

Managing director and head of sales Christophe Chouard outlines the strategy and investment processes that are driving performance at fund of hedge funds manager HDF Finance.

HW: What is the background to HDF?

CC: HDF was founded in 1986 by Gilles du Fretay, current president and co-chief investment officer of the firm, which manages only funds of funds. Total assets under management were USD4.3bn in April.

The principals on HDF's management board are Christophe Jaubert, managing director and co-chief investment officer, Christian Bartholin, managing director and secretary general, myself as managing director and head of sales, and chief operating officer Erwan Duquoc.

HW: Who are your key service providers?

CC: Our custodians are RBC Dexia Investor Services Bank for French funds, and HSBC/Bank of Bermuda for offshore funds. Our administrators and calculation agents are HSBC Securities Services for French funds and Bisys (Bermuda) for offshore funds. Our auditors are PricewaterhouseCoopers.

HW: Have there been any recent launches or additions to the management team?

CC: In July 2006, we launched HDF Japanvest, a Japanese equity long-short fund of hedge funds, and in March this year we launched HDF Eurovest Unit Trust, the dividend-bearing yen-denominated version of our European Equity Long-short fund of hedge funds, HDF Eurovest. Last August we hired our single hedge fund operational risk control officer, and in November we hired our chief operating officer, who is a member of the HDF management board.

HW: What is your investment process?

CC: Our management process is structured through four key steps. First is sound analysis of the macro economic situation: Gilles du Fretay holds a PhD in economics and is a 15-year sparing partner with Christian de Boissieu, the president of the French prime minister's Economic Council.

Second is asset allocation, namely choices of asset classes, regions, strategies and styles. Fund selection involves an 80 per cent qualitative and 20 per cent quantitative choice of the best experts in each strategy that has been selected in the asset allocation process. Finally comes portfolio construction and risk control.

HW: How have your funds of hedge funds performed?

CC: HDF enjoys a 20-year track record. Our net-of-fees figures for flagship HDF funds of hedge funds over the past seven years, as of the end of the first quarter of 2007, are as follows:

		7Y Return	Volatility
Multi Strategy	HDF Xiphias Investissement	8.87% p.a.	4.7%
Multi Strategy Low Vol	HDF Arbitrage	4.92% p.a.	1.8%
Fixed Income Long-Short	HDF Optimix	6.22% p.a.	2.1%
Equity Long-Short	HDF Xiphias International	7.56% p.a.	5.0%
European Equity Long-Short	HDF Eurovest	9.04% p.a.	5.2%
Equity Long-Only	HDF Global Equity	5.30% p.a.	9.8%
Equity Index	MSCI World	-2.35% p.a.	16.0%

HW: How many funds and strategies are in your portfolio?

CC: Our multistrategy funds of hedge funds have about 11 strategies and some 45 funds. Fixed-income long-short funds of funds have some seven strategies and about 30 funds, while equity long-short funds of funds have four strategies and about 40 funds

HW: Are you linked to any hedge fund indices, or do you have plans to do so?

CC: No, we do not have any link with any indices and do not plan to have any.

HW: What makes a manager or strategy special enough for you to select him?

CC: A strategy must be hedgeable, with sufficient market liquidity, and with independent asset valuation. A manager must be the specialist and the best expert of the strategy he manages. Also, we must be comfortable with the manager's integrity, management process and risk control.

HW: What are your criteria for removing managers from the funds?

CC: We can remove a manager either because our top-down analysis indicates that its strategy should not perform, or because the manager no longer matches our investment criteria.

HW: How many managers do you have on the substitutes bench?

CC: On average, we have, at all times around five new funds immediately available for investment, plus about 20 funds which are considered for investment, but for which additional information is still required

HW: What events do you expect to see in your sector in the year ahead?

CC: With the still growing credit derivatives market and the wider number of trading opportunities, we expect to see both a broader series of credit long-short strategies and opportunities for more return.

HW: How will these changes impact on your own portfolios?

CC: We are currently increasing the allocation of our multi-strategy and fixed-income funds of hedge funds to credit long-short strategies.

HW: What differentiates you from other managers in your sector?

CC: We value macro economic analysis and asset allocation in our investment process. We bring diversification in single hedge fund selection relative to other funds of funds; being based in Paris, we are not influenced by any hedge fund gossip that's usually found in New York, London or Geneva.

We value extreme risk control. As an illustration, we are prudent with distressed strategies, with long-only strategies such as asset-backed lending and private investment in public entities, and with unknown extreme risk strategies such as weather derivatives

HW: Some funds of funds have complained that managers are not taking enough risks in the current environment - what are your views on this, and on risk in general?

CC: As a fund of funds ourselves, we do not put any particular pressure on our fund managers so that they take more risks. We just want to make sure that the return that they generate is in line with the risks they take.

HW: Are investors' expectations moving upwards, and how do you deal with this?

CC: We rather see investors putting more emphasis on the way risks are managed and controlled. Those investors wanting more return understand that a well-managed single strategy fund of hedge funds can deliver better results than a multi-strategy fund of funds that takes too much risk.

HW: How do you distribute your products?

CC: We use a mix of institutional sales people on our headcount, and third-party distribution to high net worth investors through private banks

HW: Are you planning any further launches this year?

CC: Yes, we are planning to launch HDF Optimix 2x, a two times leveraged version of our Fixed Income Long-Short fund of hedge funds HDF Optimix.