

GOING GLOBAL

PATRICK BLESSING AND KRIPA KAPADIA OF SCOTIA CAPITAL TALK TO THE *HFMWEEK* CANADA REPORT ABOUT THEIR INTERNATIONAL EXPANSION, TAKING THE LESSONS THEY HAVE LEARNT IN THE CANADIAN MARKET AND BUILDING ON THEM ON A GLOBAL SCALE



Patrick Blessing

is a managing director and co-head of Scotia Capital's Global Prime Services Business. Patrick joined Scotia in 2004 and has been an integral part of the management team that has expanded the Prime Services business globally.



Kripa Kapadia

is responsible for sales and marketing in Canada for Scotia Capital Prime Services, and is also a senior member of the global capital introduction team, joining Scotia Capital prime brokerage in 2005.

With the hedge fund industry experiencing rapid growth and globalisation, more and more operators within Canada are expanding their presence internationally and spreading Canadian hedge funds' appeal to a world-wide market. Having to adapt to different markets, investors and regulations can be a challenging task but Patrick Blessing and Kripa Kapadia explain how a well-planned campaign of playing to existing strengths and taking into account new regulatory environments will allow them to navigate the business accordingly.

HFMWeek (HFM): How is Scotia Capital expanding its international presence?

Patrick Blessing (PB): Since the credit crisis in 2008/2009, we seized upon the opportunity that was presented to our prime services business to expand our presence globally. Prior to the crisis, we were able to lay the foundation through the opening of prime offices in Toronto, New York, London and Singapore. However, post crisis, the opportunity that was presented really enabled us to resource the business more effectively.

The first thing was the quality of the talent attracted to join a Canadian headquartered bank with global prime services capabilities. Along these lines, during the past year, we have hired a team in New York, starting with my partner John Stracquadiano. John led the team to be the first Canadian bank to offer full service US domestic prime brokerage services, which I feel is quite a compelling niche these days.

Following on from that, the opportunities to work with global hedge funds as a Canadian bank are very strong. I think a lot of our hedge funds clients found that just diversifying within the same banking jurisdiction does present itself with some systemic risk. What we talk about regularly with our hedge fund clients is the importance for jurisdictional diversification, which has become quite a powerful message.

We have also now expanded the team in Europe and Asia, for similar reasons as our US expansion, namely, the appetite to diversify to a Canadian headquartered bank with local market presence and expertise has never been stronger.

HFM: In such a busy international market, how does Scotia Capital stand out from the competition?

PB: Obviously prime brokerage is a very competitive business, and I think it is important to demonstrate a niche that clients will respond to. Our niche revolves around our strengths (AA- rated credit quality, strong balance sheet and local market expertise). Thus, when we talk to prospective customers, we stand out in how we tackle issues facing hedge funds today, like counterparty strength and asset protection.

Obviously in a post-Lehman world, hedge funds are very sensitive about the counterparty that is custodian of their assets, and I think that really plays to our strengths. We can offer funds the strength and stability of Scotia, combined with strong local product expertise. That is really the key message.

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HFM: Which domiciles do you see as being the most viable currently?

PB: Obviously with increasing regulation, investors are much more sensitive to where that fund is domiciled. Historically, in Europe for example, some of the most popular fund domiciles have been Ireland and Luxembourg. Those domiciles remain very important. I think an interesting domicile that has been showing

some growth in the offshore community has been Malta, which has developed some decent expertise and has been accepted by a number of the offshore investors. From a North American point of view, Cayman Islands remain the domicile of choice with increasing competition from various Caribbean domiciles aiming to get a larger slice of the offshore fund community.

HFM: How is domiciling a fund in Canada different to other domiciles? What certain considerations need to be taken, and has this had an effect on Scotia Capital's decision to expand its global presence?

PB: Domiciling a fund in Canada does have its differences compared to the rest of the world. First of all, Canada has a series of different provincial regulators rather than one national regulator in terms of the hedge fund industry. Anyone managing external client money for a hedge fund has to be registered with the local provincial regulator. Historically, there has been a strong regulatory culture

here in Canada. There are also a significant number of high quality local service providers. From administrators and lawyers to auditors and, of course, prime brokers. This strong local infrastructure has started to service a growing international client base.

Kripa Kapadia (KK): In terms of our global presence, we have been seeing tremendous interest from US and European managers setting up Canadian structures to tap into the Canadian investor base. Generally, with Canadian domiciled funds, investors tend to be high net worth/retail based. This typically requires expertise from local fund administrators to manage the intricacies. From our standpoint, our international capabilities only assist in our ability to service non-Canadian funds establishing a Canadian structure, as well as servicing our Canadian managers with their US domestic and offshore structures when marketing to investors in those regions.

HFM: What funds do you see currently as the most popular with investors?

KK: Certainly this year we have seen a lot of interest from the high-net-worth and family office community in looking at more liquid, equity-focused strategies: long/short, market neutral and, generally, lower directional equity strategies. Given the recent market volatility, global macro, CTA and other types of short-term trading funds are increasingly of interest as well. We have also seen significant interest locally for funds

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that produce a decent yield. Hence fixed income, and particularly credit related strategies, have been receiving significant interest.

PB: I think what we have seen overall is really that investors are getting back to the traditional, more liquid, hedge fund strategies. To add to Kripa's point, I think the idea is that during the crisis the investors got caught out in a number of situations where liquidity became a major issue.

KK: In terms of non-Canadian investors, we have seen an increasing appetite for Canadian-focused managers – i.e. hedge funds that have a bias towards investing in Canadian assets. I believe the ongoing strength of global commodity markets, in addition to the resilience of the Canadian banking sector, has increased appetite for Canadian exposure with investors who never considered Canada before.

PB: Canadian hedge funds have a lot of potential due to certain dynamics at work – one being the size of the hedge fund industry in single manager funds, which we estimate at approximately C\$25bn in assets. It sounds like a large number but it represents around 1.5% of the globe's hedge fund assets. That's also smaller than Canada's representation in global equity indices. However, this is also the opportunity. When you have fewer hedge fund assets chasing similar opportunities, there are more inefficiencies prevalent in the Canadian market relative to other developed markets. That really provides some of these managers opportunities to generate Alpha. We have seen more activity from international hedge funds investing in Canada, but I firmly believe that the investing market is still dominated by Canadian hedge funds.

HFM: What can you see the next 12 months holding for Scotia Capital? Are there any possible obstacles you think you will have to consider?

PB: We are going to continue our expansion of the US prime brokerage business and continue to enhance our global prime brokerage platform that will benefit our entire client base. It is a very exciting time for us as we have taken a step forward to resource the business globally. For hedge fund clients, jurisdictional diversification will remain a very compelling reason for hedge funds to select their financing counterparties. We deliver a strong product to accommodate that.

Obstacle-wise, I think we are in the same situation as any global bank in the fact that there is great uncertainty out there due to the shifting regulatory landscape and how we have to resource the business to accommodate that. A significant amount of time has been spent on assessing the legal and regulatory environment and the upcoming changes, particularly in Europe and the US, that are going to impact banks, prime brokers and the hedge fund industry. I think it is just a case of making sure that we are putting resources towards reviewing and assessing the impact of these changes and navigating the business accordingly. ■



RAISING CANADA'S PROFILE

THE SCOTIA CAPITAL CANADIAN HEDGE FUND PERFORMANCE INDEX HELPS BOTH MANAGERS AND INVESTORS COMPARE FUND PERFORMANCE AGAINST TRADITIONAL INDICES AND GLOBAL COUNTERPARTS

TM Trademark of The Bank of Nova Scotia. Scotia Capital is the marketing name used in association with the global corporate and investment banking and capital markets businesses of The Bank of Nova Scotia and its various subsidiaries in the countries where they operate. Past performance of indices is not a guarantee of future performance.

Launched in 2005, the Scotia Capital Canadian Hedge Fund Performance Index was designed to heighten the Canadian industry's profile and give both managers and investors a useful yardstick to measure the relative performance of individual funds against both traditional market indices, and their global fund counterparts. The Index has now grown from 24 funds to 58, and assets have more than tripled from \$2.6bn to nearly \$9bn.

"Five years ago, the Canadian landscape was dominated by traditional long/short equity managers," notes

Les Marton, managing director of Scotia Capital's hedge fund consulting group. "More recently, Canadian managers have been finding new and innovative ways to generate alpha for their domestic and global investors."

This has helped Canadian managers generate higher returns than traditional equity indices with a fraction of the volatility.

Based on most recent data to July 2011, the Index has generated an annual return of 11.32% since inception. This rate compares to less-than-stellar returns of only 5.24% for the TSX Composite, and 0.98% for the S&P 500 for the comparable period. ■

HISTORICAL MONTHLY PERFORMANCE



INDEX SUMMARY

*Month end July 2011	Value	Return MOM	Return YTD	Annualised return**	Annualised standard deviation***
SC CDN HF Performance Index Asset Weighted	2,026.03	3.39%	-0.82%	11.32%	11.83%
SC CDN HF Performance Index Equal Weighted	1,560.58	1.57%	-2.09%	6.99%	9.92%
S&P TSX Composite	12,945.63	-2.67%	-3.70%	5.24%	15.69%
S&P 500 (quoted in USD)	1,292.28	-2.15%	2.75%	0.98%	15.95%
S&P 500 (CAD-adjusted)	1,234.39	-2.98%	-1.65%	-2.43%	11.88%
DEX 91 Day Treasury Bill Index*	385.39	0.07%	0.59%	2.43%	0.47%
DEX Universe Bond Index**	820.58	2.04%	4.29%	5.63%	3.34%

*All returns quoted in CAD except where indicated

**Compound annual returns since index inception (31 December 2004)

***Of monthly returns

*Formerly: Scotia Capital 91 Day Treasury Bill Index

**Formerly: Scotia Capital Universe Bond Index