



US Investor Intentions H1 2022 **Hedge funds**

February 2022



with.
Intelligence

Introduction

A welcome return to promised good form

As 2022 takes off, With Intelligence's latest Investor Intentions survey finds hedge funds back near the top of US investors' wish lists. Don't call it a comeback? Few industry insiders would. But the industry's recent double-digit growth has proved to be a much-needed reminder that hedge funds can still deliver tangible benefits. It's a welcome development that's re-engaging investors with hedge funds.

After all, things haven't looked this good for hedge funds for several years. Over the past decade, confidence and growth dwindled, as the industry delivered mixed results at questionable prices, giving critics ammunition and clients cause for concern. Even US investors, long the industry's biggest fans, were being lured by private markets and raising serious questions about the size and role of their commitments to hedge funds.

However, as we have seen, hedge funds ended 2021 by posting another annual double-digit gain. The industry also saw its first net inflow since 2017. It's this kind of activity that's seen hedge funds gaining momentum as we roll into 2022, the third year of the pandemic. Read on to see how and why US investors are voting with their intentions.

224

US allocators surveyed
for this report

50%

Allocators increasing
their HF allocation

10.2%

HFM Global Composite
Index return in 2021

\$50m

US allocators' median target
ticket per HF manager

1 in 3

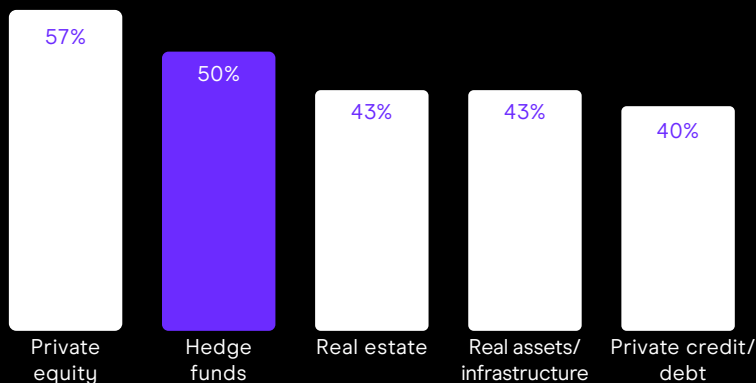
US family offices seeking
North American L/S equity

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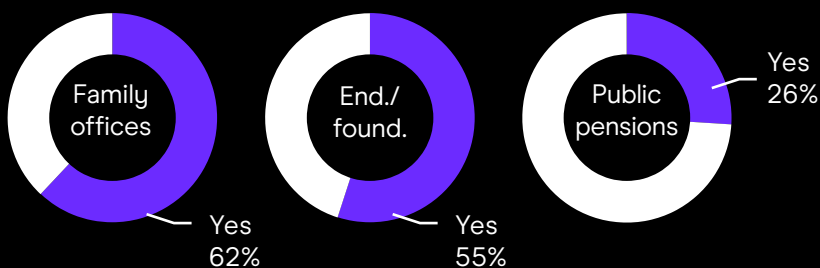
Key findings

- Half of US allocators surveyed by With Intelligence said they were likely to increase their allocation to hedge funds in the next 12 months
- Interest is being driven by family offices (62%) and foundations/endowments (55%), with the former citing equity valuation concerns
- Interest is being focused on long/short equity and multi-strategy hedge funds, particularly those with global and North American remits
- Overall, more US allocators were interested in hedge funds (50%) than all other alternative asset classes bar private equity (57%)

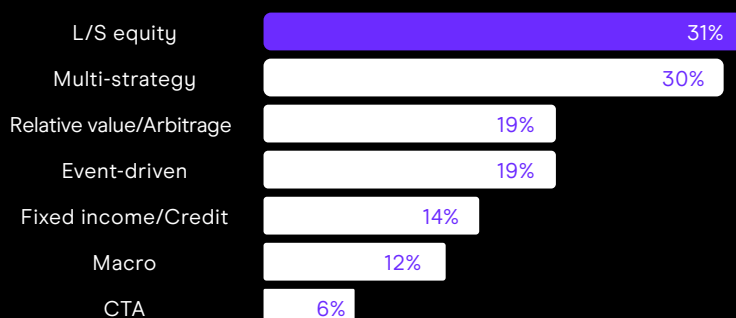
Investors likely to increase allocation to alternatives



Investors likely to increase allocation to hedge funds



Allocators interested in particular hedge fund strategies



40%

Equity valuation concerns
— top reason for increase

62%

Family offices increasing
their HF allocation

1 in 5

California-based investors
increasing to HFs

4 in 5

Illinois-based investors
increasing to HFs

1 in 10

US foundations interested
in Asia-Pacific HFs



Section 1

Overview

An exciting year ahead for a proven alternative

With Intelligence's Investor Intentions data shows many US allocators see a starring role for hedge funds in 2022. This is a welcome result for an industry that, in recent years, has played second fiddle to private market asset classes. Three years ago, many institutions were indeed adjusting their alternatives portfolios away from hedge funds. And often doing so vocally. They were making space for larger allocations to the likes of private credit and real assets. While the trend towards illiquid opportunities remains, we anticipate some positive changes with a renewed focus on hedge funds this year.

The results of With's survey of 224 US allocators (conducted in December 2021 in collaboration with AIMA), points to private equity (57%) and hedge funds (50%) as the alternative asset classes most likely to see investor inflows. Both asset classes performed strongly during the recent upheaval. Both offer timely benefits for risk management and niche opportunities. But, more than that, many allocators believe that private equity and hedge fund managers are best placed to navigate ongoing risks from rising interest rates and government

Key Statistic — US Investor Intentions

50%

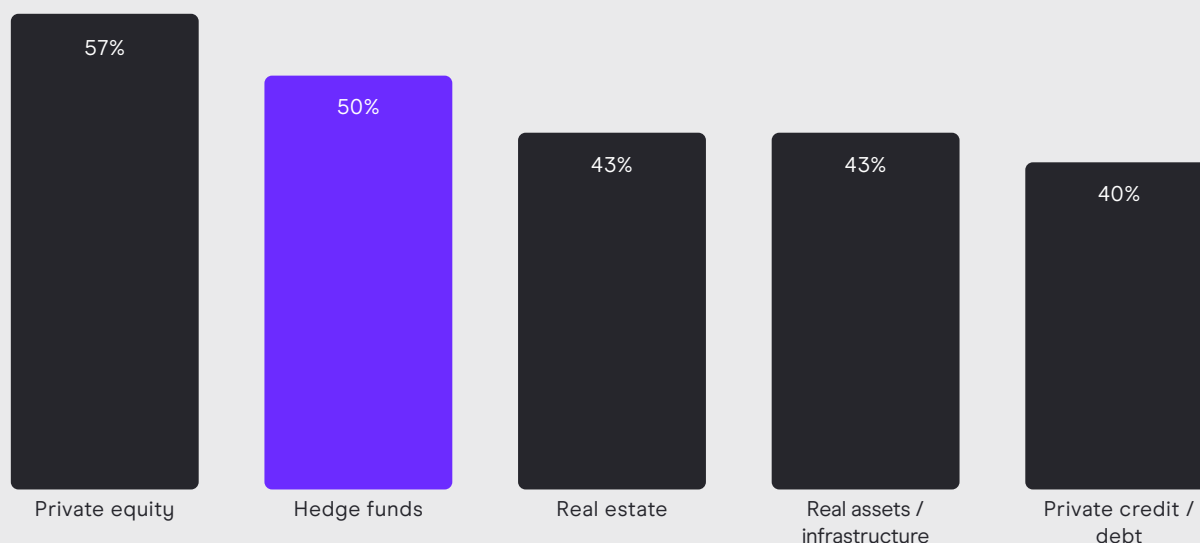
Proportion of US investors increasing their HF allocation

and central bank intervention. Because if some investors see private credit benefiting from modest rate hikes, there are also concerns that the value of real assets and real estate could be negatively impacted by property cooling measures such as tightening the loan-to-value limit, total debt servicing ratio and raising stamp duties. Hedge funds, meanwhile, have now performed strongly in each of the past three years and look well set for the challenges ahead.

A lot still depends on investor type. Family offices are the US investor group most likely to register hedge fund interest in 2022. With Intelligence's survey found more than 60% of family offices are looking to increase their allocation.

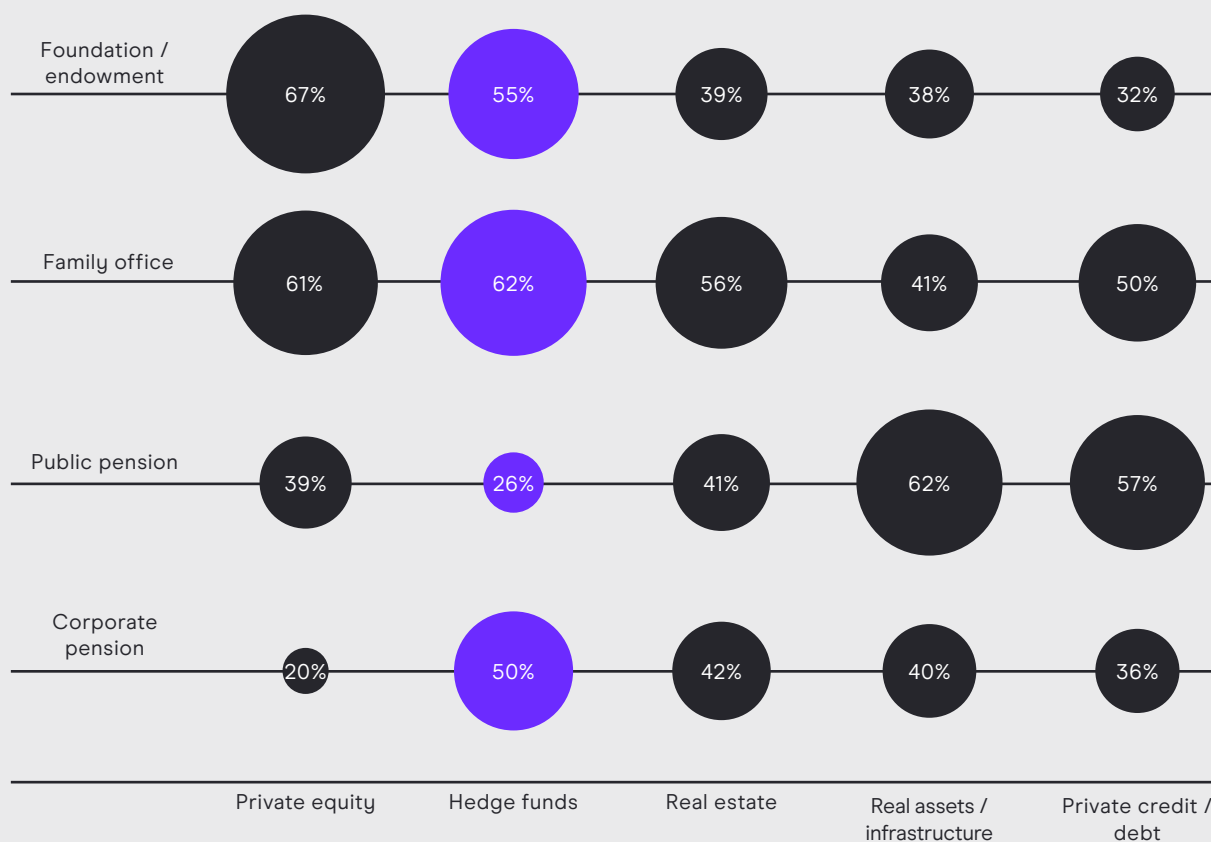
1 Proportion of US allocators surveyed likely to invest in alternative asset classes in the next 12 months

Source: With Intelligence survey, December 2021



2 Proportion of US allocators surveyed likely to invest in alternative asset classes in the next 12 months, by allocator type

Source: With Intelligence survey, December 2021



Perhaps that's unsurprising, given market conditions and the group's historical preferences. Like other allocators, family offices are concerned by the potential for anemic equity returns and a market downturn. We're now in a trading environment that seems more suited to nimble, opportunistic managers. Family offices are on average smaller sized, with a flexible structure, streamlined decision-making and higher tolerance for risk. Hedge funds can point to innate strengths and recent outperformance. Given all the above, family offices and hedge funds seem to be particularly well matched.

Other enthusiasts for hedge funds include foundations/endowments, who are staying true to their history of advocating hedge funding strategies. Also, one in two corporate pensions are likely to increase their hedge fund allocations. However, this finding came from a smaller sample size, one that also produced evidence of healthy interest in real estate, real assets and private credit.

Case study: North Dakota Board of University and School Lands

The North Dakota Board of University and School Lands made investments in two multi-strategy hedge funds in Q4 2021, aiming to reduce risk and enhance returns within a largely market neutral framework. The Bismarck-based investor awarded around \$290m each to Millennium Management and PineBridge in October 2021, following the recommendation of its consultant, RVK, to introduce a new hedge fund component to the absolute return portfolio. RVK specifically argued for market-neutral, multi-strategy funds as the preferred outcome. To make room, North Dakota cut the GMO Benchmark-Free Allocation Fund's \$400m mandate entirely due to underperformance and reduced its allocation to PIMCO.

The clear outlier when it comes to US investors' hedge fund intentions? Public pensions. Only a quarter of US public pensions surveyed said they were likely to invest in hedge funds over the next 12 months. A majority prefer real assets/infrastructure and private credit during 2022. They seem less worried about liquidity issues, seeing long-term tailwinds in these asset classes.

Concerns over equity valuations

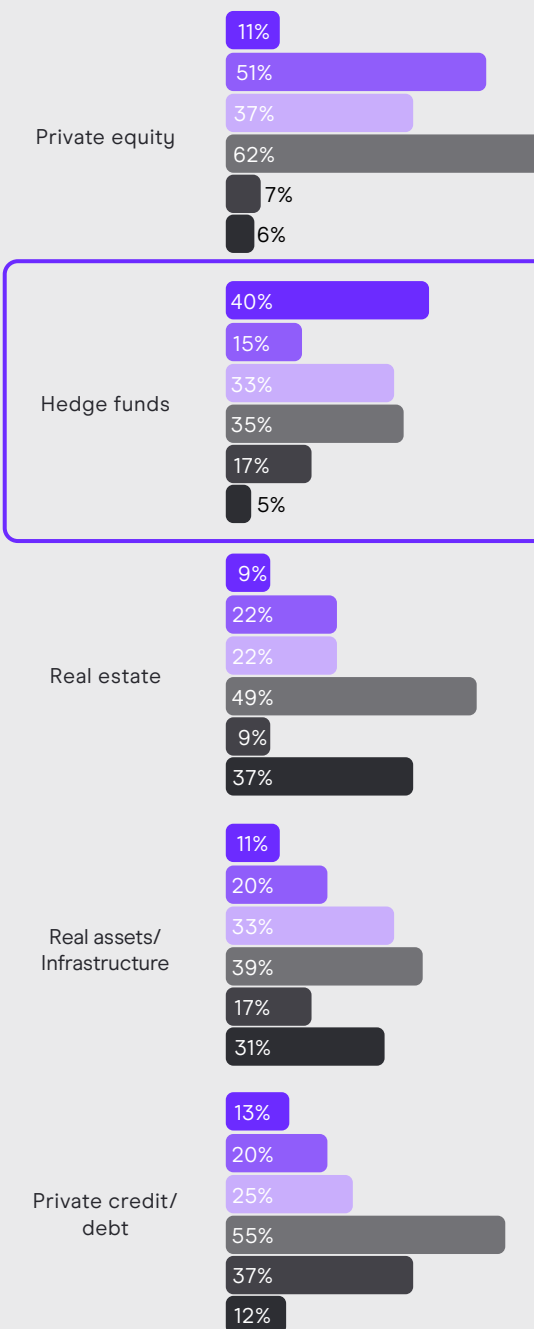
So why are US investors turning to hedge funds? The leading reason they gave was concerns over equity valuations, an issue cited by 40% of respondents, and most pronounced among family offices. The 40% showing among hedge funds was the highest score for the reason across all alternative asset classes — implying that allocators view certain hedge fund strategies as safer bets in more volatile times. However, investors concerned about rising inflation are looking at other alternative asset classes, notably real assets and real estate.

“2021 proved challenging for alpha, particularly in the long/short equity space... but we think that the year ahead is likely to be a little bit more exciting.”

Nat Kellogg, president of Chicago-based investment consultant Marquette Associates

Another conspicuous reason for interest in hedge funds (35%) is to fill a target allocation gap, but it's a weaker driver than for other asset classes. That said, it is a stronger motive for US foundations and endowments, which may have a greater capacity for working with hedge funds than other investor types do. Investing in 'exciting new opportunities' ranks as a close third for hedge funds (33%). A finding that bodes well for nimble long/short equity, event-driven and multi-strategy managers. This excitement is also a strong driver for interest in private equity and real assets.

3 Reasons that US allocators surveyed are likely to increase their allocation to alternative asset classes in the next 12 months

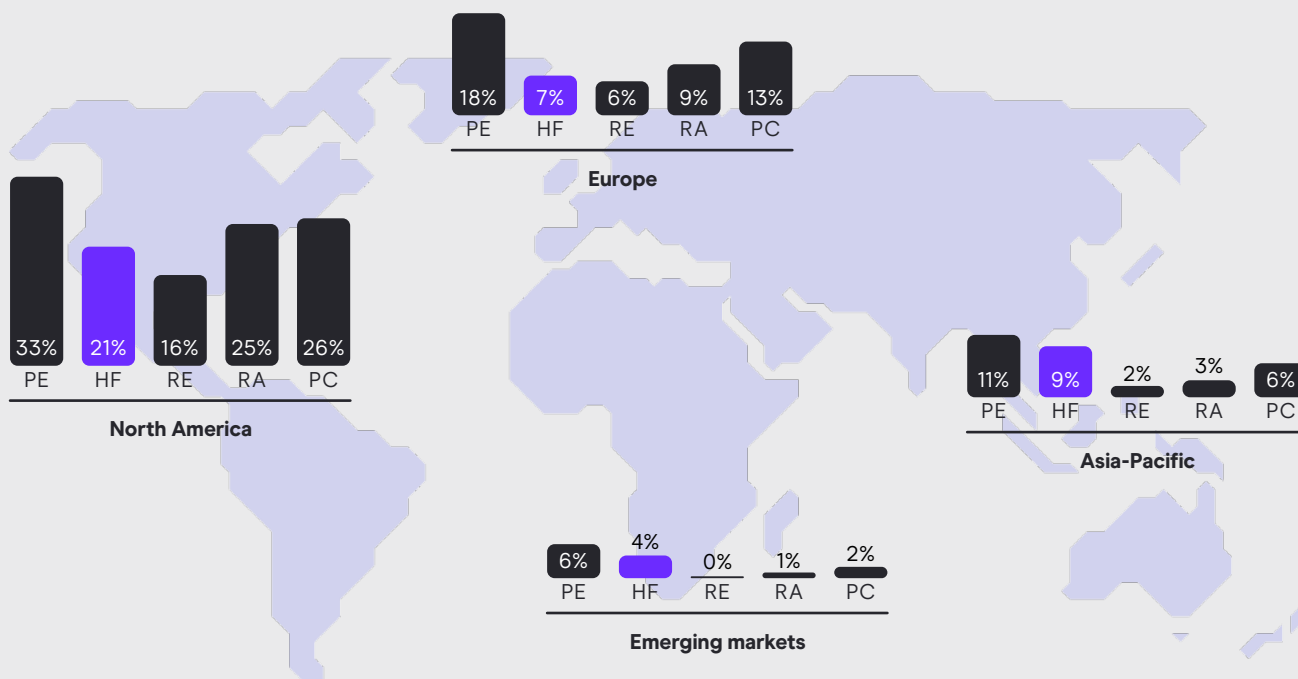


- Equity valuation concerns
- Expect strong returns
- Exciting new opportunities
- To reach target allocation
- Low fixed income yields
- Inflation concerns

Analyst note: Multiple choice question. Source: With Intelligence

4 Regions that US allocators are interested in investing in with alternative asset classes

Analyst note: Covers all US allocators surveyed, including those not likely to increase their allocation to a particular asset class. Sourced from With Intelligence survey, December 2021. Interest in 'Global' strategies was recorded but is not featured in this chart.



“We pass on a million things we really like. The stars really have to align for an investment to get across the finish line!”

Director of investments at an East Coast college

Research methodology

With Intelligence surveyed hundreds of US allocators in December 2021, yielding intentions data from 224 different entities. A plurality of respondents were from foundations and endowments, followed by family offices and public pension funds. For further details on the research methodology and respondent pool, read the methodology section on page 22.

Looking away from hedge funds, our survey results suggest US investors are most likely registering their interest in alternative assets so they can reach unfulfilled target allocations. This suggests that private equity, real estate and private credit/debt are seen as good risk diversifiers. Private equity is also notable for the 51% of US investors who are increasing their allocation because they expect strong returns from the asset class in 2022. This is more than twice the score of any other asset class in this category. This reason's highest score otherwise was 22% for real estate.

Viewing our survey by region, North America is, as expected, the preferred investment destination for most US-based alternatives allocators. This is especially true for those allocators focused on private equity, real estate and private credit/debt. While US investors in hedge funds prefer to invest globally (29%), followed by North America (22%), Europe does interest some investors seeking private equity and private credit opportunities. But when it comes to hedge funds, only 7% of US investors surveyed were interested in Europe.



Section 2

Hedge funds

Momentum regained

With Intelligence research suggests that US investor interest in hedge funds is back at levels seen in December 2020, recovering from a mid-2021 dip caused partly by topmy equity markets and questionable alpha generation in H1. Last year's 10% industry return breaks down roughly as 9% in H1 and 1% in H2 — and this growth might be considered as more forward-looking to 2022, rather than being a direct endorsement of recent returns. However, the completion of consecutive years of double-digit returns has no doubt positioned hedge funds more favorably for positively inclined investors.

Still, 12 months of high asset valuations, low interest rates and cheap money have made most alternative asset classes more attractive to US investors. There have been steady increases also in the proportions seeking private equity and real assets, and minimal change from a high base in those seeking real estate and private credit.

Key Statistic — Intentions by Investor Type

62%
Family offices

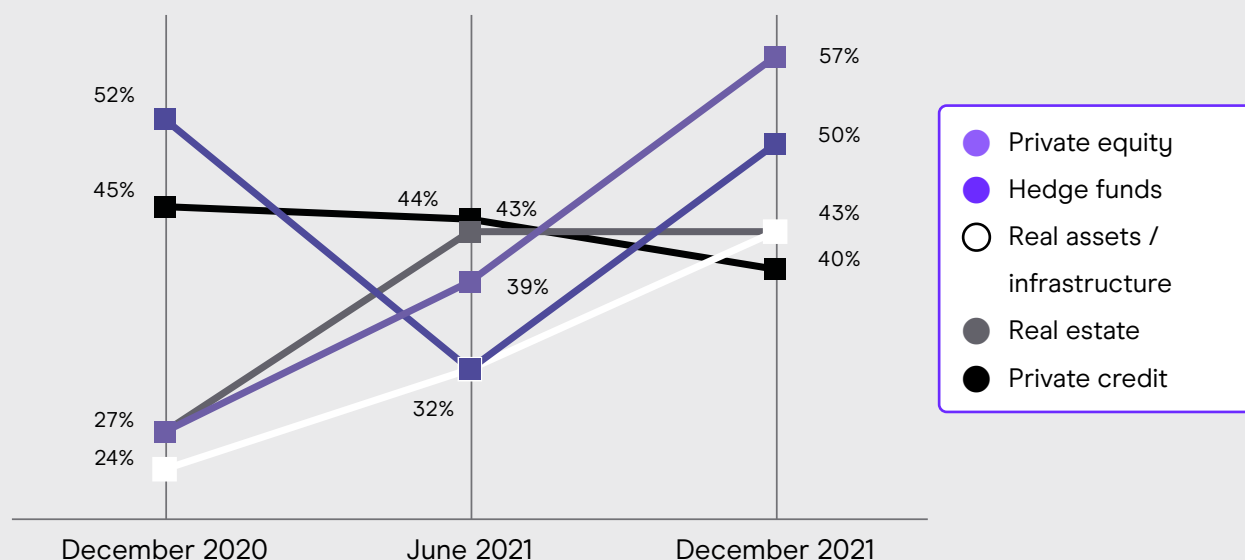
55%
Foundations /
Endowments

50%
Corporate pensions

Source: With Intelligence

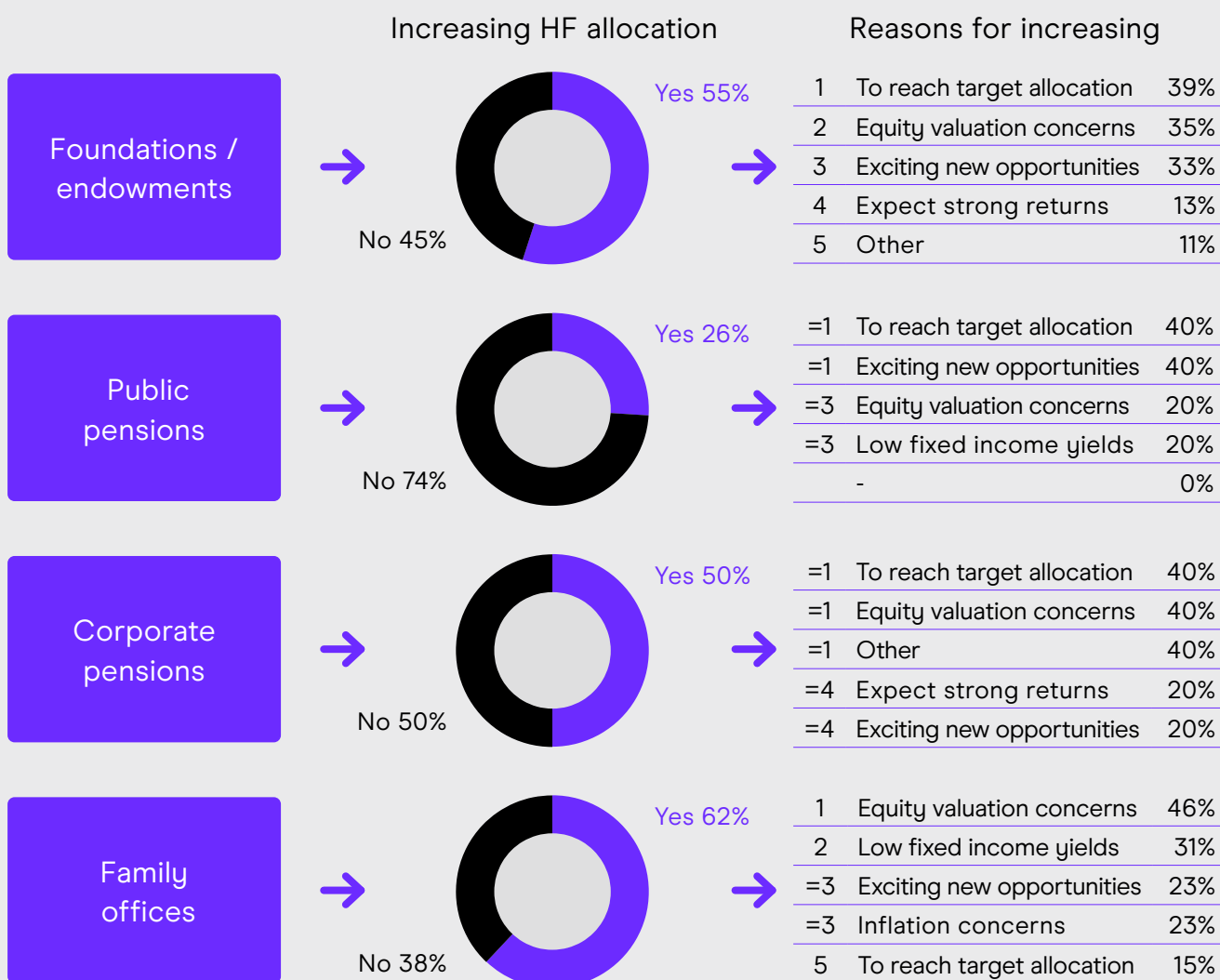
5 Proportion of US allocators surveyed increasing their allocation to alternative asset classes in the next 12 months, December 2020 to December 2021

Analyst note: Data points for June 2021 and December 2020 are for North America. Surveys from June 2021 and December 2020 referenced 'Natural resources / Infrastructure' instead of 'Real assets / Infrastructure'. Sourced from With Intelligence.



6 Top reasons US allocators are increasing their allocation to hedge funds

Analyst note: Survey respondents could select multiple options from: To reach target allocation, Expect strong returns, Exciting new opportunities, Equity valuation concerns, Low fixed income yields, Inflation concerns, and Other. Covers only those allocators likely to increase their allocation to a particular asset class. Sourced from With Intelligence survey, December 2021



Case study: Florida SBA

The Florida State Board of Administration (SBA) is seeking relative value, diversifying credit and, potentially, macro hedge fund managers, after increasing its target allocation to hedge funds in early 2021. The Tallahassee-based treasury, which oversees the \$204bn Florida Retirement System and other local funds, has gone the past 12 months without hiring new managers after increasing its internal team in the strategic investments asset class, and remains keen to reach its adjusted target allocation. Hedge funds sit within SBA's strategic investments asset class where it allocates 9.4% (\$19bn).

“We continue to look for attractive relative value managers, there aren't that many around, but we like that because it can offer uncorrelated returns.”

Trent Webster, Head of Strategic Investments, Florida SBA

Despite investors' ongoing interest in private markets, hedge funds remain well placed, particularly with foundations/endowments and family offices. Equity valuations are a prominent concern for these kinds of investors, and this has helped make long/short equity the most sought-after hedge fund strategy overall (31%).

For institutional investors, increased appetites for long/short equity investments are borne out of lingering geopolitical tensions and the coronavirus pandemic — these global issues have distorted valuations and created challenges around traditional asset investing. For smaller investors, like family offices, high valuations and market uncertainty are factors, exacerbated by the challenges they face accessing some of the larger private market and real asset opportunities that could help them combat low fixed income yields.

Key Statistic — Hedge Fund Strategy Intentions

48%

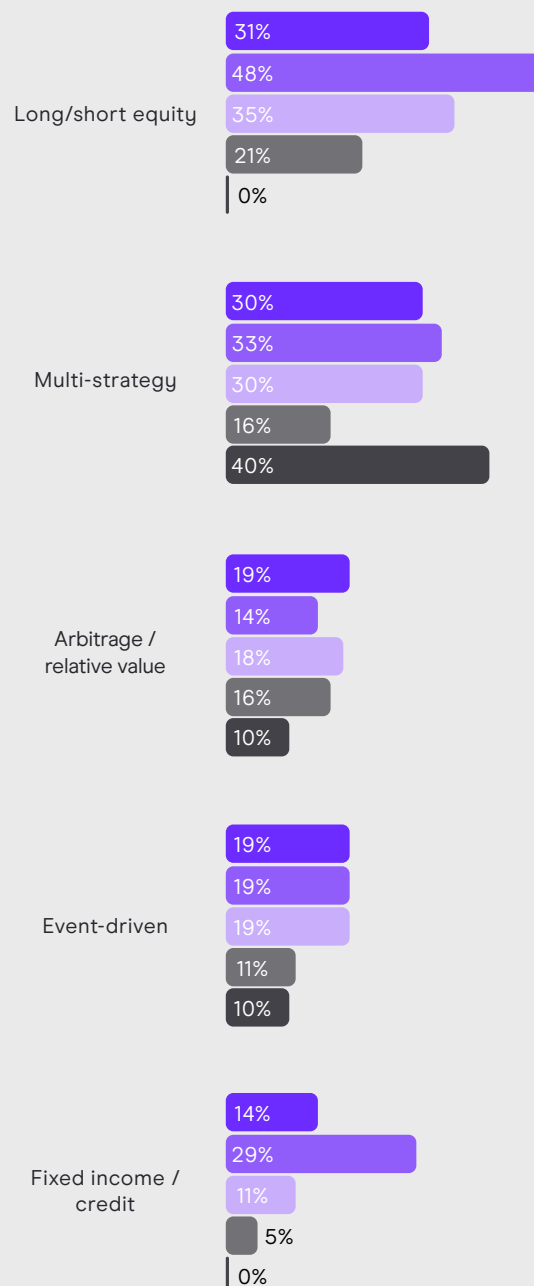
Proportion of US family offices interested in long/short equity

All of this has translated into long/short equity interest from 48% of US family offices surveyed, 35% of US foundations/endowments and 21% of US public pensions. Only US corporate pensions — with their distinct set of challenges — are resistant to the appeal of long/short equity (0%). Their preferences are for multi-strategy (40%) and macro (30%).

Multi-strategy is the second-ranked hedge fund strategy preference overall, usurping macro as the multi-asset strategy considered best-placed to navigate the transition out of Covid and rising rates. One-third of family offices and 30% of foundations/endowments are interested in multi-strategy hedge funds. Its popularity also speaks to the 33% of foundations/endowments seeking hedge funds for new investment opportunities. Despite the interest shown from US corporate pensions, macro features towards the bottom of the list.

7a Hedge fund strategies that US allocators are interested in

Analyst note: Covers all US allocators surveyed, including those not likely to increase their allocation to hedge funds. Sourced from With Intelligence survey, December 2021.



- All US allocators
- Family offices
- Foundations / endowments
- Public pensions
- Corporate pensions

Looking elsewhere, with no further allocations, the recent outperformance of event-driven hedge funds in 2021 (14.9%) appears to have run its course. This is partly due to softening investor exceptions for post-Covid M&A, or it could be that a natural ceiling for the strategy's value in portfolios has been reached. (Although there is still some consistent interest across all investor types.) It may also be a surprise to see CTAs figure so low, given some relatively large inflows and solid returns in 2021 (8.3%) after years of underwhelming performance.

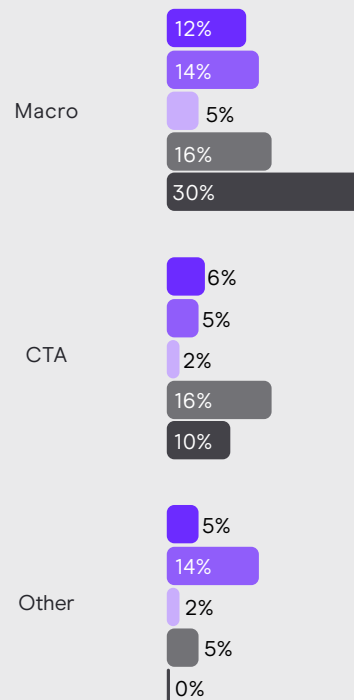
“Family office capital is more and more becoming the permanent capital that was coveted by endowments and foundations from years past.”

East Coast single-family office

US investors from 11 states had at least 50% of survey respondents likely to increase their allocation to hedge funds (this statistic excludes the 22 of the 40 states covered in this report with fewer than three investors). The list is headed by four states on 80%, which are in the Midwest and on the East Coast.

7b Hedge fund strategies that US allocators are interested in, continued

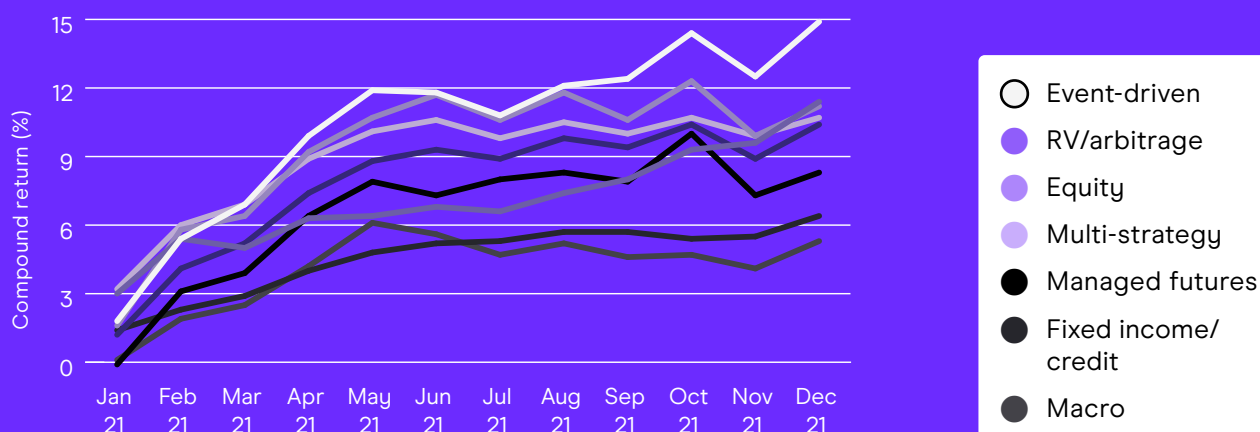
Analyst note: See 7a



- All US allocators
- Family offices
- Foundations / endowments
- Public pensions
- Corporate pensions

8 Hedge fund strategies' 12-month compound return through 2021 (%)

Chart sourced from With Intelligence's 2021 Hedge Fund Spotlight report, published January 2021. Performance indices represent the mean average return of the funds included in the relevant single-manager strategies that report to the HFM database. Based on funds reporting to HFM as of 17 January 2022 and are subject to future revision.



Illinois has the highest debt-to-assets ratio in the US with a primary source of that being pension and other post-employment obligations. There are similar stories in Washington D.C., Missouri and New Jersey, which goes some way to explaining those states' need for higher returns and increased appetite for hedge funds. California is notable for being towards the bottom of the list, with only one in four of its respondents increasing their allocation.

Looking beyond domestic investments, most US allocators appear uninterested in increasing their allocations to non-US-focused hedge funds. Asia-Pacific is slightly more preferred than Europe, especially among foundations/endowments, where the proportion of investors that prefer Asia-Pacific to Europe is almost double. Our data suggests that European managers with local investment mandates face an uphill battle to win business from US allocators.

Key Statistic — US State Intentions

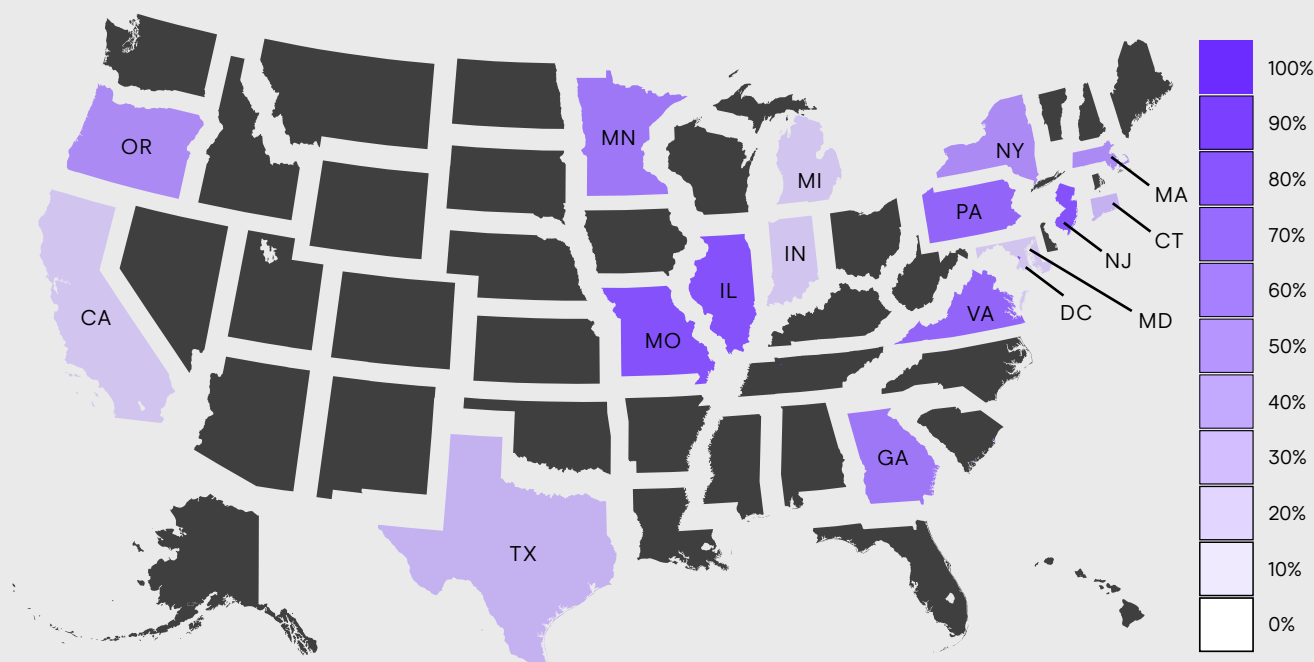
80%

Proportion of Illinois-based investors increasing their HF allocation

“Specific breakdowns on asset classes — we don't think that way. We can be flexible for the best opportunities, not just trying to fit stuff in a box.”

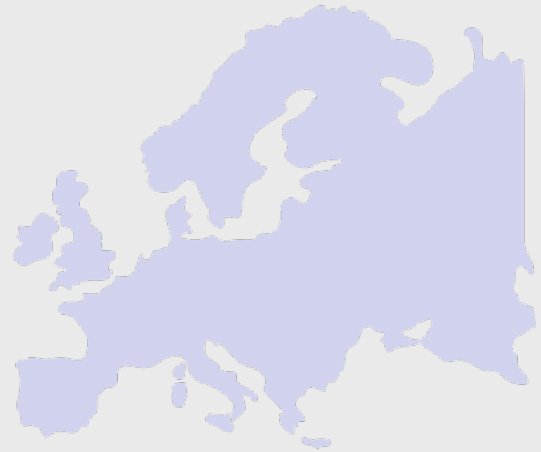
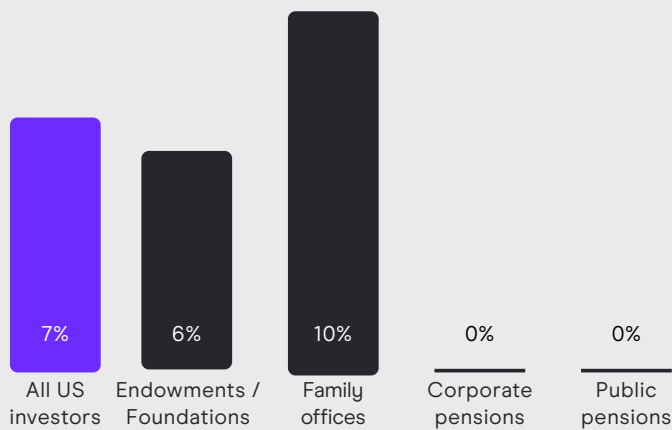
Mid-western public DB pension

9 Proportion of US allocators planning to increase their allocation to hedge funds, by US state

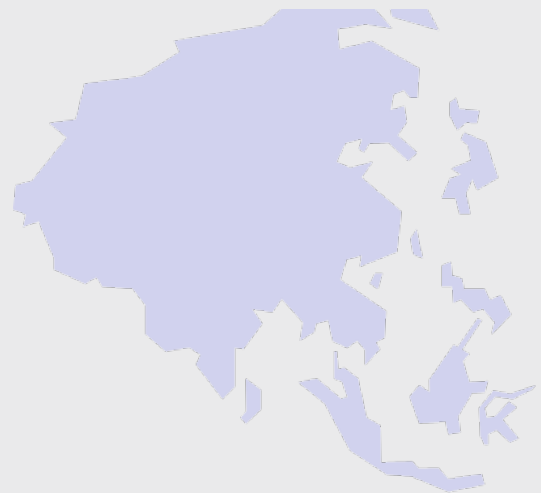
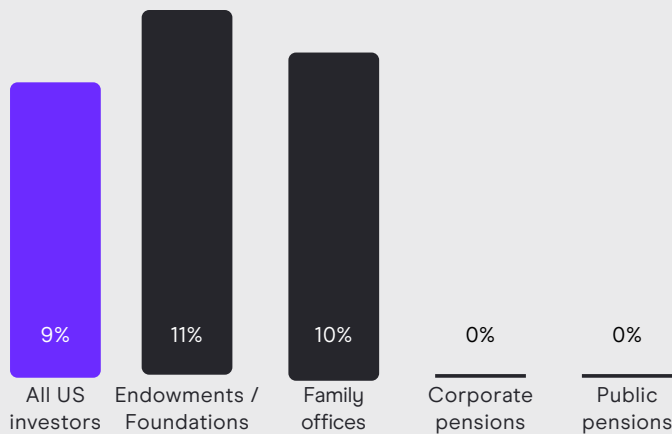


Source: With Intelligence survey, December 2021

10 Proportion of US allocators planning to increase their allocation to hedge funds that invest in **Europe**



11 Proportion of US allocators planning to increase their allocation to hedge funds that invest in **Asia-Pacific**



Source: With Intelligence survey, December 2021

Case study: Pennsylvania PSERS

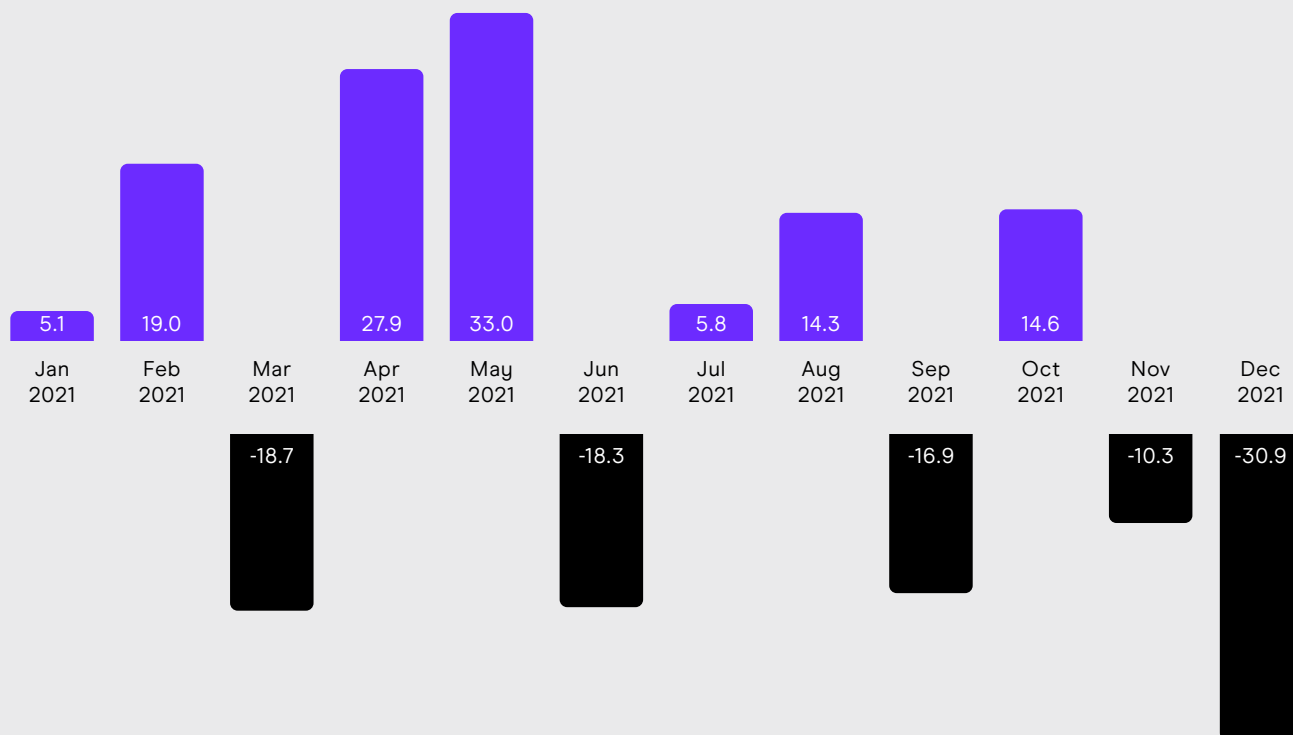
In December 2021, the Pennsylvania Public Schools Employees Retirement System (PSERS) eliminated its \$6bn target allocation for absolute return in favor of a greater allocation to traditional equities, with consequences for managers like Bridgewater Associates, PIMCO and Garda Capital. The \$73bn Harrisburg-based system had already decreased its absolute return target from 10% to 8% in 2020, as well as making small target reductions in emerging markets, private credit, and public real assets. The decision to cut, approved on December 17, led to a rise in exposure to US equities from 11% to 21%.

“The board’s decision to change the asset allocation by adding more public equity over time will increase PSERS’ net investment income in positive market conditions.”

**Pennsylvania PSERS chairperson
Chris Santa Maria**

12 Global hedge fund investor flows, 2021 (\$bn)

Analyst note: Data as of February 3 and subject to revision.



Key Statistic — Hedge Fund Investor Flows

\$25bn

Net investor hedge fund flows in 2021

-\$15bn

Net investor hedge fund flows in 2020

-\$17bn

Net investor hedge fund flows in 2019

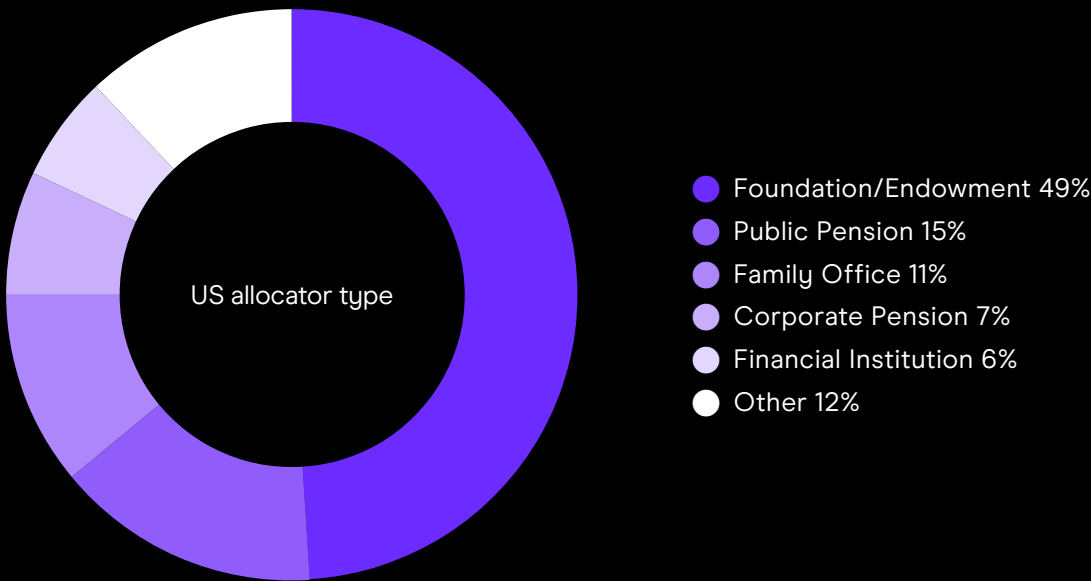
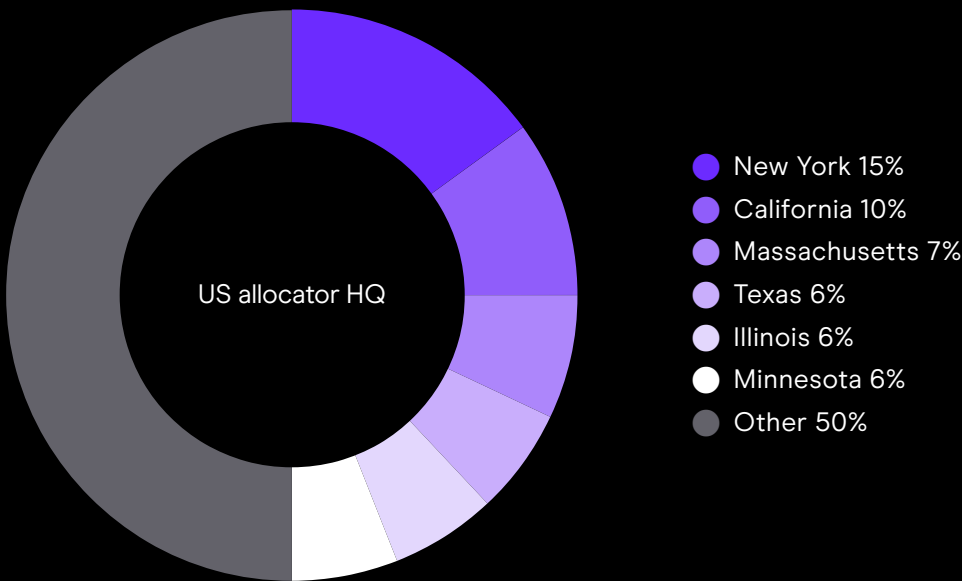
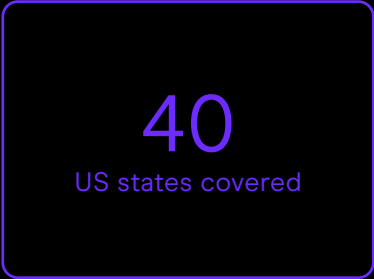
Analyst note: Data as of February 3 and subject to revision.

Last year, global hedge fund investor flows were positive but lumpy. With Intelligence investor flows data shows seven positive months and five negative months in 2021, largely mapped to the usual quarterly redemptions cycle. The year's largest monthly outflow came, as might be expected, in December (-\$31bn), albeit at a level significantly higher than in December 2020 (-\$5bn) and December 2019 (-\$12bn). December 2021's elevated outflow can be partially explained by fears of central banks losing control of inflation, the potential for tighter monetary policy hitting equity values, and the emergence of Omicron. Even so, 2021 was noteworthy as the first year of net inflows since 2017.

If 2022 is to repeat last year's patterns, there will be winners and losers within the headline inflow. Our Investor Intentions data suggests that hedge fund allocations will flow from US foundations/endowments and family offices to global and North American long/short equity and multi-strategy funds. More broadly, anecdotal evidence suggests other strategies and, in particular, Asia-Pacific funds, are also well placed. All in all, plenty of reasons to be optimistic. ●

Methodology

The findings in this report are based on the results of a survey of 224 US allocators conducted by With Intelligence’s *The Allocator* in December 2021. Respondents were based across 40 US states and represented types ranging from single family offices to triple-digit billion-dollar institutions. Most of the exhibits in this report are based on the results of this survey, with additional exhibits and data points using With’s mandates, investor flows and performance data.





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About AIMA

The Alternative Investment Management Association (AIMA) is the global representative of the alternative investment industry, with around 2,100 corporate members in over 60 countries. AIMA's fund manager members collectively manage more than \$2.5tn in hedge fund and private credit assets. AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programmes and sound practice guides. AIMA works to raise media and public awareness of the value of the industry.
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