



Hedge funds need technology for institutional credibility

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The traditional image of a hedge fund is two guys in an office with nothing more sophisticated than a Bloomberg terminal and an Excel spreadsheet.

But the technological infrastructure supporting hedge funds is now being eyed closely by institutional investors, who increasingly favor hedge funds that tick the right boxes in areas such



as operational efficiency, risk management, compliance and, above all, credibility.

The reason why hedge funds have historically depended on fairly basic technology has a lot to do with the industry's origins.

Hedge funds usually get set up by managers who have jumped ship from big investment banks, whose back-office resources and technology they took for granted. Running

their own start-up hedge fund, they rarely give much thought to integrating systems and processes as they are too busy trying to grow the business. In addition, they have limited financial and IT resources which rules out the type of IT systems used by big fund managers.

Even today, start-up hedge fund managers with less than \$100m AUM make up around 30 percent of the industry.

But the nature of the hedge fund industry is changing fast. Hedge funds with rudimentary technology tools look out of place in an industry where institutional capital rather than rich individuals is driving market growth.

A more cautious atmosphere for hedge fund investment has developed following the Lehman crisis and there is a greater focus on limiting downside and preserving capital.

That may clash with the traditional image of hedge fund managers making big bets in the hope of rich rewards, but hedge funds that want to win institutional mandates have to behave more like conventional fund managers with monthly reporting, tight risk limits and a safety-first approach.

According to a recent report from research firm [AITE Group \(http://www.aitegroup.com/\)](http://www.aitegroup.com/):

“Institutional credibility—the idea of a firm’s operational stability existing beyond reproach in investors’ eyes—is the buzzword driving hedge funds’ operational efficiency, regulatory requirements, risk management, and investment decision-making priorities.”

Compliance requirements for hedge fund managers are also a lot tougher than they used thanks to the Alternative Investment Fund Managers Directive (AIFMD) in Europe to Form PF of the Dodd-Frank Act in the US.

To win over institutions and satisfy regulators, hedge fund managers can no longer afford to depend on disparate systems and outdated technology tools.

Hedge funds need to put in place robust processes and integrated systems to better support the growing and increasingly complex business.

In the front office, for example, an integrated order entry system is essential once they have passed the initial start-up phase. It enables them to efficiently execute and manage growing volumes of orders and tie together trading, operations, compliance and portfolio management

Order management technology not only boosts scalability but makes the whole business much more efficient.

For example, hedge fund managers pride themselves on being nimble in changing market conditions. But if a hedge fund manager needs to rapidly re-balance a growing range of portfolios following a sudden change of policy on asset allocation, it is time-consuming and error-prone to have to do the rebalancing manually using spreadsheets.

In the past, the reporting function was often neglected by hedge fund managers. Today it has a heightened importance due to the desire of institutional clients for more frequent and more detailed reporting of their hedge fund investments, and the greater reporting burden imposed by regulations such as AIFMD.

According to a survey by AITE Group, 56 percent of hedge fund managers said that dealing with regulatory issues was “somewhat challenging” or “extremely challenging” to their portfolio management and accounting process.

These heightened needs led ClearStructure to develop an integrated portfolio management system that links together the once-separate back office and front office functions, and meets the specialized requirements of hedge funds in areas such as order management, compliance, reporting, and risk management.

Recognizing the limited resources of small hedge funds, ClearStructure has now developed ClearStart, a cost-effective way for start-up managers to leverage the same technology used by big institutions but at a discounted price.

The ClearStructure package of technologies and services are delivered for a fixed fee and because ClearStructure’s technology is cloud-based, it does not need in-house infrastructure or dedicated IT staff, so allowing smaller hedge fund managers to concentrate on managing portfolios and winning new mandates.

