COWEN

AIMA

EMERGING STRONGER

Emerging Manager Survey 2022

The next generation of hedge fund firms

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Please note: Percentages in charts may not add up to 100% due to rounding.

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EXECUTIVE SUMMARY

In the fourth quarter of 2021, AIMA, in conjunction with Cowen, conducted a short questionnaire on the next generation of hedge fund managers (which we describe as hedge funds running up to $500 million in assets under management (AUM), also known as 'emerging managers') and those that invest in them. This report acts as an update to a report published in 2017[1] which sought to better understand how these fund managers operate their business.

Key areas of focus include fees charged by funds, average headcount of the fund, costs (including the estimated breakeven costs) of running a fund and the average length of time to close on a new investment.

The report to follow is broken down into two key sections. Part one will highlight the key findings that we extrapolated as it relates to all the flagship funds of the fund managers who responded to this survey, while part two discusses the key findings of their firms. Where relevant, we offer a time series analysis of how the responses have changed since our previous like-for-like survey in 2017.

AUTHORS

AIMA | Tom Kehoe, Managing Director, Global Head of Research and Communications, AIMA

COWEN | Lawrence Obertelli, Director, Prime Brokerage Sales

[1] Alive and Kicking (AIMA Emerging Manager Survey 2017) | Alive & Kicking (aima.org).

DEMOGRAPHICS

This report is based on responses to two surveys, one for managers and one for investors.

IN THIS SECTION

MANAGERS

149

RESPONDENTS

$16.7bn

AGGREGATE AUM APPROX

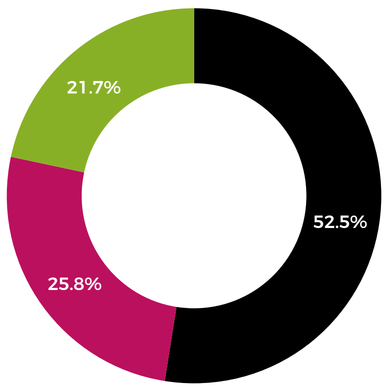
$112m

AGGREGATE AUM PER MANAGER VERSUS 2017 AVERAGE AUM OF

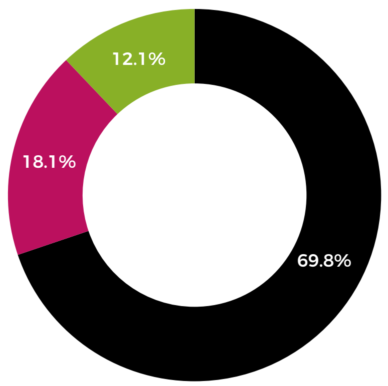
$153m

AUM breakdown, by year

2017



2022



- Less than $100m
- $101m - $249m
- $250m - $500m

Upon closer examination of the manager demographic for this year's survey (which similar to the 2017 report polled managers running below $500 million AUM), nearly 70% of all respondents are fund managers with less than $100 million AUM compared to 53% of fund managers that said the same in 2017. This impacts several of the data points that follow throughout this report Related to this, it's also notable that just 12% of all respondents are from fund managers in the upper AUM band ($250 million to $500 million) compared to one in four respondents that reported in 2017.

INVESTORS

26

RESPONDENTS

>$400bn

BILLION TOTAL ASSETS UNDER MANAGEMENT

>$50bn

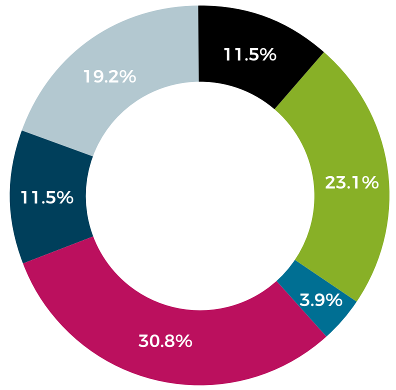
BILLION OF WHICH ALLOCATED TO HEDGE FUNDS

48%

PROPORTION THAT ALLOCATE $1BN+ TO HEDGE FUNDS

Q3. What best describes you as an investor?

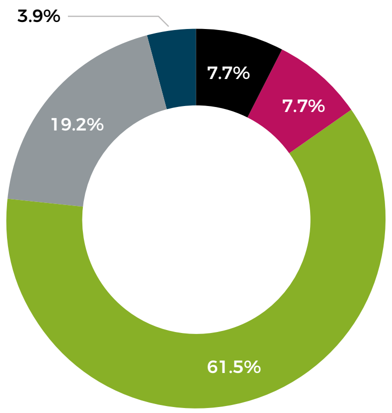
2022



- Endowment and Foundation
- Fund of Funds/Multi Manager
- Insurance Company
- Private Pension Plan
- Single Family Office
- Sovereign Wealth Fund/State Pension
- Other

Q4. Where is the head office of your investment plan located?

2022

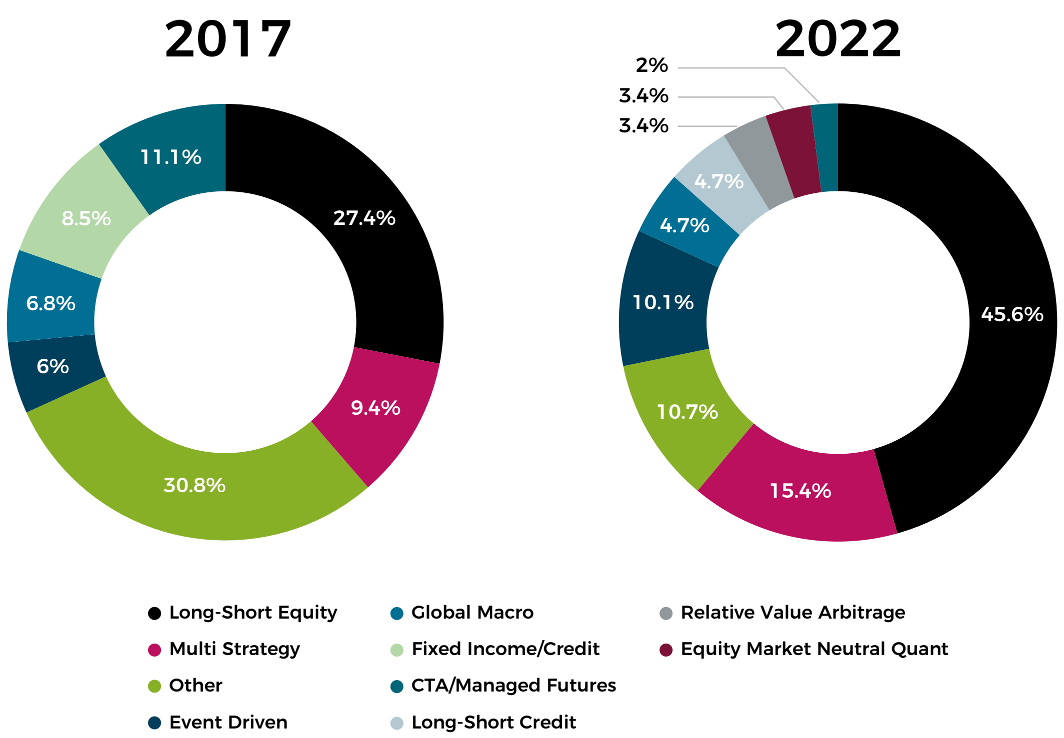


- Asia-Pacific
- Europe ex-UK
- North America
- UK
- Rest of the World

STRATEGY BREAKDOWN – MANAGERS

On a strategy basis, long-short equity and multi strategy funds dominate the responses this year, accounting for over 60% of all respondents. The 'other' bucket only accounts for just over 10%, whereas in the previous survey nearly a third of respondents differentiated themselves in this category. Further, this year is mainly populated by long-only equity strategies whereas the previous survey contained a far greater variety of niche strategies. One popular observation put forward from manager feedback roundtable discussions we conducted was that this may reflect hedge funds offering a more sophisticated investor solution than what would be typically packaged in a standard ETF product.

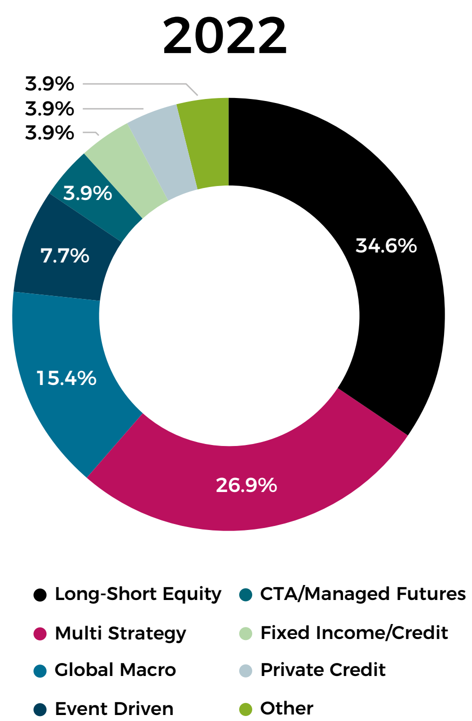
Based on this data set, it would seem there is less motivation among small and emerging fund managers to pursue niche strategies given the overall strength of performance across global equity markets in recent years.



Strategy breakdown, by year

STRATEGY BREAKDOWN – INVESTOR

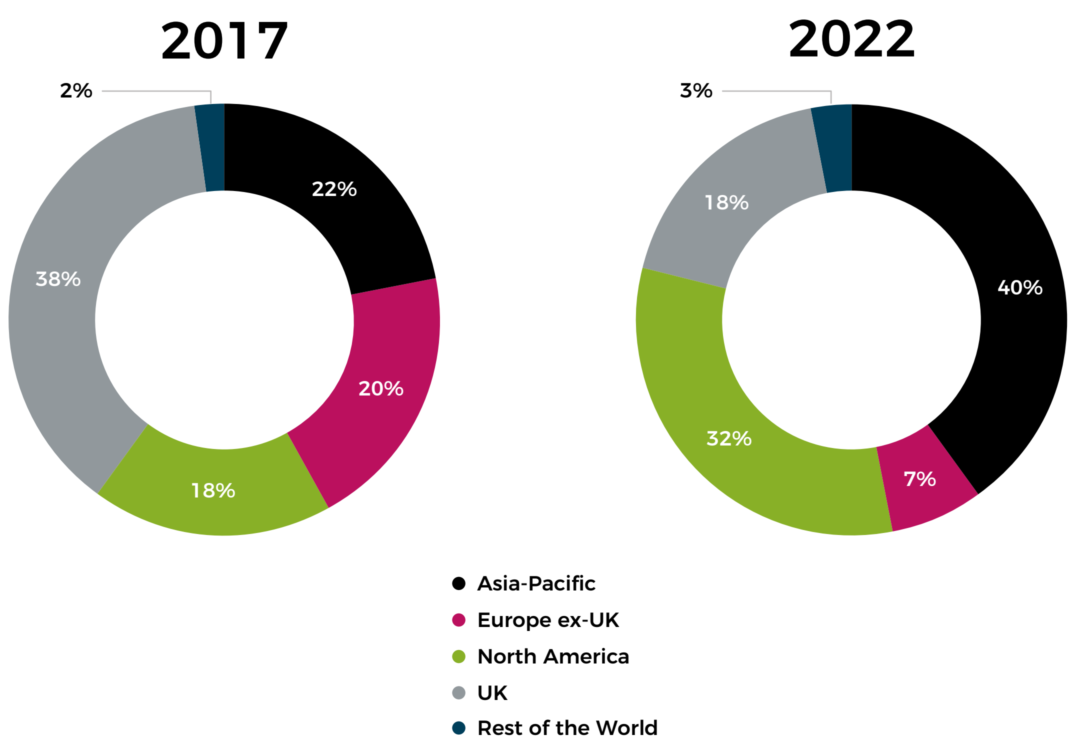
Investors' strategy preferences are seemingly tightly matched with managers, with long-short equity and multi strategy taking up a total of 62%. It's notable that the 'other' section is also down dramatically versus that reported in 2017.



Q5. What hedge fund strategies were most prominent in your investment allocations this year?

REGIONAL BREAKDOWN – MANAGERS

This year, APAC-based managers accounted for the largest percentage of respondents (40%), with double the number of funds that surveyed from the region in 2017. North America (31.5%) also saw an increase in fund managers who surveyed compared to 2017. Meanwhile the UK (18.1%) and Europe ex-UK (7.4%) have less fund manager representation than what was reported in 2017.



Manager location breakdown, by year

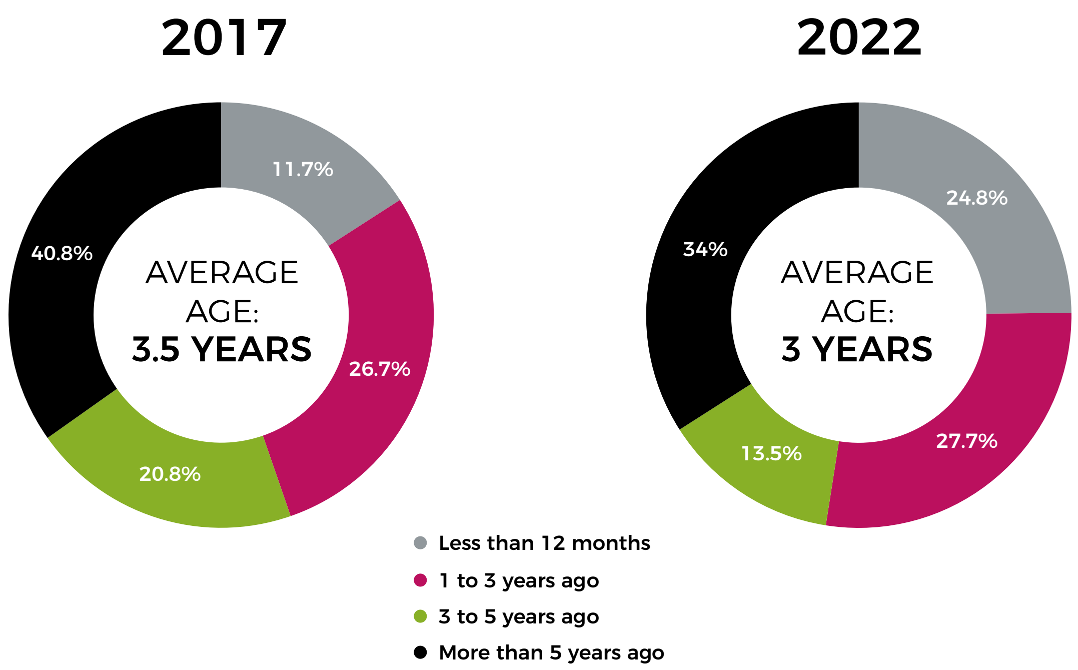
1

FLAGSHIP FUND

As per the responses from this survey, the average fund age is 3 years, slightly down on the figure of 3.5 years reported in 2017. There are also fewer funds in the 'three-to-five year' old age band.

IN THIS SECTION

MATURITY BREAKDOWN



When did you launch your flagship fund, by year?

Extrapolating these numbers, we can deduce that hedge funds are taking longer to scale to $100 million AUM *(widely seen as a key threshold for funds looking to attract a wider variety of capital investment).*

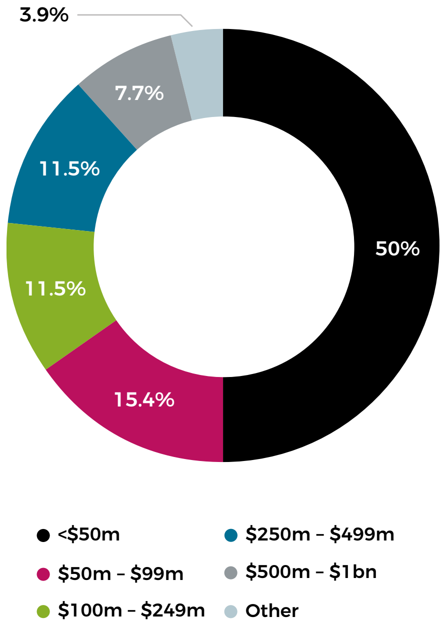
This point is demonstrated in the table below; funds that are five years or older yet still managing $100 million or less are more common this year than what we reported in 2017.

Funds are taking longer to reach $100 million AUM

Fund maturity, AUM breakdown	Maturity breakdown by AUM range (%)
2022: Fund maturity range	Less than $100m
More than 5 years ago	50
2017: Fund maturity range	
More than 5 years ago	38.9

However, fund managers should take solace from the view expressed by the investors that we surveyed. Two thirds of whom say that they would allocate to funds less than $100 million.

2022

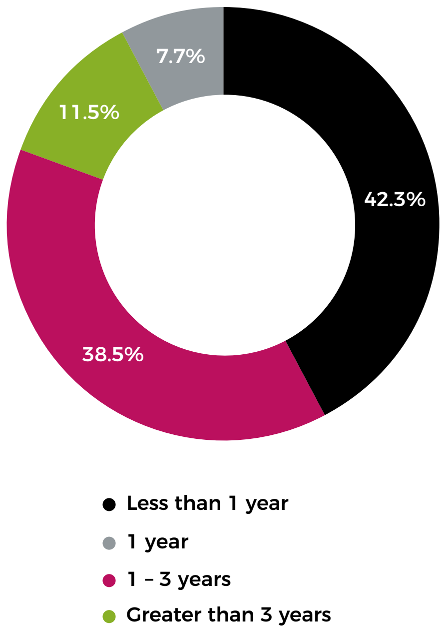


Q7. What is the smallest fund (as a measure of its AUM) that your investment plan would consider allocating to?

ALLOCATOR TRACK RECORD REQUIREMENTS

Whilst the vast majority of allocators accept managers that have a track record of 3 years or less (88%), it's worth noting a modest increase cited by investors that require longer track records, 12% now versus 4% cited by investors when asked the same question in 2017.

2022



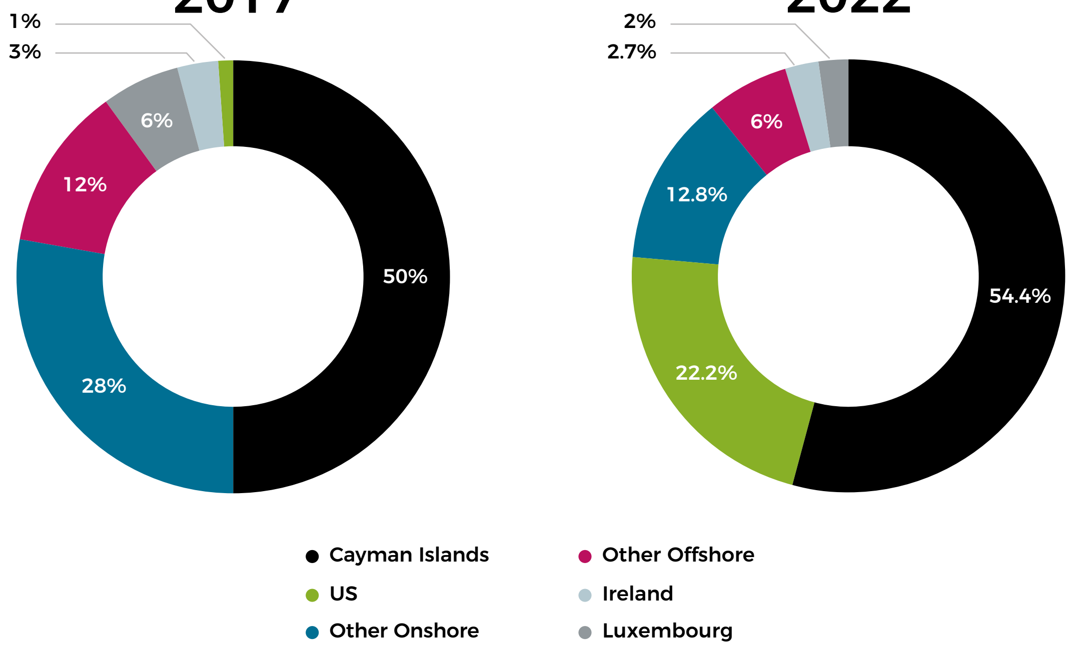
Q6. How long a track record do you need the flagship fund to have when evaluating it for investment?

FUND DISTRIBUTION/DOMICILIATION

We found a similar pattern to that of the previous report. The Cayman Islands is the preferred venue for just over half of all respondents.

This pairs well with investor preferences, 58% of which invest in offshore managers.

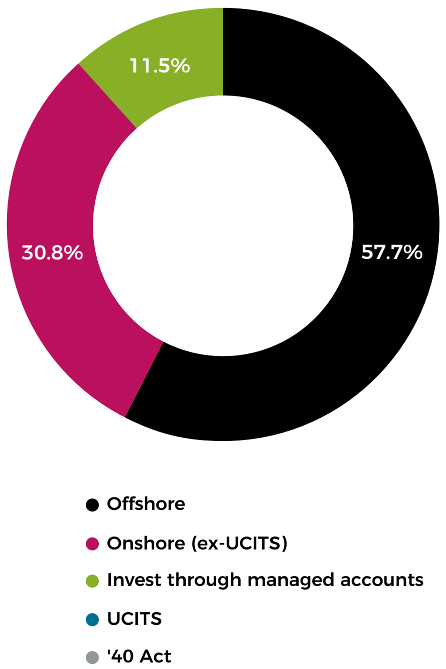
A notable change from the 2017 report is the emergence of the US being the second most popular location – up from the least popular last time – indicative of the larger number of North American funds that participated this year versus previously. The number of funds that domicile onshore continues to come down, this year accounting for just 13% of all responses, half the number reported in 2017.



Where is your flagship fund domiciled?

When cross referencing the domicile preference in relation to the AUM of respondents, larger managers are far more likely to be domiciled in Cayman. Just under half of all respondents managing $100 million or less are based in Cayman compared to 74% of those managers that have between $101 million and $249 million AUM, and 61% for those with $250 million up to $500 million. Outside of Cayman, managers that run less than $100 million have their funds domiciled in the US (28%).

Q8. Which hedge fund structure do you predominantly allocate to?



Hedge Fund Domicile (by AUM size)

Hedge Fund Domicile (by AUM size)						
	Cayman Islands	Ireland	Luxembourg	USA	Other offshore	Other onshore
Less the $100m	48.1%	2.9%	1%	27.9%	6.7%	13.5%
$101m - $249m	74.1%	0%	3.7%	7.4%	3.7%	11.1%
$250m - $499m	61.1%	5.6%	5.6%	11.1%	5.6%	11.1%

FEES

Hedge fund compensation remains resilient despite continued scrutiny from both investors and other industry stakeholders.

MANAGEMENT FEE

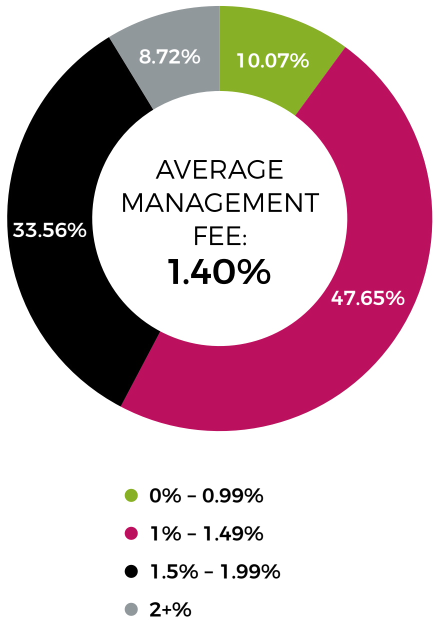
This year's survey found no change with that reported in 2017 with the average management fee again coming in at 1.4%. Notably, this year only 9% of fund managers charge 2% or higher versus 14% in 2017. Simultaneously, the 1%-1.49% band increased from 36% in 2017 to 48% in 2022. The other fee bands have stayed mostly consistent.

We have known for some time that the so-called '2 & 20' fee model is all but redundant. This data point reinforces our view of the fee structure being charged by hedge funds becoming increasingly varied. Managers and investors are showing their willingness to work with various fund and fee structures to better meet the demands of investors as well as ensure that their businesses remain viable.

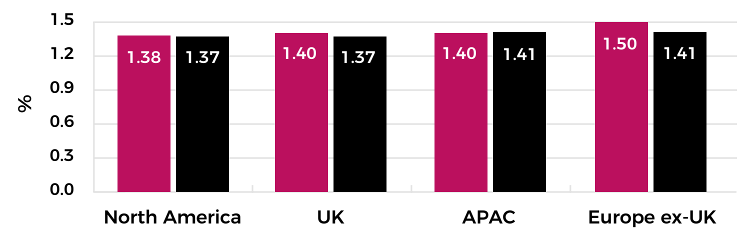
When split by region or strategy, average management fees remain closely clustered. Regionally, the highest is Asia Pacific (APAC) (1.41%), while the lowest is in the UK (1.37%).

By strategy, long-short credit funds charge the highest fees (1.57%) while global macro are the most fee competitive (1.10%).

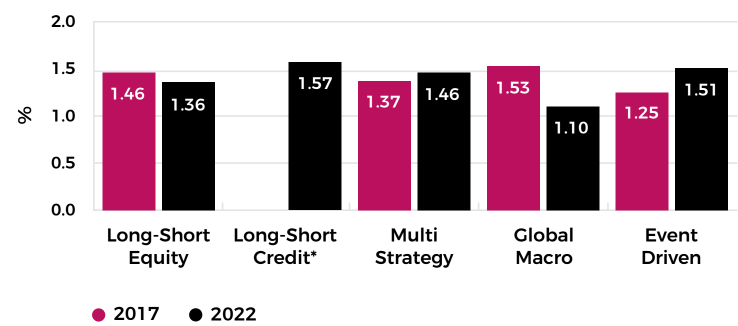
What is the standard management fee of your flagship fund?



Average management fee, by region - time series



Average management fee, by strategy - time series



* Long-Short Credit was not a strategy option that hedge funds could select in the 2017 survey.

In a similar fashion, average performance fees remained steady at approximately 16%, although the 15%-19.99% band accounts for half of all respondents this year, up from 34% in 2017.

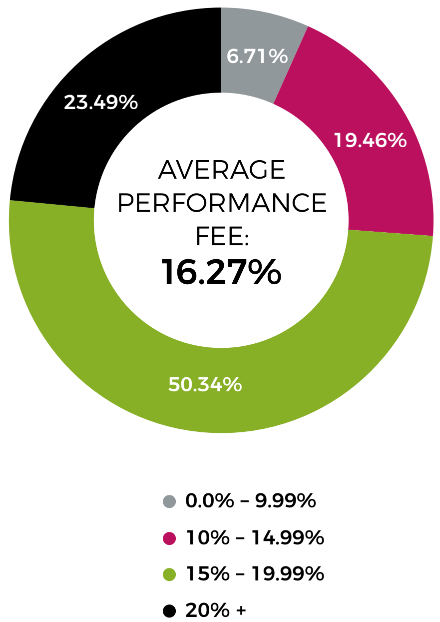
Moreover, this high-level consistency belies a difference in the spread of respondents.

For example, the population of respondents in the '15% to 19.99%' band is notably larger in this year's survey, compared to five years ago. Moreover, there is a notable reduction in the number of managers who are charging 20% or greater this year, from 2017.

Elsewhere, performance fees diverge more significantly than management fees when compared across strategies in this year's survey. Event driven funds command an average performance fee of 17.7%, while long-short equity make do with 15.1%.

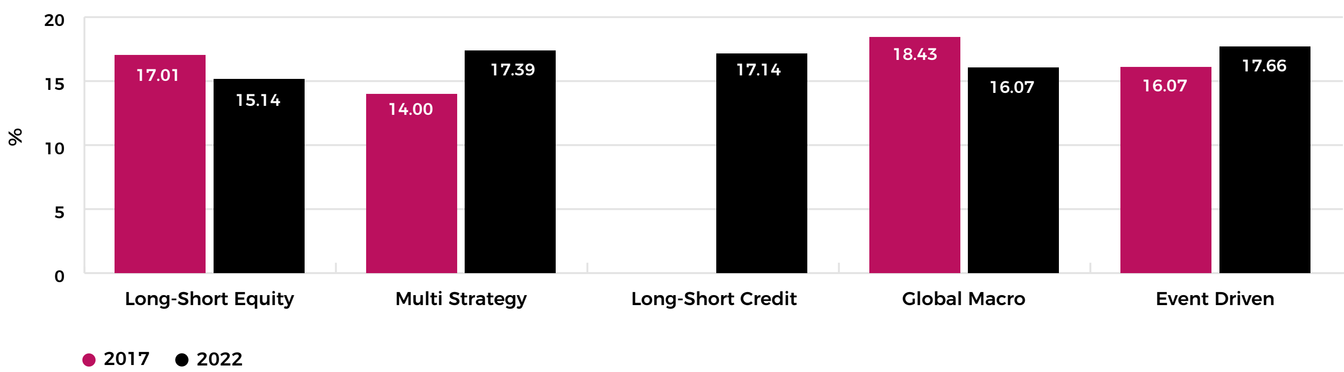
By region, performance fees are stacked the same way. APAC once again top the chart with an average performance fee of 16.6%, while the UK has the lowest at 15.8%.

2022



What is the standard performance fee of your flagship fund?

Average performance fee, by strategy – time series



PERFORMANCE INCENTIVES

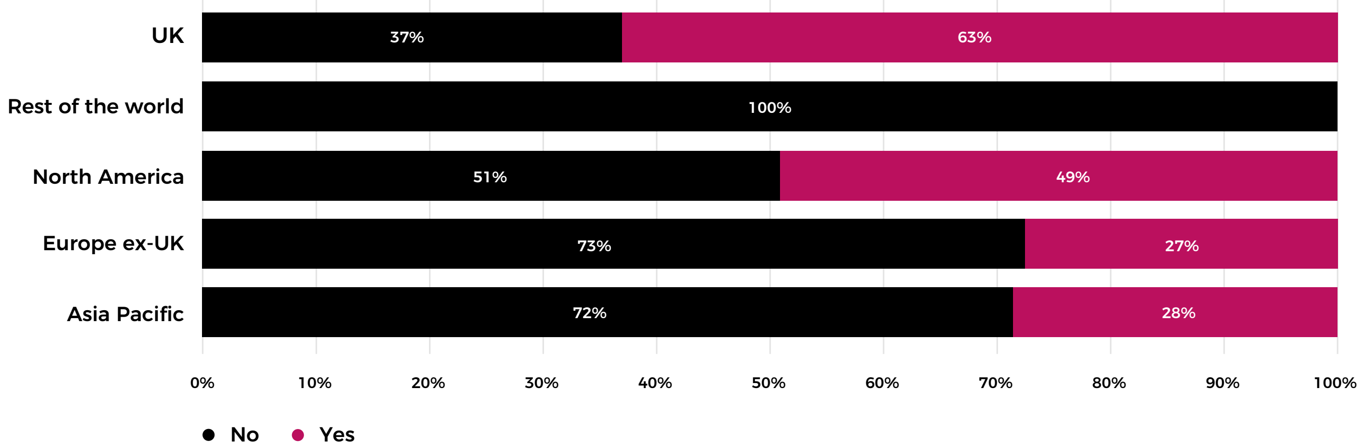
Interestingly, 23% of respondents operate without a high watermark. Of that portion, the vast majority (80%) are managers with $100 million AUM or less. Just under half are from North America, while 40% are from APAC. Closer examination of this population shows that majority of funds are long-short, followed by multi strategy. While the suspicion would be that those funds would need to be older, that is not the case with two-thirds of those without a high watermark operating a flagship fund that is three years old or younger.

ADDITIONAL FUNDS:

When looking to what extent managers have added to their stable of funds, we find that 44% of respondents have at least one additional fund. The data shows that the percentage of those with additional funds grows as we move up the AUM bands. Regionally, respondents from APAC and Europe ex-UK are the least likely to have an additional fund, whereas the UK managers are the most likely, with over two-thirds having at least one additional fund.

Delving deeper – of those that do have an additional fund – half of all fund manager respondents have between one and three additional funds, whereas 38% have only one additional fund; the remainder have between three and five extra funds.

Do you have an additional fund? By region



COWEN AIMA

2

YOUR FIRM

IN THIS SECTION

EMPLOYEES

Arguably the greatest asset of any business is its people.

Among the fund manager respondents that participated in this survey, there are on average seven employees, marking a decline of one person from the average employee number reported in 2017.

The pandemic period has seen an acceleration of outsourcing and new ways of working, including part-time, hybrid and remote working, as well as a greater effort by firms to become more efficient. This is borne out when we look more closely at the average headcount per firm's AUM, with firms running less than $100 million having on average five persons while firms between $250 million and $500 million having on average 13 persons.

Albeit the UK has a smaller population of firm respondents with sub $100 million managers, if we compare them to their global peers, they employ more people on average than firms in North America or Europe.

On a strategy basis, global macro, multi strategy and long-short equity had the larger average headcount.

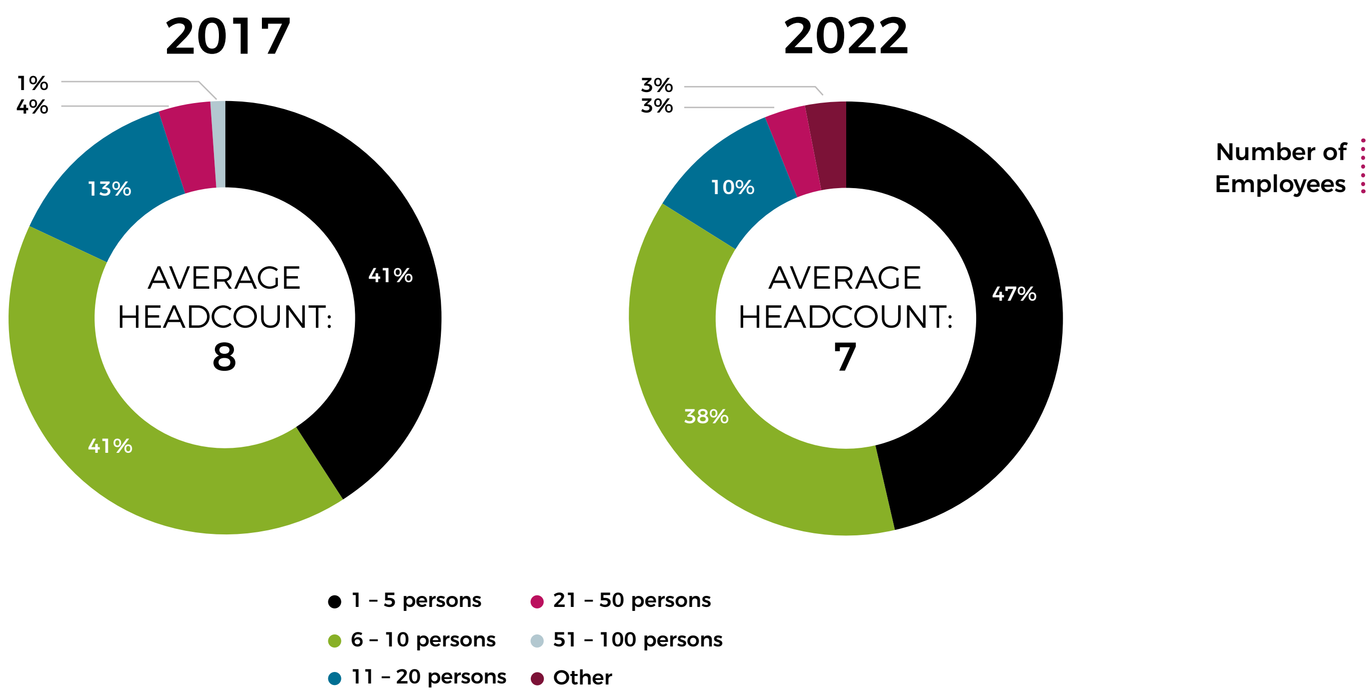
Average headcount, by region – time series

Year	North America	UK	APAC	Europe ex UK
2022	8	9	10	6
2017	6	10	7	7

Average headcount, by strategy – time series

Year	Long-Short Equity	Multi Strategy	Global Macro	Event Driven	Long-Short Credit
2022	7	9	11	5	6
2017	7	14	10	8	N/A*

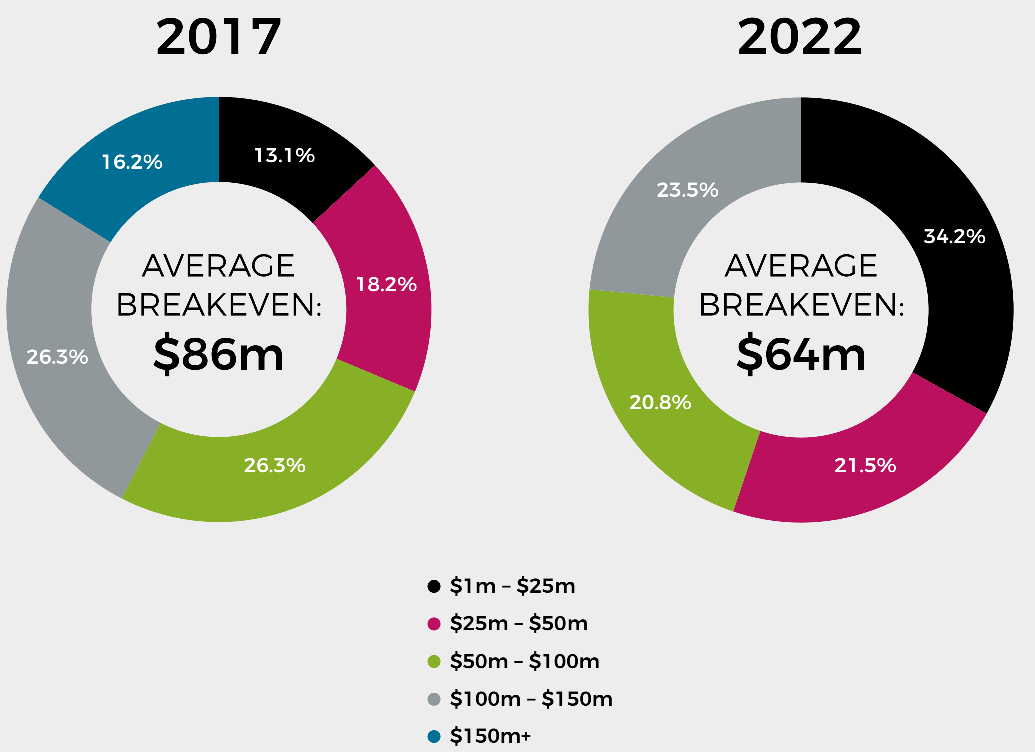
* Long-Short Credit was not a strategy option that hedge funds could select in the 2017 survey.



BREAKEVEN

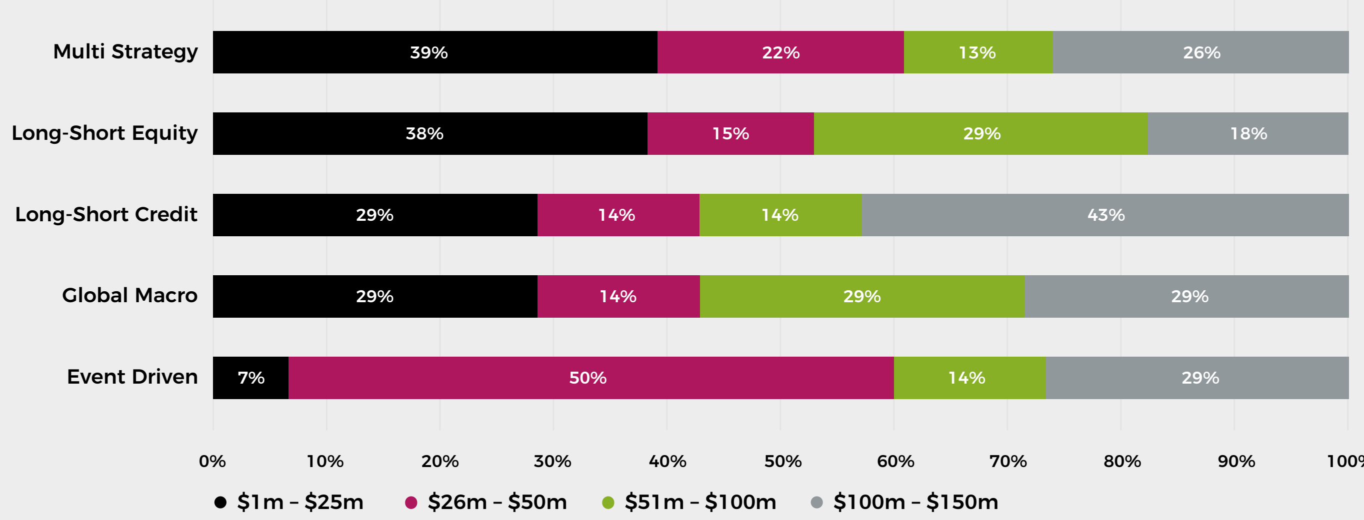
Making a profit is the key aim for any business. A crucial milestone to meet in delivering profit is being able to break even[1] in the first instance. Businesses of all types that are starting out incur a high burn-rate on their working capital. Hedge funds are no different. The firms that participated in this survey suggest that cost containment within these early years is achievable.

When compared to the breakeven figure reported in 2017, this year's average breakeven is down by almost a quarter, further evidence that firms are striving to be more efficient, outsourcing more, including core parts of their business. Moreover, recalling the dip in average headcount noted above, this drop-off compared to 2017 is derived from the sub $100 million fund managers who appear to be doing more while managing with slightly less personnel than before.



What is the breakeven for your business, by year?

2022: What is the breakeven for your business? By strategy



Breakeven ($m)					
Year	Long-Short Equity	Global Macro	Multi Strategy	Event Driven	Long-Short Credit
2022	62.2	73.6	62.3	71.2	84.3
2017	85.8	132.1	97.5	108.3	N/A*

* Long-Short Credit was not a strategy option that hedge funds could select in the 2017 survey.

Closer examination of the breakeven by region provides a similar result to our findings five years ago, with the UK again one of the most expensive regions for emerging managers to operate a hedge fund business globally, with an average breakeven of $85.5 million. By contrast APAC and North America firms can achieve breakeven at almost two thirds the breakeven being managed by UK firms, $60.6 million and $59.9 million respectively.

Breakeven ($m)				
Year	Europe ex-UK	North America	APAC	UK
2022	47	59.9	60.6	85.5
2017	75.7	82	101.9	91.3

[1] The amount of total revenue required to cover the total costs needed to operate the business.

WHY THE LOWER BREAKEVEN?

FOCUS GROUP FEEDBACK

1 Salary sacrifice

- It is not uncommon for the vast majority of capital invested in an emerging/start-up hedge fund at its inception and throughout its early years to come from the founders/principals.
- Increasingly, the first few years will be lean, even more so than in previous years. Greater salary and other personal sacrifices being put before the welfare of the business is becoming more commonly practiced.
- Deferred remuneration is an increasingly common feature practised by small start-up fund managers. It is also common that principals reinvest any deferrals into their fund.

2 More outsourcing?

- *2021 KPMG/AIMA* research[1] points to a growing number of hedge funds expanding their outsourcing efforts. Investors are increasingly comfortable with hedge funds outsourcing more, with some even pushing them further in this regard.
- The pandemic forced hedge funds into having to think about being even more efficient and accelerated trends like outsourcing.

3 Less travel – more savings to the firm's bottom line

- Undoubtedly firms have saved on travel and entertainment and the acceptance of virtual connection (online due diligence, etc) has meant that firms now travel less.

4 Use of platforms

- The emergence of regulatory hosting platforms has allowed firms to manage themselves at a fraction of the cost required to operating the compliance function fully in-house. The popularity of such platforms with managers – and indeed acceptance by investors – has risen steadily over time, contributing to overall cost-savings in the industry.

5 Reduction of office costs

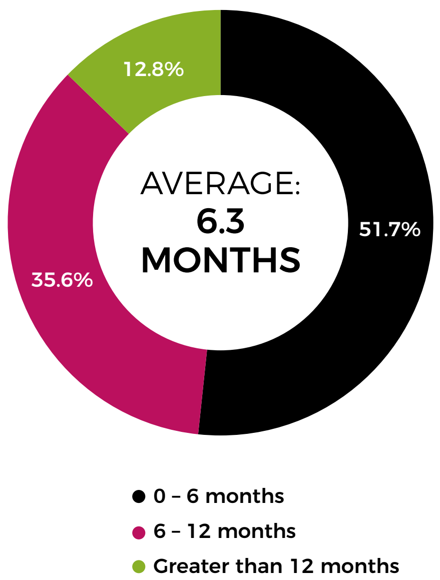
- Another trend accelerated by the pandemic is the decision for some firms to relocate out of inner cities to more remote locations, with lower costs of living.

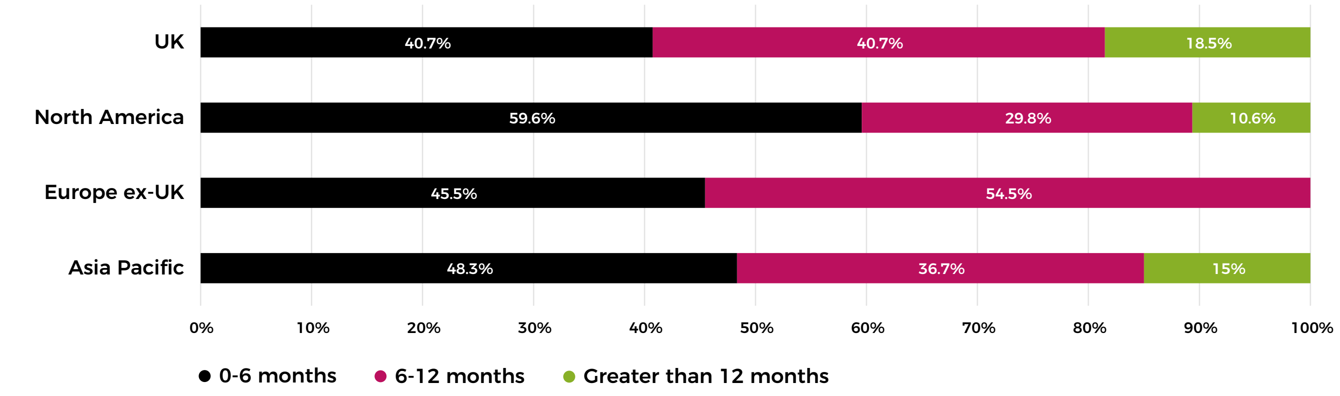
[1] Accelerating out of the Pandemic.

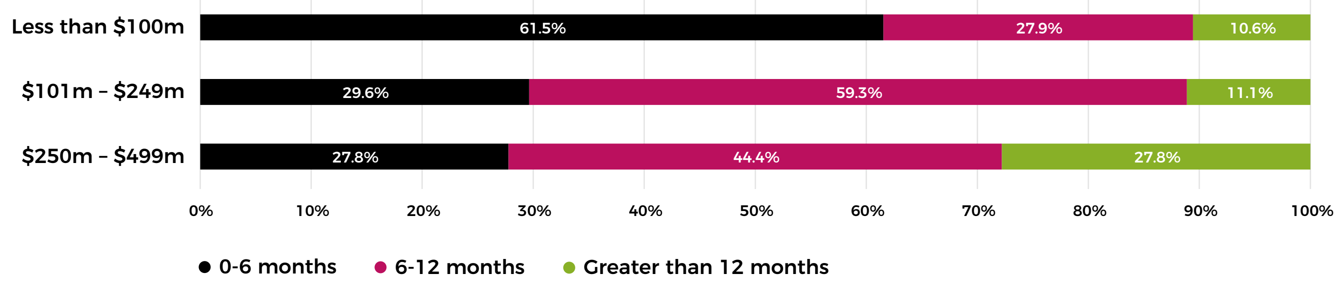
RAISING CAPITAL:

2022

What is the average period to close on a new investment into the fund?







Another positive consequence of the pandemic period has been the greater level of acceptance for virtual investor meetings. The evolution and optimisation of digital tools such as video conferencing and data sharing rooms have accelerated the investor relations process in terms of availability of senior partners for meetings, cutting back on time to travel and overall due diligence also being more efficient. Some of the managers that we spoke to mentioned being able to raise capital entirely virtual throughout this time, albeit they did have a pre-existing relationship with the investor prior to the onset of COVID-19.

Breaking down the population by AUM, funds that had less than $100 million in AUM enjoyed the shortest period to close on a new investment with the average fund taking just under six months (5.83 months), two months shorter than funds running above $100 million AUM. As funds grow their asset base and look to attract institutional investor money, times to onboard new investment will be longer.

BARRIERS TO INVESTING:

Response	Response %
Concerns regarding operational due diligence, poor administration standards and lack of fund transparency	80.8%
Investment Style drift, too much illiquidity	69.2%
Unrealistic target, poor business plan or viability	61.5%
Fees charged to the fund are deemed too excessive	42.3%
Fund does not use recognised top tier service providers	38.5%
The business is cash flow negative	23%
Targeted or minimum investment exceeds the investment plan's threshold to hedge funds	15.4%
Targeted or minimum investment represents more than a certain percentage of the fund's total AUM	[11.5%]
Only invest in start-ups or segregated accounts	7.7%

[In 2017 this was by far the #1 barrier to investing]

To get the other side of the picture, we asked investors what barriers they had which would prevent them from allocating to small and emerging fund managers. The overwhelming takeaway was the need for managers to ensure their fund operations are sound, that their investment approach aligns with that agreed with their investors and that they have a good business plan. Interestingly, when comparing notes from the question asked in 2017, just 11% of investors this time are limited by the size of the potential fund that they are looking at, compared to 40% of investors who said so five years ago.

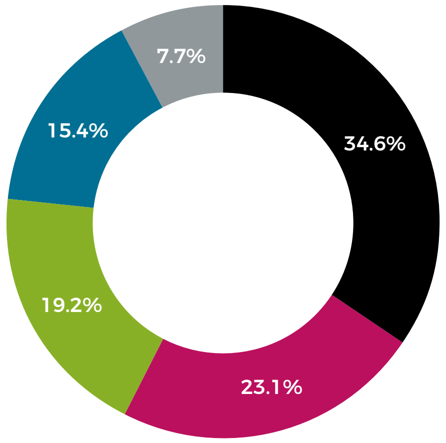
Another important change from the views reported in 2017 is investor attitude towards fees. Whilst we noted earlier in this report that both management and performance fees remained largely unchanged, investors recognise that fund manager fees have become more competitive and where fund managers can deliver outperformance on a consistent basis, that they should be rewarded.

How investors are finding their investments is also evolving would seem to make sense given recent Covid restrictions.

Prime Broker Capital Introduction teams are now the second most popular resource for investors.

Q9. What is the source of your most recent hedge fund allocation?

2022



- Personal network
- Capital introduction via Prime Broker
- None of the above
- Referral from manager that you allocate to
- Previously invested with the hedge fund
- Referral from third party marketer

CONCLUSION, ACKNOWLEDGEMENTS & ABOUT

CONCLUSION

We believe the findings of this survey illustrate the resilience and adaptability of emerging hedge fund managers. Against the backdrop of Covid and its many knock-on effects, managers have largely maintained their fees and headcount whilst simultaneously reducing their costs to breakeven[1]. Further, the investors that allocate to this group are seemingly harder to please these days, with even greater expectations regarding the operational ability of the firm and the performance of its fund(s)

The good news is two-fold; (1) if managers can rise to these demands, investments are now taking only 6 month roughly to attain and (2) low-AUMs are less of a barrier; Managers that emerge stronger have every chance of success.

We would like to thank all the respondents to this survey. We hope you have found the report useful and informative.

[1] Measured as the total costs to operate the fund divided by the average value of its AUM.

ACKNOWLEDGEMENTS

We would like to express our sincere gratitude to members of the AIMA Next Generation of Managers'[1] for providing their input to the development of this survey and participating in various roundtable discussions throughout this project. We would also like to extend our thanks to the group of investors who contributed to this survey and provided valuable insight regarding their views and expectations as to what is best required from small and emerging hedge fund managers to secure investment.

[1] AIMA's Next Generation of Managers' Group provides a platform for the exchange of ideas and development of a peer networking group, for senior individuals at firms managing less than $500 million in assets under management. The group meets on a regular basis to discuss issues of common concern including capital raising, operational matters and managing the business. Membership is open to all, including AIMA members and non-AIMA members, in the case of the latter for a minimum period of time.

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 $2.5 trillion 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.

AIMA is committed to developing skills and education standards and is a co-founder of the Chartered Alternative Investment Analyst designation (CAIA) – the first and only specialised educational standard for alternative investment specialists. AIMA is governed by its Council (Board of Directors).

For more details go to **www.aima.org**

ABOUT COWEN

Cowen is a diversified financial services firm that provides investment banking, research sales and trading, prime brokerage, outsourced trading, global clearing and commission management services. Cowen also has an investment management division which offers actively managed alternative investment products. Founded in 1918, the company is headquartered in New York and has offices worldwide.

Cowen Prime Brokerage is a full-service institutional offering that partners with emerging to established investment managers to help them build and grow their business. Its model is flexible and highly personalized, ensuring clients get the differentiated solutions they need as their business evolves. By partnering with Cowen, clients have access to its award-winning prime brokerage services, global trading desk, operational support, capital introduction and business consulting, backed by the institutional capabilities of a global investment bank.

For further information, visit **www.cowen.com**

E: COWENPRIMEBROKERAGE@COWEN.COM

COWEN.COM **COWEN** **COWEN**RESEARCH **COWEN**

COWEN INTERNATIONAL LIMITED

E: INFO@AIMA.ORG

@AIMA_ORG **AIMA** – THE ALTERNATIVE INVESTMENT MANAGEMENT ASSOCIATION