

Record declines in hedge funds

Industry report shows third quarter saw all-time highs in investor redemptions and asset shrinkage.

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NEW YORK (CNNMoney.com) -- Nervous investors fled hedge funds as the market meltdown got underway, setting records for investor redemptions and asset declines in the third quarter, according to a report from an industry research firm issued Friday.

Hedge Fund Research, a Chicago-based firm, said investors took out more than \$31 billion in the quarter, the largest net capital redemption in the industry history.

This redemption of capital by investors has contributed to a record \$210 billion decline in industry assets during the quarter, most of it from investment losses. The quarterly drop was more than last year's total record inflow of \$194 billion.

"Investors in the current market conditions are eagerly looking to rush to cash," said Kenneth Heinz, president of Hedge Fund Research.

"They're so distraught by performance losses, not only by hedge funds, but wherever you are in financial markets," said Heinz.

He said investors need the cash to fill commitments elsewhere, like paying bills.

Scott Baker, a principal at Connecticut-based Cook Pine Capital, said much of the retreat by investors with the largest percentages of their net worth in the market.

"The smaller investors need the quicker liquidity," said Baker.

However, he said wealthier investors and historically strong institutions have not pulled out of the market. Baker said his firm, focused on high net worth clients who rely on hedge funds for a minor portion of their portfolios, has not seen any redemptions of late.

For the first nine months of 2008, funds have registered a net capital decline of \$2.5 billion.

The firm said September, which saw such events as the Lehman Brothers bankruptcy and government intervention in Fannie Mae (FNM, [Fortune 500](#)), Freddie Mac (FRE, [Fortune 500](#)) and American International Group (AIG, [Fortune 500](#)), was the second worst month in industry history. It said funds lost 5.5% last month, second only to the 8.7% drop in August 1998, when the Long-Term Capital Management hedge fund went bust, shaking the financial markets and forcing a Bear Stearns-like bailout by investment banks.

Total capital in the entire industry shrunk to \$1.72 trillion at the end of the third quarter, down from \$1.93 trillion at the end of the second quarter.

An index developed by Hedge Fund Research indicates that this year could result in the first annual hedge fund performance decline since 2002.

"With losses continuing through October, it appears that 2008 will be the worst year on record for both hedge fund performance and industry asset flows," said Heinz, in a statement. ■

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