Levine on Wall Street: Calpers's Exit and Alibaba's Debut

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More Calpers.

Here is Cliff Asness on Calpers's exit from hedge funds: "hedge funds are too correlated to equity markets," "most hedge funds are too expensive," and while there are some very good hedge fund managers, "we are not surprised that some have found that the broad universe of hedge funds, and thus likely any very large diversified portfolio of them, is not an attractive enough proposition." Since my views on the story are largely based on his previous writings, you will not be surprised to find that I am in sympathy with this. Here is a chart of the wide dispersion in stock-picking skill among hedge funds. Here is Tadas Viskanta on the implications of Calpers's withdrawal. And here are other investors pondering the implications, including one saying that "There is a lot of disappointment that hedge funds have not been able to capture more of the market results," which I guess is sort of the opposite of Asness's complaint.

Alibaba and governance.

What should you think about Alibaba's corporate governance? The possible choices are "meh whatever" or "it's a terrrrrrible risk," and only one of those is worth writing about, so the writing about it skews worried. Here is Lucian Bebchuk: "It is important for investors, however, to keep their eyes open to the serious governance risks accompanying an Alibaba investment." He focuses on the fact that the people who run Alibaba hold only a relatively small chunk of the equity, and so are not aligned with shareholders; in particular Jack Ma is a bigger owner of Alipay than he is of Alibaba (itselt the result of a transaction that left people a bit puzzled), and so the worry is that he will seek to benefit Alipay at the expense of Alibaba shareholders.

The headline on Bebchuk's piece, which I bet he didn't write, is "Alibaba’s Governance Leaves Investors at a Disadvantage," and the important question there is "disadvantage compared to what?" Compared to not investing in Alibaba? Like, if the stock goes up, and then you sell it, how did your disadvantage manifest itself? Here is a very thoughtful Aswath Damodaran post on the value to shareholders of corporate governance, reviewing both the theory and the evidence: "Proponents of stronger corporate governance argue that it critical to corporate performance, but the evidence of the link between the two is not very strong." Damodaran's personal conclusion about Alibaba is "I don't like being asked for my money (as an investor) and then being told that I have no say in how it's run," but that is an idiosyncratic preference. All of my money is invested in companies in which I have no practical say in how they're run, and I would never want to tell a company how to run itself; I can barely manage my own life. If some smart entrepreneur wants to use my money to make more money and then give me a share in the profits, without bothering me for input, more power to him. Though obviously I'd prefer that he not just run off with my cash.
**Bill Ackman and governance.**

If you run an activist hedge fund, you're probably pretty committed to the idea that shareholders own companies, they should have a say in how those companies are run, etc. etc. But if you take your activist hedge fund public, you're probably pretty committed to irony! Because obviously Bill Ackman is not going to go public in a vehicle where he can lose a proxy fight and be replaced by Carl Icahn, though I really hope Icahn will give it a go. Anyway here is the story of Pershing Square Holdings's dual-class share structure; apparently Holdings will be controlled by "a Canadian breast-cancer charity unaffiliated with the investment firm or with Ackman," mostly to meet legal requirements associated with doing the thing offshore.

**Credit Suisse is making risky loans.**

U.S. banking regulators have decided that they don't like leveraged loans; in particular, loans to companies levered at more than 6 times Ebitda are suspect. Banks have more or less decided to ignore the regulators -- they "seem to be testing the mettle of the regulators," says a lawyer. The regulators are mad and have escalated in the way regulators do: They have sent Credit Suisse a sternly worded letter "known as a Matters Requiring Immediate Attention" (sic). These rules just feel weird, don't they? (We've previously discussed them [here](#).) Like, the way the game is supposed to work is that regulators micromanage the right-hand side of banks' balance sheets, with capital and funding requirements, but they mostly leave the left-hand side alone and let banks make whatever loans they want. Or, more accurately, they regulate the left-hand side through risk-based capital requirements; the more capital you need to make a loan, the less attractive that loan is, but there's always a game to be played of maximizing returns within the constraints of the capital rules. So the job of the regulator is to decide how banks capitalize themselves, and the job of the banker is to decide what to do with the money. Just telling bankers that they can't lend at more than 6 times leverage seems to go too far somehow.

**Some dark pools.**

Eric Schneiderman [filed his response](#) to Barclays's motion to dismiss his dark-pool lawsuit, which sounds like it's more jurisdictional (does the Martin Act apply only to sales of securities, or also to sales of places to sell securities?) than entertaining. But he's already having an effect, as dark pools are becoming more transparent in the wake of Schneiderman's discovery of Barclays's ... umm creativity in marketing its dark pool. And [here is a speech](#) from Securities and Exchange Commission member Daniel Gallagher about high-speed trading and market structure, with a lot of skepticism about Regulation NMS, the SEC rule that more or less created modern U.S. equity market structure:

To begin, it is well past time to place Reg NMS under a microscope and analyze the underlying assumptions that led the Commission -- in a contested 3-2 vote -- to adopt it, as well as the unintended consequences that have arisen from its implementation. ... A prime example of one of the many elements of Reg NMS that should be subjected to a de novo review is the “trade-through” rule, which requires trading centers to establish, maintain, and enforce written policies and procedures reasonably designed to prevent the execution of trades at prices inferior to protected quotations displayed by other trading centers. In other words, rather than allowing
markets to compete for order flow, the trade-through rule requires orders to be routed to an SRO that displays the national best bid or offer.

**Some Rule 105 dopes.**

A thing called Rule 105 says that you're not allowed to sell a stock short right before it prices a public offering, and then buy shares in that offering, because that just seems unsporting. But people do it all the time! Big, responsible people like BlackRock. One assumes that it's totally inadvertent; like, one manager in this $1.1 trillion BlackRock entity shorts a stock, and another puts in an order for some stock in the offering, and the systems don't prevent it. But the systems should prevent it, and inadvertence is no defense to a small fine and a minor embarrassment. Here is the SEC fining 19 firms relatively small amounts of money for doing this. I've heard this referred to as the SEC's equivalent of broken-windows policing, and there's a pretty good argument that if you only focus on big dangerous intentional violations of the securities rules no one will have the right incentives to get the little-but-still-important things, like Rule 105, right.

**Oh, Radio Shack.**

Here is Steven Davidoff Solomon making fun of Radio Shack, which has had a long and varied and comical history.

**Things happen.**

Roddy Boyd and Keith Larsen on "a 50-year old inventor, teacher, community leader, entrepreneur and soon-to-be space tourist." The Wall Street Journal on Paul Bilzerian's efforts to avoid paying an SEC judgment. Bill Gross replaced Treasuries with futures. These equity-neutral convertible bonds are weird. "Abatement Corp." was a Ponzi. SAC Capital is no longer registered with the CFTC. Bill Koch vs. fake wine. More views on Olive Garden. Some Guy On Tinder Just Has A Picture Of His Bank Balance As His Profile Pic. The Government Keeps Helping People Buy Failing Cold Stone Creameries. This Coffee Start-up Uses Whiskey Instead of Water in Its Cold Brew. There are hipsters in Portland. Trend Piece. Read books, more of them, mostly print.