

Welcome to the November edition of *Hedge Fund Investor Spotlight*, the monthly newsletter from Preqin, providing insights into institutional investors in hedge funds. This month *Hedge Fund Investor Spotlight* contains information from our industry-leading online product, *Hedge Investor Profiles* and the newly released *2010 Preqin Global Hedge Fund Investor Review*.

## Investors: Shaping the Future of Hedge Funds

### Feature Article

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#### Institutional Investors: Shaping the Future of Hedge Funds

This week's feature article features information and data taken from the newly released *2010 Preqin Global Hedge Fund Investor Review*. It examines the role that institutional investors are going to play in shaping the future of the asset class.

### Investors in Focus

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#### UK Private Sector Pension Funds

Each month *Investor in Focus* examines a particular group of investors, using data from Preqin's *Hedge Investor Profiles* service. This month we examine UK private sector pension funds.

### Strategy in Focus

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#### Credit Funds

Each month *Strategy in Focus* examines a particular hedge fund strategy, using data from Preqin's *Hedge Investor Profiles* service. This month we examine credit funds.

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We look at the upcoming events in the hedge fund world.

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This month's *Investor News* identifies some of the most important new developments in the institutional investor universe. Full profiles for all institutions featured in *Investor News* can be viewed on our online service, *Preqin Hedge Investor Profiles*.

Featured this month:

- Shell Contributory Pension Fund UK
- Georgetown University Endowment
- Sentat Asset Management

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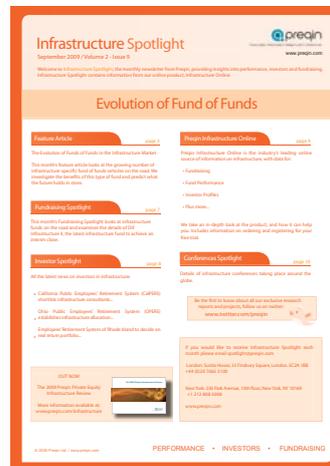
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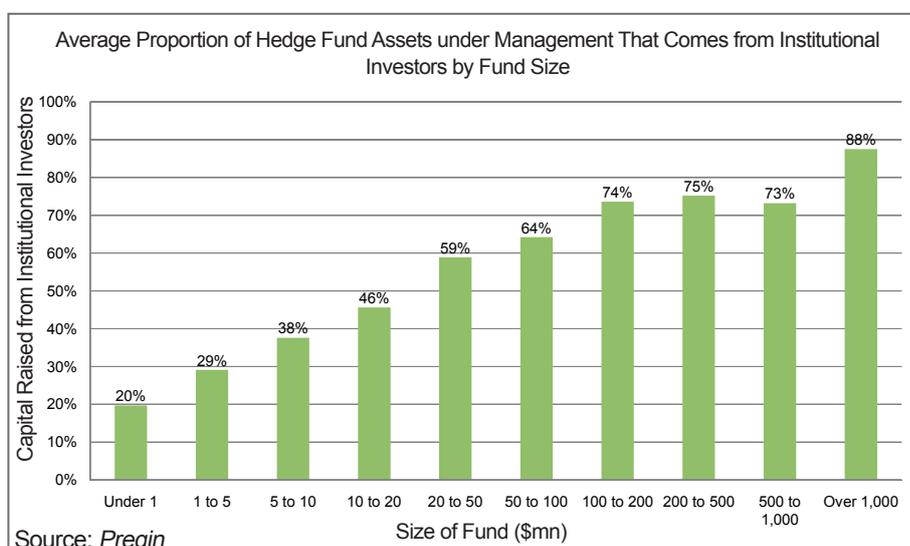
# Institutional Investors: Shaping the Future of Hedge Funds

Up until the global financial crash of Q3 2008, the hedge fund industry was booming, with more funds, more investors and more assets flowing into the market year on year. However, the asset class did not escape the downturn, and now managers must be more aware of investors' demands in order to attract support from a changing investor community. As conditions have improved, the outlook for the future has become clearer: institutional investor confidence in the asset class is returning and investors are now actively looking to make new investments over the course of 2010.

## The Importance of Institutional Backing

Hedge funds, traditionally the domain of the high-net-worth individual, have experienced an increased level of institutional support over the past five years. In a recent Preqin analysis of over 300 individual hedge fund managers (across strategies and regions) Preqin established that 72% of hedge fund

Fig. 1:



assets are now coming from institutional (including funds of hedge funds) backers. As Fig. 1 demonstrates, institutional support is particularly important for the larger funds, which can expect to get three-quarters of their assets

from institutional investors.

Once limited mostly to the portfolios of endowments, family offices and a handful of pension funds, hedge funds are today found in the portfolios of thousands of institutional investors across the world. Preqin's

Hedge Investor Profiles database tracks 2,500 institutions active in hedge funds, with this figure growing every day as new investors make their first investments in the asset class.

## Returning Institutional Confidence

The events of 2008 considerably dented investor confidence in the hedge fund industry: despite outperforming other asset classes, many hedge funds failed to produce the absolute returns they had promised. This, coupled with high-profile scandals and gating of assets, left some institutional investors disenchanted with the industry in 2008. However, over 2009 investors were more satisfied with their hedge fund investments and as a result have more confidence in the asset class than they did at the end of 2008. Over 73% of institutional investors are satisfied with hedge fund returns in 2009, up from

Fig. 2:

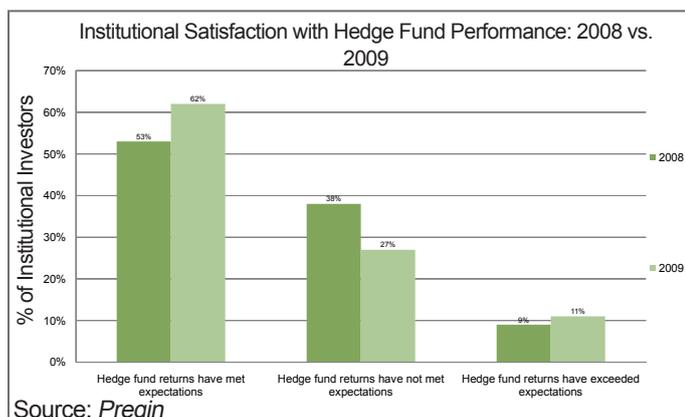


Fig. 3:

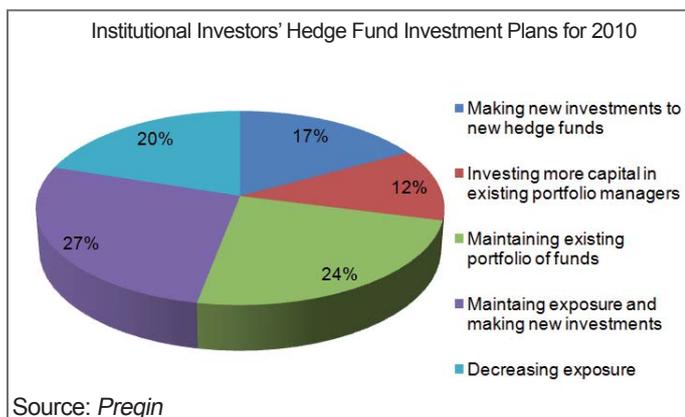
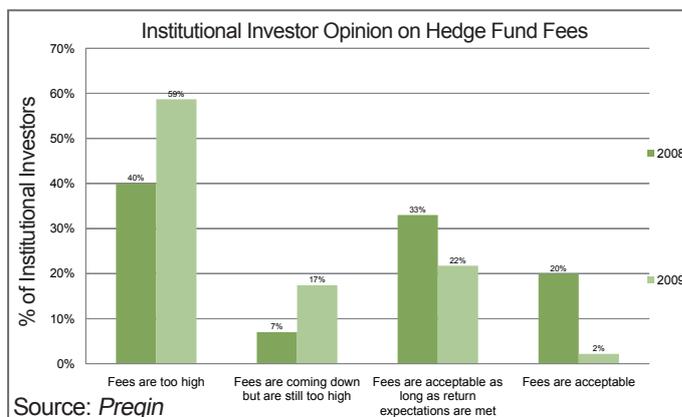


Fig. 4:



62% in 2008, and in turn approximately 66% of all hedge fund investors are either confident or very confident in the ability of hedge funds to perform portfolio objectives. If hedge funds continue to perform well, and managers listen to the demands of their investors, then we expect institutional confidence to continue growing, and as a result, for institutional investors to become an even more vital source of capital to the industry.

### The Return of Net Inflows into the Asset Class

Following the financial crisis in 2008, many institutions put all new investments on hold and redeemed some existing hedge fund holdings, either to meet short-term liquidity requirements or because of poor performance. Consequently, at the end of 2008 and the beginning of 2009, there were net outflows of assets from hedge funds and the industry suffered a significant contraction. However, the industry has recovered swiftly and in 2009 many funds have generated their best returns in years, with many hedge funds capitalising on the opportunities created as a result of the downturn. Institutional investors have steadily been making new investments in hedge funds over the second half of 2009. Additionally, Preqin has found that 29% of institutional investors intend to increase the amount of capital they invest in hedge funds over 2010, with 51% maintaining their

existing exposure and 20% decreasing their current exposure. However, from Fig. 3 it is clear that even some of those investors that are seeking to maintain their current allocation to the asset class are also looking to make investments in new funds as they seek to rebalance their portfolios and to take advantage of the latest opportunities and the best performing hedge fund strategies.

### How to Attract Institutional Investors

Fund transparency has replaced fund performance as the greatest consideration for investors when selecting new hedge fund managers. Risk management and firm reputation have also grown in importance following the high-profile hedge fund scandals that dogged the industry in late 2008 and early 2009. In 2008, the performance record of a fund was the most important criteria for institutional investors when assessing new hedge fund opportunities, however investors are now more conservative in their reasons for investing in hedge funds, with most choosing these vehicles for diversification and to improve the risk/return profile of their portfolio rather than to produce outstanding returns.

It is clear that institutional investors are becoming increasingly disillusioned on the subject of fees. Over the course of 2009, several prominent hedge fund investors (notably CalPERS) have

publicly called on hedge fund managers to reduce their management and performance fees, making the reduction of hedge fund fees a buzz topic in 2009. Today, just 24% of institutional investors feel that hedge fund fees at their current level are justified. Approximately 60% of institutional investors feel that hedge fund fees are too high, with a further 17% of investors surveyed stating that although fees are coming down, they remain too high. Institutional investors are becoming more aware of their power to negotiate fees and are increasingly using this power to drive fees down.

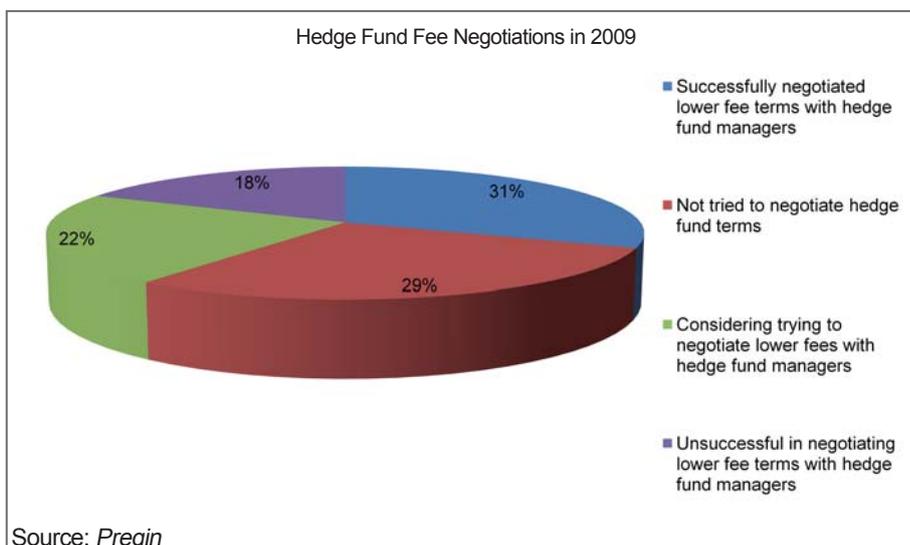
When Preqin asked institutional investors whether they have tried to negotiate better terms with their hedge fund managers, we found approximately half of all investors surveyed have tried to negotiate the management and performance fees associated with their hedge fund investments, with 62% of those investors attempting negotiations being successful. As can be seen in Fig. 5, a further 22% of institutional investors were considering approaching negotiations with hedge fund managers to reduce the fees charged on their funds. As more investors continue to negotiate the terms associated with their hedge funds, we can expect there to be a further consolidation of fees at a level below the standard "2&20" that has been the industry norm for years.

## The Key Message: Institutional Backing is Vital

Institutional investors are an essential source of capital for hedge fund managers: by obtaining institutional backing, emerging hedge funds become established, medium-sized funds become large funds, and managers have access to a long-term source of capital. In comparison to high-net-worth individuals, they have proved more likely to stick with their hedge fund investments through the market crisis and their confidence in the asset class is returning following the events of last year. Managers that are able to cater to the demands of institutional investors will be the ones which will gain their support in 2010.

Amy Bensted

Fig. 5:



Much of the information and data in this article was taken from the newly released 2010 Preqin Global Hedge Fund Investor Review.

In this year's Review we have included profiles and analysis for the most important 1,000 investors from around the world, all split into separate regions and countries for ease of use. We have also included analysis and listings of investors with a preference for the 10 most important fund strategies. This publication will save you thousands of hours of research and will put you in touch with the key people at the key institutions interested in your vehicle.

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Roger Gray, Chief Investment Officer, USS, United Kingdom  
Timo Ritakallio Chief Investment Officer, Ilmarinen, Finland

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**Institutional Investor**

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- Listings and analysis for 116 third party marketers and 62 prime brokers
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# Investors in Focus: UK Private Sector Pension Funds

Fig. 1

Key Facts: UK Private Sector Pension Funds	
% of UK private sector pension funds investing in hedge funds	52.8%
Average allocation to hedge funds	8.3%, GBP 339 million
Average target allocation to hedge funds	8.9%, GBP 363 million
Most favoured investment approach	Funds of Hedge Funds
Average # of hedge funds in UK private sector pension funds' portfolios	9
Typically been investing in hedge funds for...	2-2½ years

Source: Preqin

UK private sector pension funds are one of the newer groups of institutional investors to enter the hedge fund market, with many of these investors having been active in the asset class for two years or less. The relative inexperience of these pension funds has led to a significant number of them gaining exposure to the asset class through funds of hedge funds. As Fig. 2 shows, 71% of UK private sector pension funds have a preference for funds of hedge funds. Funds of hedge funds allow for exposure to a range of different hedge fund strategies and therefore are well suited to inexperienced investors in the asset class. Other strategies are favoured by only a small proportion of pension funds, and multi-strategy is the second most utilized strategy, with 13% of all private sector pension funds seeking to invest in this type of fund.

The relative inexperience of UK-based private sector pension funds also has a bearing on the geographic focus of the funds in which they invest. As Fig. 3 illustrates, 66% of UK private sector pension funds have a preference for global hedge funds. Investing in funds with a global focus is another way in which this type of investor can seek to

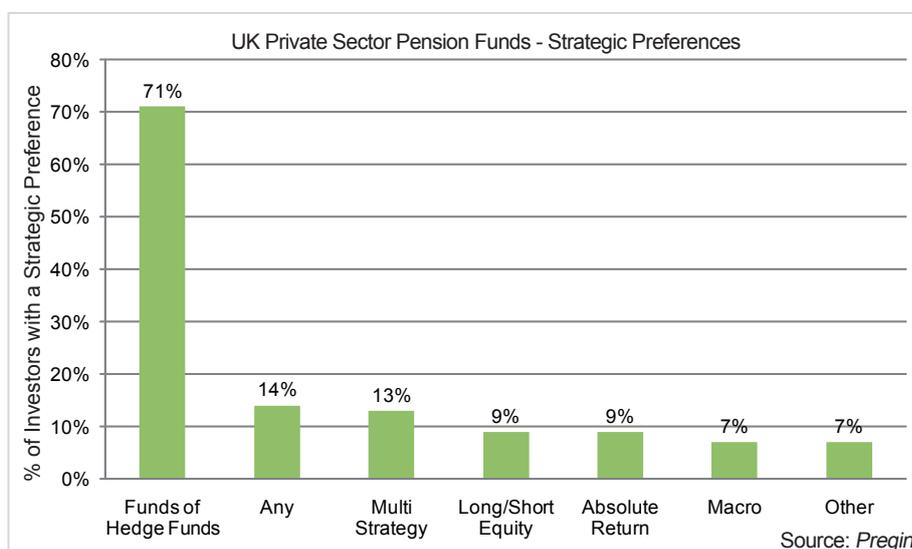
diversify its portfolio.

The second and third most favoured regions are Europe and North America, with 53% and 22% of private sector pension funds targeting investments in these areas respectively. Emerging markets and Asia attract the least amount of capital from this type of investor and this again is due to the fact that UK private pension funds are still relative newcomers to the asset class and

therefore favour more established hedge fund markets.

Railways Pension Trustee Company is the largest UK private sector pension fund investor in hedge funds, with \$2 billion committed to the asset class. Following the economic downturn, UK private pension funds are now beginning to show confidence in hedge funds and the asset class is seeing an influx of capital from these institutions. The \$17.4

Fig. 2:



billion Shell Contributory Pension Fund UK is looking to increase its exposure to alternatives and is planning to make its debut investment in hedge funds within the next six months.

Suganniya Kanaganayagam

Fig. 3

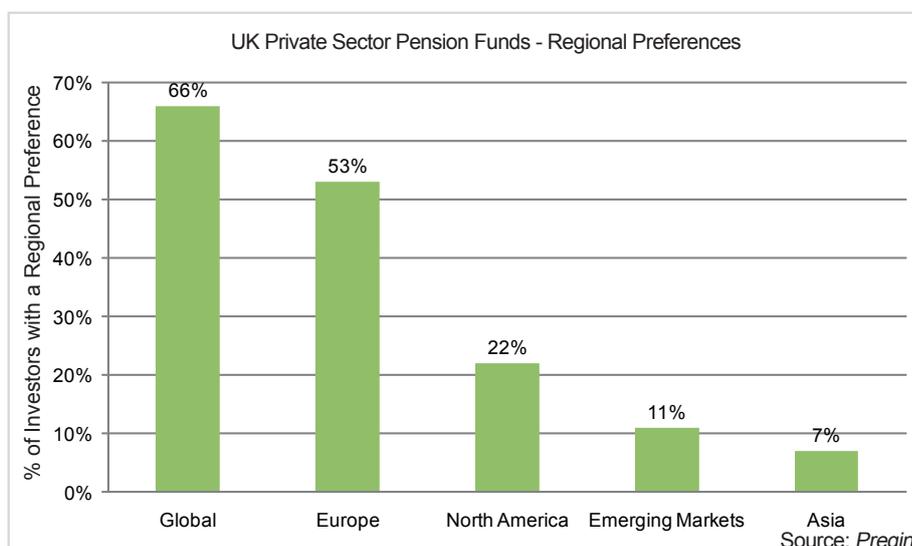


Fig. 4:

Top 10 UK Private Sector Pension Funds	
Investor	Allocation to HF (\$mn)
Railways Pension Trustee Company	2,393.9
BT Pension Scheme	2,216.1
Royal Mail Pension Plan	1,601.6
Shell Contributory Pension Fund UK	845.9
Diageo Pension Plans	494.7
Tesco Pension Scheme	488.3
Unilever UK Pension Fund	397.5
Cable & Wireless Pension Fund	353.2
Philips UK Pension Fund	349.3
Nestlé UK Pension Fund	338.3

Source: Preqin

The information and data contained in this article was taken from Preqin's Hedge Investor Profiles.

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# Strategy in Focus: Credit

Fig.1:

Key Facts - Credit Investors	
% of institutional HF investors that state credit as a preference	11.1%
Median AUM of a credit investor (\$bn)	2.0
Average allocation to hedge funds of credit investors	19%
Average returns sought from credit investments	8%
Most favoured investment approach (funds of hedge funds, direct hedge funds, mixture of both)	Direct hedge funds
Average lock-up of a credit fund (months)	16.6
Maximum lock-up accepted by credit investor (months)	23.1

Source: Preqin

Credit has been the fastest growing hedge fund strategy in terms of institutional investor mandates over 2009, with nearly twice as many institutional investors stating it as a preference this year compared to October 2008. Preqin currently monitors 191 institutional investors that have an active interest in credit hedge funds.

Funds of hedge funds are a large source of capital for credit hedge fund managers: with their ability to shift quickly into new strategies, funds of funds were the first group of investors to begin allocating to this type of fund. Many multi-manager firms have launched specific credit funds of funds over 2009, including the Paris-

based Olympia Capital Management. In addition, many endowments have begun investing directly in credit strategies this year. For example Georgetown University began a search for credit managers in the third quarter of 2009. Credit is still a relatively niche choice of hedge fund for the institutional investor, however it has rapidly grown in popularity throughout 2009 as a result of the opportunities created in the space following the market crisis.

North America and Europe are the largest sources of capital for credit funds, with 88% of the capital invested in the strategy coming from these regions. However, credit funds are becoming

more favoured by Asian and Rest of World investors, with 20% of investors based in this region identifying it as a strategic preference for 2009 and 2010. There have been many credit opportunities created in Asia as a result of the global financial crisis, and several Asian credit hedge funds have been formed as a result. Consequently, many institutions in the region have sought to capitalise on opportunities in their local markets by making investments in credit hedge funds.

Amy Bensted

Preqin currently holds profiles for 191 institutional investors with an active interest in this sector, on its industry-leading product Hedge Investor Profiles. For more information, or to register for trial access, please visit

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Fig.2:

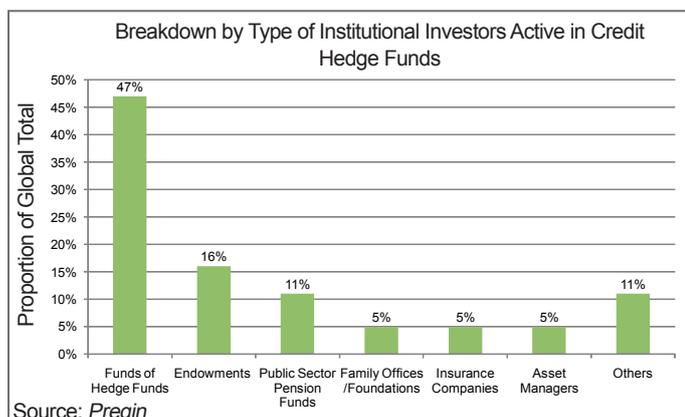
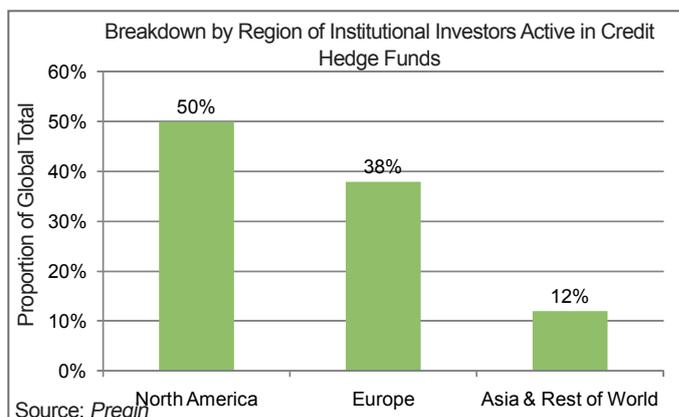


Fig.3:



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Preqin maintains a range of products for professionals involved with sourcing institutional investors for hedge fund vehicles, all based on our detailed database of over 2,500 institutions. With online services, data downloads and publications all available, Preqin can help you to identify and contact future investors.



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# Conferences Spotlight: Forthcoming Events

## Featured Conferences

### Hedge Funds World Zurich 2009

**Date:** 1-3 December 2009

**Location:** Dolder Grand, Zürich

**Sponsor:** Terrapinn

Now in its 12th year Hedge Funds World Zurich 2009 is Europe's premier hedge fund investment event for Swiss based family offices, pension funds and private bankers together with the hedge funds and asset management community who serves them.

**Information:** [www.terrapinn.com/2009/zurich/](http://www.terrapinn.com/2009/zurich/)

### Institutional Investor's European Pensions Symposium

**Date:** 3-5 February 2010

**Location:** St Regis Grand Hotel, Rome

**Sponsor:** Institutional Investor

Institutional Investor's European Pensions Symposium is one of the world's leading forums for heads of pension funds. Now in its 18th year, the two-and-a-half day event is attended by over 70 chief investment and executive officers from some of Europe's largest and most innovative pension funds.

**Information:** [www.iiconferences.com/EPEN.html](http://www.iiconferences.com/EPEN.html)

## Other Conferences

CONFERENCE/EVENT	DATES	LOCATION	ORGANISER
HedgeCo Capital Introduction Round Table	10 November 2009	New York	HedgeCo Networks
Effective Hedge Fund Tax Practices	16 - 17 November 2009	New York	Financial Research Associates
Hedge Funds World Africa 2009	17 - 20 November 2009	South Africa	Terrapinn
Gaim Ops Europe	30 Nov - 2 Dec 2009	Geneva	ICBI
Hedge Funds World Zurich 2009	1 - 3 December 2009	Zurich	Terrapinn
Institutional Research Meeting	13 - 14 January 2010	London	Institutional Investor Institute
GAIM USA 2010	19 - 21 January 2010	Boca Raton	IIR USA
European Pensions Symposium	3 - 5 February 2010	Rome	Institutional Investor
GAIM Ops Cayman	28 February - 3 March 2010	Grand Cayman	IIR USA

# Investor Spotlight: Investor News

## **Sentat Asset Management is seeking Nordic-based energy managers**

Sentat Asset Management is currently looking to diversify its portfolio. Initially focusing on energy strategies and moving on to other strategies such as convertible debt and distressed debt, it plans to hire between one and three Nordic-based managers. The USD 10 million asset manager currently manages one fund of funds vehicle which is focused on long/short strategies.

## **Shell Contributory Pension Fund UK announces plans to invest hundreds of millions of pounds in alternative assets**

The UK-based pension fund is going ahead with plans to increase its exposure to alternative assets. In October 2009, the GBP 10.6 billion pension fund had a 5% allocation to private equity and planned to invest a further 5% of its assets under management in hedge funds, infrastructure funds and commodity funds. This will be the first time that the pension fund has invested in the hedge fund asset class.

## **RecruitmentSuper looks to hire a new fund of hedge funds manager by the end of the month**

The Australian superannuation scheme will be hiring a new fund of hedge funds manager in the next few weeks. It is currently in the process of short-listing asset managers and a decision will be made following a meeting later this month. RecruitmentSuper expects to award AUD 25 million to the successful firm.

## **Co-operative Group Pension Scheme looks to hire new managers by mid-2010**

The GBP 5 billion pension fund is actively seeking new managers for its alternatives portfolio and is hoping to hire by mid-2010. Co-operative Group Pension Scheme is a relatively new but active and opportunistic investor in hedge funds. It has a target allocation of 13% of its total assets under management to alternatives, but has no set allocation to individual asset classes. The pension fund recently announced plans to increase its exposure to the hedge fund asset class, although potential mandate sizes have not been determined yet.

## **Milwaukee County Employees' Retirement System is seeking a long/short fund of hedge funds manager**

The USD 1.4 billion retirement system is currently looking to add one or more long/short equity fund of hedge funds managers to run a USD 160 million mandate. It is seeking managers with a track record of five years and fund of hedge funds vehicles with at least USD 300 million in AUM. It has also specified that the manager must have at least two senior members on the investment team who have been in place on the product for at least three years.

## **Georgetown University Endowment moves to increase its exposure to hedge funds**

The USD 1 billion university endowment is considering boosting its allocation to hedge funds. At present, Georgetown University Endowment allocates approximately 20% of its assets under management to the asset class. It is hoping to benefit from the effects of the recent market crisis by investing in hedge funds that were previously closed but are now accepting capital. The endowment is planning to add up to two long/short equity, credit or event driven managers to its portfolio.

## **Teachers' Retirement System of the State of Illinois switches hedge fund investment strategy**

The US-based retirement system is going to change the focus of its hedge fund portfolio and plans to reposition it into more of an absolute return strategy. It intends to allocate more assets to equity market neutral investments and less to distressed managers. It hopes that this change will generate more stable returns and make its hedge fund portfolio less sensitive to the market conditions.

## **NewAlpha Advisers launches incubator fund of hedge funds vehicle**

The firm has launched NewAlpha Genesis 4, a fund of hedge funds vehicle that focuses on incubating emerging hedge fund managers. It aims to invest in five or six new hedge fund managers and has a structure similar to a private equity offering, as investments will be locked up for up to three years. It plans to initially look for fixed income, global macro and commodities managers but it is also keen on event driven and Asian focused funds.

## **Alaska Retirement Management Board adds two new funds of hedge funds and looks to hire new managers**

Alaska Retirement Management Board (ARMB) recently announced that it has added funds of hedge funds GAM and Prisma Capital Partners to its investment portfolio. GAM will manage USD 100 million and Prisma will receive up to USD 50 million. In June 2009, the investment board announced that it would reduce absolute return investments by 1%, and was intent on diversifying its other assets among an increased number of hedge fund managers. ARMB is likely to hire new hedge fund managers to its fund of funds portfolio in the coming months.

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Each month Spotlight provides a selection of the recent news on institutional investors in hedge funds. More news and updates are available online for Hedge Investor Profile subscribers. Contact us for more information - [info@preqin.com](mailto:info@preqin.com)