

Preqin Special Report:

Alternatives Investment Consultants

November 2010



Alternatives Investment Consultants: Changing Market, Changing Role?

As we move towards the end of 2010, a number of new trends are emerging within the various strands of the alternatives industry. While conditions are starting to improve in a number of different ways, it is clear that a return to the status quo of recent years is extremely unlikely, with the approach institutional investors take towards alternatives having undergone a radical and possibly permanent shift. Investors' experiences of the downturn have altered the way that they review existing and potential new alternative investment manager relationships, with their consultants playing a vital role in this new dynamic.

The Fundraising Trail

Similar patterns have been seen across all the various areas of the alternatives landscape with regards to managers' ability to raise new capital for their vehicles. Following the onset of the global economic downturn, private equity, real estate and infrastructure funds all saw a decline in new fundraising, while the hedge fund industry was hit with redemptions. In more recent months excellent performance from hedge funds has reignited institutional enthusiasm, and while the closed-end fund market has been slower to improve in terms of fund performance or new fundraising, there are some encouraging signs to be seen, with some high profile closings and slowly improving overall fundraising statistics.

A Change in Approach

While the latest statistics are certainly encouraging from an overall industry perspective, they are less useful and illuminating for those managers already out there on the road and those considering when to launch their next fundraising bid. Managers that successfully raised capital back in 2005 – 2008 will find that investor attitudes have changed considerably, with the new market dynamics requiring a considerably different approach to investor relations and fundraising. Preqin maintains a dialogue with over 6,000 institutional investors around the world. Clearly each investor has its own individual principles and approach towards investments in alternatives, but there have been some clear, discernable industry trends that have emerged over the course of the past year:

- Reduction in the number of manager relationships: Across all the various asset classes there has been a trend of reducing the number of relationships maintained.

- Increased attention to due diligence: Past performance and the proven viability of proposed strategies in the current market are being given special attention as part of an overall increase in due diligence processes. Terms and conditions are also receiving increased focus as investors look to take advantage of the increased power they now wield in such discussions.
- Automatic re-ups a thing of the past: The increased attention to due diligence is being applied not only to new opportunities, but also to existing relationships. Effective investor relations is more essential than ever in ensuring a high investor retention rate.

What Are the Implications?

The change in approach being taken by institutional investors has some clear implications that must be heeded by all institutional investment managers actively seeking to maintain and increase their investor base.

- Some managers will go out of business: Investors are more unforgiving than ever before, and whether it be through redemptions or an inability of funds on the road to achieve a final close, some consolidation within the alternatives industry is a certainty.
- Fundraising and investor relations require more attention: With existing relationships being more closely scrutinized and new opportunities, fundraising and IR will become a full-time function for managers, requiring increased consideration and resource.
- Opportunities for the best prepared managers are excellent: The flip-side to the shift in attitudes is that managers able to effectively communicate appealing strategies, with proven performance and a focused approach towards interacting with new and existing investors, are already enjoying success and will continue to do so.

Where Do Investment Consultants Fit In?

In the newly emerging alternatives landscape, maintaining effective communications with investment consultants represents a more vital consideration than ever before for all those involved in fund marketing and investor relations.

Alternatives Investment Consultants: Changing Market, Changing Role?

As Fig. 1 shows, the 341 investment consultants covered in the 2011 Preqin Alternative Investment Consultant Review hold discretionary or non-discretionary influence over the portfolios of thousands of institutional investors, 1,363 of which are specifically named along with their advisors in different areas within the body of the publication. In terms of sheer numbers, showcasing a fund to the appropriate investment consultants is the most effective method of showcasing a firm to a wide audience.

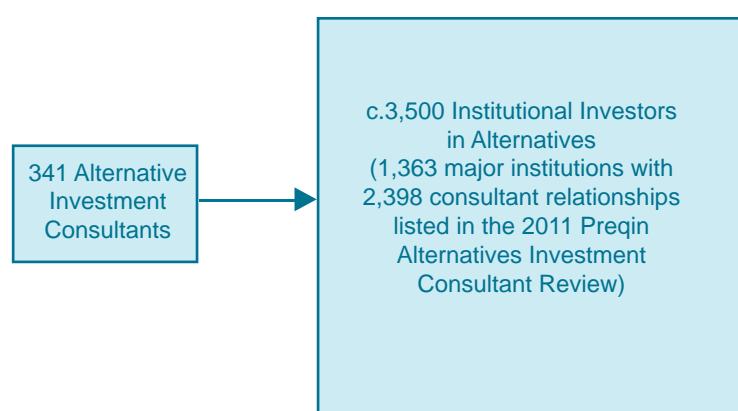
In many cases, the investment consultant represents the only method by which fund managers can gain commitments from certain investors that defer either initial screening responsibilities or sometimes entire control of certain aspects of their portfolios to their consultants. Fig. 2 shows the split of services offered by the investment consultants covered in the Review.

With investors paying closer attention towards existing and potential new relationships, more weight than ever before is being paid to the advice given by their consultants, especially in terms of making recommendations for new investments. Where consultants have previously offered a more advisory role, we are now seeing some relationships evolving to the point where consultants are being given more responsibility to make more solid recommendations, with clients retaining the ability to veto such decisions. Fund marketers and IR professionals must therefore maintain effective communications with both institutional investors and their consultants if they are to be successful in the current environment.

Considerations for Investment Consultants

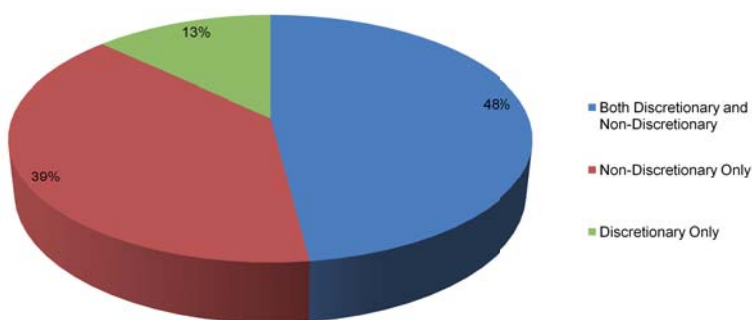
The close scrutiny placed on investors' investment manager relationships is also being seen in the attention being given towards their investment consultants.

Fig. 1: The Alternative Investment Consultant and Underlying Investor Universe



Source Preqin

Fig. 2: Breakdown of Alternatives Investment Consultants by Nature of Services Provided



Source Preqin

In order to assess investor attitudes towards their investment consultants Preqin undertook a survey of 120 leading institutional investors that make use of the services of an investment consultant for some or all of their investments in the alternatives space, the full results of which can be seen in the 2011 Preqin Alternatives Investment Consultant Review. The split of respondents is representative of the global makeup of institutional investors in alternatives by type, size, and location.

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As Fig. 3 shows, a significant 11% of institutions are very likely to be seeking out new consultants in the next 12 months, with an additional 19% stating this to be a possibility. Such sentiment raises a number of opportunities for investment consultants to attract new clients in the coming year.

Fig. 4 shows the areas in which investment consultants must focus in order to maintain good relationships with their clients and effectively attract new retainers. Investors were posed questions on performance-related issues and their investment consultant review procedure. Survey respondents were asked to rank the level of importance they place on several of the key attributes they consider when assessing and reviewing investment consultants. Each attribute was ranked on a scale of one to five, with one denoting a low level of importance and five denoting a high level of importance.

As the chart shows, track record in fund selection remains a key attribute, growing in importance even further from previous years. Another interesting trend that can be discerned in the survey results is the continuing increase in the importance paid towards value for money, with competitive price now seen as considerably more important than in 2008 when the survey was first conducted.

Fig. 3: Likelihood of Investors Seeking New or Additional Advice on Alternative Investments in the Next 12 Months

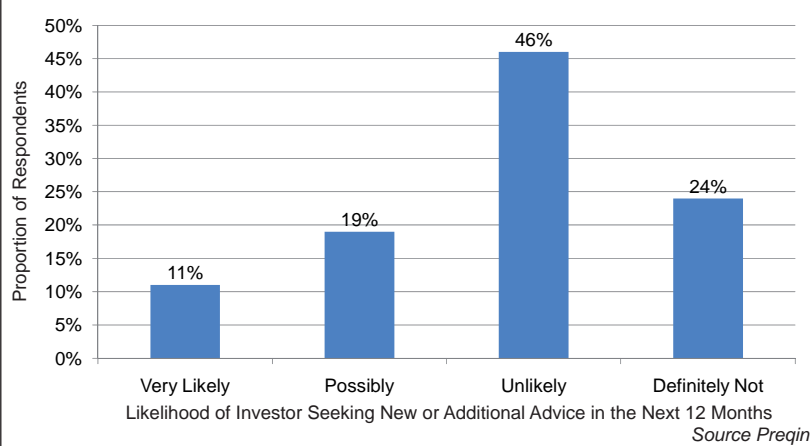
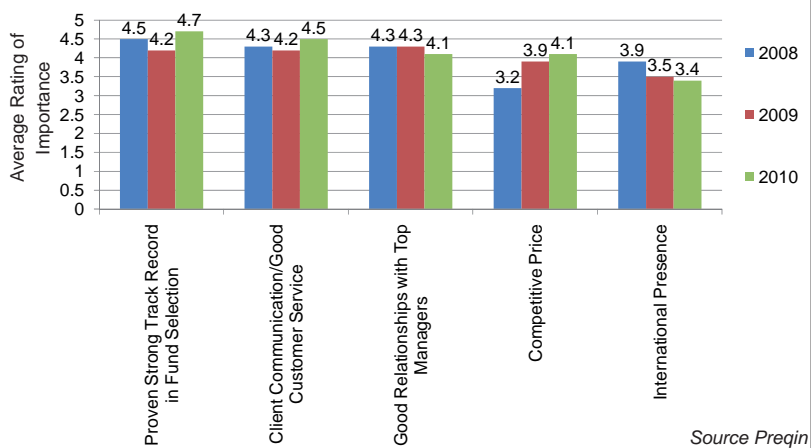


Fig. 4: Attributes Clients Consider When Reviewing Alternatives Investment Consultants



Alternatives Investment Consultants: Investment Consultant Overview

Consultant Location

- 65% of consultants that cover alternative investments are headquartered in North America. It is unsurprising that such a high proportion of firms are located in this region given that a large number of investors in alternative assets are also based in this area.
- Just over a quarter of firms are based in Europe, with the majority being located in either the UK or Switzerland.
- 6% are headquartered in Asia and Rest of World, notably in Australia. Although the demand to invest in funds in emerging markets has grown, the number of consultants headquartered in these areas has not increased to reflect this. Many of the larger, more established advisory firms headquartered in North America or Europe have instead opened offices in Asia and Rest of World.

Consultants by Number of Employees

- A breakdown of investment consulting firms by number of employees is shown in Fig. 6. 26% of firms employ between 1 and 19 employees, and the largest proportion of firms, 34%, have a staff of 20-49.
- A significant 11% employ 500 members of staff or more. Some firms seek to maintain a client-to-consultant ratio and as such will recruit consultants as their client base expands.

Fig. 5: Breakdown of Alternatives Investment Consultants by Primary Location

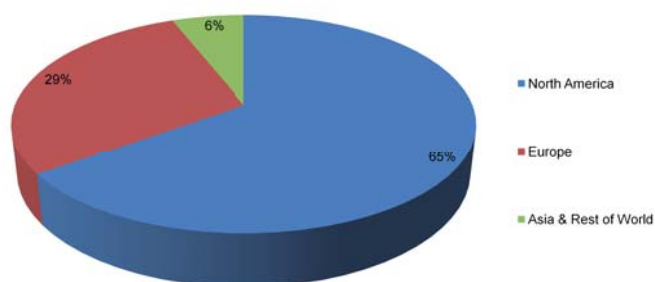
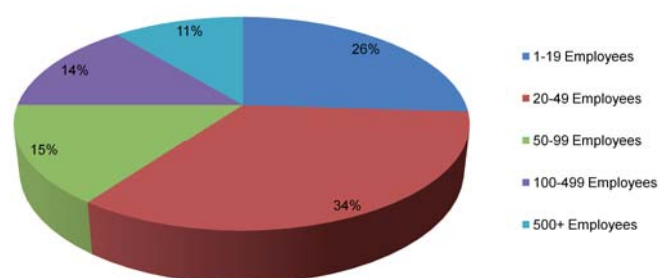


Fig. 6: Breakdown of Alternatives Investment Consultants by Number of Employees



Alternatives Investment Consultants: Investor Usage Overview

Proportion of Investors Using Consultants

- The proportion of institutional investors that use an external consultant to assist with their investments in alternatives is similar to last year, when 61% used an external consultant. As shown in Fig. 7, 60% of investors now seek advice from an investment consultant on one or more alternative asset classes within their investment portfolios.
- These external consultants could be a general consultant, advising across all asset classes, or an asset class-specific consultant employed by the investor to advise solely on private equity, real estate, infrastructure or hedge fund investments.

Proportion of Investors Using Consultants by Region

- Fig. 8 shows the proportion of investors in each region that use investment consultants to assist with their alternative investments. North American investors make the most use of investment consultants when making alternative investments; 77% of North American investors use an external consultant. This is an increase of nine percentage points from last year, when 68% of North American institutional investors in alternatives used an external consultant.
- In contrast, the proportions of investors in Europe and Asia and Rest of World that make use of a consultant for their alternative investments have declined, with only 47% and 42% of investors in these regions using consultants respectively. These two regions also had similar proportions last year; 55% of investors in Europe and 52% in Asia and Rest of World used alternative investment consultants respectively.

Fig. 7: Proportion of Investors Using Investment Consultants

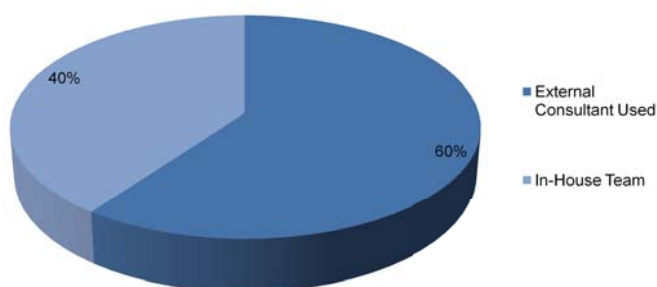
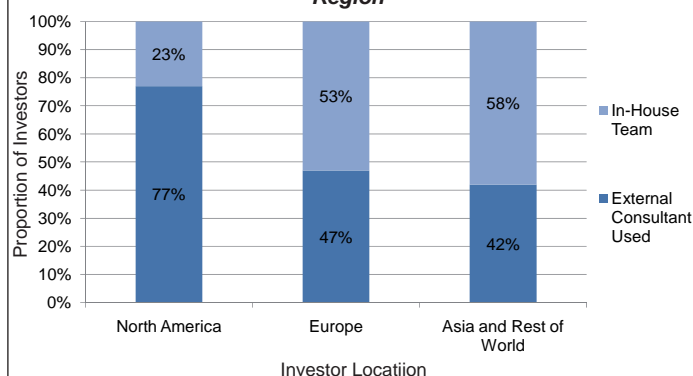


Fig. 8: Proportion of Investors Using Investment Consultants by Region



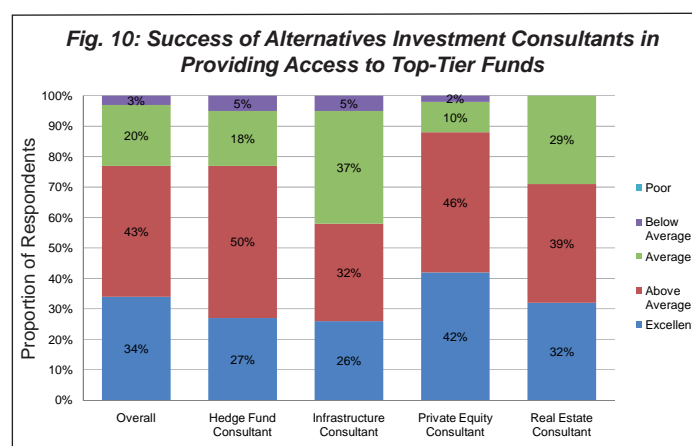
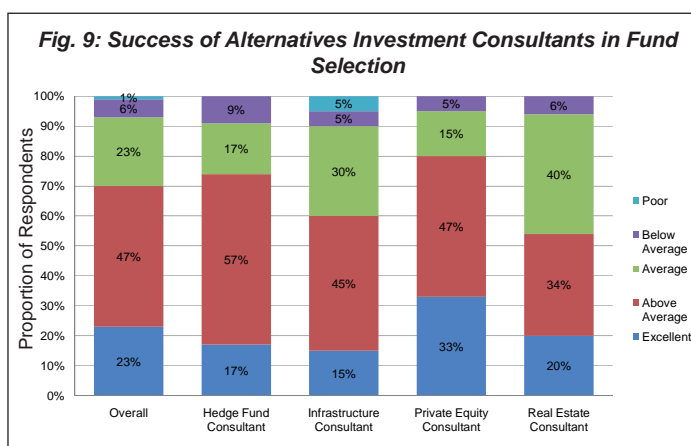
Alternatives Investment Consultants: Investor Survey

Fund Selection

- Fund selection is a key area in which investors expect their consultants to perform well. A consultant's success in this area is of the utmost importance to clients; consultants are relied upon to supply information on the most favourable investment opportunities.
- As Fig. 9 shows, 70% of investors rated their consultant's performance in this area as above average or excellent, while the figure increases to 80% when the feedback from investors on private equity consultants is considered on its own. 7% of respondents overall rated their consultant's performance as below average or poor in terms of fund selection.
- When the asset classes are considered separately, performance in this area was rated slightly less favourably by those ranking infrastructure investment consultants, with 10% stating that they felt that their consultants' success in selecting the best performing funds had been below average or poor. 9% of respondents rating hedge fund consultants also felt that their consultant's success had been below average in this area.

Access to Top-Tier Funds

- By employing an investment consultant, institutional investors can make use of the relationships the consultant has with fund managers, thus improving the chance of being able to invest in oversubscribed, top-tier funds. This is particularly valuable for smaller or newer investors.
- When asked to rate the success of their advisor in providing access to top-tier funds, 77% felt that their consultant's performance was excellent or above average, as shown in Fig. 10.
- No less than a quarter of respondents within each asset class rated their consultant's performance in this field as excellent, and the figure reached 42% for respondents that rated their private equity consultants. 5% of institutional investors rated their hedge fund and infrastructure consultants as below average, although none of those rating real estate consultants felt that their consultant's performance fell below an acceptable level.



The 2010 Preqin Alternatives Investment Consultant Review



A good source of intelligence on the alternatives investment consultant industry is a vital tool in helping fund managers and marketers build relationships with these important custodians of institutional investor capital. It is also an important consideration for consultants seeking to maintain an accurate overview of the market, and for investors utilising and considering the services of consultants.

The 2011 Preqin Investment Consultants Review is the ultimate guide to this important sector within the alternatives sphere, containing profiles for 300 different investment consultancy firms. Consultant profiles within the Review contain information on the types of services offered, asset classes covered, key financial information, direct contact information for relevant contacts and perhaps most importantly, details showing which consultants are being retained by 1,300 institutional investors from around the world.

Key features of this publication include:

- Vital analysis on all aspects of the alternatives investment consultant universe. Includes key trends plus information on the market's make-up.
- Specific intelligence on activity in private equity, real estate, hedge funds and infrastructure included in all analysis and profiles.
- Comprehensive profiles for over 300 investment consultants.
- Profiles include key individual contact information, areas of speciality, plans for 2011 and beyond, financial information, service coverage etc.
- Details for 2,400 sample clients. See who is advising whom for each area of alternatives.
- See which firms operate a buy-list, which firms consider first-time managers, and what they look for when considering new opportunities.
- Results of our in-depth survey showing investor satisfaction with their consultants and other key information.
- League tables.

More information:
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2011 Preqin Alternatives Investment Consultant Review

The **2011 Preqin Alternatives Investment Consultant Review** is a necessary guide for all fund marketers, fund managers and those in the industry looking for information on the alternative investment consultant industry.

Key content includes:

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