: "If you need something out of the ordinary, explain it to us." In general, he says he has no hard-and-fast rule in this area, but he stresses that he wants to know he has the same terms and fees as everyone else in the fund. "I'd rather be in a fund where everyone is treated the same," he adds.

Interestingly, three of the four firms that rank at the top in this category are based in London: Egerton, Winton Capital Management and Marshall Wace. Elliott is the only firm with an overall A grade that scores poorly in this category. "We probably have less liquidity than other funds," concedes Hobbeheydar. "We have longer lock-ups and restrictions on redemptions." But he points out that Elliott's terms are aligned with its liquidity profile. For example, the fund has an initial two-year lock-up, then it has sliding fees depending upon the liquidity the investor chooses.

> "We take risk and don't hedge it away. We don't hide it, don't apologize for it, and we understand it is not the taste for everybody."
>
> *Christopher Hohn, The Children's Investment Fund Management U.K.*

Independent Oversight is ranked next to last among the eight attributes, and investors interviewed about the survey appeared to have few concerns in this area. Perhaps it is assumed that all of these firms' funds are audited by a major accounting firm or that they have quality boards of directors. In any case, the firm that ranks the highest is New York–based Fir Tree Partners, founded by Jeffrey Tannenbaum; it also receives an A overall.

Although Investor Relations ranks last among the eight categories, in some ways its importance is underestimated by many hedge fund firms. Ideally, investors want regular access to the portfolio manager, but this is not practical. Therefore it is up to the IR department not only to tell the investor when the portfolio manager is unavailable but to provide the information the investor is seeking — which could make or break the relationship.

"We have had situations where the IR person was not pleasant and we did not invest," says Weinberg's Hook. "But that is rare. IR can make other things easier, such as the due diligence process."

Citadel's Griffin personally meets his 20 largest investors each year, but he insists he is available to all others "at any time." If there is a significant news story involving the firm, he adds, "our IR team reaches out to investors to answer questions and give context around a story."

The reality is, the more time that managers spend speaking to investors, the less time they have to perform the investment tasks for which they are being paid big fees. Although Morgan Creek's Hennessy says he would like direct access to all managers in his portfolio, he concedes they can't do it for all of the limited partners. But he notes, "If they have top-notch IR people, it could be okay." a

INVESTOR RELATIONS

RANK*	FIRM (LOCATION)	SCORE	GRADE
TOP 5			
1	Perry Capital *(New York, NY)*	9.00	A
2	Silver Point Capital *(Greenwich, CT)*	8.83	A
3	Egerton Capital *(London, U.K.)*	8.71	A
4	Citadel *(Chicago, IL)*	8.68	A
5	Fir Tree Partners *(New York, NY)*	8.60	A
BOTTOM 5			
54	Cevian Capital *(London, U.K.)*	6.20	D
55	Mason Capital Mgmt *(New York, NY)*	6.14	F
56	BlueCrest Capital Mgmt *(London, U.K.)*	5.80	F
57	Lone Pine Capital *(Greenwich, CT)*	5.71	F
58	Convexity Capital Mgmt *(Boston, MA)*	4.83	F

*The full list is available at institutionalinvestorsalpha.com

LIQUIDITY TERMS

RANK*	FIRM (LOCATION)	SCORE	GRADE
TOP 5			
1	Egerton Capital *(London, U.K.)*	9.29	A
2	Winton Capital Mgmt *(London, U.K.)*	8.85	A
3	Perry Capital *(New York, NY)*	8.25	A
4	Marshall Wace *(London, U.K.)*	8.07	A
5	Canyon Capital Advisors *(Los Angeles, CA)*	8.05	A
BOTTOM 5			
54	ValueAct Capital Partners *(San Francisco, CA)*	5.67	D
55	Eton Park Capital Mgmt *(New York, NY)*	5.58	F
56	Greenlight Capital *(New York, NY)*	5.00	F
57	Convexity Capital Mgmt *(Boston, MA)*	4.83	F
58	Cevian Capital *(London, U.K.)*	4.40	F

*The full list is available at institutionalinvestorsalpha.com

HOW WE COMPILED THE RANKINGS

Investors were asked to score the funds they're invested in on eight attributes: Alignment of Interests, Alpha Generation, Independent Oversight, Infrastructure, Investor Relations, Liquidity Terms, Risk Management and Transparency. Investors also rated each of the attributes in terms of importance. The scores in the attribute categories are based on the average of the ratings for each hedge fund firm by its investors. For the overall ranking we started by calculating weighted scores for the attribute categories for each firm, using the importance ratings for those attributes. The attribute-weighted scores were added up for each firm, then divided by the total possible maximum score to come up with the overall weighted scores. A grading curve was applied to the results to arrive at the relevant letter grades.