

January 2010 / Volume 2 - Issue 1

Welcome to the January 2010 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.

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#### The Outlook for Emerging Managers

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This month's Investors in Focus looks at Asian insurance companies, examining their regional and strategic hedge fund preferences.

### Strategy in Focus

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#### Funds of Hedge 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 funds of hedge funds.

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A 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:

- BluMont Capital
- State of Wisconsin Investment Board
- Vodafone

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The 2010 Preqin  
Global Hedge Fund  
Investor Review



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# Feature Article: The Outlook for Emerging Managers in 2010

Despite the financial turmoil of the recent past, institutional appetite for emerging manager hedge funds is as strong as ever. Over recent years, as the market has become increasingly institutionalised, more and more institutional investors have added emerging managers to their portfolios in order to capture some of the extra alpha associated with such funds and to tap into new strategies and sources of returns.

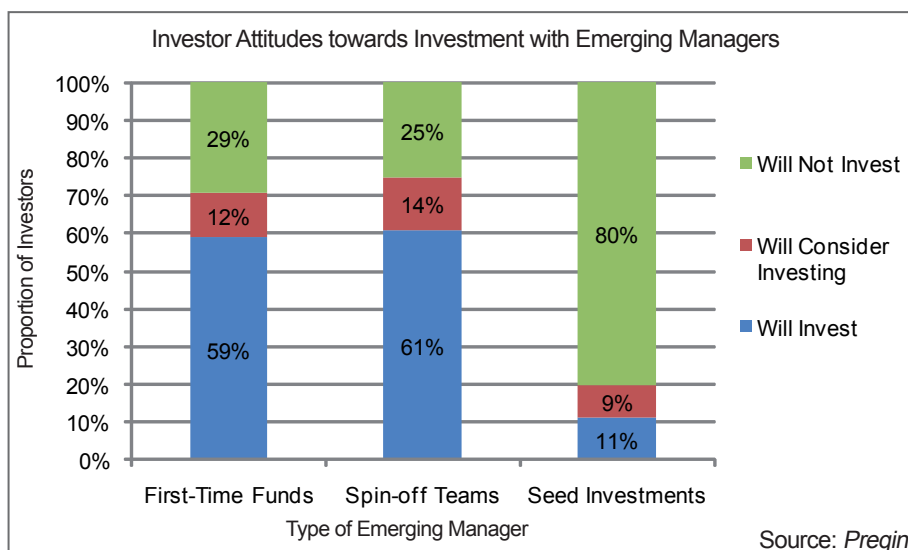
There was a large reduction in the size of the industry between the end of 2008 and beginning of 2009 and many emerging funds were amongst the casualties of the industry contraction. However, the best emerging managers have survived the downturn and have become very attractive to institutional investors, having either adapted their products or launched new products to suit the current economic climate.

## Investor Attitudes towards Emerging Managers

Fig. 1 shows that investment teams that have spun out from other firms are the most widely used type of emerging managers amongst institutional investors. These hedge fund managers are attractive to investors because they have a track record and are able to take the knowledge and experience from their previous firms into their own funds. This is appealing to institutional investors as they can carry out due diligence on the track record at the individuals' previous funds.

First-time fund management teams are also popular, with 59% of institutional investors investing with such teams. The past 12 months have proved to be

Fig. 1:



a litmus test for emerging funds: many funds were unable to cope with the redemption requests and deleveraging of the industry and disappeared completely in 2008 and early 2009. However, those funds that emerged from the market contraction with better than average performance are very attractive to the institutional market today. Many investors have used the turbulence of the past 12 – 18 months to assess emerging fund managers. The start-up funds that did well over 2008 and 2009 will appeal to institutional investors as the potential top performing fund managers of the 2010 and beyond.

Seeding hedge funds remains a relatively niche activity for institutional investors. It has been a difficult two years in terms of the seeding of funds: many seed investors lost capital as start-up funds collapsed following market turbulence

and as a result, many seeders put this part of their investment activity on hold. However, now that the volatility in the market is more manageable, and new managers are looking to launch new funds, there has been a revival in the seeding industry. For example, the seeding unit of London-based fund of funds FRM, FRM Capital Advisors, made new seed investments in October 2009, including its first seed investment in an Asian hedge fund. In addition, Blackstone is expected to launch a second seeding platform in early 2010, a follow on vehicle from its first seeding fund, the Blackstone Strategic Alliance Fund. The provision of seed capital remains largely the domain of funds of hedge funds and dedicated incubation platforms, with institutional investors preferring to access emerging managers early on, but not as the first investors in a fund.

### Track Record Requirements

Fig. 2 shows that more than 50% of institutional investors will consider managers with a track record of two years or less, with one-quarter searching for managers with a two-year track record. Institutional investors are able to assess how these funds have fared through both good and bad times and carry out thorough due diligence before making a commitment. Nearly a fifth of institutional investors look for a fund track record of five years or more; these investors are almost exclusively pension funds or insurance companies that will only allocate to “brand name” hedge funds.

### Assets under Management Requirements

Although 29% of investors will consider small funds (those with less than \$100 million in assets under management); this activity is, in the main part, restricted to funds of funds. There is a critical limit for most institutional investors active in hedge funds of \$100 million, after which institutional commitment becomes viable. Most investors allocate relatively large sums to funds, in comparison to high-net-worth individuals, and therefore cannot feasibly invest in funds of less than \$100 million without taking what they consider to be too large a stake in that vehicle. Above this, fund size becomes less significant for hedge fund investors, which instead look to the firm’s track record as the most important criteria for investment.

### Emerging Manager Appetite by Investor Type

Funds of hedge funds and asset managers are the largest providers of capital to emerging manager hedge funds. Such institutions have large investment teams and resources to put into hedge fund research and due diligence, and tend to look at the strategy and potential returns of a hedge fund rather than just its track record. As large investors in hedge funds, funds of funds and asset managers tend to diversify their portfolios across a variety

Fig. 2:

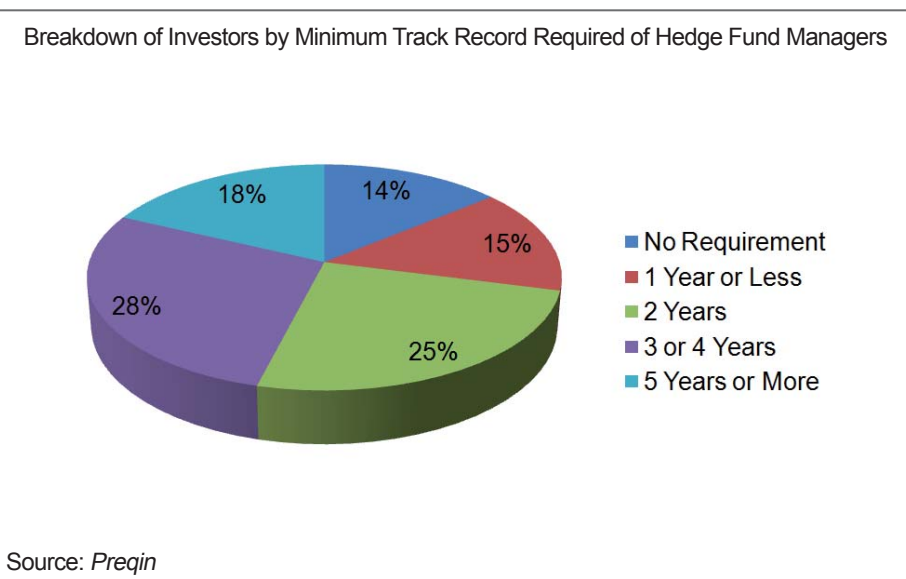
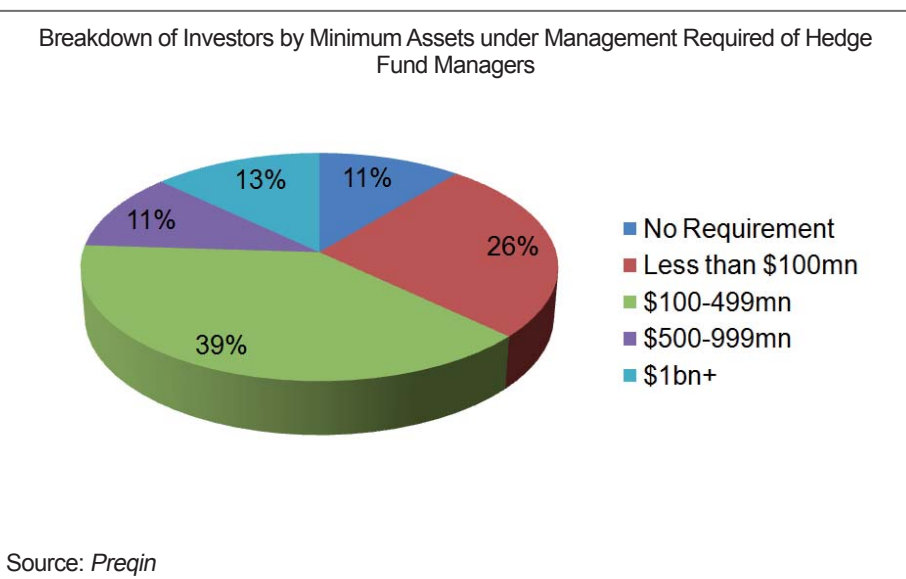


Fig. 3:



of fund types, including a mixture of both established and emerging hedge funds. Additionally, there are some dedicated fund of funds vehicles that solely invest in emerging manager funds.

Large proportions of endowments, family offices and foundations also invest in emerging manager hedge funds. These groups of institutional investors were early entrants into the hedge fund industry and have built up the experience

required to make investments that are perceived to be of a higher risk.

Although just under half of all pension funds use emerging managers to some extent, they are the group of investors least likely to commit to a first-time fund. When this group of investors allocate assets to emerging hedge fund managers it tends to be through a mixture of funds of funds and direct investments.

## Geographic Breakdown of Emerging Manager Investors

North American investors are the largest source of capital for first-time fund managers, representing 59% of all emerging manager investors. As the centre of the hedge fund industry, North America is home to the largest number of hedge fund investors, as well as the largest number of start-up funds. Since many investors prefer to invest with managers based in their domestic region, it is easier for investors based in established hedge fund markets to invest in emerging manager funds as there are a greater number of start-up funds in these areas. Asia and Rest of World investors are less prominent sources of capital for emerging managers, however 16% of all Asia and Rest of World investors will invest in these funds, usually to capitalise on opportunities within their local markets.

### Conclusion

The past 12 months have been challenging for all hedge funds – both established and emerging. However, many of the smallest and youngest funds in the market were hit the hardest, as they did not have the cushion of institutional assets to soften the high-net-worth redemptions that hit the market in 2008. However, in the second half of 2009 we witnessed an increasing number of fund launches, as well as net inflows of institutional capital returning to the asset class. Those emerging managers that came through the market turbulence with a strong performance record are now picking up institutional mandates following institutional assessment of their funds through the market downturn. For new fund launches it is clear that gaining the attention of funds of funds and seed providers is key to the early success of a fund. After this it is vital to attract institutional investors such as endowments, family offices and foundations, once the fund has reached a critical size, in order to grow and further establish the fund.

Katy Johnson

Fig. 4:

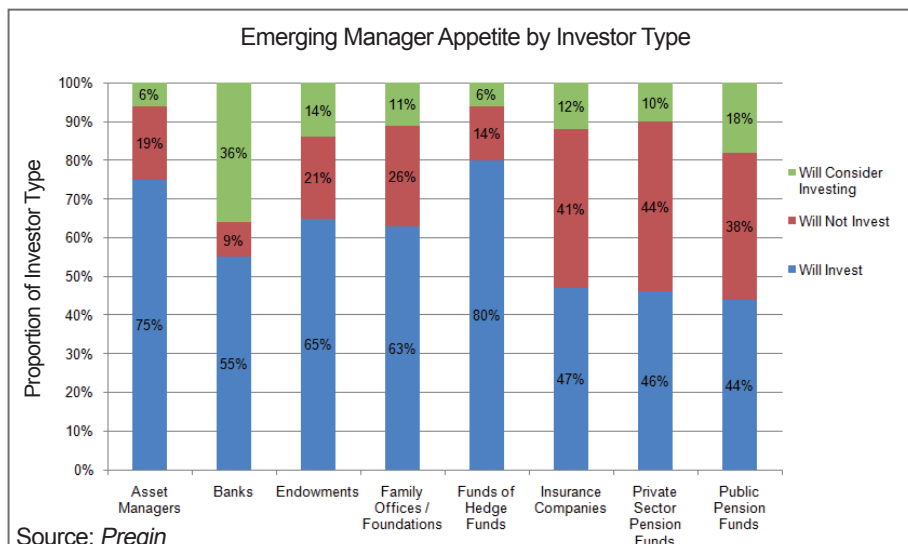
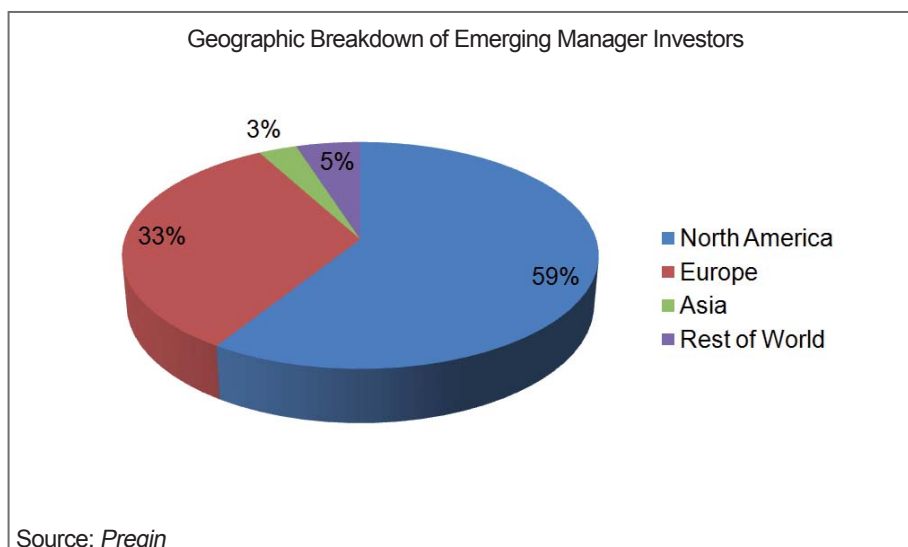


Fig. 5:



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This year's Global Hedge Fund Investor Review includes 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. The Review also includes analysis and listings of investors with a preference for the 10 most important fund strategies.

Full contents include:

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- Analysis and league tables for investors from each region
- Analysis for investors in each of the ten most important hedge fund strategies with listings for active investors
- Listings and analysis for 116 third party marketers and 62 prime brokers
- Analysis of emerging manager investors
- Exclusive information gained through direct contact with institutional investors



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# Investors in Focus: Asian Insurance Companies

Asian insurance companies account for just 1% of all hedge fund investors. Although this is a fairly low figure, it is expected to rise as Asian investors gain more confidence in hedge funds and become more experienced investors. Japanese insurance companies represent more than half of all insurance companies investing in hedge funds in this region. Taiwan is the second most significant region for this investor type and represents 14% of all Asian insurance companies investing in the asset class.

A high percentage of Asian insurance companies have a preference for North America-based hedge fund managers. North America is a popular area with many hedge fund investors because it is the hub of hedge fund activity. As shown in Fig. 2, 36% invest with hedge fund managers based in Asia.

Funds of hedge funds are a popular investment choice for Asian insurance companies. As newer entrants to the hedge fund asset class, Asian insurance companies invest in funds of hedge funds to gain exposure to a diverse range of investments and reduce risk. Credit and multi-strategy are also favoured by Asian insurance companies.

Katy Johnson

Fig. 3:

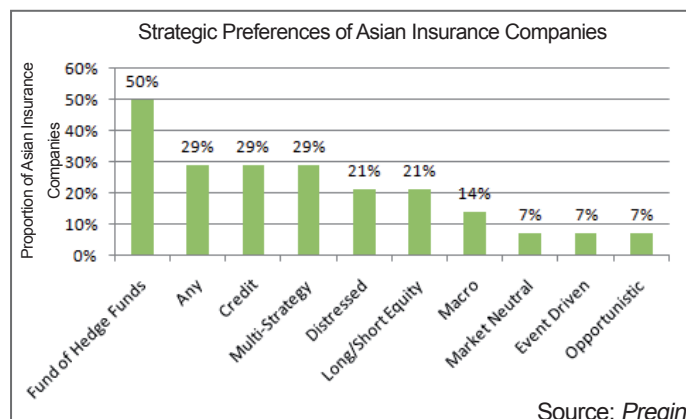


Fig. 1:

Key Facts: Asian Insurance Companies	
% of Asian insurance companies investing in hedge funds	42%
Average allocation to hedge funds	10.6%, USD 1,088 mn
Most favoured investment approach	Both direct and funds of hedge funds
Average # of hedge funds in Asian insurance companies' portfolios	22
Typically been investing in hedge funds for...	10 years

Source: Preqin

Fig. 2:

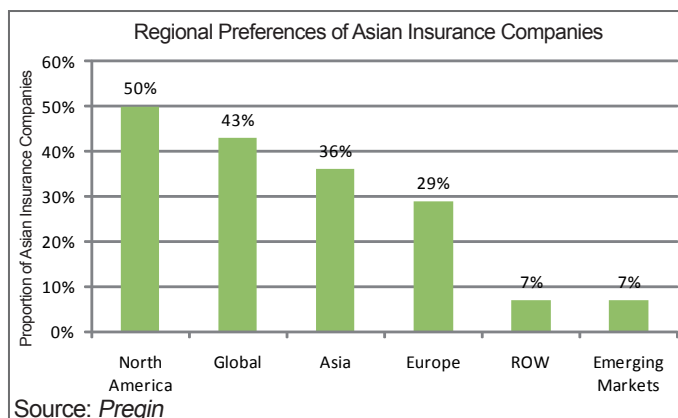


Fig. 4:

Top 5 Asian Insurance Companies Investing in Hedge Funds	
Investor	Allocation to HF (\$mn)
Sumitomo Life Insurance Company	3,000
Daido Life Insurance	1,782
Tokio Marine and Nichido Fire Insurance	990
NLI International	983
Meiji Yasuda Life Insurance Co.	743

Source: Preqin

# Strategy in Focus: Funds of Hedge Funds

Preqin monitors 741 institutional investors with an active interest in funds of hedge funds, and it is currently the most utilised investment style for hedge fund investors. However, there was a decline in the proportion of investors with an active preference for funds of funds over 2009 as compared to 2008 (57% of investors in 2009 versus 64% of investors in 2008). Over the course of 2009 the fund of funds industry underwent scrutiny following larger than average losses in 2008 and the exposure of some high-profile vehicles to the Madoff funds. This brought the due diligence procedures of funds of funds as well as their value into question.

Over 2009 there was a shift towards institutions making direct investments alongside fund of funds investments, and currently 45% of all funds of funds investors also make strategic direct investments. Funds of hedge funds are still the investment method of choice for newer or smaller investors in hedge funds that use these vehicles to gain a greater understanding of the asset class or to create a diverse portfolio of funds through a single investment.

Fig.1:

Key Facts - Investors Active in Fund of Hedge Funds	
% of institutional investors which state FoHF as an active preference	57.10%
Average AUM of a FoHF investor (\$ bn)	1.4
Average allocation to hedge funds of a FoHF investor	9.50%
Average returns sought from FoHF investments	6.20%
Average lock-up of a FoHF fund (months)	6.3

Source: Preqin

Funds of hedge funds are also used by investors seeking exposure to new strategies or regions.

have at least one fund of funds in their portfolio.

Nicole Rubbi-Clarke

Public and private pension funds are currently the most active investors in funds of hedge funds, with 84% of all public pension funds and 58% of all private pension funds stating fund of hedge funds as a strategic preference. North American institutions are the most common investors in funds of hedge funds, with more than half of all investors in this strategy based in this region. However, proportionally, the use of funds of hedge funds is greatest in Europe, where more than two-thirds of all hedge fund investors

Fig.2:

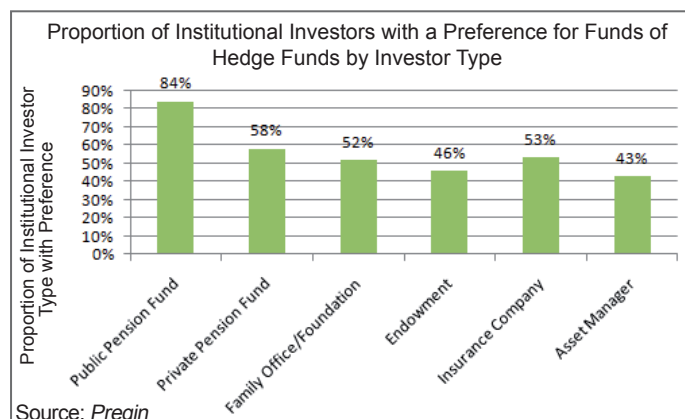
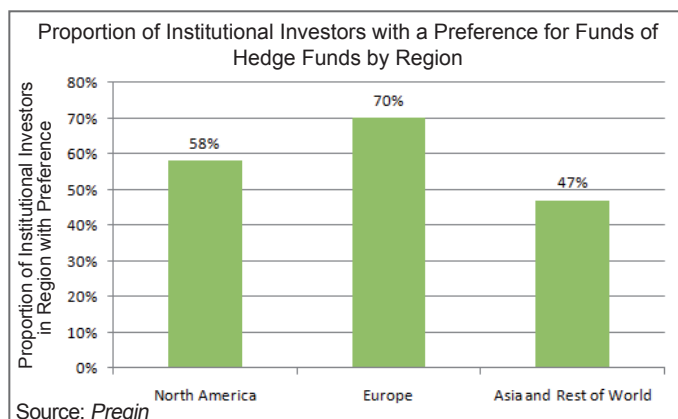


Fig.3:





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# Conferences Spotlight: Forthcoming Events

## Featured Conferences

### Hedge Funds Regulation, Reporting & Controls

**Date:** February 26, 2010  
**Location:** TBC, Central London  
**Sponsor:** Infoline

This timely and practical conference explores in detail how the new alternative investment regulations will affect the way you work, sell, invest and do business. The focused agenda will bring you the very latest in hedge fund regulations from the decision makers behind the policies. The event draws together a high profile speaker panel representing key names from hedge fund firms, prime brokers, institutional investors and trusted advisors to the industry.

**Information:** [www.infoline.org.uk/r.php?uID=1530](http://www.infoline.org.uk/r.php?uID=1530)

**Who Should Attend:**

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- Legal & Compliance
- Internal Audit, Risk
- Fund Administration
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Restructuring the Business of Hedge Fund Management

26 February 2010 • Central London

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- Identify the impact on existing business models
- Learn how to manage compliance under new regulations
- Examine the effect on investment decisions
- Find out how to minimise and manage costs of regulatory change

This comprehensive agenda includes:

- REGULATORY PERSPECTIVE**
- Get to grips with the implications of the AIFM for managers, investors and prime brokers

**HEDGE FUND MANAGERS' PERSPECTIVE**

- Evolving your business model in the face of new regulations
- Restructuring funds under new regulations
- Guidance on restructuring your business with taxation in mind

**INSTITUTIONAL INVESTOR PERSPECTIVE**

- How will investors view a post-regulation hedge fund world
- Find out what information and disclosures investors expect
- Will new regulations open hedge funds up to a wider range of investors

**PRIME BROKERAGE PERSPECTIVE**

- Examine how regulation will change the prime broker/manager relationship
- Explore new ways to 'design-in' effective controls to check performance and meet regulatory obligations
- Identify where prime brokers can help hedge funds meet regulatory obligations

**With insights from:**

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## Other Conferences

CONFERENCE/EVENT	DATES	LOCATION	ORGANISER
Institutional Research Meeting	13 - 14 January 2010	London	Institutional Investor Institute
GAIM USA 2010	19 - 21 January 2010	Boca Raton	IIR USA
The Activist Investor Conference	21 - 22 January 2010	New York	DealFlow Media
European Pensions Symposium	3 - 5 February 2010	Rome	Institutional Investor
GAIM Ops Cayman	28 February - 3 March 2010	Grand Cayman	IIR USA
Asset Allocation Summit Asia 2010	15 - 17 March 2010	Hong Kong	Terrapinn
AsiaHedge Forum 2010	17 - 18 March 2010	Hong Kong	HedgeFund Intelligence
Fund Forum Asia 2010	19 - 23 April 2010	Hong Kong	ICBI
Global Hedge Fund Summit	2 - 4 May 2010	Bermuda	Institutional Investor
Emerging Managers Summit	19 - 21 May 2010	Chicago	Opal
Hedge Funds World Asia 2010	13 - 15 September 2010	Hong Kong	Terrapinn

# Investor Spotlight: Investor News

## **State of Wisconsin Investment Board plans to invest over USD 3 billion in hedge funds in its first foray into the asset class.**

In December 2009, State of Wisconsin Investment Board (SWIB) was gearing up to make its first foray into hedge funds with an initial 2% allocation, which it planned to increase to 5% by mid-2010. SWIB manages the assets of Wisconsin Retirement System, the ninth largest pension fund in the US, State Investment Fund and other state trust funds. The pension fund has a hedge fund mandate of around USD 3.1 billion. It intends to hire up to 25 hedge fund managers, initially seeking 15 and then adding 10 by mid-2010. Cliffwater advises SWIB on all its hedge fund investments.

## **BluMont Capital will acquire Northern Rivers Capital and its management team in February 2010.**

BluMont Capital, a subsidiary of Integrated Asset Management and one of Canada's most prominent hedge fund companies, announced on December 16, 2009 that it would be purchasing the investment management firm Northern Rivers Capital. BluMont plans to integrate Northern Rivers Capital's management team, comprised of portfolio managers Hugh Cleland and Alex Ruus. Both are experienced portfolio managers with expertise spanning the technology, healthcare, resource and energy sectors. The purchase is expected to close in February 2010.

## **IMQubator makes its second seed investment.**

The fund has announced its second seed investment but has yet to reveal any other details of the move. It plans to seed four more funds at the beginning of 2010 and received over 140 responses to its initial search for new seed investments. It announced in November that it was looking to attract hedge funds from outside of the Netherlands and will typically seed each manager with EUR 25 million.

## **BlackRock Alternative Advisors gears up to launch new fund of hedge funds vehicle.**

BlackRock plans to roll out the BlackRock Core Alternatives Portfolio in early 2010. The fund will aim to enable wealthy individuals access to hedge funds that have boosted pension funds' and endowments' returns. It will invest in long/short equity and/or fixed income strategies, distressed debt security strategies, absolute return strategies and emerging markets. BlackRock takes an active approach to asset allocation based on its relative value determination. In addition to the extensive manager selection and due diligence processes, BlackRock's operations and administration staff conduct extensive reviews of hedge fund managers, paying particular attention to the operating framework of a fund.

## **Texas Treasury Safekeeping Trust Company plans to add as many as 40 direct managers to its portfolio over the next 12 months.**

The company is planning to transform its current hedge fund portfolio by adding more single manager hedge funds and redeeming some of its current fund of hedge funds investments. It is looking to focus the bulk of its portfolio on single manager hedge funds. It intends to allocate USD 20 million to each new investment and will add as many as 40 hedge funds. It plans to redeem six of its current fund of hedge funds investments to make room for the new funds. Despite market turbulence during 2009 and losses suffered through one of its hedge fund investments, Texas Treasury Safekeeping Trust Company remains positive about hedge funds and believes they are well suited to an endowment portfolio.

## **San Bernardino County Employees' Retirement Association (SBCERA) hires consultant to review its hedge fund portfolio.**

SBCERA has hired HedgeMark Institutional Consultants to prepare a report on how it accounts for its hedge funds holdings, as well as how it manages risk for individual funds and its entire fund portfolio. The pension fund currently invests around USD 490 million in hedge funds, 10% of its total capital, although it can invest up to 12% in the asset class. The evaluation will cover the structure and administration of the pension plan's hedge fund investments, risk management procedures, manager surveillance and compliance with plan policies. HedgeMark is due to present its preliminary findings in January. As a result of this review, SBCERA may shift some of its investments into separate accounts from commingled funds.

## **Vodafone delays alternatives foray.**

The UK Pension plan for the telecoms giant considered adding alternatives to its investment portfolio during 2009 and was initially intending to make a decision by the end of the year. However it has postponed the final decision on whether to make its first steps in alternatives until this year. The GBP 1 billion pension plan began considering alternatives following the appointment of a new general consultant, Watson Wyatt Investment Consulting, in December 2008.

Nicole Rubbi-Clarke

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)