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Mad as hell and Icahn take it any more

"Independence is for the very few; it is a privilege of the strong."

- Friedrich Nietzsche.

There has been much chatter among the financial chatterati about Carl Icahn's recent decision to hand back capital to investors in his funds. Since he's apparently keeping some $5 billion of his own money invested, this doesn't appear to amount to a closure as such, rather a polite de-emphasis of third party client capital. Here is what he wrote to his limited partners:

"While it may sound "corny" to some, the losses that were incurred by investors in our funds in 2008 bothered me a great deal more, in many respects, than my own losses. Perhaps this is because over the years I have become inured to dealing with large "paper" losses for myself. During 2008 and part of 2009, unlike many other funds, we did not impose "gates" on our investors that would have prevented them from withdrawing capital from our funds if they chose to do so. Therefore investors seeking liquidity did withdraw a fair amount of cash from our funds. Additionally, rather than liquidating positions that we believed in, we infused our own new capital into our funds which provided cash for withdrawing investors. As a result, fee paying assets now constitute only 25% ($1.76 billion) of total assets in the funds of approximately $7 billion.

"While we are not forecasting renewed market dislocation, this possibility cannot be dismissed. Given the rapid market run-up over the past two years and our ongoing concerns about the economic outlook, and recent political tensions in the Middle East, I do not wish to be responsible to limited partners through another possible market crisis. After careful consideration of all relevant factors, we have determined to return all fee paying capital to investors."

The knee-jerk response by the financial chatterati was that Icahn had grown "weary" of managing other people's money, and was getting out while the going was good, ahead of a possible "market dislocation" that he was careful to suggest, rather than predict. The chatterato on the Clapham Omnibus, the FT's Lex columnist, pointed out that hedge fund managers Stanley Druckenmiller and Paolo Pellegrini last year either "chucked it all in" or returned external capital:

"Cynics say that hedge funds are simply being found out at last.. the decisions to quit raise a bigger concern: that the industry remains a fragile one based on superstars."

We draw an entirely different conclusion, consistent with the fact that we do not represent a financial newspaper heavily dependent on advertising revenue from traditional fund management firms: Mr Icahn's decision to return money to external investors is a principled decision to conserve his investors' capital. If anyone is being "found out" here, it is those traditional asset management groups that continue to tout for business irrespective of any necessary obvious ability to add value for their investors that those investors are not capable of delivering for themselves. There are, in other words, fundamentally only two types of institutional investors: asset ***managers***, and asset ***gatherers***. Mr Icahn can plainly be seen to be in the first school. We prefer not to point fingers as to who might be caught nervously 'cramming' in the second, but as a clue you can probably find plenty of their advertisements in publications such as The Financial Times. We are certainly hounded sufficiently by them in unsolicited approaches either in email or telephonic form. It is an intriguing insight into the over-sophistication of the London capital markets that fund managers are now busily selling to each other: the market has started to eat itself. In the words of Mark Twain, fund managers are now furiously taking in each other's washing. Could it be that, three years into the banking crisis, fund managers are now the only people with any money left ?

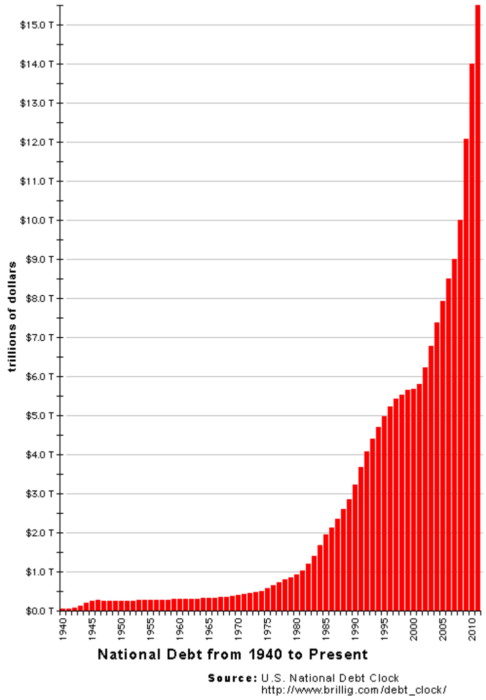
We find behaviour such as Mr Icahn's refreshing, albeit exceedingly rare. One beauty of hedge funds that Lex's probably imaginary (or self-representing) cynics do not recognise is that the typical hedge fund manager has plenty of skin in the game, in the form, ordinarily, of a substantial part of his or her net worth as part of the fund's overall capital. Their interests are largely aligned with those of their investors. The same cannot be said for the typical open-ended, long-only, traditional fund, in which the typical manager is a hired hand, with little or no skin in the game. The fact that the typical traditional manager is invariably pursuing an index-relative (read: unsophisticated, if not plain stupid) strategy merely adds insult to injury.

The decision of individuals like Messrs Icahn, Druckenmiller and Pellegrini to de-risk their clients' assets may not be indicative of a wider trend, given the extraordinarily low barriers to entry and constant churn in the asset management business. If it is, it is likely only to reflect the decision-making of principled investors with a greater focus on capital preservation and their clients' well-being than on asset gathering and fee generation. It is to be applauded, rather than disparaged as part of a generalised attack on a sub-set of the asset management business marked 'alternative'.

Interestingly, within the same edition, Lex also cites "Star" bond fund manager Bill Gross, of Pimco. We have no animus against Mr Gross whatever, but we do wonder whether he or his company has ever turned down new assets citing size of assets constraints or fears about prospective returns. If they haven't, they may wish to. (We note their recent sales of US Treasuries.) Because contra-indicator par excellence James Glassman has now advised anyone mentally deranged enough to buy his latest book, 'Safety Net: the strategy for de-risking your investments in a time of turbulence' to load up the truck on US Treasury bonds.

Those who appreciate stunningly poor investment advice will need no introduction to James Glassman. He is the co-author of a book titled 'Dow 36,000' which was published in 1999, just months ahead of the market peak. Your correspondent remembers this book with a certain grisly satisfaction, since his erstwhile employer, Merrill Lynch Private Banking in London, distributed free copies to the entire ~~sales~~workforce shortly before the stock markets blew up. Having succeeded once at inadvertently calling a huge market top by advising everyone to pile in to the stock market, it could well be that Mr Glassman has, incredibly, managed to pull off the same trick in relation to the US government bond market. We have no intention of wasting any time in reading this almost certainly clownish piece of magical thinking, but within it Mr Glassman purportedly recommends a 50/50 allocation between stocks and bonds. There would appear, sadly, to be no role for absolute return investments or real assets in Glassmanland – a realm, perhaps, populated entirely by writers about investments all guesting on channels like CNBC dispensing unsolicited investment insights to the mentally defective, none of whom are likely listening to a word that their fellow panellists say, all of whom refuse to admit when they've got it catastrophically wrong in the past. Evidently the financial media in 2011 is much like a particularly easy-going Heaven: all sins are forgiven, and penitence isn't even required for entry.

Time to buy US Treasuries ? The US national debt (in $ *trillions*)



In the grotesque event that Mr Glassman is right about buying US Treasuries, the good news is that at least there's no shortage of the damn things. You should have no trouble buying them to your heart's content. And to those of us who insist on being defensively positioned as a matter of course given the strained financial environment, news like Mr Icahn's is a bit like hearing an ice cream van tootling past: all quite nice, but it doesn't really change anything.

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