

Further evidence that hedge fund managers don't always know what investors want

Just yesterday I was talking to a fund manager from Australia. He had launched an equity and equity options fund two years ago, performance had been good and he was on the road to raise capital.

His pitch was to launch immediately into the options trading strategy, which was fairly sophisticated and interesting. He spent nearly an hour talking about his choice of strikes, his decision to take delivery or roll, how he rolled, how he scaled in or out of a trade. At the end of this I asked him a simple question: How do you choose which stocks to execute your options strategy on?

It was only then that he began to tell his story of stockpicking and he turned out to be a good stockpicker. What to him was a matter of course, to an investor was of utmost importance. Here was a stockpicker, someone who analysed companies, their asset value, their cash flows and earnings, their return on investment, the quality of management, the soundness of their business model, and what does he concentrate on? Trade expression. The pitch was back to front. Selling his story as he had done so to many investors would have led them to lose interest or misunderstand and run scared. The diligent investor would have discovered his edge or his fundamental style of investing, but they would have been made to work hard to find it.

This manager was trying to raise capital. Clearly he wanted to impress. But he didn't know what investors want and so went about it in reverse. He could have said, look, I'm a good stock picker, I am an investor, not a trader. Here is how I

pick stocks. When I am done picking stocks, I find the best way of expressing my long and short ideas. Here is my option strategy. Instead he would have given a potential investor the impression that here was an options trader, mostly writing options and thus open to tail risk, often getting exercised and thus not the best risk manager, and with little consideration to the quality of the underlying securities...