Mid-Year Survey of Hedge Fund Investor Sentiment

Summer 2017

Credit Suisse Capital Services
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For more information on this survey or on our Prime Services business generally, please contact:

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Part I - Introduction and Executive Summary

Overview

As an extension to our Annual Global Hedge Fund Investor Sentiment Survey conducted in January, where investors indicated that they remained committed to hedge funds and optimistic about the industry’s performance, we wanted to take a fresh look at investors’ current appetite at the mid-year point as well as their levels of interest going forward.

In addition to looking at preferred strategies / regions and allocation plans for the second half of 2017, we also wanted to understand the pulse of investors around the current interest in quantitative strategies as well as the continuing new alignment discussion.

Our Mid-Year Survey of Hedge Fund Investor Sentiment indicates continued appetite to allocate to hedge funds in the second half of the year as well as increased interest in quantitative strategies in the medium-term. The survey also shows that the new alignment discussion continues, with more LP-friendly structures and terms being employed by managers.

Our survey polls over 200 respondents representing nearly $660 billion in hedge fund investments.

Investors from all regions participated with a breakdown as follows:

<table>
<thead>
<tr>
<th>Region</th>
<th>Number of Responses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Americas</td>
<td>127</td>
</tr>
<tr>
<td>EMEA</td>
<td>47</td>
</tr>
<tr>
<td>APAC</td>
<td>38</td>
</tr>
<tr>
<td>Total</td>
<td>212</td>
</tr>
</tbody>
</table>

INVESTOR BREAKDOWN
By AuM (in $USD)

INVESTOR BREAKDOWN
By number of responses
Executive Summary

- **Realignment of interests in the hedge fund space continues**, with hurdle rates and founder’s share class structures in more than 70% of investor portfolios. The most valued fee structures amongst investors – hurdle rates and manager AUM based sliding fee scale – are not always found in their portfolios, indicating **there is still room for further alignment**.

- Quantitatively focused strategies are top of mind for the majority of investors, with nearly 60% indicating they plan to increase allocations to the strategy over the next 3-5 years.

- Looking ahead, **81% of investors said they would likely make allocations to hedge funds during 2H 2017**, an increase of 8% from our 2016 Mid-Year Survey. **EMEA showed the largest rebound in hedge fund allocation appetite** from last year (up 20%).

- **Hedge funds saw the largest positive swing in net demand for any asset class surveyed this year**, with investors reporting +12% net demand for hedge funds in their asset allocation models. This compares favorably with last year, when investors indicated -3% net demand for hedge fund allocations.

- Of those investors who redeemed from hedge funds during the first half of the year, **87% expect to recycle that capital (up from 82% in 2016)** to other hedge fund managers rather than other asset classes (9% reported being undecided as to where to allocate the recycled capital).

- **Top 3 strategies identified for potential 2H 2017 allocations** are Equity Long / Short, Global Macro - Discretionary, and Quantitative - Equity Market Neutral / Statistical Arbitrage. **Strategy preferences across the regions were very much in-line**, with all regions placing Equity Long / Short as their first choice.

- **Investor interest by region for the second half of 2017 proved to be very similar to what we saw in our 2016 Mid-Year Survey**. Investors indicated an appetite for Global strategies, Developed Europe (Ex-UK), North America, and Asia-Pacific (ex-Japan).

- **All alternate vehicles (structures different from traditional Master/Feeder) grew in interest from last year**, with Co-Investments and Risk Premia the most preferred.
Part II – Reflecting on 1H 2017 and Second Half Forecast

Alignment of Interest

What is the frequency of use in your portfolio for the following fee structures? Which do you value most?

- Hurdles rates (79%), founder’s share class (71%), and reduced fees for longer lock-up (66%) are the most frequently used fee structures.
- Although only coming into play in late 2016, the 1 or 30 fee structure model is already in 14% of investor portfolios.
- The most valued fee structures amongst investors are hurdle rates (96%), manager AUM based sliding fee scale (90%), and founder’s share class (88%); indicating there is still room for further alignment amongst investors and managers.

How do fee structures compare across investor types?

<table>
<thead>
<tr>
<th></th>
<th>Pension</th>
<th>EAF</th>
<th>FOF</th>
<th>Adv/Cons</th>
<th>Fam. Office</th>
<th>All</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hurdle rate</td>
<td>83%</td>
<td>67%</td>
<td>77%</td>
<td>71%</td>
<td>85%</td>
<td>79%</td>
</tr>
<tr>
<td>Founder’s class</td>
<td>42%</td>
<td>73%</td>
<td>82%</td>
<td>60%</td>
<td>73%</td>
<td>71%</td>
</tr>
<tr>
<td>Longer lock-up</td>
<td>36%</td>
<td>100%</td>
<td>59%</td>
<td>69%</td>
<td>78%</td>
<td>66%</td>
</tr>
<tr>
<td>Sliding fee scale</td>
<td>58%</td>
<td>87%</td>
<td>57%</td>
<td>60%</td>
<td>58%</td>
<td>62%</td>
</tr>
<tr>
<td>Larger ticket</td>
<td>100%</td>
<td>53%</td>
<td>57%</td>
<td>67%</td>
<td>33%</td>
<td>56%</td>
</tr>
<tr>
<td>Loyalty structure</td>
<td>18%</td>
<td>53%</td>
<td>30%</td>
<td>38%</td>
<td>17%</td>
<td>33%</td>
</tr>
<tr>
<td>1 or 30</td>
<td>18%</td>
<td>14%</td>
<td>15%</td>
<td>7%</td>
<td>11%</td>
<td>14%</td>
</tr>
</tbody>
</table>

- Utilization of fee structures varied considerably amongst the investor universe.
- Pensions tended to frequently utilize larger ticket discounts in their portfolios, while endowments & foundations took advantage of longer lock-up discounts.
- Given their tendency to allocate to new / emerging managers, fund of funds were the most frequent users of founder’s share class opportunities.
How do you anticipate your capital allocation to quantitative strategies will change over the next 3-5 years?

- Over the next 3-5 years, **57% of investors plan to significantly / moderately increase their allocation to quantitative strategies.**
- Over **20%** do not plan to have any allocation to quantitative strategies.

Which investors are most likely to increase allocations to quantitative strategies?

- **Pensions and Advisors / Consultants** showed the largest interest in quantitative strategies, with 67% and 63%, respectively, stating they plan to increase allocations over the next 3-5 years.
- Fund of Funds, Family Offices, and Endowments & Foundations were in a tight band of 53%-55%.
**Hedge Fund Allocation Plans for 2H 2017**

**How likely are investors to allocate capital to hedge funds in 2H 2017?**

- **81% of investors stated they are very likely / likely to allocate to hedge funds** in 2H 2017; up 8% from their indications for 2H 2016.

  - **EMEA witnessed the largest rebound in appetite from last year** (up 20%).
  - **Fund of Funds (86%), Family Offices (84%), and Advisor / Consultants (82%)** expressed the most interest in likely 2H 2017 hedge fund allocations.

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How has net investor demand changed by asset class since last year?

- Hedge funds saw the largest positive swing in net demand for any asset class surveyed this year, with investors reporting +12% net demand for hedge funds in their asset allocation models. This compares favorably with last year, when investors indicated -3% net demand for hedge fund allocations.

- The most significant net demand for hedge fund asset allocations came from Advisors / Consultants, Endowments & Foundations, and Fund of Funds.

- Allocations to cash declined, as investors likely put money to work in other asset classes.
Reallocation of Capital

Will investors reallocate redeemed capital to hedge fund managers?

- Yes, allocate to new managers: 19%
- Yes, reallocate to existing managers: 5%
- Yes, combination of both: 63%
- No, we do not intend to reallocate to hedge funds: 3%
- Undecided if we intend to reallocate to hedge funds: 9%

87% intend to recycle redeemed capital to hedge funds.

Reallocations to hedge funds – 2016 and 2017

- For investors who redeemed in the first half of 2017, 63% intend to recycle that capital to a combination of both existing and additional hedge fund managers. 19% of investors said that they intend to recycle those allocations by adding hedge fund managers, while 5% intend to reallocate to existing managers already in their portfolios.

- 87% of investors intend to recycle redeemed capital to other hedge funds, up 5% from our Mid-Year 2016 survey.
2H 2017 Investor Interest for Strategies, Regions, and Products

Which strategies have the most investor interest for 2H 2017?

- **Equity Long / Short**, **Global Macro - Discretionary**, and **Quantitative - Equity Market Neutral / Statistical Arbitrage** were the top ranked strategies by interest going forward in our Mid-Year Survey.

2017 Annual Investor Survey Results – Strategy Appetite

Top Strategies in the 2017 Annual Investor Survey (January 2017)

1. Global Macro - Discretionary
2. Fixed Income Arbitrage
3. Emerging Market Equity
4. Equity Market Neutral - Quantitative
5. Equity Sector - Healthcare

Compared to our 2017 Annual Investor Survey which was conducted in January, investor interest by strategy for the second half of the year still favored many of the same strategies, with the exception of **Fixed Income Arbitrage, which had less investor interest** than at the beginning of the year.
Compared to last year when we saw more dispersion in investor strategy appetite between regions, there is more commonality this year.

- Equity Long / Short was the favored strategy across all three regions.
- Global Macro - Discretionary, Quantitative - Equity Market Neutral / Statistical Arbitrage, and Emerging Markets - Equity were each favored by two regions.
Investor interest by region for the second half of the year proved to be very similar to what we saw in our 2016 Mid-Year Survey with a slight change in order.

The top regions were once again a Global focus, Developed Europe (ex-UK), North America, and Asia-Pacific (ex-Japan).

India, Greater China, Japan, and the UK received the most interest from country-specific investors.

Aside from the traditional Master/Feeder, which vehicles are of most interest in 2H 2017?

While Master/Feeder structures remain the most popular structure to utilize hedge fund strategies, all alternate approaches grew in interest from last year.

Co-Investments was the most popular alternative structure (up 9% from last year) followed by Risk Premia (up 5% from last year).