

Woodfield Wire

AN E-NEWSLETTER FOR HEDGE FUND MANAGERS
AND OTHER INDUSTRY PROFESSIONALS

Welcome! Woodfield's e-newsletter brings you articles about hedge fund-related topics and best practices. We welcome your thoughts—just hit "reply" and send us your comments.

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Excuse me—have you two met?

Lately we've been getting a lot of questions from our clients and prospects about capital introduction—the process by which prime brokers introduce client funds to interested investors. How does it work? How long does it take? What results can a fund manager expect?

So we picked up the phone and called Patrick McCurdy, partner and head of capital development at [Merlin Securities](#), a leading prime brokerage services and technology provider for hedge funds and managed account platforms. Before coming to Merlin a year and a half ago, Patrick worked for six years in Morgan Stanley's prime brokerage division.

"Capital introductions have evolved to become an extension of a hedge fund manager's capital-raising mandate," Patrick said, explaining that a capital introduction team provides introductions of fund managers seeking capital to allocators seeking investments—including funds of funds, family offices, foundations and endowments, corporate and private investment funds, and consultants who work in an advisory capacity for an institution or high-net-worth investors.

The capital introduction team works in an outsourced capacity for these hedge fund managers, Patrick said, but it does not act as a placement agent or as a broker for a hedge fund manager. Once the introduction is made, the capital introduction team takes a step back so as not to be seen as brokering the investment (which would activate different SEC requirements).

How does capital introduction work?

Patrick explained some of the forms the process can take:

- **Large investment symposiums** hosted by the capital introduction team—content-driven, often multi-day events in which fund managers participate in panels, speak on timely issues and then sit down and meet with investors directly.
- **Small, focused dinners** that give one hedge fund manager a chance to present to a group of investors—a great environment for communicating a manager's story.
- **Roadshows** assisted by the capital introduction team.
- **Targeted calling campaigns.** When a capital introduction team is working with a manager that may meet the investment criteria of an investor they know, they can reach out individually and share information about that fund.
- **Inbound requests.** A capital introduction team will receive requests for certain strategies, such as distressed managers, global macro, etc., and can suggest a possible match.

As a hedge fund manager, what can I do to make my fund appealing for capital introduction?

"Traditionally, investors have been focused on performance," Patrick said. "Today, along with performance—which is still number one—are liquidity, transparency, and volatility. To be successful today, you need to be able to address all four when meeting with investors and institutions."

Before talking with investors, Patrick said, fund managers need to ask themselves questions like:

- Is there a fit with the investor given your strategy and track record?
- How much transparency are you providing?
- How liquid are the assets—not only now but over the long term? If there's a crisis in the industry, how soon can investors get their money back?
- How does your strategy mute the volatility in the market?

Merlin has authored a number of white papers this year, all available at www.merlinsecurities.com, designed to help hedge funds better prepare themselves for meetings with potential investors.

Does the capital introduction team help a fund develop its marketing?

"As a capital introduction team, we help our managers develop and refine their message, especially for new launches," Patrick said. "Our approach is to stay abreast of the investment community and track the larger trends. With industry-wide insight, we are able to help funds focus their marketing in a way that reflects the needs of various investors, particularly those investors most likely to allocate to a given strategy."

What's the difference between good and bad marketing?

"Consistent follow-up," Patrick responded without missing a beat. "You need to be in front of investors, and the right investors. A good capital introduction team puts you in front of the right investors. But there is a long due diligence process that may involve multiple meetings. Consistency is key. You need to stay in front of investors so that when they have capital to allocate, your fund will be front of mind."

Does capital introduction take the place of a fund's in-house marketing?

"No. Capital introduction is only an extension of a fund's marketing—one arrow in the quiver," said Patrick, adding that a manager should have at least one person dedicated to marketing. It could be the COO or a marketing director.

As for bringing in a third party, Patrick feels that putting too much of a dependence on any external marketing organization is taking the focus away from where it needs to be. The focus of marketing a hedge fund needs to be done in house. "Nobody is better equipped to discuss the book than the portfolio manager himself," he said.

"The capital introduction team is a consultant," he added. "They can expertly advise you, produce an efficient roadmap, and even guide you to the right investor, but, ultimately, the responsibility for raising capital rests on the fund manager's shoulders."

How much time is involved?

That varies from investor to investor. "The time it takes to convert an investor has increased from pre-4th Quarter 2008 levels," Patrick said. "Investors need more comfort now from the manager they're investing with and will often monitor them for 6-12-18 months until they're comfortable and convinced that good performance is repeatable."

What does a fund need to be in order to have a realistic shot? Is there some threshold of assets under management and longevity before capital introduction is a possibility?

There's opportunity for all managers of any size, Patrick said. "Investors are opportunistic and want to find the best managers. Regardless of your fund size, \$5 million or \$500 million, if you are employing a unique strategy, it can certainly be of interest. Not all investors will have the ability to invest with smaller managers, but a good capital introductions team can guide you on which investors to focus on given where your fund is in its lifecycle."

What's unique about Merlin's capital introduction program?

"We're focused on bringing our managers in front of the right investors," Patrick said, "and we've always focused on emerging managers. As you know, the field is extremely challenging and competitive. For new fund launches, we have a whole host of vehicles to help our managers get seeded. Merlin is focused on identifying those allocators and bringing the fund manager in front of them; this focus helps funds achieve a critical AUM level at an earlier stage."

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