ALLOCATOR

TRENDS REPORT

NORTH AMERICA

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Executive Summary

Two distinct narratives emerged about the hedge fund industry in 2018, depending on whom you ask.

The first narrative was one of doom and gloom, as media headlines painted a picture of an industry in crisis.

- Reuters: Hedge fund number to shrink, first drop since crisis
- Pensions & Investments: Tough environment has hedge fund heading for the exits
- Institutional Investors: Investors pull back from hedge funds

Despite these headlines, allocators remain committed to alternative investments. Based on a survey of nearly 450 institutional allocators in attendance at Context Summits Miami 2019, our data showed:

- **72%** of investors said they felt “optimistic” or “very optimistic” about the alternative asset management industry, compared to 83% who felt the same way at Miami 2018
- **97%** said they planned to increase or maintain their net positions in alternative investments by the end of 2019; in comparison, 99% of allocators at Miami 2018 said they wanted to increase or maintain their allocations to alternative investments
- **80%** of investors said they will either decrease or maintain their cash position in 2019, indicating a willingness to put capital in the market; this compares to 77% of investors who said the same at Miami 2018

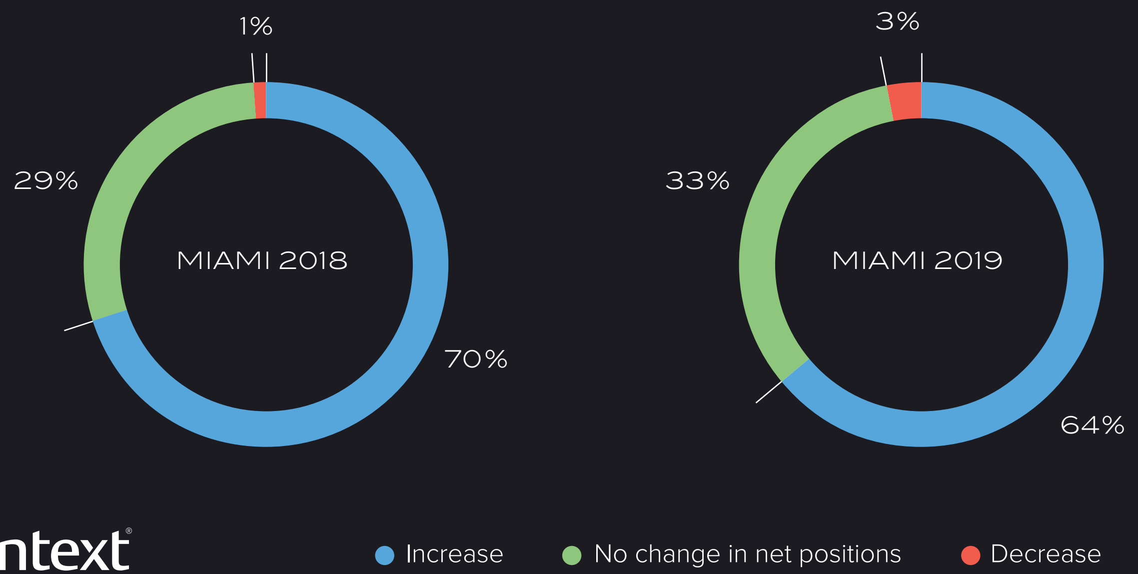
These numbers suggest a different narrative – one of an industry in a state of evolution.

First, consider that 90% of the 70 asset classes tracked by Deutsche Bank posted negative total returns in dollar terms for 2018 through mid-November. The previous high was in 1920, when 84% of 37 asset classes were negative. Comparatively, in 2017, just 1% of asset classes delivered negative returns. This data suggests that the value proposition for hedge funds hasn’t changed; what’s changed is the market environment.[1]

It’s easy to criticize hedge funds in a time when the bull market is stretching into its second decade. The value of a hedge fund strategy has always been more about its potential as a source of asymmetrical returns during times of market volatility or down

[1]Source: Deutsche Bank

What are your planned changes to net positions in alternative investments by year end?



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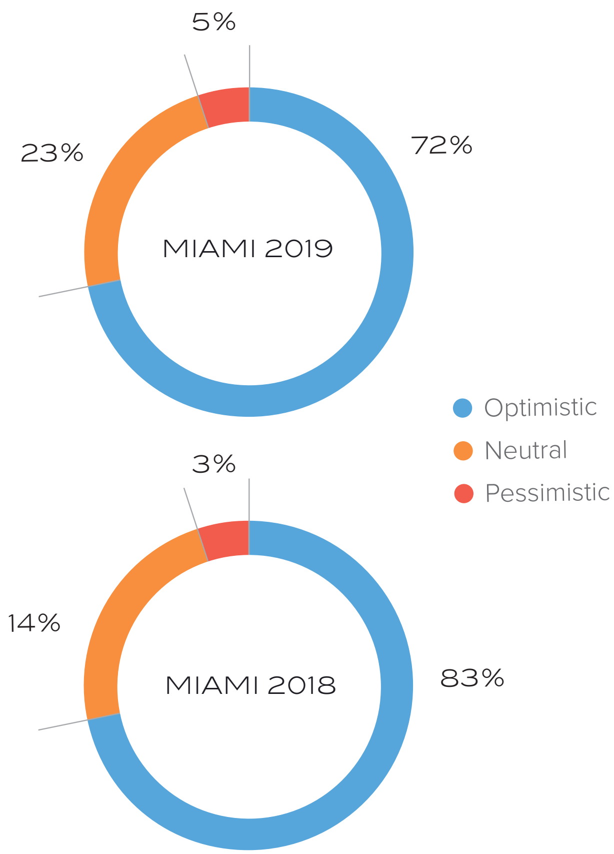
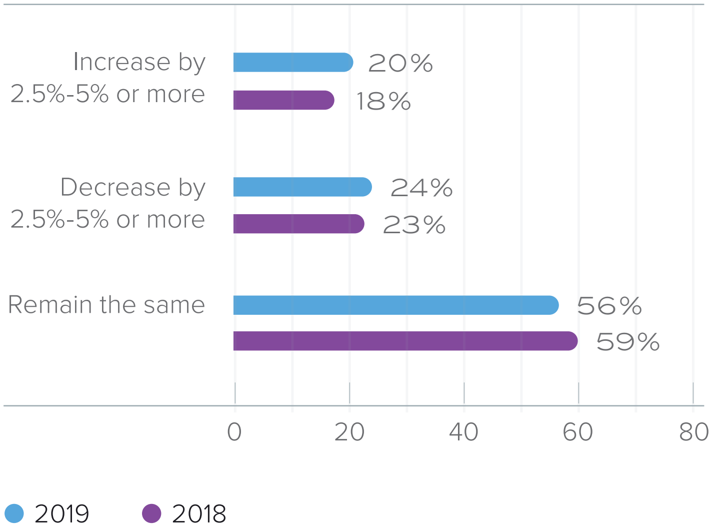
What are your general sentiments towards the alternative asset management Industry?



How much will your cash position likely change in this year?



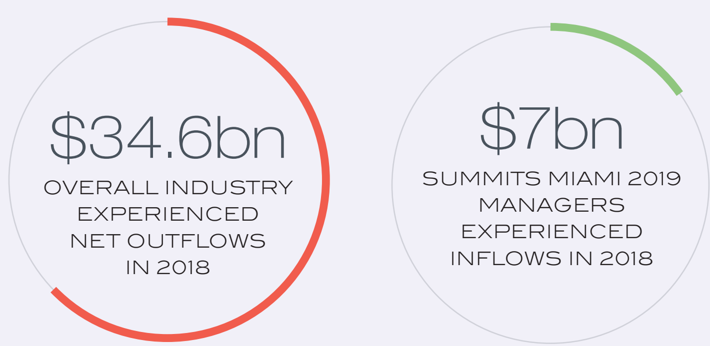
markets. If and when a down market occurs, this value will once again be on full display.

Second, not all hedge funds are created equal. In fact, hedge fund strategies today are more varied than ever and available to investors across a wide spectrum of risk-return profiles. For example, the best-performing equity hedge funds earned close to 5% returns in 2018, while the worst ones dropped by almost 15%.[2] The key is separating the strong performers from the poor ones.

This is why we believe this second narrative, one of evolution, is a true representation of the hedge fund industry. With around 16,000 active hedge funds in the world today, it's harder than ever for investors to identify top managers and the best strategies for their portfolios.[3]

This is exactly why we created Context Summits. We pride ourselves on offering an environment where investors can come and meet with the top managers. In 2019, we welcomed more than 2,000 attendees, including fund managers and investors representing nearly $5 trillion in alternative AUM, to our flagship event. These investors come to our events to put capital to work, with 82% saying they've allocated to a fund they met at a Context Summits event. Perhaps more impressive, over a quarter of investors surveyed said they had allocated to five or more funds they met at our event.

So contrary to headlines, our data suggests investors are not pulling back from hedge funds at all, but rather taking a more sophisticated approach in how they allocate capital. This helps explain the disparity between the $34.6 billion of net outflows in 2018 in the industry with the contrast of hedge fund managers in attendance at Context Summits Miami 2019 that experienced $7 billion in inflows during the same time period.[4] We expect there will continue to be a strong demand for alternative investments.



[2]Source: Preqin
[3]Source: Preqin
[4]Source: HFR, Context Summits

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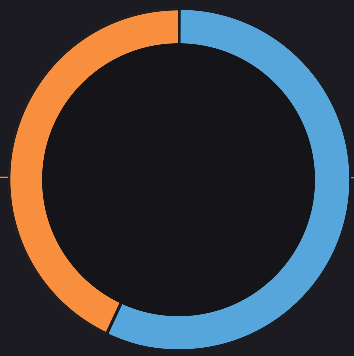
Allocators Prefer Emerging Managers

Are you more likely to allocate additional capital to emerging managers or established managers?

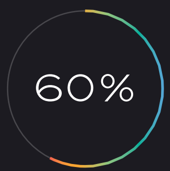
43%
Established managers



57%
Emerging managers[4]

[4]New or emerging managers are defined as those with shorter than a 3-year track record and/or less than $300 million in AUM

MIAMI 2018



Favor emerging managers

This remains mostly in line with the **60%** of institutions that favored emerging over established managers from Miami 2018

Allocators attending Context Summits Miami 2019 continued to show consistent support for emerging managers. A majority of investors (57%) said they favor new managers over more established ones. That figure tracks closely to the 60% of investors who said the same thing in 2018, and is a number that has remained remarkably steady over the past few years.

The lone exception is Europe, where roughly 75% of the allocators in attendance at Context Summits Europe 2018 said they preferred emerging managers. This makes sense for the European hedge fund space, which tends to be smaller in terms of funds launched and assets raised than in the U.S. However, we predict this disparity will narrow as the European hedge fund sector continues to mature.

Overall, total hedge fund numbers remained steady at around 16,000, as fewer funds launched and closed in 2018. Allocators had fewer new fund managers from which to pick in 2018 as fund launches declined for a fifth consecutive year to 609. Meanwhile, fund liquidations slid for a second straight year to 746, their lowest in half a decade.[5] The combination of these trends suggests that there may be fewer emerging managers for allocators to pick from, but it also shows the standard of what it takes to stand out and succeed in the hedge fund industry is higher than ever.

[5]Source: Preqin

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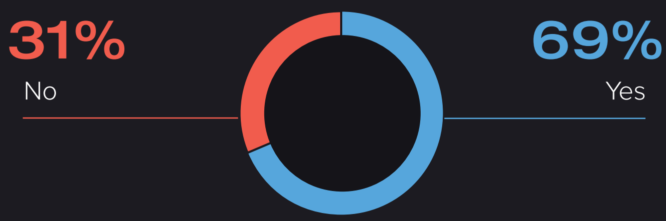
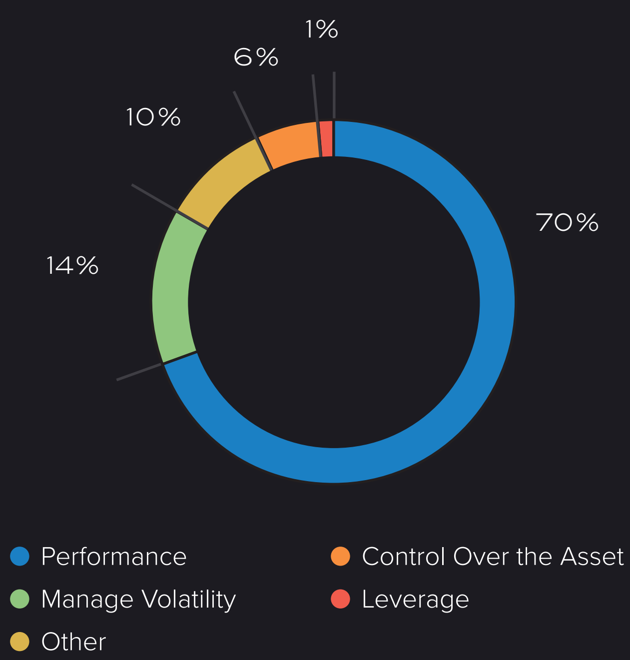
Allocator Market Outlook – Planning for 2019

Do you allocate to less-liquid strategies?



What is your primary motivator for allocating to less-liquid strategies?



Making market predictions is always a tenuous task. The institutional allocators who frequent Context Summits events were accurate in their market outlook last year when 69% predicted that the market would perform worse in 2018 than in 2017.

The market's hard landing over the final three months of 2018 delivered a sobering message to allocators, reminding many how suddenly and painfully sentiment can turn.

The decade-long bull run in equities, which pushed into record territory, grinded to a halt in 2018. Investors' fears over slowing economic growth and decelerating earnings deepened. By the close of December 31, the S&P 500 had logged its largest annual decline in a decade, sliding by 6.24%.[6]

The correction also brought equity valuations nearer to their long-term averages, suggesting to allocators that the rally still has legs. This has fueled optimism about a potential rebound in 2019, with about 63% of survey respondents predicting that the market will perform better this year than in 2018. This may be setting a low bar, as stronger year-over-year performance could still mean a second straight year of negative returns and even a recession. But it does suggest that investors view 2018 as more of a speed bump than a concrete wall.

[6] Source: S&P 500

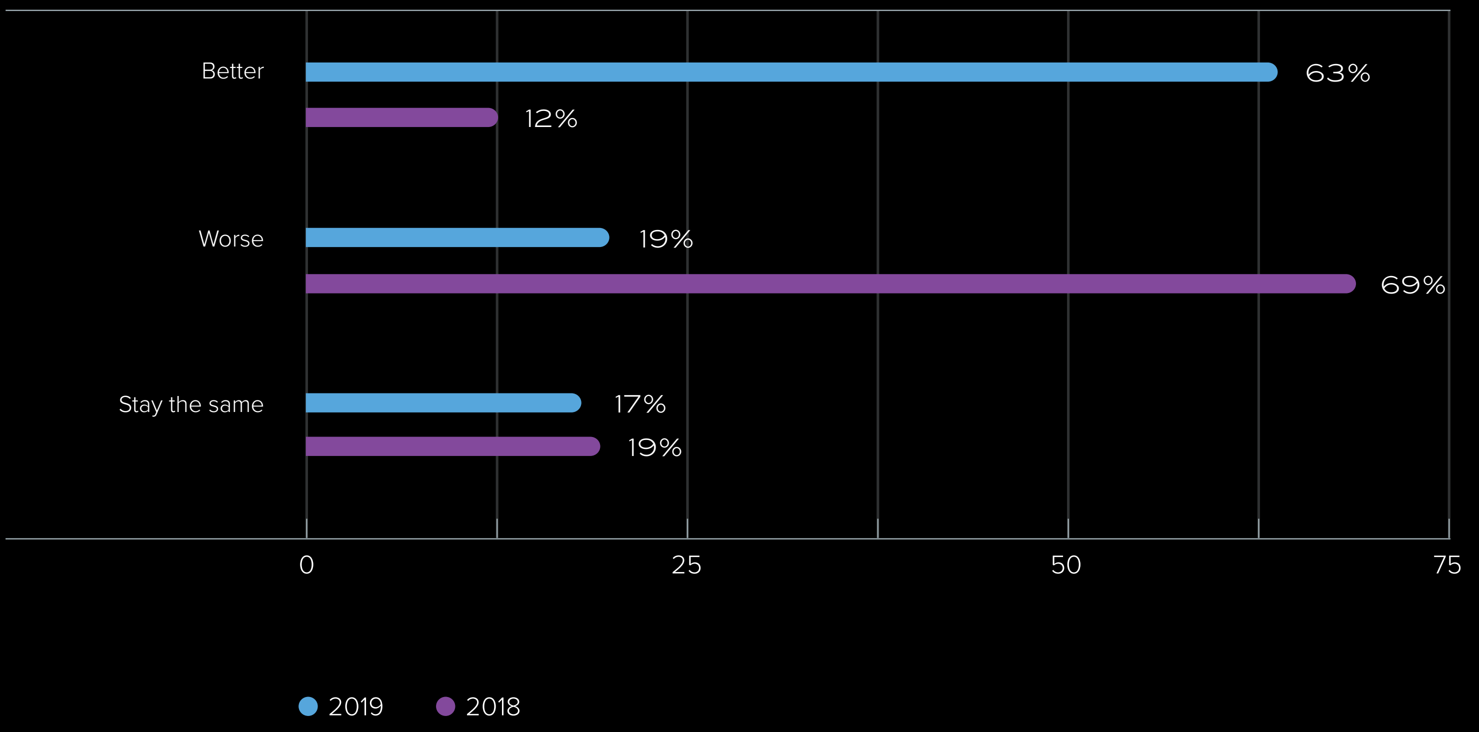
Against this backdrop, it should come as no surprise that institutional allocators continue to find value in less-liquid strategies.

Of the respondents who said they allocate to less-liquid strategies, an overwhelming majority (70%) said their primary motivation was to improve performance. Illiquid strategies may offer a haven, of sorts, to investors as interest rate-driven markets shift. These strategies can be less volatile due to their less frequent mark to market.

Those institutional investors who allocate to asset managers with deep experience navigating credit and economic cycles stand to benefit.

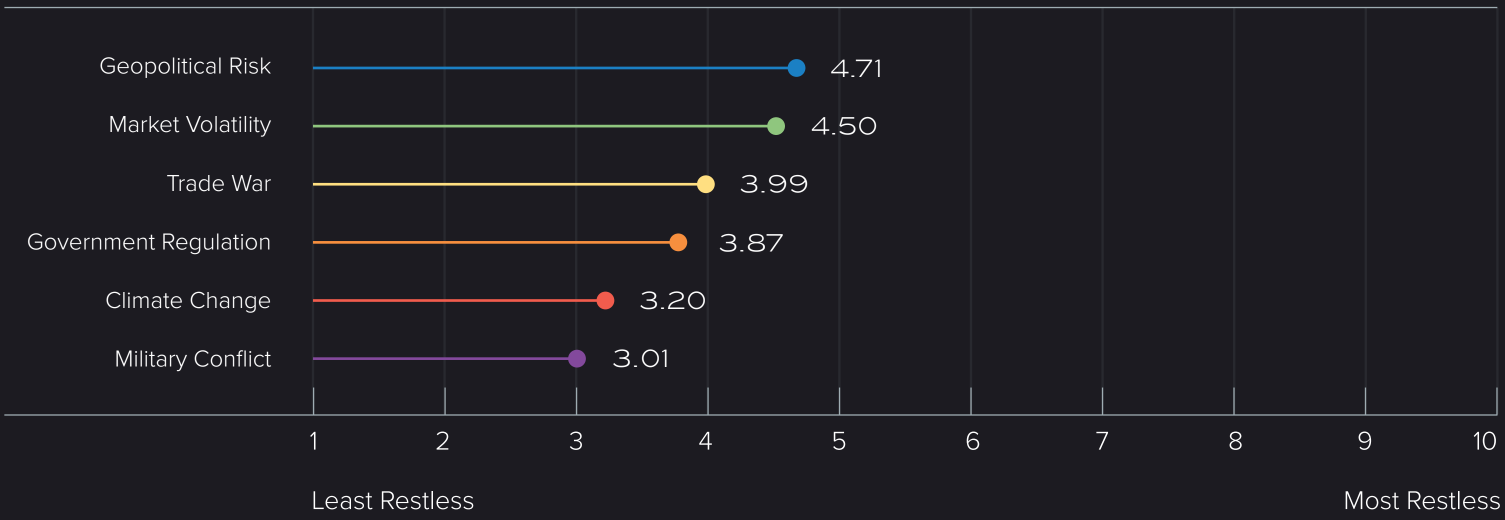
Despite trepidation over a potential market crash and a shift in the credit cycle, we expect allocators to continue to seek opportunities in less-liquid strategies.

Do you think the market will perform better or worse this year compared to last year?



What's Top of Mind—Allocators' Biggest Concerns

On a scale of 1-10, with 10 being the most restless, how much are each of these topics keeping you up at night (ranked most to least)?



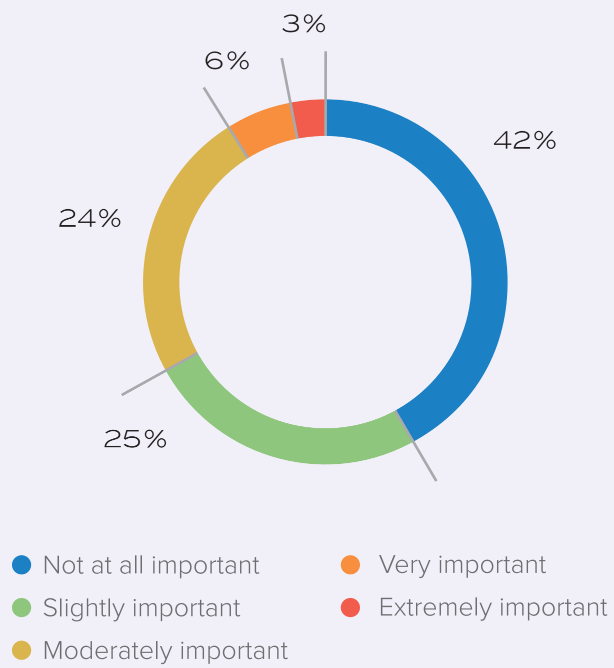
As with every new year, 2019 arrived with equal parts promise and peril. For allocators in Miami, it's the latter that keeps them up at night. The data show that geopolitical risks worry allocators the most, followed by market volatility and the threat of trade wars. These three things have much in common, and offer a telling reflection of the topics that have dominated headlines in recent months.

In contrast, allocators were less immediately concerned about climate change and the threat of military conflict. Investors seem fairly confident that neither risk will threaten markets in 2019.

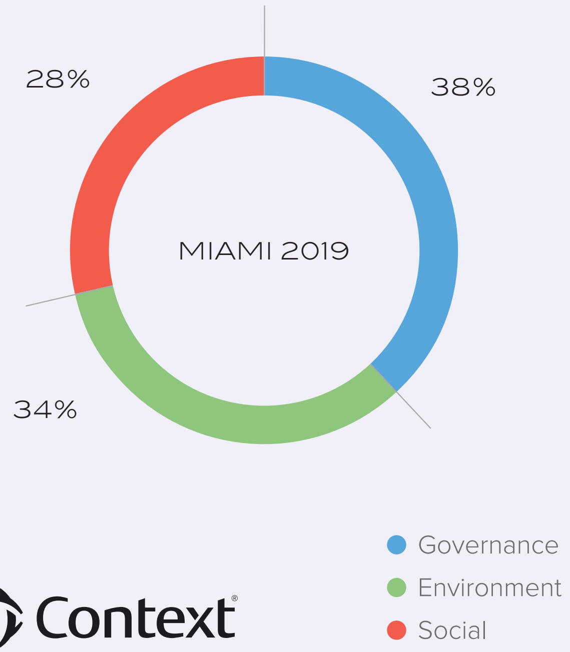
There is certainly no shortage of things for investors to be concerned about in today's world. But risk also equals opportunity. Alternative asset managers are better positioned than traditional asset managers to take advantage of these risks and deliver differentiated returns. Whether it's offering a unique view of how a trade war will play out or constructing a portfolio that prioritizes companies offering sustainable solutions, the alternative investment industry is set up to offer investors a path to navigate market volatility and uncertainty.

Investor Trends in ESG

How important are ESG (Environmental, Social, Governance) issues when evaluating strategies?



Which factor is most important to your portfolio?



ESG investing continues to come into the mainstream within the alternative investment industry. More than half of allocators (58%) attending Context Summits 2019 said they consider ESG issues when evaluating strategies. Further, allocators' conviction is significant, with a full 33% reporting ESG considerations are moderately to extremely important.

This is an interesting uptick from the 38% of investors who reported they consider ESG or responsible investing factors as part of their overall investment strategy at last year's Miami Summit. Of that group, 51% also indicated an intention to increase allocations to these funds. It does seem some of them followed-through for this year.

There is little conclusion to draw from which factor is most important between governance, environmental, and social as results showed each of them captured about a third of responders. For now, governance seems to have a very slight edge as being more important relative to social and environmental factors. It will be interesting to track this trend over time.

Conclusion

Despite dramatic headlines and news reports dominating 2018, allocators continue to embrace the value of alternative investments. With the backdrop of last year's historic market performance, investors remained consistent with our Miami 2018 Allocator Trend Report findings reporting a plan to maintain their net positions allocated to alternative investments. Further, the vast majority of allocators continue to report a plan to increase their alternative investment allocations.

While the alternative investment industry may be in a state of evolution, investors remain steadfast in their commitment to the alternatives market.

As for the markets, this audience is also consistently optimistic with their 2019 predictions. While there is a drop (11%) in optimism from 2018 to 2019, pessimism gained no ground and remained at 5% or less when comparing this year's report to last year's.

Context Summits Miami allocators are a highly engaged audience, evidenced by the fact that over 80% of respondents report allocating to at least one fund met at a Context Summit.

In evaluating this success, we have found investors from family offices to pension funds come to our events to discover innovative strategies from emerging and established managers. By facilitating an environment where investors can match their searches with strategies, and managers can match their strategies to allocator searches, the Context Summits model continues to attract engaged investors and top performing managers.

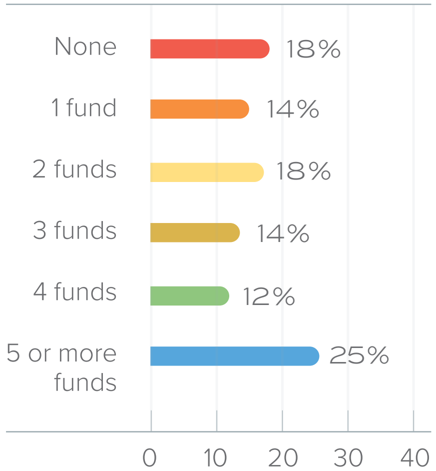
Survey Methodology

The survey was conducted to provide insights into allocator trends for 2019 and offer a snapshot of their current outlook for the alternative asset management industry. The report summarizes the survey findings and reflects one-on-one and small group interactions at Context Summits Miami 2019, which was held at the Fontainebleau Miami Beach Hotel from January 30 – February 1.

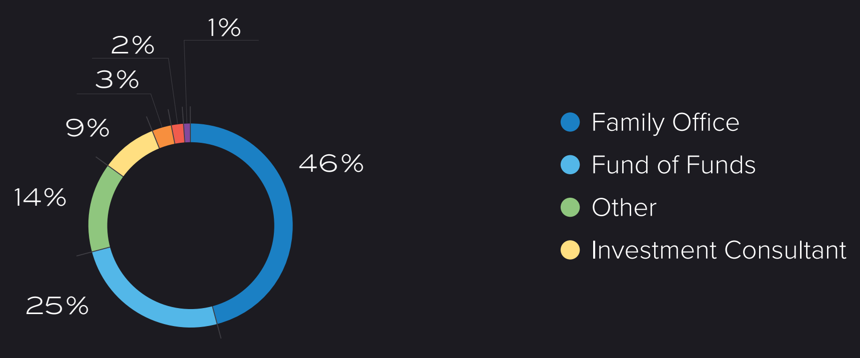
In its sixth year, Context Summits Miami 2019 assembled more than **2,100** attendees, representing over **525** fund managers managing $3.5 trillion (at the firm level), and more than **650** allocators and family offices managing **$1.3 trillion** in alternative assets.

Data is based on responses from almost 450 allocators, including family offices, fund of funds, investment consultants, foundations and endowments, sovereign wealth funds and pension funds. Not all attendees answered every survey question. About two thirds of respondents (68%) were repeat attendees of a Context Summits event. Nearly 80% of respondents said they had allocated to at least one fund due to their attendance at a previous Context Summits event, including a quarter who have allocated to five or more funds.

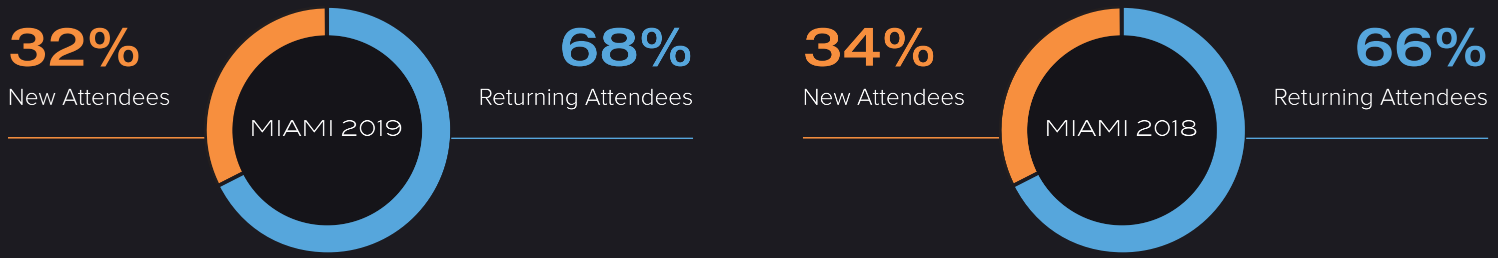
How many funds have you allocated to that you met at a past Context Summit?



What type of investment firm do you work for?



ALLOCATOR PROFILE



About Context Summits

As the preeminent producer of events for the alternative asset management industry, Context Summits focuses on elevating the conference experience through an innovative format and structure where relationship building leads to unmatched results. A pioneer of the one-on-one “summit” format, Context Summits utilizes an innovative approach to deliver effective and transparent networking events that elevate the conference experience for managers, allocators, and service providers. Through its systematic approach, Context Summits is able to attract high quality attendees, making meetings efficient and productive. For more details, please visit: http://www.contextsummits.com

About Context Capital Partners

Context Capital Partners, LP is a leading alternative investment specialist firm headquartered in Bala Cynwyd, PA. Through direct and indirect partnerships, Context provides seed capital, marketing, distribution, operations and infrastructure support by partnering with top-tier alternative asset managers. Context's focus is delivering superior investment solutions to institutional investors and family offices by launching and expanding low correlation investment products that deliver clear edge. For more information on Context Capital Partners, please visit: www.contextcp.com

Upcoming Summits

Context Summits Europe 2019
May 12-14, 2019
Fairmont Monte Carlo
Monaco

Context Summits West 2019
June 2-4, 2019
Terranea
Rancho Palos Verdes, CA

Context Summits New York 2019
October 3-4, 2019
Hilton Midtown
New York, NY

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