

Welcome to the August 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: Preqin Secondary Market Monitor

## PE Secondaries: Opportunities for Hedge Funds

### Feature Article

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#### Opportunity Knocks for Hedge Funds

This month's feature article looks at how the private equity secondary market is becoming increasingly attractive to hedge fund investors.

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### Investors in Focus

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#### Swiss Funds of Funds

Each month *Investors in Focus* examines a particular group of investors, using data from Preqin's *Investor Profiles Online* service. This month we examine Swiss funds of funds, looking at their strategic and regional preferences, and identifying some of the most important key facts.

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### Products and Services

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Preqin is the industry's leading source of information on institutional investors in hedge funds. Our information is available in three principal ways:

- Online Profiles
- Publications
- Data Downloads

Please see page 6 for more information

### Strategy in Focus

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#### Convertible Arbitrage Investors

Each month *Strategy in Focus* examines a particular hedge fund strategy, using data from Preqin's *Investor Profiles Online* service. This month we examine convertible arbitrage investors.

Please see page 8 for more information

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### Investor News

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This month's *Investor News* section 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.

Featured this month:

- Florida State Board of Administration
- SYZ & CO
- Universities Superannuation Scheme
- TerraVerde Capital Management

Please see page 11 for more information

If you would like to receive *Hedge Fund Spotlight* each month please email [spotlight@preqin.com](mailto:spotlight@preqin.com).

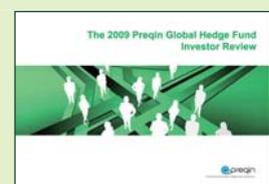
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# Private Equity Secondaries: Opportunity Knocks for Hedge Funds

Mark O'Hare



I was fortunate enough to attend and speak at the Capital Roundtable Private Equity Secondaries conference in New York on July 23rd.

It was a well-attended event, with several informative and thought-provoking presentations and panels. The participants included many of the usual suspects – secondaries firms, private equity fund of funds firms, institutional investors, private equity fund managers, advisors – but also some noticeable newcomers to the private equity secondaries scene in the form of several multi-strategy hedge funds.

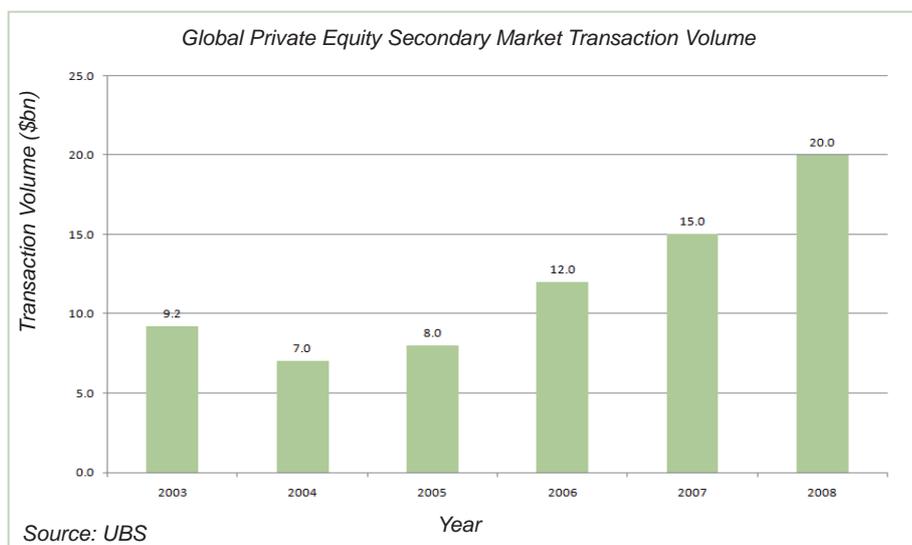
## Traditional Boundaries Becoming Blurred

Although such activity is not yet widespread, there have been an increasing number of instances where the traditional line between private equity and hedge funds is being blurred. On the private equity side, the current financial climate may see some private equity fund managers seeking to take advantage of undervalued public companies through taking minority stakes in publicly traded shares.

On the hedge fund side, we have seen a significant growth in the number of hedge fund managers adopting a more private equity style mindset when making investments. Long term investments such as financing leveraged buyout deals have become more commonplace, as have managers adopting a distressed investment strategy. Distressed asset hedge fund managers are now operating in exactly the same markets as private equity houses, and are accessing the same opportunities and even working side by side in certain deals.

In order to accommodate for these more illiquid investments,

Fig. 1:



we have seen a number of structural changes for these more hybrid managers, with longer redemption periods, and even completely separated pools of capital within the same fund whereby the illiquid investments are subject to a more private equity style of performance fee than the liquid portion.

## The Next Logical Step

Although investing in new funds from the outset does not represent a viable strategy for most of these hybrid fund managers, the undervalued, more mature offerings available on the secondaries market are becoming an increasingly important area of interest, and it's not hard to see why.

As Fig. 1 shows, private equity secondaries have historically been a small but growing part of the private equity world, with transaction volumes reaching \$20 billion in 2008.

The profitability of these investments has been very good, with most dedicated private equity secondaries funds raised over the period 2000-2005 delivering IRRs in the 20-30% p.a.

range (Fig. 2). Furthermore, very few funds have disappointed, with almost all of them delivering positive net returns (all these figures are net of management fees and performance fees). Combine this with a generally shorter carrying period than primary private equity investments, and it is clear that secondaries have delivered very good risk-adjusted returns for investors. As a result, there has been a strong flow of money into dedicated secondaries funds, with just over \$60 billion raised since 2004. So where does that leave the private equity secondaries market in 2009? And what is the supply:demand balance of capital and opportunities looking forwards?

Put simply, the evolving supply:demand balance looks incredibly favourable for buyers. Estimates of available capital dedicated to secondary investments vary, but generally lie in the \$30-60 billion range. Set against that, the potential volume of transactions is huge: last year's estimated \$20 billion of transactions comprises less than 1% of the \$2.5 trillion AUM in the global private equity industry. Investors in private equity funds have historically invested in primary funds and then held them through to maturity; this, however, seems certain to change. As Fig. 3 shows, private equity investors enjoyed a golden period from 2004 to 2006, as net distributions from funds exceeded net cash calls and this meant that money was coming back to LPs faster than they could commit to new funds. In response, most LPs adopted over commitment strategies, aiming to commit 150% or more of their target allocations in an attempt to put the money to work. 2007 then saw an uneasy balance, with both cash calls and distributions at a record level for the industry. The model came unstuck in 2008, as even the declining volume of cash calls exceeded distributions by a factor of 2.5:1 (these figures refer to buyout funds only, and exclude venture, mezzanine, real estate etc).

As a result, many LPs have been hit by the denominator effect and a severe cash flow crunch, which resulted in a considerable number having to sell interests in the last quarter of 2008. Thus Q4 2008 saw large numbers of secondary transactions,

especially from financial institutions and endowments. This trend has not continued in 2009 however, instead the market has come to a standstill. The first wave of forced sellers exited in Q4 2008, and those still needing to sell are now faced with a huge bid:ask spread, and are holding back for more favourable conditions. Fig. 4 shows the discounts to NAV for listed private equity funds, a very good proxy for market prices for secondary interests. With prevailing discounts of between 40% and 60% of NAV, only those with extreme cash flow problems are

Fig. 2:

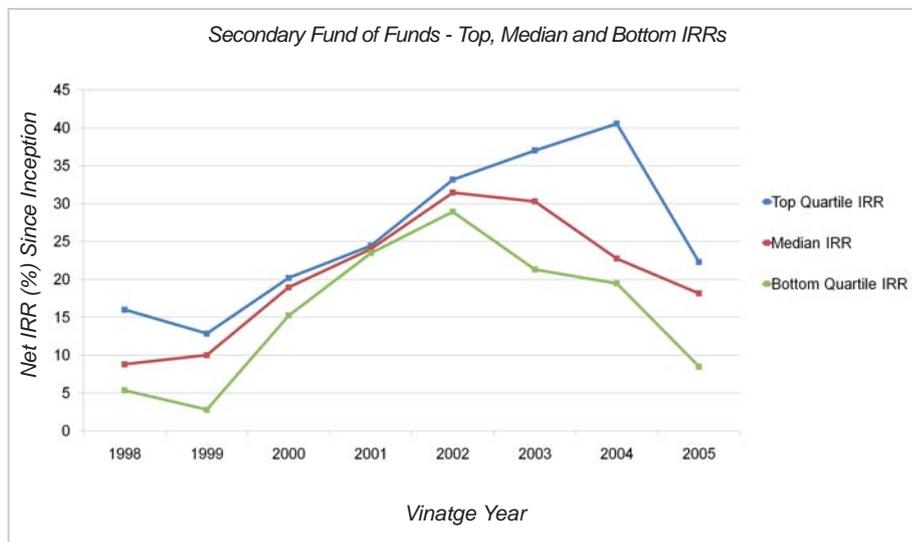
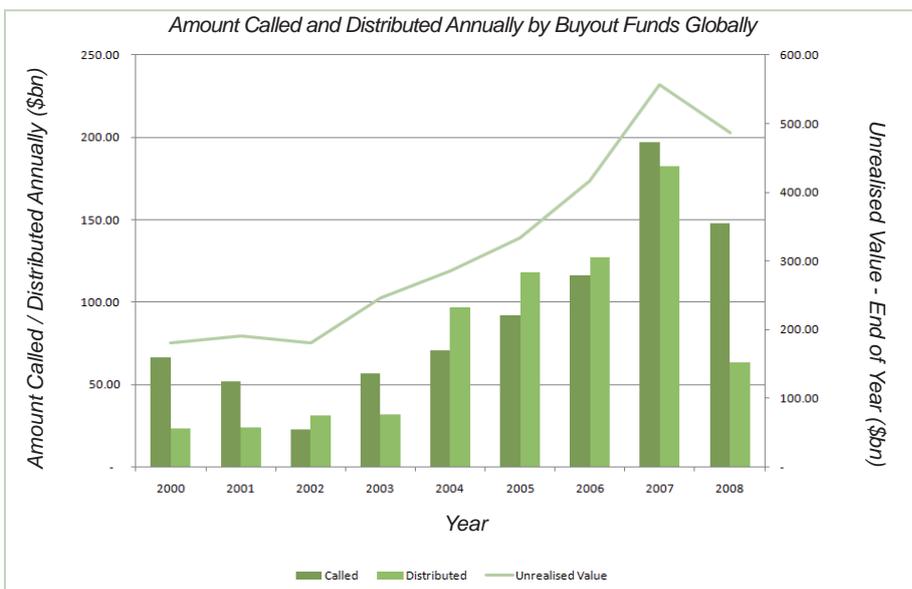


Fig. 3:



deciding to transact in these conditions, so transaction volumes during 2009 to date have been relatively low. Those sellers in less dire situations are waiting for pricing to improve before they sell, and most can afford to as private equity dealflow – and hence cash calls to LPs – have been minimal in 2009 to date. Which will happen first: will bid:ask spreads narrow, or will more sellers be forced to sell? As always, nobody really knows the answer, but the evidence suggests that more investors will be forced to sell, and paradoxically the reasons behind this could be an improvement in the economy and in markets. Private equity firms have over \$1 trillion of dry powder and are waiting for the right conditions to start making investments again. When they do start making these investments, they will of course increase cash calls to LPs, thus forcing those who can't respond to sell existing commitments. People in the industry talk of a coming tsunami in secondary supply.

Which brings us full circle to the hedge funds attending the PE Secondaries conference: a favourable supply:demand

Fig. 4:



balance; a coming wave of forced sellers; historically good risk-adjusted returns; and prices at potentially large discounts to NAV.

PE Secondaries, anyone?

In order to provide both buyers and sellers with a tool to help them find opportunities in this market, Preqin has recently launched the Private Equity Secondary Market Monitor, which has now been expanded to include information on real estate private equity.

LP Investors: can benefit from three key features of the service:

- **Preqin Price Indication:** the LP investor can enter a fund or portfolio at any time, and Preqin's powerful online pricing model algorithm calculates an instant indication of the likely current secondary market value;
- **Buyer and Advisor Profiles:** the LP investor can find profiles of all significant players in the market, helping them decide who they should be contacting if they wish to pursue buying or selling opportunities; and
- **Third Party Price Indication:** if the LP investor is interested in selling, they can submit their portfolio for a price indication from one of the buyers and advisors using the service. The buyers and advisors can see the portfolio and decide whether to submit a (non-binding) indication of likely price, but cannot see the identity of the LP investor. The LP investor therefore benefits from these further indications of likely value, and can contact the buyers and advisors for further discussions, potentially leading to a transaction.

Buyers and Advisors: also benefit from using the service, giving them information and generating potential dealflow:

- **Preqin Price Indication:** this is also available to these users, giving them an initial indication of current price levels for any fund or portfolio;
- **LP Strategies and Contacts:** Preqin's researchers are speaking with over 100 LPs per week, understanding who are the potential sellers and buyers. This vital information on potential

dealflow, together with contact details and the LP investor's program and strategy, is available only to users of the Secondary Market Monitor;

- **LP Pricing Requests:** LP investors submit their requests for Third Party Price Indications through the service. If the Buyer or Advisor wishes to respond with a (non-binding) price indication, then this price indication is submitted to the LP investor, together with the Buyer's / Advisor's profile and contact details. The LP investor can then initiate direct contact with the Buyer / Advisor if they would like to discuss the portfolio in further detail. The Buyer / Advisor can also send messages to the LP investor through the system.

In summary, the Preqin Secondary Market Monitor aims to give LP investors unique and vital information on current pricing and counterparties, and to give Buyers and Advisors unique access to potential dealflow. Significantly, the service is free for LP investors.

Please contact us if you would like to know more about the service, or alternatively, please view our product page at:

[www.preqin.com/SMM](http://www.preqin.com/SMM)

What is the true value of mature private equity investments?

## Preqin's Secondary Market Monitor

For more information on Preqin's services for potential buyers and sellers, please visit:

[www.preqin.com/secondarymonitor](http://www.preqin.com/secondarymonitor)

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# Investors in Focus: Swiss Funds of Hedge Funds

Switzerland has long been established as a centre for fund of hedge funds management, with many investment banks having set up multi-manager subsidiaries for their clients in the 1990s or earlier. In spite of this prevalence, however, the Swiss fund management industry has been severely affected by the market turbulence of the past 18 months, and the Swiss fund of hedge funds market is currently a lot smaller than it was at the end of 2007.

Many Swiss funds of funds were hit by the mass high-net-worth redemptions that characterised 2008 and this has

led to a large number of firms having to either shut up shop or consolidate into a larger asset management company. Additionally some of the largest Swiss funds of funds saw their reputations severely damaged when their exposure to the fraudulent Madoff vehicles was revealed at the end of 2008. However in the past two to three months there has been a noticeable uptick in fund of funds activity in the region – new vehicles have been launched and Swiss funds of funds have been winning investor mandates as institutional confidence in the asset class grows. Some Swiss funds of funds have even started to expand into new regions with the announcement that Syz & Co. is moving into the Spanish market with its 50% stake in the Spanish fund of funds N+1.

Amy Bensted

Fig. 1:

Top 10 Swiss Funds of Hedge Funds by HF Allocation	
Fund Name	Allocation to HFs (\$ mn)
UBP Alternative Investments	32,252
RMF Investment Management (now offered through Man Investments)	19,000
Pictet & Cie	13,822
Notz Stucki Group	12,000
3A	11,058
EIM Group	9,500
UBS Global Asset Management	8,700
Gottex Fund Management	8,500
LGT Capital Partners	5,000
Harcourt Investment Consulting	4,000

Fig. 2:

Key Facts Swiss Funds of Hedge Funds	
% of Swiss investors are FOF	39%
Average AUM	USD 2.7 bn
% of Swiss FoF that invest in emerging managers	66%
% of Swiss FoF that invest in emerging markets	27%
Average number of investments in Swiss FOF portfolio	76-100

Fig. 3:

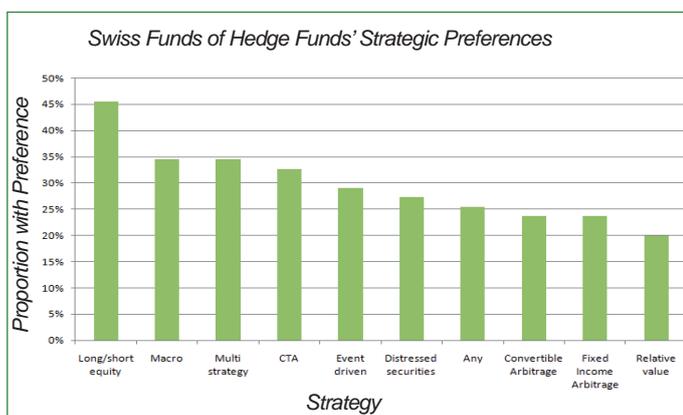
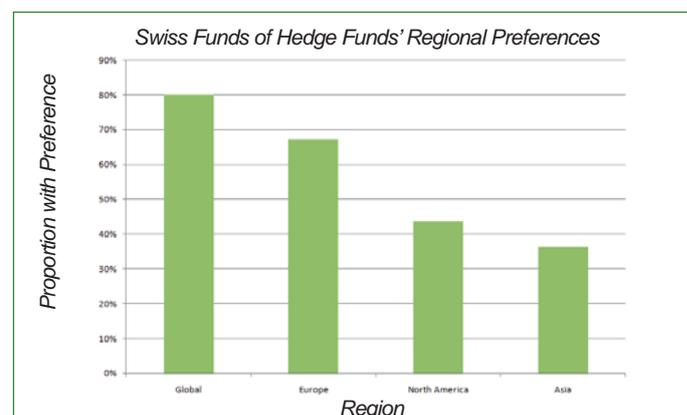


Fig. 4:



# Strategy in Focus: Convertible Arbitrage Investors

Despite a strong start, 2008 proved to be an *annus horribilis* for convertible arbitrage, with short selling bans, the nationalization of Fannie Mae and Freddie Mac and the bankruptcy of Lehman Brothers. These factors all contributed to certain managers losing six years of performance returns in six months over the latter half of the year. 2009, however, has marked a rally in the convertibles sector and some good investment opportunities have started appearing.

Fig. 1:

Key Facts: Convertible Arbitrage Investors	
% of institutional HF investors that state convertible arbitrage as a preference	5.93%
Average AUM of a convertible arbitrage investor	USD 9,974 million
Average allocation to hedge funds of a convertible arbitrage investor	19.80%
Average returns sought from convertible arbitrage investments	8.95%
Most favoured investment approach (fund of hedge funds, direct hedge funds, mixture of both)	Direct Hedge Funds

2008 saw a huge contraction in the number of managers running convertible arbitrage strategies, but, with fewer managers chasing these opportunities, many investors are seeing convertible arbitrage as a smart option, encouraged by the solid returns that managers have been producing over the first half of 2009.

The current investor interest in convertible arbitrage funds is dominated by funds of hedge funds in both North America and Europe. FoHFs are well equipped to react to the rapidly changing economic landscape, and convertible arbitrage funds have proved to be a good means of generating solid returns during 2009. Consequently, funds of funds are increasingly inclined to add these managers to their portfolios.

Providing convertible arbitrage continues to post consistent

returns, and institutional confidence picks up, we at Preqin predict that other groups of institutional investors will begin to invest greater sums of capital into such funds and convertible arbitrage managers will be able to pick up new mandates from a broader spectrum of investors.

Katy Johnson

*Preqin currently holds profiles for 141 investors with an active interest in this sector, including 68 North America-based, 54 Europe-based and 19 Asia and Rest of world based institutions.*

*To find out more and register for a free trial of Preqin's Hedge Investor Profiles visit: [www.preqin.com](http://www.preqin.com)*

Fig.2:

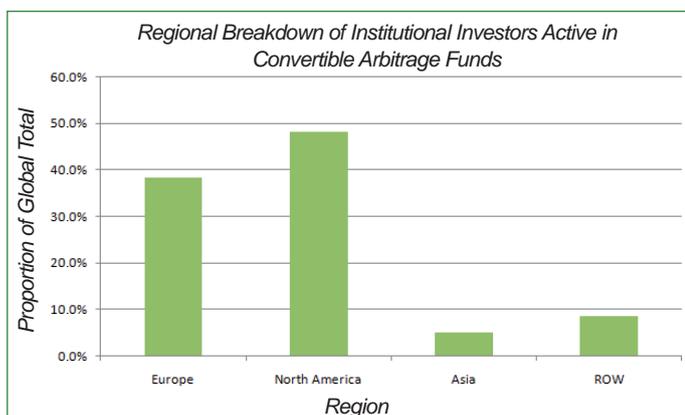
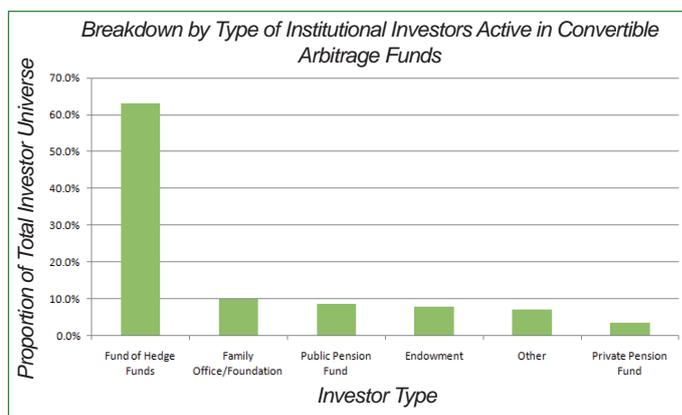


Fig. 3:



# Preqin: Hedge Fund Services

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 2,200 institutions. With online services, data downloads and publications all available, Preqin can help you to identify and contact future investors.



## Investor Profiles Online

See detailed profiles for over 2,200 investors of all types globally - pension funds, insurance companies, banks, foundations, endowments, family offices, fund of hedge funds and others.

Profiles include background, contact details, investment plans, preferences, assets under management, firms previously invested with and more.

Investor News section keeps you up to date with the latest developments in the market.

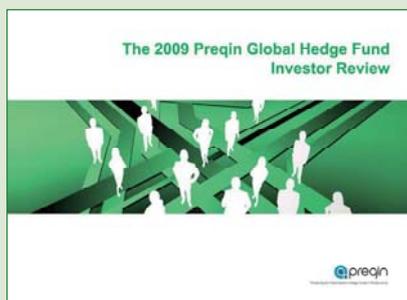
Database constantly updated by our team of dedicated analysts

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## 2009 Preqin Global Hedge Fund Investor Review

The newly released 2009 Preqin Global Hedge Fund Investor Review is the ultimate guide to institutional investors in hedge funds, featuring both profiles for 400 leading investors, plus comprehensive analysis on this increasingly important sector of the market.

For more information please visit:  
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With over 550 fund of hedge funds listed and contact details, including phone number and email address, for more than 1,750 individuals at these firms, the Fund of Funds download is a vital tool for all hedge funds looking to promote their fund to the multi-manager market. The fund of funds on this download are distributed across the globe, with interest in a wide range of strategies and fund types

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# Conferences Spotlight: Forthcoming Events:

CONFERENCE/EVENT	DATES	LOCATION	ORGANISER
Due Diligence for Fund of Funds & Hedge Funds	9 - 10 September 2009	London	IIR
World Alternative Investment Summit Canada	14 - 16 September 2009	Niagra Falls	Canadian Hedge Watch
Hedge Fund Activism and Shareholder Value Summit	22 - 23 September 2009	San Diego	IMN
7th Annual Alternative Investments Summit	22 - 23 September 2009	San Diego	IMN
Meeting of the Hedge Fund Business Operations Association	24 - 25 September 2009	New York	Financial Research Associates
Hedge Fund Regulation 2009	30 September 2009	London	InvestoRegulation
3rd Annual Hedge Fund General Counsel Summit	1 October 2009	Old Greenwich, CT	Incisive Media
Hedge Funds World Asia 2009	5 - 8 October 2009	Hong Kong	Terrapinn
Hedge Funds Regulatory Climate: Opportunities and Threats 2009	14 - 15 October 2009	London	Hedgestar
Hedge Funds World LatAm 2009	19 - 21 October 2009	Miami	Terrapinn
GAIM Fund of Funds	19 - 21 October 2009	New York	IIR
Global Hedge Fund Summit	25 - 27 October 2009	Bermuda	Institutional Investor
Hedge 2009	3 - 5 November 2009	London	Terrapinn
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

# Investor Spotlight:

## Investor News

### **TerraVerde Capital Management launches green fund of funds.**

The New York-based firm has recently launched a cleantech focused fund of hedge funds. The vehicle will invest in underlying hedge fund managers that are focused on the global reduction of carbon emissions, including through alternative energy. The firm will only invest in managers utilising strategies that have exposure to clean energy, clean technology, water, weather, agriculture, carbon and carbon trading. TerraVerde Capital Management was founded by Richard Bookbinder, managing member of Bookbinder Capital Management.

### **Florida State Board of Administration searches for hedge fund consultant as it plans its initial foray into the asset class.**

The pension fund has been considering making a maiden allocation to hedge funds since the end of 2008 after it hired Ashbel C William as its executive director and CIO. William had previously been a managing director at the hedge fund firm Fir Tree Partners. Florida State Board of Administration is currently reviewing proposals for a hedge fund consultant and is expected to make a decision on this by the end of September. The consultant will assist in deciding what hedge fund strategies to tap into and whether to invest directly or through funds of hedge funds. The board is likely to finalise a decision on its allocation and source of funding by the end of 2009.

### **East Sussex County Council Pension Fund begins the search for its first absolute return manager.**

The GBP 1.5 billion UK public pension fund has issued a tender for a traditional multi-asset absolute return manager to run 10% of its total assets. It will be considering both long only managers and hedge funds. It is searching for a manager that has prior experience in managing an absolute return strategy for a UK local authority and at least a three-year track record. Hymans Robertson, the pension fund's consultant, is assisting in the search.

### **SYZ & CO expands its Spanish operations by taking an operating stake in Madrid-based fund of hedge funds.**

The Swiss banking group has taken a 50% stake in N+1, a provider of investment banking, asset management, wealth advisory and alternative investment services, including fund of hedge funds. The new entity will be called N+1 SYZ Gestión. SYZ & CO already has a Spanish presence through its OYSTER funds. In addition to its OYSTER funds, already registered in seven European countries, the group is materially present in Austria, London and most notably Italy, through Banca Albertini Syz & C.

### **Penjing Asset Management announces plan to start a pool of money dedicated to seeding.**

The fund of hedge funds manager intends to seed five or six managers with its flagship Penjing Asia Fund and will begin with USD 25 million. The new pool will have fewer seeding restrictions than Penjing's existing funds of hedge funds, which cap any single holding at five percent of investments to diversify risks. It will look for candidates that meet at least one of the following criteria: strong performance, unique investment strategy, or the potential to rapidly expand assets. Its seeding activity will focus on start-ups but it may also include new offerings from managers that have been in operation for a while. Penjing's seeding investments so far range from USD 5 million to USD 15 million each. Future investments could amount to as much as USD 25 million after the new pool is set up.

### **Baylor University Endowment Fund searches for new investments.**

The USD 1.1 billion endowment fund is looking to invest in additional managers and is keen to add liquid strategies including long/short equity and global macro funds. It will look into opportunities with several top managers that had been closed for years but due to the current situation have re-opened to investors.

### **Universities Superannuation Scheme looks for hedge fund managers to run a GBP 1 billion mandate.**

The GBP 23 billion superannuation scheme has announced that it plans to hire around 50 managers over the next two years, each to manage around GBP 50 million. It is primarily looking for core strategy managers, but will consider both tactical and niche strategy exposure once a core portfolio is established. The superannuation scheme believes that it has the resources to manage a diversified program itself but does not rule out fund of hedge funds investments. It has been planning to increase its hedge fund exposure since the end of 2008, and a review of its entire hedge fund portfolio in June of this year confirmed this decision.

### **Teachers' Retirement System of the State of Illinois (TRS) plans to start looking for new managers in August 2009.**

The USD 27.2 billion public pension scheme intends to look for new investments between August and October 2009. This move follows the decision made by the board in May to double its target allocation to hedge funds. The target allocation now stands at 5% of its total AUM, but it has yet to decide if it will invest in funds of hedge funds or direct managers.

Angela FitzGerald

*Each month Spotlight provides a selection of the recent news on institutional investors in hedge funds.*

*More news and updates are available online for Investor Profile Online subscribers.*

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