
A horizontal banner with a background image of a classical architectural facade, showing stone columns and doorways. The text is overlaid in white.

Semi-Annual Hedge Fund Portfolio Review –Period Ending Jan 2014

Los Angeles • New York

Prepared for the Rhode Island State Investment Commission

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## Equity Hedge Fund Portfolio

## Description of Strategy

Managers investing primarily in equities making active security selection on long and short positions.

Sub-strategies:

- Equity long/short – investing in equities
- Event Driven – investing primarily in equities but also debt while anticipating a particular change or event to occur with a company (e.g. acquisition)

## Role in the Total Fund

The equity hedge fund portfolio's role is to increase the Sharpe ratio of the total fund's equity exposure by:

- Over the long term, producing equity returns by combining some equity exposure and significant alpha generation
- Over the short/medium term, reduce the volatility of the equity portfolio by hedging the exposure



## What is in the Portfolio

Total portfolio market value:

- \$635 million
- 8% of total fund

### Diversification

Two substrategies

- 55% Equity Long Short
- 45% Event Driven

Nine managers

- Largest 13%

### Risk

Beta (ACWI)

- 0.24

Gross Exposure

- 189%

Net Exposure

- 52%

Since Inception Standard Deviation


- 3.66%

### Equity Hedge Managers

Manager/Fund	Total Fund Weight	Strategy
Ascend Partners Fund	0.9%	Equity Long Short
Davidson Kempner Institutional Partners	0.9%	Event Driven
Elliott Associates	0.9%	Event Driven
Indus Asia Pacific Fund	0.6%	Equity Long Short
Mason Capital	0.9%	Event Driven
PFM Diversified Fund	0.9%	Equity Long Short
Samlyn Onshore Fund	1.0%	Equity Long Short
Third Point Partners	0.9%	Event Driven
Viking Global Equities	1.0%	Equity Long Short

### Recent Large Long Positions

Sony	Capital One
Eaton	Hess
Gilead	Pfizer
Time Warner	Sanofi
Google	Porsche



Absolute Return Hedge Fund Portfolio

### Description of Strategy

Managers generally investing in non-equity asset classes or investing with a low net exposure (i.e. low equity beta). Exposures include both long and short positions on interest rates, credit, currency, commodities, and to a limited degree equities.

#### Sub-strategies:

- Credit– investing in corporate credit instruments taking both long and short positions
- Relative Value– investing in fixed income, on a long and short basis, seeking price discrepancies of instruments with similar fixed income risk
- Macro – investing across asset classes, on a long and short basis, based on fundamental or quantitative judgments
- Multi-strategy- investing across hedge fund strategies

### Role in the Total Fund

The absolute return hedge fund portfolio’s role is to increase the Sharpe ratio of the total fund and to provide an expected return with low volatility by:

- Over the long term, produce a significant return premium over the risk free rate (e.g. T-bills)
- Over the short/medium term, maintain a low beta or exposure to equity markets
- Over the long term, produce a level of volatility comparable to fixed income

## What is in the portfolio

Total portfolio market value:

\$511 million

6% of total fund

### Diversification

Four sub-strategies

- 31% Discretionary Macro
- 6% Systematic Macro
- 21% Long Short Credit
- 32% Multi Strategy

Nine managers

- Largest 19%

### Risk

Beta (ACWI)

.09

Gross Exposure

664%

Net Exposure

24%

Standard Deviation

2.38%

### Absolute Return Managers

Manager/Fund	Total Fund Weight	Strategy
BlueCrest Capital LP	0.2%	Discretionary Macro
Brevan Howard LP	0.9%	Discretionary Macro
Brigade Leveraged Capital Structures Fund LP	0.7%	Long/Short Credit
Capula Global Relative Value Fund Ltd.	0.6%	Relative Value FI
Claren Road Credit Fund, Ltd.	0.6%	Long/Short Credit
DE Shaw Composite Fund LLC	0.8%	Multi Strategy
Graham Global Investment Fund I	0.6%	Discretionary Macro
OZ Domestic Partners II, L.P.	1.1%	Multi Strategy
Winton Futures Fund Limited	0.4%	Systematic Macro



## Overview

Performance review covers the entire period Rhode Island has been investing in hedge funds (Nov 1, 2011 to Jan 31, 2014)

All returns are net-of-fees and annualized, as are risk measures

Three hedge fund composites are evaluated:

– **Real Return Hedge Funds:**

- \$511 million invested in 9 hedge funds
- Target 7% of total assets, within the 11% overall real return allocation
- Benchmarks – T-bills; HFRI Fund-of-Funds Index

– **Global Equity Hedge Funds:**

- \$635 million invested in 9 hedge funds
- Target 8% of total assets, within the 51% overall global equity allocation
- Benchmarks – MSCI ACWI Index; HFRI Equity Hedged Index

– **Combined Hedge Funds:**

- Combines the Real Return and Global Equity Hedge Funds into one composite

### Hedge Fund Portfolio Return and Risk: Inception through Jan 31, 2014

	ERSRI Global Equity	ERSRI Real Return	Combined ERSRI Hedge	HFRI Fund of Funds Index	HFRI Equity Hedged Index	ACWI	T-bill	Barc Agg
Total Return	10.50%	5.75%	8.33%	4.94%	7.78%	13.34%	0.08%	2.06%
Total Risk	3.66%	2.33%	2.80%	3.40%	6.35%	11.73%	0.02%	2.03%

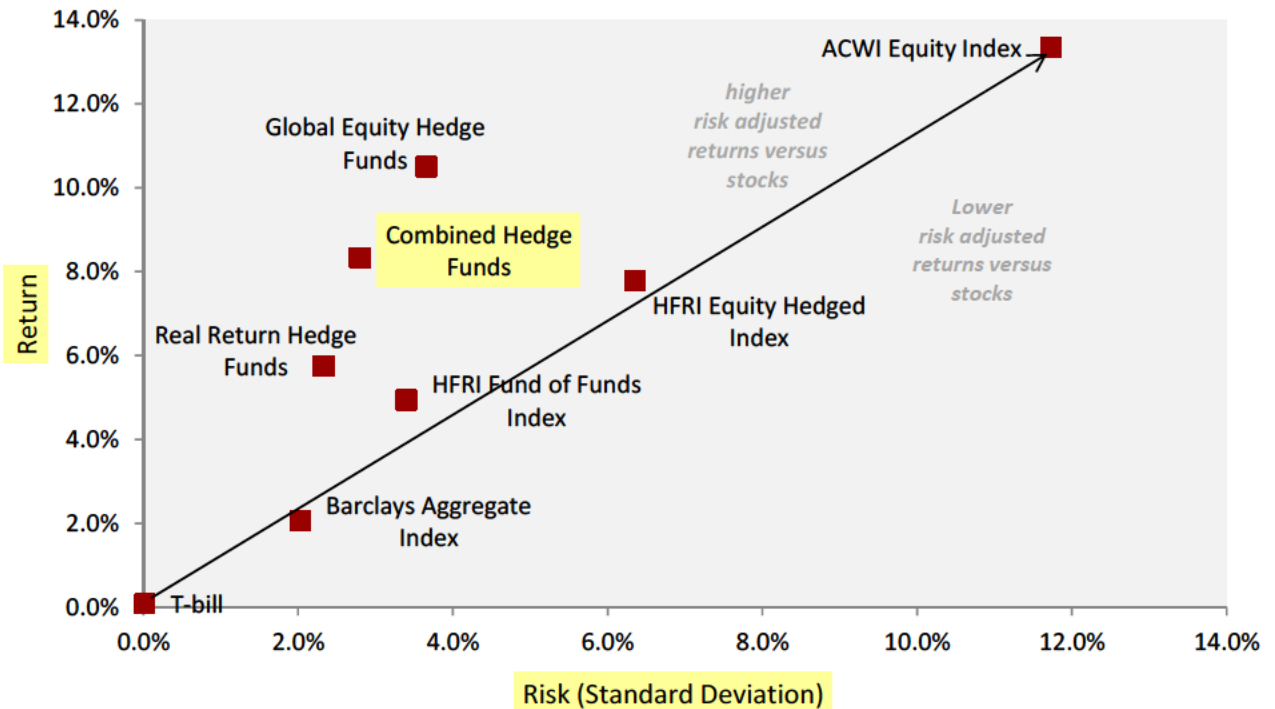


# Rhode Island Hedge Fund Total Return & Risk

Rhode Island hedge fund portfolios outperformed HFRI FOF Index over the 27 month period from inception (**8.83%** versus 2.80%, respectively) and had significantly better risk-adjusted returns

Both the RI Global Equity hedge funds (**10.50%** return) and the Real Return hedge funds (**5.75%** return) earned returns above their respective benchmarks (HFRI Equity Hedged Index and HFRI Fund of Funds Index, respectively) and at a lower level of risk.

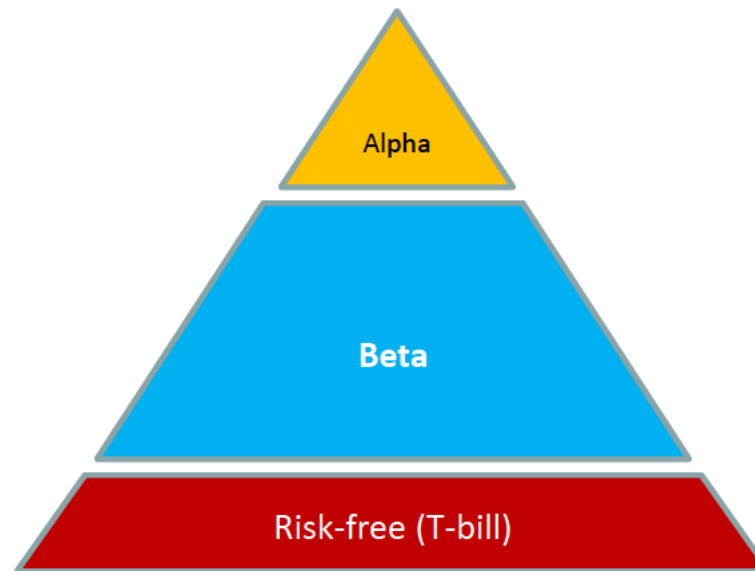
**Return and Risk (Standard Deviation)  
(Nov 1, 2011 to Jan 31, 2014)**



All assets have three return components:

- **Risk-free return:** all assets are priced to earn at least the risk free return (T-bill)
- **Beta return:** markets themselves generate investor returns to reward risk taking. These returns can be accessed at little to no fee through index funds and ETFs
- **Alpha return:** active managers try to produce excess return but often competition and fees get in their way

## Three Components of Return



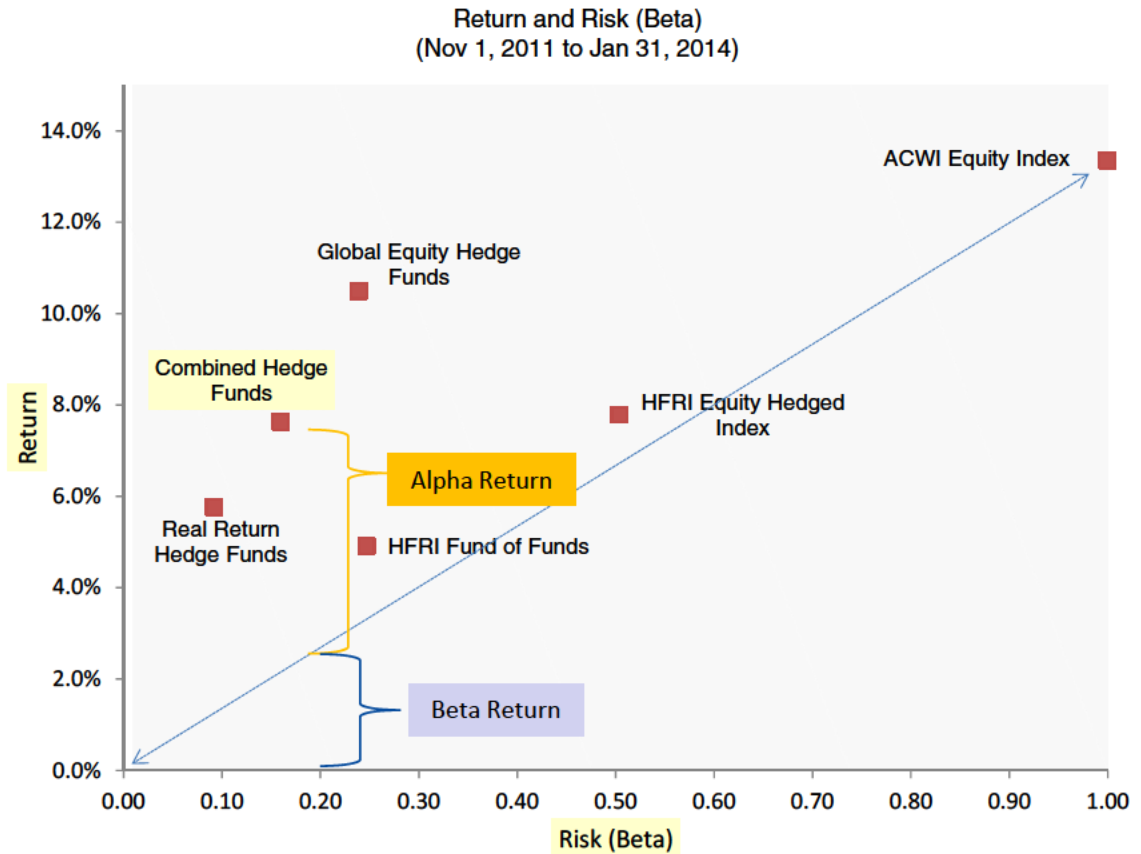


# Rhode Island Hedge Fund Return Attribution into Alpha, Beta, and Risk Free

Rhode Island hedge funds combined earned alpha equal to 5.41%, which exceeds Cliffwater's expected combined alpha of 3.75%

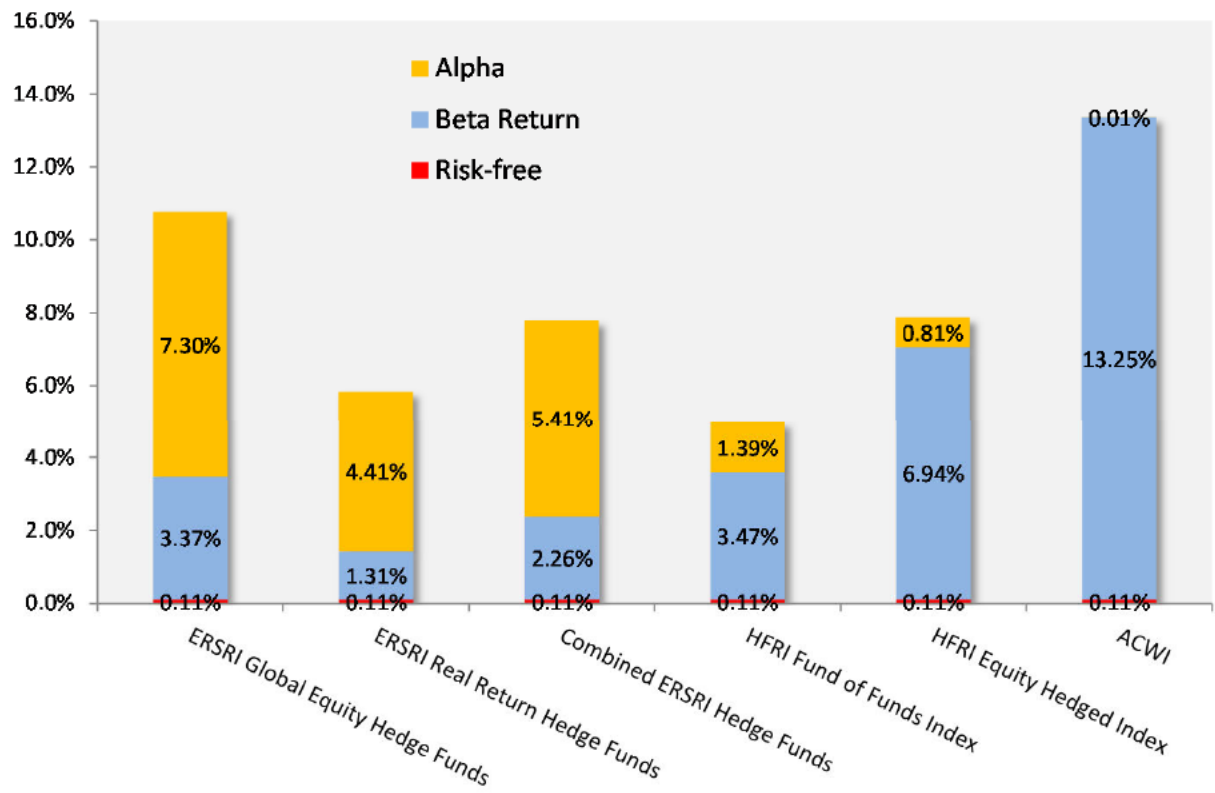
The equity beta for the Global Equity Hedge Fund portfolio equaled 0.24 over the period, well below the 0.50 average beta for equity hedge funds. The Real Return Hedge Fund Portfolio had a beta of 0.09 over this period.

Both the Global Equity and Real Return portfolios produced strong alpha of 7.30% and 4.41%, respectively.



# Hedge Fund Performance Attribution

Annualized Returns: Nov 2011 to Jan 2014



# Hedge Fund Performance Attribution

## Real Return Managers .....

## Global Equity Managers .....

	BlueCrest Capital LP - Class B	Brevan Howard LP - Series B	Composite Fund LLC (Ordinary Shares)	Global Investmen t Fund Ltd. -	OZ Domestic Partners II, L.P.	Futures Fund Limited - Class B	Leveraged Capital Structures Fund LP	Global Relative Value Fund Ltd. -	Claren Road Credit Fund	Ascend Partners Fund II LP	Kempner Institutional Partners, L.P.	Elliott Associates, L.P. - Class B	Indus Asia Pacific Fund, LP	Mason Capital Ltd. - Class F
Total Return	2.32%	2.61%	14.58%	3.24%	11.88%	2.00%	5.54%	4.06%	3.60%	5.94%	8.03%	11.70%	3.72%	6.59%
Total Risk	2.55%	5.05%	3.97%	2.85%	2.92%	7.87%	2.60%	2.19%	5.12%	2.53%	1.67%	3.37%	6.14%	6.62%
Return/Risk														
Correlation	0.14	0.34	0.09	0.37	0.74	0.33	0.60	-0.27	-0.26	0.43	0.68	0.57	0.65	0.34
Beta	0.03	0.15	0.03	0.09	0.18	0.22	0.14	-0.05	-0.05	0.09	0.10	0.16	0.34	0.19
Beta Return	0.52%	2.10%	0.45%	1.56%	2.61%	3.64%	1.61%	-0.85%	-0.64%	1.33%	1.37%	2.31%	5.74%	3.32%
Beta Risk	0.35%	1.73%	0.37%	1.05%	2.17%	2.59%	1.59%	0.59%	0.59%	1.09%	1.13%	1.91%	3.94%	2.25%
Alpha	1.70%	0.41%	14.11%	1.59%	9.45%	-1.83%	3.86%	4.75%	4.86%	4.58%	6.66%	9.54%	-2.27%	3.26%
Alpha Risk	2.53%	4.74%	3.95%	2.65%	1.96%	7.43%	2.06%	2.11%	5.09%	2.28%	1.23%	2.78%	4.70%	6.23%
Info Ratio*	0.67	0.09	3.57	0.60	4.81	(0.25)	1.87	2.25	0.95	2.00	5.41	3.43	(0.48)	0.52
Risk-free	0.12%	0.11%	0.11%	0.12%	0.11%	0.12%	0.13%	0.12%	0.12%	0.11%	0.11%	0.11%	0.12%	0.12%
#months	25	27	27	25	27	26	23	26	10	27	27	27	25	25

## Global Equity Managers .....

## Composites .....

	Diversified Offshore Fund A.I., Ltd. - Class	PFM Diversified Fund, L.P. - Class B	Samlyn Onshore Fund, L.P. - Series A	Point Partners Qualified L.P.	Global Equities, LP - Class H	Global Equity Hedge Funds	Real Return Hedge Funds	Combined ERSRI Hedge Funds	HFRI Fund of Funds Index	HFRI Equity Hedged Index
Total Return	13.38%	13.70%	13.63%	19.94%	16.72%	10.49%	5.76%	7.63%	4.91%	7.79%
Total Risk	8.36%	8.33%	5.19%	6.19%	4.18%	3.66%	2.33%	2.79%	3.40%	6.35%
Return/Risk								2.74		
Correlation	0.66	0.66	0.63	0.69	0.57	0.77	0.46	0.67	0.85	0.93
Beta	0.48	0.48	0.28	0.36	0.21	0.24	0.09	0.16	0.25	0.50
Beta Return	5.61%	5.62%	4.73%	6.17%	3.38%	3.37%	1.31%	2.26%	3.47%	6.94%
Beta Risk	5.64%	5.64%	3.23%	4.25%	2.41%	2.81%	1.08%	1.87%	2.90%	5.91%
Alpha	8.01%	8.34%	9.21%	14.47%	13.70%	7.30%	4.41%	5.41%	1.39%	0.81%
Alpha Risk	6.18%	6.13%	4.06%	4.50%	3.42%	2.35%	2.07%	2.07%	1.77%	2.31%
Info Ratio*	1.30	1.36	2.27	3.22	4.01	3.11	2.13	2.62	0.78	0.35
Risk-free	0.13%	0.13%	0.12%	0.12%	0.12%	0.11%	0.11%	0.11%	0.11%	0.11%
#months	23	23	25	25	26	27	27	27	27	27

## Appendix A: RI Hedge Fund Performance through Jan 31, 2014

Fund	Market Value	Actual %	Returns						
			Jan	QTD	YTD	FYTD	1 Year	Incep	Std Dev
<b>Global Equities</b>									
Ascend Partners Fund II LP	68,326,164	6.0%	0.08%	0.08%	0.08%	8.15%	10.11%	5.95%	2.53%
Davidson Kempner Institutional Partners, L.P.	71,390,296	6.2%	0.36%	0.36%	0.36%	4.21%	8.43%	8.03%	1.67%
Elliott Associates, L.P.	76,957,746	6.7%	1.80%	1.80%	1.80%	8.87%	13.48%	11.70%	3.37%
Indus Asia Pacific Fund, LP	43,151,711	3.8%	-3.40%	-3.40%	-3.40%	-0.84%	-2.16%	3.71%	6.14%
Mason Capital Ltd.	68,514,730	6.0%	-2.09%	-2.09%	-2.09%	5.76%	14.84%	6.58%	6.62%
PFM Diversified Fund, L.P.	38,366,618	3.3%	2.49%	2.49%	2.49%	18.59%	21.67%	13.69%	8.33%
PFM Diversified Offshore Fund A.I., Ltd.	38,161,562	3.3%	2.59%	2.59%	2.59%	18.55%	21.50%	13.38%	8.36%
Samlyn Onshore Fund, L.P.	78,300,375	6.8%	-0.16%	-0.16%	-0.16%	9.65%	14.62%	13.63%	5.19%
Third Point Partners Qualified L.P.	67,674,238	5.9%	-1.80%	-1.80%	-1.80%	9.16%	17.19%	19.94%	6.19%
Viking Global Equities, LP	83,860,499	7.3%	0.90%	0.90%	0.90%	15.49%	20.95%	16.71%	4.18%
<b>Total Global Equities</b>	<b>634,703,941</b>	<b>55.4%</b>	<b>-0.01%</b>	<b>-0.01%</b>	<b>-0.01%</b>	<b>9.22%</b>	<b>13.83%</b>	<b>10.50%</b>	<b>3.66%</b>
MSCI AC World Index Free - Net			-4.00%	-4.00%	-4.00%	11.16%	12.70%	13.34%	11.73%
Russell 3000 Index (DRI)			-3.16%	-3.16%	-3.16%	13.40%	22.62%	20.24%	9.87%
HFRI Equity Hedge (Total) Index			-0.73%	-0.73%	-0.73%	8.24%	9.84%	7.78%	6.35%
<b>Real Return</b>									
BlueCrest Capital LP	20,979,079	1.8%	0.71%	0.71%	0.71%	1.58%	-0.08%	2.32%	2.56%
Brevan Howard LP	79,469,607	6.9%	-1.38%	-1.38%	-1.38%	-2.43%	0.12%	2.61%	5.05%
Brigade Leveraged Capital Structures Fund LP	55,442,052	4.8%	-0.15%	-0.15%	-0.15%	4.11%	4.90%	5.54%	2.60%
Capula Global Relative Value Fund Ltd.	54,509,791	4.8%	1.10%	1.10%	1.10%	5.47%	8.29%	4.07%	2.19%
Claren Road Credit Fund, Ltd.	51,797,622	4.5%	2.39%	2.39%	2.39%	1.50%	-	3.60%	5.12%
DE Shaw Composite Fund LLC	67,922,486	5.9%	1.40%	1.40%	1.40%	5.17%	13.29%	14.59%	3.97%
Graham Global Investment Fund I SPC Ltd. - Discretionary Segregated P	53,438,644	4.7%	-0.68%	-0.68%	-0.68%	0.77%	1.35%	3.24%	2.85%
OZ Domestic Partners II, L.P.	96,556,092	8.4%	-0.31%	-0.31%	-0.31%	6.87%	11.74%	11.88%	2.93%
Winton Futures Fund Limited	31,310,635	2.7%	-2.37%	-2.37%	-2.37%	2.22%	4.20%	1.99%	7.87%
<b>Total Real Return</b>	<b>511,426,007</b>	<b>44.6%</b>	<b>0.05%</b>	<b>0.05%</b>	<b>0.05%</b>	<b>2.97%</b>	<b>5.89%</b>	<b>5.75%</b>	<b>2.33%</b>
ML 3-month T-Bills			0.01%	0.01%	0.01%	0.04%	0.08%	0.08%	0.02%
HFRI Fund of Funds Composite Index			-0.62%	-0.62%	-0.62%	4.50%	5.77%	4.94%	3.40%
<b>Total Hedge Fund Portfolio</b>	<b>1,146,129,948</b>	<b>100.0%</b>	<b>0.02%</b>	<b>0.02%</b>	<b>0.02%</b>	<b>6.35%</b>	<b>10.18%</b>	<b>8.33%</b>	<b>2.80%</b>
HFRI Fund of Funds Composite Index			-0.62%	-0.62%	-0.62%	4.50%	5.77%	4.94%	3.40%



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