Does “2 and 20” Still Exist?
Results of Preqin’s Hedge Fund Terms &
Conditions Survey – Fees Special Report
July 2009
Over the course of April to June 2009, Preqin, the industry-leading provider of information on institutional investors in hedge funds through its Hedge Investor Profiles service, conducted a survey of hedge fund managers in order to present a snapshot of the industry’s terms and conditions as they currently stand. Preqin’s survey was designed to assess how the current economic downturn had affected the terms of investment laid down by managers, and whether it had affected the composition of investors in the asset class. We surveyed both single manager fund managers and fund of funds managers across a wide variety of strategies and global regions. The following research report contains a brief summary of our findings specifically regarding fees.

Management Fees

As illustrated by Fig. 1, more than two-thirds of funds have management fees of 1.5% to 2% inclusive, and 93% fall between 1% and 2% inclusive. Very few funds differ significantly from this norm. The mean management fee for the funds that we surveyed was 1.63%, which is significantly lower than what has traditionally been considered the industry standard of 2%. A single fund reported having no management fees at all, relying solely on a performance fee. At the other extreme, one specialised CTA fund had a management fee of 7.5%, which in turn was balanced out by a very low performance fee.

Performance Fees

As Fig. 2 shows, nearly 7 in 10 hedge funds still maintain a performance fee of 20%, which demonstrates that many investors are still willing to reward top performance. However, an increasing minority have lower fees of between 10% and 20%. In fact, 12% of surveyed funds have a 10% performance fee, significantly lower than the traditional 20% fee. At the top end of the range, a CTA fund had a performance fee of 33%, while several specially-structured fund of hedge funds had no performance fee at all. The mean performance fee we found was 17.21%.
Breakdown by Strategy

As mentioned in the previous section, one CTA fund we surveyed has a 7.5% management fee, and as Fig. 3 shows, this is not an isolated occurrence, with CTAs having the highest average management fees of any fund type surveyed. Longer-term strategies, such as special situations and distressed securities, command some of the highest fees, while fund of hedge funds unsurprisingly demand much lower fees. More traditional hedge fund strategies, such as long/short equity and market neutral, also charge lower fees, likely reflecting the high levels of competition within these strategies.

There is some correlation between the strategy breakdowns for performance fees and management fees in Fig 3. Event driven, CTA, distressed securities and special situations funds are all again high up the fee scale, while fund of hedge funds and multi-strategy funds again charge quite low fees. Most other strategies have moderate fee levels.

Breakdown by Fund Size

There is a clear correlation between the size of a fund and fees charged, as shown in Fig. 4. Both management and performance fees trend downwards as fund size increases. Performance fees in particular show a sharp drop as fund size increases. To some extent, this reflects the fact that many of the larger funds are fund of hedge funds, which levy much lower performance fees. The exception to this downward trend is in the highest fund size brackets, where management fees actually rise again. This is indicative of the higher demand that the largest funds can generate, due to both the security they offer through sheer scale and the returns they often deliver that helped make them so in demand in the first place. Many investors are therefore willing to pay higher management fees to access these funds. At the other end of the scale, small funds tend to invest in niche strategies that are often more volatile, but

### Fig. 3: Average Fees by Investment Strategy

<table>
<thead>
<tr>
<th>Strategy</th>
<th>Management Fee</th>
<th>Performance Fee</th>
</tr>
</thead>
<tbody>
<tr>
<td>CTA</td>
<td>2.17%</td>
<td>18.90%</td>
</tr>
<tr>
<td>Event Driven</td>
<td>1.71%</td>
<td>20.00%</td>
</tr>
<tr>
<td>Special Situations</td>
<td>1.71%</td>
<td>20.00%</td>
</tr>
<tr>
<td>Distressed Securities</td>
<td>1.70%</td>
<td>19.30%</td>
</tr>
<tr>
<td>Credit</td>
<td>1.69%</td>
<td>18.10%</td>
</tr>
<tr>
<td>Relative Value</td>
<td>1.67%</td>
<td>16.70%</td>
</tr>
<tr>
<td>Macro</td>
<td>1.67%</td>
<td>16.30%</td>
</tr>
<tr>
<td>Other</td>
<td>1.63%</td>
<td>18.20%</td>
</tr>
<tr>
<td>Multi-Strategy</td>
<td>1.55%</td>
<td>16.60%</td>
</tr>
<tr>
<td>Market Neutral</td>
<td>1.53%</td>
<td>18.90%</td>
</tr>
<tr>
<td>L/S Equity</td>
<td>1.53%</td>
<td>18.60%</td>
</tr>
<tr>
<td>Fixed Income</td>
<td>1.44%</td>
<td>18.30%</td>
</tr>
<tr>
<td>Arbitrage</td>
<td></td>
<td></td>
</tr>
<tr>
<td>FOHFs</td>
<td>1.26%</td>
<td>10.60%</td>
</tr>
</tbody>
</table>
with the potential for higher returns, and they charge higher fees to reflect this expected higher performance.

Manager Location & Fees

Fig. 5 shows that there are significant differences between managers based in different regions. Perhaps due to greater competition, or the greater maturity of its hedge fund market, North American managers have markedly lower fees for investors than their European counterparts. The emerging hedge fund markets in Asia have lower fees than both, likely in order to attract previously sceptical investors to the region.

Summary & Conclusions

It is clear that the idea of the ‘2 and 20’ structure as the industry standard is becoming outdated. Our analysis in fact suggests a ‘1.63 and 17.21’ formula – although less succinct – would be more accurate. Fees which for years have conformed to the industry standard of ‘2 and 20’ are now being driven down as investors become more powerful in the manager/client relationship. US pension funds such as CalPERS and Utah Retirement System have been vocal in their belief that the hedge fund compensation structure needs to evolve and managers, in response to these demands and those of other institutional investors, are changing their fee structures. The troubles the industry faced last year have resulted in a significantly smaller universe of hedge funds, and those funds which are flexible in the terms they can offer their investors are the ones which are picking up the new investment now assets are flowing back into hedge funds. Less liquid strategies that demand longer timeframes to come to fruition, but promise greater returns, such as distressed securities and special situations, still largely command ‘2 and 20’ fees, but they are the exception now, rather than the rule.

### Table: Management Fee & Performance Fee

<table>
<thead>
<tr>
<th>Location</th>
<th>Management Fee</th>
<th>Performance Fee</th>
</tr>
</thead>
<tbody>
<tr>
<td>North America</td>
<td>1.54%</td>
<td>16.33%</td>
</tr>
<tr>
<td>Europe</td>
<td>1.72%</td>
<td>17.94%</td>
</tr>
<tr>
<td>Asia</td>
<td>1.55%</td>
<td>15.88%</td>
</tr>
<tr>
<td>RoW</td>
<td>1.67%</td>
<td>19.25%</td>
</tr>
</tbody>
</table>
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 2,350 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 2,350 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.

To register for your free trial please visit: www.preqin.com/hedge

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: www.preqin.com/InvestorReview

Fund of Funds Download

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.

For more information please visit: www.preqin.com/hedge

Emerging Managers Download

With contact details on over 550 institutions who have expressed an interest in investing in emerging managers our Emerging Manager Download is an excellent way of targeting the best potential investors for your fund. Investors include Hedge Fund of Funds, public pensions, endowments and family offices and foundations.

For more information please visit: www.preqin.com/hedge
About Preqin:

Preqin provides information products and services to alternative assets firms, fund of funds, investors, placement agents and fund marketers, law firms, investment banks, advisors and consultants across five main areas:

- Fund performance
- Fundraising
- Investor profiles
- Fund terms
- Fund manager profiles

Our customers can access this market intelligence in four different ways:

- Hard copy publications
- Online database services
- Consulting and research support
- Tailored data downloads

Approach:

Our services and products are used daily by thousands of professionals from around the world. If you are in need of information on the alternative assets industry then we can help.

Our information is drawn from as many sources as possible, with our large teams of dedicated analysts working to ensure that our research is far reaching, detailed and up to date.

A large proportion of our research and data is exclusive to Preqin, and is not available anywhere else.

If you want any further information, or would like to apply for a no-obligation free trial to any of our products please contact us.

Contact:

London:

Scotia House
33 Finsbury Square
London EC2A 1BB

Tel: +44 (0)20 7065 5100
Fax +44 (0)870 0330 5892

New York:

230 Park Avenue
10th Floor
New York
NY 10169

Fax: +1 212 808 3008
Tel: +1 440 445 9595

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

More info: please email info@preqin.com
Press enquiries: please contact press@preqin.com