Lock-Up Period

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A lock-up period is the minimum investment holding period required by hedge funds. During the lock-up period, the investors cannot take money out of the fund. The hedge fund industry distinguishes between hard and soft lock-ups. A soft lock-up can be neutralized by paying an early redemption fee, a hard lock-up cannot. In general, most hedge funds require a 12-month lock-up period. A lock-up period also refers to the initial subscription—hence, when reinvesting more funds, investors are again subject to the lock-up period, even if the initial period has expired. Lock-ups mean more flexibility for hedge fund managers because they can stay invested in illiquid assets for a longer period of time.

Numerous academic studies have found a positive correlation between the length of the time the capital is invested and the hedge fund performance. One explanation for this phenomenon may be the illiquidity premium investors realize if they are willing to provide capital to a hedge fund over the long term. The liquidity realized by hedge fund investors, however, is always expected to be a function of the liquidity of the traded instruments. Aragon (2004) found that the yearly return of hedge funds with lock-up periods is about 4% higher than the return of those without lock-up periods. Agarwal et al. (2004) found that hedge funds with a respective track record and a lock-up period generally do not receive the same amount of capital as comparable hedge funds without lock-up periods. At the same time, however, they note that hedge funds with restrictive capital outflow mechanisms are expected to show better future returns because of the possibility of holding illiquid positions. These results coincide with those of Liang (1999), who finds that the large hedge funds with long lock-up periods and short track records exhibit superior performance overall.

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Long Position

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In finance, a long position indicates that the investor/trader promises to purchase an asset in the future. As a result, an increase in the asset price creates a gain for the holder of a long position contract. In the derivatives market, a long position implies that the holder of a long position contract promises to purchase the asset at a prespecified price for the delivery of the asset at a future date. For example, a trader taking a long position in a commodity futures contract promises to purchase the commodity at the delivery date by paying the prespecified future price at the delivery date. Similarly, a long position in a call option for a foreign currency indicates that the holder of the option contract will take delivery of the foreign currency at the maturity (or perhaps before maturity depending on the type of option contract). To sum up, one of the parties to a contract involving a derivative assumes a long position and commits to buying the underlying asset/instrument on a certain future delivery date for an agreed-upon price. The other party takes a short position and commits to selling the same asset/instrument on the same delivery date for the same agreed-upon price.

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Long Short Equity

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"Make money on alpha." Long short equity is a strategy that belongs to the category of opportunistic strategies. In long short strategies, undervalued equities that are expected to rise are bought long and/or overvalued equities that are expected to decline are sold short on spot and on futures markets. The long short disciplines are equity hedge, equity nonhedge, and short selling. Equity hedge portfolios are, usually, leveraged long positions that are hedged with derivative securities or short selling of stocks/stock indices at all times. For example, a manager could hedge the market risk with a put option on the relevant index. Equity nonhedge funds are very similar to traditional investment funds. Typically, they are long in equities and perform stock picking, but occasionally they also make use of derivatives and short selling. Short sellers concentrate on stocks with expected price losses. They generally assume that the market for short sales is less efficient because most investors try to find undervalued stocks.

Among others as a consequence of the chosen long short discipline, the long short equity portfolio can be long biased, short biased, or market neutral. A long biased portfolio has a net long position that results in a positive correlation to the market. The opposite is true for a short biased portfolio. Thus, the hedge funds can actively participate in falling (negative beta) or rising (positive beta) markets (market timing strategy). The special case of zero beta is called market neutral. For instance, this can be reached by the use of index derivatives.

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Long the Basis

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A person or firm is termed "long the basis" if he or the firm buys a commodity in the