



**Opalesque Exclusive: As FoHFs seek ways to win the liquidity and risk management battle, Markov releases paper titled `Monitoring Daily Hedge Fund Performance When Only Monthly Data is Available`**

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From Kirsten Bischoff, Opalesque New York: With 80% of hedge fund redemptions flowing through fund of hedge funds (even after positive performance in the first quarter of 2009), this sector of the hedge fund industry is facing an uphill battle to get back into the good graces of investors. Liquidity issues plaguing the global financial markets have had an exaggerated effect on fund of hedge funds due to their inherent delay in reaction time because they form an outer ring within the hedge fund industry.

"If you ask any fund of hedge funds or investor in hedge funds, the biggest issue today is liquidity," Michael Markov, CEO of Summit-NJ based investment research firm Markov Processes International told Opalesque. "Anything that will address this issue is at the top of their interest."

**Closing the gap on reaction time**

The challenge of improving investors' insight into hedge funds performance intra-month led to the Wednesday release of a research paper titled "Monitoring Daily Hedge Fund Performance When Only Monthly Data is Available". Markov and his co-authors Daniel Li, Quantitative Analyst, MPI; and Russ Wermers, Associate Professor of Finance at University of Maryland's Smith School of Business have released the paper (which is still a work in progress) earlier than expected, so that investors considering allocating to the hedge fund industry are made aware at the potential for transparency in such investments.

Although MPI provides its clients with an array of analytical tools and methodologies (including hedge fund index performance projections at the close of each month), the goal of the study was to create a very simple approach that will allow investors "to model the risk of their hedge fund investments, on a daily basis, using commonly observed investable assets with liquid, daily market prices."

The modelling, which allows an investor to project a fund's performance on a daily basis even as hedge fund managers are only disclosing NAV on a monthly basis, is meant to close the reaction-time gap for investors in hedge funds such as fund of funds. "It allows them to see [performance] coming and to make redemption decisions and hedging decisions intra-month, before they get numbers from funds," says Markov. Although MPI has concentrated on long/short equity for this paper, Markov says the process is applicable to any other strategy, and the team will be adding research into other strategies as they continue this work.

The authors suggest that during October 2008 hedge fund investors may have expected poor performance from their managers, but had little ability to evaluate the extent of these losses until managers reported results (which averages 3-5 days into the following month). Without an accurate indication of potential portfolio losses, these investors were not able to react with prompt risk management (such as hedging investments by allocating to other areas).

[http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1362265](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1362265)

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