EK INVESTMENT MANAGEMENT LIMITED

5 November, 2001

Investment Products Department
Securities and Futures Commission
12th floor Edinburgh Tower
The Landmark
15 Queen's Road Central
Hong Kong

Dear Sirs,

Re: Consultation Paper on the Offering of Hedge Funds

I refer to your Consultation Paper on the Offering of Hedge Funds.

In view of the lack of a clear definition for the term "Hedge Fund" the decision on whether a "market segmentation approach" or a "full public offering approach" should be adopted depends greatly on the criteria the SFC uses in defining what constitutes a hedge fund. I am not sure if a logical discussion of the relative merits of the two approaches can be carried out until such criteria are clearly established.

I also believe that the qualitative criteria used to judge the suitability of a fund manager deserves further consideration. In particular, the paper suggests that two important criteria used to judge the quality of a fund manager are (i) the number of years of fund management experience of key personnel and (ii) the size of fund under management. Unfortunately, neither criterion bears any relationship to the overall performance or risk level of the funds managed by the fund manager — and the *risk* of the fund and its *performance* are the *key* criteria in assessing the protection of investors' interest. It is true that *accurate* measures of risk can be difficult to find, and performance at a particular point in time can be misleading, but there are many criteria that are *more* relevant than using years of experience and the size of fund under management.

Similarly, the requirement for frequent narrative reports does not necessarily provide investors with any protection at all. This is because it is often extremely difficult if not impossible to determine, even on hindsight, whether any narrative report accurately reflects reality.

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1802 Bank of America Tower, 12 Harcourt Road, Hong Kong.
Telephone: (852) 2973 0622 Fax: (852) 2521 4964

For the above reasons the SFC should consider the use of quantitative measures. The challenge in using quantitative measures is to identify those that are useful to the SFC and/or investors but not intrusive to a fund manager's possible proprietary or commercially sensitive information. For example, many managers will object to the timely disclosure of underlying positions since such information can be commercially sensitive and freely used by competitors.

However, there are quantitative measures that are informative but not intrusive. One measure would be the ratio of funds managed by a manager that have outperformed their respective benchmarks *since inception of the respective funds* to the total amount or number of funds managed by the manager. Any manager that provides valuable service to investors should be able to show a ratio of over 50% under both methods except under extreme circumstances.

There are many other quantitative measures in addition to the one cited above. An exhaustive discussion of the pros and cons of the many possible measures, both quantitative and qualitative, is beyond the scope of this letter. However, I hope that the above has highlighted some issues that should warrant further study.

Thank you for your attention and consideration.

Yours sincerely,

Edward Kong
President

EK/rf