



# MAXIMISING YOUR FUND PROVIDER RELATIONSHIPS

AMANDA MCLEAN, OF INTERACTIVE BROKERS, PROVIDES INSIGHT INTO SELECTING THE RIGHT SERVICE PROVIDERS FOR YOUR HEDGE FUND

**A**s competition picks up for fund managers looking to capture performance and seed capital from potential investors, the fund providers selected during the early launch process can often help maximise the fund's long-term success.

Over the last few years, due to Fatca regulations and enormous compliance burdens, many traditional prime brokers have asked managers to seek out new clearing firms at the early start of a fund's launch, which can create mid-year disruptions.

Even if they have the time to pick a new prime broker-

age firm, the manager's investors may not take well – or understand – the notice of a business disruption so early on in a fund's inception, and that single event can potentially shake investors' confidence. Managers of new funds want to avoid vendor turnover and focus their time on trade performance, so here are some tips to help you select a prime broker for the long haul.

## FINDING A PRIME BROKER PARTNER

It is important to ask the right questions to avoid potential pitfalls. Make sure your clearing firm can support your strategy. If breadth of product is important to you,

ask how many asset classes you can access. If trading around the clock is essential, determine if the broker provides a 24-hour global trade and clearing solution. If you hedge in options or futures, you want to make sure that your prime broker can support your trading in all products through one single account.

For example, so far this year, the industry has seen an uptick in the formation of quantitative funds and with funds that employ some type of systematic trading as a part of their overall strategy. Therefore, it is important to make sure that your prime broker can support API and FIX connectivity and can integrate with your in-house built strategy. Moreover, your prime broker should be able to easily integrate with your other vendors for portfolio performance and trade reporting needs. Less sophisticated prime brokers, or firms that introduce to larger firms, may not offer this level of integration and that can create latency and performance issues with your strategy and operational workflow hurdles that require additional staff.

Make sure the firm is clear about any commission minimums, ticket charges or monthly custodial fees. Hidden fees can come as a nasty surprise and hurt your fund's performance.

Check the company's net capital and other measures of financial security. Generally, a clearing firm's ability to provide a turnkey solution for all of your trade, clearing and reporting needs will ensure a seamless day-to-day trade workflow that will let you focus more of your effort on trading and performance and less on operational tasks.

Lastly, a prime broker's balance sheet offers your partners comfort that you are working with a solid clearing partner.

#### DOES MY PRIME BROKER BUY OR BUILD?

Find out whether the prime brokers you are considering "white label" outside products or develop technology in-house for the way markets behave today.

You should select a prime broker that offers block trade allocation, rebalance tools and reporting and can handle all of your service needs with one login point. Ask whether you can manage multiple funds all under one umbrella on a single platform. Also make sure the algorithms and trading tools your prime broker provides are geared towards best execution and accessing all available liquidity without having to worry about whether the firm has a competing trade desk or that they are selling your order flow. You simply have to check a firm's 606 order routing report to confirm whether they are routing your orders directly to the market.

#### STOCK LOAN AND MARGIN FINANCING

Confirm stock loan and margin financing costs. These can hurt fund performance and are sometimes less transparent to fund managers. If you have to call in to short stock, sell or purchase bonds, or do not see your interest charged fees until month-end, you should think about selecting another clearing firm. Look for a firm that posts its stock loan inventory online and provides indications on borrow fee



**Amanda McLean** has over 24 years' experience in the financial industry. McLean traded London exchange and over the counter derivative products for many years and assisted in running algorithmic institutional sales for Edge Trade Inc., which later merged with Knight Securities Inc. She joined Interactive Brokers in 2007, where she works closely with both established and newly formed global institutional hedge funds, wealth managers and institutions.

rates in real time. If your fund trades internationally, look for firms that offer global stock loan programmes.

#### HEDGE FUND CAPITAL INTRODUCTION PROGRAMME

Ask if the programme caters to the firm's top funds or if they actively allow you to post performance and offer your strategy to the firm's wealth managers, private banking clients and accredited investors. For example, some prime brokers will let you post contact information about your fund as part of the firm's online hedge fund capital introduction programme if you have an audited track record and meet a certain AuM threshold. Some may even facilitate investments into your fund directly from their clients' accounts.

#### HOW CAN MY ATTORNEY HELP?

Some prime brokers can recommend attorneys to help managers form their funds and some even offer compliance support in-house. Attorneys can assist you in preparing marketing materials that showcase your background and investing experience to help give prospective investors an understanding of how your strategy is unique from other managers. Having well-prepared formation documents can position you better in your discussions with potential investors.

Your attorneys may also know of funds of funds (FOF) and other accredited investors who are looking to conduct due diligence into hedge funds. Be open to securing capital from a variety of sources and careful that you don't shut the door on additional capital down the road.

#### FUND ADMINISTRATOR IS A KEY PARTNER

When picking a fund administrator, you want to make sure you have access to a team that is experienced. Avoid being placed with a junior analyst, because the firm is so large your fund gets lost in the shuffle. Your fund administrator often guides you on your selection of a banker and can

make sure your fund structure can accommodate both onshore and offshore investors.

The administrators are often in contact with FOFs or with larger funds looking to sub-advise, so ask them for marketing guidance and suggestions. In many cases, they may even know of several third-party marketers that can assist you in marketing your fund.

#### AUDITED TRACK RECORD

Fund managers should secure an audited track record early on if they want to be taken seriously by potential funds and accredited investors. Do not wait more than a year to get this done. There are several respected auditing firms and your fund administrators will be able to steer you on the right path. You do not want to have to ask a potential investor to wait while you get your track record audited as their capital may find a new home in the meantime.

Don't be afraid to ask for referrals. The vendors that helped get you up and running in the first place may also be well-positioned to help you generate alpha and investor capital. Your prime broker can be your secret weapon in ensuring your fund's long-term success. ■

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