

HEDGE FUND: ECONOMY

NEWS: Chevron share rises as it clinches Hess acquisition after winning Exxon legal battle

WHAT'S IN THE NEWS?

Hedge funds are private investment vehicles for wealthy investors, employing aggressive strategies like leverage and short-selling for high returns, with limited regulation globally and falling under SEBI's Category III AIFs in India. Their distinct features include high "2 and 20" fee structures and limited liquidity, differentiating them significantly from mutual funds.

Hedge Funds and the Chevron-Hess Acquisition Outcome

The recent conclusion of Chevron's **\$53 billion acquisition of Hess Corp.**, after a **20-month delay** caused by arbitration challenges from ExxonMobil, has led to **significant gains for hedge funds**.

Hedge Funds: Definition and Nature

- **Definition:** A hedge fund is a **private investment partnership**. It serves as a pooled investment vehicle that gathers funds from a select group of investors, typically high-net-worth individuals (HNIs) or institutional investors.
- **Management:** These funds are actively **managed by professional portfolio managers**.
- **Aggressive and Diverse Strategies:** Hedge fund managers employ a wide array of **aggressive and diverse investment strategies** with the primary goal of maximizing returns. These strategies often include:
 - **Leverage:** Using **borrowed money** to amplify potential returns (and risks).
 - **Derivatives:** Investing in complex financial instruments like futures, options, and swaps whose value is derived from an underlying asset.
 - **Short-selling:** Profiting from a decline in asset prices by selling borrowed securities and buying them back later at a lower price.
 - **Arbitrage:** Exploiting price discrepancies between identical or similar assets in different markets to make risk-free (or low-risk) profit.
 - **Non-traditional Assets:** Investing in a broader range of assets beyond traditional stocks and bonds, such as commodities, currencies, and real estate.

Risk Profile and Investor Base:

- **High Risk, High Return:** Hedge fund investments are classified as **alternative investment vehicles** and are generally considered **high-risk, high-return** propositions due to their aggressive strategies and use of leverage.
- **Targeted Investor Base:** Due to their inherent risks and often complex nature, hedge funds typically have strict requirements, including a **high minimum investment or a high net worth** for investors. They specifically target:
 - **Accredited Investors:** In the US context, these are individuals with an annual income greater than \$200,000 (or \$300,000 with a spouse) for the last two years, or a

net worth exceeding \$1 million (excluding their primary residence). Similar criteria exist in other jurisdictions.

- **Institutional Investors:** Large entities such as pension funds, university endowments, and insurance firms, which have substantial capital and a higher risk tolerance.

Regulatory Framework:

- **India (SEBI):** In India, hedge funds are not necessarily required to be registered as "hedge funds" under a specific category. However, structures akin to hedge funds typically fall under **Alternative Investment Funds (AIFs)**, specifically **Category III AIFs**, which are regulated by the Securities and Exchange Board of India (SEBI).
- **Global Regulation:** Globally, hedge funds generally face **less stringent regulation** compared to traditional mutual funds. This is particularly true in jurisdictions known as offshore financial centers, such as the **Cayman Islands or British Virgin Islands**, where many **offshore hedge funds** are legally domiciled.

Hedge Fund vs. Mutual Fund: Key Distinctions

Aspect	Hedge Fund	Mutual Fund
Target Investor	Accredited / wealthy individuals, institutional investors	General public / retail investors
Instruments Used	Real estate, stocks, bonds, derivatives, currencies, commodities	Primarily stocks, bonds, money market instruments
Regulation	Lightly regulated (e.g., SEC, SEBI-AIF Cat III)	Heavily regulated (e.g., SEBI, SEC)
Liquidity	Limited; often subject to lock-in periods and redemption gates	High liquidity; typically redeemable on demand (daily)
Strategy	High-risk, high-return, often speculative, absolute returns, market-neutral	Conservative to moderate, long-term growth, relative returns
Fee Structure	High fees; typically "2 and 20" (2% management fee + 20% of profits)	Lower fees (usually 0.5%–2% as expense ratio)

Source: <https://economictimes.indiatimes.com/news/international/us/chevron-share-rises-as-it-clinches-hess-acquisition-after-winning-exxon-legal-battle/articleshow/122767487.cms?from=mdr>