



Hedge Fund Management
B40.3379.30
New York University
Tentative Syllabus¹ and Schedule
(as of May 7, 2007)

PLEASE READ THE ENTIRE SYLLABUS. Important information is contained herein.

Overview

Sundays, 9 am to noon and 1 to 4 pm, [KMC X-XX]

Three ingredients are essential to success of hedge funds: trading strategies, capital, and infrastructure. While the first two seem obvious, the third is equally important. For example, one can develop a strategy that generates much profit when traded on paper, but unless the fund has a good relationship with a prime broker, if the strategy involves short sales to hedge long positions, the fund will not be able to execute the hedged positions.

This course will cover critical managerial aspects and characteristics of hedge funds and the hedge fund industry. It will look at the legal foundations and structures of hedge funds including the primary regulations in the U.S. and abroad that are most relevant for hedge funds. It will describe operations, control, and administration, due diligence, and valuation issues. Also, while explicitly not a course on hedge fund trading techniques, it will introduce a sampling of major hedge fund strategies from a general perspective so that students better understand the concept of absolute-return strategies. Moreover, we will discuss performance evaluation and investing in hedge funds from the investor's perspective, as well as issues of potential changes in regulation, risk management, and the use of leverage. The course will touch upon ethics in the industry. It is designed to be a multi-functional course that focuses on practical aspects of hedge fund management.

Those who attend the course should have a broad understanding of the essential knowledge necessary to successfully launching a hedge

¹ This syllabus has evolved from courses that I co-taught with Prof. Christopher C. Geczy of the Wharton School (Fall 2004) and Ms. Tanya S. Beder, formerly, CEO, Tribeca Global Management LLC (Spring 2006).

fund upon the course's completion provided they have a trading strategy and access to capital.

Students, whose reason for enrolling is an expectation that they will learn winning trading strategies, will be disappointed, and are discouraged from enrolling.

Other than the Final Project described below, the course will not be quantitatively rigorous.

Leon M. Metzger, an 18-year industry veteran, will lead the course.

Those who want to launch a hedge fund, join an existing one, invest in one, or provide services to one will register for this course. Students who are looking to learn the secrets of moneymaking, however, are advised to register for other investment management courses offered by the Business School.

In general, 50 percent of the grade will be based upon a "mock" hedge fund due diligence questionnaire that student groups must create and 50 percent will be based upon class participation.

Text

There is no single course textbook. Useful Reading Material (not required):

Alexander M. Ineichen (Author), Alexander Ineichen, *Absolute Returns: The Risk and Opportunities of Hedge Fund Investing*.

Jaeger, Robert, *All About Hedge Funds*.

Lederman, Jess, (Editor) and Robert A. Klein (Contributor), *Hedge Funds: Investment and Portfolio Strategies for the Institutional Investor*.

Strachman, *Getting Started in Hedge Funds*.

Schwager, *Market Wizards and The New Market Wizards*.

Other Material

Additional material like article links may be referenced in class or posted on the course intranet, as appropriate. They may include the following:

- Various articles on hedge funds
- SEC Staff Report “Implication of the Growth of Hedge Funds, 2003.
- IAFE white paper on valuation concepts
- FASB Statement 157—Fair Value Measurements
- AIMA’s Industry Guidance on Side Letters
- Securities and Exchange Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934
- AICPA’s Alternative Investments Audit Considerations: A Practice Aid for Auditors

Topics

Some of the topics that we might cover during our lectures include:

Administrator
Allocators to Funds
Alpha vs Beta
Alternative Investment Choices
Amaranth Case
Anti-Money Laundering
Benefits of Hedge Funds
Broad Metrics and Trends
Considerations
Definition of Hedge Fund
Due Diligence
ERISA
Expenses
FASB Statement 157—Fair Value Measurements
Fees
Funds of Funds
Future
Hedge Fund Study Act
Hedge Funds compared to Mutual Funds
History
IAFE Valuations Whitepaper
Infrastructure
Ingredients for Success
Institutional Investors
Investable Indices

Investment Vehicles
ISDA
Legal Structure
Locale
LP or LLC Agreement
Marketing
Master-Feeder Structure
Multi-Strategy Funds
Offering Memorandum
Performance Metrics
Prime Broker
Ratings
Registration
Regulatory Environment
Risk Management
Securities Laws
Selecting a Fund
Service Providers
Side Letters
Side Pockets
Soft Dollars
Strategies
Subscription Agreement
Transparency
US Tax Exempts
Valuations

Other Resources

The available resources on hedge funds have exploded in the last several years. The following internet resources may be of interest and use to you as the course proceeds:

www.mfainfo.org

www.hedgeworld.com

www.nfa.futures.org

www.sec.gov/answers/hedge.htm

www.hfalert.com

www.mahfa.org

<http://www.sec.gov/rules/interp/2006/34-54165.pdf>

Evaluation and Administrative Details

You will be evaluated in this class by your performance on a final group project and on class participation.

Final Project

Students will form groups of about five to seven people² in the second class of the semester, i.e., the afternoon session of May 13; those not in a group by the end of the third class, i.e., the morning session of May 20, will be assigned by me (note that I reserve the right to make *ad hoc* changes to any group, at any time, for any reason, at my sole discretion). Each member is considered a principal or employee of a hypothetical hedge fund. By the end of the third class, each group will be required to appoint a "Manager" or "CEO," who must inform me what his or her fund's trading strategy will be. Each fund will be responsible for developing a due diligence questionnaire. While I will endeavor to let the students select the strategies and various attendant characteristics of their funds, I reserve the right to overrule. Evaluation will be according to industry best practices as if the presentation were made for an actual startup hedge fund. The final project will account for 50 percent of your final course grade.

Students should not wait until the end of the semester to prepare for the final project.

No matter what the order of presentations, all written materials and any other supporting documentation for all groups will be due electronically at the same time, **Sunday, June 3, 8 am.**

I expect to receive special permission from the Alternative Investment Management Association (AIMA) to use its DDQ for the class, provided that the students respect the copyright.

In general, every member of the final project team will receive the same grade, no matter the level of participation for that project. Only under extreme circumstances will someone receive a different grade.

Class Participation

You will also be assessed based upon your class participation, especially the frequency of **quality** comments. A formal part of your class participation may take the form of a twenty-minute group presentation to the class about a strategy or topic that I assign to you

² There are 35 about students registered to take the course. Ideally, there should be 6 groups.

or for which you may volunteer ("strategy presentation"). The strategy presentations may account for as much as 25% of your final grade. If you make a strategy presentation, either please email to me your presentation materials by 8 am on the day of your presentation, or bring the presentation to class on a memory key. Bringing the presentation on your own laptop can cause an unnecessary delay in class. If you want me to preview your presentation, please email it to me no later than by 9:30 pm on the night before you present.

Strategy presentations can cover the following aspects:

- Describe strategy
- Players
- Size
- What drives returns
- Conditions for success
- Risks
- Historical performance
- Trends
- Outlook
- Cases or examples

The topics are:

- Distressed investing
- Convertible arbitrage
- Stat arb
- Prime brokerage
- Long/short
- Event driven
- Global macro
- Fund of funds
- Volatility arb
- Should hedge funds be regulated debate

In general, timely and regular class attendance is not mandatory. In general, class attendance will not be marked at the very beginning of each class and attendance will not be graded. Whether or not you attend class, however, you will be responsible for the material covered that day. Moreover, if you miss a class, you will have lost the opportunity to earn credit for class participation. Except for documented illness, religious observances, and serious family emergencies (e.g. bereavement) that are brought to my attention, by email, before the start of each class you will miss, absences will not be "excused" during this semester. The difference between an excused absence and one that is not is that in the case of the former, we may be able to work together to find a mutually convenient time to review

what was discussed during the class you missed. If you prefer, for whatever reason, that I not call upon you in a particular class, please inform me beforehand.

General

Note: Individual exceptions to the timing of the course requirements cannot be made to accommodate job interviews, travel schedules, etc., according to School policy. If you experience an emergency or illness that will interfere with any course requirement, including attendance at class, you must contact me with the appropriate explanation before the due date. Again, interviews and job-related absences are not emergencies or illnesses, as per the School's official policy (and common sense).

I will treat the classroom setting as a simulated hedge fund office. Accordingly, you will be "employees" of the NYU Hedge Fund and I will be your regulator. I expect you to treat your "colleagues" and me in the same professional manner that you would treat any co-worker at or regulator of a hedge fund. And, although it should go without saying, I need to make clear that I expect you to adhere closely to the School's code of academic conduct. In addition, I expect classroom conduct to take place on a high level. More important, I will not tolerate harassment of any type in our classroom.

Also, I realize that many of you are interested in landing jobs at hedge funds or their service providers. Notwithstanding the prominence of the hedge fund industry leaders that might attend, the class is not a placement office, and unless a guest requests resumes, it is inappropriate to solicit a visitor for a job.

Office Hours

My office and call-in hours are on Sunday, by appointment, in my office, KMC 9-150.

My remaining contact information is:

Email: lmetzger@stern.nyu.edu

By far, the best method of contacting me is by email.

Web Page

The web page for this course accessible via the course intranet is at Blackboard. This web site contains most class material that I

distribute as well as other items of interest that you may download using standard web browsers.

Email

Because of the importance attached to email and web pages, all students must have proper email accounts, and must check them regularly every day.

Teaching Administrator

There is no Teaching Administrator for this course.

Assignments

All assignments and other instructions will be given through e-mail. All students are therefore expected to check and respond over this medium regularly.

Class Notes

There is no requirement to prepare class notes that summarize the class discussion.

Stopwatch

For in-class group or individual presentations, I may use a stopwatch to monitor your allotted time. While some may feel that graduate students should not be subject to such a measuring device, as one who has appeared before Congress, the CFTC, and the IRS/Treasury to discuss hedge funds and was subjected to an electronic timer, I believe that this device simulates what you may expect to encounter should you have any responsibility for government relations later in life.

Suggested Grading Standards for the Department of Finance

The Department of Finance has a policy on suggested grading standards.

The Department's reputation depends in part on the ability of prospective employers to ascertain quickly that a student really understands financial policy and theory, and has the technical capability to use the tools learned in finance. It is part of my

responsibility as a faculty member at New York University to evaluate a student's understanding of the materials in my course with examinations or written assignments that are sufficiently demanding to reveal differential performance. I have chosen to use the final project and class participation as the tools with which to evaluate you.

These are the suggested standards for Department of Finance courses. The Department is particularly concerned that I do not give too many A and A- grades (those should be earned competitive grades that reflect superior performance in the current class and among students from the past five years). According to the Department, a grade of C is appropriate for students who are clearly below standards, and grades of D or F apply for students still further and further below the Department's expectations of performance in a top program.

Suggested Percent Grade Distributions	
A	10
A-	10 to 15
B+	10
B and B-	50 to 60
C+, C, C-, D and F	10
IP and IF	<i>No more than 5</i>

The Department is not concerned about (plus or minus) 5% variations in any distribution below the A or A - grade levels, and says that I may be still more selective on A and A- grades.

Special Note

This syllabus should be viewed as describing how I intend to run the course in the current semester. You should be aware, however, that anything herein or elsewhere might change without notice, reason or explanation. This includes but is not limited to evaluation methods, texts, materials and scheduling. If you are not comfortable with this uncertainty, then please do not take the course.

Course Session Schedule

#1, May 13, 2007 morning session

Lecture Topics: Introduction to course; who will benefit from course; what is a hedge fund; introduction to hedge funds; overview; definition, etc.

Video: Who Never Heard of the Term, "Hedge Fund," Before He or She Entered School?

#2, May 13, 2007 afternoon session

Lecture Topics: Traditional and alternative investments; definition of asset class; comparison to mutual funds; broad metrics and trends; risks facing hedge fund investors today; trends in trader compensation; taxation of hedge funds vs mutual funds; 130/30 funds; size of industry; growth of industry; etc.
size of alternative investment industry; comparison to equity, fixed income; credit and mutual funds; recent performance; hedge funds and politics; role of private equity and its convergence with hedge funds; risk to financial markets; secondary market makers in hedge funds; surveys of investor satisfaction; ownership trends; talent attraction; etc.

Lecture Topic: Hedge Fund Strategies

#3 May 20, 2007 morning session

Lecture Topic: Risk Management

Discussion Topic: Amaranth Advisors—Part I
Should Amaranth shut down?
Should Amaranth allow redemptions not according to schedule?
What should Amaranth do about employee retention?
Where should Amaranth cut costs?
What grade would you give to its media policy?
What do you think of the September 20 letter?

#4 May 20, 2007 afternoon session

Discussion Topic: Amaranth Advisors—Part II
Why wasn't the LTCM 1998 crisis repeated?
Was leverage the real culprit?
Why is CT AG Blumenthal investigating?
Are any prime brokers in jeopardy?
Did risk management fail?

Was Amaranth a multi-strategy fund?
Was Amaranth a hedge fund?
Do recent events give "multi-strategy" funds a black eye?
Was Amaranth a hedger or speculator in natural gas?
What lessons can investors learn from this episode?

Lecture Topics: Amaranth—Part III
Lessons about risk, leverage, and liquidity

Reading material: <http://www.iafe.org/upload/IAFEValuationConcepts0604.pdf>

Lecture Topic: Valuations of financial instruments held by hedge funds; Benefits to society from hedge funds; Alpha; Infrastructure; Marketing rules.

#5, June 3, 2007 morning session

Lecture Topics: DDQs; Non-financial risk management; Service providers; Administrator; Funds of funds; Investment vehicles; Hedge fund indices; and History.

#6, June 3, 2007 afternoon session

Lecture Topics: Regulations
Structuring hedge funds
Tax aspects

Instructor Biography

LEON M. METZGER, an adjunct professor at Columbia and NYU, lecturer at Yale, and consultant to the financial services industry, was associated with Paloma Partners Management Company for 18 years, most recently as its vice chairman and chief administrative officer. An expert witness on hedge fund matters, he also has developed and taught hedge fund courses at Wharton. Metzger has testified before Congress on capital markets, and has appeared as an expert on valuations and hedge funds before the CFTC, SEC, Treasury, IRS, GAO, and IOSCO. He has an MBA from Harvard and BS in economics from Wharton.