

## Convertible Hedging: What's Going On?

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Hedge funds dominated the headlines in May, with special attention devoted to losses within the convertible hedging community. The press was particularly focused on “the GM trade”: buy the undervalued debt, short the overvalued equity. This trade lost on both sides as the debt was downgraded to junk status and Kirk Kerkorian, a major shareholder, offered to increase his equity stake in the company from about 4% to over 8%. Certain large hedge funds became forced sellers as they scrambled to control losses, which led to anxieties about the brokers that lend to hedge funds; those anxieties led to broader worries about the credit derivatives market. By late May the level of media hysteria had subsided somewhat, which makes this a good time for taking a closer look at some issues ignored in the media frenzy...