

FOREWORD BY STEVE GALBRAITH

TED SEIDES

SO YOU WANT TO START A
HEDGE FUND

LESSONS FOR MANAGERS
AND ALLOCATORS

WILEY

Additional Praise for *So You Want to Start a Hedge Fund*

There are virtually no books on the topic of how to pick individual hedge fund managers, so this is a must read for any asset allocator, whether a professional or a high net worth investor. In fact, all aspiring or current managers would also benefit from reading this book. Ted shares his wisdom from two decades of investing in hedge funds of all types and sizes, with particular insight into investing in early stage managers.

—Jonathan A.G. Auerbach, Hound Partners

There is no one better-equipped than Ted Seides to author a book on starting a hedge fund. From his early training at the Yale Investment Office to his instrumental role at Protégé Partners backing some of the best and brightest investment managers, Ted has forgotten more than most of us will ever know about the challenges of launching a fund. His refreshingly honest insights will resonate with readers of all backgrounds.

—David Z. Solomon, Managing Director,
Goldman Sachs Investment Partners

Ted Seides' extensive experience in identifying and supporting emerging hedge fund teams provides him with a unique insight into the hedge fund industry and valuable lessons for investors in the asset class. His book provides an interesting view into the challenges and opportunities for astute investors.

—Paula Volent, Senior Vice President for Investments,
Bowdoin College

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For Eric, Ryan, and Skylar (in alphabetical order),
My three most treasured start-ups.

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FOREWORD

When I followed one of my mentors, Barton Biggs, in setting up my own investment firm a few years back I felt uniquely prepared to embark on that effort. After all, I had spent nearly a decade at one of the best run hedge funds in the business, a number of years at Morgan Stanley, one of the most important brokers servicing the industry, several years as a securities analyst covering the investment management industry and ten years teaching Ben Graham's Securities Analysis Class at Columbia Business School. Just through osmosis I got to know a number of folks who have built wildly successful investment operations. I even sat (and still sit) on the board of Rich Pzena's eponymous investment firm. What the heck else was there for me to possibly consider? Hang out my shingle, raise a few shekels and get on with it.

Well, before I rang that opening bell a friend of mine counseled that I should reach out and spend time with Ted Seides. I am glad I did. No one knows more about the start-up process for a hedge fund than Ted. He has become a key player in driving the growth of the modern hedge fund industry from its early stage as the popular new kid on the block, through awkward adolescence to the mature, institutional paradigm that dominates the landscape today. Ultimately, Ted not only became an important early investor in my fund but also a friend; I am immensely grateful to know him in both capacities.

Which brings me to *So You Want to Start a Hedge Fund*. Prior to college, I must have read every book ever published on baseball. Good (*My Turn at Bat*) or bad (*Super Joe—The Life and Legend of Joe Charboneau*) the combination of statistics and larger than life personalities sucked me in where fiction could not. When it became clear the Red Sox were not going to be in the market for a left-handed shortstop, I turned my literary focus to books on the investment world. I am not ashamed to admit it—I have read pretty much every book published on investing. From *People* magazine-like treatments of investment “stars” to the only true investment Bible—Ben Graham’s *Securities Analysis* I must have read them

all. Amazingly though, despite explosive growth in the hedge fund industry (there are now more hedge funds than stocks listed on the NYSE) and breathless coverage from the media that vacillates between fawning and *schadenfreude*, there have been virtually no insightful treatises on the inner workings of hedge funds. Until today.

So You Want to Start a Hedge Fund is the first book written by an insider that looks under the hood of the industry and offers thoughtful views on key success drivers and pitfalls—for asset allocators and managers alike. Effectively, through a combination of anecdotes, data and reasoned judgment, Ted has produced the first owner's manual for the hedge fund industry. Crucially though, this is not a cookbook. That is, there is no secret recipe inside that says start with a bag of dough, add some quantitative meat, season with experience and you have an alpha pie. As with picking stocks—while there may be basic True North principles in building (or selecting) an investment management business—there is also an immense amount of nuance to the process. Ted captures that here.

Ted has also seen firsthand virtually every mistake an investment entrepreneur can make. I now know—I made a bunch of 'em—most outlined vividly in this book. For the budding hedge fund manager—trust me—you will

find your own creative and original mistakes to make, so you may as well use this book to avoid the more familiar ones. Indeed, one of my chief regrets is that Ted did not write the book three years ago so I could have read the galleys *before* I launched my firm. Not only might the knowledge imparted from *So You Want to Start a Hedge Fund* saved me time and effort—it would have kept me out of the damn book altogether as one of the proverbial cautionary tales.

Finally, while Ted accuses me of being one of the more likeable guys on Wall Street (which, to be clear, would merit a slander lawsuit from any number of today's hedge fund *Masters of the Universe*) it is obvious that *he* has to take the nice guy blue ribbon. After all, only Ted Seides could engender enough goodwill to get me to write a foreword to his first book after subjecting my firm to the financial equivalent of a colonoscopy in his due diligence process. What a wonderful business. It is captured superbly in the pages that follow—enjoy.

Steve Galbraith
Founder
Herring Creek Capital
Stamford, CT
October 12, 2015

ACKNOWLEDGMENTS

I want to take this opportunity to thank the people who influenced my career and led me down the path leading to this publication.

Many friends have been influential in helping me learn about myself, an essential characteristic for success in investing and in life. My parents, Jane and Warren Seides, have provided unconditional love and support through every mountain and valley on my journey. I am deeply indebted to Shari Greenleaf, Michael Mervosh, and Kali Rosenblum, each of whom has shared countless pearls of wisdom walking alongside me.

My investment education started under the tutelage of David Swensen and Dean Takahashi at Yale back in 1992. The building blocks of my knowledge came from

Acknowledgments

their brilliant minds, scholarly approach, and teaching orientation. I was lucky to land in their offices upon graduating college and am grateful to have started my career working for a dynamic duo who imparted values of integrity, balance, and service that resonated strongly within me.

While at Yale, I met Charley Ellis, then a member of Yale's Investment Committee. Charley was one of the first investment luminaries who saw something in me I had not yet seen in myself. He encouraged me along the way, wrote a recommendation that helped me gain entry to business school, and overwhelmingly expressed his enthusiasm at this effort, just as he did when David wrote his seminal work 15 years ago. Charley is a masterful storyteller and a gracious man who knows how to make each person he is with feel like they are the most important one in the room; an admirable exemplar of presence to behold.

The team at Protégé Partners since its onset experienced these stories alongside me and contributed to my understanding of the lessons learned. I am indebted to my former colleagues for their hard work and challenging insights along the way.

Acknowledgments

Much of what I learned at Protégé came from our partnerships with money managers. Some are mentioned in this book and many others are not. You all know who you are, and you have my deepest gratitude for being the driving force behind Protégé's success.

INTRODUCTION

A little over two decades ago I had the good fortune to enter the working world under the tutelage of one of the world's greatest investors, Yale University's renowned chief investment officer David Swensen. David is a gifted teacher and provided an unparalleled investment education to everyone who had the privilege to work for him. His innovative investment ideas and disciplined framework established a foundation that my former colleagues and I built off in our own ways ever since.

From those early years in my career, I developed a passion for investing in people. One of Yale's many levers of success has been its extraordinary ability to partner with top managers across all asset classes in the start-up phase

of their businesses. Helping someone at a key moment in their career and serving as a catalyst to realize their dreams resonated so strongly with me that it carried through my post-MBA path to the formation of Protégé Partners.

I have met so many passionate, intelligent, and high-quality people through my work the last 20 years that these pages could not give the vast majority justice. Some of these folks have become world famous—from my first manager meetings in 1992 with Jeremy Grantham and Tom Steyer to what became an infamous charitable wager with Warren Buffett. Many others have demonstrated fantastic investment success while maintaining a low profile in the investment world and next to none outside of it. Many more never achieved their lofty aspirations despite herculean efforts.

My role in this ecosystem afforded me the privilege of working with those I believed would be the best of the best and fostering those relationships over time. It should come as no surprise that many also have become friends. As I once told Warren, I invest in people—the smartest, hardest-working, and best ones I know. He responded, “I do the same thing.”

THE SECRET SAUCE

I wish after all this time that I had a secret recipe to deliver success to deserving start-up investment funds. Unfortunately, no such recipe exists. A new fund in today's market faces an intensely competitive landscape in an industry with a preexisting cornucopia of products. Differentiating based on product or price has been tried in just about every way, shape, and form already.

A number of managers nevertheless launch successfully every year, thereby defying the odds for start-ups in aggregate. These firms create meaningful businesses that reward their clients, employees, and ultimate beneficiaries over time. The checklist of essential ingredients for the winners in this game appears generic on the surface—a record of success throughout life, ability to raise money, skill to generate excess returns, development of repeatable processes, creation of suitable infrastructures, attraction and retention of talented investment staffs, temperament and grit to weather challenging times, and good luck. This same set of characteristics describes more failures than successes, so the subtleties in executing each facet of the business matter.