

Strategy Drift

Compliance

Audit Review

Conflicts of Interest

Risk Management

Regulatory Risk

Background Investigation

Leverage

Operational Risk

Hidden Fees

Valuations

Liquidity

Redemption Risks

Fraud

Legal

Counterparty Risk

Fund Structure

Disaster

Signature Rights

Recovery

Key People

UCITS - Safe Haven or Trap?

Pitfalls, Benefits and Focus Areas for Fund Selection and Due Diligence

ASCOSIM Convegno, Milano, January 22, 2014

Desired Characteristics of an Investment Vehicle

- In your opinion?
- Often mentioned:
 - Transparency
 - Liquidity
 - Strong risk management
 - Limited risks
 - Independent administration
- UCITS framework as conclusion?
- Not necessarily

Some Observations

- Based on SwissAnalytics' proprietary risk assessment framework
- 120+ factors scored individually
- Factor scorings below average are "flagged"

		Average "Flags" per Fund				Average "Flags" per Fund	
		UCITS	Non - UCITS			UCITS	Non - UCITS
Documentation		5.65	3.95	Setup		2.70	2.26
Reporting & Transparency		0.70	0.58	Portfolio Valuation & NAV Calculation		1.60	1.24

Pitfalls of UCITS: Docile Regulators and Complacent Investors

- Perceived transparency greater than actual transparency
 - Disclosures and mandated documents vs. information not regularly provided
- Regulator patronizes investors
 - Even though regulators often lag latest structuring developments and knowledge is inferior compared to investment managers
 - Transparency requirements only apply to regulators but findings are not shared with investors
- Rules do not guarantee compliance
 - Rules and guidelines keep changing
 - Lengthy transition periods
 - Local implementations vary significantly

Where Details Do Matter

- Service provider agreements
 - Define the level of services provided and the distribution of responsibilities

- Assumptions and methodologies
 - Risk management and leverage
 - VaR Calculations
 - Stress tests

 - Collateral
 - Pool composition
 - Valuation methodologies

Other Areas to Scrutinize

- Fund governance
 - Requirements to manage and disclose conflicts of interests and to appoint non-affiliated directors
 - Limited leverage to investors to enforce their interests
- Liquidity match
 - Regulation of liquidity offered, diversification of positions, and eligible instruments
 - Ability to meet redemption requests could still be severely limited
- Fees
 - Disclosures regulated but levels are high
- Slippage
 - UCITS fund tend to lag parallel fund they mirror

Benefits of UCITS

- Security of assets
 - Safekeeping at independent custodian which is liable for loss of assets
- Segregation of duties
 - Independent risk management and compliance function
- Applies also to AIF and to some extent to offshore funds

Conclusion

- UCITS brought a lot of improvements
- It comes at a price
- Regulation is no substitute for conducting thorough due diligence and regular monitoring

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Thank you for your attention

SwissAnalytics' Profile

- One of a select handful of independent due diligence providers globally
- Avoids conflicts of interests by working for investors only
- Due diligence methodology follows standardized process aimed at identifying potential issues
- Offers different service modules to allow customizing coverage to each client's unique needs
- Employees' backgrounds in fund of fund management, fund analysis, back office operations
- Team of 5 investment professionals (CFA, CAIA, FRM)
- Initially started as hedge fund lending value calculation business for Zurich-based private bank in 2005
- Privately owned, wholly independent

Christian Nauer, M.A.HSG, CFA



Partner, CEO

Christian began his alternative investment career with Man Investments with the Relative Value Team within the RMF subsidiary. During this time, he became primarily responsible for co-managing RMF's commodities strategies and energy funds (combined \$2.5 billion AUM), in addition to sourcing funds, and advising portfolio management on commodity strategies. At the same time, he was responsible for formulating and presenting market opinions. After completing his assignment with Man Investments and prior to joining SwissAnalytics, Christian shifted focus and took on the challenge of restructuring a distressed fund of funds portfolio for Horizon21. Being entrusted with legacy position management and an investment mandate overhaul, he worked in close concert with underlying managers and investors to bring about an orderly and timely liquidation of the portfolio.

Christian has been conducting onsite due diligence for over ten years and, having spent several years based in New York, has developed a profound knowledge of a wide range of alternative and traditional investment strategies, as well as their operational, legal, and strategy risks.

Christian holds a Master's degree in Finance and Capital Markets from the University of St. Gallen (HSG) and is a CFA charterholder. He serves as the Advocacy Chair of the Swiss CFA Society. A Swiss citizen, Christian is fluent in English, German, French and speaks some Italian.