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Less than three years after starting operations, InfraHedge, offering a different model to traditional managed account providers, ranks as the largest MA platform operator in a survey of the industry, writes Kris Devasabai

Mapping the future

There is a new king of the hedge fund managed account platform (MAP) business.

InfraHedge, a subsidiary of State Street Corporation, ranks as the largest MAP operator in *Hedge Funds Review*'s annual survey of the industry. With total assets of $11.5 billion, it just edges Lyxor Asset Management's $11.3 billion platform into second place.

InfraHedge shot to the top of the rankings after assets on the platform grew nearly $4 billion from $7.6 billion in 2012 – a 53% rise. This is particularly impressive considering overall MAP assets were flat over the past 12 months, rising to $75 billion from $73 billion in 2012.

Excluding InfraHedge, overall MAP assets fell $2 billion compared with the previous year's survey.

Any business that rises to the top of its industry less than three years after starting operations has to be doing something right. What InfraHedge does is provide institutional investors with the infrastructure to create their own dedicated MAPs. This is a very different business model to the traditional MAPs that earn their fees from distribution and investment advisory services, says CEO Akshaya Bhargava.

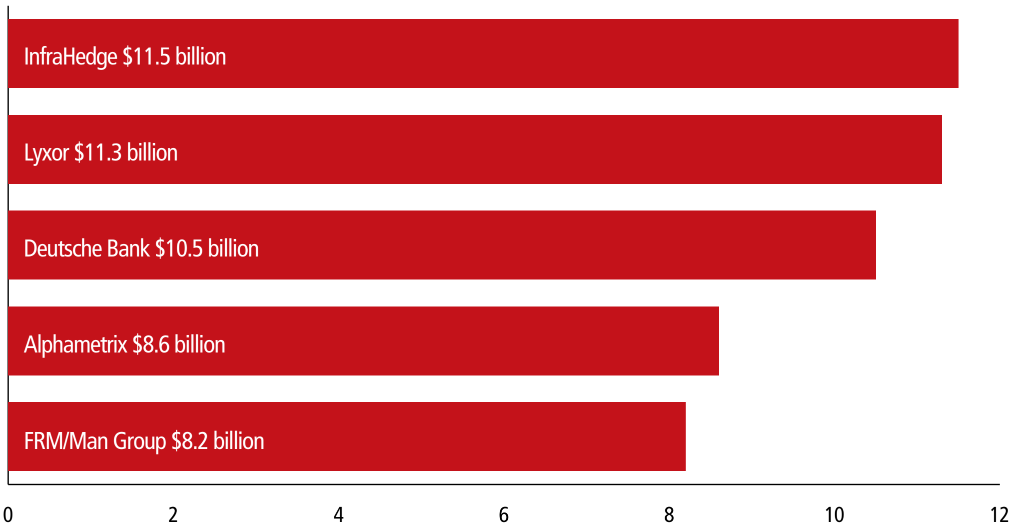
"We provide the managed accounts infrastructure – the legal structuring, operations, connectivity, data aggregation, compliance and risk reporting functions – and that's all we do," he says. "We don't select the funds, we're not asset managers. The client either makes the investment decisions themselves or they hire an adviser or consultant for that service."

This model has a couple of advantages. The first is flexibility. The client can customise every aspect of the platform from the managers and strategies through to the service providers and legal structure of the accounts.

Second is price. Because InfraHedge does not have any asset management-related costs, Bhargava says it can deliver a private MAP to clients at a far lower price than competitors. "Our fees are significantly lower because we're not providing investment management or advisory services; our clients do that in-house."

InfraHedge's approach has clearly struck a chord with big

Five largest MAP operators



Source: *Hedge Funds Review* research

2012 *Hedge Funds Review* survey of managed accounts platforms

Rank	Operator	Name	Date started operation	AUM (June 2013)	AUM (June 2012)	No. of funds on platform	Strategy	Minimum investment	Fee structure	Domicile
1	InfraHedge	InfraHedge	2011	$11.5 billion ▲	$7.6 billion	Not disclosed	Not disclosed	Not disclosed	Not disclosed	Multiple
2	Lyxor Asset Management	MAP (Managed Account Platform)	1998	$11.3 billion ▲	$10.9 billion	106	Equity hedge: 32.6% Event driven: 24.1% Macro/CTA: 30.3% Relative value: 13%	$100,000 (B class)	70bp maximum for B class	Jersey, Ireland and Luxembourg
3	Deutsche Bank	Deutsche Bank Hedge Fund Platform	2002	$10.5 billion ▼	$11.8 billion	241	Equity hedge: 11.8% Event driven: 17.2% Macro/CTA: 70% Relative value: 1%	$250,000	Not disclosed	Multiple
4	AlphaMetrix	AlphaMetrix Global Marketplace	2005	$8.6 billion ▲	$8.4 billion	175	Equity hedge: 15% Event driven: 5% Macro/CTA: 55% Relative value: 15% Other: 10%	$250,000	Not disclosed	Multiple
5	FRM (Man Group)	Not applicable	1998	$8.2 billion ▶◀	$7.6 billion	71	Equity hedge: 16% Event driven: 14% Macro/CTA: 52% Relative value: 16% Other: 2%	Varies	Not disclosed	Cayman Islands, Ireland and Luxembourg
6	Permal Group	PMAP	2001	$7.2 billion ▲	$7.2 billion	77	Equity hedge: 18% Event driven: 12% Macro/CTA: 36% Other: 34%	$25 million	Not disclosed	British Virgin Islands
7	Amundi Alternative Investments	Amundi Absolute Return Managed Account Platform	2006	$4.4 billion ▲	$2.8 billion	31	Equity hedge: 18% Event driven: 25% Macro/CTA: 20% Relative value: 37%	€100,000	Not disclosed	Ireland
8	Morgan Stanley & Co International	Morgan Stanley Multi-Asset Platform	2006	$4.3 billion ▲	$3.6 billion	57	Equity hedge: 44% Macro/CTA: 39% Other: 17%	Varies	Not disclosed	Ireland, Cayman Islands, Delaware and others
9	Innocap	Innocap Managed Account Platform	1996	$2.126 billion ▼	$2.4 billion	30	Equity hedge: 20% Event driven: 7% Macro/CTA: 57% Relative value: 13% Other: 3%	$150,000	50bp	Malta, Canada, and Ireland
10	HFR Asset Management*	HFR Platform	1998	$1.9 billion ▼	$3 billion	61	Equity hedge: 17.3% Event driven: 14% Macro/CTA: 21.2% Relative value: 30.5% Other: 17%	$1 million	Not disclosed	Bermuda and Ireland
11	Goldman Sachs International	n/a	2005	$1.75 billion ▼	$4 billion	25	Equity hedge: 26% Event driven: 30% Macro/CTA: 44%	$1 million	not disclosed	Cayman Islands, Ireland and Luxembourg
12	Guggenheim Fund Solutions*	Guggenheim Fund Solutions	2011	$1.6 billion ▶◀	not available	16	Equity hedge: 43.3% Event driven: 10.4% Global macro/CTA: 16.5% Relative value: 29.8%	$133,333	not disclosed	Ireland
13	Sciens Group Fund Services	Sciens Group Alternative Strategies PCC	2002	$800 million ▲	$582 million	35	Equity hedge: 26% Event driven: 6% Macro/CTA: 45% Relative value: 3% Other: 18%	$250,000	not disclosed	Guernsey
14	Gottex Fund Management	Gottex Solutions Services and Luma Solutions Services	2009	$675 million ▼	$1.7 billion	9	Equity hedge: 20% Event driven: 21% Relative value: 43% Global macro: 14% Other: 2%	$100,000 for Cayman SPC; €10,000 for Luxembourg Ucits; €125,000 for Luxembourg SIF	30-40bp	Cayman Islands and Luxembourg

* estimates based on SEC filings, all other data supplied by platform operators. Research by Hannah Keenan. Source: *Hedge Funds Review* research .

institutional investors but it is not for everyone. Private MAPs are only suitable for the largest and most sophisticated investors.

InfraHedge's clients have at least $250 million invested in hedge funds and commit a minimum of $25 million to each of the managers on their private platforms. This means the pool of potential clients is relatively small, although the ticket sizes are large enough to make it an attractive business for MAPs.

The emergence of InfraHedge raises the ante for other large MAP operators competing for mandates from large institutional investors that want dedicated platforms.

These types of deals are nothing new for the industry's big players. Lyxor, Deutsche Bank and FRM all run dedicated platforms for large investors – but not everyone believes they represent the future of the MAP business.

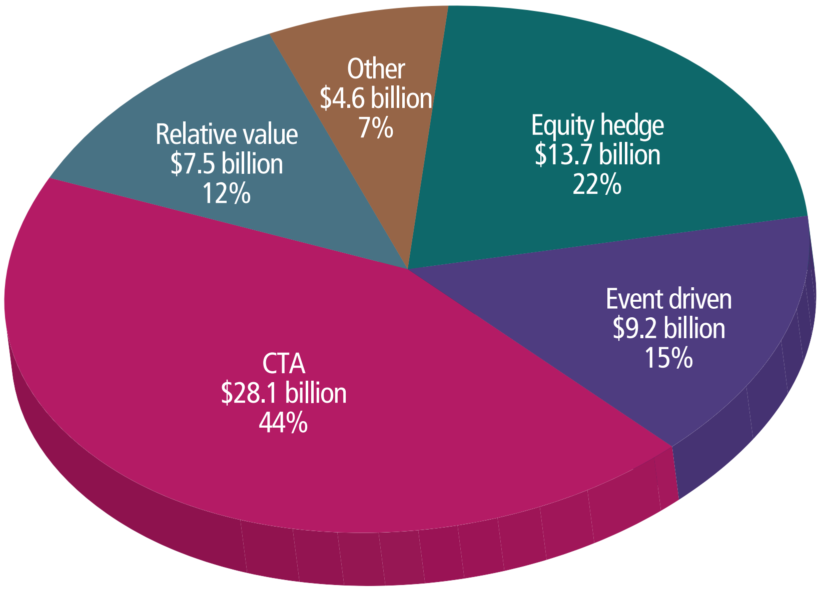
Lyxor created one of the first dedicated MAPs for the Dutch pension fund manager PGGM in 2010. That was a pure infrastructure deal with PGGM selecting the managers and Lyxor providing the operations, technology and infrastructure for the managed accounts.

"There is growing demand for dedicated managed account platforms, especially from pension funds with large allocations to hedge funds and the ability to manage this internally," confirms Nathanaël Benzaken, deputy head of Lyxor's alternative investments business.

"We are competing for those deals. We also want to work with institutions that also require asset management or advisory services. We have the DNA of an asset manager combined with a scalable and flexible platform, which means we have the ability to provide many different solutions adapted to each client's needs."

Lyxor's deal with the $170 billion California State Teachers' Retirement System (Calstrs) is an example of the demand for a more complete MAP service.

MAP strategy breakdown



Source: *Hedge Funds Review* research

Lyxor was hired in late 2011 to advise Calstrs on the creation of a $200 million global macro portfolio. Lyxor is providing investment research, manager selection, portfolio construction and due diligence services to Calstrs on an advisory basis in addition to facilitating investments through its managed accounts infrastructure.

The emergence of the infrastructure-only model seems to have encouraged the traditional MAP operators to redouble their efforts to drive down fees and costs.

One of Lyxor's major initiatives this year has been the launch of an institutional share class, called the S share, on its commingled platform.

"The idea was to offer one of the benefits of a dedicated platform – the ability to negotiate lower fees with the manager – to mid-size institutions that lack the scale to have a private MAP," says Lionel Paquin, head of the Lyxor managed account platform. "So we approached the managers and asked them if they would offer lower fees for investors in exchange for larger, stickier tickets and monthly liquidity."

So far nearly 40 managers have signed up to the S share class, which has a $5 million minimum investment and offers monthly liquidity. Paquin's team was able to negotiate average fee discounts equivalent to the 0.7% platform fee Lyxor charges for its B share class, which carries a $100,000 minimum and weekly liquidity.

"We know that mid-size institutions are fee-sensitive and this is a solution that allows them to invest in a managed account at exactly the same TER as the benchmark hedge fund," says Paquin. "The S share class has quickly gotten significant traction, especially from institutions in the US and Japan," he adds.

The top MAP platforms take the issue of fees seriously and

> "We provide the managed accounts infrastructure – the legal structuring, operations, connectivity, data aggregation, compliance and risk reporting functions – and that's all we do."
> **Akshaya Bhargava, InfraHedge**

have eschewed practices such as revenue sharing arrangements with managers.

For instance, Deutsche Bank passes all fee concessions it negotiates to investors and has 'most favoured nation' clauses with managers that agree to them, ensuring that its clients always receive the best deal available.

"We have to ensure the benefits of the platform exceed the cost and one way to do that is by negotiating competitive fees with all our service providers and reviewing our costs regularly," says Hans Feder, global head of Deutsche Bank's dbSelect platform. "Typically, we can offer a better overall cost structure for the investor because of our very efficient infrastructure setup. We make the cost very transparent by charging an 'all in' fee that includes all the admin costs."

FRM has taken the initiative to lower costs even further. It recently started working with a third party that specialises in monitoring and benchmarking trading counterparties. "We're in the implementation stage with an initiative that will allow us to make sure we're paying the best ticket charges, commission rates etcetera to counterparties across the different markets and instruments that our managers trade. This should result in further cost reductions for our investors," says Stephen McGoohan, head of FRM's managed account business.

Fee negotiations are one of several ways MAP operators can deliver added value. Permal's president Omar Kodmani sees the group's investment capabilities as an integral part of its managed account platform offering. "We run an investment-led platform," he says. "It's not a case of simply offering transparency, liquidity and control – we're using our investment skills to generate better returns for investors."

This is achieved in a number of different ways. First, Permal puts a strong emphasis on using its scale and industry knowledge to negotiate favourable fees with investors. Second, the group works with managers to fine-tune and customise their mandates. "We don't just ask managers to run a copy of their flagship funds. We look to re-engineer the product to improve performance."

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> **Nathanael Benzaken, Lyxor**

This has produced positive results. The managed accounts on Permal's platform have generated excess alpha of 2.4% a year over the benchmark funds. Part of that comes from fee discounts but a significant portion of the outperformance is the result of what Kodmani calls Permal's "product engineering".

The full-service MAPs may well find they have to find ways to deliver this sort of value to compete with lower-cost infrastructure-only platforms.

For now investors may only have scratched the surface of what is possible with MAPs.

Stavros Siokos, CEO of Sciens Alternative Investments, reckons MAPs could ultimately encourage higher inflows into emerging managers. "Everyone accepts that small and mid-size funds generate the best returns but investors are concerned about the operational risks with these managers. A managed account addresses this issue," he says. Sciens recently added a top-performing mid-sized Japanese equity manager to its platform that is already attracting interest from investors.

The growth of MAPs is also changing the way investors view hedge fund investments in other ways.

"The real benefit of a MAP is that it enhances your ability to manage risk and take a more targeted and active approach to managing hedge fund portfolios," says Praveen Kanakemadala, global head of risk at Permal Investment Management Services.

Permal runs a series of highly concentrated managed account portfolios, some with fewer than 10 names, for investors that want targeted exposure to everything from hard assets to technology stocks.

The liquidity of managed accounts has also enabled Permal to respond more quickly to market events. Kanakemadala gives the example of the sell-off in Japanese stocks this May. The investment team concluded this was a temporary correction and quickly shifted capital to a long-biased Japanese equity manager to capture the rebound.

"The ability to act quickly is a big advantage," says Kodmani. "We put a lot of emphasis on developing strong top-down views and we can implement those much faster with managed accounts."

The turnover of Permal's hedge fund portfolios has doubled from 10% to 20% in the past three years as a result of its adoption of managed accounts. Kodmani reckons this more active management style has been additive to returns.

Indeed, he thinks MAPs with embedded asset management capabilities have an important role to play in helping investors to make the most of the transparency, liquidity and control – or TLC as he calls it – of managed accounts.

Deutsche Bank's Feder also sees signs of MAP investors becoming more sophisticated. For instance, some investors are optimising their hedge fund portfolios with factor-based index products.

McGoohan says FRM's clients are taking a similarly sophisticated approach. "Some larger clients are interested in using managed accounts to obtain different types of exposures, like alternative beta. We're now looking at tapping into the capabilities of GLG and AHL to provide cost effective exposure to certain hedge fund strategies via the MAP." ■