

Kendrick Wakeman, CFA  
kwakeman@badonhill.com  
781-544-4047

### YOUR HEDGE FUND STRATEGY IS PROBABLY NOT AS DIFFERENTIATED AS YOU THINK

The SEI 6<sup>th</sup> Annual Global Survey<sup>i</sup> was entitled “Six Ways Hedge Funds Need to Adapt Now” and pointed out several areas of improvement for managers who wish to field a successful hedge fund product. The number one suggestion was entitled “Sustainable Edge” and encompassed a bunch of concepts that speak to the lack of differentiation in hedge fund strategies.

The survey found that, if you ask 10 investors, 7 of them will say there is not enough differentiation between hedge fund managers (presumably they are talking about managers in the same sub-index). Our anecdotal experience would lead us to believe that if you asked 10 hedge fund managers, they would all say they are highly differentiated.

This seems to indicate a dislocation between the way hedge fund managers think of their strategy and the way investors think of their strategy. Given that investors presumably have a much fuller picture of the competing funds available, hedge fund managers should take this critique to heart.

The good news is that these sorts of headwinds can be a marketing tailwind if managers are willing to take some real steps towards differentiation. As one respondent puts it in the survey: “This is an area ripe with opportunities for differentiation.”

Our advice for hedge fund managers, particularly those who are having trouble with marketing:

1. Conduct a formal study of your strategy, resources and process relative to your peers. Attack any presumptions of differentiation to see how robust they are and if they can objectively be thought of as giving you a sustainable edge. Confirm your presumptions with outside sources. As an aside, we would strongly discourage managers from thinking that “being really smart” or “having done this for a long time” are highly differentiating factors in this day and age.
2. Challenge yourself and co-workers to come up with ways that the process can be improved in a differentiating way. Don’t ignore the thoughts of junior staff, people new to the firm or outside opinions as they may be looking at your strategy with fresher lenses.
3. Update your marketing materials to bluntly and brutally highlight the things about your fund that represent differentiated, repeatable sources of alpha. According to the survey, these are going to be the primary points of decision for the investor.

---

<sup>i</sup> “6 Ways Hedge Funds Need to Adapt Now” *SEI Knowledge Partnership*, 2013