OPALESQUE

Opalesque Round Table

NEW YORK

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Introduction

Dear Reader,

Opalesque is going West! After having covered New Zealand, Australia, Singapore, Hong Kong and Japan in our Roundtable Series, on May 14th we had a stop in New York for a Roundtable with local hedge fund managers and allocators.

You will find this an intriguing piece of intelligence on the future of hedge funds:

- What is the future of today's hedge funds?
- What is "permitted disintermediation"? Will hedge funds be the new banks?
- What will happen in the distressed space?
- "We are seeing tremendous opportunities in multiple asset classes, some we have not seen in almost a decade" - where are these opportunities? Or is the current floor not a floor at all?
- Why AIG is setting up a seeding joint venture?
- and much more!

The Opalesque New York Roundtable was sponsored by the Abernathy McGregor Group (www.abmac.com) and took place in their New York office.

Participating Managers:

1. Glenn August, President Oak Hill Advisers LP
2. Tom Priore, CEO of ICP
3. Justin B. Dew, Managing Director, Clinton Group
4. George A. Kellner, Kellner DiLeo & Co., Managing Director, Chief Executive Officer
5. Keith M. Moore, PhD, Kellner DiLeo & Co., Principal, Portfolio Manager, Merger Arbitrage and Opportunities Funds and Director of Risk Management and Quantitative Analysis

Allocators:

1. Girish Reddy, Managing Partner of Prisma Capital Partners
2. Antonio Munoz, CEO EIM USA
3. Bob Discolo, Head of Hedge Fund Strategies Group, AIG Investments
4. Kevin Heller, Head of Research, Focus Group

Enjoy "listening in" to the Opalesque New York Roundtable!

Matthias Knab
Director Opalesque Ltd.
Knab@opalesque.com

Cover Photo: Statue of Liberty, Manhattan, New York

Participant Profiles

Seated (left to right)

Kevin Heller, Keith Moore, George Kellner, Bob Discolo, Tom Priore

Standing (left to right)

Steve Bruce (Abernathy McGregor, sponsor), Justin Dew, Glenn August, Girish Reddy, Antonio Munoz, Matthias Knab

Introduction

Keith Moore
Kellner DiLeo & Co.

Keith Moore, Portfolio Manager of Kellner DiLeo's Merger Fund and Opportunities Fund, as well as the Risk Manager of the firm's overall portfolios.

George Kellner
Kellner DiLeo & Co.

George Kellner, CEO of Kellner DiLeo & Co. We have been around since 1981 and for most of our existence were a merger arbitrage firm with a little convertible arbitrage dollop added. In 2002, we became more diversified, developed an event fund and restructured ourselves. We brought some new people in and also got into the distressed and special situations area. In 2004-2005, we again fine-tuned our organization bringing in another group of people including Keith in 2006 and Kate Kutasi in 2005 to run our distressed fund.

Basically, we have spent the last couple of years restructuring the organization and now we are set to move forward in these four areas and then perhaps into additional asset classes

Kevin Heller
Focus Investment Group

Kevin Heller, the Head of Research at Focus Investment Group. We were founded in 1994 as an asset management company with a fund of funds as the principal product. We partner with private banks and other institutions looking for alternative strategies.

Over these 14 years we have placed a heavy emphasis on building our own research process, our own database and our own technology tools. In 2008 we actually spun off that backbone - the research, the technology, and the database - into a separate company. Which means, we can offer that basic service to other institutions that may be allocating directly to single managers but don't want to manage those functions themselves. In essence, also our fund of funds division becomes the client of that company but then that company can grow by serving other institutions as well.

I joined the firm ten years ago as a Junior Analyst, and I wear a few different hats. In addition to being the Head of Research, I manage some of our niche fund of funds products: the event driven fund, an Asia-focused fund, and a fund focused on Europe. Other portfolio managers at Focus handle multi-strategy, or the emerging manager portfolio, and we have separate people managing the spin-off business.

The founder of the firm is Mazen Jabban, he is the CIO and principal shareholder. We are an employee-owned firm, which means there are a number of people who are incentivized to really grow the firm.

Girish Reddy
Prisma Capital Partners

My name is Girish Reddy, I am the Managing Partner of Prisma Capital Partners. Prior to forming the firm I was at Goldman Sachs as a partner managing the Equity Derivatives Business out of Europe. Prisma Capital was formed as a joint venture between three former Goldman partners and AEGON insurance in 2004. We are primarily a fund of hedge funds business and currently manage about $5 billion. 95% of our assets come from institutions, pensions, and insurance firms, and this is the primary focus for our business.

The firm is 40% owned by employees and AEGON owns the rest; the primary strategies are multi-strategy in a low-vol portfolio. Portable Alpha is a big application for us, about half our business is in customized portfolios. Our clients usually ask us to build a portfolio according to defined characteristics which can be based on risk or certain strategy exposures.

Glenn August
Oak Hill Advisors LP

My name is Glenn August and I am the President of Oak Hill Advisors. I've been at Oak Hill for almost 21 years. For the entire time, we've been focusing on the leveraged capital markets, including leveraged loans, high-yield debt, mezzanine debt, distressed debt and turn-around private equity. We go long and short, invest in the US and in Europe, and do so in the cash and derivatives markets. Our business has grown as the markets have grown. We have about $11 billion of capital today in credit hedge funds, CLOs, separate accounts and specialty funds. The 21 years we have been around for have been pretty exciting; and, of course, you can say the same for the past 12 months, which, at times, felt like 21 years!

Justin Dew
Clinton Group

My name is Justin Dew, I work for Clinton Group. Clinton Group was founded in 1991 by George Hall and a number of other partners. It started with a focus on mortgage backed securities, but evolved into converts and ultimately into a multi-strategy shop. In addition we run a number of CDOs and CLOs and also, through a subsidiary, a co-investment private equity fund. Finally, a few years ago we developed an additional strategy as a stand-alone product, a market neutral equity fund. I would agree in every sense of the word that the past 12 months have been as volatile as the accumulated last 12 years.

I joined the firm about a year-and-a-half ago; my role at the company is Head of Strategic Development, which includes identifying and hiring new talent and growing the firm through acquisitions, joint ventures and client related matters.

Tom Priore
Institutional Credit Partners

My name is Tom Priore, I am the CEO of Institutional Credit Partners. I had formed ICP along with three other founding members in August 2004 to operate a merchant bank focused on the fixed income space. ICP has a multi-strategy fixed income, absolute return focused asset management business. Our assets stand currently at $13 billion across structured funds and a couple of hedge fund strategies.

Alongside our asset management business, we participate in the capital markets as an originator similar to an investment bank, with the intent of being able to access our investments down the point of origination. Simply put, we like to be involved in the manufacturing process of the assets we are buying when we can. Depending on the situation, we like to have the choice of accessing our risk at the loan and obligor level (the manufacturing floor if you will) or from retail at the investment banks depending on which offers the best value. We cover the ABS sector, RMBS, commercial real-estate, shipping and infrastructure, finance, and corporate credit as well the leverage credit space, the CDO, SIV space.

Antonio Munoz
EIM USA

Antonio Munoz, I am the CEO of EIM USA. EIM was founded by Arki Busson in 1992 and manages close to $15 billion. We create customized solutions using hedge funds for our institutional clientele. EIM has investment offices around the world with a heavy focus on research. I have been with the firm seven years. My previous position was Global Head of Research, and I transitioned into the CEO role of our US business about one and a half years ago, when we decided to fully develop the US entity (formerly a research and investment office) and import our global customized model into the US market.

Bob Discolo
AIG Investments

I am Bob Discolo, I run the Hedge Fund Investments for AIG Investments. We manage about $10 billion in hedge funds. We are not really a fund of funds - true, we run $10 billion but half of that is AIG's own money, and the other half is from partners, for which we design customized solutions. AIG Investments has been investing in hedge funds since 1982. I have been there nine years. Personally, I have been investing in hedge funds for the last 18 years. AIG Investments also manage about $35 billion in private equity, so we probably are the fifth or sixth largest alternative firm in the world. Our total institutional investments stand at around $750 billion, of which $600 billion is AIG's own assets and the other $150 billion are clients' funds.

Matthias Knab **Obviously we have to take at least some time and examine the state of the economy. How does it affect your hedge fund or your hedge fund investments? Are you a victim of the circumstances? Is there a way to manage this? Are you profiting from the current environment?**

Kevin Heller I wanted to kick it off just because I find some humor in the topic. Just opening up the Wall Street Journal today, on the same page we have an article that says, '*Recession for US, not so fast, some economists say*', and just below it, '*Fed officials say economy may remain sluggish for some time*'. And within the article we have several prominent economists from big investment banks and institutions which are bullish-bearish and somewhere in between.

Greenspan said in an article in early April that "*We are in the throes of recession and the economy is going through the most wrenching crises since World War II.*" Soros had a similar comment and now of course in May (which I think is pretty close to April), they are tempering their views because recent economic data suggested that inflation might not be so bad, retail sales are okay, etc.

Personally, I am also not sure where we stand, but it seems clear that the Goldilocks economy is over, and things will be more challenging than they have been in the recent past. What does the macro picture say? Gasoline, electricity, home heating, and food prices are all up. And then we have falling housing prices, indicated by 5 million unsold homes, and a 112% increase in foreclosures in the first quarter. We also have witnessed an increase in continuing unemployment claims. Finally, we have all read about the poor shape the banking system is in due to sub-prime and other credit write downs. While we might debate how long and deep a US slowdown/recession will be, we can at least agree that conditions are more challenging than they were 12-18 months ago.

I believe this back-and-forth in the markets, with a lot of volatility, will continue. As the US is a very highly consumer-driven economy, whatever happens to the consumer will in the end be decisive, which is why I keep coming back to high energy, high food, and falling housing prices being a significant headwind.

While just now two-thirds of the S&P500 companies have reported earnings that are better than expected and inflation looks a little bit tame, I would like to point out that these are all backward looking numbers. I find it personally difficult to think that we just went through the entire credit cycle in less than one year.

Tom Priore I think what we have witnessed over the last six weeks to eight weeks (March and April) is a classic bear market rally, which is not unusual. We saw the same phenomenon back in 2001 in the last recession - 2001 to 2002. But if you kind of look for some granular explanation of what's going on, there is a lot of capital sitting on the sidelines, certainly at the insurance companies. Insurance portfolio managers have an asset-liability match focus, they have a budget to spend money, and they spend that money relative to acquiring assets against those liabilities. I believe they took on positions, and this phenomenon gave the market some legs and squeezed some of the shorts, as we have seen. In addition, traditional core fixed income and Lehman Aggregate managers appeared to rotate out of treasuries and into spread products adding to the pressure on credit spreads.

When you look at the economic data, we are entering a period where seasonal adjustments particularly on retail sales, are very favorable. If you overlay that with the stimulus package that has just gone out - and make no mistake the people in Washington, they may have their flaws, but they know how to influence the public perception - this stimulus package was timed to come out in May/June/July during the weakest period of historical retail sales comparisons.

So, we may very well see growth numbers over the next few months that look okay, because the money is returning to consumers' pockets. If you were to give every US citizen an extra dollar to spend per day, that alone would boost GDP by 1% annually (assuming they actually spent that dollar). In the stimulus packages, half the US population is given $2 a day; anyone who makes less than $75,000 - which is half the population - receives $600.

This money, as it flows back into the economy, can create the perception that things are okay. We saw this in the seasonal adjustments for CPI - we saw that the impact of gas prices increased less than last April, so that sent inflation numbers down. However, all I know is that gas is well over $4 a gallon, and last year it was $3. That looks like a pretty substantial increase.

Glenn August

But, let's look at the stimulus package and the change in gas prices: if you drive 12,000 miles a year and your car gets 15 miles a gallon, the entire stimulus check, or more, will be spent on the higher price of gasoline.

The economy has been remarkably resilient for all that has occurred thus far, without showing real signs of a true recession yet. But, looking at all of the different companies we invest in, it feels like the economy, or Europe, is going to weaken.

Tom Priore

I would certainly concur with that assessment. Apart from the weaker economic activity that we are hearing about, you've got to add another element into this equation: the banking system, which is really the source of the trouble, and reflect the long-term effects of the current crisis.

The banking system, which enabled the consumer to get over-leveraged, is now deleveraged. This is forcing deleveraging both at the consumer level, and at the corporate level. You could say that the driver of the economic activity that we've enjoyed was actually leverage, the availability of liquidity, and leverage, which no longer exists.

The banks have major regulatory capital problems and are applying extreme means to raise their capital ratios. They are certainly not lending to consumers or corporations – this reality is going to have a drag on the economy and the capital markets. It seems poised to unwind and unravel towards the beginning of the third quarter.

Antonio Munoz

Let me focus on the fixed-income space rather than pure equity. We are probably at the worst time since the early '90s in terms of the potential for housing negative equity, the potential for negative real interest rates, for higher inflation, and the lowest purchasing power that the US citizen has had outside the US. The dollar stands at historical lows, we have the weakest income data, and the unbalance of readjusted purchasing power abroad, both in Asia and Europe. Combine this with the current structural crisis in the finance world - credit derivatives, financial de-leveraging - and it seems like every single thing that made money for the last five years is on the verge of collapse.

But somehow all of that doesn't really crystallize into an adequate risk premium in the different asset classes. There is a potential mismatch between the pricing and assessment of risk across asset classes and the probability of things really falling over the cliff....

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Antonio Munoz

George Kellner

I guess the consensus then is that we are in a fairly lengthy slowdown, and I would agree with that. The next question is: how big and how deep will this slowdown be?

I believe that we are entering into a longer down period, though on the other end most seem to be saying "Gee, we are done with the worst credit crisis since the great depression, so there might be some springtime here pretty soon…" For those who are optimistic, I would like to point out that statistics are very dangerous in as much as you can find statistics that will support whatever position you would like to take. I intuitively think that the worst may still be around the corner, particularly in the credit space, even if it's an election year. The rebates came because we are in an election year. I don't know about the rest of you, but I would guess that Mr. Obama will be our next President. And if you look at some of his economic notions, it doesn't bode so well for the economy nor for the markets, regardless of your political or social views.

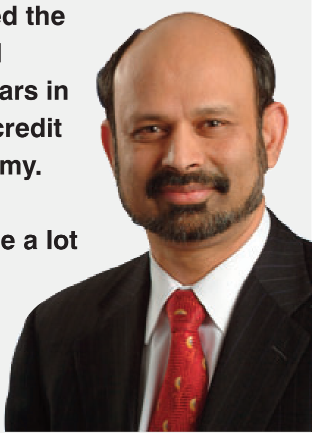
I don't see a whole lot of light at the end of the tunnel. We are at the juncture when we really have to put a floor under the dollar. I think, if that doesn't happen, then we are going to have major negative structural consequences. And, you can't put a floor under the dollar unless you start to raise interest rates. Once you start to raise interest rates, the markets and the ecomony rarely do well in those circumstances.

So my view could be classified as "cautiously pessimistic". The glass for me is half empty. I am a relatively short guy, so people always say when I get pessimistic it is because I am not tall enough to look past that half full glass. But I really do not see a lot to give me great confidence looking forward other than the fact that we have been able, in this country at least, to muddle through very difficult periods in the past. And we may do it again since I must admit that given the body blows the U.S. has experienced in the last few years (the Iraq war, huge oil price increases, and a credit meltdown, just to name a few), we are doing a lot better than we have any right to expect.

I do not have a strong view about the economy, but the thing that strikes me the most is how disconnected the fixed income and credit markets are relative to the equity markets. To us, as we look at the valuation or the risk return rewards, we feel like we have come full circle from 2004 when we started the firm. We were much more bullish on equity strategies and much more bearish on fixed income and credit strategies because of the leverage in the system. Now, after four years in the business, we have restructured our portfolios considerably because we think the credit and fixed income markets are implying severe distress in the system and in the economy.

The equity markets on the other side - the domain where I have grown up - seems to be a lot more complacent about the economy. So at this time, we have clearly reduced our equity event type managers and increased our credit and fixed income type strategies.

Girish Reddy



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Justin B. Dew

That is true. We definitely see a lack of follow through up to the downside in the equity markets relative to the credit markets. It's particularly relevant to the CMBS and RMBS markets and how those two marketplaces have adjusted so far in terms of spread widening. Certainly they widened to what most would consider historical levels, implying significant losses going forward from a default perspective. We certainly wouldn't believe that it's as bad as some of those markets would imply and are in some cases positioned in that regard, but I'd be interested to see what the perspective is for the rest of the group.

Glenn August

We recently added a structured product group – a team of professionals from Blackstone. They would share the view that I think all of us around this table have – namely, that there is a severe dislocation in the corporate credit structured market, and, you can almost say, in all forms of structured credit.

We think that the top parts of the capital structure are very attractively priced for buyers. Because of the deleveraging in the system, people aggressively sold the top part of the capital structure leaving what we think are good long-term opportunities. This goes even beyond corporate credit into higher quality mortgage paper. Leveraged loan assets are quite interesting, even though they have already rallied a bit.

In terms of the fixed income versus the equity markets, I would echo Girish's view. We have expressed that in our portfolios where we are net short unsecured debt and equities. This is because we see that disconnect. If you can make unleveraged 8% to 10% returns in senior portions of capital structures where you are investing at the 30%/40%/50% layer of the capital structure, we think that's incredibly attractive on a long term basis.

The default rates have been and still are very low, but we think they are going to go significantly higher; the ranges we have heard reach from 6%-13%. If that happens, there is going to be incredible opportunity, a once in a several generations opportunity, particularly in distressed and perhaps even in high yield.

George A. Kellner

We recently had a first closing on a distressed fund. The fund is structured as a delayed draw fund, so we have the opportunity to choose when we want to draw the capital. A lot of our investors have asked me if we are drawing the capital right now. The answer is no, not just yet.

Default rates remain very low at 1.5% to 2.0%, and while high yield spreads have widened to 600-700 basis points over Treasuries, they are still only yielding 10% to 11%. Furthermore, we believe that the economy is likely to weaken year-over-year and believe this will drive leverage higher. That is especially significant since the $800 billion of deals done between 2005 and 2007 were among the most leveraged in history. Accordingly, we believe that the large scale distressed market is more likely still to come, rather us being in the middle of it now.

Our sense is that within the next 12-24 months, especially as you see year-over-year earnings weakness and six times levered capital structures go to 8, 9, or 10 times leveraged structures, some very good investment opportunities will develop.

George A. Kellner

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Glenn August

We think the default rates are not likely to go up very much, very soon. This is simply because many of the deals done between 2005 and 2007 have no triggers. They have very few covenants and they include transaction documents that give the sponsor enormous room to bring in additional debt or to use additional equity to cure cash flow tests. Where they do have covenants, they are set at levels down 25%/30%/35% from plan!

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Glenn August

We believe this is going to lead to a distressed trading market for the next couple of years, rather than a change of control market. As year-over-year earnings come in lower and leverage levels increase, that debt has to be re-priced to equity type of returns. But, if these companies can ride through the cycle with a capital structure that has no covenants, there actually is a chance that investors can recover and get taken out of par in three or four years from now, yielding a 20% to 25% return.

We think change of control opportunities are only likely in the event of a severe recession, in certain sectors, like housing, autos and specialty finance, or in two to three years from now when some amortization on the debt begins.

Keith Moore

Examining how economic activity might influence specific hedge fund strategies - our business revolves a lot around merger arbitrage and corporate reorganizations - and certainly the credit crisis and weakening economy have had a dramatic affect on merger and acquisition activity. It has declined substantially from last year's record levels. This year it is down about 32% in the US, though I should point out that deal levels are about at their historic average, the last two years being exceptionally robust.

Going forward, we believe that there may be some significant changes. We believe that strategic transactions as well as cross border transactions are going to continue to grow and become the focus of the M&A market. We don't look for the large LBOs to come back anytime soon; but believe it or not there really are still a number of positive factors that can affect merger and acquisition activity.

We still are at very low levels of interest rates, and a lot of corporations actually do have quite a bit of liquidity on their own balance sheets. The trouble is getting the banks to lend to them. Over the last couple of months, some big corporations have been able to structure a number of very large transactions. The dollar's weakness is providing a great opportunity for foreign investors to acquire assets cheaply.

The big wild card here is inflation. We believe that inflation is probably worse than what is being reported in the media. We also think it's going to accelerate, given what the Federal Reserve's stance has been towards trying to stimulate the economy. In the last couple of cycles where we have had increased inflation, we have seen M&A activity accelerate tremendously. The notion is that it is cheaper to buy than to build will drive M&A activity.

We will see a strong renewal of M&A activity, but it's hard to pinpoint exactly when that might be. My personal view is that we should see the inflection point in the second half of this year. Increased inflation certainly is not going to be good for the American people trying to finance all of these higher costs, but it should present a good opportunity for both M&A activity as well as the merger arbitrage investment strategy.

Bob Discolo

I am not going to add anything on the economy, but just listening to what you are saying - words like dislocation, inefficiency, mispricing, undervalue, opportunity of a generation. For an investor, these are all good things. These are the things you want to hear.

I am not going to add anything on the economy, but just listening to what you are saying - words like dislocation, inefficiency, mispricing, undervalue, opportunity of a generation. For an investor, these are all good things. These are the things you want to hear.

If you just go back before last year, for the prior three or four years, everything was just bland and boring, low volatility etc., but now there is opportunity. I can say this just by looking at our portfolio - the managers we invest with and other managers out there - this is the first time in maybe ten years that no one is really closed. Every manager tells us he sees opportunities, and what I have heard so far at this Roundtable backs that up.

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Kevin Heller

As global head of research at Focus I spent February into April actually traveling through Europe and Asia. As everyone here knows, our sub-prime and credit issues really had a very strong reverberation around the world. Some of it happened for a good reason, there are obviously some European banks, some Australian banks that have some of these products and have some of the same capital requirements. But in many cases the reactions were in my view overdone and that creates a lot of opportunities.

From an equity perspective, in a lot of international markets and sectors, the baby was thrown out with the bathwater and I agree that this is a potentially very exciting time. As a hedge fund allocator, we are not looking at an equity market per se, but we are looking at an equity long short market. My travels this quarter were dramatically different than ones that I have had in prior years. Years in which the common theme was extremely low credit spreads and LBO money was searching the globe for very cheap companies that maybe should have been shorted otherwise...but you couldn't, since the LBO money was driving the stock up and stopping you out. However, now as you travel around, you are hearing more long/short equity managers talk about short books, short themes, and things to short, while at the same time having a reasonable basket of long ideas, or about divergences on the sector basis.

Financials are still arguably in trouble and there might be still be some shorts to pick there. On the long side, there are some commodity companies trading at very reasonable valuations. Personally, where I focus the most now is an equity long/short market, which hasn't been there for a while...

George Kellner

So you are suggesting that money is going to be made more on the short side than the long side?

Kevin Heller

More than it has been in the past. Maybe I will focus more on these sets of divergences, and I also think that even on the long side, some of the markets may have overreacted to U.S. markets and domestic U.S. issues. Of course the U.S. is still the biggest economy in the world and a slowing here will impact the global economy. The key question is to what extent have global equities reacted to that? I think the most important point I am trying to make, George, is that there are a lot of opportunities on both the long and short sides on a global equity basis, whereas in periods prior to "sub-prime meltdown", managers consistently talked about how it did not pay to short.

George Kellner

Emerging markets have suffered some big losses this year. From January until very recently I think they were down over 20% and even more in India and China.

These markets have declined by over 20%, yet the basic fundamentals are the same. Is India different today than it was six months ago (except that it is probably more attractive in a lot of ways)? The valuations have become more compelling. In the last few years, you couldn't really be that short because of the global bull market. Now that has changed. Market participants have become more risk-averse. It's the same old story: fear and greed, and now, fear is in the ascendency.

Girish Reddy

I agree with Rob. For the first time we hear from our managers that they are not having capacity issues, because of the opportunities they see. We invest in all sectors, and managers in all of them alert us to extraordinary opportunities: convertible managers say the issuance is up, the terms are really attractive, equity long/short manager say they can truly short and not get hurt, credit managers tell us about the higher capital structure, AA and AAA tranches, which look extremely attractive.

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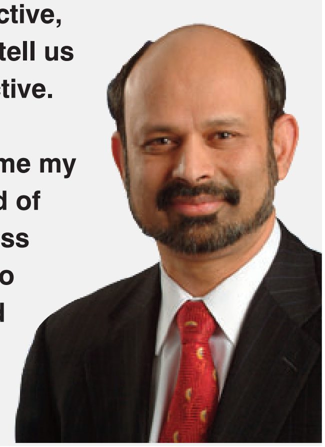
Hardly anyone we meet says "I have nothing to do, I am waiting for the markets to come my way". The other factor which we haven't touched yet, which is exciting for us as a fund of funds investing in hedge funds, is that when these things turn around, there will be less competition for alpha or returns. Because the prop trading desks at the banks have no risk appetite any more. You could say these are the guys creating the dislocation, and I can't see them turning around and buying bank debt at $0.91 after having sold it for $0.85 on the dollar.

Girish Reddy



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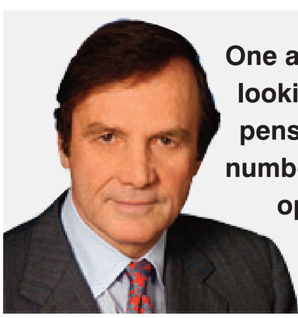
It's unlikely to see banks revving up their risk appetite anytime soon and I actually believe that hedge funds will be the beneficiaries by stepping into the right opportunities.

George Kellner

One area where we will also see innovation and new products is cash enhancement. We are looking very hard at creating a cash enhancement partnership. Many larger institutions, pension funds etc. need to have some way to improve their cash returns since quite a number of them have significant constant cash balances. There may well be a huge opportunity since one of the principal ways to enhance returns on money market instruments was the auction rate markets and you all know how that has turned out. These markets are dead and unlikely to ever resuscitate to anything remotely close to their former importance.



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George A. Kellner

In fact, our belief is that we can create 2-3 times the money market rate of return on cash accounts at virtually the same risk. This current environment brought about by the credit crisis gives rise to opportunities in areas that we haven't been explored fully in the past.

Tom Priore

Fundamentally speaking, there is complete asymmetry in the some investment opportunities right now. We think that a lot of that seems to be driven by the need for cash.

One of the things we have done at ICP is to position ourselves as a merchant bank. We have tried to position ourselves with the investment banking capabilities to originate structures, to change cash flows the way we want them, and to be a principal investor.

We see enormous opportunities going that route, to actually build the channels of origination. It seems our industry is crossing over into the banking world which can also include becoming a direct lender.

Tom Priore

The banks, the prop desks etc. are all regulatory capital players. They are leveraging the bank equity capital through procedures which really amount to a type of accounting game. That game is clearly over, but these opportunities in AAA, RMBS, in the highly rated sectors in CLOs and other structured products are presenting some attractive opportunities.

This is where we have focused. We have about $10 billion in AAA Prime RMBS assets with 30 year fix rate loan underlying. Those products backed by real borrowers who defined the leverage at the time of origination. Now these securities are trading in the 80s and that have 20 points to pull to par a month with a defensive credit profile. Here is one cash enhanced strategy with a very strong claim on cash flow. Because of the run we have had in equities and in CDS, you can pick up very cheap protection against fixed rate, prime borrower defaults, long before your cash flows in these securities is impaired.

I think one of the interesting questions coming out of the current environment is: With this decline in the bank prop desk area, with banks having less appetite to take on risk, how does that change our business?

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We see enormous opportunities going that route, to actually build the channels of origination. It seems our industry is crossing over into the banking world which can also include becoming a direct lender.

Girish Reddy

I believe we are going to see or are seeing already a fundamental change in a flawed financing model. To me it makes no sense for 30-times levered investment banks to be lending to hedge funds to lever up again 6-times. That is not stable capital. Hedge fund managers are now going to longer-term investors with more stable, dedicated capital and telling them to take advantage of these dislocations.

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You see that already in many areas, for example, infrastructure funds. Going forward you will see that funding will come directly or indirectly from these sources, from an insurer or pension funds.

I would phrase this phenomenon (and I just came up with the term), "permitted disintermediation." For many years, the banking community was very upset if you, as a client, wanted to talk directly to the sponsors about a deal - because obviously that would take away their opportunity to make an underwriting fee. But today, as the banks have such limited capital, and we on the other side have great sponsor relationships and capital, the banks are actually looking for partners to help them commit to the capital, and then syndicate it out.

Glenn August

Glenn August In the last six to twelve months, big insurers and pension funds - who have been long term players in these asset classes - have recently increased their allocation to us. In fact you will be amused, given earlier comments: some explicitly stated that they were taking money directly out of their equity portfolio and putting it directly into their credit portfolio. Here they are - our new sources, new providers of incremental capital.

Coming back to Tom's comment about forming a merchant bank, I agree this is one of the most exciting dynamics at the moment. I would phrase this phenomenon (and I just came up with the term), "permitted disintermediation." For many years, the banking community was very upset if you, as a client, wanted to talk directly to the sponsors about a deal - because obviously that would take away their opportunity to make an underwriting fee. But today, as the banks have such limited capital, and we on the other side have great sponsor relationships and capital, the banks are actually looking for partners to help them commit to the capital, and then syndicate it out.

In the last six months, we have worked directly with a number of banks and some very large sponsors. In one case, we worked with a bank where the bank was not a capital provider, but a pure intermediary, a less financially remunerated intermediary. They were basically trying to assist their client, but could not do so with their own capital. We have provided a couple of financing commitments in the $1-$2 billion range, in which we formed a syndicate of 7 to 10 of our buyside relationships to help provide a financial sponsor with a "no outs" financing package to bid for a company.

In both cases these deals didn't happen, but the fact that we could actually work with a bank partner to raise $1-$2 billion more than once seems to suggest that there will be exciting opportunities, at least for the next six to twelve months. If you think about it, the current situation is very similar to 1990-1992.

One of my partners recently prepared an analysis of companies in today's financial crisis to the same period in the early 1990s. In short, all the major banks stocks were down by comparable levels, as these institutions digested the financial markets crisis and recession of the early 90s. The situation today is nearly identical. And yet, within 2 to 3 years from 1990-1991, the crisis was just a memory, and so it may very well be that this permitted disintermediation may no longer be permitted in 2010-2011, but right now there are some very exciting opportunities.

Tom Priore Fundamentally, the world of financial services is changing in that regard. There is a window of opportunity for people like us to disintermediate and create a new system that can stay in place - that does not necessarily go back to the old guard at some point in the future.

Antonio Munoz It is interesting to hear all these dichotomies. We talk about great opportunities soon to come, but they're not quite ready. We have just expressed our concerns that the current floor may not be a floor. We may be trying to catch a falling knife and we all forget, particularly the managers we invest in (that means you guys), we forget how bad it can get when it gets bad. I am skeptical enough to know how bad it can get. As everyone knows, we just started the 21st century, with these 25-Sigma events. I am really tired out hearing managers, "Oh! This was a 25-Sigma event; God we never expected that!" And the last twelve to eighteen months have been a 50-Sigma event, or whatever it is.

It's interesting how you guys are raising funds. Hopefully, you are not charging fees while you have not invested the capital...Personally speaking, we are not the buyer into this intermediation idea. We do agree, there is no doubt that the transportation of risk-taking is happening, so let's focus for a moment on that transportation of risk-taking. We have seen that over the last two decades, the next round of investors get smarter, and at the same time they also forget some basic things.

The prop capital will not participate in such plays - I used to be a prop trader so I can really blame them - but on the other side you have all the multi-strats, multi-events and arbs, all these multi-hedge fund types that are all starving to come into the same areas. Perhaps some of you will go into different areas, but overall everybody is looking at the same plays, the same asset class, same geographies etc. With this herding effect, I wonder if the IRR's will be as interesting and appealing, as you know/think them to be? Is the liquidity going to be as easy as it used to be?

George Kellner

Just two observations. One is that it seems to me that if capital moves into financial assets, that's one set of facts, but if it moves into real assets then that's a different set of facts. I am referring here to that synthesis of private equity and hedge funds which is occurring among the big players. You guys who are running multi-billion dollar hedge funds are in a unique place. Due to your size and given the opportunity, some of the large hedge funds are starting to look at real assets as opposed to financial assets. I think that there is a very important distinction between these asset classes and this should be watched carefully.

Secondly, in comparison to your larger size, we are relatively small, and we see terrific opportunity in off-the-run distressed and similar type plays where moving between the feet of the elephants can be quite profitable.

In fact, we probably have portfolios that are completely different from others in the room and your portfolios are probably alien to me. There are a lot of attractive situations in the smaller corporations which today are unappreciated and not even looked at by most people because of overall bigger credit problems. When folks are worried and scared, they often ignore even terrific opportunities in the less followed sectors.

Bob Discolo

I think we all agree there are opportunities out there, including big or mega-opportunities. We had our client conference back a few months ago and one presenter, an economist, asked a question to the global audience - "*Are you positive on the economy or negative?*" Of the 150 people there, two raised their hands for positive, two or three were negative, and the rest did not even move. This shows people are very apprehensive right now. Everyone is sitting back and holding cash.

It's funny when Glenn mentions that someone sold their equities and invested it into his credit fund. We are seeing people sell things but going into cash. We see a lot of money on the sidelines.

On the other hand - you are running a credit opportunity fund? At AIG Investments, we must have had 45 people come to our office with credit opportunity funds. Everyone is starting one of these funds. But people aren't funding those funds just yet. I think they are a little apprehensive of what's going on.

To some extent, this really affects the industry, cash is king and if you have money to allocate, you have probably received twice as many phone calls as you had last year. With all of these managers asking for capital, I believe now is a great time to strike bargains. That is basically why we are setting up a seeding joint venture. We think there is talent, we think there are opportunities, we think we can get money too and pull in fees. But, as with all things, in a year or two, it's all going to be changed again.

If you are a pension fund, you may sit back and think for a moment, saying ”Well I have 10% cash now, let me reallocate a bit. Oh wait a second, I have a 1% allocation of hedge funds. I am going to double, triple, quadruple that because last year I did fine, I made 10/11/12%. And this year so far - although I didn’t make money, I didn’t lose too much money either and things are coming back…” The education level of the trustees involved in these pension funds is there, and I think the sovereign wealth funds will not invest in treasuries; they will invest in hedge funds.

In my view, the hedge fund industry is going to grow tremendously, more than we are ever imagining it. But I think there are going to be a lot of winners and a lot of losers. That is why our job becomes much more important.

My final comment refers to our discussions about hedge funds stepping up in the capital markets...If I go back 10-12 years ago, everybody was talking about Steinhard, Soros and Tiger, saying all of these big hedge fund companies are going to be the next Goldman Sachs, the next Morgan Stanley. Today, they are all out of existence, but we are talking again about these giant hedge funds as if they are going to live forever....

Antonio Munoz

Again, I may be the skeptical one but we are very nervous about whether this is the right timing to jump into all these great capital market players, (i.e., acting as investment banks etc) and great new managers with everybody being open and everybody wanting money. It may have to do with my emerging market background, but I know that what you find now at 40 could go to 20, and 10 and nobody gets it until everybody is bleeding.

I agree it is funny that ten years ago there was this talk about these hedge funds going to be the next Wall Street behemoths, but by the same token there were many more banks that are not around now either, so again we find that transportation or transformation of risk-taking. And I don’t think we have seen at all the consolidation in the financial industry or the asset management industry.

We have been talking a lot about macro views but to some extent, that has very little to do with what I actually do on a day-to-day basis, which is a more bottom-up manager selection.

I want to support Antonio a bit here in his skepticism. We have been investing in distressed and high yield for at least the 10 years that I’ve been at the firm. While the fundamentals of this strategy had changed with the credit spreads going tighter and tighter and leverage levels going up, you do have to wonder to what extent the managers understand these dynamics; or, if they have chosen to ignore those facts.

I met managers when credit spreads were at 1400 and they said “this is a great opportunity”; then it was 800, “great opportunity”; then 600, “great opportunity”; then 200, “great opportunity”. And when I ask the manager, “at 200 over, are you being rewarded? Why aren't you shorting? Why aren't you hedging? Where are you moving your capital?” I often get to hear that I was the simpleton.

Kevin Heller

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it was 800, “great opportunity”; then 600, “great opportunity”; then 200, “great opportunity”. And when I ask the manager, “at 200 over, are you being rewarded? Why aren’t you shorting? Why aren’t you hedging? Where are you moving your capital?” I often get to hear that I was the simpleton. That I don’t understand credit risk is being spread out and balance sheets are reduced. That I don’t understand this time it’s going to be different, there is a new paradigm etc. I seem to have a hard time finding a broad group of managers in structured credit products that change their view and their portfolio over the credit cycle.

As an allocator, we are faced with macro-view versus a draw-down, the market view basis...I can’t argue with anything we have discussed so far at this table, like there maybe some junior tranches worth zero but maybe the senior tranches aren’t worth seventy and that’s where they are trading. I won’t argue about this, but on a day-to-day basis what we want to know is if a manager has a real understanding of who the players are in the market:, what they will likely to do, what the liquidity is, etc. We want to see them pay attention to timing, leverage levels, risk management and things like that. It is not just looking at a ten-year view, but how to implement a strategy on a monthly and/or quarterly basis. As an allocator, if I can’t get comfortable with that, we are just not going to allocate.

Glenn August

When I started in 1987, the high yield market was a $250 billion market. Today, the cash market is a $2.5+ trillion market, and the derivatives market in below investment grade leveraged finance is at least $7.5 trillion. So that gives you a $10+ trillion market. There are so many hedge funds, credit funds, CLOs, credit opportunity managers, that the firms are running out of names for new funds!

Yet for experienced investors with capital, this is an extremely interesting time. Despite the sentiment that the economy is going south or sideways, there are good managers looking at really good investment opportunities. As a hedge fund manager, that is what we do - look at opportunities while managing risk in terms of asset selection, leverage and liquidity. If you can find those right investments (from the long side or from the short side), and if you have a process that prices risk and return, then you’re doing a good job for your investors.

At Oak Hill, we have grown our business very deliberately over the years, not just for the sake of growth, but because we want to maintain relevance in the market. In many cases, you are not relevant today to a sponsor who has $50-$60 billion of capital if you’re running $2 billion, and can only take $30 million in a deal.

Justin Dew

I think it’s interesting that a lot of the fund of funds say ”we are looking for new ideas and opportunities, for people that think differently, the non-typical view”, but at the same time the preponderance of capital being allocated to hedge funds are going to the same usual suspects.

I used to be on the allocation side as well and in an investor committee meeting there is a certain kind of risk to suggest a small manager. Even if you think he is smarter than the next guy. But because he may not work at the biggest shop in the world, no one really wants to recommend him or her. So, with allocations accumulating at the big shops, this also contributes to the evolution of hedge funds into mega banks or replacements for banks...

On the topic of “Hey! is it time to jump in?", or: “Hey! go out and load the boat up, get long, just don't worry about hedge's, we're at the bottom...” - I don't think anybody is suggesting that. What is being said is that there are some fundamentally very low volatility cash flows that investors can invest in on the long side and buy protection against the disruption of those cash flows at very attractive levels. Why? We have said it here, cash is king. There's a dislocation, there's a supply-demand imbalance in cash – between those that have it and those who need it.

So you can access cheap cash flows and hedge them very responsibly, to create stable return profiles which lets you manage the NAV growth without a great deal of volatility

Tom Priore

Tom Priore

If I can just maybe comment on a few of the themes that have come up. First off, on the topic of "Hey! is it time to jump in?", or: "Hey! go out and load the boat up, get long, just don't worry about hedge's, we're at the bottom..." - I don't think anybody is suggesting that. What is being said is that there are some fundamentally very low volatility cash flows that investors can invest in on the long side and buy protection against the disruption of those cash flows at very attractive levels. Why? We have said it here, cash is king. There's a dislocation, there's a supply-demand imbalance in cash – between those that have it and those who need it.

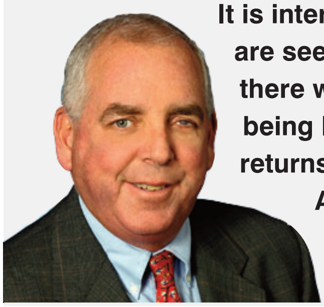
So you can access cheap cash flows and hedge them very responsibly, to create stable return profiles which lets you manage the NAV growth without a great deal of volatility, that's point number one.
My second statement refers to the disintermediation we have touched on, whether or not it's going to continue, how profitable it is etc. I have a bias in that however, to me it is a no-brainer.

The capital market is fundamentally a pretty simple place where banks package raw materials into securities for distribution. George mentioned that you have to look at whether you are investing in real assets or financial assets. Well, those financial assets, they are made of real assets. They are made of loans on properties. Whether it is commercial real estate, residential real estate, or loans to companies etc. Those raw assets get packaged up by investment banks that add a fee and ship it out to traditional relative value investors. Fees that can be taken out provide embedded return, there's profit in that. Disintermediating the banking process to the extent that you can, will present additional return.

The challenge then becomes - and I think this is where the rubber meets the road - how do you then take those plays that you think have the right value and use the capital markets to access liquidity? You present your idea to other capital markets participants the capital markets: mutual funds, banks, insurance companies or hedge fund investors etc., and according to their profile they may want to help you finance your long term goals or your leverage goals on that underlying asset.

That's the world of investment banking. That has traditionally been their domain and that's changing and I think the opportunities are there for businesses like ourselves to have the flexibility to perform those types of activities..

I want to highlight for a moment some specific opportunities that the markets present to us at this very moment. I earlier commented how much M&A activity has declined as compared to last year's record levels. This provides us with fewer choices, and you would think that it might be less profitable to be involved in the merger arbitrage business.



It is interesting that reality is quite to the contrary. Even though we have low interest rates, we are seeing very attractive spreads. In the last cycle when we saw interest rates decline, there was also a lot of competition, and capital was flowing into the business. With rates being low, people also accepted lower rates of return and quite frankly, the investment returns declined quite dramatically.
As a follow up to what Antonio was saying about risk premiums, this may be one of the few investment areas where the risk premium is priced to a large extent.
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As a follow up to what Antonio was saying about risk premiums, this may be one of the few investment areas where the risk premium is priced to a large extent.
Despite the credit crisis, we are seeing plenty of really high quality situations where we can put money to work on an annualized basis in the low to mid teens without even ratcheting up risk or leverage very much.

Girish Reddy

I think all of us in our discussion continue to focus on opportunities that look attractive on a fundamental basis. We may be forgetting that technicals in the market have created this dislocation and will continue to dominate the fundamentals.

The technicals continue to worry and scare us. We actually don't think the market fully understands the deleveraging that still needs to be done. I think in the next couple of quarters there could be a lot of surprises from banks and investment banks where the "hedged portfolio" will not work out as hedged as it should have and the banks will continue to deleverage as these hedges do not work.

Matthias Knab

So what are you investing in?

Girish Reddy

We are currently focused on fixed income and credit opportunities particularly in the mortgage securities.

With proper risk control, bank debt, residential mortgages, commercial mortgages, mortgage servicing opportunities, IO instruments all look attractive - if hedged correctly, you can get high single digits and low double digit returns with very little leverage. Returns relative to the risk in a low interest environment with little or no leverage looks very attractive.

Glenn August

The older I get, the more we appreciate technicals. Today is interesting because we have both investors and allocators together at this roundtable. Technicals are ultimately a combination of supply and demand, obviously. If you take a close look, the deleveraging is actually demand and increasing the supply of paper. Because Investors who would normally be buying the paper are getting deleveraged themselves.

All of us in this room, with probably $50+ billion of capital to spend (leaving AIG out, which would multiply this number), have grown our businesses pretty dramatically in the last few years. My question for the allocators around the room, the question I ask myself on a regular basis is: Will there be an unwind in those flows?

While a lot of institutional investors are still underweight alternatives, what keeps me awake at night is the thought of a substantial unwind in the hedge fund business. If there was an unwind, there would be an enormous supply/demand imbalance. I am just curious: Is this a scenario that can happen? Is is a matter of when versus if? And if so, when might that be?

Kevin Heller

I represent the smallest of the allocators here in this room, but still, interestingly, while the first quarter of 2008 was probably the worst performance for hedge funds in ten years, we're getting more and more meetings with pension funds. It's picking up pace, and I can't confirm these end investors would be shying away from the asset class.

Also, in this Roundtable we've been talking a lot about credit and certainly there are other strategies out there like health care funds, energy funds, commodity traders and so on. Addressing credit hedge funds, I made that point before that I saw in the last credit cycle where a lot of people see the opportunity to put on leveraged structure credit products and then they don't see when the time came to get out and hedge. If a better job can be done this time around, perhaps managers can attract interest again. But, I would have to ask myself if investing in products that by definition need to use financial leverage would be superior to an unleveraged investment in say a distressed strategy, Asian equity strategy, event driven strategy, etc.

George Kellner

There is a reason why, over the past one and a half years or so, some large firms like Blackstone have raised equity - to avoid that problem. Permanent capital has been the big issue for hedge funds. You either go public (if you can) or lock up investors for three to ten years or however long you can do it.

Girish Reddy

The fundamental attributes of hedge funds are attractive. Investors prefer protection on the downside and participation on the upside. Hedge funds have done a reasonably good job demonstrating that they can deliver this and so I believe the growth will continue.

Pension funds historically took a lot of tracking risk by being heavily invested in equities relative to their liabilities, hoping to capture the additional risk premiums. This has come at a large cost and volatility as equities underperformed over the last 10 years and funds have had to make contributions.

Today, a portfolio of hedge fund strategies with a derivative overlay can better match liability risk and still generate stable alpha. Pension funds will start moving more to an endowment model and "alternatives" will become "main stream assets".

Tom Priore

Price is a reflection of where you can finance. What Girish may call technicals, I think of as liquidity. It includes risk management and maybe more so, how do you manage your financing? As hedge funds, we are effectively managing a finance company. Our liabilities are the permanence of our capital. Our liquidity terms are in a relation to the liquidity of our assets versus the permanence of our financing on those assets, the different ways our capital can get called away.

What keeps me up at night is trying to plan for what was mentioned by George: how do you create permanent capital? How do you create an operating company environment? Not one that is a hedge fund balance sheet, but a financial services company balance sheet - with a real corporate balance sheet to borrow against, to raise equity against so that you can maintain your commitment to certain marketplaces where you can excel over a long term.

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Tom Priore

Antonio Munoz

I agree with Girish that all of these institutional allocators - certainly the pension plans both private and public, will invest more and more into the hedge funds. And they demand more and more institutional quality. However, in the short term, I want to point out that for the second quarter I expect a massive net redemption coming for hedge funds. Considering that at least 30%-40% of hedge fund assets are coming from fund of hedge funds, this also means there is a massive net redemption at the fund of hedge funds levels.

These redemptions may be driven more by the retail high net worth investor than by the institutional investors. And here is another dichotomy: yes, more and more, there are a few institutions showing interest coming into the asset class, but they are not investing yet. Meanwhile, at the same time you see other allocators coming out. So I guess this is one of the first times we could be experiencing quite severe net redemptions in the second quarter, and it could even get worse in the third one.

I agree the industry will grow. The larger firms will get larger. The smaller firms - I am not sure they will get larger, and the smallest, I am not sure if they survive. It's not just about your return profile or certainly your risk management, it's more about how you conduct your business as a business. It's about all the operational aspects of the firm, the compliance etc. To a certain degree, who cares about 200 or 300 basis points of performance, if you fail in these vital aspects? The key issue is how many emerging, talented managers are going to be able to put together an institutional quality shop that will be able to attract the institutional capital.

The demands regarding "being institutional" will only be increasing. The amount of operational due diligence, of legal and infrastructural checks, risk management etc. causes a very unequal treatment of start-ups versus established funds.

Bob Discolo As an allocator, one question you often come across is who is really delivering the better performance, large funds or small funds? I can show you 10 studies that say small funds do better than large funds, and then there are 10 studies that say just the opposite.

As an allocator, one question you often come across is who is really delivering the better performance, large funds or small funds? I can show you 10 studies that say small funds do better than large funds, and then there are 10 studies that say just the opposite.

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Bob Discolo

At AIG Investments, we thought we would do our own analysis. Surprisingly, we found the returns are almost exactly the same. So, in our case, we like big funds and we like small funds. The next question then becomes, are these two groups doing things differently? If so, to what extent? Are they providing alpha that is different from the other group?

Glenn August What was the correlation between the small bucket and the large bucket?

Bob Discolo It sort of depends on the strategy..

Glenn August Ok, so if you look at it by strategy, was it high or low?

Bob Discolo It was actually lower than I thought. It was much lower than I thought with certain strategies. But then again, for some strategies you just need larger funds, there are economies of scale and such things involved.

We have investments in pretty good managers. They are very good at controlling the debt piece of their balance sheet, prime brokers and credit lines and things like that. One of the problems we're seeing, where I am actually shocked, is seeing how they have managed their equity piece - their investors. I think also some funds of funds have gotten too large. People will disagree with me, but if you're running $20 billion or $30 billion, you are doing $0.5 billion allocations, and when the new boss comes in, which always happens, they are going to say, "*Well you know what, I don't like the way that guy dresses and so we're going to pull out.*"

We had a manager who suffered a $700 million redemption from one single client - that's a big number for any fund. So I think it gets a little scary there....
Coming back to our question, "Where should people invest?" I think people already know about the ideas. The reason why people aren't investing right now is because they are afraid. Just look what happened last year. A lot of people said, "Well, in August credit markets kind of collapsed, so let's go in September" - and they got burnt, so I think they are waiting right now.

As we all know, the business is now much, much more complicated. Ten years ago, we had a handful of hedge fund strategies, I understood everything personally. Now, I have 30 specialists around the world helping me. There are some things I don't know, and I will admit that right now. I have a CFA, CPA, MBA, CAIA and all of that great stuff, but I am just shocked when I see big pension funds writing large checks with one person or two people in charge of the program. I think they don't understand, especially things like structured credit or volatility arbitrage. These are complicated strategies, and I think people are just apprehensive about doing it.

Matthias Knab **What do you tell these people? What do you recommend? What do you want to alert them to, or what do you want them to think about?**

Bob Discolo If you ask anyone: "What's your biggest risk in hedge funds?" they all are going to tell you the same thing: "Blowing up, my name in the newspapers, etc." We think the biggest risk in hedge funds is mediocrity in correlation. We talked about emerging markets -- they got killed in the first quarter. Let's be realistic, most of the managers are doing the same thing, so if you study them and try to find out what they are doing different than the regular emerging market mutual fund manager? The answer for most would be - nothing.

You may be allocating to hedge funds in the emerging market, while you may have emerging markets already in your portfolio, so you may be doubling that allocation and secondly, you are probably paying three or four more times in fees.

If you are a large pension fund, you may decide to take out the extra layer of fund to funds than hire the right staff to do it. Investors really have to understand what they're doing there...I think every hedge fund here has at least 10 stories like "this guy came in to see me, I had no idea what he was doing, but he still gave me money...." It's surprising how some of them make the plunge into hedge funds.

And speaking to those who haven't allocated to alternatives at all, if you're running a pension firm right now and you have a lot of money in cash, you can't stay there for too long. Your liabilities are here and your 60:40 split is down there. Many pensions are trapped with that gap, and they have to do something.

Glenn August But the shorts will make them nervous...

Bob Discolo Yeah, while things just get worse. I think people have to start moving to do something. I am not saying it should be necessarily hedge funds or any particular strategy, but they have to do something.

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