

Preqin Special Report: Hedge Funds

Institutional Investors on the Hunt for Hedge Funds

September 2011



Foreword:

Since the launch of our hedge fund services in June 2007, Preqin has been delving deeper into the topic of the increasing institutionalization of the hedge fund industry and the effects this has had on the notoriously private sector. In this, the latest study on the growing importance of institutional capital we look further into investors' plans for the future and examine in more detail which investors will be allocating capital to the asset class in the next 12 months.

The fundraising environment of the past few years has been difficult and hedge fund managers have had to show great flexibility in adapting to a more demanding institutional investor. In this study we analyze the types of funds that are more likely to be successful in institutional fundraising, as well as taking a closer look at the management groups that institutional investors are seeking.

All the findings of this study are based on underlying investor profiles for 3,000 institutional investors, all regularly updated via direct contact with our international team of analysts.

Data taken from Preqin's Hedge Fund Investor Profiles database reveals that 32% of investors have fixed plans to invest in additional hedge fund vehicles over the next 12 months. Total capital earmarked for new hedge fund investments from these institutions ranges from \$125 billion at investors' lower estimates, up to \$195 billion at the top end of the scale. To gain a piece of this capital, please read on to find out more about institutional appetite for hedge funds in the next 12 months.

Contents:

Know Your Investors - The Institutional Universe in 2011	p. 3
The Globalization of Hedge Fund Investors	p. 4
Strategies and Structures over the Next 12 Months	p. 5
Emerging Manager Outlook	p. 6
Preqin Hedge Fund Investor Profiles	p. 7

Know Your Investors - The Institutional Universe in 2011

With up to \$195 billion earmarked for new hedge fund investments in the next 12 months, the time is ripe for hedge fund managers to market to the growing institutional sector of the investor community. However, to gain the interest of the increasingly sophisticated institutional market, managers must first understand the variation between investors within the institutional universe and the differing needs and demands of the investors allocating fresh capital in the next year.

From Fig. 1 it is clear that funds of hedge funds are looking for new hedge fund opportunities in the greatest numbers of all institutional investor types, with over half of all funds of funds looking for new vehicles over the next 12 months. Multi-managers constantly monitor funds in the marketplace in order to source the best opportunities for their investors and to keep abreast of new and emerging strategies. Such firms traditionally have a higher turnover of investments, as well as larger portfolios and a shorter typical holding period when compared to other institutional investors. An example of a fund of funds that intends to allocate to hedge funds in the next year is Permal. The \$23 billion multi-manager could add up to 25 new funds to its portfolios over the next 12 months, as a result of a new fund of funds launch and natural turnover within its existing vehicles.

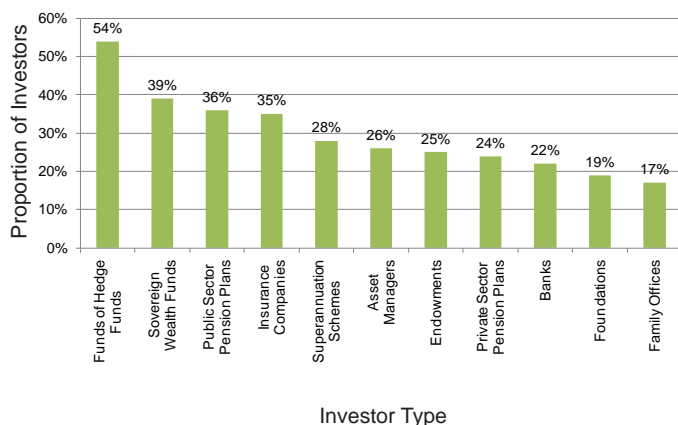
Public pension funds have been increasingly adding hedge funds to their portfolios over the past five years and despite the global recession remain committed to the diversification benefits these vehicles can offer within their portfolios. The mean allocation to hedge funds of public pension funds has grown year on year since 2007, when it stood at 3.6% of total assets to 6.6% invested in the asset class today. As they have increased their target allocations to the asset class they have sought new funds to manage their capital, and increasingly are looking to invest directly rather than through their traditional access point - funds of hedge funds. However, second to their private sector counterparts, they show the next highest appetite for funds of funds over the next 12 months, with 57% of the public pension funds on the search for new managers looking for multi-manager vehicles as part of their portfolio expansion. In comparison, 67% of private sector pension funds with plans for new investment are searching for funds of hedge funds.

“Public pension funds have been increasingly adding hedge funds to their portfolios over the past five years...”

Other notable investor types that will be allocating more capital in hedge funds in the next 12 months include insurance companies and superannuation schemes.

Sovereign wealth funds also have a significant interest in new hedge fund investments, with over a third of those active in the asset class looking at making additional allocations over the next 12 months. 36% of public sector pension funds that invest in hedge funds are on the hunt for further investments in the asset class in the next 12 months.

Fig. 1: Proportion of Each Investor Group Seeking to Make New Fund Investments in the Next 12 Months



Source: Preqin

The Globalization of Hedge Fund Investors

The size of the hedge fund industry is back to pre-crisis levels and investors are demonstrating their renewed faith in the asset class, with their planned increases in allocations. The industry has undergone many changes in the past few years, driven by the difficult market conditions and the changing face of the institutional market. One of the largest changes affecting in the industry is the increasing globalization of the investor base. Here we examine in greater details the geographic diversity of the institutional universe and the regions managers should be focusing their marketing efforts upon.

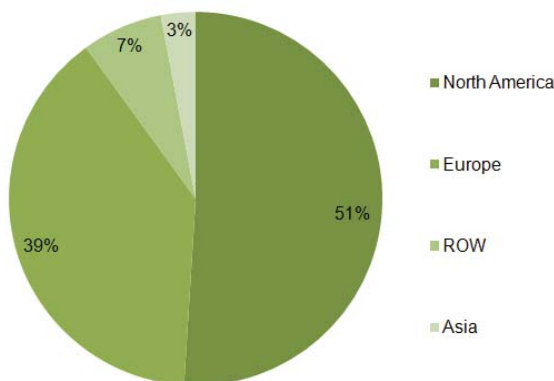
Although more than half of all investors seeking to make investments in the next 12 months are based in North America, proportionally just 29% of North American investors have fixed plans for new fund allocations in 2011 and into 2012, in comparison to 45% within Europe.

Investors in Asia and Rest of World also offer comparatively small, but significant, opportunities for managers wishing to raise capital from the institutional market, with 32% of investors in the area searching for new managers in the next 12 months. Many of these investors have only just begun investing in hedge funds following changes in local regulations and the propagation of new funds being set up in their domestic region. As a result, such institutions are investing in hedge funds to fill out their maiden target allocations to the asset class.

“...there has been a restoration of confidence amongst European investors...”

Many European investors have been relatively conservative since the market crisis and have not been very active in allocating fresh capital to the asset class. Despite this, there has been a restoration of confidence amongst European investors who, further buoyed by better performance and the proliferation of new structures such as UCITS, have begun to allocate capital to the asset class once again. For instance, Opplysningsvesenets Fond reduced its exposure to hedge funds in 2010 following policy change, but is now growing its portfolio once again by searching for one or two new CTA funds to add to its holdings in the next year.

Fig. 2: Geographic Breakdown of Investors Seeking to Make New Fund Investments in the Next 12 Months



Source: Preqin

Strategies and Structures over the Next 12 Months

Capital inflows into hedge funds are expected to be strongly positive over the next year. Investors have become much more focused on their searches for funds, with strategy and fund performance returning to the top of the list of the most sought-after features of a hedge fund. With funds of funds suffering arguably the most difficult three years, there has been a revival in the interest of institutional investors in the multi-manager sector. In this section we examine in closer detail which strategies will be most popular in the next 12 months and what fund structures institutions are looking to allocate to.

A very large percentage (87%) of investors planning to add to their hedge fund portfolios over the next 12 months include long/short equity as one of the strategies under consideration. Investors looking specifically at long/short equity funds in the next 12 months include Clariden Leu, the Zurich-based fund of hedge funds manager. Clariden Leu intends to allocate capital to 10 managers in the next year, investing a total of \$30 million. Macro hedge funds are also a popular choice with investors seeking to take advantage of currency movements, geopolitical events, and inflation and interest rate changes. For instance Barrett Capital Management, an asset manager has around \$22 million invested in small sized hedge funds, is currently searching for one or two new vehicles to add to its portfolio and has a particular interest in currency and global macro strategies. Next to long/short equity and global macro, 58% of institutions planning to make new fund investments are taking an “open door” approach to allocating to hedge funds and consider fund strategies on an opportunistic, case-by-case basis.

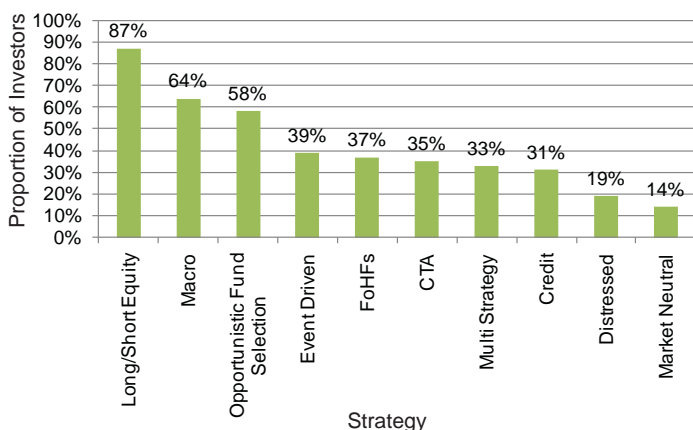
Commingled direct managers can expect to see the largest inflows over the next 12 months, with 83% of investors including an allocation to single-manager funds. As fund of hedge funds managers are the most prominent group making new investments in the next 12 months, much of this capital will continue to be siphoned via multi-manager funds; however other groups of institutional investors are beginning to allocate more capital to

single manager funds, often at the expense of their fund of hedge funds holdings. For instance, University of Houston System Endowment, which invests 26% of its total assets in a mixture of single-manager funds and funds of funds, has been increasing its weighting to direct investments over the past two years, with the intention of continuing on this path over the rest of 2011.

However, the future is looking far more positive for funds of funds following the difficult fundraising environment of the past three years. Funds of hedge funds are being sought by 47% of investors with plans to make new allocations in the next 12 months. Much of the new investment being made by the multi-manager market is being driven by inflows coming into their funds of funds vehicles at the top end, so as their funds grow so do their allocations to single manager vehicles. Funds of hedge funds are still the vehicle of choice for the newest investors in the asset class, as well as being utilized alongside direct investments by more experienced institutional investors to access niche strategies, or emerging themes and regions.

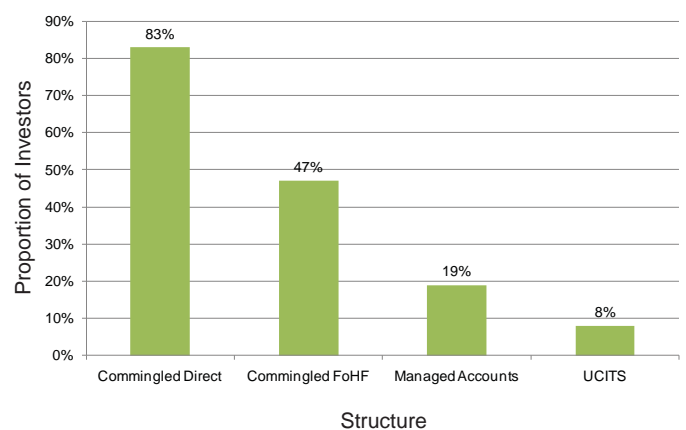
Managed accounts are continuing to grow in popularity amongst the liquidity- and transparency-hungry institutional community. 19% of all institutions planning to make new investments over the next 12 months prefer their capital to held in a separately managed account.

Fig. 3: Most Popular Strategies Being Sought in the Next 12 Months (% of Investor Searches Including the Strategy)



Source: Preqin

Fig. 4: Fund Structures Being Sought by Institutional Investors



Source: Preqin

Emerging Manager Outlook

Emerging managers have had mixed fortunes over the past three years. Although many investors express an interest in the emerging manager sector of the market, much of the inflows in 2010 were solely in the extra large funds as investors sought safety in numbers. However, investors are once again looking to allocate to the smaller, younger funds in their quest for alpha and access to the next generation of top performing funds.

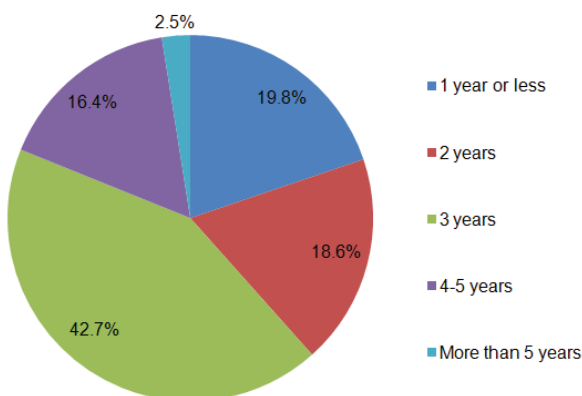
To examine in more detail what types of managers can expect inflows from the institutional market, we analyzed the minimum track record (Fig. 5) and minimum AUM requirements (Fig. 6) of investors planning to make allocations to hedge funds over the next year. It is clear that track record is still important to investors, and over 60% of the searches being conducted in the next year will focus on managers with a track record of at least three years. Nevertheless, investors are continuing to look at smaller managers, with just over a third of all institutions that are looking to add funds to their portfolios in the next 12 months considering vehicles with less than \$100 million in assets.

at the moment. A lot of talented men and women are starting hedge funds, so many that we wished we had more capital to invest in them!"

"...there is much more talent in the [emerging manager] arena at the moment..."

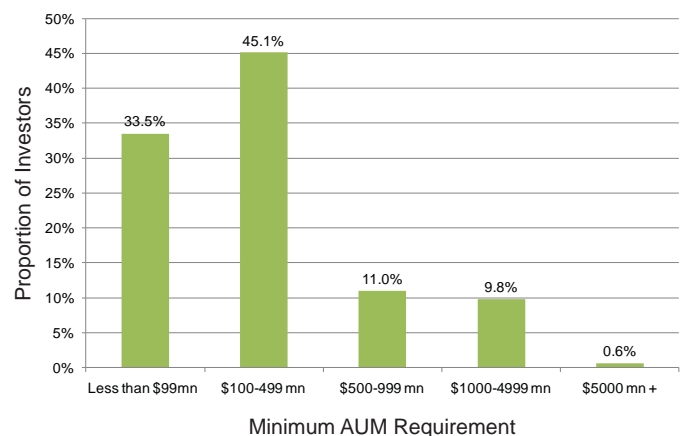
As part of our ongoing conversations with the 3,000 institutional investors on Hedge Fund Investor Profiles, we asked a selection of institutions seeking to make investments in 2011 and 2012 what their thoughts on emerging managers were. 28% stated that they were more open to marketing from emerging managers today than they were a year ago, and one prominent fund of hedge funds with a 20-year track record informed Preqin analysts that "although we have always invested in emerging managers we have definitely noticed that there is much more talent in the arena

Fig. 5: Minimum Track Record Requirement of Institutions Searching for New Funds



Source: Preqin

Fig. 6: Minimum AUM Requirement of Institutions Searching for New Funds



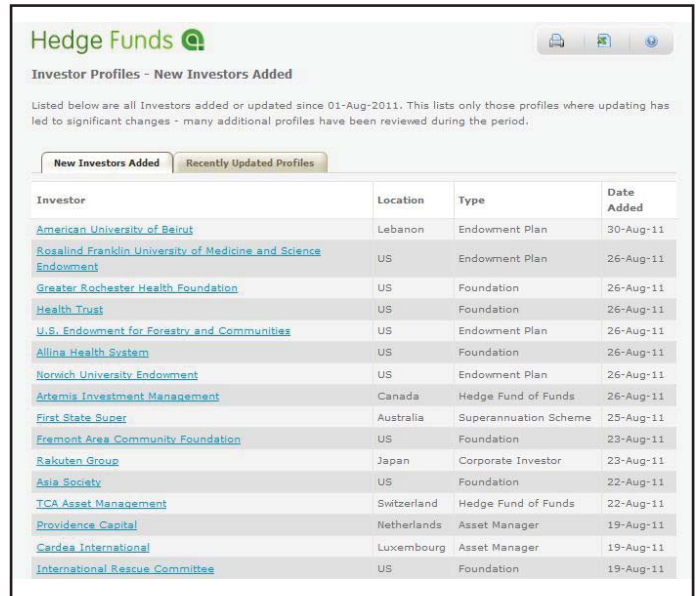
Source: Preqin

Preqin Hedge Fund Investor Profiles

Preqin Hedge Investor Profiles is the most comprehensive resource for hedge fund managers looking to raise institutional capital. With our exclusive data on investors in hedge funds we can help you achieve your fundraising goals.

Preqin Hedge Investor Profiles include:

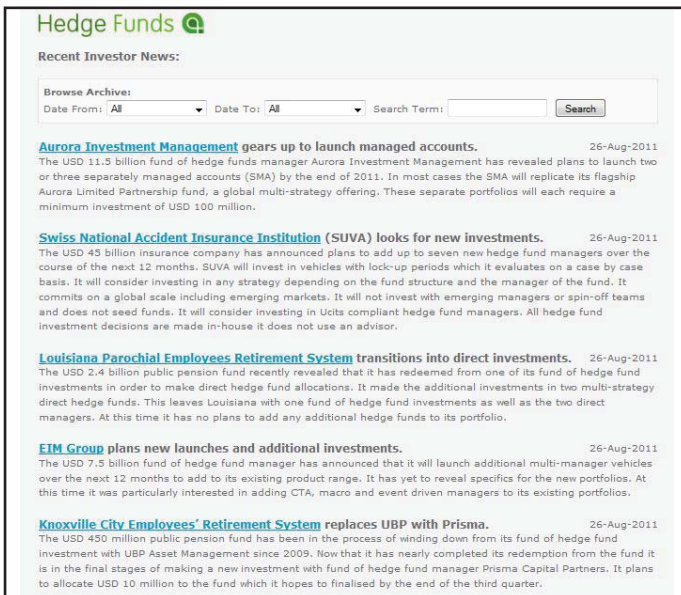
- Hedge fund preferences including strategic information, geographic preferences, emerging manager preferences, investment background – with both historic and forward-looking investment plans, typical commitment size, plus more...
- Key contacts including job titles, emails and direct phone numbers of key personnel responsible for hedge fund decisions.
- Detailed information on advisors and consultants active in institutional investment in hedge funds (premium access only).
- Advanced search facility to tailor your search to identify the best target for your funds.
- Download targets and contact details to Excel (premium access only) and create target lists for your fundraising road shows.



Hedge Funds Investor Profiles - New Investors Added

Listed below are all Investors added or updated since 01-Aug-2011. This lists only those profiles where updating has led to significant changes - many additional profiles have been reviewed during the period.

Investor	Location	Type	Date Added
American University of Beirut	Lebanon	Endowment Plan	30-Aug-11
Rosalind Franklin University of Medicine and Science Endowment	US	Endowment Plan	26-Aug-11
Greater Rochester Health Foundation	US	Foundation	26-Aug-11
Health Trust	US	Foundation	26-Aug-11
U.S. Endowment for Forestry and Communities	US	Endowment Plan	26-Aug-11
Allina Health System	US	Foundation	26-Aug-11
Norwich University Endowment	US	Endowment Plan	26-Aug-11
Artemis Investment Management	Canada	Hedge Fund of Funds	26-Aug-11
First State Super	Australia	Superannuation Scheme	25-Aug-11
Fremont Area Community Foundation	US	Foundation	23-Aug-11
Rakuten Group	Japan	Corporate Investor	23-Aug-11
Asia Society	US	Foundation	22-Aug-11
TCA Asset Management	Switzerland	Hedge Fund of Funds	22-Aug-11
Providence Capital	Netherlands	Asset Manager	19-Aug-11
Cardea International	Luxembourg	Asset Manager	19-Aug-11
International Rescue Committee	US	Foundation	19-Aug-11



Hedge Funds Recent Investor News:

Browse Archive: Date From: All Date To: All Search Term: Search

Aurora Investment Management gears up to launch managed accounts. 26-Aug-2011
The USD 11.5 billion fund of hedge funds manager Aurora Investment Management has revealed plans to launch two or three separately managed accounts (SMA) by the end of 2011. In most cases the SMA will replicate its flagship Aurora Limited Partnership fund, a global multi-strategy offering. These separate portfolios will each require a minimum investment of USD 100 million.

Swiss National Accident Insurance Institution (SUVA) looks for new investments. 26-Aug-2011
The USD 45 billion insurance company has announced plans to add up to seven new hedge fund managers over the course of the next 12 months. SUVA will invest in vehicles with lock-up periods which it evaluates on a case by case basis. It will consider investing in any strategy depending on the fund structure and the manager of the fund. It commits on a global scale including emerging markets. It will not invest with emerging managers or spin-off teams and does not seed funds. It will consider investing in UCITS compliant hedge fund managers. All hedge fund investment decisions are made in-house it does not use an advisor.

Louisiana Parochial Employees Retirement System transitions into direct investments. 26-Aug-2011
The USD 2.4 billion public pension fund recently revealed that it has redeemed from one of its fund of hedge fund investments in order to make direct hedge fund allocations. It made the additional investments in two multi-strategy direct hedge funds. This leaves Louisiana with one fund of hedge fund investments as well as the two direct managers. At this time it has no plans to add any additional hedge funds to its portfolio.

ETM Group plans new launches and additional investments. 26-Aug-2011
The USD 7.5 billion fund of hedge fund manager has announced that it will launch additional multi-manager vehicles over the next 12 months to add to its existing product range. It has yet to reveal specifics for the new portfolios. At this time it was particularly interested in adding CTA, macro and event driven managers to its existing portfolios.

Knoxville City Employees' Retirement System replaces UBP with Prisma. 26-Aug-2011
The USD 450 million public pension fund has been in the process of winding down from its fund of hedge fund investment with UBP Asset Management since 2009. Now that it has nearly completed its redemption from the fund it is in the final stages of making a new investment with fund of hedge fund manager Prisma Capital Partners. It plans to allocate USD 10 million to the fund which it hopes to finalised by the end of the third quarter.



About: Close Asset Management specialises in a range of financial services including specialist fund management such as fixed income and alternative investments alongside open and closed end and property funds, technology tracker funds and hedge funds.

Assets (mn):

Total Funds under Management (GBP mn):	10,000	
Already Committed to Hedge Funds:	3,000	30.0%

Preferences:

Locations: North America, Europe, Global

Strategies: Macro, Multi Strategy, Event Driven, Long/Short Equity, Relative Value Arbitrage, Equity Market Neutral, Absolute Return, Sector-Focused, CTA, Commodities

Volatilities: Low

Structures: Managed account - direct, Managed account - FoHF, UCITS

Structural Preferences: UCITS

Next 12 Months:

Year of First Investment in Hedge Funds: 1999

Emerging Managers: Yes

First Time Fund Preferences: Spin Offs: Yes Seed: Yes

Minimum Manager Requirements: Funds Under Management: GBP 300.0 mn

Currently Investing in Hedge Funds: Yes

Number of Hedge Funds in Portfolio: 80

Lock-ups Acceptable: ✓

Hedge Fund Investment Plans: Close Asset Management began investing in hedge funds in 1999. As of Q1 2011 it had 30% of its total assets under management invested in around 80 hedge fund vehicles. At this time it was invested through fund of hedge funds and direct hedge fund vehicles.

Contact us for more information or register your interest for [demo access](#).

New York: +1 212 808 3008
London: +44 (0)20 7645 8888
Singapore: +65 6408 0122

Email: info@preqin.com
Website: www.preqin.com



Contact Us

Preqin

Information for Hedge Fund Professionals

Preqin Hedge Funds provides information, products and services to hedge fund firms, funds of funds, investors, placement agents and investment consultants.

Available as:

- > Hard Copy Publications
- > Online Database Services
- > Consultancy and Research Support
- > Tailored Data Downloads

If you want any further information, or would like to apply for a demo of our products please contact us:

New York:

230 Park Avenue
10th Floor
New York
NY 10169

Fax: +1 212 808 3008

Tel: +1 440 445 9595

London:

Equitable House
47 King William Street
London
EC4R 9AF

Tel: +44 (0)20 7645 8888

Fax +44 (0)87 0330 5892

Singapore

Samsung Hub
3 Church Street
Level 8
Singapore 049483

Tel: +65 6408 0122

Fax: +65 6408 0101

Email: info@preqin.com

Web: www.preqin.com