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Highland, Brevan Howard Build Out Retail Alts Funds

By Rachael Levy May 11, 2016

A handful of hedge fund firms are building out their retail product lines, tapping into new sources of capital at a time when investors are clamoring for lower fees.

Each of the funds has unique structures, but all have the same goal: raise money from investors who for the most part are not eligible to invest in private funds.

Highland Capital Management is prepping a slew of "interval" funds that would be open to a wider swath of investors. Meanwhile, **Brevan Howard** has opened two retail UCITS funds in Luxembourg and **Man Group** is teaming up with American Beacon Advisors to launch a new mutual fund, the second in its repertoire, according to people familiar with each firm.

The moves come as hedge funds have been under fire for underperforming and charging relatively high fees.

"Philosophically, these hedge fund managers have seen some of the big successes from the likes of **Blackrock** and **AQR** that have jumped into the [1940 Investment Advisers Act] space," says **Dick Pfister**, CEO of **AlphaCore Capital**. "They're looking to get access to that retail customer and diversify their client base."

Highland is in the early stages of prepping seven interval funds that will target the wealth management channel, says **Dustin Norris**, Highland's chief product strategist.

The funds, structured as regulated investment companies (RICs), can take on more illiquid securities than alternative mutual funds and set longer redemption periods, often quarterly.

Highland's plans, currently under regulatory review, put it alongside other alts players that have launched interval funds in recent years, including **Skybridge Capital** and Blackstone Group, as reported. Interval funds are becoming more popular as the liquid alts trend grows and as investors seek higher returns through more illiquid assets, says **Andrew Rogers**, CEO of **Gemini Fund Services**.

The new products fill a growing pocket of interest, Norris says.

"Right now, there's a demand for lower-fee products, and greater transparency than most private offerings," he says.

Highland's interval funds would invest in illiquid assets – such as high yield credit and REITs – that are unsuitable for mutual funds. The firm plans to make the funds accessible to all investors and offer quarterly liquidity, Norris says. Highland's funds would charge a management fee but no incentive fee, a better fit for retail investors, who aren't used to paying performance fees, Norris says. The lack of an incentive fee also is what would allow Highland to market the funds to all investors, he adds.

The new funds are coming on line as Highland has hired 14 sales representatives targeting independent brokerage advisors.

"There are some larger broker dealers and wirehouses where we might be able to sell this product, but largely I think there will be demand in independent broker-dealer channel," he says.

The retail expansion shouldn't hurt the manager's hedge fund unit, adds **Michael Gregory**, CIO of Highland Alternative Investors, a platform within Highland's retail arm.

"This is a fund management company creating different product types, not just for different channels, but to meet end market demand," Gregory says. "We don't see this being cannibalistic in any way."

London-based Brevan Howard is also joining the retail fray, as it preps distribution for two UCITS funds that it seeded last year, according to a source familiar with the firm. Brevan Howard may even open U.S. alternative mutual funds later down the line, the source says.

"Liquid alts is a big thing, a big trend for managers," the source says. "Brevan Howard doing this is pretty much inevitable."

The firm had been looking to break into liquid alts for some time, bringing on former UBS exec **Roberto Hoornweg** to oversee liquid alts development in 2014, the source says.

The launches come as Brevan Howard's private funds business faces headwinds. Its master hedge fund manages about $20 billion, about half what it managed in 2013. The fund returned a negative 2% last year and is down 1.8% through April this year, the source says. Investors requested $1.4 billion in redemptions in the first quarter, the source adds.

London-based Man Group is also expanding its offerings in the retail space. The firm is in the early stages of preparing its second mutual fund, this time focusing on fixed income, partnering with American Beacon, according to sources familiar with the plans. The first fund, the American Beacon AHL Managed Futures Strategy Fund, launched in 2014 through a partnership with Man Group's **Man AHL** subsidiary and has steadily grown in assets, now managing $464.5 million.

These retail launches come as some managers have faced bumps in the market. **Blackstone Group**, for instance, recently lost **Fidelity Investments** as a major investor in one of its liquid alts vehicles. But the alts firm still plans to plow ahead with retail funds, and expects to hit "the double digit billions on this kind of stuff," according to comments during a recent earnings call from Blackstone COO and president **Tony James**.