TrimTabs

The Leading Independent Research Firm for Equity Market Liquidity

THE HEDGE FUND FLOW REPORT

SHOWING ONLY THE TOPICAL STUDY INCLUDED IN THE NOVEMBER 2010 ISSUE

BarclayHedge

The Global Leader in Alternative Asset Research

Topical Study: TrimTabs/BarclayHedge Survey of Hedge Fund Managers

- Hedge fund managers remain downbeat on equities. About 39% of the 102 managers we surveyed are bearish on the S&P 500, while 36% are bullish. Nevertheless, the bullish reading is up significantly from 17% in August.
- Other indicators confirm that hedge funds and speculative traders are downbeat on stocks. NYSE short interest decreased 2.1% between August 31 and October 15, while the S&P 500 soared 12.1% in the same period. Triple long leveraged U.S. equity ETFs have redeemed $1.5 billion since the start of September, while triple leveraged short U.S. equity ETFs hauled in $1.2 billion.
- Hedge fund managers are bearish on Treasuries. About 28% are bearish on the 10-year Treasury note, the largest share since the inception of our survey in May, while only 22% are bullish, the smallest share since June. In contrast, managers have turned much more upbeat on the U.S. dollar index. About 32% are bullish, the largest share since June, while 30% are bearish.
- Downbeat stocks sentiment notwithstanding, managers remain inclined to lever up. About 19% aim to increase leverage in the coming weeks, while only 9% plan to reduce it - the smallest share since we started our survey.
- We attribute this desire to add leverage to short-term interest rates that round to zero - borrowing is virtually costless - and relatively poor performance. A third of the funds in the BarclayHedge database are underwater for the year, and about half posted a return smaller than 2% through September. Many managers need a blockbuster Q4 in order to collect performance fees.
- About 32% of managers cite currency wars as the biggest threat to global financial stability. About 25% name sovereign defaults in developed economies (which probably would have been the most popular answer in the previous two quarters), while only 7% identify excessive speculation in emerging markets.
- About 36% of managers feel too-big-to-fail institutions should be the top priority at the November 11-12 G-20 Seoul Summit, while 20% cite better transparency in the OTC derivatives market. About 51% of managers think a large victory by the Republican party in November's U.S. midterm elections will be positive for the stock market.

Note on Methodology:

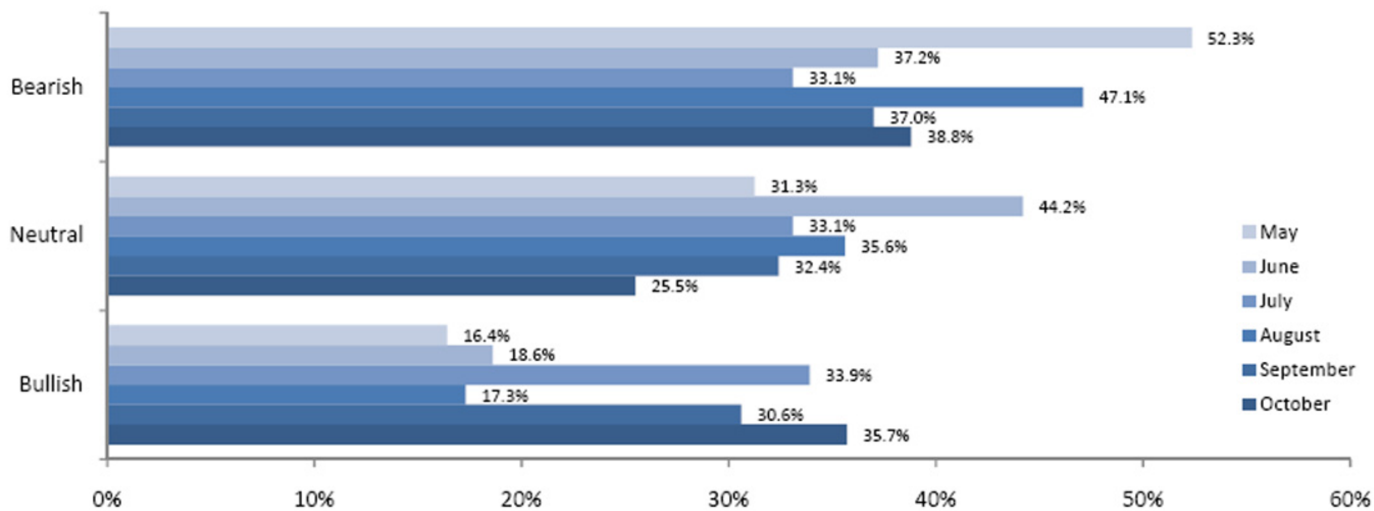
We conducted our October 2010 survey between October 18 and October 22. We surveyed hedge fund managers and commodity trading advisors, and we offered a complimentary issue of the Topical Study featured in the November issue of the TrimTabs/BarclayHedge Hedge Fund Flow Report for participating. One hundred and two managers responded. Their assets under management average $30 million and top out at $375 million.

Hedge fund managers remain bearish on equities. Bullish contrary indicator - leveraged long equity ETFs redeem hefty $1.5 billion since start of September, while leveraged short ETFs haul in $1.2 billion.

Hedge fund managers remain downbeat on equities. About 39% of the 102 managers we surveyed in the past week are bearish on the S&P 500, while 36% are bullish. Nevertheless, the bullish reading is not only up significantly from 17% in August, but also the largest since the inception of our survey in May.

TRIMTABS/BARCLAYHEDGE SURVEY OF HEDGE FUND MANAGERS

S&P 500 Sentiment



Generally bearish sentiment is a bit surprising given the recent rally (the S&P 500 has soared 13.0% since the start of September), but it squares with other indicators. NYSE short interest decreased 2.1% between August 31 and October 15, while the S&P 500 surged 12.1% in the same period. Short interest is heaviest in Consumer Discretionary (5.9% of market cap) and Telecommunication Services (4.8%), the most cyclical sectors, while it is lightest in Consumer Staples (2.9%) and Utilities (3.3%), the most defensive sectors.

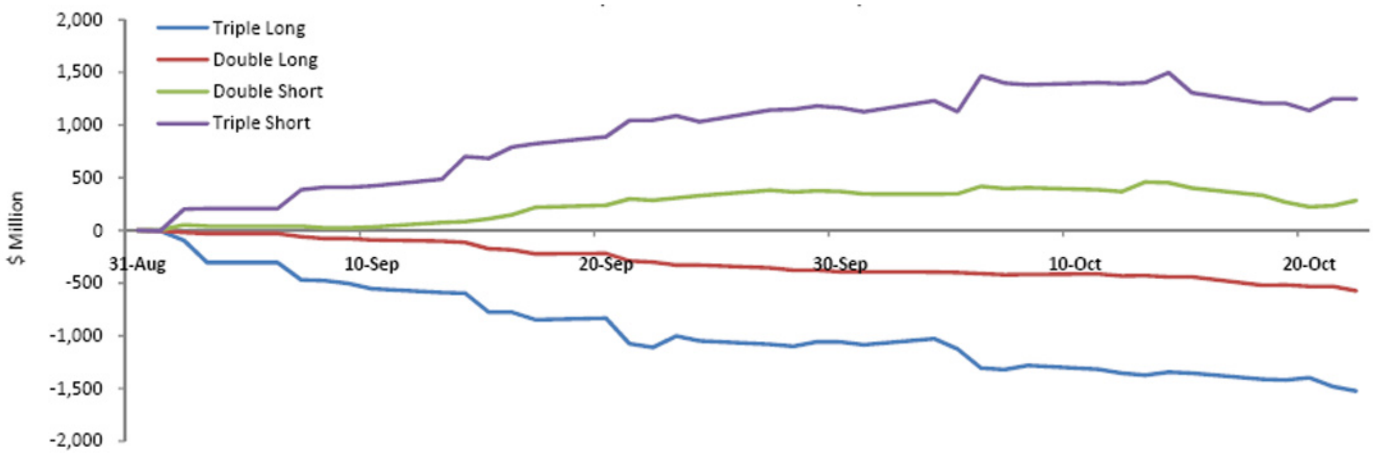
Sector Focus: Short Interest as % of Market Cap for S&P 500 Stocks

	11-Oct-10	30-Sep-10	15-Sep-10	31-Aug-10	13-Aug-10	30-Jul-10
Consumer Discretionary	5.87%	5.93%	6.01%	5.84%	5.52%	5.31%
Consumer Staples	2.90%	2.92%	2.91%	2.89%	2.90%	2.87%
Energy	4.03%	3.90%	3.79%	3.73%	3.74%	3.69%
Financials	4.07%	4.07%	4.13%	4.04%	3.95%	3.94%
Health Care	3.37%	3.41%	3.37%	3.31%	3.21%	3.15%
Industrials	3.34%	3.36%	3.43%	3.27%	3.21%	3.21%
Information Technology	4.39%	4.52%	4.54%	4.30%	4.31%	4.25%
Materials	4.53%	4.52%	4.62%	4.49%	4.32%	4.23%
Telecommunication Services	4.80%	5.06%	4.78%	5.74%	5.56%	5.37%
Utilities	3.25%	3.50%	3.46%	3.66%	3.39%	3.52%
All	**4.12%**	**4.17%**	**4.19%**	**4.11%**	**4.00%**	**3.95%**

Additionally, leveraged ETF flows, which best reflect the mood of the most speculative investors, have been extremely bearish. Triple long leveraged U.S. equity ETFs have redeemed $1.5 billion since the start of September, while triple short leveraged U.S. equity ETFs have hauled in $1.2 billion. This is akin to investors dumping $10.0 billion in domestic stocks. Our research shows that leveraged ETF flows are an excellent contrary indicator, so we view a large increase in leveraged short bets and a hefty decrease in leveraged long bets as especially bullish for equities.

NET POSITION OF SPECULATIVE TRADERS ON TREASURY FUTURES

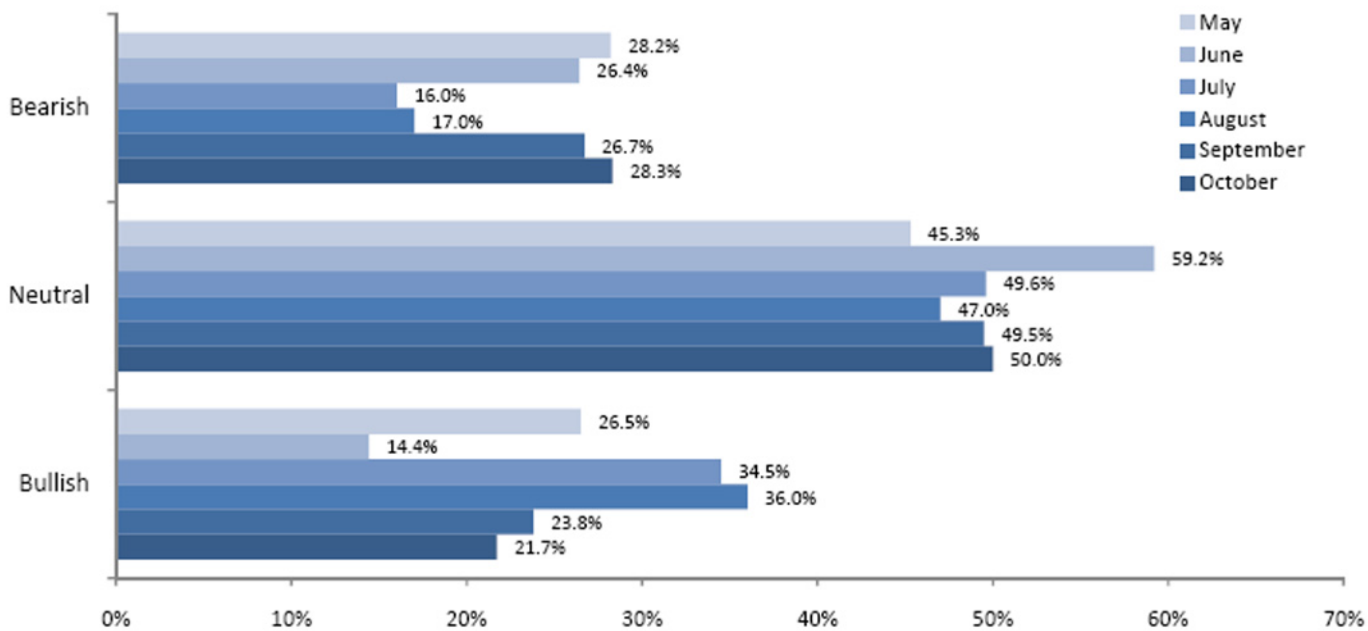
Getting Burned



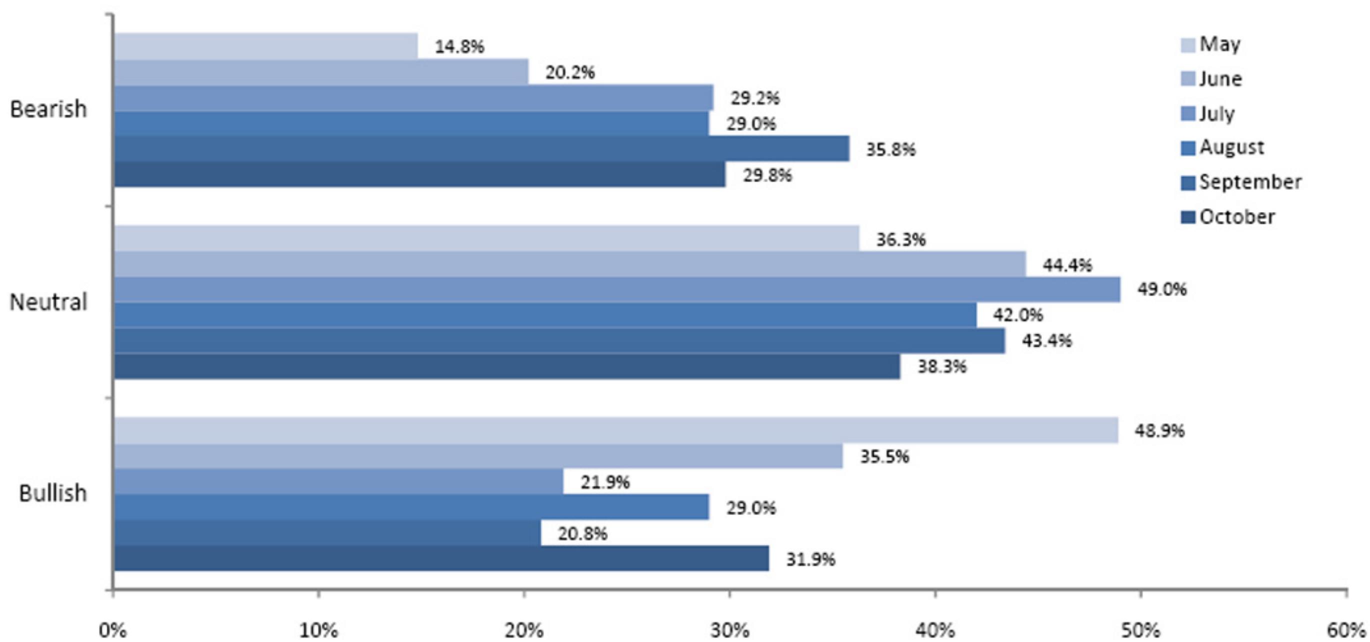
Hedge fund managers bearish on Treasuries. Managers turn bullish on U.S. Dollar Index but remain bearish on greenback pairs.

Hedge fund managers are also bearish on Treasuries. About 28% of the managers we surveyed are bearish on the 10-year Treasury note, the largest share since the inception of our survey in May, while only 22% are bullish, the smallest share since June. In contrast, managers have turned much more upbeat on the U.S. dollar index. About 32% are bullish, the largest share since June, while 30% are bearish.

Sentiment on 10-Year Treasury Note



Sentiment on U.S. Dollar Index



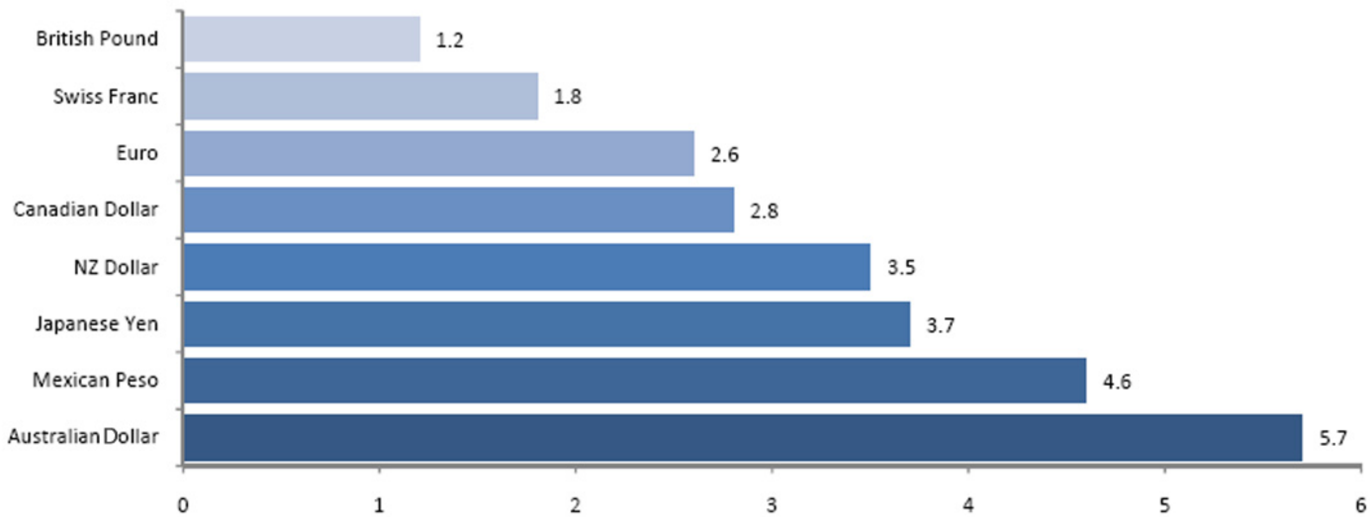
Commitments of Traders (COT) reports (http://www.cftc.gov/marketreports/commitmentsoftraders/index.htm) also reveal upbeat greenback sentiment. Speculative traders (including hedge funds and commodity trading advisors) are long U.S. dollar index futures to the tune of 22,789 contracts, while they are short 19,608 contracts.

Interestingly, spec traders are simultaneously bearish on greenback pairs. In fact, we do not see a single currency spec traders are selling against the U.S. dollar. Spec traders have net long positions of 5.7 to 1 on the Australian dollar, 3.7 to 1 on the yen, 2.8 to 1 on the Canadian dollar, and 2.6 to 1 on the euro.

We believe the greenback's safe-haven status explains the discrepancy. The dollar typically rallies when stock prices decrease, and most managers expect the S&P 500 to decline. Managers are bullish on the U.S. dollar index in that they expect the greenback to appreciate in generic terms.

At the same time, our surveys show that managers are extremely concerned about the impact of quantitative easing and runaway deficit spending. The U.S. might well be the country that has thrown the most money at its economy, so hedge fund managers are hard-pressed to come up with a specific currency against which they like the greenback to rally.

Spec Traders Long/Short Ratio on Currency Futures vs the U.S. Dollar

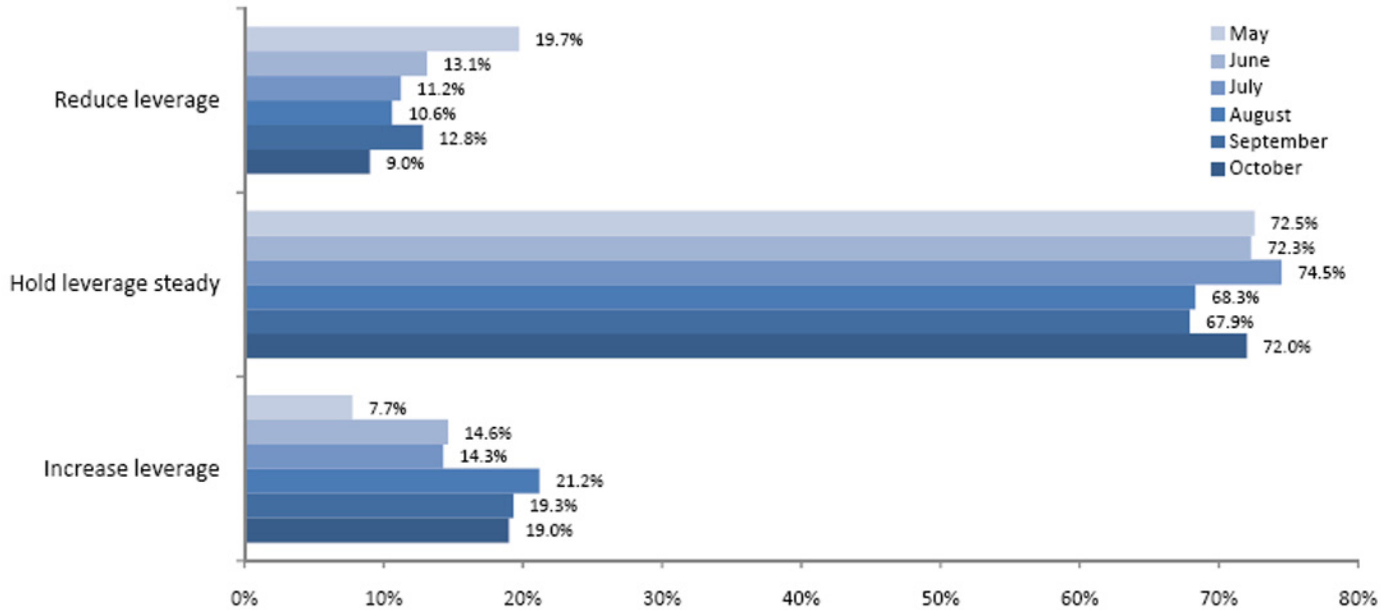


Hedge fund managers aim to increase leverage. A third of hedge funds are underwater for the year.

While hedge fund managers are predominantly bearish on equities, they remain inclined to lever up. About 19% aim to increase leverage in the coming weeks, while only 9% plan to reduce it - the smallest share since the inception of our survey in May.

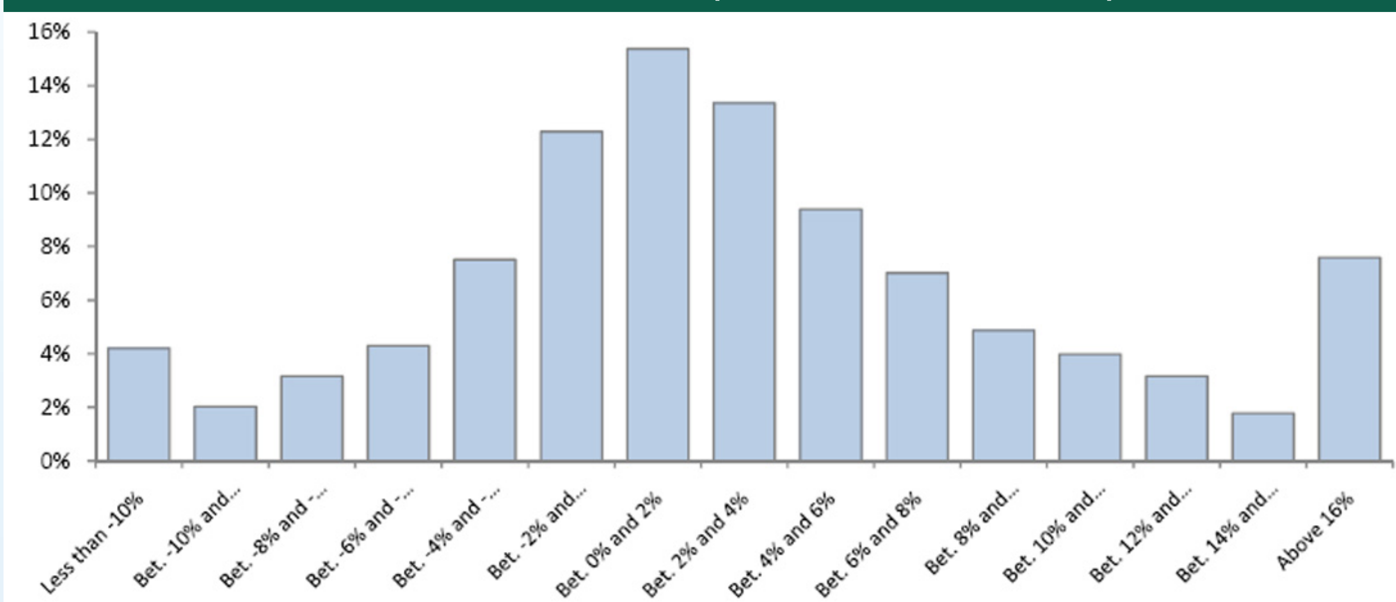
Why are downbeat managers interested in increasing leverage? First, short-term interest rates that round to zero are a huge incentive to lever up. Yields and spreads are so low that managers need much more leverage to reach target returns. When it costs virtually nothing to borrow, even very small spreads are profitable if enough leverage is applied.

What are your leverage plans for the next month?



Second, many managers need a blockbuster Q4 in order to collect performance fees. About 34% of the funds in the BarclayHedge database are underwater for the year, and 49% posted a return smaller than 2% through September (the S&P 500 is up 2.3% in the same period). The pressure to deliver returns is even more intense because most hedge fund indices stand only slightly north of their May 2008 high water marks. Hedge funds rebounded dramatically last year, but most managers did not collect performance fees because they had to recoup losses suffered in Q4 2008. Most managers can ill afford a third year of forced frugality.

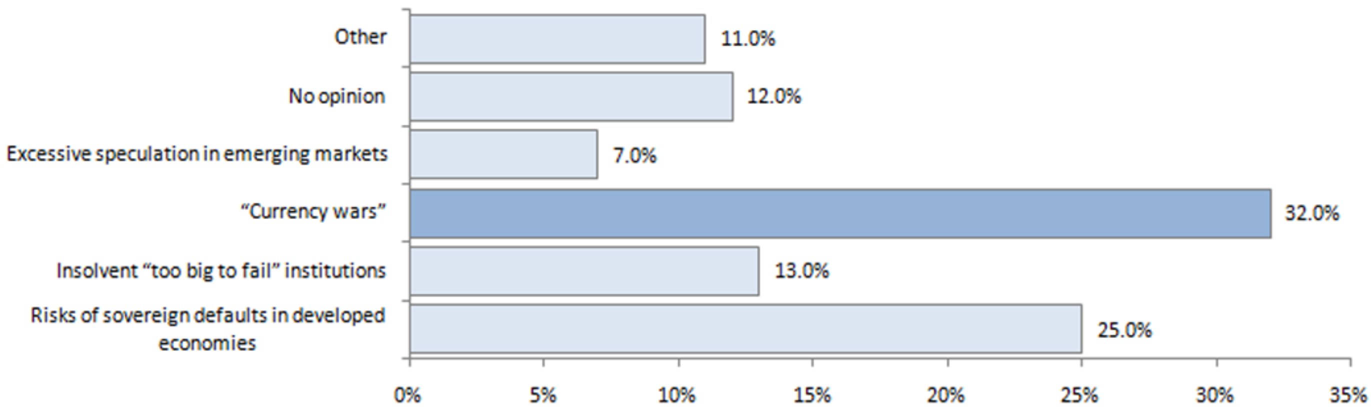
RETURNS OF HEDGE FUNDS (YEAR-TO-DATE SEPTEMBER 2010)



Hedge fund managers view currency wars as the biggest source of systemic risk. Managers want G-20 to focus on too-big-to-fail institutions.

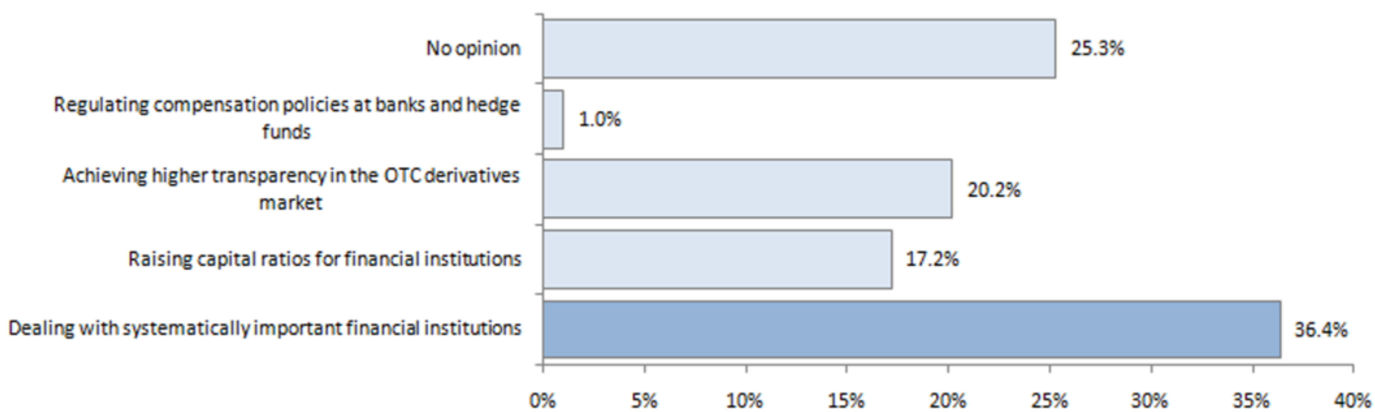
Our other survey questions focus on macro financial stability. When we asked managers to identify the biggest source of systemic risk, 32% cited currency wars and 25% named sovereign defaults in developed economies (which probably would have been the most popular answer in the previous two quarters). Only 7% of managers cited excessive speculation in emerging markets. About 11% named other factors such as government intervention and QE2 (6%) and the U.S. mortgage market (2%).

In your opinion, what are currently the biggest sources of systemic risk?



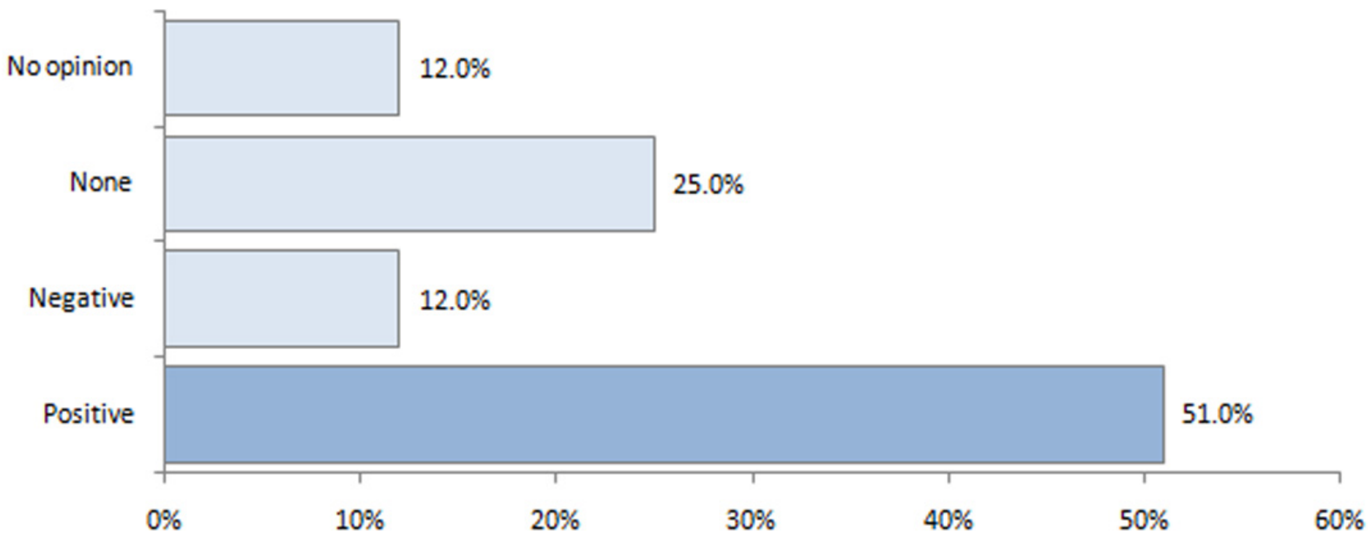
We also asked managers what should be the most important item on the agenda at the November 11-12 G-20 Seoul Summit. About 36% of managers feel too-big-to-fail institutions are the top priority, while 20% cite better transparency in the OTC derivatives market. Not surprisingly, only 1% of hedge fund managers name tighter regulation of compensation at banks and hedge funds.

In order to prevent another financial crisis, the upcoming G-20 meeting in Seoul should focus on:



Finally, we asked hedge fund managers if they think a large Republican victory in next month's midterm elections will be a positive for the stock market. We guessed that most managers would answer in the affirmative because Republicans are generally viewed as more pro-business than Democrats and history shows that equities perform better when one party does not control the executive and legislative branches of government. Most managers do feel a Republican win is a plus for equities, but the figure is relatively small (51%). Additionally, 25% of managers feel a GOP victory will have no impact on stocks, while 12% view it as a negative. We attribute these figures to two factors. First, the gambling line on Republicans taking control of the House is prohibitively expensive. Odds makers put the chance of a GOP win at 83%, so markets have already priced it in. Second, many managers probably believe there is little government can do to support asset prices. Our previous surveys suggest that managers view monetary policy (especially quantitative easing) as the most dominant driver of short-term market moves.

What effect would a large victory by the Republican party in the U.S. midterm elections have on the U.S. stock market?



This article was included in the November 2010 issue of the TrimTabs Hedge Fund Flow Report.

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Methodology and Survey Response Rate

Graphs: Flows & Returns by Strategy

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