



CASE STUDY

Derivatives Fund: Investment and Valuation Assessment

An FTI Consulting expert advised a top tier bank's prime brokerage business in its assessment of a potential claim against the investment manager ("IM") of a derivatives foreign exchange ("FX") hedge fund.

SITUATION

An Asia based hedge-fund (the "Fund") became insolvent following a large move in spot price and volatility in the USD vs. Turkish Lira (and other Turkish Lira cross currencies). This created a significant loss to a top tier bank prime brokerage business.

The Fund was invested primarily in complex derivatives FX strategies that involved a core strategy of volatility risk premium monetization with a long volatility convexity overlay implemented through a spread of volatility derivatives (long variance swaps vs. short volatility swaps).

OUR ROLE

The FTI Consulting expert:

- reviewed the details, expected implementation and the expected mechanism to capture returns based on the Fund’s stated strategy;
- analyzed the Fund’s trading patterns and positions;
- reconstructed the actual strategy employed by the IM; and
- compared the Fund’s actual strategy with the Fund’s investment mandate and public communications.

We provided an assessment of various valuation and risk management issues with the complex derivative products traded by the Fund, including concentration and illiquidity.

The expert at FTI Consulting analyzed the events in the Turkish Lira spot price and volatility markets and the impact on the Fund’s derivatives portfolio. We reviewed the IM’s trading activity following an initial market shock and evaluated its competence in managing the Fund in that stressed period.

We assessed the IM’s thesis of what caused the Fund’s losses and provided a corrected analysis of what led to the Fund’s insolvency.

OUR IMPACT

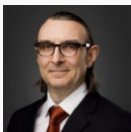


Through a detailed quantitative analysis, the FTI Consulting expert established that the IM didn’t act responsibly. It deviated from its stated strategy and investment mandate, misrepresented and/or misunderstood the risks of its strategy and ran excessive market, liquidity and concentration risk.



We provided our client with key strategic options and critical investment and quantitative expertise in its litigation strategy.

The views expressed herein are those of the author(s) and not necessarily the views of FTI Consulting, Inc., its management, its subsidiaries, its affiliates, or its other professionals. FTI Consulting, Inc., including its subsidiaries and affiliates, is a consulting firm and is not a certified public accounting firm or a law firm.



FRANCK RISLER, Ph.D.

Senior Managing Director & Leader
Securities, Commodities and Derivatives
+1 212.841.9348
franck.risler@fticonsulting.com