

PERSPECTIVES

Prime Time: How to Evaluate Your Counterparty Relationships

Key considerations for selecting a prime broker



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As a hedge fund manager, you know the indispensable value of strong and meaningful counterparties. Whether you are an emerging manager looking to strengthen your offering and find ways to generate alpha or an established fund looking to differentiate counterparty risk profile, evaluating your prime brokerage partners should be an ongoing undertaking.

The right combination of prime brokers can help you better execute your investment strategy through maximizing securities lending access, streamlining trade execution, creating efficient financing solutions, and bolstering your cash management approach.

We believe that it is a best practice to continuously evaluate your counterparties. Markets are constantly evolving. Think of the changes in the market over the past few years — from rising interest rates and inflation to geopolitical issues and regulatory changes. It's a lot, but the core tenets of diversifying and evaluating your prime brokerage relationships remain the same. You want to have diversification of risk, of securities lending access, of financing and balance sheet. We believe this will leave you best situated for success in an ever-changing market environment.

How to evaluate a prime broker

You should consider several characteristics when looking to diversify your prime brokerage counterparties, including the institution's business model, risk profile, balance sheet strength and flexibility. Here are a few things to watch for beyond the basics.

- **Find the right mix of institutions.** You should look to diversify your counterparties among banks with different risk and business profiles. Consider custody banks versus investment banks, U.S. banks versus European banks and retail-oriented banks versus institutional banks.
- **Seek stability.** When determining the best complementary partner, be sure to consider their product offering, source of securities lending supply, financing capabilities, and stability in weathering volatile markets.
- **Dig a little deeper.** Look at a provider's level of transparency in its financing costs and securities lending offering, its customer service, and ultimately its level of personalized attention.

The value of the right relationships

Hedge funds work most effectively when they have a diverse roster of business partners. Combining the strength of prime brokers with different risk profiles and complementary suites of services can enhance the alpha generating capabilities of a fund. The ultimate goal of a hedge fund is to deliver outperformance — and you cannot do so without working with a prime broker that helps to mitigate risk while helping you deal with the ever-increasing complexity of today's investment landscape.

- **Explore value-added services.** Value-added services and a differentiated product offering are often points that drive informed decisions on adding a prime broker.
- **Expand your network.** If adding new investors is a driving factor in your decision, take a closer look at the prime broker's Cap Intro team. Are they able to provide the resources and attention you'll need to connect with new investors?
- **Examine your gaps.** Review the products and services of your current prime broker and compare them to those offered by other firms. The goal is not to find a counterparty who mimics the strengths and offering of your existing provider, but rather to identify a prime broker who can help fill gaps and complement your current partner.
- **Ask the right questions.** Is your prime broker the right size for you? Are you an important client to a few counterparties or are you spread too thin over many? Are you working with a team that is focused on your needs and provides meaningful and impactful client service?

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