Why hedges fund asset growth is declining

While more than 90% of industry assets have successfully transitioned into the regulated space, hedge fund industry assets under management (AUM) decreased by 9.1% year-on-year. This was the industry's first decline in AUM in over five years, which saw assets dropping to R62.2bn.

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This decline was caused by a combination of factors, such as poor fund performance, outflows and funds transitioning to the regulated environment, Eugene Visagie, head of hedge fund investments at Novare, explains.

“According to the survey findings, the main contributing factors to the decline include in-house consolidations of product offerings by asset managers and outflows due to meagre performance in the period under review,” he says. “The introduction of the new regulation caused uncertainty within the hedge fund industry, and subsequently, a few anticipative trends emerged.”

These trends include investors changing mandates and switching to either traditional long only mandates or to unique segregated mandates. as well as and the consolidation of smaller hedge funds and not classifying these funds as hedge funds. “This is done with the aim of running the fund as a private portfolio until such time that it achieves a solid track record and asset base,” he says.

Changing strategies

The decline in assets also came from bigger hedge funds, especially funds with an equity long/short bias. The strategy itself experienced a challenging year and subsequently showed the biggest withdrawals. Fund of hedge funds AUM dropped significantly by over 7%, despite historically being among the main allocators. Visagie explains that this decrease might be an indication that funds are changing strategies to include other assets, or that fund of funds also suffered from major redemptions.

A few equity long/short managers were trapped by the selloff and sector rotation at the start of 2016 resulting in very low market exposure for the rest of 2016 and 2017. Hedge fund managers also had strong views on the direction of the rand which resulted in managers failing to capitalise on the rand's strength. As the year draws to an end, the industry has received an unexpected pick-me-up, reversing the fortunes for some and proving to be a boost going forward for others.

"Performance has been the main driver of industry asset growth since 2009. New funds and closed funds did not significantly impact the industry in terms of contributing to year on year growth." Given the current economic climate and subsequent pedestrian fund performance experienced over the last year, it comes as no surprise that the industry experienced a drop in assets.

"In the coming year(s), it would serve the industry well to explore external investor sources in addition to improving performance in order to attract new inflows and achieve sustainable growth. Despite the decline in AUM, we remain optimistic that inflows will pick up the pace once the regulation dust has settled and the new requirements become more acceptable to investors," concludes Visagie.