

"To Find the Perception Towards Hedge Fund Strategies of Dealers in Surat City"



Management

KEYWORDS : Hedge Fund, Hedge Fund Strategies, Institutional investor, Risk Management.

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ABSTRACT

A hedge fund is a fund that undertakes a wider range of investment and trading activities there is wide range of investment strategies employed in such funds. , but which is generally open for the investors specified by the regulators There is often the use of the multi strategy for the hedge fund where by the fund manager can change the investment strategies base on market condition, allocation or appropriation of the capital and resources among the different strategies. It could be seen that establishment of the formal mechanism for the hedge fund strategy is bound by the underlying phenomena that these strategies are persistently changes and the hedge fund manager also change its strategies according to shift in the investment policy and market conditions. The Hedge fund strategies are driven by factors which changes with institutional profile and dealers accordingly need to study factors for appropriate hedge fund strategy to reap high benefits. The study shows that the dealer preference for factor driving hedge fund strategy selection is different for each strategy. The study shows that dealers give more importance to long/short hedge fund strategies and location based hedge fund strategies.dealers have given least importance tactical hedge fund strategies.The other strategies like tactical and eventdriven are risky which are taken with due support of management but if it successful ,gives better results too.

1. INTRODUCTION

A hedge fund is a fund that undertakes a wider range of investment and trading activities there is wide range of investment strategies employed in such funds. , but which is generally open for the investors specified by the regulators. These investors are institutions, such as pension funds, university endowments and foundations, or high-net-worth individuals, who are considered to have the knowledge or resources and the ability to understand the nature of the funds. Investors can invest and withdraw money at regular, specified intervals. An increases and decreases in the value of the fund's investment assets (and fund expenses) are directly reflected in the amount an investor can later withdraw. The lack of clarity of agreement on its term and the spectrums of diversity, They are typically characterized by high leveraging, derivatives trading a short selling compared to Mutual Funds.

Hedge funds are basically develop as a speculative mechanism to capitalize the information held by the managers and insiders so as the. hedge fund concept develop as the concept of strong form of efficient market hypotheses in which the manager of the hedge fund reveal the information of the strategies pursue by him after extracting the benefit from it.

The hedge fund strategies can be classified from one of the several bases as asset class, correlation with the market, returns enhancer and risk minimization, systemization of the trading and discretionary funds, location based. The hedge fund often can be classified according to the asset class by making the underlying like sole equity, fixed income, currencies and commodities. While they can also be classified on the base of the correlation with market and in such context it can basically divided in two types

- 1) The fund which have the low correlation with market yield that is describe as market natural
- 2) And on other hand the fund's return which is strongly correlated with market is defined as market directional fund.

The hedge fund strategies can also be grouped on the base of return enhancer which is like distressed securities, event driven approach while arbitrage strategies and long short strategies are such a risk reducer strategies. Some strategies can also be categorized on the base of the trading pattern like strategies developed from the market and technical perspective of the market are known as systematic fund while which are developed from the judgment of the hedge fund manager are defined as the discretionary fund. Fund can also be categorized from the geographic approach like some fund focused on the emerging market opportunities while some may focused on the European asset. There is often the use of the multi strategy for the hedge fund where by the fund manager can change the investment

strategies base on market condition, allocation or appropriation of the capital and resources among the different strategies. It could be seen that establishment of the formal mechanism for the hedge fund strategy is bound by the underlying phenomena that these strategies are persistently changes and the hedge fund manager also change its strategies according to shift in the investment policy and market conditions. There is also wide era of the fund of fund system in which mutual fund manager will allocate its capital among various hedge funds opportunities or the same hedge fund.

The Hedge fund strategies are driven by factors which changes with institutional profile and dealers accordingly need to study factors for appropriate hedge fund strategy to reap high benefits. The research is done to understand various strategies for risk management in hedge fund, this study enable to optimize the investment in the institutional investors and minimize the potential losses.

2. LITERATURE REVIEW

Hedge Fund Research, Inc. has constructed an accurate, relevant, robust and contemporaneous Strategy Classification System for all investment managers present in the HFR Database. The classifications reflect the evolution of strategic trends in the hedge fund industry, cognizant of the reality that over market cycles the classification system is likely to continue to evolve, as new opportunities attract investor capital. The objective of the system is to define pure strategy and sub-strategy buckets which can be used to characterize pure strategy return at each level of analysis, to be used for purposes of quantitative index construction. 2

William Fung, David A. Hsieh (1997) this article presented some new results on an unexplored data set on hedge fund performance. The results indicate that are highly dynamic. The article found five dominant investment styles in hedge funds, which when added to Sharpe's (1992) assets class factor model can provide an integrated frame-work for style analysis of both buy and hold and dynamic trading strategies.

Schneeweis (1998) observed some hedge fund strategies (for example, fixed income arbitrage) were previously the proprietary domain of investment banks and their trading desks. One driver for the growth of hedge funds is the application of investment bank trading desk strategies to private investment vehicles.

William Fung; David A. Hsieh (2001) Hedge fund strategies typically generate option-like returns. Linear-factor models using benchmark asset indices have difficulty explaining them. Following the suggestions in Glosten and Jagannathan (1994) , this article shows how to model hedge fund returns by focusing on the popular "trend-following" strategy. We use look back straddles to model trend-following

strategies, and show that they can explain trend-following funds' returns better than standard asset indices. Though standard straddles lead to similar empirical results, lookback straddles are theoretically closer to the concept of trend following. Our model should be useful in the design of performance benchmarks for trend-following funds.

Nicholas Chan, Mila Getmansky, Shane M. Haas, Andrew W. Lo (2005) Systemic risk is commonly used to describe the possibility of a series of correlated defaults among financial institutions---typically banks---that occur over a short period of time, often caused by a single major event. However, since the collapse of Long Term Capital Management in 1998, it has become clear that hedge funds are also involved in systemic risk exposures. The hedge-fund industry has a symbiotic relationship with the banking sector; and many banks now operate proprietary trading units that are organized much like hedge funds. As a result, the risk exposures of the hedge-fund industry may have a material impact on the banking sector, resulting in new sources of systemic risks. This paper attempted to quantify the potential impact of hedge funds on systemic risk by developing a number of new risk measures for hedge funds and applying them to individual and aggregate hedge-fund returns data. These measures include: illiquidity risk exposure, nonlinear factor models for hedge-fund and banking-sector indexes, logistic regression analysis of hedge-fund liquidation probabilities, and aggregate measures of volatility and distress based on regime-switching models. The paper suggested that the hedge-fund industry may be heading into a challenging period of lower expected returns, and that systemic risk is currently on the rise.

3. OBJECTIVE OF THE STUDY

- To find the preference among dealers for 'hedge fund' strategies.
- To find the preference of factors for the selection of hedge fund strategies

4. PROBLEM STATEMENT

This study will enable to search and magnify the investment avenues and to minimize and manage the risks to the institutional investor. It will help to understand the events which are take place in the market.

5. RESEARCH METHODOLOGY

This study enables to search and magnify the investment avenues and to minimize and manage the risks to the institutional investor. It will be limited to the hedge fund strategies only and risk management concept of the hedge fund. This study conducted through the descriptive research design. The non probability convenient sampling method is used. Sample size is 50 dealers. Data is collected from both the primary and secondary sources. Data is collected through survey method using structured questionnaire.

6. DATA ANALYSIS

Specifically dealers understand that hedge fund is institutional investor's fund governed by specific regulations and they had given the priority to the second response which convey above statement.

Ho: Factors driving selection of hedge fund on the basis of hedge fund strategy of location based are not related.

H1: Factors driving selection of hedge fund on the basis of hedge fund strategy of location based are related

Table 1: Friedman test for factors driving selection of hedge funds

	Mean Rank
Trading style	5.23
Asset class	6.18
Equity index	3.53
Interest rate	5.42
Exchange rate	6.97
Volatility	3.17
Moving avg.	3.20
Return	2.30

Test Statistics^a

N	30
Chi-Square	105.387
df	7
Asymp. Sig.	.000

a. Friedman Test

In Table 1 above as significance value is less than .01 significance level, we reject null hypothesis and accept alternative hypothesis that factors are related to each other. As per the rank from Friedman test the dealer gives importance to exchange rate, asset class and trading style respectively for location based hedge fund strategies.

Ho: Hedge Fund Strategies are not related to each other.

H2: Hedge Fund Strategies are related to each other.

Table 2: Friedman Test for Preference of Hedge Fund Strategies

	Mean Rank
Event driven	2.80
Relative value	2.52
Long short	3.82
Tactical	2.23
Location based	3.63

Test Statistics^a

N	30
Chi-Square	29.370
df	4
Asymp. Sig.	.000

a. Friedman Test

From Table 2 Friedman test gives a rank which shows importance of the strategy's as per dealers. As significance value is less than .01 significance level so this strategies are significantly related to each other and dealers give more importance to long/short hedge fund strategies and location based hedge fund strategies. Dealers have given least importance tactical hedge fund strategies.

7. SUGGESTIONS

- Hedge fund strategies are extremely varied but at the same time Hedge funds focus on strategies that traditional funds cannot undertake, or cannot do well.
- The dealers give more importance to long/short hedge fund strategies and location based hedge fund strategies. Dealers have given least importance tactical hedge fund strategies. The other strategies like tactical and event driven are risky which are taken with due support of management but if it successful, gives better results. So dealers could make awareness and get basics about this strategies.

8. CONCLUSION

The most of Dealers understand hedge fund as institutional investor's fund governed by specific regulations. The study reveals that the dealer gives importance to interest rate, exchange rate and volatility of assets respectively for event driven hedge fund strategies. The dealer gives importance to volatility of assets, interest rate and equity index respectively for relative value hedge fund strategies. The dealer gives importance to volatility return on future contract and equity index respectively for long short hedge fund strategies. The dealer gives importance to exchange rate and trading style respectively for tactical hedge fund strategies. The dealer gives importance to exchange rate, asset class and trading style respectively for location based hedge fund strategies.

Long-short strategies rely on hedge funds' freedom to short equities and take derivatives positions, both of which are often forbidden for traditional funds, or restricted by funds investment

mandates. Hedge fund strategies requiring sharp decisions in risky environments such as event driven strategies and tactical trading strategies, are helped by the very strong management incentives used by hedge funds. The investment opacity of hedge funds is crucial in many relative-value strategies, since it prevents other investors from uncovering the funds positions and squeezing its transactions in illiquid markets.

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