



Federal Financial Analytics, Inc.

HEDGE FUNDS TO BE BATTERED BY NEW RULES, FEDFIN REPORT FINDS

“The bottom line: the bank regulators and SEC won’t mind much if a few hedge funds fail, but they’re doing their all to ensure no bulge-bracket banks go with them.”

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WASHINGTON, D.C. – Hedge funds should take little comfort from all the statements this week disavowing new federal rules, concludes a report released today by Federal Financial Analytics, Inc. (FedFin). Although direct hedge-fund regulations are unlikely, an array of supervisory initiatives already well under way will change the terms on which hedge funds do business with big counterparties and prime brokers. The most highly leveraged funds – and that’s a lot of them – will find it extremely challenging to do business under the new margin and collateral requirements. Further, new internal disclosures and valuation standards will change pricing – again to the detriment of many high-flying funds, FedFin reports.

FedFin notes that the banking agencies and SEC will issue official guidance on how to do business with hedge funds only to strengthen their hand in any enforcement action. The current plan is to demand tough risk-management and infrastructure improvements behind closed doors, adding the regulators’ stick to the carrots already offered to

encourage voluntary industry efforts. FedFin also concludes that Congressional action – including any to unwind the SEC registration rule – is highly unlikely.

“When the once and current Fed Chairman, the soon-to-be Fed Vice Chairman and the president of the New York Fed say the same thing at the same time, it’s not exactly a coincidence,” said FedFin managing partner Karen Shaw Petrou. “A concerted effort to improve U.S. counterparty credit risk management, OTC derivative trading and prime brokerage is under way. Firms that fail to heed these signals will get pulled over.”

A copy of the FedFin report is attached.

Federal Financial Analytics, Inc. has for the past twenty years counseled large financial institutions and even their regulators on major legislative, regulatory and policy issues that pose strategic risk. It does not lobby on behalf of clients, but advises them on appropriate responses in light of identified challenges, working on an array of GSE, Basel II, and acquisition-value issues. The firm publishes numerous information and analytical services, including Financial Services Management and GSE Activity Report.

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