Hedge fund insiders are calling the Melvin Capital unwind a 'black swan' not a larger trend: 'The massive carnage is done'

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As the dust settles in the aftermath of embattled hedge fund Melvin Capital's big wind down, some on the Street may be wondering if the bleeding will stop with Melvin, or come for more of the industry. But according to some Wall Street insiders, despite the turmoil in the broader markets, the funds' demise likely won't foreshadow a similar fate for its hedge fund peers.

"It's yesterday's news, it's over," argues Thomas Hayes, the chairman and managing member of Great Hill Capital, a long/short equity firm based in New York. He believes "if [hedge funds] didn't get pounded out in the first quarter and the last few weeks building up cash, they're not going to get taken out to the woodshed." Put another way: "basically, the massive carnage is done," he argues.

After sustaining big losses on bets over the last year or so, including a notably bad short bet on meme stock GameStop, and with the funds down 23% year-to-date through the end of April, per a source familiar with the funds' performance, Melvin Capital founder Gabe Plotkin wrote investors Wednesday that he will wind down the funds and return cash to all investors, according to a letter viewed by *Fortune*.

Hayes notes this has all been a "massive unwinding" of the tech trade, which has hit other recent poor performers like titan Tiger Global and its so-called Tiger cubs. Indeed, tech stocks have fared even worse than the battered broader market, with the Nasdaq Composite down 27% year-to-date.

But from a more optimistic view, Hayes posits "if anything else, the selling may be exhausted, and you may see a bid start to come into the market."

And as for whether there may be more letters like Plotkin's coming from the hedge fund world? Hayes thinks it's behind us. "You'll see some marginal firms potentially close down, but more than that, you're just gonna see some widespread redemptions," he suggested. Hedge fund titan Ken Griffin, whose firm Citadel previously invested in Melvin Capital but pulled back its position earlier this year, echos Hayes' sentiment, saying at an event hosted by Bloomberg

Intelligence in New York City this week that he wasn't worried about what happened to Melvin happening to other funds, and that since the average lifespan of a fund is roughly three years, closures aren't uncommon.

Others like Darrell Cronk, the CIO for wealth and investment management at Wells Fargo, agree that while "anything's always possible," he doesn't think it's "a broader systemic problem, particularly as the broader industry has ... drawn down leverage," he told *Fortune*. Cronk notes the data shows many hedge funds have lowered their risk amid the "ongoing, sustained downward trend." Hayes also points out that cash levels have recently increased (according to a Bank of America fund manager survey out Tuesday, to the highest levels since 9/11 in 2001).

But in contrast to those like Melvin Capital, Cronk notes some hedge funds actually posted positive performance in the first quarter (though it is over a month and a half behind us, before more recent pain in the market). Hedge fund strategies, and in particular global macro hedge funds, "have limited the downside of this recent economic downturn and provided absolute returns," according to a Wells Fargo Investment Institute note on May 16, citing global macro was up over 10% from January through April, while global equities were down over 13%, per the report.

Although other big hedge funds with tech exposure like Tiger Global and Viking Global have had a rough year, those like Hayes suggest Melvin Capital was a "black swan"—the culmination of the pandemic, Reddit and retail trading especially around GameStop, and the downtrend in tech (in other words, those stalwarts like Tiger Global are not on the chopping block, Hayes and Cronk emphasize).

However, not all hedge funds are in the clear amid the volatility. Hayes says he's keeping an eye on risk parity funds in particular for potentially rockier waters, while Cronk suggests there may be more pain ahead in the broader market (he says he's watching technical support levels for the S&P 500, around 3,850 points).

Wells Fargo's Cronk says he's chatting with hedge funds constantly, and at the moment, they echo his overall sentiment: That the worst may yet be to come in the equity markets, but managers are being patient, he says (he describes what he's seeing in positioning right now as more "paralysis than panic").

As for the Melvin Capital's of the asset management world? "You can have someone who has a problem because they have too concentrated exposure or too much leverage or whatever the case is," says Cronk, "but it doesn't look to be an industry problem."