BIZCOMMUNITY

Call for policy change in hedge fund investing

By Linda Ensor

11 Jan 2016

The prohibition on unit trusts investing in hedge funds should be removed so they can better manage their risks, particularly in the current context of market turbulence and volatility, says an industry expert.

©zerbor via 123RF

Robert Foster, chairman of the Association of Savings and Investments - SA's standing committee on hedge funds - has urged the Financial Services Board (FSB) to consider a change in its policy on the prohibition. His comments follow a clarificatory notice issued by the FSB last November to the effect that the prohibition of unit trust investments in hedge funds remained in place.

The clarification was contained in the draft regulations regarding the conditions for pension fund investments in hedge funds. The industry has until 29 January to comment on them.

Currently pension funds are allowed to invest up to 10% of the value of their funds in hedge funds on condition that no individual hedge fund receives more than 2.5% of the 10% subject to normal investment guidelines. Foster believes that this limit is too low and should be increased. He said the hedge fund industry was concerned that collective investment schemes that complied with all the regulations pertaining to pension funds were not permitted to invest in hedge funds, which was an anomaly, as both collective investments and hedge funds were subject to the same law - the Collective Investment Schemes Control Act (Cisca) - and the same regulator. Hedge funds were regarded as a legitimate investment vehicle in terms of the law.

"You would expect that on this basis they would be allowed to invest in each other's products," Foster said. He believes that the prohibition limits the ability of collective investment scheme fund managers, as well as pension fund managers to manage risk efficiently. The first regulated hedge funds were approved last month and Foster hoped that as more were approved in the coming months the FSB would change its stance and liberalise its approach to unit trust investments in hedge funds.

Draft conditions

Bowman Gilfillan Africa Group senior associate Naticia Chetty noted that in terms of the new draft conditions for pension fund investments in hedge funds, they could invest only in a hedge fund that was administered by a manager registered under Cisca. Pension funds investing in hedge funds must also monitor compliance by the manager with official notices, including compliance with rules on the inclusion of derivatives in the portfolio.

"The draft conditions also provide for transitional arrangements with respect to pension funds currently invested in hedge funds whose managers have not been registered as managers of collective investment schemes. The transitional arrangements place various obligations on the pension fund such as monitoring compliance by the manager of the hedge fund with any time periods and other conditions determined by the registrar of collective investment schemes for the application as a registered manager under Cisca," Chetty said.

"The explanatory memorandum issued together with the draft conditions states that despite the declaration of a hedge fund as a collective investment scheme, any investment by a pension fund in a hedge fund is regarded as an investment in a hedge fund as defined in the regulations to the Pensions Fund Act. As such, any direct or indirect exposure to a hedge fund must be disclosed by the pension fund as an investment into a hedge fund and the pension fund need not apply the look-through principle in respect of the underlying assets of a hedge fund," she said.

Source: Business Day