

Content Includes:

# Preqin Special Report: Hedge Fund Service Providers

May 2016

## Changing Service Provider

Thirty percent of surveyed hedge fund managers changed at least one service provider in 2015.

## Pricing

Do hedge fund managers believe investors are concerned with the rising cost of service providers?

## Outsourcing

Which business functions are hedge fund managers planning to outsource in 2016?

## League Tables

The leading service providers by proportion of funds and fund launches serviced.





# Foreword

As the hedge fund industry has grown and matured, third-party service providers have come to play an increasingly important role in the provision of essential services to fund managers. Following the Global Financial Crisis and the Madoff scandal, examining the length and quality of a fund manager’s service provider relationships has become an essential part of institutional investors’ due diligence processes. The push for more efficient business models has also encouraged an increasing number of fund managers to outsource more business functions to third-party providers, in order to concentrate on their core business of generating alpha for their clients.

All of these factors contribute to the growth and success of the hedge fund service provider sector, which encompasses a wide range of businesses such as fund administrators, custodians, auditors, prime brokers, legal advisors and third-party marketers. In this report, we examine the key trends in the service provider market at present, drawing on a survey of over 300 fund managers and data on over 1,300 service providers from Preqin’s **Hedge Fund Online** database.

With 30% of fund managers surveyed by Preqin having changed at least one of their service providers in the previous year, we look at which types of service providers are most likely to be changed and managers’ reasons for doing so. We also examine two of the key trends influencing hedge fund managers’ use of service providers at the moment, repricing and outsourcing, in order to see how these developments are affecting their businesses and clients. Following significant growth in the industry and consolidation among some of the major players, particularly in the fund administration space, we also look at which service providers are currently dominating their respective markets and which have been most successful at winning new business recently.

Preqin’s **Hedge Fund Online** database provides an invaluable tool to help service providers to identify new clients and to allow fund managers and investors to carry out due diligence and analyze the service provider relationships of their peers and competitors. To find out more about this and Preqin’s other services, please visit [www.preqin.com](http://www.preqin.com) or contact us at [info@peqin.com](mailto:info@peqin.com).

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## Key Facts



**30%**

Proportion of hedge fund managers that have changed at least one service provider in the past 12 months.



**40%**

The largest proportion of hedge fund managers changed service providers due to dissatisfaction with the quality of service provided.



**21%**

Proportion of hedge fund managers that have been repriced by at least one of their service providers in the past 12 months.



**30%**

Proportion of hedge fund managers that plan to outsource part of their capital-raising process in the next 12 months.



**15%**

Estimated proportion of hedge funds serviced by SS&C GlobeOp following the acquisition of Citi Alternative Investor Services, making it the largest fund administrator.



**37%**

Proportion of hedge funds launched since the beginning of 2015 serviced by Morgan Stanley Prime Brokerage.

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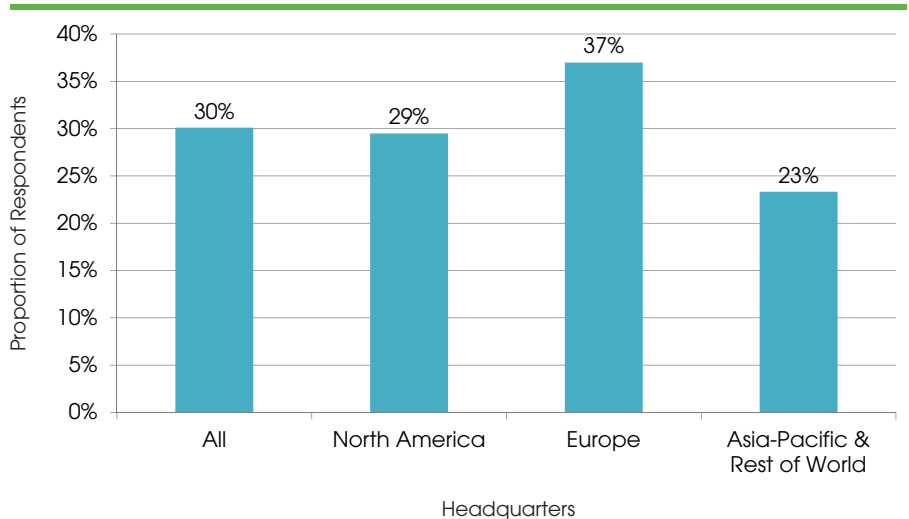
# Changing Service Provider

Although hedge fund managers will aim to establish relationships with high-quality service providers from the inception of their fund, there will be times when managers need or choose to change their counterparties. As firms grow their assets under management (AUM) and increase the number of investors that they are dealing with, they may find that some of their service providers are no longer suited to their business; equally, these managers may feel that they are not receiving an adequate service from their service provider, or need to cut costs.

Thirty percent of hedge fund managers surveyed by Preqin reported that they had changed at least one service provider in 2015 (Fig. 1). Europe-based respondents were the most likely to do so – 37% changed a service provider in the past year; in comparison, just 23% of managers based outside North America and Europe changed service providers in this time.

Fund managers most frequently changed their prime brokers and fund administrators: 39% of those that reported changing service providers in the past year changed their prime broker, while just over a third changed their fund administrators (Fig. 2). The most commonly cited reasons for changing service providers were dissatisfaction at

**Fig. 1: Hedge Fund Managers that Changed Service Provider in 2015 by Headquarters**



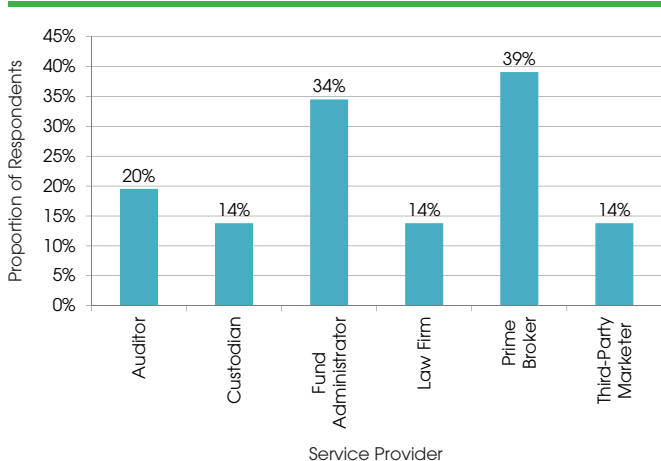
Source: Preqin Fund Manager Survey, November 2015

the quality of service provided (40%) and the cost of the service provider (31%, Fig. 3). Internal developments also played a role in fund managers' decisions – 26% of fund managers that had changed service providers stated that growth in their firm's AUM was a factor in their decision.

Fund managers were most likely to change their fund administrators, prime brokers and third-party marketers due to concerns about quality of service, and most likely to change their custodians due to the cost of the service. Respondents

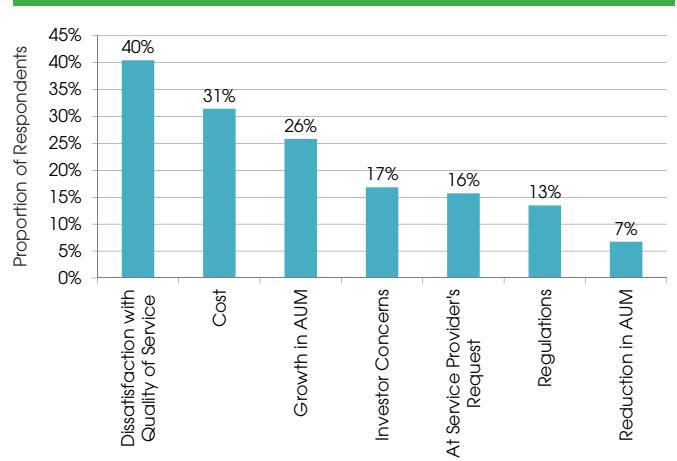
were equally likely to change their auditors due to concerns about service and costs. Law firms were the only service providers to fall outside this trend: fund managers were most likely to change their law firms due to growth in their own AUM, possibly due to the additional legal and regulatory requirements of larger firms combined with the extra legal resource needed by firms seeking capital from a broader investor base outside their home markets.

**Fig. 2: Types of Service Provider Changed by Hedge Fund Managers in 2015**



Source: Preqin Fund Manager Survey, November 2015

**Fig. 3: Reasons Why Fund Managers Changed Service Provider in 2015**



Source: Preqin Fund Manager Survey, November 2015



# Issues in Focus: Pricing and Outsourcing

Twenty-one percent of hedge fund managers reported that one of their service providers changed pricing in 2015. Of these, 52% reported that their prime broker had changed its pricing, while 34% and 32% of managers saw fees change from their fund administrators and auditors (Fig. 4).

Although practices vary widely between different fund managers, many of these costs are ultimately paid for by investors, either through management fees or specific expenses pass-through charges. Despite this, only 21% of fund managers felt that investors were concerned by the increased cost of third-party providers (Fig. 5). Forty-

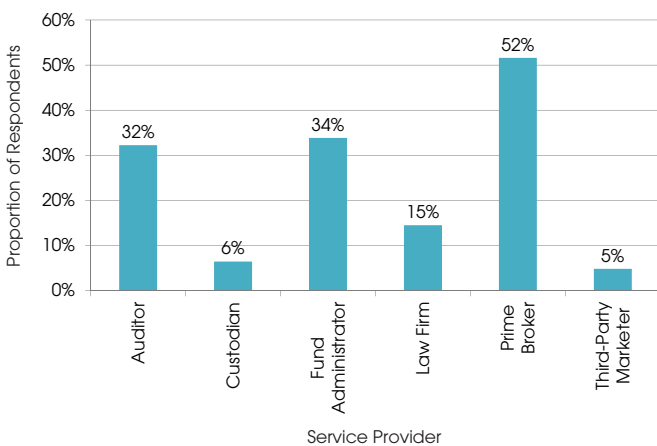
two percent were unsure whether their investors were concerned by repricing, suggesting that more dialogue is needed between parties regarding this issue, particularly given the large number of investors that have expressed concerns about fees. As shown in the **2016 Preqin Global Hedge Fund Report**, 46% of institutional investors are seeking further reductions in hedge fund management fees over the course of 2016.

Fund managers remain focused on their core competencies of portfolio management and investor relations, with the vast majority of respondents choosing to keep these functions purely in-house (Fig. 6). Managers are much

more likely to make use of outsourcing for their IT and legal/compliance teams, with a significant proportion making use of some third-party providers to assist with their middle and back office functions.

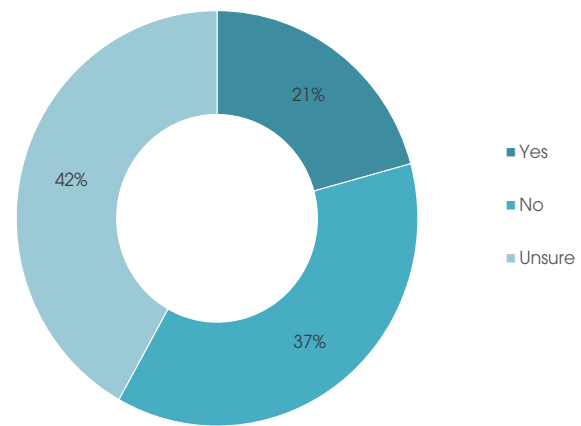
Fund managers will continue to seek to establish new relationships with third-party providers and a significant number will look to outsource various office functions in the year ahead. Thirty percent of fund managers surveyed planned to outsource some elements of their capital-raising process in the next year, with 28% aiming to outsource NAV calculations (Fig. 7).

**Fig. 4:** Hedge Fund Managers that Have Seen a Change in the Price of Services by Service Provider Type



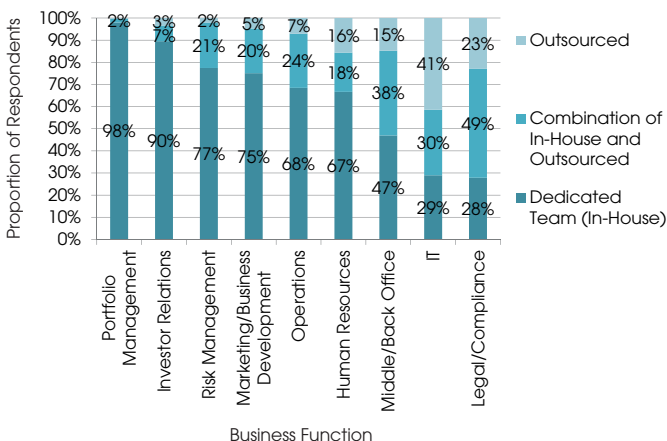
Source: Preqin Fund Manager Survey, November 2015

**Fig. 5:** Hedge Fund Managers' Views on Whether Investors Are Concerned by the Increased Cost of Service Providers



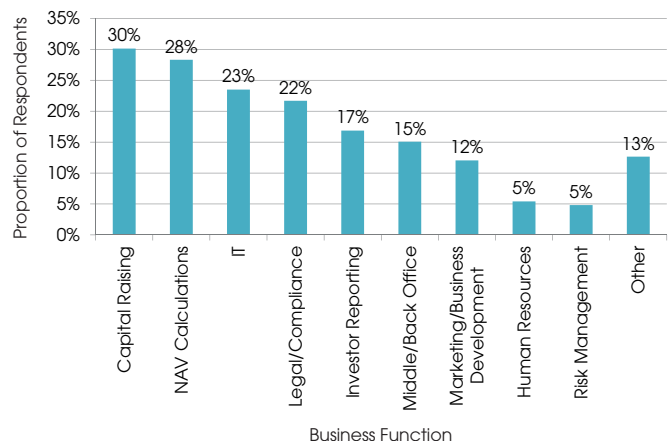
Source: Preqin Fund Manager Survey, November 2015

**Fig. 6:** Business Functions Outsourced by Hedge Fund Managers



Source: Preqin Fund Manager Survey, November 2015

**Fig. 7:** Hedge Fund Managers' Plans for Outsourcing in 2016 by Business Function



Source: Preqin Fund Manager Survey, November 2015



# League Tables

**Fig. 8:** Top Five Fund Administrators Servicing Hedge Funds

| Firm                                       | Proportion of Hedge Funds Serviced |
|--|------------------------------------|
| SS&C GlobeOp*                              | 15%                                |
| Citco Fund Services                        | 12%                                |
| International Fund Services (State Street) | 9%                                 |
| BNY Mellon                                 | 5%                                 |
| Morgan Stanley Fund Services               | 5%                                 |

Source: Preqin Hedge Fund Online

**Fig. 9:** Top Five Fund Administrators by Proportion of Hedge Fund Launches Serviced, 2015 - Q1 2016

| Firm                                       | Proportion of Hedge Fund Launches Serviced, 2015 - Q1 2016 |
|--|--|
| SS&C GlobeOp*                              | 17%  |
| Citco Fund Services                        | 9%   |
| HedgeServ                                  | 9%   |
| Morgan Stanley Fund Services               | 7%   |
| International Fund Services (State Street) | 6%   |

Source: Preqin Hedge Fund Online

**Fig. 10:** Top Five Fund Administrators by Proportion of CTAs Serviced

| Firm                               | Proportion of CTAs Serviced |
|------------------------------------|-----------------------------|
| NAV Consulting                     | 12%                         |
| SS&C GlobeOp*                      | 10%                         |
| CACEIS                             | 6%                          |
| Citco Fund Services                | 5%                          |
| Northern Trust Fund Administration | 4%                          |

Source: Preqin Hedge Fund Online

**Fig. 11:** Top Five Custodians Servicing Hedge Funds

| Firm                              | Proportion of Hedge Funds Serviced |
|-----------------------------------|------------------------------------|
| J.P. Morgan                       | 31%                                |
| Goldman Sachs                     | 29%                                |
| Morgan Stanley                    | 22%                                |
| BNY Mellon                        | 17%                                |
| Credit Suisse Prime Fund Services | 13%                                |

Source: Preqin Hedge Fund Online

**Fig. 12:** Top Five Custodians by Proportion of Hedge Fund Launches Serviced, 2015 - Q1 2016

| Firm                            | Proportion of Hedge Fund Launches Serviced, 2015 - Q1 2016 |
|---------------------------------|--|
| Goldman Sachs                   | 29%  |
| Morgan Stanley                  | 27%  |
| J.P. Morgan                     | 19%  |
| BNY Mellon                      | 14%  |
| Northern Trust Custody Services | 11%  |

Source: Preqin Hedge Fund Online

\* Estimated following SS&C GlobeOp's acquisition of Citi Alternative Investor Services, completed in March 2016.



**Fig. 13:** Top Five Prime Brokers Servicing Hedge Funds

| Firm                              | Proportion of Hedge Funds Serviced |
|-----------------------------------|------------------------------------|
| Goldman Sachs                     | 36%                                |
| Morgan Stanley Prime Brokerage    | 29%                                |
| J.P. Morgan                       | 23%                                |
| Credit Suisse Prime Fund Services | 17%                                |
| UBS Prime Services                | 13%                                |

Source: Preqin Hedge Fund Online

**Fig. 14:** Top Five Prime Brokers by Proportion of Hedge Fund Launches Serviced, 2015 - Q1 2016

| Firm                           | Proportion of Hedge Fund Launches Serviced, 2015 - Q1 2016 |
|--------------------------------|--|
| Morgan Stanley Prime Brokerage | 37%  |
| Goldman Sachs                  | 34%  |
| J.P. Morgan                    | 18%  |
| UBS Prime Services             | 11%  |
| Interactive Brokers            | 11%  |

Source: Preqin Hedge Fund Online

**Fig. 15:** Top Five Auditors Servicing Hedge Funds

| Firm     | Proportion of Hedge Funds Serviced |
|----------|------------------------------------|
| KPMG     | 26%                                |
| EY       | 23%                                |
| PwC      | 21%                                |
| Deloitte | 12%                                |
| RSM      | 4%                                 |

Source: Preqin Hedge Fund Online

**Fig. 16:** Top Five Law Firms by Proportion of Onshore Hedge Funds Serviced

| Firm                     | Headquarters   | Proportion of Onshore Hedge Funds Serviced |
|--------------------------|----------------|--|
| Seward & Kissel          | US             | 10%  |
| Schulte Roth & Zabel     | US             | 7%   |
| Maples & Calder          | Cayman Islands | 6%   |
| Sidley Austin            | US             | 5%   |
| Elvinger, Hoss & Prussen | Luxembourg     | 4%   |

Source: Preqin Hedge Fund Online

**Fig. 16:** Top Five Law Firms by Proportion of Offshore Hedge Funds Serviced

| Firm                 | Headquarters   | Proportion of Offshore Hedge Funds Serviced |
|----------------------|----------------|---|
| Maples & Calder      | Cayman Islands | 21%   |
| Walkers              | Cayman Islands | 12%   |
| Schulte Roth & Zabel | US             | 9%  |
| Seward & Kissel      | US             | 8%  |
| Ogier                | Jersey         | 8%  |

Source: Preqin Hedge Fund Online



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# Preqin Special Report: Hedge Fund Service Provider

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## Preqin: Global Data and Intelligence

With global coverage and detailed information on all aspects of the hedge fund asset class, Preqin's industry-leading **Hedge Fund Online** service keeps you up-to-date on all the latest developments across the hedge fund universe.

### Source new investors for funds

Find the most relevant investors, with access to detailed profiles for over 5,000 institutional investors actively investing in hedge funds, including insurance companies, pension funds, family offices, foundations, wealth managers, endowment plans, banks, fund of hedge funds managers and more.

### Identify potential investment opportunities

View in-depth profiles for hedge funds seeking capital, including information on investment strategy, geographic focus, structure, service providers used, sample investors, direct contact information and more.

### Find active fund managers of hedge funds

Search for firms operating hedge funds. View information on key contacts, assets under management, performance history, key investment preferences, known investors and more.

### Benchmark performance

Identify which fund managers have the best track records with fully customizable performance benchmarks, and view performance details on individual named funds and share classes.

### Examine fund terms and conditions

Access fund-by-fund and industry level fund terms and conditions data for individual hedge funds, which provide a market overview, enabling you to see the current trends for specific strategies, structures, sizes and more.

### View detailed profiles of service providers

Search for active administrators, custodians, prime brokers, auditors and law firms by type and location of funds and managers serviced. Customize league tables of service providers by type, location of headquarters, and total known number of funds serviced.

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