

Corporate & Financial Weekly Digest

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FSA Reports on Assessing Possible Sources of Systemic Risk from Hedge Funds

On February 29, the UK Financial Services Authority (FSA) produced its latest biannual report *Assessing Possible Sources of Systemic Risk from Hedge Funds*. This report sets out the results of the FSA's latest (September/October 2011) performance of its two regular hedge fund surveys: the Hedge Funds As Counterparties Survey (HFACS) and the Hedge Funds Survey (HFS). The FSA conducts these surveys every six months to assist it in understanding potential sources of systemic risk in the hedge fund sector. (For an article on the most recent previous HFS and HFACS, see the July 29, 2011 edition of [Corporate and Financial Weekly Digest](#).)

The February 29 report's conclusions include the following:

- The footprint of surveyed hedge funds is generally small when measured by the value of their exposures and by turnover. Potential exceptions are the markets in convertible bonds, commodity derivatives and interest rate derivatives.
- In aggregate, hedge funds reported that they are able to liquidate their assets more quickly than when most of their liabilities fall due. Nearly all surveyed funds reported the ability to suspend investor redemptions or create side pockets. However, the risk of a sudden withdrawal of funding during stressed market periods is likely to remain, with an associated risk of fire sales of assets.
- Counterparty credit exposures to hedge funds remain fairly concentrated among five counterparty banks. From the perspective of the banks, by tightening their financing terms they have increased their resilience to possible fund defaults.
- Leverage, measured in aggregate, has not changed significantly relative to previous surveys. It remains highest for fixed income strategies.
- Most surveyed hedge funds reported negative returns for the survey period.

The FSA stated that it intends to repeat the HFS and HFACS in March/April 2012. It also intends to continue to work closely with the International Organization of Securities

Commissions and other national regulators with a view to achieving a consistent and proportionate global approach to systemic risk data collection for hedge funds.

For more information, click [here](#).

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