

A HELPING HAND

AMBASUTHAN JANANAYAGAM OF POINT NINE OUTLINES THE CHALLENGES AND PITFALLS AWAITING START-UP MANAGERS, AND HOW TO NAVIGATE THESE WITH A LITTLE HELP



Ambasuthan Jananayagam

is a managing partner at Point Nine, a full service, middle and back office solutions company. Previously, Jananayagam spent thirteen years in investment banking. These included roles running trading and structuring desks at ABN Amro and Deutsche Bank. He started his career at JP Morgan in 1996.

When it comes to the costs of starting up a hedge fund, making mistakes early on can seriously stifle future growth. Ambasuthan Jananayagam from Point Nine Financial Technologies talks to *HFMWeek* about the hidden costs that managers should look out for from day one, and provides insight into how the strategic use of operational infrastructure can help grow a fund to the next level.

HFMWeek (HFM): What are the trends you are seeing in the small hedge fund space?

Ambasuthan Jananayagam (AJ): It is no secret that post-crisis regulatory barriers are going up. Both investor and regulatory demands for robust processes are increasing, and fulfilling these demands involves higher costs. Some vendors have withdrawn from the small fund manager space either because the infrastructure necessary to deal with these hurdles was too expensive, or margins were too small. Institutional investors are also increasingly attracted to the diversity that alternative investment strategies can offer. Encapsulating alternative strategies with robust processes will place further demands on small hedge funds' infrastructure. Fund managers need to be smart about how they deal with these demands and costs do not have to be exorbitant; doing your homework will pay off. The changing environment means only the most automated and efficient vendors are able to cater to small funds in a cost-effective manner.

HFM: What kind of operations infrastructure can start-up fund managers adopt in order to attract institutional investors?

AJ: Post-Lehman crisis everyone understands the importance of having a multi-prime platform, and with that comes additional operational needs. Funds will need to demonstrate: adequate risk management and reporting capabilities; T+0 trade reconciliation deliverables which capture any trade errors early; tried and tested disaster recovery procedures; and the ability to demonstrate their backup systems, locations and people. Start-up fund managers need to ensure that their vendors have a solid track

record, are using current technology (such as web-delivered services and cloud computing, and so on), and can produce the reports required by the fund manager and the fund's investors. Also highly prized is the ability to carry out independent valuations (including a shadow NAV), and ensuring that processes are automated and light on manual intervention. Finally, small fund managers should certainly seek vendors' high-quality service support during the critical 'launch' phase. Ideally, a fund manager would ensure an operations solutions vendor ticks at least a few of these boxes, if not all of them.

HFM: What advantages do 'best of breed' independent providers hold over larger 'one-stop-shop' operations?

AJ: One popular myth is that one-stop-shops are cheaper. 'Best-of-breed' packages compete on the headline costs but go further in addressing potential costs. Start-up clients need a really high quality of service both pre- and post-launch. Implementing an operations platform can create a myriad of operational process challenges which will need solutions. Some common examples are: integrating the different vendors a fund is using; creating the right reporting suites, particularly where the fund manager is trading a variety of asset classes; and finally eliminating as many manual processes as possible. Start-up fund managers frequently underestimate the number of changes to the original launch plan that may be required. Start-ups will find a nimble and flexible vendor invaluable during the launch phase. We consider the support our clients get from the managing partners during the launch phase as a key differentiating

“ THE CONCEPT THAT ONE SIZE FITS ALL JUST IS NOT TRUE. FUNDS HAVE SPECIFIC MANDATES, DEFINED ASSETS AND TARGET INVESTORS: YOU NEED FLEXIBLE VENDORS ”

factor between Point Nine and our peers. We stay in close touch throughout the launch process and should the client need to change tack, we endeavour to minimise (if not eliminate) the extra charges. The concept that one size fits all just is not true. Funds have specific mandates, defined assets and target investors: you need flexible vendors; going down the best-of-breed route means that you can package together the correct set of vendors who can deal with your needs.

HFM: What risks are involved in choosing a provider?

AJ: Both the benefits of getting it right, and the costs of getting it wrong, are substantial. Obviously you have the headline figure, the price you get from all your vendors, but it is important to look further and to pay attention to hidden costs. Contracts frequently feature hidden costs for new interfaces, extra reports, new assets, and essential upgrades and maintenance which might become necessary in the future. As a start-up manager you need to know what those are. As your fund grows, your needs will change and you do not want to be penalised for growth with a hefty bill. The cost of errors is also an important factor. If your systems are not sufficiently robust and an error goes unnoticed you are liable to lose the money of the market movement during that period. In the big blue-chip funds the costs of such errors run into the millions.

Then there are the intangibles such as management time spent resolving operational problems. Any time that a fund manager does not spend managing his fund or raising money is precious time lost. Ideally fund managers, like any good business, should focus upon their core competencies.

Finally, the worst potential cost of all is that by failing to get infrastructure and operational platform right, you risk failing to draw the big institutional investors you need in order to grow your fund to the next level.

HFM: How can start-up managers mitigate these risks?

AJ: Speculate to accumulate. The key is to pay money for a little good advice early; many fund managers try to become experts on operational systems and services in a very short time and often get mired in the process. There are many affordable and well-informed consultants and it is worth engaging them early. As with any service, the best way to find a reputable company is to ask around.

Plan ahead. Lay out a full plan of where you want to go. Given the fund's strategy, and assuming growth goes according to plan, what is the full spectrum of assets the fund would trade? Are there other services that will be necessary (for example, collateral management)? Try and choose vendors who have solutions for you now, and the capacity to serve you in the future. Upgrading vendors and infrastructure half way through could be a costly mistake.

Thirdly, stick to what you do best: don't outsource and forget, but certainly outsource with oversight. Our advice is to demand that your vendors give you regular reports and internet or instant access to what they (your vendors) are doing, but let them do the heavy lifting while you carry on playing to your strengths and managing the assets.

Finally, take a fresh look at the market. Many fund managers make the mistake of coming out of a business and wanting to use exactly the same technology they used before, whereas there might be other options better suited to a smaller and lighter fund than their previous, larger institution. Start-up managers should scope out the costs of all the solutions. If, for example, you are going to get a new IT system, make sure you know the total cost, including: hosting costs, staffing costs and the costs involved in contingencies (staff leaving, trading a new asset class or creating a new process). Managers should endeavour to have a 'cost tree', which will allow for better cost planning



in the different contingencies and allow the fund manager to be more prepared.

HFM: What qualities should start-up fund managers look for when outsourcing support?

AJ: Quality of service in terms of staff and the use of current technology are key. Point Nine is a full service, middle office shop and we really hold our clients' hand all the way through the process. The management team has over five decades of experience of trading and managing trading businesses. It is the management team who scope out the clients' needs and design the specific solution most suitable for our client. Post-launch we hand over to our operations team comprised of individuals who typically have over a decade of experience. The management team continues to work with clients in a relationship management capacity. We find that keeping up with our existing clients' demands is the best way of maintaining our firm's edge in this space. Our technology is current and completely proprietary (which means that we control our implementation deadlines). Our service is web-delivered, and deals with the full spectrum of asset classes (from vanilla equities to complex exotic derivatives). We are a nimble, solutions driven company. To date, no client has ever left Point Nine for another vendor and we strive to keep it that way. ■