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All That Glitters Is Not Gold: An Analysis of U.S. Public Pension Investments in Hedge Funds.

Hedge funds have aggressively pursued U.S. public pension dollars, maintaining that they offer pension funds absolute return and volatility reduction in exchange for the high management and performance fees that they charge. And many public pension systems, with encouragement from their investment consultants, have made significant allocations to hedge funds, chasing the promise of superior returns and downside protection. These pension funds now have sufficient experience to evaluate whether hedge funds have delivered on their promise, and whether the purported benefits are worth the high fees.

This report by Elizabeth Parisian of the American Federation of Teachers and Roosevelt Institute Fellow Saqib Bhatti examines whether hedge funds have, in fact, provided U.S. pension funds better and less correlated returns, and whether hedge fund fees are adequately disclosed and as disproportionately high as critics suggest. In other words, they seek to answer the question: "Would public pension funds have fared better if they had never invested in hedge funds at all?"

To answer this question, the authors analyzed 11 U.S. public pension funds' experience with investing pensioners' savings in hedge funds. Using publicly available data and information provided directly by the pension funds, they conducted a simple year-by-year comparison of hedge fund net returns and total fund net returns for each pension fund. They also compared these rates of return to fixed income net returns for each pension fund to determine whether hedge funds delivered on the promise of uncorrelated returns and whether less expensive fixed income strategies do better. Because hedge fund fees are almost never reported or fully accounted for, Parisian and Bhatti used industry standard fee structures like management and incentive fees then projected actual fees captured by hedge fund mangers based on readily available statements of net return to investors. These calculations, while not precise due to lack of transparency with respect to fees, allow them to draw general conclusions about the performance of pension funds' hedge fund investments.

Read the Report.

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