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Hedgebay debuts tool to value fund "side pockets"

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* Service designed to boost trade in illiquid assets

* Ten percent of hedge funds still have side pockets

* Current side pockets could take 2-3 yrs to wind down

By Nia Williams

LONDON, Dec 20 (Reuters) - Hedgebay, a secondary market for hedge fund stakes, has launched a tool to help investors value the billions of dollars worth of illiquid assets still held in opaque "side pocket" portfolios left over from the credit crisis.

An estimated 10 percent of funds in the $1.8 trillion hedge fund industry still have so-called side pockets, according to Hedgebay co-founder Elias Tueta, referring to separate portfolios created by hedge funds during the crisis to house hard-to-shift assets.

Tueta said a more transparent pricing system could help boost trade in these assets.

"More informed investors will be more willing to trade and as a result create a deeper and more liquid market," he said in an interview on Monday.

The most illiquid assets include certain emerging market bonds, secondary real estate, pre-IPO securities and private convertible bonds -- representing billions of dollars of investors' money that cannot be touched.

At the height of the crisis, when buyers for many assets disappeared and investors started demanding their money back, hedge funds created side pockets that could be wound down separately to stop clients who redeemed later from being left with the hard-to-sell assets.

Investors pulled out a net $330 billion from hedge funds in the year to June 2009, according to Hedge Fund Research.

Tueta said Hedgebay's valuation method is a market-based model that uses data about transactions that have already taken place to assess an individual investor's portfolio, while analysts poll funds to check how much they would be willing to pay for certain assets.

Customers so far have included auditors, fund managers and banks, and last year's improving hedge fund returns of 18.6 percent suggest a pick up in risk appetite among certain investors.

"A number of specialist funds have decided there's an opportunity in these illiquid assets for people who are patient, who can wait for prices to come back. They have capital and have made their own assessments of what shares are worth," Tueta said.

But slowing activity in November, with assets sold at an average of 74 percent NAV, down from 80.16 percent in October according to the Hedgebay Index, means investors could have to wait until 2013 before getting cash back from assets currently locked in side pockets.

"In the next two or three years present side pockets are going to be liquified or taken down to zero but new illiquid assets will appear in the meantime," said Tueta.

"Every month a little bit of the side pocket disappears, distributing cash to the holders. But obviously what remains in the side pocket is a little bit less liquid." (Editing by Laurence Fletcher and Jon Loades-Carter)