REUTERS

Reyl says time ripe for hedge fund seeding

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By Martin de Sa'Pinto

ZURICH (Reuters) - Money has been flowing back into hedge funds in recent months after gushing out during the financial crisis, but only to the largest, most liquid funds, leaving glaring opportunities for more intrepid investors.

The dearth of investment in hedge fund launches since the financial crisis struck has allowed willing seed investors to profit from both the funds' performance and take a share of future revenues, a Reyl Group executive said on Tuesday.

"The difficulties faced by hedge funds trying to raise capital are allowing investors who can provide seeding to cut great deals," Fabrizio Ladi, head of alternative investments at Reyl's Asset Management arm told Reuters in an interview.

"There is a shortage of risk capital available to new managers. It is at historic lows. The premium for those who can provide it is at historic highs, so it is a great business opportunity," Ladi said.

But since the crisis whacked performance at many funds and several blow-ups and frauds hammered the industry's reputation, investors have preferred larger funds, considering them safer and subject to tighter scrutiny than smaller ones or startups.

But, said Ladi, that means some opportunities go begging.

The Geneva-based private bank has seeded five funds to date through Reyl Accelerator, a vehicle advised by London-based hedge fund specialist FRM Capital Advisors which seeds start up hedge funds.

Funds will be seeded with $30 to $60 million, with the aim of seeing successful managers growing to at least ten times the size of their seeding, Ladi said.

By investing in FRM deals, Reyl Accelerator has a multi-year share of future revenues from the seeded funds, giving investors a revenue stream beyond just investment performance.

"We can recycle our capital every two years, while retaining revenue streams of funds seeded in the past," said Ladi.

"The longer investors hold the shares, the higher their profit potential. If we seed 30 deals over six years while holding on average ten funds, investors have market exposure to ten funds but receive a profit share from all thirty."

The fund, which has seeded five startups and may complete two more seedings by October, has been offered to a few large, sophisticated clients. It may within some months open to clients investing a minimum 250,000 euros ($316,000).

"We want to build a stable of products and a track record first, we hope to present ourselves to clients when the market is a little less nervous about capital raising," Ladi said.

Like a private equity fund, Accelerator calls for cash only when needed, preventing uninvested cash from being a drag on performance. After being locked in for a year, investors will be able to withdraw their money semi-annually.

Ladi said he also wants funds seeded to apply a lock up.

"We never want to see our managers become forced sellers because they have to satisfy redemptions, you want to be a buyer at that moment," he said.

Ladi likes illiquid strategies such as event-driven, which looks for catalysts such as takeover bids to boost the value of its investments. Fat corporate balance sheets could support an accelerating wave of mergers and acquisitions, he said.

Distressed debt strategies should also perform well, along with equity and debt arbitrage strategies, Ladi said.

Investors preoccupied with liquidity were missing out on big opportunities in less liquid strategies while crowding out the returns in more liquid ones, which could in the end work against them, he said.

"People are overpaying for perceived liquidity, but at the moment they all run for the door it's not going to be there."

(Editing by Mike Nesbit)