Discussion About the Key Performance Indicator of the Segmentation Strategy and Macro Environment of the Privately Offered Fund

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Abstract. This paper focuses on the meaning of privately offered fund and its classification, studies its segments, and analyzes the core focus metrics of segmentation strategies. Secondly, it gives a better presentation of the characteristics and trends of privately offered fund through the above analysis. Finally, it discusses the macro environment suitable for privately offered fund segmentation strategy.

Keywords: Private Equity fund; Segmentation Strategy; Key Performance Indicator.

1. Definition and characteristics of the privately offered fund

1.1. Definition

Privately offered fund refers to that a non-public investment institution aims to help a small number of investors to achieve higher returns by providing a flexible investment approach and expertise, which can be achieved by fund-raising. It also helps investors have higher profits through sound management and control of risk.[1]

1.2. Characteristics

1.2.1 High threshold for investor participation

The raising of private securities funds is subjected to investors with a scale of assets and incomes, and good risk identification and tolerance ability, meaning legal investors as regulated in *Interim Measures for the Supervision and Administration of Private Investment Funds.* Investors must comply with relevant requirements of laws and regulations with a total number of less than 200. Therefore, investors must have good professional knowledge and skills.[2]

1.2.2 Limited fund-raising ways

According to the *Fund Law of the People's Republic of China*, fund-raising from non-qualified investors and advertising to non-specific audiences through any form of media shall not be allowed, which has resulted in the public knowing little about private equity [3] The Privately offered fund aims to provide financing services to qualified investors. Therefore, it must adopt a non-public and personalized approach to raise money.

1.2.3 Flexible investment strategy

The privately offered fund is used for investing in financial products such as stocks, bonds, futures, options, and commercial paper. Investment funds will be traded in the secondary market. Fund managers can flexibly adjust funds according to the market performance of different products, thereby reducing risks and achieving higher returns. Privately offered fund is very flexible in its investment strategies with a variety of investment tools to maximize returns, including fund long (buy out), fund short (sell out), fund short positions, and leveraged trading.[4]

2. Classification

2.1. Structural classification

Currently, the structural classification of the privately offered fund is as shown in the figure below. China's regulators have long adhered to the principle of Professional Management (professionals implement professional management) to ensure its effective management. Therefore, the privately offered fund is characterized by its investment direction and scope as the core classification criteria.

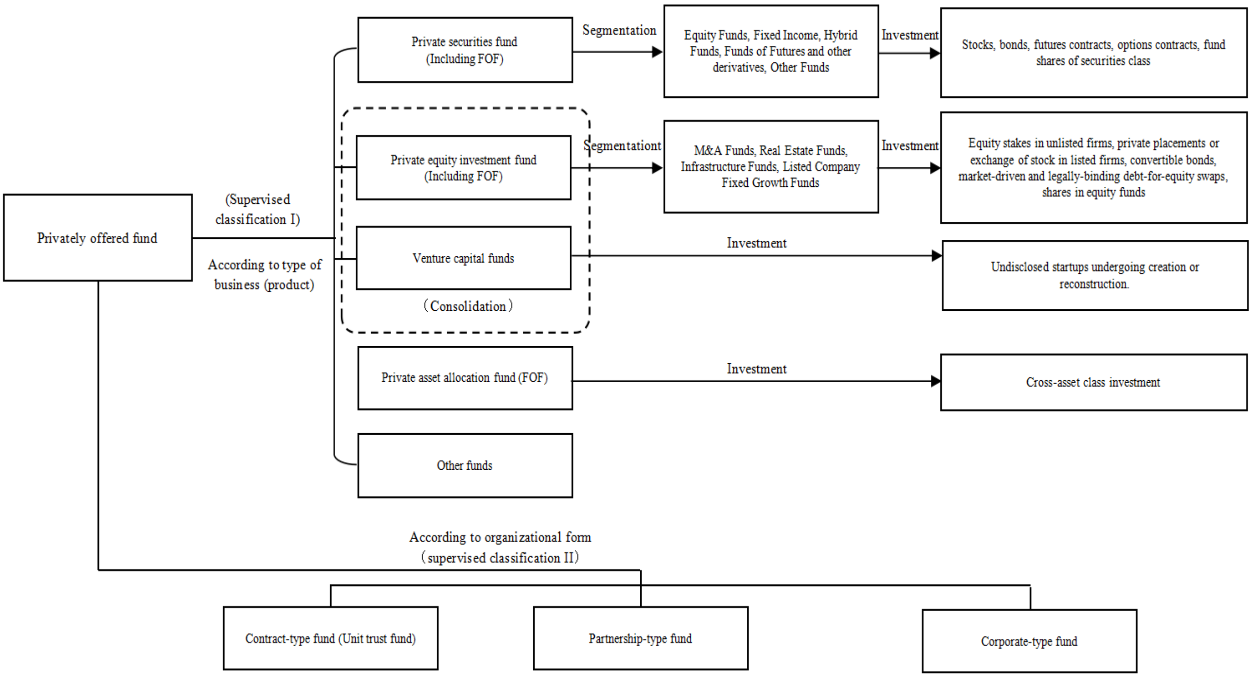

Figure 1. Classification of the investment direction of the privately offered fund [5]

Table 1. Classification of the investment scope of the privately offered fund.

Four major categories	8 fund types	Business	Product Type
Private Securities	Private securities investment fund	Used for investing in publicly traded stocks, bonds, futures, options, fund shares of joint-stock companies and other securities and their derivatives as prescribed by the China Securities Regulatory Commission;	Equity Funds Fixed Income Hybrid Funds Funds of Futures and other derivatives Other Funds
	Private securities FOF fund	Used for investing in privately offered funds for asset management plans such as securities-based privately offered funds, trust plans, brokerage firms' capital management, and fund-dedicated accounts;	-
Private Equity	Private equity investment fund	Used for investing in non-publicly traded corporate equity except for investing in venture capital funds; fixed growth funds are classified as equity investment funds.	M&A Funds Real Estate Funds Infrastructure Funds Listed Company Fixed Growth Funds Other Funds
	Private Equity Investment FOF Fund	Used for investing in privately offered funds for asset management plans such as such as privately offered funds, trust plans, brokerage firm’s capital management, and fund-dedicated accounts;	-
Venture Capital Fund	Venture Capital Fund	Used for investing in stock equity of growth unlisted enterprises in different stages (New Third Board listed enterprises are considered as unlisted enterprises); for the so-called Growth Funds in the market, if they are not involved in the Shanghai and Shenzhen Stock Exchange listed companies to invest in fixed growth stock investment, putting on records in accordance with the venture capital fund; if they are involved in the listed companies to invest in fixed growth stock investment, putting one records in accordance with the listed company fixed growth fund in the private equity investment funds.	-
	Venture Capital FOF Fund	Used for investing in privately offered funds for asset management plans such as securities-based privately offered funds, trust plans, brokerage firms' capital management, and fund-dedicated accounts;	-
Other Funds	Other private investment funds	Used for investing in other funds except for securities and their derivatives and equities;	Commodity Funds such as wine and art Other Funds
	Other private investment fund FOFs	Used for investing in privately offered funds for asset management plans such as securities-based privately offered funds, trust plans, brokerage firms' capital management, and fund-dedicated accounts.	-

2.2. Types and their definitions of privately offered fund products

The privately offered fund includes many types. To accurately classify them into different categories, it is necessary to have an in-depth understanding of these types.[6]

Table 2. Types and their definitions of privately offered fund products.

Fund Category	Product Type	Definition
Private securities fund	Equity Fund	It refers to a private securities fund used for investing in stocks or equity funds with more than 80% (including 80%) assets according to the investment scope agreed in a contract.
	Fixed Income Fund	It refers to a private securities fund used for investing in financial products with more than 80% (including 80%) assets such as bank deposits, standardized bonds, bond-type funds, share pledge buyback, and bank financial products and trust plans with expected yields according to the investment scope agreed in a contract.
	Hybrid Fund	It refers to a private equity investment fund used for investing in stocks, bonds, and money market instruments without specific investment direction according to the investment scope agreed in a contract.
	Futures and other derivatives funds	It refers to an advanced private securities investment fund used for investing in futures, options, and other financial derivatives according to the investment scope agreed in a contract.
Private equity funds	M&A Fund	It refers to a private equity fund used for acquiring the existing stocks of companies in the reconstruction period.
	Real Estate Fund	It refers to a private equity fund engaged in developing primary real estate projects, including investment funds by mezzanine capital.
	Infrastructure Fund	It refers to a private equity fund used for investing in infrastructure projects, including investment funds by mezzanine capital.
	Listed Company Fixed Growth Fund	It refers to a private equity investment fund used for investing in the fixed growth of listed companies.
Other Funds	commodity funds such as wine and art	It refers to a private equity investment fund used for investing in commodities such as wine and art.

2.3. Classification of the stock-based privately offered fund

2.3.1 Stock bull fund

As a flexible investment strategy for investors, it includes investments in both stocks and money-based funds and bonds. Such investments have no hedging or short positions so investors can flexibly adjust their investment strategies according to their investment needs to achieve higher investment returns.

Table 3. Classification of the stock-based bull fund

First-level classification	Investment Philosophy	Whether to benchmark the index
Stock bull	Subjective bull	/
	Quantitative bull	Reinforced type
		Quantitative stock-picking type

2.3.2 Equity market neutral fund

As an investment strategy, it invests in high-risk investors in the equity markets by hedging funds to avoid Beta risk and generate higher returns. Investment strategies commonly used by the neutral fund include equity index options, financing and securities loan, and over the counter/in-the-counter derivative investments.

Table 4. Classification of the Equity Market Neutral Fund

First-level classification	Secondary Classification
Equity Market Neutral	Trading type
	Traditional multi-factor
	Machine Learning
	T+O
	Composite

2.3.3 Equity long-short fund

As an investment strategy, it is used for investing in stocks that offer good investment returns and those with uncertain investment prospects to achieve the dual benefits of growth in undervalued assets and reduction in overvalued assets. Such a fund has a long-short advantage, allowing fund managers more freedom to make investment decisions.

Table 5. Classification of the equity long-short fund

First-level classification	Means of investment
Stock Long-short	Quantitative stock Long-short
	Subjective stock long short

2.4. Classification of the non-equity privately offered fund

2.4.1 Bond fund

The bond fund is used for investing in bond financial institutions, with higher management risks than public funds. The reason is that these institutions have a more complicated operational status and higher moral and credit risks.

Table 6. Classification of the bond fund

First-Level classification	Secondary Classification
Bond fund	Straight bond
	Forced bond
	Fixed income compound strategy

2.4.2 Managed futures fund

Commodity Trading Advisors focuses on different futures and options investment, including stocks, bonds, commodities, and OTC options by observing and analyzing price fluctuations in the market to achieve investment returns. The futures market is more investment value than the equity market by introducing a long-short system and leverage system. Investors not only gain investment returns from the volatility of the market but also enhance their investment returns by using the leverage principle.

Table 7. Classification of the Managed Futures Fund

First-level classification	Classification basis	Type
Managed futures	According to investment philosophy	Subjective
		Quantification
	According to Strategies	Trends
		Arbitrage
		Composite

2.5. Classification of the cross-asset privately offered fund

2.5.1 Arbitrage fund

The arbitrage fund refers to an investment fund used for buying and holding or long-short pairing mispriced assets to spread benefits through information asymmetry, valuation analysis, and high-speed trading. This type of fund can be laid out in various types of assets, such as commodities, foreign exchange, and ETFs.

Table 8. Classification of the arbitrage privately offered fund.

First-level classification	Arbitrage method
Arbitrage hedging	Convertible arbitrage
	Fixed income Arbitrage
	EFT arbitrage
	Other arbitrage strategies
	Fund arbitrage
	Stock index futures arbitrage
	Equity arbitrage

2.5.2 Macro fund

As an investment fund, it is used for allocating suitable assets in the waves of the economic cycle through subjective judgment or quantitative means based on a large-scale asset allocation method to maximize returns and reduce portfolio volatility.

2.5.3 FOF/MOM/Multi-strategy Funds

The FOF fund refers to a fund of funds, meaning an investment fund that an investment manager selects outstanding funds in each investment area suitable for his/her investment philosophy and style through long-term tracking and research of funds across the market and then entrusts the account funds to these funds for management.

The MOM fund refers to a manager's manager fund, meaning an investment product that an investment manager selects outstanding fund administrators in each investment area suitable for his/her investment philosophy and style through long-term tracking of market-wide investment administrators and in-depth study of their investment decision-making process, philosophy and styles and delegates sub-accounts to multiple administrators for investment management.

The multi-strategy fund refers to an investment fund that an investment manager selects strategies for allocation to the portfolio under different market conditions through long-term tracking of each strategy system and in-depth study of its theoretical basis.

The common point of the three types of funds is their use of diversification in funds across multiple funds/managers/sub-strategies for management, thus effectively reducing their systematic risks.

3. Segmentation strategies and key performance indicator of the privately offered fund

3.1. Stock Strategy

Stock strategies can be categorized into two major branches, subjective and quantitative strategies according to research methods and trading approaches. Similar to the public stock strategy, the traditional investment strategy-subjective stock picking strategy can be further divided into different types according to stock positions, investment themes, fund styles, and others. The quantitative strategy can be divided into two categories: quantitative long and quantitative hedging according to the use of hedging tools. It has developed rapidly in recent years with the technological development and the increasing market activity. Tens of billions of private stocks have sprung up one after another. Some institutions have marched towards 100 billion private stocks.

3.2. Quantitative Long Strategy

Known as quantitative stock picking strategy or air index increase, it is used for index-enhanced products, with the CSI 300, CSI 500, and CSI 1000 as the benchmark index. Private equity firms mainly focus on high-frequency volume and price strategies, holding as many as one or two thousand stocks and as few as a few hundred stocks, with a turnover rate of 50 to 200 times. Public equity firms mainly focus on fundamental quantitative stock picking, holding 100 to 300 stocks, with a turnover rate within 10 times.

3.3. Quantitative Hedging Strategy

It refers to using such ways as stock index futures and securities loan to short trading to form a hedge with the long side of the stock. It can be divided into two categories according to the exposure: market-neutral strategy and timing hedge strategy. The former is fully hedged or slightly exposed. The latter leaves a larger exposure, generally above 10% and dynamically adjusts according to market conditions.

3.4. Managed Futures Strategy (CTA)

With diverse product types due to the two-way trading and margin trading characteristics of CTA underlying investment target, it can be divided according to the investment target, trading method, trading frequency, strategy type, and other dimensions. According to the investment target, it includes commodity futures and financial futures: the former is mainly concentrated in energy chemicals, ferrous metals, and non-ferrous metals; the latter generally refers to stock index futures, options and treasury bond futures. According to the trading method, it can be divided into subjective strategy and quantitative strategy. According to trading frequency or position cycle, it can be divided into high frequency, medium frequency, and low frequency. According to the strategy type, it can be divided into trend following and statistical arbitrage.

3.5. Bond Strategy

It can be broadly classified into interest-rate bonds, credit bonds, convertible bonds and high-yield bonds according to the underlying investment target, with a lower proportion as a whole in privately offered funds. Due to the existence of privately offered fund performance compensation accrual, bond strategy can attract investors unless it brings significantly better returns than the public offering. Therefore, convertible bonds, low- and medium-grade credit bonds, and high-yield bonds have gotten attention from investors and some investment institutions.

3.6. Arbitrage Strategy

As a low-volatility and robust product, it helps acquire spread benefits while reducing price risk by capturing the trading opportunities of transient price deviations of different assets in the market based on the principle of spread reversion. It can be generally classified into statistical arbitrage (term arbitrage, cross-period arbitrage, and cross-market/cross-species arbitrage), pricing arbitrage (option volatility arbitrage, ETF/LOF arbitrage, convertible/interchangeable bond arbitrage, and option/futures/spot arbitrage), and event-driven arbitrage (fixed growth arbitrage, and block arbitrage).

4. Discussion about the macro environment suitable for the segmentation strategy of the privately offered fund

4.1. Macroeconomic environment

It refers to the overall economic performance of a country or region, including GDP growth rate, inflation rate, unemployment rate, and other data, which reflect the effect of macroeconomic policies and the changes in market supply and demand. Therefore, the macroeconomic environment is one of the important factors for the evaluation system of privately offered fund segmentation strategy. Specifically, its impact on the privately offered fund is mainly reflected in the following aspects: first, it affects the level of investment return; second, it affects the competitive pattern of the industry; third, it affects the financing capability of enterprises; fourth, it affects the risk appetite adjustment of investors. In practical application, we can determine the scopes of investment targets suitable for different types of privately offered fund segmentation strategies by analyzing the macroeconomic environment. For example, if the macroeconomic environment is in a stable growth period, it’s advisable to increase investment in growth enterprises; on the contrary, if the macroeconomic environment is in recession, it’s necessary to pay more attention to robust investment projects. In addition, the macroeconomic environment directly affects some key indicators in the evaluation system of privately offered fund segmentation strategy, such as enterprise profitability, and cash flow.

4.2. Economic cycle

There have different investment demands and market performances in different stages of the economic cycle. During the expansion period, investors tend to choose products with high returns due to the overall upward trend of the market. At this stage, it is advisable to appropriately increase the proportion of investment in growth stocks while reducing investment in robust products in a privately offered fund. In addition, it is a good time to identify more high-quality investment targets by improving the research team’s competence. However, during the economic contraction period, investors will be affected in their risk tolerance by the noticeable market volatility. At this stage, it is necessary to adopt a more conservative investment strategy and avoid excessive risk-taking in a privately offered fund. Specifically, allocating funds to some relatively stable areas such as fixed-income products or defensive industries should be considered. In addition, investing more in cash management to deal with unforeseen events should be considered. Above all, it is wise to choose different allocation strategies for privately offered funds in different economic cycles.

4.3. Financial market environment

The development level of the capital market is closely related to the investment demands for privately offered funds. With the continuous development of the domestic economy, the capital market is also gradually improving and developing. Moreover, changes in financial regulatory policies also directly affect the investment behaviors of privately offered funds. For example, to encourage innovation and start-ups, the government has introduced a series of corporate investment programs and tax incentives in recent years, which have provided privately offered funds with more opportunities and space to conduct business. In addition, the risk status of the financial market is also an important factor to be considered. Although China's financial market faces relatively low risks, uncertainties still exist due to changes in the macro-economy at home and abroad. In summary, the financial market environment plays a vital role in the operation of privately offered funds.

4.4. Technical environment

First, the Internet financial technology used in the privately offered fund industry has become mainstream. As mobile payment, third-party payment, and other newly developing businesses are emerging, Internet financial technology has been widely used in the privately offered fund industry. Meanwhile, with Internet financial technology upgrading, blockchain technology and artificial intelligence technology have gradually penetrated various fields of the private equity industry. Second, big data analysis technology is also critical for this industry. With the improvement in data volume and computing power, this technology is becoming a necessary skill for the private industry. Privately offered fund managers can accurately grasp market trends and risk factors by analyzing huge amounts of data with this technology, thus making more informed investment decisions. Finally, it is essential to deal with changes in investor demands and market risk. With the increasing volatility and uncertainty in the financial market, investors have increased their risk awareness. Therefore, privately offered fund managers need to take appropriate countermeasures for these changes to ensure the stability and safety of their products.

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