



UNRAVELING THE COMPLEXITY:

exploring the dynamics and implications of hedge funds in the financial landscape

DESVENDANDO A COMPLEXIDADE:

explorando a dinâmica e implicações dos *hedge funds* no cenário financeiro

DESCIFRANDO LA COMPLEJIDAD:

explorando la dinámica e implicaciones de los fondos de cobertura en el panorama financiero

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ABSTRACT

The objective of this article is to provide a historical contextualization of the emergence and institutionalization of a financial investment structure called hedge funds. Incipient, even in the debate of international sociology of finance, this object is, in practical terms, the representation and consolidation of what is considered one of the forefronts of investment and risk. The article consists of two sections. The first section presents the context and emergence of hedge funds in the United States and how it was adapted to the Brazilian context. The second section, based on the analysis of normative devices, presents the distinctive dimensions in relation to traditional investment funds. Through documentary research, particularly manuals, regulations, and legislation from the United States and Brazil regarding hedge funds, as well as specialized media sources (Valor, The Economist, Time), and in-depth interviews with market operators in Brazil, the unique dimensions of hedge funds were traced, mapped, and evaluated. These dimensions include freedom, transparency, objectivity, and low tolerance for losses. The article contributes to the understanding of the operational dynamics of hedge funds, their key dimensions, and helps disseminate a distinct ethos within the Brazilian financial space.

Key words: Hedge fund; Sociology of finance; History of Brazilian finance.

RESUMO

O objetivo deste artigo é fornecer uma contextualização histórica do surgimento e institucionalização de uma estrutura de investimento financeiro chamada *hedge funds*. Incipiente, mesmo no debate da sociologia internacional das finanças, esse objeto é, em termos práticos, a representação e consolidação do que é considerado uma das vanguardas do investimento e risco. O artigo é composto por duas seções. A primeira seção apresenta o contexto e o surgimento dos *hedge funds* nos Estados Unidos e como eles foram adaptados ao contexto brasileiro. A segunda seção, com base na análise de dispositivos normativos, apresenta as dimensões distintivas em relação aos fundos de investimento tradicionais. Por meio de pesquisa documental, especialmente manuais, regulamentos

e legislação dos Estados Unidos e do Brasil relacionados aos *hedge funds*, bem como fontes de mídia especializada (Valor, The Economist, Time) e entrevistas aprofundadas com operadores de mercado no Brasil, as dimensões únicas dos hedge funds foram traçadas, mapeadas e avaliadas. Essas dimensões incluem liberdade, transparência, objetividade e baixa tolerância a perdas. O artigo contribui para a compreensão da dinâmica operacional dos *hedge funds*, suas dimensões-chave e ajuda a disseminar um ethos distinto dentro do espaço financeiro brasileiro.

Palavras-chave: Hedge fund; Sociologia das finanças; História das finanças brasileiras.

RESUMEN

El objetivo de este artículo es proporcionar una contextualización histórica del surgimiento y la institucionalización de una estructura de inversión financiera llamada hedge funds. Aunque incipiente en el debate de la sociología internacional de las finanzas, este objeto es, en términos prácticos, la representación y consolidación de lo que se considera uno de los frentes de vanguardia en inversión y riesgo. El artículo consta de dos secciones. La primera sección presenta el contexto y surgimiento de los hedge funds en Estados Unidos y cómo se adaptaron al contexto brasileño. La segunda sección, basada en el análisis de dispositivos normativos, presenta las dimensiones distintivas en relación con los fondos de inversión tradicionales. A través de una investigación documental, especialmente manuales, regulaciones y legislación de Estados Unidos y Brasil relacionadas con los hedge funds, así como fuentes especializadas de medios de comunicación (Valor, The Economist, Time) y entrevistas en profundidad con operadores del mercado en Brasil, se trazaron, mapearon y evaluaron las dimensiones únicas de los hedge funds. Estas dimensiones incluyen libertad, transparencia, objetividad y baja tolerancia a las pérdidas. El artículo contribuye a la comprensión de la dinámica operativa de los hedge funds, sus dimensiones clave y ayuda a difundir un ethos distintivo dentro del espacio financiero brasileño.

Palabras clave: Hedge fund; Sociología de las finanzas; Historia de las finanzas brasileñas.

INTRODUCTION

The aim of this article is to provide a preliminary assessment of a research agenda within the field of Brazilian sociology of finance. Specifically, the article introduces a new object of study: the Brazilian hedge funds. Despite being incipient, even in the international socio-anthropological debate (NEELY, 2022), these funds take a growing importance in the global financial markets, with a representation of a not-so-new investment structure within the financial-economic space. Alongside venture capital funds, private equity funds, and hedge fund-of-funds, they are considered cutting-edge opportunities for high-risk investments, establishing themselves as alternatives to traditional investments.

The family of hedge funds belongs to the category of alternative and innovative funds, characterized by significant operational freedom and strong managerial involvement. The elements that compose the distinctive traits of this fund family are diverse, present in some and absent in others. For example, two globally renowned funds, the Quantum Hedge Fund, established in 1973 by Hungarian investor George Soros, operates with a highly distinct portfolio compared to Bridgewater, created in 1975 by the American mega-investor Raymond Thomas Dalio.

The investment approach of the Quantum Fund is grounded in macroeconomic analysis and a global investment strategy. George Soros is known for his "trend investing" strategies, which involve identifying opportunities in global financial markets based on his perspectives on macroeconomic and geopolitical forces. The Quantum Fund was one of the early adopters of the "macro investment" strategy and gained recognition for its successful bet against the British pound in 1992, famously known as "Black Wednesday."

On the other hand, the investment strategy of Bridgewater is based on decision-making principles grounded in economic principles. The company is known for its systematic approach and clear rules for investment decisions. Bridgewater offers various investment strategies, including long-term and short-term strategies.

Although both Bridgewater Associates and the Quantum Fund have macro investment strategies, there are differences in how they approach and implement these strategies. Bridgewater is known for its systematic approach based on rules and economic principles, while the Quantum Fund is known for George Soros' more discretionary approach, which is influenced by his views and interpretations of macroeconomic forces.

Furthermore, the literature of finance (LIMA, LOPES, 1998, 1999; GIAMBIAGI, GARCIA, 2010; AALI-BUJARI, VENEGAS-MARTÍNEZ, PÉREZ-LECHUGA, 2016; YADAV, & MISHRA, 2017) lacks a consistent and uniform definition or conceptualization of hedge funds. However, there are a series of characteristics that are unique to hedge funds and distinguish them from other collective investment structures, allowing for their identification.

As presented in Bichoffe (2023), one justification for studying this object lies in the rapid accumulation of net assets in this specific type of fund compared to the total investment fund market. According to data from the Brazilian Association of Financial and Capital Market Entities, from 1994 to 2014, the assets of Brazilian funds increased from R\$ 232 billion to R\$ 2.686 billion, representing a growth of 1,054% (ANBIMA, 2014), and the number of institutions increased from 632 in December 1993 to 14,097 in December 2013, a growth of 2,131%. In recent research conducted on the Anbima website, were identified 16,742 registered funds, representing an increase of approximately 19%. Those statistics and information on this segment in Brazil are reliable because, as we will see, all investment funds, regardless of their strategy or classification, are supervised and report their net asset values uniformly and periodically to Brazilian authorities.

Hedge funds are private investment funds that aim to generate high returns for their investors by employing more complex and diversified investment strategies than traditional investment funds. Although there are various types of hedge funds, they generally seek to profit

regardless of market conditions through strategies such as arbitrage, leverage, derivative trading, and short positions.

Understanding the functioning of this type of instrument and its integration into the national financial space provides a promising entry point to identify how new mechanisms of wealth accumulation unfold within the realm of elites. Particularly, hedge funds tend to primarily benefit wealthy investors, especially in Brazil, where due to minimum financial and legal investment requirements that are accessible only to accredited investors. Furthermore, certain hedge fund strategies, such as derivative trading and short positions, can increase the volatility of financial markets, as some of these strategies may capitalize on financial crises or economic shocks, further amplifying socioeconomic disparities. Additionally, specific funds may specialize, for example, in hostile takeovers and corporate restructurings, resulting in mass layoffs and job losses¹.

As Hardie and Mackenzie (2007) pointed out, a preliminar question for any discipline that studies financial markets is how we should theorise actors and action in those markets. The analytical framework guiding this article is Michel Callon's anthropology of economics and economies approach (CALLON, 1998). Suported by this approach, this work explores a theoretical framework that combines anthropological perspectives with economic analysis to understand the social and cultural dimensions of economic activities. Callon argues that economic phenomena cannot be reduced solely to market mechanisms but must be examined within broader social contexts. His approach emphasizes the role of networks, relationships, and power dynamics in shaping economic behaviors and outcomes. Callon's work highlights the interplay between actors, but, fundamentally in devices, like technologies, standards, norms

¹ During interviews conducted between 2020 and 2021 with Brazilian analysts and hedge fund managers, we identified arguments in defense of this type of instrument. They argued, for example, that hedge funds play an important role in financial markets by providing liquidity, enhancing market efficiency, and facilitating price discovery. They also highlight that hedge funds can offer long-term investment opportunities involving risks and help drive economic growth. Advocates of hedge funds contend that these funds contribute to market liquidity by actively trading and participating in various financial instruments, thereby enhancing overall market efficiency. They argue that the presence of hedge funds can lead to more accurate price formation as they engage in rigorous research and analysis to identify mispriced securities. By capitalizing on market inefficiencies, hedge funds can potentially generate profits and contribute to a more efficient allocation of capital. Additionally, proponents argue that hedge funds can provide opportunities for long-term investment strategies that involve taking calculated risks. By actively managing portfolios and employing sophisticated investment techniques, hedge funds may achieve higher returns compared to traditional investment vehicles. This potential for attractive returns can attract capital and stimulate investment, which in turn can contribute to economic growth. It is important to note that these arguments put forth in defense of hedge funds represent the perspectives of industry professionals and should be understood within the context of ongoing debates surrounding the benefits and drawbacks of these investment vehicles. Critics raise concerns about potential market manipulation, systemic risks, and the exacerbation of income inequality. Evaluating the overall impact and role of hedge funds requires a comprehensive analysis of their practices, regulations, and their effects on financial markets and society as a whole.

and institutions in the construction and transformation of economic systems, providing valuable insights into the complex and multifaceted nature of financial processes.

The aim of this article is to present, albeit briefly, elements of distinction that characterize and differentiate the structure of hedge trading, focusing on norms and standards that have shaped the social space of hedge funds. Based on extensive documentary research, particularly manuals, regulations, and legislation on hedge funds, as well as news from specialized media sources (such as *Valor*, *The Economist*, and *Time*), and in-depth interviews with market operators in Brazil, categories deemed familiar to hedge funds were traced and mapped according to the perception of economic agents (investors, banks, analysts, traditional funds, journalists, other hedge funds, and government agencies). These categories, as been explored forward, include freedom, low tolerance for losses, transparency, and objectivity.

Thus, the article is structured into five sections. The first section is the present introduction, which provides a concise presentation of the object and justification for the study. The second section offers a brief conceptualization of this type of fund. The third section subsequently conducts an exegesis of hedge funds, reconstructing a chronology of these instruments that originated in the United States and reached Brazil in the 1990s. The following section presents a panoramic overview of the hedge fund industry, with special attention to the regulatory peculiarities in the Brazilian context. This section aims describe the institutional and standards settings of the fund's trading, the assets it trades, and the arrangements that make it possible for a small number of people to engage in global trading. In the concluding remarks, we aim to explore the potential for an interdisciplinary interface between the sociology of finance, sociology of critical capabilities, and the study of elites. Our proposal is to undertake a comprehensive mapping, classification, and analysis of the actors involved in this process and the trajectories they navigate in the task of institutionalization. By examining the evolution of hedge funds over time within the context of contemporary international finance, which is characterized as a volatile, uncontrollable, and high-risk market, we seek to shed light on the intricate dynamics that shape and reshape the financial landscape. This sociological perspective allows us to critically examine the power dynamics, social structures, and systemic implications inherent in the development and proliferation of hedge funds, ultimately contributing to a deeper understanding of the complexities and social implications of financial practices.

DEFINING HEDGE

A starting point is the understanding that hedge primarily refers to a type of coverage against fluctuating prices. In practice, it is an investment for protection, a form of insurance, aimed at reducing the risk of adverse price movements in a particular asset (Yadav, Mishra, 2017). Typically, hedging involves taking a compensatory position in a related security, such as a futures contract, in an attempt to neutralize losses.² In their dynamics, these transactions involve an intricate orchestration of layers and sub-levels of valuations and exchanges that become increasingly complex. This tangled web of levels produces what is known as "secondary markets," which are sustained by a delicate balance.

These transactions can also be conceptualized as interconnected units, operating with varying degrees of autonomy. However, they exhibit a remarkable sensitivity and possess an incredible capacity for propagation when even minor fluctuations impact them. This intricate network of products and instruments traded across market layers is referred to as "derivatives" precisely because their buying and selling prices derive from an index, a rate, or even the price of another asset, known as the underlying asset³. A range of tools and products are traded in this chain of secondary markets, derived from transactions in the primary layer. Examples include the swap market, such as credit default swaps (products that allow financial institutions to transfer the risk of borrower default) and, therefore, related to credit default. Another example is weather derivatives, which are linked to specific weather conditions. These instruments enable market participants to strategically manage risk by providing protection or engaging in speculation against adverse or unexpected weather conditions. Weather derivatives allow for the transfer of weather-related risks, providing a means for hedging or profiting from adverse or unexpected weather conditions⁴.

Hedge operations, therefore, comprise a web of trading cores, connecting a heterogeneous set of institutions such as funds, companies, banks, asset managers, brokers, and administrators. These institutional actors operate a variety of instruments and apply them to achieve objectives ranging from hedging (protection), risk management, portfolio diversification, to speculation.

² A perfect hedge is one that eliminates all risks in a position or portfolio. In other words, the hedge is 100% inversely correlated with the vulnerable asset. This is obviously an idealization because it is impossible, even with the most sophisticated financial algorithms, to predict all impactful variables and hedge them in all possible scenarios. And perhaps, even if such an approach existed, the costs of this hypothetical perfect hedge would be impractical.

³ Derivative markets are a relatively young American creation and are closely intertwined with risk and debt markets (AALI-BUJARI; VENEGAS-MARTÍNEZ; PÉREZ-LECHUGA, 2016).

⁴ They gained prominence around 1996 in the USA as a risk management strategy for both commodity producers and buyers.

Brief Chronology of Hedge Funds

The practice of creating hedging strategies against price fluctuations and loss risks emerged even before the term itself was coined. The search for protection can be traced back to records of transactions in the late 18th and 19th centuries in the United States, as documented in historiographical research (OLEGÁRIO, 2006; PINEDA, 2012; POON, 2012). These early instances of hedging were primarily associated with agricultural credit issues and industrial expansion. However, interesting but relatively unexplored evidence found in the work of Olegário (2006) and Pineda (2012) also reveals that by the 19th century, transactions related to hedging were present, but more closely associated with speculative practices and arbitrage involving leveraging with "derivatives." These practices had already diverged from their initial purpose of providing protection to farmers and rural landowners or credit to industrial entrepreneurs.

The Wall Street crash of 1929 and the subsequent Great Depression prompted the U.S. government to establish the U.S. Investment Company Act of 1940, a law that made it illegal for investment companies to engage in short selling, which involves leveraging by selling securities one does not own. An example of this type of transaction is borrowing securities with the hope of repurchasing them at a lower price later, or buying securities with borrowed funds. The regulations implemented in the 1940s mandated that any economic actor in the U.S. wishing to engage in short selling or leverage had to structure themselves in a way that would not classify them as an "investment company" under the Act (BICHOFFE, 2018).⁵

Indeed, it is within this environment that hedge funds emerged as an organizational structure designed to maneuver the regulatory requirements imposed on banks and traditional funds. Hedge funds can be understood as collective investment vehicles that are privately organized and managed by professional managers, and they are not openly available to the general public (JAEGER, 2003).

⁵ The interview books by American trader and writer Jack Schwager are considered important references for those interested in the opaque universe of the financial market. In "The New Market Wizards: Conversations with America's Top Traders" (1992) and "Hedge Fund Market Wizards: How Winning Traders Win" (2012), Schwager engages in conversations with established names in the financial space, exploring their career stories, investment strategies, and significant moments in the field. Of particular interest is a version, apparently crystallized among traders, regarding the origin of the term "Hedge Fund," which was first publicly used by Carol J. Loomis in an article titled "The Jones Nobody Keeps Up With" in Fortune magazine in 1966. It referred to the investment strategy adopted by Alfred W. Jones, who bought undervalued stocks and, to protect against market risks, sold overvalued stocks short. The protection, referred to as a "hedge" in English, is said to have inspired the name of these funds. This established version is often repeated by actors in the field, almost like a legend.

In general terms, hedge funds were born as a means to ensure that the capabilities of financial actors were not restricted by the U.S. Investment Company Act and its counterparts in other countries. Based on the historiography retrieved from the literature review (LOWENSTEIN, 2000; OLEGÁRIO, 2006; SCHWAGER, 1992, 2012; HARDIE, MACKENZIE, 2007; MALLABY, 2010; MURRAY, SCOTT, 2012; PINEDA, 2012; POON, 2012), this article proposes summarized the history of hedge funds into three distinct periods.

The first period originated in the 1940s with the emergence of the initial transaction structure and lasted until the onset of the first major crisis in the 1970s. During this time, hedge funds began to establish themselves as alternative investment vehicles.

The second period, which emerged in the 1980s, marked a resurgence and increased utilization of hedge fund structures. This period witnessed significant growth and expansion, driven by technological and computational advancements, with the internet speeding up and transforming the ways of trading - leading up to the global financial crisis of 2008. It was also during this phase that the structure of hedge funds gained traction in Brazil, finding its way into the local financial landscape. The third period commenced in 2010, as the hedge fund market regained its momentum and rebounded to pre-crisis levels of trading activity and capital. This period solidified hedge funds as one of the most prominent segments within the global financial markets, a status they continue to hold to the present day.

The detailed reconstruction of these chronology is not the primary objective of this article. However, it is pertinent to note that the first hedge fund widely recognized as such was A.W. Jones and Company, established in 1949 by Winslow Jones. Jones's pioneering concept revolved around the appropriate combination of two speculative techniques: long and short strategies, augmented by leverage. The objective was to effectively manage and mitigate overall portfolio risk while constructing a conventional portfolio with minimal exposure, yet still exhibiting correlation with the broader market performance. This approach involved the utilization of speculative instruments for conservative purposes, thereby challenging conventional notions of risk management within investment strategies.

One of the innovative elements propagated by this architecture was the combination of two instruments: leverage and short selling. This functioned as follows: a portion of the fund's portfolio was invested in stocks that had the potential to appreciate over time, with leverage employed to increase the possibilities of gains. Simultaneously, short selling was executed for other stocks, which could eventually depreciate over time (LANDAU, 1968).

Thus, by engaging in both long and short positions, whereby purchasing certain securities while simultaneously promising to sell them in the future, investors could mitigate

risks and isolate themselves from the volatile movements of the overall market. Additionally, Jones had two other key ideas: first, to invest all his savings alongside the investors in the fund he managed, and second, to secure a profit of approximately 20 percent of the overall returns generated by the fund. Through this audacious approach, Jones successfully aligned the interests of the investors and fund administrators ⁶(HARDIE, MACKENZIE, 2007; YADAV, MISHRA, 2017), By adopting such a strategy, Jones aimed to reduce what is known in the field of finance as "moral hazard," which refers to minimizing the exposure of the investor or fund manager to unnecessary risks. Through this approach, both the investor and the fund manager would share in the gains as well as the losses, thereby aligning their incentives and mitigating the potential for adverse risk-taking behavior.

Based on Jones's practices, hedge funds began to gain popularity in the United States during the 1960s and 1970s. Essentially, these were limited partnerships engaged in statistical arbitrage operations, commonly known as "long and short" strategies. Due to their distinct structure, they operated outside the regulatory purview of conventional mutual funds, allowing them greater flexibility and autonomy in their investment activities.

The international crises of the 1970s, particularly the oil crisis of 1973-74, shook the financial markets and led to the downfall of many small hedge firms. However, according to information available on the website of the Federal Reserve (2022), the central bank of the United States, the number of hedge funds has been rapidly growing in recent decades. In 1993, the American industry managed around \$50 billion in assets, which surged to \$600 billion by 2003. As of 2021, this figure has exceeded the \$1.5 trillion mark, distributed among more than 8,000 funds classified in this category. Although the total number of funds and assets under management is lower compared to the mutual fund industry (\$2.106 trillion), their growth highlights their significance as an investment alternative. Globally, in 2021, the top 250 hedge funds collectively held \$3.88 trillion in assets (HEDGELIST, 2021).

The rapid rise of hedge funds is closely linked to the derivatives market, which has significantly expanded in the past two decades, not only in terms of volume but also in terms of flexibility and the variety of available financial instruments. To provide an indication of the scale of this market, in 2011, the Bank for International Settlements (BIS) released data for the year 2008 on the global volume of derivatives, which amounted to approximately \$592 trillion.

⁶ This structure remains in place today, including in Brazil. The performance fee serves as a positive incentive, encouraging the pursuit of results. The investment made by the fund manager in their own fund has the effect of aligning the incentives of the manager and the client, thereby reducing moral hazard in this fiduciary relationship. Additionally, an attractive performance fee serves as an excellent draw for qualified and motivated professionals and may provide sufficient reward for managers to assume the risks associated with the endeavor.

This value is significantly higher than the gross domestic product (GDP) of the United States, the world's largest economy, which at that time stood at just over \$13.8 trillion. Derivatives contracts increased more than sevenfold between 1998 and 2014 (AALI-BUJARI, 2016).

In 2016, Brazil gained a box for the first time within the Triennial Survey report produced by the Bank for International Settlements (BIS) on derivatives. This highlights the growing significance of the derivatives market in Brazil and its inclusion in international research and analysis.⁷.

The inclusion of data about Brazil in the BIS Triennial Survey report reflects the acknowledgment of a relatively large and well-developed derivatives market compared to other emerging countries. "The Brazilian derivatives market stands out for its depth and high level of development, demonstrating innovation and resilience even in times of financial stress" (BIS, 2016). This robustness of the derivatives market in Brazil can be seen as a contradiction in relation to the country's economic development.

Despite the economic challenges and financial fluctuations faced by the nation, this sociotechnical arrangement (HARDIE, MACKENZIE, 2007), denominated derivatives market, has remained strong and efficient, offering opportunities for hedging, speculation, and portfolio diversification for market participants. This ability to withstand and overcome adversities can be attributed, in part, to the specific characteristics and regulations of the Brazilian derivatives market, as well as the active participation of financial institutions and investors that contribute to its robustness and resilience.

In the face of the widespread of a cultural perception of brazilian economic instability and insecurity (GRÜN, 2007, 2013) there has been a significant surge in demand for risk hedging instruments, leading to the development of a robust derivatives market. This market has aimed to effectively address not only the challenges posed by inflationary pressures but also the subsequent volatility of interest rates and exchange rates. As highlighted by Goede (2004), risks represent an inexhaustible source of demands. This suggests that the possibilities for creating markets in risk management products are limitless and potentially highly profitable. Such markets encompass a wide range of risks, including currency fluctuations, and even extend to safeguarding against or speculating on various imaginable risks, such as unpredictable weather patterns or election outcomes.

⁷ The BIS (Bank for International Settlements) is tasked with ensuring monetary and financial stability in the International Financial System. It fulfills this role by establishing regulations, fostering cooperation, and promoting integration among its member central banks. Often referred to as the "central bank of central banks," the BIS plays a vital role in maintaining stability and facilitating collaboration in the global financial landscape.

The significant international growth over the past three decades, and in the case of Brazil, the expectations of gains appear to be much more appealing to market participants in the first instance, despite the risks that lie ahead. This has even prompted major investment banks to establish hedge fund units. To a large extent, this development has been made possible due to deregulation, as will be further discussed in the following.

Singularities of Hedge Practice

Both the literature (LIMA, LOPES, 1998, 1999; GIAMBIAGI, GARCIA, 2010; AALI-BUJARI, VENEGAS-MARTÍNEZ, PÉREZ-LECHUGA, 2016; YADAV, & MISHRA, 2017) and exploratory interviews conducted with hedge fund operators indicate that investment collectives exclusively engaged in hedge practices exhibit certain singularities that differentiate them from other entities operating in financial markets. These singularities can be classified into three dimensions: freedom, transparency and objectivity, and low tolerance for losses. The first dimension, freedom, emerges as highly valued and emphasized in both documentary research and field investigations, as it is considered the foundation upon which hedge fund operations are structured. The propagated freedom is operationalized in the following ways: i) through the absence of legal restrictions on the use of instruments such as leverage and short selling; ii) the flexibility to manage their cash position; iii) engaging in futures market transactions; iv) buying and selling exotic derivatives; v) swiftly entering and exiting positions.

This notion of freedom permeates the activities of hedge funds, empowering them to navigate financial markets with a wide range of strategies and instruments. Such flexibility allows them to respond promptly to market dynamics and seize profitable opportunities. Moreover, the absence of legal constraints provides them with the autonomy to employ innovative and sophisticated financial instruments. It is through this freedom that hedge funds differentiate themselves and cultivate their unique operational characteristics.

Furthermore, transparency and objectivity play essential roles in hedge fund operations. By maintaining transparent and objective practices, hedge funds aim to build trust with their stakeholders, including investors, regulators, and other market participants. This emphasis on transparency ensures that relevant information is disclosed accurately and timely, enabling stakeholders to assess and evaluate the fund's performance and risk profile. Objectivity serves as a guiding principle, shaping investment decisions based on rigorous analysis and risk management techniques, rather than emotional or subjective factors.

Additionally, hedge funds exhibit a low tolerance for losses, reflecting their focus on risk mitigation and capital preservation. This emphasis on minimizing losses is driven by the awareness of the potential impact of adverse market conditions and the need to safeguard investor capital. As a result, hedge funds employ rigorous risk management practices and closely monitor their portfolios to mitigate downside risks.

In summary, the literature and exploratory interviews highlight the singularities of hedge fund collectives, emphasizing freedom, transparency and objectivity, and a low tolerance for losses. These dimensions shape the operational characteristics and differentiate hedge funds from other entities in financial markets, allowing them to navigate complex financial landscapes with autonomy, transparency, and a strong focus on risk management.

The American financial system is internationally recognized as the least regulated, and this structure extends to hedge funds, which actually have even more flexibility than traditional funds. In the United States, for example, (RIACH, CUTCHER, 2014) there are not as stringent regulations as in Brazil for the operation of these financial entities. In the United States, organizations can qualify as hedge funds if they possess the following characteristics: i) limited liability firms; ii) flexibility in the movement of shareholders; iii) fewer than 500 investors; iv) they cannot make public offerings or engage in any form of advertising; v) fund managers are not necessarily required to demonstrate formal education or other technical competencies; vi) their investors must be knowledgeable about market dynamics and qualify as qualified institutional buyers (QIBs), meaning that funds are prohibited from accepting investments from the general public and are restricted only to certain categories of institutions and individuals (such as individuals whose net worth exceeds \$1,000,000) (YADAV, MISHRA, 2017). Due to the low level of regulation and oversight, there is no obligation, for example, to provide any type of report to financial authorities unless there is suspicion of fraud and the documents are officially requested.

In Brazil, the situation is different, where the operating conditions are much more regulated, and the oversight is more stringent (AALI-BUJARI, VENEGAS-MARTÍNEZ, PÉREZ-LECHUGA, 2016). One of the interviewees explains that these are "special" funds that are not regulated in the same way as conventional funds (such as mutual funds and pension funds). Another interviewee states that a hedge fund is something that, in a certain way, cannot even be considered a traditional "fund." It resembles much more a regular limited liability company with multiple partners. As he recalls, "In the United States, for example, a hedge fund is, in terms of social contract, a limited liability company (referred to as an 'LLC,' which would be the equivalent of an 'Ltda' in Brazil), and perhaps one of the few restrictions imposed by

financial authorities is that they cannot accept investors who are not 'accredited.' In Brazil, we would have qualified and highly qualified investors as equivalents to the 'accredited' investors."⁸. One of the main characteristics of funds that exclusively engage in hedge trading is the restriction on investor profiles, which involves the requirement of a minimum capital investment and registration with regulatory bodies. This restriction aims to ensure that only qualified and accredited investors participate in these funds.

By imposing such limitations, hedge funds seek to mitigate risks and protect the interests of investors. Qualified and accredited investors are individuals or entities that possess a certain level of financial knowledge, experience, and capital, which enables them to understand and bear the potential risks associated with hedge fund investments.

This selective approach to investor eligibility distinguishes hedge funds from conventional investment funds, such as mutual funds and pension funds, which typically have fewer restrictions on investor profiles. The rationale behind this differentiation lies in the complex and often sophisticated investment strategies employed by hedge funds, which may involve greater risks and require a more sophisticated understanding of the financial markets.

Moreover, the regulatory authorities impose these restrictions to ensure that hedge funds operate within a framework that safeguards the stability and integrity of the financial system. By limiting access to qualified and accredited investors, who are presumed to possess the necessary financial resources and expertise, regulators aim to mitigate potential systemic risks that may arise from the activities of hedge funds.

Therefore, the restriction on investor profiles, achieved through capital requirements and registration with regulatory bodies, stands as one of the key features of hedge funds that engage exclusively in hedge trading. This feature reinforces the specialized nature of hedge funds and their commitment to maintaining a higher level of scrutiny and control over their investor base.

⁸ The CVM (Securities and Exchange Commission of Brazil) considers the following investors as qualified: (i) financial institutions, (ii) insurance companies and capitalization societies, (iii) open and closed supplementary pension entities, (iv) individuals or legal entities that hold financial investments exceeding R\$ 300,000.00 (three hundred thousand Brazilian reais), (v) other investment funds exclusively intended for qualified investors, (vi) portfolio managers and securities consultants authorized by the CVM in relation to their own resources, or (vii) social security self-managed pension plans established by the Federal Government, states, the Federal District, or municipalities. In order for individuals who hold investments exceeding R\$ 300,000.00 to be qualified, they must also declare their intention to be classified as such to the CVM. There is also a second category of investors known as "super-qualified" in the financial market jargon. The changes brought by CVM Instruction No. 465, dated February 20, 2008, allowed for the identification of this special category, exclusively intended for investors who contribute a minimum amount of R\$ 1,000,000.00 (one million Brazilian reais) (GERMANOS, 2009).

The second aspect concerns a low tolerance for losses. This issue deserves careful consideration, as it is not only about the promise of above-average market returns, but primarily about avoiding loss and mitigating losses. This sentiment is strongly emphasized in the interviews. The pursuit is for balance, to the extent that one statement exemplifies this proposition: "If you compose your investment at 8-9% per year, you will be in a better position than investors whose results fluctuate, rise and fall, and who experience excellent periods and horrible losses in others. Losses will kill you. They ruin your capitalization rate, and portfolio composition is the magic of investment" (Interviewee 3).

The previous passage highlights the phenomenon of low tolerance for financial losses among investors. It emphasizes the significance of avoiding losses rather than solely seeking above-average returns. This attitude is closely examined within the context of investment decision-making. The text underscores the desire for stability and equilibrium in investment strategies, as opposed to volatile and unpredictable outcomes. The quote provided from Interviewee 3 exemplifies the notion that minimizing losses is paramount in preserving one's capital and achieving long-term investment success. It reflects a belief that losses can have a significant negative impact on an investor's overall financial standing and the composition of their investment portfolio.

In summary, the proposal of low tolerance for losses by hedge funds involves an attractive combination of two asymmetries (opposite performances in the markets). These asymmetries allow for a high capital composition per unit of risk and can be implemented through passive means. For example, a long-only equity investor can purchase put options to prevent their portfolio from declining when the market falls. However, in this case, the investor compromises their return. The idea of a hedge fund portfolio is not necessarily to pay for insurance, but to achieve these asymmetries through active risk management instead of paying for insurance that compromises returns.

Lastly, the third aspect, transparency, and objectivity, also appears frequently, especially in interviews and documentary research. This dimension is demonstrated through three fronts: i) discourse that does not conceal losses with profits from other sectors; ii) a close contact approach with investors; iii) issuing reports to investors more frequently than investment banks and traditional funds.

It is worth highlighting that Brazil is at the forefront of embracing Corporate Governance (GRÜN, 2003, 2004a, 2004b, 2007, 2013) and financial prudence standards, including the Basel norms implemented by the Central Bank and CVM. These regulations have played a pivotal role in enhancing the calculation of financial risk within financial institutions

(BICHOFFE, 2018; CAVENAGHI, 2018). As a result, Brazil has established itself as a leader in adopting these standards, fostering improved risk assessment practices and ensuring greater stability in the financial sector⁹. As a consequence, there exists a well-defined set of regulations that govern and monitor funds within the country. These regulations serve as a framework for ensuring transparency, accountability, and responsible behavior in the operations and management of funds. They provide guidelines and requirements that funds must adhere to, encompassing aspects such as reporting obligations, risk management practices, investor protection measures, and compliance with relevant legal and regulatory frameworks. The presence of these established norms contributes to the overall integrity and stability of the fund industry, instilling confidence among investors and promoting a fair and orderly market environment.

Two regulations deserve highlighting. The first one is that in Brazil, it is not possible to use a regular limited liability company ("Ltda") as a vehicle for publicly open investments, even if it is targeting qualified investors. Instruction 555 issued by CVM in 2014 explicitly states that the only way to establish an investment fund in Brazil is through a "real" fund, such as a mutual fund, multimarket fund, pension fund, or a structured fund (such as real estate funds or equity funds). Specifically for hedge funds, the regulations specify that they must fall under the category of multimarket funds (Article 97 of ICVM 409), adhering to the comprehensive set of guidelines that govern, regulate, and supervise them. These regulations ensure that investment funds operate within a well-defined framework, promoting transparency, accountability, and investor protection in the Brazilian financial market.

The second regulation pertains to the requirements for fund managers to operate investment funds. These individuals are highly specialized in portfolio management activities. The Brazilian Securities and Exchange Commission (Comissão de Valores Mobiliários, CVM) establishes strict criteria for the education and experience of these professionals, including the requirement of certifications obtained through examinations conducted by the Brazilian

⁹ In the specific case of Brazil, the implementation of Basel II guidelines began in 2007. A work schedule between 2008 and 2012 involved stages such as the preparation of the technical staff of the Central Bank, the creation and establishment of norms, and a period of adaptation for financial institutions operating in the domestic markets. Even before the completion of the incorporation of the second agreement, the international financial crisis demanded a new commitment. In December 2010, two documents were published - Basel II: A global regulatory framework for more resilient banks and banking systems, and Basel III: International framework for liquidity risk measurement, standards, and monitoring, known as Basel III. These documents establish norms to strengthen the ability of financial institutions to absorb shocks from the financial system itself or other sectors of the economy, reducing the risk of financial crises affecting the real economy. Just like in previous agreements, the Central Bank of Brazil initiated a work cycle in 2013, which concluded in 2019, to incorporate emerging categories in the field and operationalize them through internal and external norms and rules.

Association of Financial and Capital Market Entities (Associação Brasileira das Entidades dos Mercados Financeiro e de Capitais, Anbima).

These criteria ensure that fund managers possess the necessary qualifications and expertise to effectively manage investment portfolios. The rigorous requirements set by the CVM and Anbima aim to safeguard the interests of investors and promote professionalism and competence in the field of portfolio management. By demanding specific educational backgrounds and certifications, these regulations contribute to maintaining high standards of quality and professionalism within the investment industry in Brazil.

An element that deserves more emphasis is the establishment of relationships between fund agents and their investors¹⁰. This is because the target audience consists of unique and highly demanding individuals who possess at least a basic understanding of financial instruments and strategies. Through documentary research, it has been observed that hedge fund investors, like fund managers, are required to hold an Investment Specialist credential registered with the Brazilian Association of Financial and Capital Market Entities (Associação Brasileira das Entidades dos Mercados Financeiro e de Capitais, Anbima). This certificate is mandated by the CVM for Qualified and Superqualified Investors.

Of particular interest is the category of "superqualified" investors. According to the changes introduced by CVM Instruction No. 465, issued on February 20, 2008, this group of individual investors received a specific identification and a special category for operating within the hedge fund structure. This is because it refers to investors who invest a minimum amount of R\$ 1,000,000. These funds targeting this limited, superqualified audience are exempt from the asset concentration rules that other Investment Funds must comply with.

This distinction highlights the unique nature of hedge fund investment and recognizes the sophistication and financial capacity of these superqualified investors. The relaxed regulations for these funds acknowledge the level of expertise and risk tolerance of this particular investor category.

In addition, funds targeting superqualified investors are allowed to allocate their entire portfolio to investments of any type abroad, as long as they are financial assets. This level of freedom is exceptional when considering that even Multimarket Funds can only invest up to 20% of their portfolio in authorized foreign financial assets, while other funds operating within the system are restricted to a maximum of 10%. Furthermore, superqualified investors enjoy an additional benefit, as the wording of the regulation allows for an interpretation of the definition

¹⁰ Investors in hedge funds often judge them on their performance month-to-month, especially in the case of a relatively new fund.

of "financial assets" that potentially overcomes any restrictive barriers imposed by a narrow definition. In practice, this understanding permits fund managers to invest in any type of instrument abroad, including non-standardized derivatives, providing them with full asset mobility (GERMANOS, 2009).

CONCLUSION

In conclusion, this article provides a preliminary assessment of the field of Brazilian sociology of finance, focusing on the emergence and characteristics of Brazilian hedge funds. These funds, along with other innovative investment structures, have gained importance in global financial markets and offer high-risk investment opportunities as alternatives to traditional investments. The article examines the distinct traits of hedge funds, such as operational freedom and strong managerial involvement. It acknowledges the lack of a consistent definition of hedge funds in the literature of finance but identifies unique characteristics that distinguish them from other investment structures.

The article highlights the rapid growth of hedge funds in Brazil, emphasizing their integration into the national financial space and their potential implications for wealth accumulation and socioeconomic disparities. Drawing upon Michel Callon's anthropology of economics and economies approach, the article underscores the importance of understanding the social and cultural dimensions of financial activities, emphasizing the role of standards and norms devices in shaping economic behaviors and outcomes.

Therefore, there is a new stratum within the elite of financial agents that not only challenges the conventional hierarchy but also has led to a remarkable concentration of wealth, in a dynamic of enrichment that has been relatively underanalyzed. This new stratum of financial agents and investors operates in innovative and complex financial instruments, leveraging their expertise to generate significant profits. As a result, they have amassed considerable wealth, contributing to the widening wealth gap and raising questions about the implications of this concentration of wealth within the financial system and society at large. Further analysis is needed to fully understand the dynamics and consequences of this phenomenon.

This article aims to provide an initial approach and raise some indicators that contribute to understanding this financial architecture. However, further research and analysis are necessary to fully grasp the implications and consequences of these mechanisms on the Brazilian society and its financial landscape.

One of the particularities of hedge funds, pointed by this work, is the operational freedom granted to fund managers, allowing them to adopt efficient and agile strategies to capitalize on opportunities that may not be available in more rigid structures, such as traditional funds. This flexibility enables hedge funds to navigate dynamic market conditions, respond swiftly to changing trends, and exploit market inefficiencies. By having the ability to employ a wide range of investment strategies, including long and short positions, leverage, derivatives, and alternative assets, hedge fund managers can actively manage risk and potentially generate higher returns.

This operational freedom and agility are key advantages of hedge funds, as they allow for a more proactive and opportunistic approach to investing. Unlike traditional funds, which often adhere to stricter investment mandates and regulatory requirements, hedge funds can swiftly adapt their portfolios and strategies to capitalize on emerging market conditions or unique investment opportunities. This adaptability is particularly valuable in fast-paced and dynamic financial markets, where the ability to act quickly and efficiently can be crucial in generating alpha and delivering attractive risk-adjusted returns.

However, it is important to note that this operational freedom also comes with inherent risks, as the use of complex strategies and instruments may expose hedge funds to higher levels of volatility and potential losses. Therefore, effective risk management and thorough due diligence are essential in hedge fund operations to ensure that the pursuit of opportunities is balanced with prudent risk control measures.

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