February 2024

The Alternative Investor

Performance
News
Trends
Regulatory updates

How Impact & Crypto investing is being driven by positive change.

In this edition, **Lendable's Chris Wehbé** writes about the drive to standardise impact terminology, which is creating a more homogeneous data environment, helping the growth of impact investing. **Aristata's Rob Ryan** looks at the emergence of impact litigation that has been a catalyst for social empowerment, fostering a more equitable legal landscape. **3iQ's Louis LaValle** changes tack from impact to look at how the digital asset environment is undergoing a transformation that is heralding a new era of investment possibilities as institutions, regulators, and active finance gets behind it. And in *Letter from America*, **Prosek's Mark Kollar** looks at the new-found attraction of infrastructure investing.

A Brodie Consulting publication in conjunction with Capricorn Fund Managers and RQC Group.

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Funds up but India is the standout performer

From a macro perspective, January was a mixed month, with the European economy spluttering along, skirting recession, and the US confounding with 3.3% growth in the final quarter. But inflation has not gone away and after the sharp falls, it appears to have found a new baseline. To read more click here. In this environment, the HFRI Composite index was +0.3%, with all sectors, bar Event Driven, in positive territory for the month.

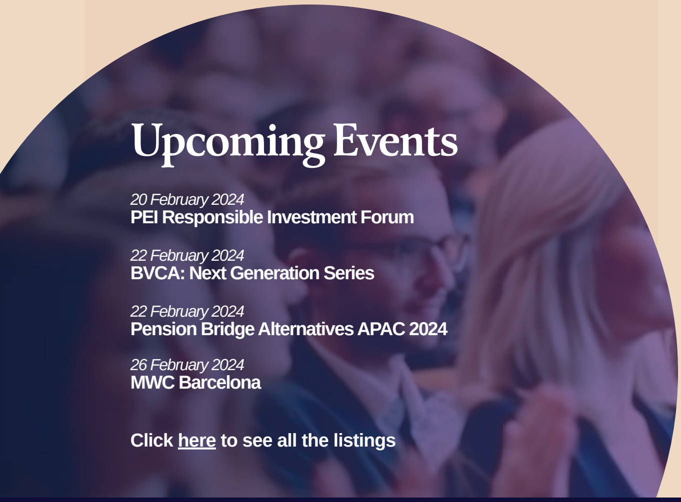
The HFRI Equity Hedge (Total) Index was up +0.2%. Within this, the best performing sub-sector, by far, was Technology, +3.2%, spurred on by big tech gains. Also performing well were Healthcare and Equity Market Neutral, both +2.0%. At the bottom, the laggard was the Energy/ Basic Materials Index, down -0.9%.

Event Driven was more nuanced, with the HFRI Event-Driven (Total) Index down -0.3%. Activists struggled this month, -2.2%, as positions sold-off. Also in the red were Merger Arb and Multi-Strategy, -1.0% and -0.6%, respectively. Conversely, Credit Arbitrage had a very good month, +2.4%.

Macro held its own in January, up +0.4%. The Commodity Index led the pack, +1.4%, as managers profited from increased volatility in the space as Middle East instability ratcheted up. Multi-Strategy followed, +1.3%, and then Systematic and Trend-Following Directional, up +0.6% and +0.5% apiece, mainly benefiting from US equity tailwinds. Trailling were Active Trading and Discretionary, down -1.7% and -0.7%.

The Relative Value (Total) Index was up +0.6%, with only one red sub-sector, Yield Alternatives, -0.9%. The best performing was Fixed Income Corporate Index, +1.1%, followed by Fixed Income Convertible Arbitrage, +1.1%.

Regionally, the standout performer continues to be the Indian market, +3.8%, which is now up +42% over the past 12 months. Elsewhere in the emerging markets, it was more challenging, with China again struggling, -3.0%, followed by LATAM -1.5%. In Western markets, Japan was the best performing, +2.0%, followed by Pan Europe, +1.0%.



Upcoming Events

20 February 2024
PEI Responsible Investment Forum

22 February 2024
BVCA: Next Generation Series

22 February 2024
Pension Bridge Alternatives APAC 2024

26 February 2024
MWC Barcelona

Click here to see all the listings

$723bn

Long/Short Equity fund assets (Dec 2023)

Source: Nasdaq eVestment

$689bn

Multi-Strategy fund assets (Dec 2023)

Source: Nasdaq eVestment

Cinven hits hard cap

Cinven has raised $14.5bn for its flagship fund, the Eighth Cinven Fund, which is 30% larger than the previous fund. This will invest in 'control positions in growth-oriented, market-leading, cash generative companies with resilient characteristics.' Impressive figures, although the firm extended the fund's close from July to January to ensure that it hit the hard cap. Today, the London-based firm manages €39 billion and has made more than 140 investments.

Brookfield's 2nd transition fund

Brookfield has announced the first close of $10 billion for its second Global Transition Fund and is on target to pull in more than the $15 billion it raised for the first fund. Co-headed by Mark Carney and Connor Teskey, this fund focuses on investments that will help accelerate the global transition to a net zero economy. Seed investments includes a UK onshore renewables developer and a solar development partnership in India. All investments are managed to science-based sector pathways for net zero and the total impact of BGTF I, measured in avoided emissions, is on track to exceed the combined annual emissions of New York City, London and Toronto.

Blackstone plans new credit fund

According to reports, Blackstone is prepping a new $10 billion fundraise for an opportunistic credit fund. This will be the fifth in the series and follows other successful fundraises in credit and recent funds by Blackstone. The firm's previous credit vehicle, Blackstone Capital Opportunities Fund IV, raised $8.75 billion at its close in January 2022.

Acrmont fundraise closes at €10bn

Acrmont Asset Management has announced the final close of its direct lending fund, Direct Lending Fund IV at €10 billion, having targeted €8-10 billion. Like Amont's previous direct lending funds, IV is investing in defensive, diversified portfolio of mainly first-lien senior and unitranche loans and second-lien and subordinated loans. The fund has already committed around 55% of its capital. Over the past ten years, the firm has raised approaching €30 billion to invest across direct lending, senior loan and capital solutions and has currently deployed over €26 billion across 350 transactions.

UPDATES (cont.)

Infrastructure is firmly in play

In a world where diversification is crucial, BlackRock fulfilled this brief by acquiring Global Infrastructure Partners (GIP) in early January. This adds to BlackRock's alternative capabilities and breaks new ground for them. GIPS is all about infrastructure investment and is the biggest in the world, across energy, transportation, water and waste. As a diversification play for BlackRock, this is a valuable one and adds to their already impressive offerings. With around $100 billion AUM it also gives them a hefty chunk of assets.

Infrastructure investment is most certainly on the financial services agenda now and mid-month we saw General Atlantic buying sustainable infrastructure investor Actis.

Beyond investment managers acquiring infrastructure businesses, private equity firms have also been busy raising infrastructure funds. One of which was Macquarie's European Infrastructure Fund 7 (MEIF7), which closed at over €8 billion, making this one of the biggest European infrastructure funds and takes their assets in the European infrastructure fund series to €30 billion. This came in at the top end of the fund's target, with commitments from over 100 pension funds, insurance companies, sovereign wealth funds, asset managers and fund of fund investors, of which around 92% were previous investors. MEIF7 has already committed capital to three investments and is targeting infrastructure companies that will benefit from decarbonisation, digitalisation, the circular economy and demographic shifts.

Likewise, KKR has raised $6.4 billion for its Asian infrastructure fund, taking its total strategy assets to $13 billion. KKR Asia Pacific Infrastructure Partners II has already invested or committed more than half its capital in 10 investments. David Luboff, Co-head of KKR Asia Pacific, commented that "infrastructure is a key pillar of KKR's global and regional strategy."

Dry powder mountains

The amount of dry powder US venture capital funds are sitting on is impressive, although it is just a rounding error compared to what private equity firms have to call on.

According to recent Pitchbook data, US VC's have $311 billion of undeployed capital, with the Financial Times writing that firms are under pressure to either deploy this investment or return capital to investors.

In comparison, S&P Global estimates private equity dry powder at the end of 2023 to stand at around $2.6 trillion. The trouble is that PE and VC funds are unwilling to exit their positions at current valuations and not so keen on testing the public markets.

To get around this potential problem, funds are becoming more creative, with the rise of continuation funds to provide ongoing liquidity without going down more traditional investment exit routes.

UPDATES (cont.)

Secondary markets are on a roll

Secondary market transactions totalled $112 billion in 2023, up from the previous year's $108 billion, although down on 2021's $132 billion. But what really marked last year was the uptick in activity in the second half as deal volumes increased by 60%, alongside record fundraising and new buy-side entrants.

This data comes from Jefferies' Global Secondary Market Review, which puts the increase down to 'LPs' desire to generate liquidity and/or derisk their portfolios.'

There is certainly a buzz in the secondary market space, with plenty of assets raised and dry powder ready to deploy.

Again, leaning on Jefferies data, 2023 saw approximately 60 funds close their fundraising last year, totalling around $84 billion, with around 20 funds coming in above $1 billion, which is more than 2021 and 2022 combined. According to Jefferies' estimates, total dedicated available capital now stands at $255 billion, significantly higher than the previous record of $236 billion in 2021. Already this year, we have seen Lexington Partners close their fundraising for Lexington Capital Partners X at nearly $23 billion, very comfortably above the $15 billion target and significantly larger than the previous fund's $14 billion. We are also seeing some sizeable fundraisings for more niche secondaries funds, such as Stafford Capital's timber fund hitting $635 million.

Jefferies believes we will see a 'further resurgence' this year in the secondary space from both LP portfolio and GP-led transactions, driven by LP's need for liquidity, the tightening of the bid-ask spread and a broader universe of buyers. Such activity will take the transaction volume beyond the $130 billion marker.

Fund reap big profits in 2023

So much of what we have been writing about in the past year has been about the big brands drawing in the biggest assets and, indeed, the 2023 numbers show why this is the case, with the biggest profits ever recorded by some of the largest players in the market.

Last year, at the front of this pack, was Sir Chris Hohn's TCI, with net gains of $12.9 billion, followed by Ken Griffin's Citadel, with $8.1 billion and then Ole Andreas' Viking Global Investors, with $6 billion.

These figures come from LCH Investments' annual hedge fund rankings, which look at the 20 most profitable hedge funds of all time. Citadel leads this with net gains of $74 billion since inception, followed by Millennium and D E Shaw, each with $56.1 billion.

Not every bigfund shone in 2023

While hedge fund performances were, on the whole, pretty good last year, with the HFRI Fund Weighted Composite Index +7.6% and some of the biggest brands having a stellar year (see previous article), there were two sides to this picture.

On one side, the rosy one, the tailwind from the S&P 500 clearly suited the more equity-focused funds (HFRI Equity Hedge (Total) Index +10.5%) and, in particular, the activist managers (HFRI ED: Activist Index +18.1%).

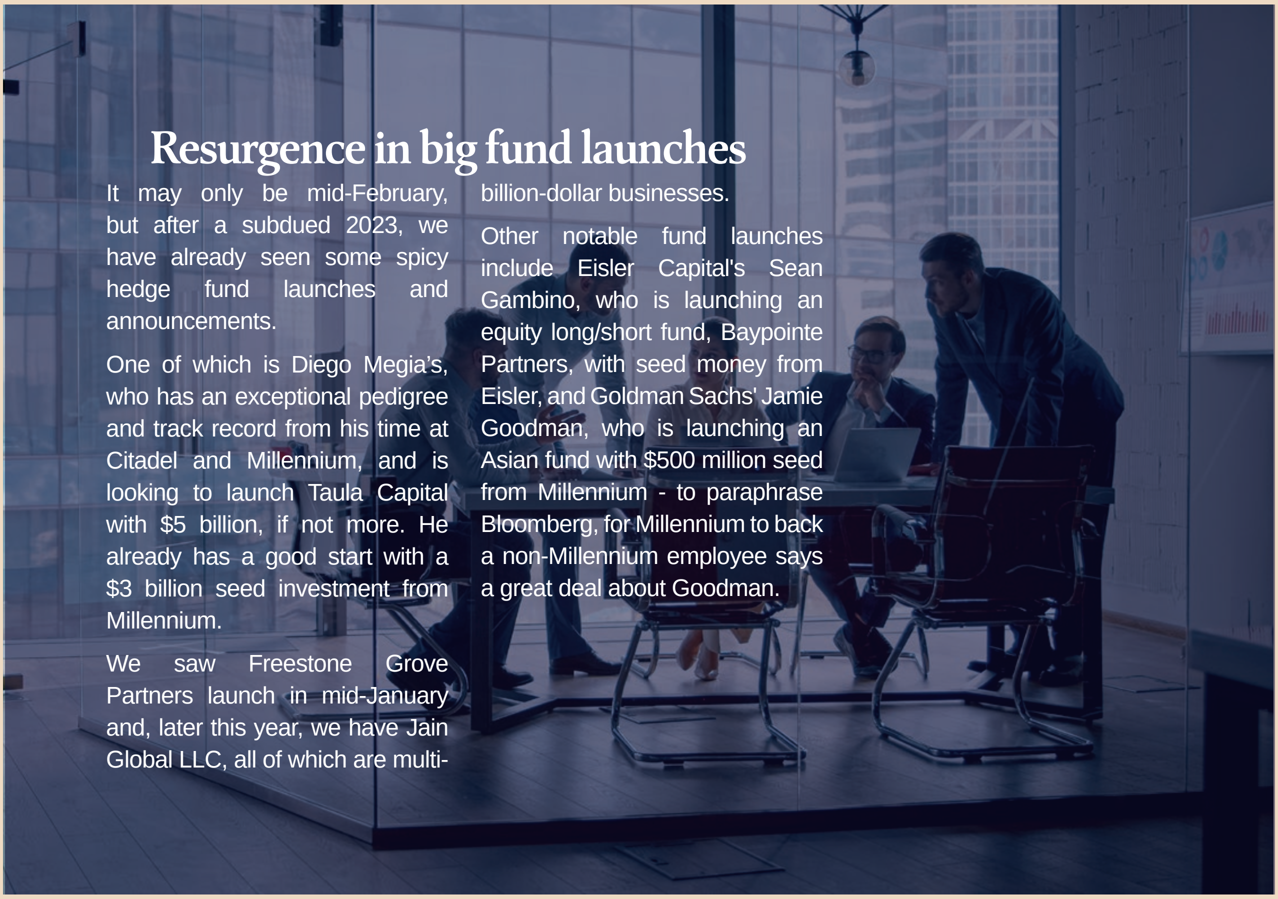
But on the other, what appears to have been missed by many commentators was the difficulties faced by some of the larger hedge funds.

Rather than looking at the Hedge Fund Research's Composite Index, where every fund carries equal weight and shows the sector up 2.6% in December, the Asset Weighted index - an index weighted according to individual fund AUM - only returned a paltry +0.5%.

This more mixed picture was also reflected in the year's returns, with the Composite +7.6% and Asset Weighted +3.6%.

Unfortunately, not every multistrategy pod made money, weighing on overall performance, and some of the most prominent Macro players, particularly in the systematic space, did not exactly cover themselves in glory, with the HFRI Macro (Total) Index (Asset Weighted) -2.1% for the year versus the Macro Index's -0.6%.

UPDATES (cont.)



Resurgence in big fund launches

It may only be mid-February, but after a subdued 2023, we have already seen some spicy hedge fund launches and announcements.

One of which is Diego Megia's, who has an exceptional pedigree and track record from his time at Citadel and Millennium, and is looking to launch Taula Capital with $5 billion, if not more. He already has a good start with a $3 billion seed investment from Millennium.

We saw Freestone Grove Partners launch in mid-January and, later this year, we have Jain Global LLC, all of which are multi-billion-dollar businesses.

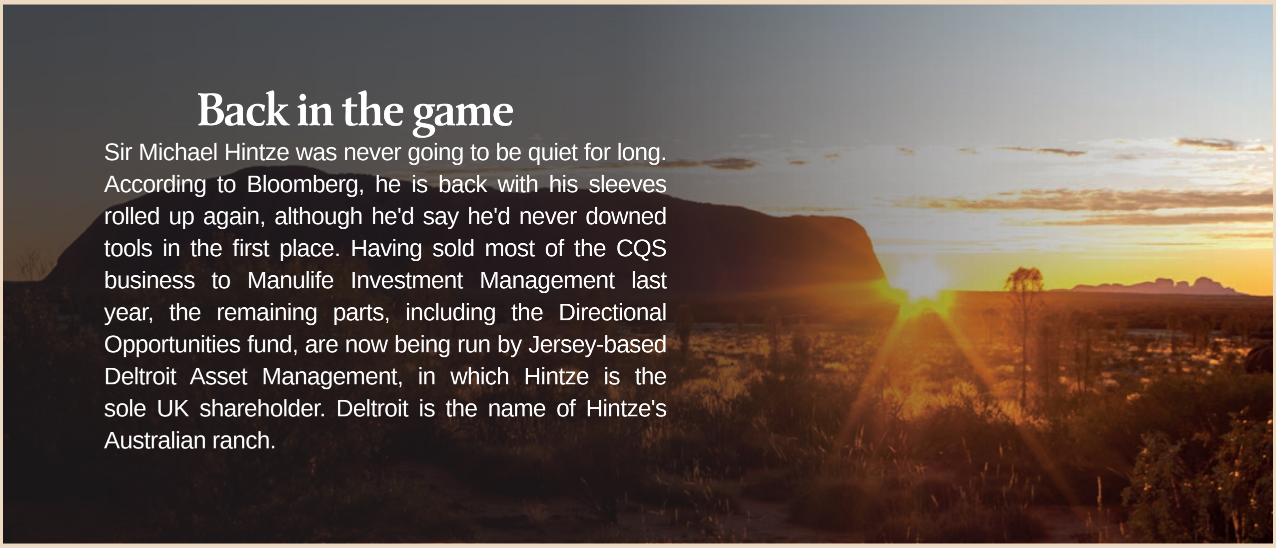
Other notable fund launches include Eisler Capital's Sean Gambino, who is launching an equity long/short fund, Baypointe Partners, with seed money from Eisler, and Goldman Sachs' Jamie Goodman, who is launching an Asian fund with $500 million seed from Millennium - to paraphrase Bloomberg, for Millennium to back a non-Millennium employee says a great deal about Goodman.

A case of setting sensible expectations

There have been plenty of conversations and coverage surrounding Bobby Jain's upcoming fund launch, with high-profile hires, big ambitions and an impressive Millennium track record.

Jain is certainly in the right space, with investors continuing to prefer multimanager funds to equity long/ short and macro. But achieving a $8-10 billion launch in this market was always going to be a big ask and we now read about expectations being revised downwards towards the $5-6 billion mark, which will still make this the biggest, or at least one of the biggest hedge fund launches of this year.

This is a lesson in not setting out your expectations so publicly. If Jain said he was looking to raise $5 billion, hoping quietly for more, and hit the $5-6 billion marker, he'd look a hero, but if he got close to $8-10 billion, he'd be a god.



Back in the game

Sir Michael Hintze was never going to be quiet for long. According to Bloomberg, he is back with his sleeves rolled up again, although he'd say he'd never downed tools in the first place. Having sold most of the CQS business to Manulife Investment Management last year, the remaining parts, including the Directional Opportunities fund, are now being run by Jersey-based Deltroit Asset Management, in which Hintze is the sole UK shareholder. Deltroit is the name of Hintze's Australian ranch.

UPDATES (cont.)

Bye Bye GLG

It is almost 30 years since the GLG name was established and 14 years since Man Group acquired the firm, becoming Man GLG, and now the GLG name is no more.

Bloomberg reports that Man is also retiring the Man Global Private Markets and Varagon names as it reorganises its discretionary trading arms into a single unit. Unfortunately, with the demise of the GLG brand goes its CEO Teun Johnston.

This is the first serious change that new CEO Robyn Grew has put in place, with Eric Burl, Head of Discretionary, put in charge of public markets, US direct lending and community housing.

Pac-Man

Like Pac-Man, the large multimanager funds are gobbling up hedge funds, as they add them to their offering. The latest to fall is Crescent Asset Management Asia, which is joining the biggest Pac-Man of them all, Millennium Management. Bloomberg reports that Crescent has been managing money for Millennium in a separate account for several years.

Bridgewater's big bucks

Back in the day, it would be an honour to intern for a leading financial firm and you would do this for very little remuneration. It is all very different nowadays, as funds fight for talent. This is particularly true in quant, where super-smart interns can quickly make a difference and often better understand the latest coding than many of the more senior employees. According to Financial News, Bridgewater is offering engineer interns $42,000 for eight weeks work.

Stuttering ESG fund flows

Morningstar's 2023 Global Sustainable Flows Report reveals a mixed picture. In the fourth quarter, Europe, which is the biggest market for sustainable funds, attracted $3.3 billion net new money, while the US saw $5.1 billion leave the space, which is more than the previous quarter's $2.7 billion. The global net result for the quarter was $2.5 billion of outflows.

This is the first time on record that net quarterly flows have been negative, which Morningstar puts down to interest rates and recessionary concerns, although these numbers also chime with broader redemptions in the global mutual fund and ETF universe, which saw an outflow of $17 billion for the same quarter. However, even with these redemptions, global sustainable fund assets increased to $3 trillion at the end of the fourth quarter, up from $2.7 trillion three months earlier. Europe also continues to be the biggest market for sustainable funds by some margin, accounting for 84% of sustainable fund assets, followed by the US with only 11%.

Parataxis hits 341%

While most crypto hedge funds that survived the fallout from Silicon Valley Bank, FTX and Signature Bank closed the year with very healthy returns, most didn't match Bitcoin's rise of 160%.

One fund, however, that did was the $50 million Parataxis Absolute Return Fund, which was up 341% from investments in Bitcoin and Solana. Speaking to Bloomberg, Edward China, the firm's CEO, said that he believes Bitcoin will hit $200,000 by early 2025.

The Builder of Businesses Now Buying the Builders

Private equity firms, often called the "Builder of Business" (think the likes of CD&R) and other asset-managers, are out on a buying spree right now actually acquiring the builders themselves.

In this year alone – and we're only in month two -- we have seen BlackRock, Inc. acquire Global Infrastructure Partners for $12.5 billion to create in its words "a world leading private-markets infrastructure investment platform." That was soon followed by General Atlantic in its acquisition of Actis, which will become the growth-equity firm's sustainable infrastructure arm.

And just last week, Brookfield Asset Management, an infrastructure investing behemoth itself, was reported to be raising more than $25 billion for two private funds focused on clean-energy investments.

At the time of his announcement, Larry Fink, BlackRock chair and CEO, said, "Infrastructure is one of the most exciting long-term investment opportunities, as a number of structural shifts re-shape the global economy." This surely seems to be the case.

On the one hand, it's good to see PE firms and asset managers in the business of buying hard assets or companies that actually make things. It's a little bit back to the future in some ways after a stretch of acquisitions in enterprise software, fintech and professional and managerial services.

But let's look at what is really happening and what is the case for infrastructure investments, a world that can mean anything from road, bridges and tunnels to airports and shipping ports, cell towers, data centers, hospitals and schools.

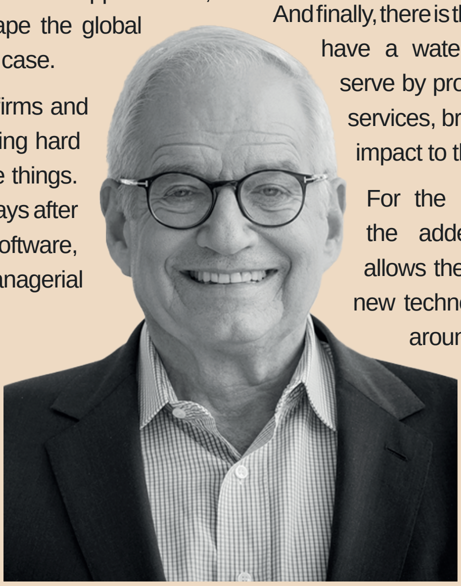
> "Infrastructure is expected to be one of the fastest-growing sectors, experts say, with a market size already estimated at $2.5 trillion and reaching $3.5 trillion by 2028. And the structural shifts driving demand are real...

First, the market is big. Infrastructure is expected to be one of the fastest-growing sectors, experts say, with a market size already estimated at $2.5 trillion and reaching $3.5 trillion by 2028. And the structural shifts driving demand are real: Let's call them the three "Ds," decarbonization, demographics and digitalization. The rapid pace of change, brought on in large part by climate change and the pandemic, highlight the need for a faster and bolder approach to energy transition, an upgraded transportation system, and improved and more secure communication hubs. By some estimates, on top of the contributions for President's Biden's Inflation Reduction Act, the US alone needs $5 trillion in investments to meet infrastructure needs.

Next, what resonates probably most for investors is that infrastructure projects tend to produce steady cash flows, a plus in times of market uncertainty, as well as consistent and stable inflation-hedged returns.

And finally, there is the benefit that infrastructure investments have a waterfall effect on the communities they serve by providing jobs at higher wages and better services, bringing a good business or sustainability impact to the projects.

For the infrastructure companies themselves, the added cash through acquisitions also allows them to access a larger capital base and new technologies and talent for growth. Wins all around. Call it business builders helping builders build businesses.



Mark Kollar
Partner, Prosek Partners

GUEST ARTICLES

The Drive for Consistency and Depth in Impact

Chris Wehbé, CEO, Lendable

As of December 2021, the Global Impact Investing Network estimated that worldwide AUM across Impact Investing managers exceeded USD 1.1 trillion[1]. This is roughly equivalent in size to the global private credit market[2] and therefore, by anyone's standards, an asset class to take seriously.

For the uninitiated, Impact Investing is the practice of investing with the intention to generate positive, measurable social and environmental impact alongside a financial return. The inclusion of these non-financial objectives is an important distinction from ESG strategies, which do not necessarily demand a broader set of outcomes, and therefore creates a need for rigorous impact measurement. This has certainly presented a challenge; unlike financial statements that have long converged to a narrow set of accounting standards, impact reports have been notable for their lack of comparable information.

Thankfully, we think this is now changing. Industry groups such as the UNPRI[3] are promoting a unified approach by proposing standardised terminology and helping shape clear expectations for managers. Whilst this process is still in its infancy, it feels like a tipping point has been reached and there is a clear path to recognised and agreed standards.

Certainly, this is exciting for impact professionals as it will create a more homogenous data environment in which comparative analysis and benchmarking can become productive. However, just as effective financial analysis requires looking "under the hood" and investigating the drivers and sensitivities of headline metrics, we think there is an important parallel need to assess "depth" of impact. In other words, what, why, how and to whom impact accrues. This is not trivial, requiring both analytical resources to understand nuance and ask the right questions, as well as access to end beneficiaries to observe and verify their experience.

[1] Link
[2] BCG report sees Private Credit AUM at USD 1bn in Sep 2020 link. To note private credit estimated at USD 1 trillion as of Sep 2020 vs USD 1.16bn for impact in Dec 2021.
[3] See article link

GUEST ARTICLES (cont.)

This need is creating an important role for groups that can provide more granular information that allows investors to improve the quality of their impact due diligence and operational value-add. For example, 60 Decibels has established sector-based, social performance measurement products based around surveys of a company's customer base. By sampling across the demographic and geographic spread of a firm, they can provide unique insights into customer experiences and impacts. At Lendable, we instead integrate with the accounting systems of portfolio companies to ingest their anonymised, granular data, which is then audited against bank account transactions. This allows for an on demand understanding of performance on a client-by-client, cohort or segment basis.

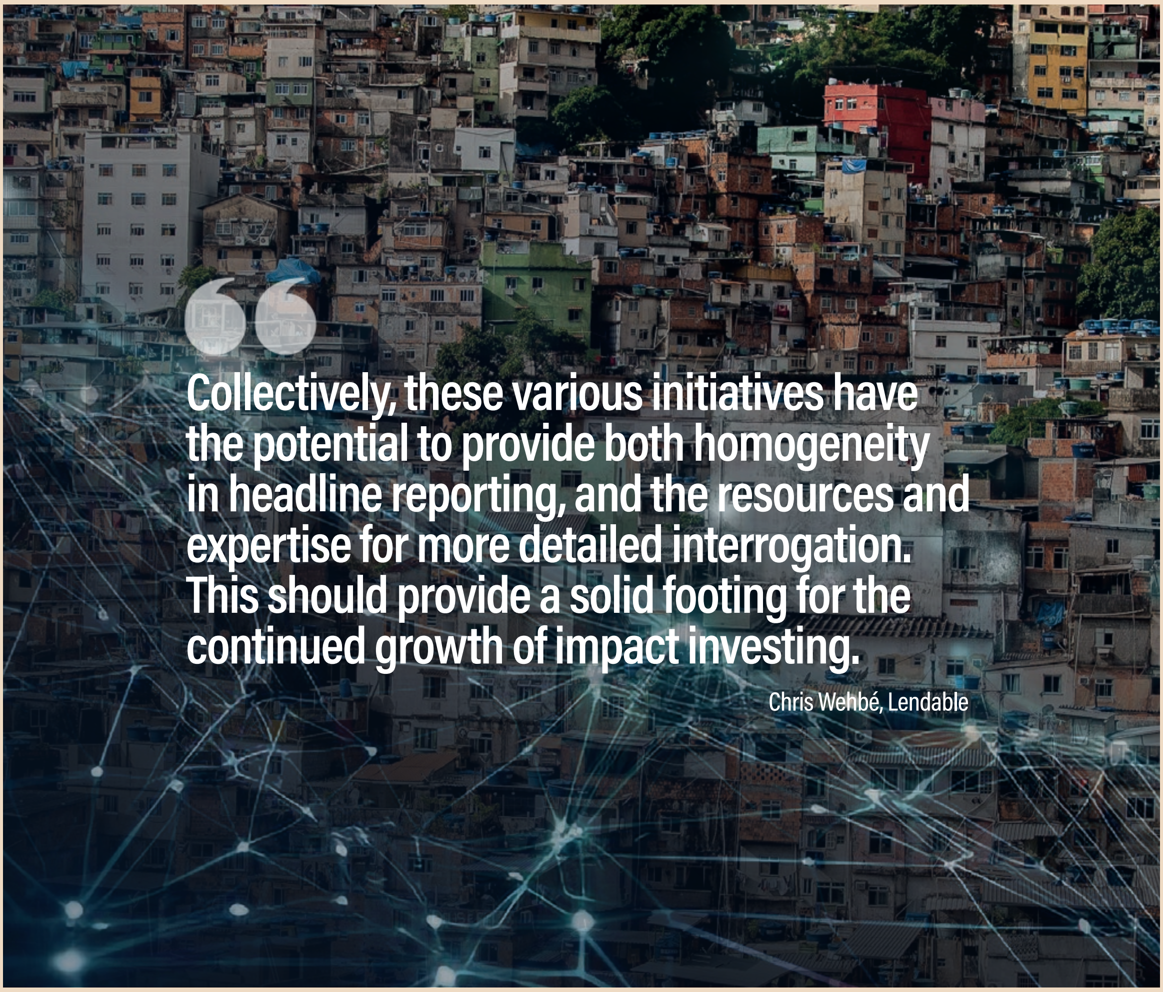
Collectively, these various initiatives have the potential to provide both homogeneity in headline reporting, and the resources and expertise for more detailed interrogation. This should provide a solid footing for the continued growth of impact investing. Given that the UN estimates a USD 4 trillion annual SDG investment gap, the necessity of greater capital deployment to solve social and environmental issues remains overwhelming.

Chris Wehbé, CEO, Lendable

Chris is the Chief Executive Officer of Lendable. Previously, he was a Partner of Arrowgrass Capital Partners where he served as Head of Relative Value globally for the multi-strategy firm, overseeing the Convertible Arbitrage, Volatility Arbitrage, and Capital Structure Arbitrage strategies.

Lendable is a technology enabled investment and alternatives platform that focuses on global impact alternatives. We believe in the power of technology and finance to create a more economically just and environmentally sustainable world.

https://lendable.io/



GUEST ARTICLES (cont.)

Why litigation finance can generate big gains and deliver big change

Rob Ryan, CEO and Head of Impact, Aristata

ESG and sustainable investment continue to attract significant capital inflows globally. Investors from retail to institutional are driving demand for asset classes and products that produce strong returns with clear social and environmental benefits – often easy to ask for, consistently hard to produce. One avenue gaining traction is social and environmental litigation finance—a niche yet growing sector that is drawing attention from conscientious investors. In this note, we explore the landscape of litigation finance, highlighting its potential to generate returns while effecting meaningful change.

In simple terms litigation finance, also known as third-party funding, involves providing capital to claimants or law firms to cover legal costs in exchange for a share of the proceeds if the case is successful. Legal claims, particularly complex commercial disputes or class actions, often require significant financial resources to pursue. With its often non-recourse nature – where repayment hinges on case success – litigation funding is particularly attractive as returns typically exhibit low correlation with broader market movements, offering investors a way to diversify their portfolios and reduce systemic risk.

The litigation funding market is maturing and attracting ever larger pools of capital - private equity, hedge funds, credit funds, pension funds, and institutional investors are among those committing substantial capital to litigation finance companies on the back of years of investment from family offices and private investors.

As traditional funding becomes mainstream, impact oriented firms are identifying claims that drive both returns and social and environmental impact. By providing capital to claimants pursuing justice in areas such as environmental degradation, human rights violations, and corporate misconduct, investors can align their financial objectives with their values. This alignment is crucial in an era where investors increasingly prioritize environmental, social, and governance (ESG) considerations in their investment decisions.

GUEST ARTICLES (cont.)

Investors seeking to integrate ESG considerations into their portfolios will seek to understand the measurable impacts of their capital allocations. Impact litigation finance offers a direct pathway for investors to deploy capital making a positive difference as well as achieving a return, where the outcome of a case can be reliably linked to impact outcomes. At Aristata, the first litigation fund to integrate clear impact assessment metrics in our investment process, we are motivated by the way our impact-first approach can amplify the voices of marginalized communities. Historically, disadvantaged groups have often been sidelined in legal battles due to resource constraints. However, with financial support, these communities can assert their rights, challenge systemic injustices, and hold powerful entities accountable. Impact litigation finance thus serves as a catalyst for social empowerment, fostering a more equitable legal landscape.

Environmental litigation in particular presents compelling investment opportunities in the era of climate change and sustainability. Cases related to pollution, resource depletion, and climate justice not only address pressing environmental issues but also carry the potential for substantial financial returns. As regulatory scrutiny and calls for corporate accountability intensify, investing in environmental litigation finance can offer a dual benefit of financial performance and positive impact. For investors doing well financially no longer needs to come at the expense of doing good.

Rob Ryan, Founder, CEO and Head of Impact

Rob is former Director of Development for ClientEarth, Europe's leading public interest law firm, with 15 years of experience developing social impact solutions for high net worth individuals, foundations, and family offices in the US and Europe. Previously Executive Director at CCS in New York, advising family offices and NGOs on impact strategy and fundraising. Robert holds an MBA from London Business School.

Aristata Capital was founded in 2018 and is the first litigation fund dedicated to driving positive social and environmental change with an attractive financial return. Aristata has two key objectives:

1. *Funding high quality litigation in order to achieve measurable social and environmental impact*
2. *Harnessing the power of private capital to drive systemic change at scale*

Aristata invests in a diversified portfolio of litigation cases across a range of impact sectors – including environment, climate change, human rights, justice reform, access to justice, foreign aid and equality - where law can be used as a potent tool for social and environmental change.

GUEST ARTICLES (cont.)

The Crypto Wind at Our Backs

Louis LaValle, Managing Director & Head of 3iQ Capital Management

The dynamic landscape of digital asset markets is undergoing a profound transformation. What began as a grassroots movement of individuals in search of an "orange pill," has evolved into a regulated industry experiencing rapid financialization and institutional adoption. As we look ahead to 2024, we anticipate a pivotal moment where institutional allocators recalibrate their focus towards digital assets, recognizing their value for portfolio diversification and return enhancement within a formal regulated asset management framework.

Driving this momentum is the recent surge in regulated trading volumes, propelled by the SEC's approval of spot ETFs in the US and the compelling advantages offered by Bitcoin and digital assets in a challenging macroeconomic environment. Institutions are no longer solely interested in accumulating digital assets; they are also harnessing blockchain infrastructure to develop tokenized products. Early initiatives like Franklin Templeton's tokenized money market fund showcase the potential for reduced costs, enhanced liquidity, and increased transparency in tokenized asset management. Global regulation has also been a driver of momentum. Jurisdictions such as the UK, Switzerland, Singapore, Hong Kong, and the UAE enhanced their regulatory frameworks over the last 12 months. These proactive measures provide much-needed clarity, boosting confidence and attracting institutional capital into the crypto market.

As the impact of FTX's collapse fades, the industry is better equipped to manage the next round of institutional investment. Banks, custody solution providers, and liquidity venues are integrating traditional financial functionalities into digital assets to meet regulatory standards. Establishing a dependable framework for digital asset custody is crucial for attracting institutional interest and mitigating risks, particularly concerning exchange failure and asset misappropriation. Enhanced infrastructure and risk mitigation strategies signify significant progress in handling crypto counterparty risks, paving the way for wider adoption of improved approaches like off-exchange settlement through tri-

GUEST ARTICLES (cont.)

party agreements. These advancements signal a significant shift towards a stable and growth-oriented digital asset ecosystem as regulatory clarity improves and institutional engagement with digital assets grows.

The most notable industry shift is being driven by the financialization of crypto markets, which has steered investment strategies towards active management, replacing the passive approaches predominant in the sector's early days. Over the past few years, significant shifts in digital asset rankings have made it challenging to maintain passive index strategies, mainly due to the rapid turnover in the top 100 assets (by market cap). The resulting highly fragmented, inefficient, volatile crypto markets that trade globally 24/7 offer a diverse array of innovative financial products (e.g., spot, derivatives, futures, perpetuals) and trading opportunities, attracting interest in active crypto strategies, particularly hedge funds.

As the crypto hedge fund landscape evolves, we find ourselves at the inception of a transformative era in digital asset management, mirroring the rise of hedge funds in the late '90s and early 2000s. Experienced investment professionals are migrating from traditional finance to capitalize on the significant alpha potential within crypto markets akin to the early successes of traditional hedge funds. The universe of strategies includes directional, long/short, quantitative, relative value and special situations with a broad range of styles from systematic to discretionary and everything in between.

The ongoing transformation of digital asset management heralds a new era of investment possibilities, driven by institutional adoption, regulatory advancements, and the migration of talent from traditional finance. As the sector matures, we anticipate continued growth and innovation, with digital assets solidifying their position as a fundamental component of modern investment portfolios.

Louis LaValle, Managing Director & Head of 3iQ Capital Management

Louis joined 3iQ in 2021 and is responsible for the development, execution, and investment management of 3iQ's institutional investment platform. He is head of the 3iQ Capital Management Operating Committee and serves as Senior Portfolio Manager for the 3iQ Managed Account Platform (QMAP). Louis brings over 20 years of experience advising global institutions on hedge fund, private equity, and digital asset investing. Prior to 3iQ, Louis held senior leadership positions at several alternative investment management firms including Neuberger Berman, EACM Advisors (BNY Mellon), Permal Group (Legg Mason) and SkyBridge Capital. He previously served as strategic advisor to Crescent Crypto Asset Management, a digital asset investment firm that created one of the industry's first suites of investable crypto index solutions. He began career in investment management working with family offices and institutional clients of Morgan Stanley and Credit Suisse. Louis holds a bachelor's degree with honors from New York University (NYU).

REGULATION — Presented by RQC GROUP

Unpacking Form ADV for Investment Advisers – how to avoid the pitfalls

Form ADV is the uniform form used by investment advisers to register with both the SEC and state securities authorities. It serves as a comprehensive disclosure document providing essential information about an investment adviser and its business practices, and is required to be filed annually, 90 days after the end of a firm's fiscal year, with additional intra-year filings also required to reflect material changes as they occur. Despite the significance of Form ADV, we see these filings frequently plagued by common deficiencies and in extreme cases even subject to enforcement action.

With ADV season upon us (for the majority of investment advisers, with a December 31 year-end), we will attempt to shed some light on some of these deficiencies, discussing their implications and offering some insight into how they might be addressed.

Incomplete or inaccurate disclosures

Form ADV provides key information about the investment adviser, including its business practices, fees, conflicts of interest and any discipline that it faced in the past. One of the most common deficiencies relates to the submission of incomplete or inaccurate information on the Form ADV, with investment advisers frequently failing to provide all the required details, or inadvertently (to give the benefit of the doubt) providing incorrect information. Form ADV is a publicly available document, and this deficiency undermines the transparency and accuracy that the Form ADV is intended to provide to investors.

Failure to update information timeously

Form ADV must be updated promptly to reflect any material changes in an investment adviser's business, such as changes in ownership, physical business location, key personnel or business practices. Failure to update information in a timely manner is a common deficiency, compromising the relevance of the disclosed information.

Inconsistencies across parts of Form ADV

Form ADV is divided into multiple parts, each serving a specific purpose. Inconsistencies between different parts of the form are another common deficiency. This can create confusion and make it challenging for regulators and investors to obtain a clear and accurate understanding of an investment adviser's operations.

Form ADV deficiencies have serious implications for both investment advisers and their clients. The SEC may view these deficiencies as the failure of an investment adviser to meet regulatory standards, and in extreme cases may even

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take enforcement action.

As a recent example, in September 2022 several investment advisers were charged with failure to promptly amend information in their respective Form ADVs concerning the audit of certain private funds.

Six firms were charged with failure to promptly file an amendment to their Form ADV after receiving audit reports for relevant advised funds. This represented a failure to comply with the instructions to Form ADV stating that an adviser that reports that audit reports are "not yet received" must promptly file an amendment to the Form ADV and update responses when the audit reports become available.

A seventh firm was charged with failure to update and amend its Form ADV where it continued to check "yes" where asked if certain of its private funds' financial statements were subject to annual audit, even though the relevant funds' financial statements were no longer subject to such audit.

"Registered private fund advisers' failures to fulfil their reporting obligations make it harder for the SEC to identify firms with possible on-going issues", said C. Dabney O'Riordan, Chief of the SEC Enforcement Division's Asset Management Unit at the time the charges were announced. "It is critical for investor protection that private fund advisers update their filings with the SEC as required."

These cases may serve as a sign that the SEC has ramped up its use of automated tools to screen Form ADVs for particular issues and flag those that merit examination or investigation.

To address and rectify Form ADV deficiencies, investment advisers should adopt a proactive approach. This involves regular monitoring and self-assessment, training of staff on compliance requirements, and the implementation of policies and procedures. Regular review (beyond just the annual amendment) of Form ADV filings will help ensure that information remains accurate and up to date.

When creating, updating, and maintaining the Form ADV, it's imperative to follow the instructions to ensure each section properly discloses all required information. Best practice would be to revisit the instructions each time an annual or other amendment is made, to ensure that it is being completed in accordance with the current regulatory requirements.

UK

'Flying' and 'Printing': FCA publishes Market Watch 76; expresses concerns

The FCA has expressed concerns about instances of possible 'flying' and 'printing', and firms' management failing to deal with this behaviour.

'Flying' involves a firm communicating to its clients, or other market participants, that it has bids or offers when they are not supported by, or sometimes not even derived from, an order or a trader's actual instruction.

'Printing' involves communicating that a trade has been executed at a specified price and/or size, when no such trade has taken place.

These activities create a false impression of a financial instrument's liquidity and/or price and may therefore constitute market manipulation.

The FCA has observed possible instances of these behaviours in markets such as fixed income, commodities and currencies in instruments such as bonds, swaps and options.

The FCA has also seen cases of management failing to deal appropriately with this behaviour including, among other things, failing to recognise the risks, failing to implement appropriate surveillance and failing to submit suspicious transaction and order reports.

PRA takes action against bank CEO for multiple breaches of the PRA's Conduct Rules

The Prudential Regulation Authority ("PRA") has fined Mr Iain Hunter, the former Chief Executive Officer ("CEO") of Wyelands Bank Plc ("Wyelands") £118,808 for breaching three PRA Conduct Rules between 7 March 2016 and 28 May 2020.

Mr Hunter failed to comply with Conduct Rule 2 (You must act with due care, skill and diligence) and to take reasonable steps to ensure that Wyelands had adequate systems and controls in relation to the large exposures regime and PRA record keeping requirements (Senior Manager Conduct Rules 1 *(You must take reasonable steps to ensure that the business of the firm for which you are responsible is controlled effectively)* and 2 *(You must take reasonable steps to ensure*

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that the business of the firm for which you are responsible complies with the relevant requirements and standards of the regulatory system)).

This announcement follows the PRA's decision in April 2023 to publicly censure Wyelands, which commenced wind-down in March 2020, for major regulatory failings.

The failures focus on the large exposures regime. This aims to act as a backstop to prevent an institution from incurring disproportionately large losses as a result of the failure of an individual client or group of connected clients due to the occurrence of unforeseen events.

The PRA found that Mr Hunter did ***not*** take reasonable steps to ensure that Wyelands:

- had adequate systems and controls to identify, assess and manage connected parties' risks in relation to large exposures;
- submitted large exposures returns which properly aggregated its exposures in respect of certain transactions with connected parties;
- had a formal and appropriate document retention policy in accordance with the record keeping obligations set out in the PRA Rulebook; and
- clearly apportioned responsibility for conducting analysis of Wyelands' connected parties before March 2019.

Consequently, Wyelands breached requirements under the large exposures regime and the PRA's record keeping rules. Mr Hunter also failed to comply with the Bank's internal policy intended to mitigate conflicts of interest arising from its membership of a family group alliance and failed to verify the accuracy of statements he made about Wyelands in two letters he wrote to the PRA.

Similar to banks, investment firms are subject to the Conduct Rules and Senior Manager Conduct Rules which are part of the Senior Managers and Certification Regime ('SMCR'). Whilst an investment firm might not be subject to the large exposures requirements, senior and other staff at an investment firm should be mindful of the continuing regulatory focus on managing risk and having effective systems and controls for contingency arrangements.

The continuing evolution of The Consumer Duty

The FCA on 5 January 2024 ran a webinar, with accompanying transcript, setting out the next steps for firms that are subject to the Consumer Duty (the "***Duty***").

To recap, the Duty took effect on 31 July 2023 and aims to set a higher standard of consumer protection in financial services.

Nisha Arora, Director of Cross Cutting Policy and Strategy, provided an overview of how firms were proceeding to embed the Duty, what the FCA was hoping to see and what firms might expect to see from the FCA. Per her speech on 1 November 2023, the Duty is an ongoing commitment, not "once and done". Though drawing on examples of good and poor practice, she noted there were no new expectations or requirements – essentials already appear in the FCA's Handbook, rules and guidance, or the Finalised Guidance.

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Focus Areas

There are two specific focus areas, both due for completion by **31 July 2024**:

1. **Closed products**

Whilst the requirements for open products took effect on 31 July 2023, a 12-month delay was enacted for closed products. A closed product is one where there are existing contracts with retail customers entered into before 31 July 2023 but which is not marketed or distributed to retail customers (including by way of renewal) on or after 31 July 2023.

The priority is to identify any areas of harm – perhaps considering ***why*** the product was closed, which may have a bearing on consumer outcomes. Was this, perhaps, because it did not offer fair value – or generated complaints, often indicative of harm, or poor outcomes?

Closed products must be reviewed against the higher standards set by the Duty. Since no longer on sale, there is no need to identify a target market or distribution strategy, but they still need to deliver the right outcomes and meet all other requirements – including the cross-cutting rules.

2. **Annual Board reports**

Once a year, a firm's Board or governing body must review and approve an assessment of the extent to which it is delivering good outcomes for customers. 31 July is the anniversary of the Consumer Duty coming into force, and therefore the deadline for firms' first board reports assessing how effectively good outcomes are being delivered (with respect to products aside from closed products).

Boards have a critical role in setting strategy and ensuring that the firm delivers the Duty and the right consumer outcomes. For this, they need effective data collection and management information. They must work with executives to challenge and drive them in the right direction, to deliver and embed the Duty. Reports should be data-led, with ongoing monitoring providing essential content – to evidence outcomes delivered, and address any gaps.

The FCA will review a sample of Board reports, looking at data evidencing outcomes, how effectively the Board has assessed performance, and action taken to address gaps - and will then feed back on its findings.

Click here for a comprehensive overview of January's regulatory developments in RQC Group's January Monthly Regulatory Newsletter.

Click here to subscribe to The Alternative Investor; or if you have a question about the publication or a suggestion for a guest article email the team at hello@alternativeinvestorportal.com.

Brodie Consulting Group is an international marketing and communications consultancy, focused largely on the financial services sector. Launched in 2019 by Alastair Crabbe, the former head of marketing and communications at Permal, the Brodie team has extensive experience advising funds on all aspects of their brand, marketing and communications.

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