H1 2023

The Alternative Investor

A look back at the first half of 2023

A collection of guest articles looking at alternative asset allocation, family office trends, Dubai's emergence as an alts hub, wine, whisky, watches, plus much much more...

A Brodie Consulting publication in conjunction with Capricorn Fund Managers and RQC Group.

#26

Contents

H1 2023 overview

For alternative managers, the first half of 2023 was a trip into unchartered waters - rate rises, confused central bank messaging, misfiring economies and ongoing war pressures - it was challenging, tiring and full of nasty surprises.

We may only be halfway through the year, but managers have already needed a complete toolkit to perform!

So far, the hedge fund heroes of last year, the quant and macro funds, have made heavy work of it, with many reporting disappointing numbers. A belief - albeit briefly - that macro was back has proved wide of the mark. On the other side of the fence, the zeroes of 2022, particularly the equity and crypto managers, have had a pretty good year-to-date, primarily buoyed by the rebound in tech stocks and the crypto reversal.

In such an environment, with so much investor uncertainty, the hedge fund world has continued to see asset outflows, with the exception of multi-strategy funds. Ironically, this is a time when investors need as much diversification as possible, so the case for such exposures should be strong.

Brand strength has become critical to investor allocation, with big brands seeing the bulk of the flows. Brands provide a layer of comfort, with investors derisking themselves by going down the "nobody ever gets fired for buying IBM" route,

The best example is Blackstone, which has just broken through the $1 trillion asset marker, and yet, at the same time, the firm has been battling reputational issues over BREIT liquidity.

However, being a brand is not a guarantee of positive asset flows. Carlyle showed what not to do last year, given its inner turmoils, and now, even with a new high-profile CEO doing all the right things, it is proving hard work to turn things around. Similarly, Tiger Global has been finding fundraising more difficult, with recent good numbers still overshadowed by last year's annus horribilis.

Without a strong brand, a tangible presence and associated assets, it is a demanding fundraising environment and unlikely to change anytime soon. These 'associated assets' include new longer-term institutional offerings, with Blackstone and Apollo, among a number of big names, to be strengthening their businesses and links to the family office space.

> ... 2023 has been more than just brand - it is also about offering the right strategy for the times...

2023 has, however, been more than just brand - it is also about offering the right strategy for the times, which today for hedge funds is multi-strategy and private equity/ hedge is private credit and secondaries.

This year we have seen activists at full throttle, with more than 100 in Europe alone. Elliott has been as busy as always, while Hindenburg Research has gone all out chasing whales, starting with Gautam Adani and then Carl Icahn.

Can we expect a change in the second half? Hopefully, there will be improvements, with an end to rate rises and possible glimmers of light, but the likelihood is more of the same. What is certain, the lion's share of the assets will continue to flow to the brands, but those funds that make a strong case for diversification with exciting ideas and high-quality teams are also in the frame to raise decent assets.

Alastair Crabbe

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The Rise of Family Office Investment Funds – An Emerging Trend

SEEMA CHANDARIA AND DAVID W. SELDEN, PRICEWATERHOUSECOOPERS UK

The number of family offices across the globe has risen steadily over the past decade, and family offices are playing an increasingly important role in the private markets. In Europe alone, both the volume and value of family office deals – whether as the target location or origin of a transaction elsewhere – are running at record levels.

A less conspicuous trend that has been gaining pace among private clients and family offices for several years and that really took off in 2022 is the establishment of family office investment funds. While these vehicles are established for a variety of purposes and with a variety of structures, the common theme has been the utilisation of structures more common to the investment funds space in lieu of (or in addition to) more traditional estate planning and wealth management vehicles.

Seema Chandaria, PwC

DRIVERS AND BENEFITS

The emergence of this trend is driven by a number of factors. Fund-like structures are inherently flexible and may be used (among other reasons) in order to:

- pool a dispersed array of investments into a single, actively managed structure;
- provide a means of allowing multiple family members and estate planning vehicles to participate;
- concentrate investment capital into a vehicle that can make investments with larger impact (ESG or otherwise);
- allow family members to elect which investments or asset classes they would like to participate in;
- enable participants to invest confidentially, protecting their identity and minimising reputational risk;
- centralise decision making and administration, which may in turn yield cost savings and consistent application of best practices;
- create a consistent and "market" approach to incentivising investment professionals;
- establish an avenue for managing third party capital.

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COMMON ISSUES

Just as no two families are the same, the ideal fund structure will vary from family office to family office. Each family brings to the design process its own purpose, pre-existing investment structures, tax considerations, estate planning vehicles, jurisdictional footprint and vision for the future. Having said that, there are some questions that will typically require consideration with the appropriate advisers:

- Which jurisdiction should the fund vehicle be established in, and from which jurisdiction will it be managed?
- What is the investment profile of the fund? For example, is the family targeting liquid or illiquid assets, or both?
- What structures will work best from a tax perspective?
- Will the fund or its manager require regulatory authorisations?
- How will investment professionals be compensated and incentivised?
- What service providers will be required?
- What sort of governance and reporting structure is appropriate?
- What commercial terms are appropriate? For example, what rights will participants have to withdraw capital?
- How will the family's values be expressed through the vehicle (e.g., through social impact investing or sustainability considerations)?

CONCLUSION

Undoubtedly, many of the key trends in 2022, including strategic asset allocation, growth in sustainable investment/ESG and investment into tech/digital assets as well as succession planning and managing reputational risk, will continue to influence how family offices think, invest, and operate. Private clients and family offices remain agile, exploring new avenues to manage and grow their wealth – investment fund structures have proven to be an important addition to the family office tool kit and we expect this emerging trend to continue into 2023 and beyond.


David Selden, PwC

David Selden joined PwC UK in 2020 from US law firm Fried Frank and Seema Chandaria joined in 2021 from international law firm, Osborne Clarke. Together, they bring together the experience and credentials to support the firm in delivering a new integrated tax, legal and regulatory service to global fund clients as part of PwC's market leading Financial Services Tax team.

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Trends which governed the family office space in 2022

CHARLIE HARRIS, LUTYENS ADVISORY

Unusual and disruptive macroeconomic events dominated the financial headlines of 2022. However, whilst attention was so often fixated on the behaviour of governments and central banks, it is worth addressing how a year of political and economic uncertainty was met by investors and, more specifically, those working in the family office space. Irregular market conditions elicited the acceleration of multiple emerging trends within the space, granting a glimpse into what its future may hold.

Amongst these trends included the growing pressure for institutionalisation. Long gone are the days when employees were assembled from a pool of distant relations and friends. A new wave of first-generation Principals are now demanding offices which reflect the rigorous business practises from which they built their wealth.

With this comes a new approach to recruitment, with the investment in executive search firms now seen as a necessary expenditure to ensure an inflow of high-quality human capital. This has resulted in a widening of the available candidate pools alongside a concurrent increase in employee compensation expectations, as those moving out of institutional investment managers bring their skills and experience at a premium.

Charlie Harris, Lutyens Advisory

However Joel Press, as quoted by James Williams in a recent FamCap article, notes that this is no bad thing. If Principals want their wealth managed securely then they need to approach their family office as though it were a "commercial firm". This includes treating, and renumerating, employees in a way which reflects what they bring to the organisation. Doing so ensures a Principal builds not only a technically proficient team, but also a culture which reflects the aims of the Principal themselves.

REASSESSING LOCATION

Institutionalising the family office has also required a reassessment of its location. Whilst competitive tax rates mean that Singapore and Monaco have remained popular there has been a noticeable increase in UHNWI relocations to other destinations. The Henley Global Citizens Report

> A new wave of first-generation Principals are now demanding offices which reflect the rigorous business practises from which they built their wealth.
>
> Charlie Harris, Lutyens Advisory

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2022 recorded a record number of investment migration applications in a single quarter, with this only offering a proportional reflection of the HNWI movement which occurred during the year.

Noticeably the UK has seen a sharp increase in American interest. The sterling's relative weakness has offset the UK's historically unattractive tax rates, with a large number of tech entrepreneurs looking to relocate out of Silicon Valley. Moreover, the UK's internationally 'safe' reputation means Principals, considering familial welfare alongside their commercial interests, have begun to realise, and act upon, London's offerings in both areas.

ESG

Finally, any article reflecting on the past year would be incomplete without a brief mention of ESG; no longer a future concern, the acronym has become a dominant force in guiding future business planning. The family office's attention to wealth preservation means that incorporating Article 8 into investments is now viewed as vital in 'fireproofing' any organisation. Moreover, in light of concerns about generational transition, Principals are increasingly conscious that their investment practises embody the interests of those who will inherit their wealth.

This necessitates going beyond a tokenistic acknowledgement of ESG; the personal nature of family offices means Principals must be aware not only of the financial risk of greenwashing associations but also its potential for reputational damage. Recent research by KPMG showed that one in five corporate risk incidents linked to ESG were the result of greenwashing. As such, whilst the past year showed sustainability-focused investments hold great promise for family offices, it is an area which must continue to be approached with care and due diligence.

THE FUTURE

Looking ahead to 2023, the family office space remains an exciting one to observe. The trends of the past year have shown its structures to be more malleable than its traditional connotations imply, promising another 12 months of challenges and changes to how the space operates and is perceived.

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Back to the future... for crypto

VINCENT MOLINO , HEAD OF OPERATIONAL DUE DILIGENCE, BITWISE ASSET MANAGEMENT

For those who remember the popular film Back to the Future (1985, Universal Pictures), the central character, Marty McFly, accidentally travels back in time to the 1950s, and in doing so alters his family's future by changing the past. Marty, aided by his friend and time machine inventor Dr. Emmett Brown, must fix what had been disturbed in the past in order to restore the future world from where he came. However, after Marty fixes what he believes to be the right order of the past, what results upon returning to his time (spoiler alert!) is a different and better future for him and his family, due to Marty's leaving a bestselling sci-fi book idea with his younger father, which his father successfully authors in the new future.

> As we look back on 2022, many may be wishing for crypto to have a Back to the Future moment, as there are a number of operational failures that the industry would hope for a chance to correct.
>
> Vincent Molino, Bitwise Asset Management

As we look back on 2022, many may be wishing for crypto to have a Back to the Future moment, as there are a number of operational failures that the industry would hope for a chance to correct. Fortunately, while time travel is still the stuff of fiction, an opportunity exists to create a better crypto future in 2023 and beyond.

Counterparty selection and risk management is likely the most significant issue which many would hope to go back in time to fix. Specifically, the failures of centralized exchanges and other crypto intermediaries have caused industry participants to question the safety of centralization, which in turn has led many down the path to directly transacting or self-custodying crypto assets.

Yet in this case the rearview mirror may be a poor guide to the future. As we look forward, there are several ongoing factors which favor staying the course with centralized third parties. First, an increasing number of crypto brokers and custodians are voluntarily submitting to regulation, and in doing so are subjecting their operations to regulatory oversight and reporting. Second, many of the same counterparties are also voluntarily, or as mandated by regulation, producing company financial statements and initiating independent audits, which should always be available for clients to review.

Third, as the crypto counterparty space evolves, an increasing number of these businesses are purpose-built for their respective functions, be it as a trading counterparty or as a custodian, and as such can provide product controls

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and services that address the specific needs of their clients. Examples of such controls are multi-party transaction authorizations, hardware security features, and in some instances physical security services.

Legal structures and agreements were another source of pain in 2022. Many crypto industry participants have learned the hard way that properly documenting bilateral terms and related recourse, giving careful consideration to contracts, and ensuring legal rights are recorded and understood must no longer be ignored in the name of getting business done. Future best practices for legal agreement processes should include seeking tri-party agreements, which can for example separate the risks of facing an exchange and an affiliated custodian. Another best practice, specific to investing in legal entities such as venture capital or hedge funds, is negotiating a side letter that can afford an investor specific desirable provisions like increased transparency; notification of organizational, legal, or regulatory events; and receiving reasonable financial documentation.

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> Vincent Molino, Bitwise Asset Management

A glaringly obvious 2022 issue, which encapsulates both of the above subjects, is the poor or severely lacking due diligence, which surprisingly has caught up many, including institutional investors. As has been publicly reported, and often relayed to investors in an apologetic manner, many industry leaders have admitted to doing little to no research on businesses which had been entrusted with client assets. Here, the simple solution to ensuring a better and risk-reduced crypto industry is conducting a thorough amount of due diligence, which should include the practices of understanding the organization one is scrutinizing, the people running the business, the operational processes and controls in place to reduce business risks, and the tools at your disposal to effectuate such due diligence, inclusive of requesting and analyzing documentation (audits, financial documentation, policies, etc.), conducting interviews, and assessing the risks that are identified.

As the above remedies make clear, the reality is that much of what caused the volatility in the crypto industry throughout 2022 is not issues related to the fundamental capabilities of crypto, blockchains, and related technologies, but rather an unfortunate choice of lax standards. This raises important questions: Does crypto have something better to offer? Is the industry able to turn a corner and put many of these traditional business issues behind it? In addition, what should be considered for crypto operations in 2023 and beyond?

One problem that will persist in the near future and beyond is cyber attacks. Attacks, breaches, and the subsequent stealing of data or assets remain a large problem for all industries, resulting in billions of dollars of losses. A truly crypto solution to such cyber risks is the operational capabilities of DeFi technology and protocols. DeFi removes much of the ability for intrusion to occur through the implementation of smart contracts. While traditional technology can allow someone to breach a central data source and be able to track or transmit information while undetectable, smart contracts can access data feeds, APIs, transactions, and accounts without blindly trusting a single, centralized source.

DeFi, by its very definition, is built to provide access to financial services for participants outside of the centralized crypto venues and products mentioned above. Yet this begs the question: How are participants going to access DeFi?

Ironically, the most likely way access to DeFi will be provided in the future is through some of the centralized players that exist today. In addition to crypto wallet providers and crypto exchanges, traditional market participants such as banks and brokers will likely be a common path for many individuals and most institutions to access DeFi. The simple reason is that these players have the resources (and potential motivation) to develop their own DeFi infrastructure and applications, in addition to existing services and policies such as client onboarding, AML checks, and other safeguards desired by most market participants.

Just as Marty McFly had to deal with the tribulations of his family's past in order to secure his future, crypto is having its moment of needing to fix years of missed operational readiness and insufficient risk management. Although there is no time machine to avoid the failures and volatility of 2022, there is nevertheless an opportunity to mature, create longevity, and ensure a better future for the crypto industry, its participants, and investors.

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UK Compliance Review of 2022

MATT RAVER, RQC GROUP

When the economy wobbles, it would appear that there are two somewhat distinct politically-driven regulatory responses.

The first was seen in the aftermath of the 2008 financial crisis which saw a dramatic increase in regulatory requirements.

Arguably and in retrospect, not all of this was required. For instance:

- AIFMD was in part borne out of an aspiration to obtain greater transparency on highly leveraged portfolios, or portfolios containing certain asset classes such as securitised assets. However, AIFMD applies to all non-retail funds regardless of investment strategy and other characteristics.
- For many firms, in particular, those in the non-retail sector, the product governance regime (eventually) introduced as part of MiFID II in 2018 is a papering exercise that doesn't add any tangible incremental regulatory protection to investors.

The second is where there is a political imperative to adjust the regulatory environment to afford a country a more competitive edge. After several decades of adopting regulation in tandem with the rest of the EU, the UK is now able to follow a different path. 2021 – the first year following the end of the Brexit transitional period – was something of a 'phoney war' – there was not much activity in terms of financial services reform and the regulatory framework that had been adopted from the EU looked broadly the same. 'Evolution, not revolution' was an oft-used phrase. However, 2022 has re-set the dial on such matters, an initiative effectively put in motion by the UK's first Chancellor of the Exchequer (now, Prime Minister) of 2022 with the year's fourth Chancellor applying the coup de grace.

Matt Raver, RQC Group

The Financial Services and Markets Bill was introduced to Parliament in July. The Bill, which is expected to become law in 2023, aims to tailor financial services regulation to UK markets to bolster the competitiveness of the UK as a global financial centre. Politically it was announced that hundreds of pieces of retained EU law will be repealed. A closer examination reveals that this does not include onshored EU primary legislation such as MIFID, MiFID II and UCITS.

> What might be more relevant is affording financial services certain powers so that the UK can act more nimbly to implement regulatory change.
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> Matt Raver, RQC Group

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What might be more relevant is affording financial services certain powers so that the UK can act more nimbly to implement regulatory change. Over time, this might accelerate the divergence from the EU rulebook and in a way that directly affects investment firms and asset managers.

Then in early December, Chancellor Hunt announced the 'Edinburgh Reforms' – a 'bold collection of reforms' to propel the government's ambition in creating a financial services sector that is open, sustainable, technologically advances, and globally competitive. Revising the ring-fencing requirements for banks that were put in place post-2008 financial crisis is one of the more high-profile aspects of these reforms. However, there are other aspects affecting investment firms and asset managers covering topics such as the senior managers and certification regime, short selling, securitisation, crypto, research, sustainable finance and the UK fund regime.

The reforms are in fact a series of initiatives that will be implemented over time, and we are very much at the start of the process. Whilst there will be no 'big bang,' it appears to be the case that the pace of regulatory evolution will increase in the coming years.

Away from holistic regulatory change, there were a number of regulatory themes that were brought to the fore within 2022 or were carried forward from previous years.

At the start of 2022, the most meaningful impacts of Covid were in the past. However, regulatory hot topics from the pandemic remained in situ. In particular, the operational and financial resilience of firms, including business continuity and cyber security.

The invasion of Ukraine added some hitherto unplanned regulatory hot topics to the agenda. The invasion pushed international sanctions regimes to the fore like never before, and there was also associated regulatory commentary on the impact of the invasion on anti-money laundering and market abuse.

Most investment firms and asset managers became subject to a new prudential regime – the Investment Firms Prudential Regime ('IFPR'). This includes putting in place a new 'harms assessment' document, the ICARA, and has also prompted a further regulatory interest in the resilience of firms during periods of stress or a wind-down of business operations.

As the year progressed, the FCA promoted a more 'hard-line' stance on matters such as regulatory permissions and the FCA application process. Regarding the former, the FCA announced that it would 'act faster' against firms that fail to meet its Threshold Conditions. This would lead to an increase in the number of cancellations and withdrawals over the next three years. The FCA can amend or cancel a regulated firm's permissions, for example if a permission is not being utilised.

As summer arrived, there were some important developments on a key regulatory initiative – consumer protection. This included the publishing of the final rules on the Consumer Duty – which takes effect in July 2023 – and an initiative to further monitor so-called 'high-risk investments.'

Whilst these have a retail slant, they are of potential relevance to firms in the 'alternatives' sector, a point made by the FCA in their 'Dear CEO letter' to such firms. Other main risks of harm articulated in the letter included the importance of conflicts of interest, risk

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controls including market abuse risk controls, conduct and culture (including the influence of senior managers, diversity and inclusion and staff remuneration) and ESG.

In October, the FCA took a significant step forward with its ESG regulatory requirements for the investment sector with proposed new requirements related to sustainability disclosures and investment labels. A new anti-greenwashing requirement is also proposed. These requirements are in addition to already introduced climate change disclosure requirements affecting various industry participants. Firms operating internationally are increasingly finding challenges in adopting multiple regulatory standards concerning ESG.

In early December the regulatory requirements on Appointed Representatives were updated, with additional operational and disclosure requirements imposed on Principal firms. Whilst – again – this has a consumer focus, it also affects the non-consumer investment firm sector, where a number of Principal firms are in operation.

Crypto continues to set challenges for regulators including the FCA. In the UK, crypto assets such as Bitcoin are regulated for money laundering purposes only, and they are not considered to be financial instrument types which means, for example, providing investment advice on crypto assets is not a 'regulated activity.' The Financial Services and Markets Bill would give additional authority and powers over crypto assets to the FCA and the Bank of England. November's collapse of FTX Trading further spooked the authorities. So do not be surprised to see significant regulatory shifts in this sector in 2023.

There was a marked increase in the number of publicly announced FCA enforcement actions as the year drew to a close. These served as a reminder that the FCA will sanction firms for systems and controls failings, even if there is no demonstrable harm as a result of this, and individuals – in particular senior managers – can also be sanctioned for their role in such failings.

Finally, for individuals such as senior managers or certification function holders, attacking a nightclub bouncer with a machete is not a wise move. As the FCA noted, they 'will continue to uphold high standards of character and conduct for those working in financial services.'

Matt Raver has been a Managing Director of the RQC group since 2013, where he supervises the teams dealing with technical regulation, regulatory change, regulatory submissions, and technology. He started at Morgan Grenfell and Nomura.

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Passion and pleasure continues to drive the watch market

BENOÎT COLSON, DIRECTOR, INTERNATIONAL SPECIALIST, SOTHEBY'S

We are constantly hearing contrasting views on today's second-hand watch market. On the one hand, after a couple of years of intense enthusiasm and euphoria, there is chatter about the market going through an unprecedented crisis, with some even predicting its demise. Yet on the other, there are those who believe the market has a bright future ahead, with plenty of growth opportunities.

Why such a difference of opinion? Simply put, they are not talking about the same topic.

The first group refers to a particular market segment: contemporary sport watches trading on the grey market. For example, Mr. Smith buys such a watch from an Authorized Dealer, who flips it immediately to another person, either a dealer or a private, who sells it on, etc. Until recently, there was enough demand and margin for a few people to make some money and with the continuous price increase helping, this pattern could continue.

> Remember at the top of a bubble, everybody is a dealer and everybody looks like a genius...
>
> Benoît Colson, International Specialist, Sotheby's

There is nothing new here, but the critical shift we have seen over the last couple of years has been the dramatic increase of players in this field; as a result, this became the focus of the second-hand market, which overtook and overshadowed other segments. Ultimately, it went too high, too quickly. Remember at the top of a bubble, everybody is a dealer and everybody looks like a genius - money was easy for newcomers, and everybody wanted a piece of the cake.

PATEK PHILIPPE REFERENCE 2499

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PATEK PHILIPPE 'SAATCHI EDITION'

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This speculation was fed by people lacking two key qualities required by any investor, nerves and knowledge. They mostly had little or no interest in watches – it was an opportunistic trade. Consequently, they lacked a real understanding of the market, the segments and their respective sizes, the products and there was no attachment or passion; a watch was just an asset to be sold with a quick profit at no risk, or at least they thought. The result has been a market correction in this space.

These market participants and their investments have overshadowed other parts of the sector that have continued to grow steadily and see higher demand. Here we are seeing two very encouraging trends. The first is the continued growth of the traditional market, namely vintage and more recently neo-vintage watches. The second is that with incredibly high prices requested for standard contemporary pieces, some collectors have started to acquire rarer, more complicated, safer-to-wear pieces for a much lower investment. This has resulted in greater demand for timeless, historically important, 'meaningful' watches across all price segments. Many of these same timepieces have seen their value quietly growing, sometimes by over 50%, particularly over the past 36 months.

> **The entry ticket for a Patek Philippe split-second chronograph perpetual calendar or a high-quality vintage Rolex Daytona does not encourage newcomers as a starter.**
>
> Benoît Colson, International Specialist, Sotheby's

To take a few examples from some of our 2022 auctions:

A 1957 Patek Philippe Perpetual calendar chronograph 2499 second series *(see picture on previous page)* in pink gold double signed by Milano-based retailer Gobbi, sold for a world record price of HKD 60,265,00 (EUR 7,027,000). The same watch was sold in 2007 for CHF 2,736,000.

The market for high-quality vintage sport Rolex is in rude health, with several record prices achieved in the last few months. This includes the Rolex Daytona Paul Newman *(see picture over page)* in 18k gold reference 6264, that was made in 1970 and recently sold for over GBP 1 million.

In the neo-vintage and even contemporary market, some rare and special pieces have seen their value going through the roof. One example is the Patek Philippe 3940 *(pictured above)* in pink gold with a brown dial made for the Patek Philippe Grand exhibition in London in 2015, which sold for a record price of CHF 214,000.

While it is difficult to predict the future in any market, the mid and long-term trend in our world is the same as ever: quality, rarity, historically interesting,

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ROLEX DAYTONA PAUL NEWMAN
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and timeless pieces from blue chip brands. This has seen a return to the basics, such as a precious metal complicated Patek Philippe; a quality vintage sport Rolex or Day-Date with special dials; and rare and limited-edition form-watches by Cartier, to name a few. The entry ticket for a Patek Philippe split-second chronograph perpetual calendar or a high-quality vintage Rolex Daytona does not encourage newcomers as a starter.

Neo-vintage watches (roughly 1985 – 2005) offer the opportunity to acquire rare pieces made in relatively small quantities, with a broad variety of timeless designs and sizes. This was also when traditional Swiss horology was re-inventing itself, and important brands were launching or starting a new chapter of their history. Think about Lange & Sohne and other independent watchmakers making their first steps, such as François-Paul Journe. This was a wonderful period of creativity that we still have not fully discovered yet. For example, you can still find an automatic perpetual calendar by Patek Philippe for less than EUR 30,000.

The collectable status of a watch will come back. The global secondary market for contemporary sport watches may shrink over the next few years as it corrects, but this is only one part of the market, with vintage and neo-vintage markets looking well placed to continue thriving and growing.

The watch market is both demanding and challenging. It requires knowledge and nerves, but it is also about passion and pleasure. Next time a person sitting next to you tells you the travails of the watch market, you can tell them about the opportunities, growth, record prices, mid and long-term investments, passion, vision, craftsmanship and history. The love of watches should make a heart beat like a well-regulated balance.

Benoît Colson

Director, International Specialist, Sotheby's

Benoît Colson joined Sotheby's in 2014. After six years in London where he was Head of Sale, Benoit moved to Paris as International Specialist. He travels extensively across Europe to meet with clients and has played a key role in securing numerous important consignments.

As a specialist, he has developed an in-depth knowledge and expertise in Patek Philippe and Rolex watches. Originally from Belgium, Benoit holds several master's degrees in History of Art and Art market from the University of Brussels and the École du Louvre in Paris.

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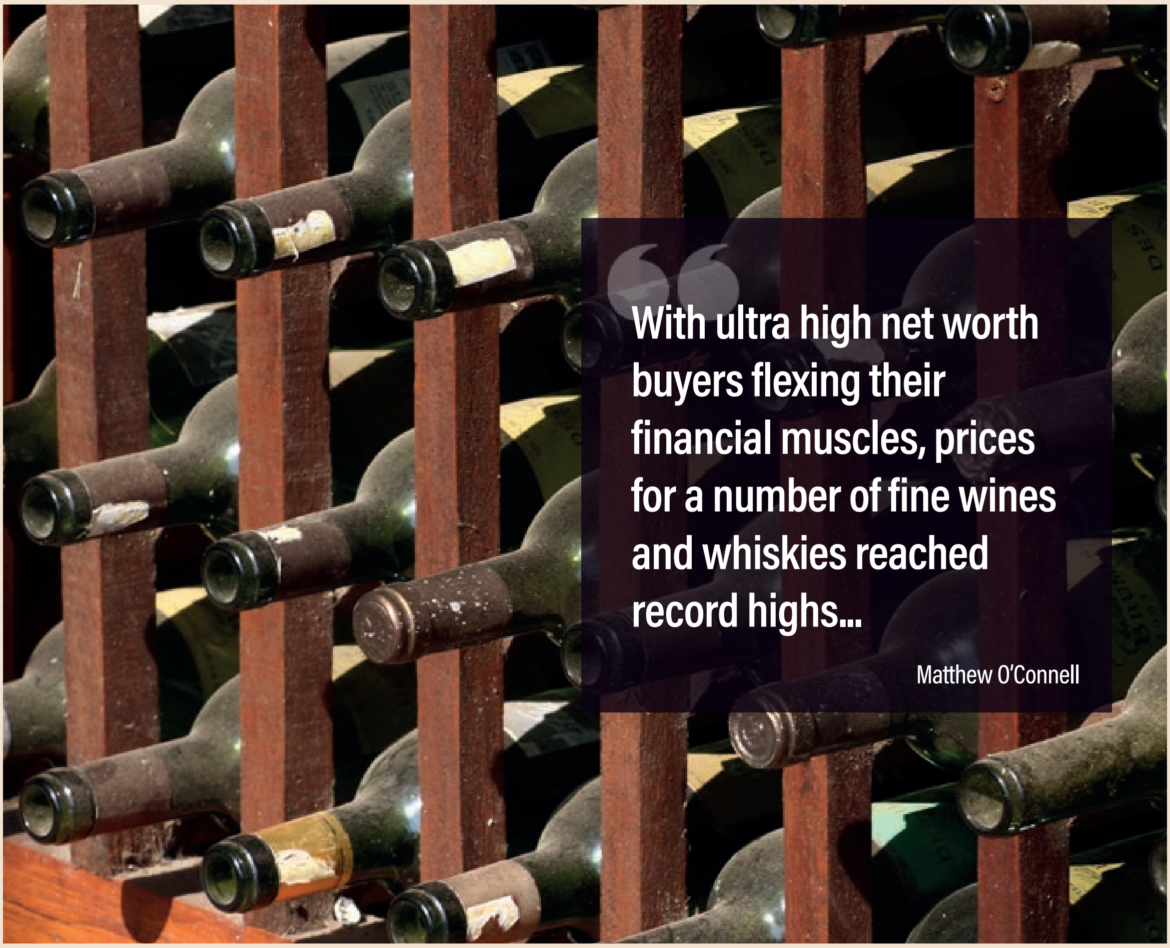
Liquid Gold: Fine Wine & Whisky as an alternative asset

MATTHEW O'CONNELL, CEO OF LIVETRADE & HEAD OF INVESTMENT, BORDEAUX INDEX

As we enter a new year, many will be happy to see the back of 2022, which brought a cocktail of challenges, from Russia's invasion of Ukraine, rising inflation and an energy crisis, to recession fears and slowing global growth. Add Covid, closed Chinese borders, the death of the Queen and the shortest-serving UK Prime Minister into the mix and it's easy to see why the Collins Dictionary chose 'permacrisis' as its word of the year for 2022.

While stock markets yo-yoed, there was a silver lining for fine wine and whisky collectors and investors, as both sectors remained not only resilient in the face of ongoing economic headwinds, but proved themselves as a productive safe haven and inflationary hedge during these turbulent times. With ultra high net worth buyers flexing their financial muscles, prices for a number of fine wines and whiskies reached record highs, particularly with a squeeze on some of the rarest items such as top Burgundy and Japan's Karuizawa whisky.

For proof of the current strength of the rare whisky market look no further than peaty powerhouse Ardbeg. The Islay distillery, owned by luxury goods giant LVMH, sold a rare cask distilled in 1975 to a private female collector in Asia for a staggering £16 million last June, knocking all previous cask sale records out of the park. The growth of the rare whisky market has exploded over the last two decades in line with a huge uptick in ultra wealthy luxury consumers, such that the global thirst for hard-to-source old and rare bottlings has reached unprecedented new heights.



> With ultra high net worth buyers flexing their financial muscles, prices for a number of fine wines and whiskies reached record highs...
>
> Matthew O'Connell

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Given these strong market performances, it is unsurprising that investors are looking beyond challenged tech and crypto assets towards wine and whisky. Both assets exhibit a compelling combination of proven capital preservation and protection against inflation with each returning circa 15-20% in 2022 and 35-40% across the last two years.

Wine is in an upwards phase – it tends to go through cycles of price consolidation and growth – and we see the potential for this to be a sustained growth phase given the increased number of wealthy market participants. If we use Champagne as an example, as well as Burgundy, both of which are reaching an ever-growing consumer base, performance has been +60-70% area over the last two years.

In the whisky segment, the market is being driven by a deep structural supply/demand imbalance driving price growth in rare Scotch in the region of 20% (compound growth) annually over the last decade, equivalent to over +400% gross increase. When there is such sustained momentum in a market, the question of a 'bubble' always arises; but for whisky this seems not to take into account the unique combination of the demand from global wealth, consumption expansion, and a product that is structurally short in supply such that a rebalancing is a decades rather than years-long process. If only distilleries knew in the 1980s and 1990s what they know now; but instead, this was a period where there were now unthinkable closures of distilleries such as Port Ellen, Brora, Ardbeg (temporarily) and bulk liquid selling from The Macallan and others.

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The fine wine investment market more broadly remains incredibly brand-driven, with top name prestige cuvée Champagnes like Cristal, Krug, Dom Pérignon and Bollinger continuing their forward march in what was the second best performing region of 2022. This hyper focus on brand makes sense given the expansion of luxury consumption and new entrants to the market, both collectors and investors, who are more familiar with well-known names and brands. Champagne has benefited from this as has Italy, namely Tignanello and Sassicaia.

The secondary market for rare whisky remains exceptionally strong and has diversified significantly as new names see ever-increasing demand alongside the ongoing growth of longtime leader, The Macallan. There is particularly strong activity in the cask market which many participants see as especially attractive given the ability to own old and rare liquid that is still ageing in an environment where the asset is increasingly scarce. Some distilleries saw price rises of over 50% in casks of 25 years old and over with Springbank, Bowmore and Highland Park being good examples.

Overall, the picture entering 2023 is an interesting one. With wine prices having risen by around 40% over the last two years and some macro headwinds, there is an argument for a period of consolidation being on the cards this year (meaningful price softening being intrinsically less likely, based on there being very few downwards price phases in wine's history and whisky really being upwards-only). However there are some reasonably certain tailwinds for prices – including the reopening of the important Chinese market - along with an ongoing broader positive momentum.

About Bordeaux Index

Bordeaux Index is the world's largest trader of fine wine and whisky operating partly through the leading online platform, LiveTrade. The company also acts as a specialist asset manager with a particular focus on Separately Managed Accounts for UHNW, family offices and other quasi-institutional investors. One of its key aims is enabling access to these compelling asset classes with the same confidence investors would have investing in equities or other traditional assets.

Matthew O'Connell
CEO of LiveTrade & Head of Investment, Bordeaux Index

FEBRUARY 2023

"It does exactly what it says on the tin!"

TOM KEHOE, GLOBAL HEAD OF RESEARCH AND COMMUNICATIONS, AIMA

Viewers of my generation and older will recall the above slogan being used in an advertising campaign for a wood stain and dye manufacturer back in the early 1990s. In fact, the slogan became so popular that the same manufacturer is still using it in advertisements and online media today, to the extent that it has become a common idiomatic phrase.

Thinking about this phrase also recalls the value proposition that an allocation to hedge funds can offer to investors. There is no escaping the fact that the past year has been tumultuous, both geopolitically and economically.

From a performance perspective, leading stock markets including the S&P 500 index and the MSCI World ended the year down around 20%. The fortunes of 60/40 portfolio investors (for a long time regarded as the cornerstone of investing) have not fared much better, also losing close to 20% of investors' money by the end of 2022.

> Amid considerable and broad-based drawdowns, hedge funds have not only performed relatively well for their investors but have materially outperformed too.
>
> Tom Kehoe, AIMA

By comparison, an allocation to hedge funds would have yielded you a gain of 1%, (where performance is measured on an asset weighted basis) according to Hedge Fund Research. Or to put another way, hedge funds gained at least 20% more than a 60/40 portfolio investment.

This is only half the story. There was a wider-than-usual disparity in performance among hedge fund strategies; macro, trend-following any many multi-strategy funds stood out as the best performers, while long-biased equity long/short funds suffered.

Recalling the aforementioned iconic slogan, it's worth examining the collateral benefits of hedge funds.

Looking at previous market corrections, hedge funds have consistently demonstrated their ability to manage these periods for investors better than anyone else. Prior to this period, the last time the market experienced a sharp correction was the onset of the Covid-19 pandemic in the spring of 2020.

At that time, leading stock markets fell 20%, while 60/40 portfolios lost 10%. At the same time, hedge funds on average fell by 6% and ended the year up 19%. Going back to 2008 further demonstrates the resilience of hedge funds.

Had you been invested in stock markets, you would have lost 50% or greater, while the average hedge fund lost 20%, and recovered its losses by October 2010 whereas the average balanced fund did not recover its losses until March 2013.

An allocation to hedge funds serve a range of purposes in investors' portfolios, extending beyond alpha generation. Events of the past year are a timely reminder to investors of the value of capital preservation and reassert the value proposition of hedge funds.

Amid considerable and broad-based drawdowns, hedge funds have not only performed relatively well for their investors but have materially outperformed too. Investors are taking note, allocating to hedge funds with interests across public and private markets.

Such an investment can provide them with more flexibility to protect and grow their capital. Integrating hedge funds into the wider investment portfolio should provide investors with returns that are uncorrelated to returns derived from investing in bonds and equities.

With most forecasts for the coming 12 months predicting market volatility to continue as well as further monetary tightening to curb the threat of prolonged double-digit inflation, the benefits of investing in hedge funds will continue to attract capital.

Tom Kehoe

Global Head of Research and Communications, AIMA

MARCH 2023

Establishing a family office practical & legal considerations

JAMES GOOLD, PARTNER, TAYLOR WESSING

WHY HAVE A FAMILY OFFICE?

Ensuring an international family's global wealth structure meets the family's varied and changing needs can be a daunting task. Many families choose to establish a family office to ensure the family's needs and the relevant legal and regulatory requirements are properly and efficiently met, and to ensure the smooth running of the family's asset holding structures.

The services provided by a family office are varied and may change over time. Services commonly include asset management, co-ordinating tax and wealth planning, administrative and concierge services, and support with philanthropic projects.

> When selecting the most appropriate structure the family's unique jurisdictional, tax and regulatory positions must be considered.
>
> James Goold, Taylor Wessing

WHAT LEGAL STRUCTURE IS BEST?

The legal structure of a family office must necessarily be bespoke – there is no one commoditised solution. When selecting the most appropriate structure the family's unique jurisdictional, tax and regulatory positions must be considered. In the UK, the typical legal form for a family office is either a limited company or a limited liability partnership.

A family office may have several branches or subsidiaries. This may be to divide functions (e.g. if certain jurisdictions provide a better base to perform certain functions), the location of key decision makers or simple geographical proximity to family members located in different countries. Whatever structure is adopted, the ownership of the family office must be carefully considered from the outset, including how the succession of that ownership will operate.

The division of responsibility between family members and specialists employed by (or engaged by) the family office also needs to be carefully considered. A governing board with both family and external representatives is commonly established to ensure that the family's vision is balanced with a degree of objectivity.

The family office may manage the family's investments itself or supervise independent, third party fund managers who provide investment management services. In the latter case, the family office structure

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would tend to be less substantial, and motivated more by geographical concerns. Whereas if the family office acts as an in-house investment manager, the structure would typically be more substantial, enabling the allocation of different functions to personnel with the appropriate expertise. Where a family office manages investments in-house, compliance with regulatory requirements will be key, subject to any specific carve-outs that apply in the local jurisdiction.

HOW SHOULD A FAMILY OFFICE BE FUNDED?

A family office will ideally operate as a self-financing entity (subject to initial start-up capital being provided by founding family members). Family offices will typically charge fees to the entities within the family's wealth structure for providing services and advice.

For a UK family office it is important, for tax purposes, that an arm's length (or commercial) fee is paid for services provided to entities within the family's international wealth structure (whether those entities are offshore or in the UK).

IS THE UK A SUITABLE JURISDICTION?

There are many attractions for locating family office functions in the UK. Its geographical location can assist in supporting family members spread over multiple jurisdictions. Also, and often a key motivator, the UK provides a long-established and highly regarded legal and regulatory infrastructure, along with a substantive network of highly skilled professionals, that are well equipped for supporting the demands of the global family.

That said, given the amount of capital invested through family offices, a number of jurisdictions across the globe are adopting (or have already implemented) entrepreneurial approaches to the tax and regulatory treatment of family offices. Other popular jurisdictions for locating family offices include Monaco, Zurich, Singapore, Dubai, the US and (historically at least) Vienna.

James Goold
Partner, Taylor Wessing

With assistance from **Joshua Boughton**, Associate, Taylor Wessing.

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The new era of family capital

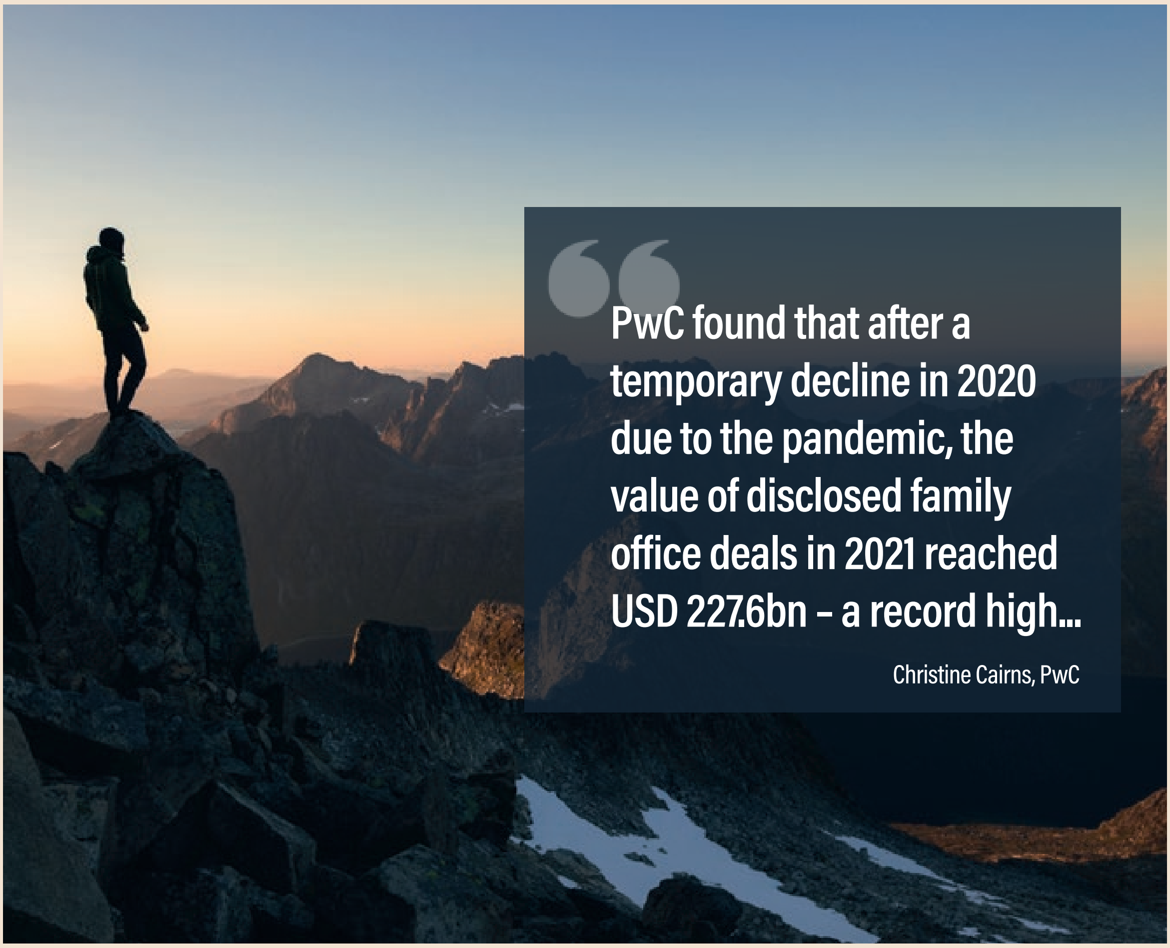
CHRISTINE CAIRNS, PWC, TAX PARTNER

Family offices were involved in an estimated 10% of all deals globally in 2021. In a study of Family Office Deals, PwC found that after a temporary decline in 2020 due to the pandemic, the value of disclosed family office deals in 2021 reached USD 227.6bn – a record high. This marked a turning point, with family office-backed transactions accounting for 10% of the entire deals market for the first time.

This research backs up the emergence of the family office as a key player in the private markets. So much so that even the term "family office" may be better substituted with "family capital" or "family investment firm". Terminology aside, a new generation of family offices are now competing head-to-head for deals alongside venture capital, private equity and sovereign wealth funds.

The traditional "family office" was the protector of family wealth, characterised by passive investing with an emphasis on preservation of capital and a long term horizon. Over the last 30 years, there has been a shift. This shift has been driven in part by the impact of low interest rates on returns and volatility in traditional asset classes, and in part by rapid innovation across multiple new sectors, opening up attractive new areas for family offices to invest in.

However, this alone does not explain the transformation of the "family office" into the "family investment firm". Twentieth century wealth was created by industrial innovation, in sectors such as steel, cars and electricity. By the early 2000s, this was supplanted by the consumer industry, technology and financial innovation, as well as consumer products, globalisation, industrialisation and infrastructure booms in Asia and other emerging markets. Family businesses drove the development of the internet and its ecosystems, led Asia's consumer products revolution and developed its factories, infrastructure and real estate. Global wealth has exploded in the new



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> This evolution is also reflective of a desire for greater control over investment decisions and the ability to make more targeted investments that align with the values and goals of the family, and in many cases of the new generation.
>
> Christine Cairns, PwC

millennium, with more billionaires being created than ever before, and the establishment of more than 50% of current global family offices.

This new generation of modern, ultra-wealthy family offices have deep pools of capital to invest and a more expansive risk appetite than prior generations. In order to gain the edge over other investors (both asset managers and other family offices), those families which first invested in start-ups with blue-chip venture capital or private equity firms opted to set up their own independent operations, creating professional mini "funds" within the family office, establishing effectively another high-performing family business operating alongside the family enterprises that spawned them, with their own professional team, governance, vision and purpose.

This evolution is also reflective of a desire for greater control over investment decisions and the ability to make more targeted investments that align with the values and goals of the family, and in many cases of the new generation. In contrast to passive investment, active investment enables family members to see their capital delivering positive impact in concrete ways, in turn reinforcing family cohesion, and boosting the sustainability of both the family and family enterprise in an increasingly challenging and complex world.

Having reached an all time high in 2021, the growth trend for family office backed deals in 2022 slowed slightly due to the current economic outlook. Notwithstanding this, the modern family office as a key alternative investor is here to stay.

Christine Cairns
PwC, Tax Partner

Christine Cairns is a tax partner at PwC, focusing on private clients and alternative investment funds. She advises on complex international personal tax matters, as well as on tax issues in connection with carried interest, co-investment, management fees, and the impact of fund and deal structures on investors.

Christine works with founders, owners and family offices within the AIF, Fintech, and FS sector more broadly. Over the last few years she has helped a number of her clients structure private investment funds, bringing together her unique expertise and experience in personal tax and funds.

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Private office, private investments? The future of family office asset allocation

CHARLIE HARRIS, LUTYENS ADVISORY

Over the last few years, there has been a slow but noticeable shift in how family offices invest. Although the structural variety within the space means making such a broad claim is risky, the definitive rise in popularity of private investments makes this a trend worth examining in the context of the family office arena.

Although there is no strict 'beginning' to this phenomenon, it is worth emphasising that it is not a trend unique to 2023. Fidelity Investments noted in 2019 that 59% of family offices surveyed would choose to hire their next investment professional from an illiquid asset investment background.

Whilst clearly not only representative of private investments, this figure suggests that the initial push for more diversified asset allocation was not the product of the pandemic's economic pressures as might be assumed. Instead, it is part of a broader change whose future is similarly boundless; Campden Wealth's 2022 Family Office Survey indicated that nearly half (45%) of all European family offices investing in private assets wanted to increase their exposure to the asset class.

> ...the expense of creating a full investment team means many offices are now choosing to create leaner, more nimble investment functions. This often takes the form of only a few investment professionals.
>
> Charlie Harris, Lutyens Advisory

However, the specific form these future investments will take is less easy to express through statistics. The enormous diversity in size and budget across the family office space means that direct private equity investments can be highly cost inefficient, or indeed unaffordable, for many family-funded portfolios. They require high volumes of capital not only to fund the investments themselves but also to build in-house teams of sufficient scale and capability to generate returns.

As such, many younger (or smaller) offices are turning to private investments via institutional managers or co-investments. Choosing investment partners in this respect can often prove simpler than selecting the investments themselves. Despite its expansion over the last 10 years, the HNWI circle is still tight knit, and the relationships forged

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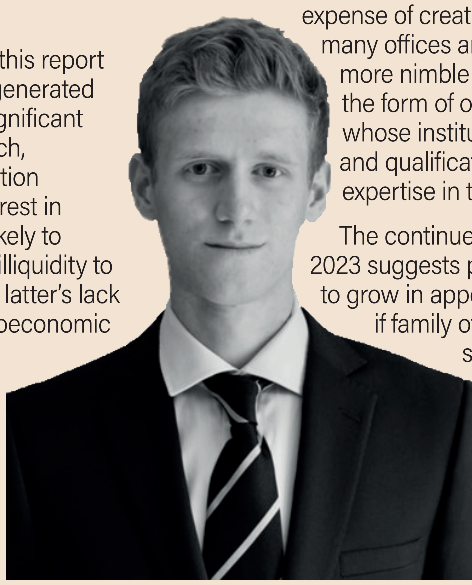
during wealth creation often pave the way for future partnerships between Principals and their offices. This has been seen in the increased prevalence of 'club' deals. By pooling their resources, multiple single family offices are collectively able to fund private investments otherwise unaffordable in isolation, granting them greater access to the private equity market.

Regardless of these variations in form, the widespread increased interest in private investments as a whole begs an obvious question – why this particular asset class? The answer is a composite one. A strong driver is the promise of attractive returns; the 2022 Campden Wealth Survey revealed that on a global basis private investments produced an average net return of c.20% across venture capital, private funds and private equity.

It is worth emphasising that this report was produced from results generated before the onset of 2022's significant inflationary pressures. As such, the continuation of high inflation throughout 2023 means interest in private investments is only likely to increase. Their comparative illiquidity to fixed income means that the latter's lack of appeal in periods of macroeconomic uncertainty will drive higher allocations to private investments as family offices seek to offset risk through portfolio diversification.

Private equity's illiquidity is also attractive given that it offers both a long-term investment option as well as a more tangible one. Whilst at first these may appear to be secondary influences on the investment process, for family offices they represent important considerations. Time horizons for family office investments must cope with a generational outlook rather than the traditional institutional long-term view of 5-10 years. Moreover, the tangible nature of private equity offers an easier introduction to investing for the office's next generation, as close interactions with acquired businesses allow for a more 'hands-on approach'.



The consequence of these incentives is that family offices are now structuring themselves to facilitate this shift in asset allocation. As previously noted, the expense of creating a full investment team means many offices are now choosing to create leaner, more nimble investment functions. This often takes the form of only a few investment professionals whose institutional and cross-asset backgrounds and qualifications give them a quantifiable expertise in the space.

The continued economic uncertainty promised by 2023 suggests private investments will only continue to grow in appeal for investors. Don't be surprised if family offices, with their lean organisational structures and capacity for swift capital reallocation, take note of the advantages on offer.

Charlie Harris
Lutyens Advisory

MARCH 2023

How to run your financial life like an institutional investor

JOHNNIE HAMPEL, CO-FOUNDER, Y TREE

It's fair to say institutional investors have some advantages over the rest of us.

They have rigorous efficiency, organisational depth, structure, transparency, scale, a strong process, governance, regulatory scrutiny, data, technology and a vast pool of human and intellectual capital - a list that might seem completely out of reach for individuals.

Let's define first what we mean by an institutional investor in this instance. When we talk about institutions, we mean big endowments (like Harvard and Yale), pension funds and some of the largest family offices, not wealth managers, private banks, asset managers or IFAs.

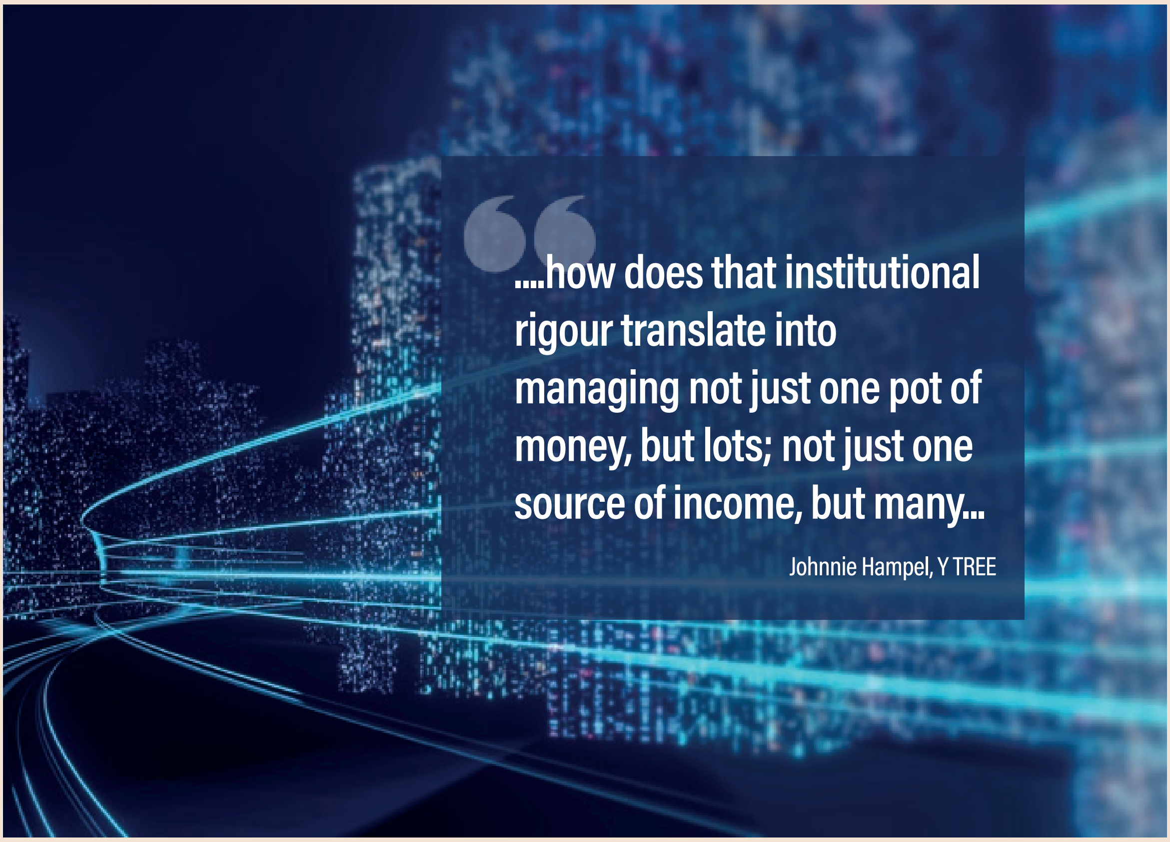
These institutions have significant amounts of data and technology at their fingertips, plus a broad bench of human expertise to manage money effectively. It's this combination that helps optimise returns and unlock value to meet both short- and long-term objectives.

But how does that institutional rigour translate into managing not just one pot of money, but lots; not just one source of income, but many; not just one investment objective, but multiple personal objectives? This is where we're seeing technology come into play, with some of the practices, processes and thinking used across the world's leading institutions increasingly being adopted in the sphere of personal wealth.

ASSET LIABILITY MODELLING

It starts with a rather sexy principle called asset liability modelling (ALM).

Institutional investors are always balancing assets with liabilities. They manage the gap between the two and constantly assess whether they have the enough assets to safely fund their short-, medium- and long-term liabilities. This gap is often measured by the ratio of assets over liabilities, also known as the funding ratio. Institutional investors seek to have a funding ratio of more than 1, which means there is always something in the pot to fund your liabilities should they be required. In an ideal world, this score should be a



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little over 100. That way, you have more than you need in case something goes wrong in the future.

The starting point of any advice should always be what you want to do with your life and what you and your family will spend in the future - your liabilities - rather than investment returns. Essentially, finding the ideal funding ratio and devising and implementing a financial life strategy to fill the gap.

But these calculations are not a manual process. It takes an engine to help us do this for diverse individual circumstances, at scale. Combining knowledge from the fields of computer science, statistics and applied mathematics, the principle of ALM can solve the most complex financial problems. Using technology, it's now accessible and, more importantly, understandable to everyone.

Of course, we can't predict what's going to happen in the future, but we can plan for the worst. By leveraging statistics and big data, it's possible to model how interest rates, inflation, economic downturns and all the rest can impact your current assets and, crucially, your liabilities.

To run your financial life like an institutional investor requires a change in mindset. The question is no longer plainly, "how do I maximise my returns?" But "how can my finances support my aspirations for my life, for my family and for generations to come?"

EFFICIENCY

Sophisticated institutional investors never overlook the power of efficiency. Multiple, marginal gains across risk mix, liquidity, currency, cost and structuring compound to significant value over time.

When you are at the top of the league, every basis point counts.

THE WORLD'S BIGGEST INVESTORS CARE ABOUT THE SMALLEST FRACTIONS

Lower cost

Lowering the costs of your providers (including fund costs, discretionary fund management fees, custody, administration, foreign exchange and transaction costs) by 2% can save you the entire principal first invested when compounded over 20 years.

Reduce underperformance vs market

Investors should be receiving an appropriate level of return, after fees, for the risk being taken. This involves a shift in attitude. When the starting point of your investment strategy is returns, you'll naturally seek out outperformance. Over the long-term, managers seldom outperform consistently. When you add fees and other costs into the mix, you'll likely end up with average market return or less. The biggest determinant of long term performance is the risk taken by an investor - much more than the manager selection - and this risk can often be replicated using low-cost index tracker funds.

Risk

Investors should set a target risk level that is appropriate to generate the returns required to meet long term liabilities and life aspirations and then stress that risk against a number of scenarios (e.g. market falls, inflation, tax changes) to understand their capacity for loss. Once the target risk level has been set it should not change, unless circumstances change (e.g. spend targets, age etc.).

Currency

Investors should match the purchasing power of their assets against their currency of spend/liabilities. This means setting currency targets for a portfolio, in a similar way to setting risk targets.

Surplus cash reinvestment

Investors tend to hold too much cash, confusing cash and

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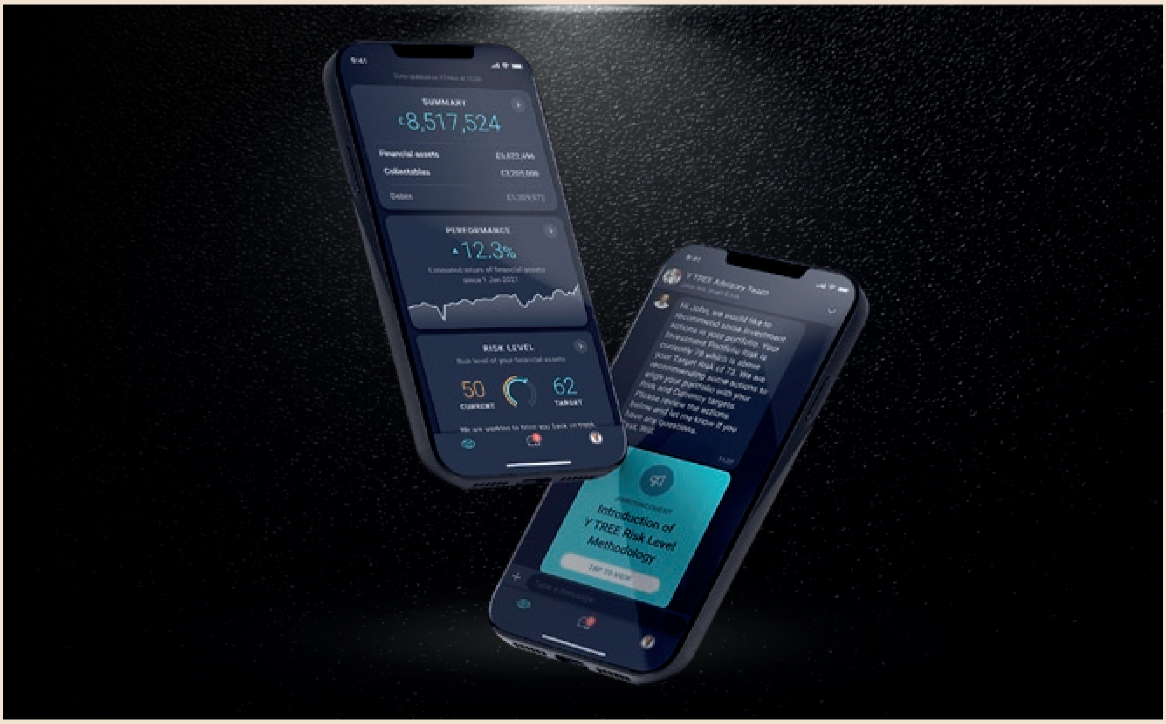

liquidity. By taking an institutional approach to liquidity management, investors should hold minimum cash to meet short term liabilities (a cash buffer). Technology feeds can show when cash inflows exceed that buffer and the excess should be invested automatically to avoid the opportunity cost of holding excess cash. Liquid investments can always be sold to generate cash required for liabilities.

Improved diversification

Multi-asset class portfolios can reap the benefits of diversification but looking through asset classes to "market exposures" is critical to understanding your risk level and risk mix.

Tax optimisation

The amount of tax you pay over a lifetime has a material impact on your wealth. We believe in making intelligent decisions about tax, informed by insight and experience, including making use of allowances, fitting risk in each tax wrapper to its tax profile, ensuring efficient account structure and ownership, as well as devising efficient accumulation or decumulation strategies.

Illiquidity budgeting

Private markets can provide exposure to market risks and access to higher returns than public markets through an illiquidity premium. Having an institutional process helps determine an appropriate long allocation and a budget for commitments to each vintage.

Dynamic risk level rebalancing

Institutional investors recognise how difficult it is to time markets and so do not attempt to time short-term market movements; instead they automatically rebalance their portfolios (unemotionally) back to their long-term target risk levels after positive or negative market performance.

MEANING

Implementing technology and data into wealth management practices will help make the process more appropriate, efficient and transparent, and ultimately build value. But what's the point of all this process if it's not life changing?

We really believe that money is only meaningful when it's being spent on what matters most to individuals, families and communities.

The real wonder of an institutional process and greater efficiency is the extra wealth it generates. That extra wealth can be the difference that unlocks real change in society because it enables us to invest more deeply in our businesses, in philanthropy and in future generations. Managing your money effectively not only means you can enjoy the life you want to live, but it helps spread that wealth further, and for better.

Johnnie Hampel

Co-Founder & Head of Client Relations, Y TREE

Visit y-tree.com to find out more.

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In Sync – How hedge funds achieve alignment with investors to foster long-term strategic partnerships

TOM KEHOE, GLOBAL HEAD OF RESEARCH AND COMMUNICATIONS, AIMA

When you strip away the lively discourse around the outsized returns that some alternative investment fund managers can generate, the proactive efforts to align their interests with their investors are arguably the most attractive aspect of their offering.

The entwining of the personal prospects of principals and those that entrust their capital to them is baked into the DNA of alternative investment fund structures, and the most successful managers are those that are most in sync with their clients' demands.

Thus is the title of AIMA's latest research piece, **In Sync: How hedge funds achieve alignment with investors to foster long-term strategic partnerships**' outlines the ways fund managers are adapting their business model in response to increasing competition and the evolving mandates of their investors. This is the third in a series done in collaboration with audit, tax, and consulting firm RSM with this year's research building on the 2019 report, "In Harmony" which examined the same GP/LP investor dynamic, including a time series analysis of how trends have changed.

This year's research is built upon the findings of a global survey of 138 alternative investment fund managers accounting for more than $700bn in assets under management and a second survey of 35 institutional investors that allocate to alternative investment funds.

Every aspect of the GP/LP offering from the fee model and performance incentives to the products offered includes characteristics designed to ensure that when the fund manager does well, the investor does well, and the fund manager only does well when the investor does well.

Among the key findings of this year's report include:

- The definitive form of alignment between hedge fund managers and investors remains "skin in the game" with over 90% of fund managers surveyed investing their own monies into their funds with the average investment standing at 8% of the fund's total assets under management. Not only principals but other key staff are also expected to invest their capital in the fund as a way of demonstrating to their firm and its underlying investors that they are committed to the mission.
- The combination of higher costs and a plateauing of industry headline fees has prompted hedge fund firms to innovate how they charge fees and manage expenses by applying new solutions underpinned by a variety of relationship pricing that reflect the changing needs of the fund manager and their clients.
- The importance of co-investment vehicles is a significant development from the findings of the 2019 survey. Over 90% of investors either engage in this type of partnership or are seeking to do so. Equally, over half of the fund managers are currently utilising a co-investment vehicle with an investor or are open to doing so.
- There has been a clear change regarding the trajectory of widespread adoption of ESG caused by the gravitational pull of macro-economic factors, including geopolitical tensions, and increasing regulatory burdens being experienced globally. A more complex investment market landscape is requiring allocators to answer the thorny issue of squaring their fiduciary duty to their underlying investors with a desire to do good.

Looking ahead to how the GP/LP dynamic will most likely continue to evolve, our research suggests that demands regarding transparency on fund fees and expenses will continue to increase.

Flexibility will continue to be key for alternative investment funds wanting to deepen their partnership with investors. Fund Managers should not lose sight of their ultimate purpose – to help their clients, ranging from pension plans to charitable organisations to meet their investor needs. Put simply, those that are in sync with their investors will succeed and grow.

AIMA's research paper **"In Sync – How hedge funds achieve alignment with investors to foster long term strategic partnerships,"** can be downloaded here.

Tom Kehoe
Global Head of Research and Communications, AIMA

APRIL 2023

Asset owners delay new investment activity as macroeconomic picture evolves

KATHRYN SAKLATVALA, BFINANCE

The past year has seen a notable slowdown in the volume of manager search activity conducted by institutional investors such as pension funds, insurers, foundations and university endowments, according to client data from independent global investment consultancy bfinance.

A turbulent macroeconomic environment has led to a climate of investor hesitancy as policymakers try to walk a tightrope between inflation and recession, armed only with the extremely blunt tool of monetary policy. The resulting fear and uncertainty appears to have placed many investors in 'wait and see' mode. As such, the number of new mandates across all asset classes—equities, fixed income, private markets and diversifying strategies—dropped by more than 10% in 2022 versus 2021, based on bfinance client data. While the first quarter has seen a modest pick-up, many investors are still postponing or reducing new investment activity.

Kathryn Saklatvala, bfinance

Interestingly, manager search activity in private markets remained remarkably resilient relative to liquid markets. As a result, 58% of new manager searches among the consultant's clients in 2022 targeted illiquid asset classes such as private equity, private debt, (unlisted) real estate and infrastructure—up from 49% in the previous year.

This may surprise readers who have tracked the overall slowdown in private market fundraising activity over the past 12 months, especially with an ongoing 'denominator effect' in play—wherein public market asset valuations decline more quickly than private market valuations, leading to an artificially (and possibly temporarily) outsized allocation. Yet there are several 'micro' trends influencing strong activity levels

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here. One is the surge in activity targeting 'impact', 'climate' and related thematic strategies within private markets: a significant proportion of client activity in private equity, real estate and infrastructure is currently focused on the rapidly maturing universe of strategies in this area. Separately, it's worth noting that a significant proportion of clients are newer entrants to some (if not all) illiquid asset classes and are still in the process of building up portfolios from a low base, meaning that the 'denominator effect' does not yet come into play.

Equity manager search activity, it must be said, bore the brunt of the slowdown among bfinance's clients. Only 15% of bfinance client manager searches in 2022 targeted this asset class, down from 24% of the previous year's higher total. In particular, there has been a dearth of regional mandates. Instead, where investors have been seeking new managers, the focus has chiefly been on global strategies, often with a specific style, size or other remit, rather than on specific geographies such as the US, Europe or China. It's also worth observing that mandates for emerging market equities represented 29% of all equity manager searches from bfinance clients, up from 22% the previous year: this sustained level was fuelled by replacement activity, with only 37% of investors indicating that they were 'satisfied' with the recent performance of their emerging market equity managers in bfinance's 2022 Asset Owner Survey, 'Traps and Transitions' (see 'How satisfied are you with the performance of active managers in the following asset classes?).

Fixed income manager search activity was relatively resilient by comparison, declining only marginally versus the previous year. Interestingly, 40% of fixed income manager searches were focused on emerging market debt, up from 29% the previous year; as was the case for emerging market equities, this was an asset class where investors have communicated weak satisfaction with the performance of their managers. Towards the end of the year we saw a resurgence in investor appetite for more conservative investment grade strategies, which continues in 2023.

New hedge fund manager search activity fell considerably, despite the outstanding performance generated in 2022 by more 'divergent' and market-independent strategies within this family. Global macro, CTAs and multi-strategy hedge funds delivered particularly strong results over a period when both equity and fixed income portfolios were generating losses. While investors did not necessarily view 2022 as an opportune window to make fresh commitments in this area, we do expect the experience of this period to shape future sentiment and anticipate ongoing demand for 'hero diversifiers' as investors consider the shape of portfolios going forwards.

The macroeconomic climate remains febrile in 2023, with ongoing instability and market shocks. It is hard to take decisive action in the face of such uncertainty. Yet investors must take advantage of the lessons from recent history—a very different macroeconomic environment—in order to re-evaluate exposures, strengthen portfolios and improve resilience to oncoming scenarios.

bfinance is an independent investment consultancy with clients in 44 countries.

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AIMA's Global Investor Board's Eight Takeaways for Alternative Investment Fund Managers

CLAIRE VAN WYK-ALLAN, AIMA

AIMA's Global Investor Board (GIB) is a global advisory board created by AIMA, the global representative for the alternative investment industry, to further strengthen its engagement with the global investment community from across the alternative investment universe.

Launched in December 2021, AIMA's GIB has grown to nearly 20 senior leaders at institutional investors from across the world. Chaired by Eduard van Gelderen, CIO at PSP Investments, the GIB provides insights on trends impacting alternative asset allocation while advancing sound practice excellence for managers.

Here are eight top takeaways for alternative fund managers based on GIB conversations since it was founded:

1. **Partnering with investors**: Being just a pool of capital is not a definitive strategic relationship. Rather, a deeper and lasting partnership can be achieved by co-investment, bespoke offerings, increased knowledge sharing and value advisory services, with both research and technology.
2. **Sharing the expense**: Investors globally are increasingly sensitive not just to the amount of compensation being paid to fund managers but also to the costs they incur in running the business. Subsequently, there is greater acceptance for additional costs to be passed through to the investor, albeit capped to a certain level of the fund's NAV.
3. **Moving towards a new equilibrium**: There is an increasing sense that fund fees and terms between hedge fund managers and their investors are moving towards a new normal. Managers are responding to investors' needs by putting in place arrangements that are more closely aligned both to the requirements of the client and the underlying investment strategy. Fund hurdle rates are increasingly becoming a prerequisite, while distribution waterfalls also matter, many investors preferring the European distribution.
4. **ESG – no-one-size-fits-all approach**: Views on ESG differ depending on the region, and the

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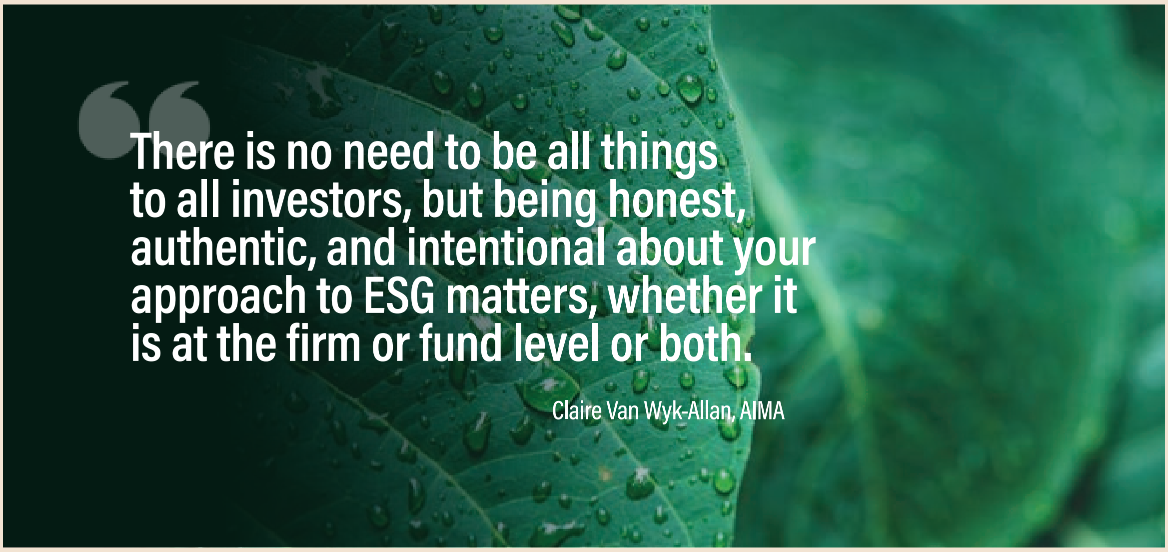
strategy of fund managers/type of investor and that will continue as various global markets diverge on their ESG frameworks. A more complex investment landscape is requiring fund managers to answer the thorny issue of squaring their fiduciary duty to their underlying investors with a desire to do good. A healthy dialogue on what ESG means and how it should influence decision making is paramount for getting the balance of interests between both parties right. There is no need to be all things to all investors, but being honest, authentic, and intentional about your approach to ESG matters, whether it is at the firm or fund level or both. Due diligence templates, carbon footprint documentation, UNPRI signatory commitments, climate risk exposure and other ESG disclosure and data reporting are important.

5. **The Denominator Effect is real**: Although investors are highly-interested in private market investments, the 'Denominator effect' (caused by the decline in public market securities inflating the proportion which investors hold in private assets) is real and will likely constrain investors from making further commitments to private markets for the next year or so, though they expect 2023 and 2024 vintage funds to offer great opportunities, given market conditions.
6. **LPs are refining their Total Portfolio Approach (TPA)**: More investors are using investment models that view the total portfolio holistically across a variety of different dimensions (i.e. active investment versus passive investment; public market allocation versus private market allocation; internal fund manager mandate versus external allocation; top-down versus bottom-up investment approach) to meet investment objectives, which may include improving the portfolio's risk-adjusted returns, increasing its diversification, mitigating drawdown risk, enhancing portfolio resilience and minimising liquidity risks.
7. **The valuation methodology is in the details**: While private equity valuations will lag, they likely aren't as over-valued as some headlines might suggest. However, managers should be much more transparent in detailing their specific approach to valuation.
8. **Viewing investors as partners:** Investor Relations professionals are encouraged to demonstrate strong ownership of the relationship through periods of difficulty, be detailed on what the fund is actually doing and upfront about how the fund may be similar or different to competitor funds.

If you wish to learn more about the work of the Global Investor Board or read their bi-monthly insights, please go to AIMA Global Investor Board or contact Claire Van Wyk-Allan for further details.

Claire Van Wyk-Allan, CAIA is Managing Director, Head of Canada for AIMA, and also co-leads AIMA's investor engagement work through the Global Investor Board and Investment Peer Group. She joined AIMA as Director, Head of Canada in 2018.

Claire Van Wyk-Allan, AIMA



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What we are seeing in the world of ESG

SEEDRS

2022 was a year of transition and consolidation for Environmental, Social and Governance (ESG) investing. On the one hand, regulatory changes and significant global economic headwinds saw European equity ESG funds underperform their benchmarks by 5%, worse than the 4.6% recorded by their traditional rivals.

However, most analysts agree that these metrics only dampen the case for ESG led investing based on short term ROI alone. The facts are that climate change is not going anywhere and the energy transition will drive sustainable fund returns over the long term. As Sarah Merrick, CEO of Ripple, who raised £2.1m on Seedrs last year, says: "There are very few sectors like ClimateTech where the fundamentals of massively accelerating demand are quite as clear and present."

That's why the world of venture capital is telling a different story when it comes to ESG. While global overall investment activity sunk by 57% in 2022, ClimateTech funding achieved an all time high, with 25% of all venture funding globally going into the sector according to a PwC report. That same report found that investors globally are set to embrace ESG investing on a massive scale and predict that it will soar 84% to $33.9 trillion by 2026 - equating to 21.5% of total assets under management or more than $1 for every $5 invested.

We're seeing evidence of this across the investment ecosystem. The world's largest sovereign wealth fund in Norway said it would vote against companies that don't set net zero carbon targets, overpay top executives, or lack diversity on their boards. Meanwhile, exchange traded funds (ETFs) aligned with ESG outcomes accounted for 65% of all net inflows into ETFs in 2022 - which suggests that investors are recognising the inevitability of long term structural change.

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And the markets only reflect what's happening in industry. For example, looking at technology adoption curves, a recent BloombergNEF report suggested that clean energy has a tipping point that 87 countries have now reached. This is a fact that car companies seem to have picked up on - almost every major manufacturer intends to stop making internal combustion engines within 20 years.

At Seedrs, these broader ESG investing trends are reflected in the investment behaviour we're seeing on the platform. In 2022, 47% more sustainability focused businesses (103 up from 70) received investment on the platform YoY, raising from 40% more investors. In particular, the Clean Energy sector thrived with investment growing 266% from £11m to £36m, with 50% more business raising from 50% more investors. And according to our summer investor survey, ClimateTech is the #1 sector of interest on Seedrs. That all explains why last year we saw alumni businesses in this sector like QED Naval, Solivus and Ripple return for another round on Seedrs to run highly successful campaigns, raising millions from our investors and their communities. At the same time, we also welcomed many innovative new businesses, like Gazelle Wind Power, who raised over €3.8m on Seedrs.

ABOUT SEEDRS

Seedrs is Europe's leading private investing platform. It enables individuals to invest in startups, growth companies, and, if eligible, top VC funds, as well as supports ambitious entrepreneurs in all sectors to raise capital from their communities, angels and institutional investors

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University spinouts need a clear roadmap for future investment

MORAY WRIGHT, CEO, PARKWALK ADVISORS

As the Chief Executive of Parkwalk, the UK's largest growth EIS fund manager, I've got to know dozens of founders over the last 14 years and as the UK's largest investor in university spinouts, it's clear to me that the UK has no shortage of talented people looking to commercialise their breakthroughs.

The UK's universities are recognised around the world as producing some of the most cutting-edge ideas. I've seen first-hand how technological innovations like quantum computing, genomics, and projectile fusion are on course to change the world. But this type of deep tech or clean tech could also be game-changing for UK productivity, and go onto employ tens of thousands of people in the jobs of tomorrow.

Indeed, UK spinouts secured £2.5bn in equity investment in 2021 - an almost 70% rise from the previous year, and a five-fold increase on investment in 2012. If we can capitalise on this momentum, UK spinouts could be the engine for growth this country needs.

But the conversations with founders I have had recently reveal a common problem. How to secure the long-term investment needed to grow and prosper in the UK?

The recent announcement of an independent review of university spinouts, led by Professor Irene Tracy and Dr Andrew Williamson, could not come at a better moment. The review must look at the kind of investment that early-stage companies need, the potential impact of sector-specific initiatives, the question of retained equity and the importance of having a clear roadmap for investors. The Edinburgh Reforms, and the changes to Solvency II, will help to provide this, but this kind of certainty is vital to encourage investment.

Above all else though, it's vital the Review team and Government create forums for collaboration with the investment industry. Only by working

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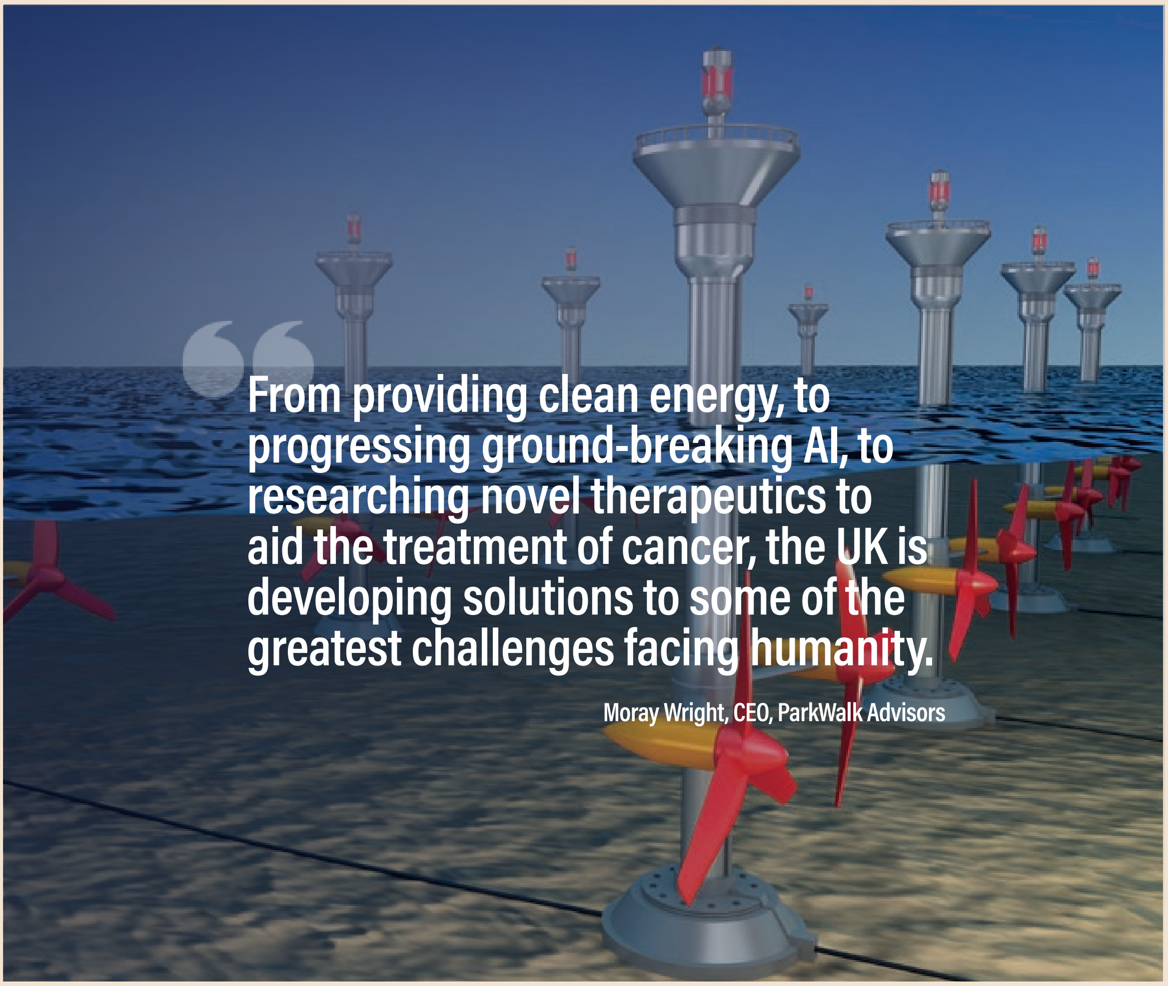

together can we foster an ecosystem which allows new ideas to become new industries – right here in the UK.

From providing clean energy, to progressing ground-breaking AI, to researching novel therapeutics to aid the treatment of cancer, the UK is developing solutions to some of the greatest challenges facing humanity. My hope is that this review signals the start of new era in which we embrace the commercial and economic potential of the innovations coming out of our world-leading academic institutions, and take action to keep them in the UK.

About Parkwalk

Parkwalk is the largest growth EIS fund manager, backing world-changing technologies emerging from the UK's leading universities and research institutions. With £500m of assets under management, it has invested in over 160 companies across its Parkwalk Opportunities and Knowledge Intensive EIS Funds, as well as the award-winning enterprise and innovation funds Parkwalk manages for the Universities of Cambridge, Oxford, Bristol and Imperial College.

Parkwalk, alongside its parent company IP Group plc, invests in businesses creating solutions to real-world challenges, with IP-protected innovations, across a range of sectors including life sciences, AI, quantum computing, advanced materials, genomics, cleantech, future of mobility, medtech and big data. For further information see parkwalkadvisors.com.

Moray Wright, CEO, ParkWalk Advisors

MAY 2023

Where venture capital firms are developing their teams

HUGH BARRAN, VENTURE CAPITAL, ARMSTRONG INTERNATIONAL

This year has so far been somewhat surprising on the VC hiring front, with many funds still looking to add investors to their team. The background of these funds are robust platforms, pre-seed to seed as their primary investment strategy with a good history of exits. Growth funds have been much quieter but the nature of seed investing is to our minds "market neutral". If only 19% of companies get to Series A in Europe as the statistics suggest, then the low probability of a seed-stage company becoming successful means that regardless of what is happening in the public markets, VCs must continue to invest.

The tougher environment will ensure that only the truly phenomenal founders survive. We should expect to see some of the most exciting companies for the next decade and beyond being created during this time.

After speaking to one Head of Talent at a top-tier multi-billion dollar VC a couple of weeks back, she mentioned that in her four years with the firm they have never stopped hiring associates. Associate hiring will never slow down, for the good ones are too hard to come by. When they do get hired by top-tier funds, they then raise the bar for the next batch to come on board. What we are seeing now is more of a focus at the associate level on the need for a computer science or technology-focused background. Being a superstar consultant or investment banker will hold you in great stead but if you can marry an authentic curiosity for

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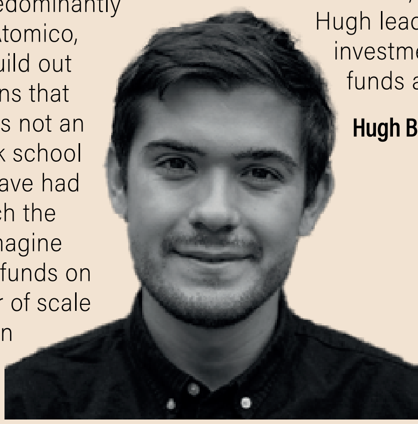
technology trends with a passion for business models, there should not be a short supply of funds looking to hire you.

European VCs are continuing to build on the platform side too. LocalGlobe recently hired a Head of Talent from Meta, who also completed stints at Gousto and Neuralink on the West Coast. Atomico has hired a Go-To-Market operating partner in the form of Thibaut Ceyrolle, who was Snowflake's first employee in Europe. It is an interesting time for the industry where funds such as Hoxton, 83North, Point Nine stick to a lean structure, predominantly Partner only, and firms such as Atomico, EQT Ventures and LocalGlobe build out across their platform and positions that directly support their portfolio. It's not an exact science, it's the Benchmark school of thought vs. Andreesen, both have had phenomenal returns but approach the industry in a different way. We imagine founders will want both types of funds on their cap table. It's more a matter of scale than anything. If we see European institutional LPs allocate more than the sub 1% currently to venture capital over the next 10-15 years, we are sure to see more platform and portfolio value creation hiring across the industry.



Armstrong International

Armstrong International is a financial services focused executive search firm. Founded in 1989, the firm built it's reputation hiring for Goldman Sachs and SG Warburg throughout the 90s before broadening into areas such as Hedge Funds, Infrastructure, Real Estate and Private Equity. Hugh leads the VC team focused on hiring investment and platform professionals for VC funds across Europe.

Hugh Barran, Armstrong International

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Multiples: going, going gone?

IOTO IOTOV, PARTNER, CAPRICORN CAPITAL PARTNERS

That private market multiples have come off the highs of 2020-2021 is not news. The why, however, is worth exploring. I propose four reasons as to why, with the fifth being higher interest rates, not discussed for fear of stating the obvious.

Mood; greed or fear in public markets: Public markets present a real-time take on pricing sentiment, unlike private markets, which may have gaps of years between price discovery. Using listed Fintech, albeit a sector particularly hard-hit, as a reflection of the public market mood is telling. In Pitchbooks 2023 Fintech & Payments Public Comp Sheet and Valuation Guide, it was shown that multiples have not just cooled off, they have fallen off. The most extreme being for high-growth payment companies, whose EV/NTM revenue multiples careened from c.20x in 2021 to c.5x by Q1 of 2023. The drop off is directionally consistent across other Fintech sub-verticals. This sentiment shift is not lost on private market investors, who question paying comparably elevated multiples for private companies when their typically larger, more mature, and supposedly better managed and stable public comparables are priced lower.

Calculating price; the valuation method employed: Building on the first point but less sentiment and more numerical, the public markets are often seen as an exit route for private market companies investors. Under the Venture Method of pricing a company, the investors work backwards, using a hypothetical IPO price as the exit value. The theoretical IPO price is calculated using the listed comparable multiples. Lower public market multiples will therefore feed back into the pricing of the private market company, leading to a drop in their multiple.

Zeitgeist; the emergence of the bottom line (over the supremacy of the top line): Go back to the heady days of 2020/2021, and few were discussing profitability. Profitability was for boring

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people, like accountants (of which I am one) and credit investors. No, what mattered was growth. Growth would solve all! Growth at all costs! This logic was, as would be expected, found to be flawed. Eventually, the company, through a sound business model, needs to generate cash flow from operations (and not just from financing) to sustain itself and pay its investors. Given this new mantra of profitability, or in its absence, the path to it, fewer companies are finding the risk capital that would have previously been available. With investors willingness to pay for growth muted, valuations have similarly retreated.

Closed; back in 18 months: Venture investing activity, both value and volume, has fallen off the peak, albeit from the Everest that was 2021. Dealroom, a data provider, calculates that global VC investment was down 32% in 2022 on 2021. As expected, valuations have fallen as purse strings have tightened. The factors of less money and more sobriety around its deployment have acted like gravity on the prices paid and by extension, the multiples achieved.

The reasons for the decrease in multiples we see in the market are numerous and often intertwined. What is worth noting, however, is that these periods of fear, or price rationality (call it what you like), have historically presented excellent buying opportunities, and the vintages have previously proven to be some of the most successful.

Ioto Iotov, Capricorn Capital Partners

Ioto is a London-based private markets investment professional, who focuses on making investments into leading financial services and enterprise software businesses. He is a qualified chartered accountant, has an MBA (Columbia Business School, New York), and has earned the CFA and CAIA charter.

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A tale of two cities Credit risk in private markets

NICK SMITH, MANAGING DIRECTOR, ACC, THE PRIVATE CREDIT AFFILIATE OF AIMA

"It was the best of times, it was the worst of times" is the famous opening to Charles Dickens' A Tale of Two Cities. This sentiment comes to mind whenever I'm asked for my views on the private credit market and how current challenges in the economy are shaping the growth of the sector and the opportunities for investors.

Credit risk is paramount for a sector which typically involves holding investments to maturity, and many factors which affect credit risk for investors are now more salient than they have been for some time. Borrowers accustomed to a long period of low interest rates and abundant liquidity now find themselves in a less welcoming environment. Inflationary pressures, supply chain disruptions, reduced customer spending and higher energy costs are all putting pressure on the corporate sector and making it harder for them to be successful enterprises. At the same time, broader challenges in the banking sector mean that many firms, but particularly small and mid-sized businesses, are likely to see their access to credit constrained.

Taken together, these factors add up to a recessionary environment and one in which it will be harder for lenders of all types to price risk and invest prudently. While many of these factors are likely to persist in the medium term, there are still several reasons for optimism about how private credit funds will navigate these headwinds.

The first would be how private credit managers assess and manage their investment opportunities. Our Financing the Economy research series has consistently demonstrated that the direct relationships private credit lenders have with their borrowers is a powerful driver of investment discipline and prudent lending. Furthermore, their risk management practices

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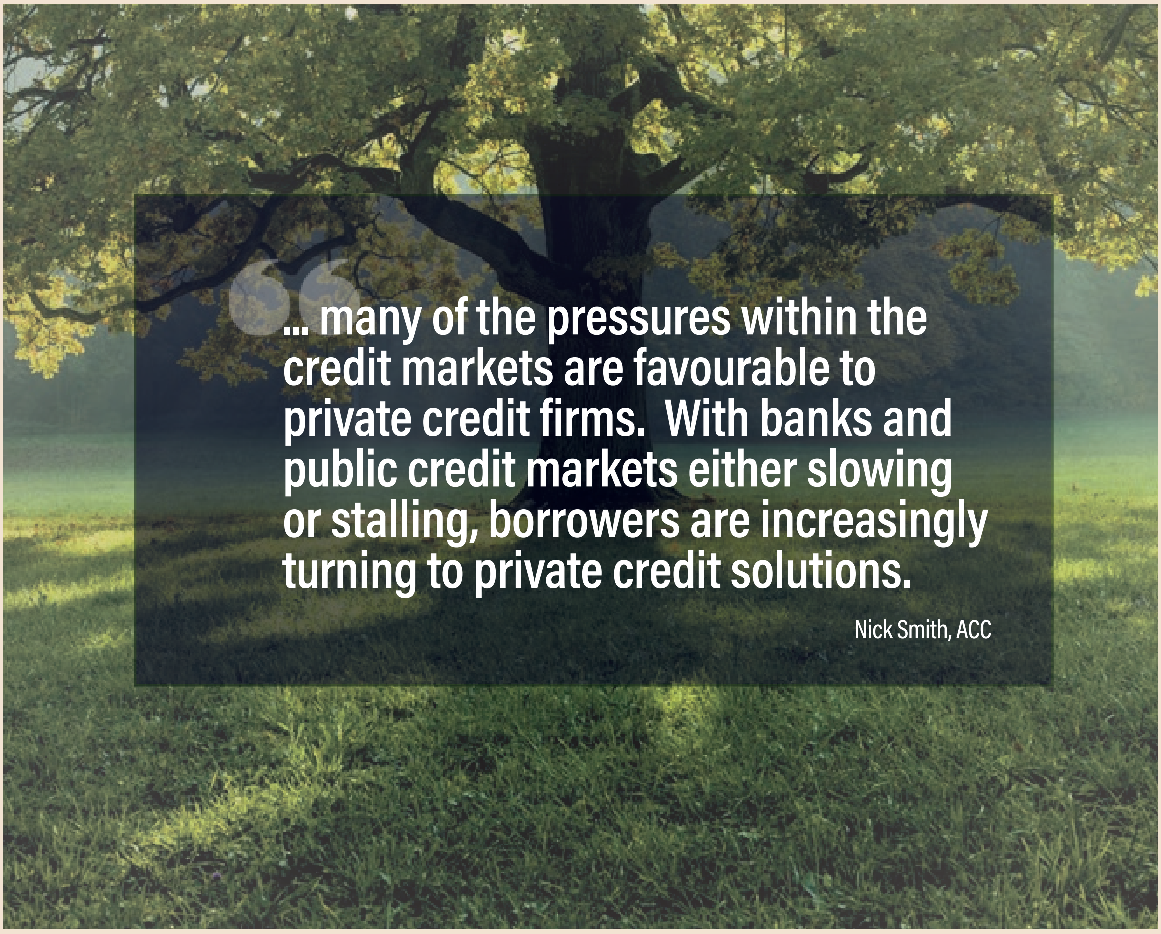

mean that stress in their portfolios is likely to be identified and managed more efficiently, improving recoveries.

Secondly, many of the pressures within the credit markets are favourable to private credit firms. With banks and public credit markets either slowing or stalling, borrowers are increasingly turning to private credit solutions. Such borrowers now increasingly include large corporates as well as mid-market businesses, as well as those outside core markets in the US and Europe. In the immediate term, this means that private credit funds continue to see good deal flow while also having more leverage when it comes to loan terms and documentation. Having a bigger footprint outside the traditional mid-market will also provide a long-term boost for the sector's overall development.

Finally, it is important to recall that the asset class is now larger and more diverse than when it first began to find its way into investor portfolios. This means that while there may be challenges within particular lenders or markets, it is now possible for investors to hedge that risk by investing across different managers and strategies.

Dickens also talks about 'the age of wisdom' and 'the age of foolishness' when beginning his story. While there will undoubtedly be examples of both in private credit's future, the attributes of the sector mean that investors have a useful partner to help them navigate the headwinds they face and take advantage of the opportunities that do exist for those ready to capitalise on them.

Nick Smith is the Managing Director, Private Credit for AIMA's private credit affiliate, the Alternative Credit Council (ACC).

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Technology and Derivatives: Revolutionising Alternative Asset Markets and Investment

NILESH JETHWA, CEO MAREX SOLUTIONS

The rapid advancements in technology have had far-reaching impacts on various industries, including the financial sector. One area that has experienced significant change is the alternative asset market. As investors continue to seek new opportunities to diversify their portfolios and enhance returns, the use of technology to improve investment performance has become increasingly crucial.

Alternative asset markets have historically been less accessible to individual investors due to their complex nature and high barriers to entry. However, technology has played a pivotal role in democratising access to these markets, enabling investors to tap into new sources of potential returns. As a result, the demand for innovative financial products, such as structured products and derivatives, has surged.

Derivatives, which are complex financial instruments whose value is derived from an underlying asset, can be used to manage market risk or provide investors with a yield on their investment. They have become an essential tool in the alternative asset markets, allowing investors to hedge against potential losses, enhance returns, and gain exposure to otherwise inaccessible asset classes. By incorporating derivatives into their investment strategies, investors can achieve a more diversified and risk-adjusted portfolio, ultimately improving their overall investment performance.

Marex Solutions, a division of Marex Group, specialises in manufacturing and distributing structured products, with a focus on Hedging Solutions for corporates and Financial Products for professional investors. Recognising the need for a more efficient and accurate way to explore investment ideas and obtain pricing information, Marex Solutions has developed Agile, a cutting-edge derivative pricing and execution platform.

The derivatives industry has been infamously referred to as creating opaque, unpredictable, and complex products that are very difficult to manage. Our platform addresses these long-standing challenges and delivers a more transparent and predictable experience for investors. This enables investors and advisors to access a comprehensive universe of asset classes, including equities, interest rates, commodities, and foreign exchange.

By leveraging advanced technology, Agile is able to streamline the investment process, allowing users to quickly and accurately price a wide range of derivative

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products. This empowers investors and advisors to make more informed decisions, as they can easily compare different investment options and assess their potential impact on portfolio performance.

In addition to providing accurate pricing, Agile also offers a range of tools and features designed to enhance the user experience. These include customisable dashboards, real-time analytics, and seamless integration with existing systems.

Agile harnesses the power of cloud-first technology to deliver unparalleled efficiency and scalability in managing market risk and investment opportunities. Our proprietary cross-asset quant library further enhances the platform's capabilities by offering comprehensive analytics and insights across multiple asset classes. This seamless integration of technology with our broad computational power enables us to serve an increasingly diverse global customer base.

Technology has had a transformative impact on the alternative asset markets, particularly in the realm of derivatives. By harnessing the power of technology, investors can now access a broader range of investment opportunities, manage risk more effectively, and ultimately improve their investment performance. Agile exemplifies this trend, offering a sophisticated and user-friendly solution for exploring investment ideas and obtaining accurate pricing across a diverse universe of asset classes. As the financial landscape continues to evolve, technology and derivatives will undoubtedly play an increasingly significant role in shaping the future of alternative asset markets and investment performance.

Nilesh Jethwa is the CEO of Marex Solutions, a division of Marex that specialises in the manufacture and distribution of customised derivative products.

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Unlocking the Future: Harnessing Integrated Technology to Transform Private Capital Markets

ERIC HEIMARK, CEO, PACTIO

Over the past decade, private capital markets have seen unprecedented growth, not only in transaction and dollar volume, but also in deal complexity. This growth has led to a significant institutionalization of General Partners (GPs). Yet, despite these strides, the industry continues to grapple with a crucial operational challenge – a daunting dependence on manual processes and a technology stack that has not kept up with the pace of contemporary advancements. The true transformation of the industry will hinge on harnessing the potential of integrated technology.

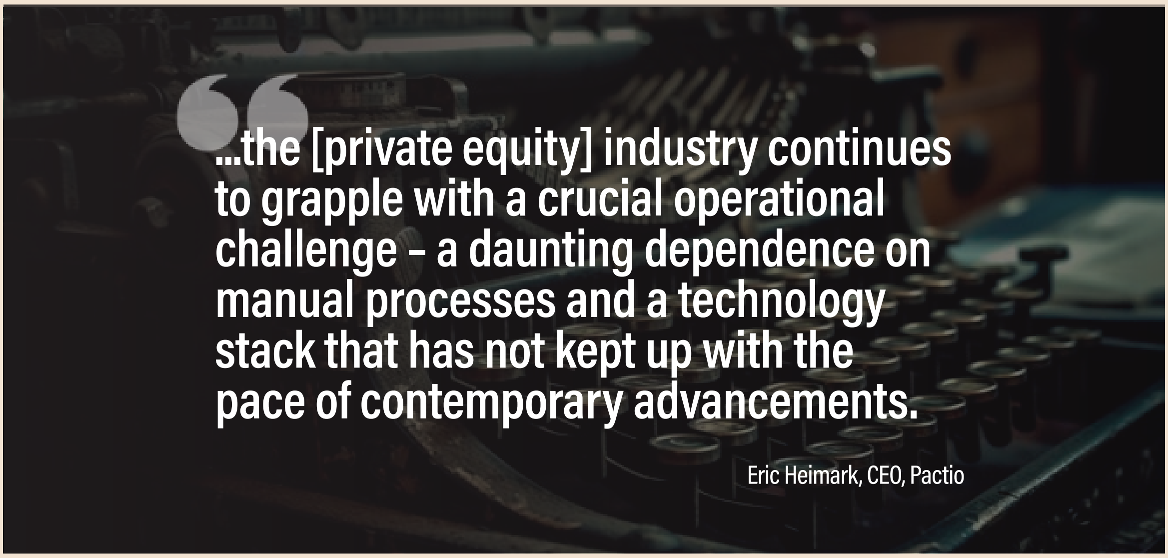
We have engaged in detailed discussions with hundreds of insiders from the alternative investment ecosystem. Our conversations spanned from investors and operational professionals at private equity GPs to professional advisors and service providers including accountants, lawyers, and fund administrators. These discussions consistently illuminated two urgent challenges:

1. Streamlining labor-intensive manual processes.
2. Effectively managing data throughout an investment's lifecycle.

The crux of these challenges lies at the deal-closing stage, which currently remains a predominantly manual process. Substantial resources, time, and energy are expended on crucial tasks where there is zero margin for error. Indeed, the high stakes involved can result in severe repercussions, as seen in 2019 when hackers intercepted a high-profile merger and stole $130 million.

Furthermore, fragmented workflows among deal team members, advisors, and support staff can lead to essential information slipping through the cracks. This issue surfaces not only during the high-pressure deal-closing phase but throughout the lifecycle of an investment. The complex coordination efforts among deal teams, advisors, fund administrators, and back-office teams make it nearly impossible to accurately track the evolution of a deal and establish a single source of truth.

Addressing these challenges is akin to taming the waters in the Gulf of Mexico. Currently, firms are resorting to patchwork downstream solutions that only partly calm the swells. A more effective approach involves moving upstream to tackle the issues at their source, namely revamping the manual process of exchange and establishing an integrated data architecture capable of supporting the intricacies of the private capital markets ecosystem.



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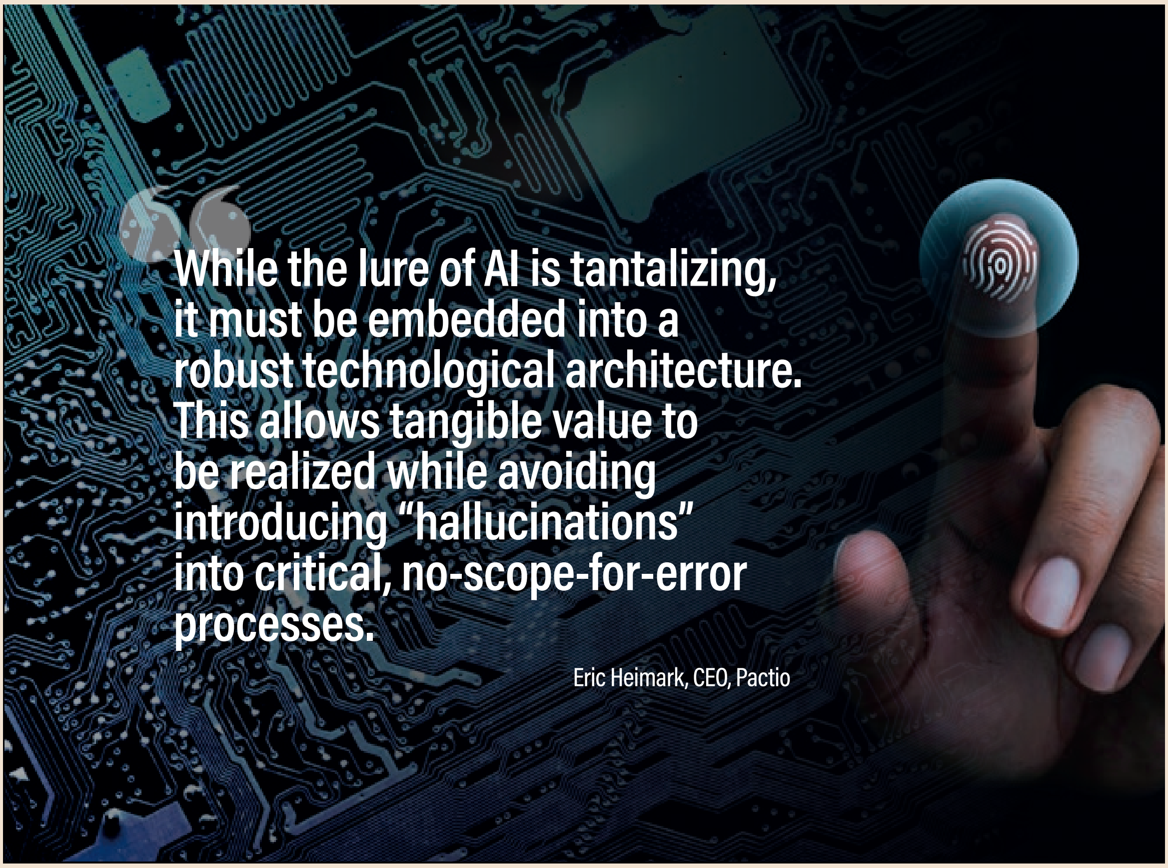

Advanced technologies offer an unparalleled opportunity for firms seeking a competitive edge. The key though is tackling the issue at its root, by implementing a solid, integrated foundation that will enable firms to harness the power of technological advances, such as increasingly powerful AI. While the lure of AI is tantalizing, it must be embedded into a robust technological architecture. This allows tangible value to be realized while avoiding introducing "hallucinations" into critical, no-scope-for-error processes.

At Pactio, we are firm believers in technology's potential to revolutionize private market operations, driving enhanced efficiency and mitigating risks inherent in manual processes. We've dedicated years to developing a comprehensive architecture that captures precise data at the source, utilizing advanced AI to bolster operational productivity immensely.

As we cast our gaze towards the future, it is the embracement of full lifecycle technology that will catalyze a true paradigm shift in private capital markets. Adopting new technology will require commitment and adaptability, but it promises substantial returns for firms willing to overcome these initial challenges.

Many private equity investors extol the virtue of tech edge in their investments, yet their adoption of quality technology hasn't kept pace with industry advancement. The moment is opportune for top-tier investors to adopt full-lifecycle technology and access its transformative potential.

Eric Heimark is the CEO of Pactio, a company that provides tech for private equity professionals. Eric was previously an investor and Executive Director in Goldman Sachs's private equity arm. Having grown up in Silicon Valley and studied computer science at Yale and Brown, he has a passion for tech.

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Accelerating growth with the power of APIs

AARON BIRD, HEAD OF ALTERNATIVES AND ENTERPRISE SOLUTIONS, ARGENTEX

Since the pandemic, which served as a catalyst for digital transformation in many financial institutions, sophisticated, new technologies are deployed with increasing velocity. Future innovation in the sector will revolutionize the way many firms operate. Funds will harness the power of Application Programming Interfaces (APIs) to improve reporting, data transparency and compliance requirements, freeing up managers to concentrate on investment strategy and client services. In such a fiercely competitive and regulated landscape, it has never been more important to stay ahead as the race to innovate accelerates.

Technology at the heart of business functions

Until recently, only institutional investors with large budgets could access the cutting-edge solutions capable of creating company-wide efficiencies and growth opportunities. Today, technology is more accessible. AI, blockchain, big data and cloud computing are commonly found at the heart of companies' business functions with more organisations taking advantage of their transformative influences.

Application Programming Interfaces (APIs) are one of the most effective tools for managing multiple tasks through a single programme. In the complex landscape of the funds ecosystem, there are hundreds of applications and software systems to create operational efficiencies. APIs enable these systems to share data in an effective and compliant way, allowing fund managers to access information in real-time for faster and more accurate decision making.

Managing the impact of currency volatility through innovation

One of the most significant innovations for investment managers are digital currency accounts that can be rapidly incorporated to reconcile payments, identify patterns through payment data and help make informed decisions about your investment's future FX

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requirements. The data can provide accurate analysis for hedging opportunities to better manage the impact of currency volatility on balance sheets and investment performance.

With the increasing adoption of technology comes a greater risk of operational and integration challenges. All technology-driven products need to be interoperable to serve their intended purpose. Firms may find themselves siloed if technology investment only covers one aspect of their business. To truly reap the benefit of today's transformative technologies, a holistic and interconnected approach is required. First adopters amongst business service providers have already developed APIs that connect their services to GPs. Thereby allowing GPs to deliver more transparent and real-time reporting as well as an improved and cost-effective experience for their LPs.

What does the future hold?

Innovation and the use of APIs is driving the future of investment funds and will have a significant impact on how they operate. Tech-driven tools will play a crucial role in meeting evolving client and regulatory requirements, making investment decisions and thriving in a competitive landscape.

As technology continues to evolve, more innovative solutions will be developed that will drive further efficiencies in the finance industry. APIs will continue to gain prominence and firms with a clear vision of how to implement them across their entire organisation will see the most benefit.

By Aaron Bird, Head of Alternatives and Enterprise Solutions at Argentex. Argentex is the leading provider of global payment and currency risk management solutions.

Visit www.argentex.com to find out more.

JUNE 2023

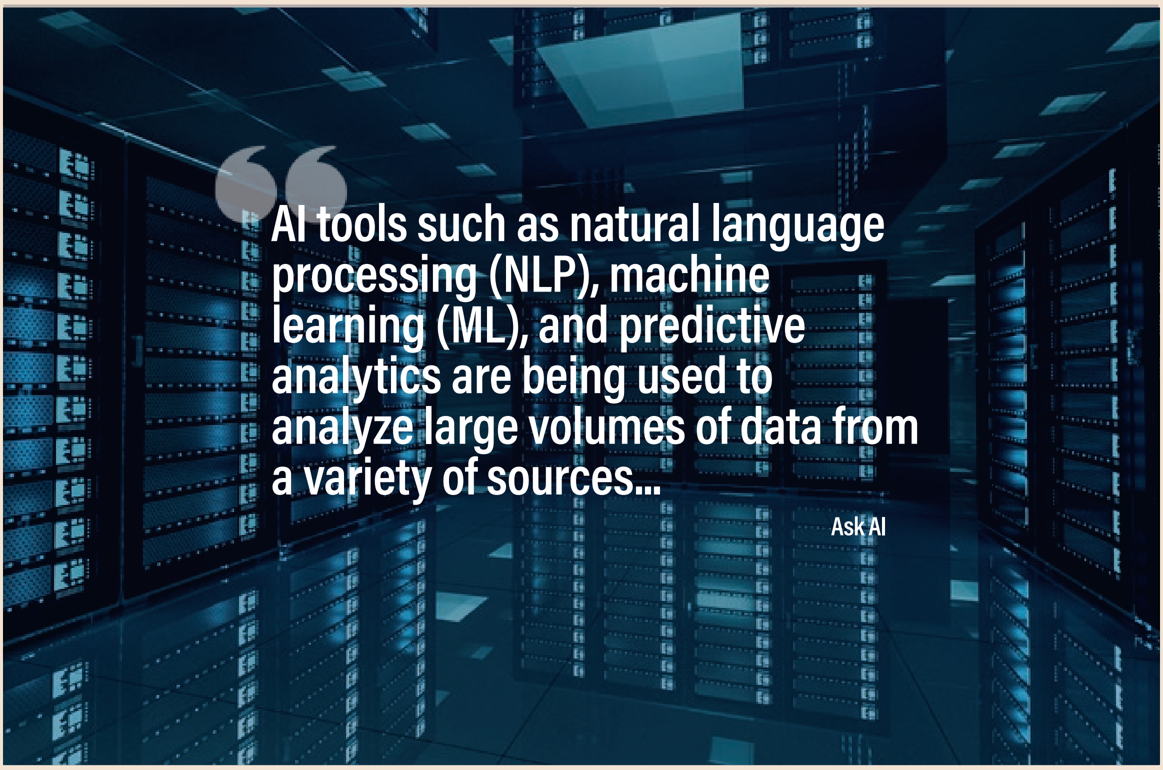
The role of AI in today's private capital markets

WHEN EVEN THE FINANCIAL TIMES IS WRITING ABOUT THE ROLE AND DANGERS - NO ESCAPE - OF AI, WE DECIDED TO TRY THE TECHNOLOGY TO TELL US THE ROLE OF AI IN PRIVATE CAPITAL MARKETS...

Artificial intelligence (AI) is rapidly transforming the private capital markets, bringing about new opportunities and challenges for investors, fund managers, and other market participants. Private capital markets have traditionally relied on human judgment and expertise to identify investment opportunities, manage portfolios, and generate returns. However, with the advent of AI technologies, private capital markets are becoming more data-driven, automated, and efficient, enabling investors to make better-informed decisions, optimize their portfolios, and achieve higher returns.

One of the key ways in which AI is changing private capital markets is by enhancing the investment process. AI tools such as natural language processing (NLP), machine learning (ML), and predictive analytics are being used to analyze large volumes of data from a variety of sources, including financial statements, news articles, social media, and industry reports. By leveraging these data sources, AI can help investors to identify emerging trends, uncover hidden patterns, and assess the potential risks and opportunities associated with different investments. For example, AI-powered algorithms can analyze financial data to predict the likelihood of a company experiencing financial distress or bankruptcy, enabling investors to make more informed decisions about whether to invest in that company.

Another way in which AI is transforming private capital markets is by improving portfolio management. AI tools can be used to optimize portfolio performance by analyzing data on historical returns, risk profiles, and market trends to identify the most promising investment opportunities. AI can also help investors to manage risk by identifying potential threats to their portfolios, such as market volatility or changes in interest rates, and providing recommendations



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on how to mitigate those risks. Additionally, AI can assist with portfolio rebalancing by automatically identifying areas of over- or under-allocation and suggesting adjustments that can help to optimize returns.

AI is also changing the way private capital markets approach fundraising and deal sourcing. AI-powered platforms can analyze vast amounts of data on potential investors and companies to identify potential matches based on investment preferences, geographic location, industry focus, and other factors. This can help investors and fund managers to identify new investment opportunities and efficiently allocate capital to the most promising deals. Additionally, AI can assist with deal due diligence by analyzing data on the financial performance, governance, and other key factors of potential investments, providing valuable insights that can inform investment decisions.

However, the adoption of AI in private capital markets is not without its challenges. One of the primary concerns is the potential for AI to perpetuate biases and exacerbate inequalities. For example, if AI algorithms are trained on historical data that reflects existing biases, such as gender or racial biases, they may perpetuate those biases when making investment decisions. Additionally, the lack of transparency and interpretability of some AI algorithms can make it difficult to understand how decisions are being made, raising concerns about fairness and accountability.

Another challenge is the need for human expertise and judgment in the investment process. While AI can provide valuable insights and data-driven recommendations, it cannot replace the judgment and experience of human investors and fund managers. It is essential that AI is used as a tool to augment human decision-making rather than replace it.

AI is transforming private capital markets by enabling investors to make more informed decisions, optimize portfolio performance, and identify new investment opportunities. However, the adoption of AI in private capital markets is not without its challenges, including the potential for bias and the need for human expertise and judgment. As AI continues to evolve and mature, it will be essential for investors to use their judgment.

Ask AI is a product developed by Codeway, a software development company that specalises in AI and machine learning.

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Dubai: a world class hedge fund hub

ARIF AMIRI, CEO, DIFC AUTHORITY

Hedge funds looking to expand their horizons are turning to Dubai with a sense of optimism at a time when they see more challenging operating environments in more established markets. Dubai and Dubai International Financial Centre (DIFC) have set themselves apart with a powerful confluence of ecosystem benefits. For hedge funds and private equity, in particular, Dubai's unique proposition includes additional regulatory, infrastructure and environmental advantages.

The Dubai Financial Services Authority (DFSA), which is globally recognised for its transparency and governance, has always been an accessible and collaborative regulator. While overseeing the DIFC jurisdiction for almost 20 years now, the DFSA frequently consults with the industry, unlike markets where funds have continued to become frustrated by slow and rigid approaches.

Alongside an environment of ambitious innovation, the DIFC ecosystem provides the perfect set of partners for funds and their portfolio managers looking to establish in Dubai. Hedge funds can hit the ground running with unparalleled access to high-calibre professional advisors, including law firms, consultancies and tax specialists within the Centre.

Over the years, DIFC has grown extensively to become a source of capital on its own, adding to some very large pools of capital that currently exist in the region. We have more than 100 family offices based in the Centre – a sector responsible for employing 80 per cent of the Middle East's workforce and contributing 60 per cent of the region's GDP.

Another benefit for hedge funds looking to set up in the emirate is the operational convenience of Dubai's central location, which bridges time zones and markets between the East and the West.

2022 saw a record number of hedge funds registering and as has been well documented there are more in the pipeline. As this number grows, the ecosystem will develop around them, attracting new and smaller hedge funds to the centre, as well as prime brokers and trading technology start-ups.

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According to the World Bank's Doing Business 2020 report, the UAE – located at the crossroads of emerging markets – holds the top spot for ease of doing business in the Middle East and North Africa. Many also appreciate the lower corporate and income tax rates. Dubai's globally competitive and enticing tax regime, including tax free income for employees, as well as the option to set up and domicile funds, make it an ideal destination for top funds amid the changing global climate.

Dubai government's focus on happiness and reputation for creating a high quality of life are also major factors in attracting hedge funds and the people who work for them. Dubai enjoys being one of the best cities in which to both live and work, ranking in the top three best cities for expats to live in globally along with Miami and Lisbon.

It's clear to see the attraction that Dubai has for hedge fund managers and at the DIFC we will continue to create an environment where they and their employees can thrive.

Arif Amiri, CEO, DIFC Authority

In his capacity as Chief Executive Officer of DIFC Authority, Arif Amiri is responsible for setting the strategy and growth direction of the Authority. Under his leadership, DIFC has emerged as a powerful catalyst for the financial services sector, as well as the leading global financial centre in the Middle East, Africa and South Asia (MEASA) region.

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How the DIFC became the largest hedge fund management hub in the MEASA region

MUNEER KHAN, PARTNER, MIDDLE EAST REGIONAL HEAD, SIMMONS & SIMMONS

The Dubai International Financial Centre (the DIFC), a financial free zone within the Emirate of Dubai, is the largest financial services centre in the Middle East, Africa and South Asia (MEASA) region. In recent years, a growing number of hedge fund managers have been attracted to the DIFC as a result of various pull and push factors. As a result, the DIFC has rapidly emerged as the largest hedge fund management hub in the MEASA region and continues to experience exponential growth.

A significant accelerant for this influx of asset managers was the COVID-19 pandemic. Whilst some financial hubs like London, Hong Kong, Singapore and New York were subject to significant COVID restrictions and stringent lockdowns, Dubai took a more balanced approach (combining a strategy of rapid vaccine rollouts, social distancing measures, open borders and remaining open for business). This resulted in many people relocating, including hedge fund portfolio managers.

The UAE's favourable tax regime (in particular, there is no personal income tax) has also been a key driver, especially when this is contrasted with the global rise in living costs and tax rises. In the global war for talent, having the ability to offer the option of a Dubai office is often becoming a decisive factor. This is particularly the case for the multi-strategy, multi-manager platforms, more and more of whom have been setting up a significant presence in the UAE.

The UAE "golden visa" scheme, which is a five or ten-year self-sponsored renewable residence visa scheme for "specialised talents" and investors has also been a draw for founders, senior managers and certain specialised finance professionals, such as quants.

The UAE has a multi-faceted regulatory landscape. Financial services such as financial promotion, advice, arranging deals or asset management, are usually undertaken from one of the jurisdictions of (i) "onshore" UAE, (ii) the DIFC or (iii) the Abu Dhabi

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Global Market (the ADGM), each of which has its own financial laws and regulations. The DIFC and the ADGM are financial free zones that were formed to encourage foreign investment by offering concessions such as zero tax guarantees and complete foreign ownership of entities.

This diverse landscape ultimately provides a number of options for alternative asset managers wanting to relocate. The DIFC in particular has gained international recognition and critical mass as a world-class financial centre and is seen as an example of how governments in emerging markets around the world can potentially fast track legal and regulatory reform.

It is clear that the UAE and especially Dubai is now at the top of the list for some of the world's largest alternative asset managers and their talent, who increasingly see it as a longer-term home for them and their families. Though one can never predict the future of global markets, especially in current times, based on our own pipeline of applications, we expect the speed at which hedge fund managers have entered and set up in the DIFC and wider UAE to continue for the rest of 2023 to 2024.

Muneer Khan, Partner, Middle East Regional Head, Simmons & Simmons

In his capacity as the Middle East managing partner and head of financial markets at Simmons & Simmons, Muneer Khan has been closely involved in advising a large number of leading international hedge fund managers on their strategies for Middle East establishment and expansion. In this context, he has also worked closely with regulators and financial centre authorities, such as the DIFC Authority, on key policy and strategy issues to facilitate growth in the asset management sector.


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The Emergence of a Global Financial Center

TATZIANA PARAGUACUTO, TOM HAGGER & TOM COCHRANE , WALKERS GLOBAL

For almost two decades, the Dubai International Financial Centre (DIFC) has been positioning itself as a leading financial hub in the Middle East and North Africa (MENA) region. While it has a strong presence in various sectors, including banking, finance, and insurance, the DIFC has also been actively promoting itself as a hub for asset management.

In recent times, a variety of factors have galvanised the DIFC's position as the dominant financial centre in the MENA region. Such factors include:

- geopolitical tensions in Eastern Europe as a result of the Russia-Ukraine conflict (which has resulted in an influx of talented asset management professionals into Dubai);
- the adept handling of the COVID-19 pandemic in the United Arab Emirates (where the response to the pandemic was generally regarding as being measured, pragmatic and proactive); and
- the continued buoyancy of financial markets in the United Arab Emirates and the MENA region more broadly (with high oil prices, among other things, allowing for continued investment opportunities at a time when much of the global economy has either stalled or experienced a downturn).

These factors, paired with the concentrated and strategic efforts of the DIFC to lure asset and wealth managers to Dubai, have been incredibly successful, and provide a strong foundation for the DIFC's continued future growth in the medium to long term. High profile names in the asset management industry to set up in the DIFC in the last twelve months include Edmund de Rothschild Group (which opened an advisory office in the DIFC in February of this year), Nomura (Japan's largest investment bank and brokerage group) and Bahrain's The Family Office (which is seeking to expand its regional client base). In total, the DIFC now has more than 300 wealth

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and asset management companies registered in the centre, representing an industry size of approximately US$450 billion.

As a top tier offshore law firm with a full service offering in Dubai (which includes the provision of certain corporate services to DIFC-domiciled entities), Walkers works regularly with a wide range of asset managers, family offices, investment banks and wealth management companies (along with their onshore counsel). Such clients typically require a mix of onshore legal services and complementary offshore legal services. For example, we have often seen asset managers establish a presence in the DIFC (and become appropriately regulated by the Dubai Financial Services Authority (DFSA), the DIFC's financial services regulator) when launching an investment fund with a Middle Eastern nexus (such as an anchor investor based in the Middle East, or a target asset located in the Middle East). For such asset managers, when considering the domicile of their fund, the Cayman Islands is a clear market leader (both regionally and globally) and the "default" choice in many cases. Pairing a Cayman Islands fund (which has the benefits of tax neutrality, cost-effectiveness, confidentiality, investor familiarity and broad flexibility) with the credibility associated with a DFSA-regulated manager is often considered the "best of both worlds" approach, leveraging the respective benefits of the relevant offshore and onshore jurisdictions.

Both the Cayman Islands and the DIFC are taking a pragmatic and sensible approach to regulation in the asset management and broader financial services space, which is helping to attract asset managers and other types of clients to both jurisdictions. In many cases, clients will need to utilise the services of both onshore and offshore legal counsel to suit their particular needs. The opportunities in this space are vast and we look forward to working with our clients (and their onshore counsel) to help them seize such opportunities.

Tom Cochrane is a partner in the Investment Funds group in Dubai; Tom Hagger is a senior Counsel in the Investment Funds group in Dubai; and Tatziana Paraguacuto is a partner and co-head of the Investment Funds group in Walkers' London office.

With one of the world's largest specialist International Financial Centre funds teams, Walkers delivers investment funds advice in Bermuda, British Virgin Islands, Cayman Islands, Guernsey, Irish and Jersey law on a global basis. Clients from well-established financial institutions to start-up managers rely on our advice to launch new products, keep abreast with regulatory change, and ensure that good governance is in place.

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Lifting the Lid on the UAE Hedge Fund and Digital Assets newest hotspot

TOM KEHOE, GLOBAL HEAD OF RESEARCH AND COMMS, AIMA

The past year has seen plenty of noise regarding alternative investment funds, including some of the largest names in the hedge fund industry migrating to the United Arab Emirates (UAE).

The region is mounting a real charm offensive, with regulators and authorities taking advantage of the recessionary environment in the UK and US, as well as the slowness of China to exit the COVID-19 pandemic.

In comparison, there is a clear intent to have the very best businesses globally move to the UAE region with the leadership offering all types of enticements to make this happen, including tax-free compensation, long-term resident visas, and a can-do attitude by the government to attract businesses to develop and prosper. Subsequently, the region is witnessing a migration of fintech, crypto and hedge funds, among others.

With its robust financial infrastructure, strategic location, favourable regulatory framework, and attractive tax regime, the UAE has emerged as a premier destination for hedge funds looking to diversify and expand their operations.

The sentiment of hedge funds in the region is captured in AIMA's quarterly Hedge Fund Confidence Index, which asks fund managers to score their confidence in their economic prospects over the coming 12 months on a scale of -50 to +50. The HFCI has run since Q4 2020 and expanded to include the Middle East in Q4 2022. Since then, the Middle East has always ranked among the most confident regions and scored the highest ever average confidence score for a region in Q1 (+22.6). The Q2 HFCI showed the Middle East to have notably resiliency in its confidence at a time when most other regions recorded more bearish sentiments, the Middle East

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remained at +16.5, second only to North America at +16.7.

Central to this migration has been the influence of two key industry players in the region, the Dubai International Finance Centre (DIFC) and the Abu Dhabi Global Market (ADGM), each of which has its own financial laws and regulations. The former suggests that as many as 20 foreign hedge funds firms have set up in the DIFC over the past year with another 20 in the pipeline over the remainder of this year. The latter is also witnessing a lot of interest from foreign firms seeking a fund license.

The UAE leadership continues to forge ahead to establish the region as a global hub for digital assets. In 2018, the Financial Services Regulatory Authority of the ADGM became the first jurisdiction globally to introduce an implement a comprehensive and bespoke regulatory framework for the regulation of exchanges, custodians, brokers, and other intermediaries engaged in virtual asset activities. The rest of the UAE was quick to follow suit. Fast forward to February of last year where the Dubai government established the world's first dedicated virtual assets regulator (the Virtual Asset Regulatory Authority or VARA) tasked with the regulation, governance, and assurance of licences for virtual asset regulated activities, including brokerage and asset management. Not to be outdone, the DFSA is also developing a framework to maintain oversight of the cryptocurrency and digital asset space.

AIMA is no stranger to the UAE, boasting members from across the region for several years. Recognising the buzz of activity with foreign firms migrating to the region, we have established a manager-only AIMA members' network. This group will be a forum for peer-to-peer discussion, supporting members actively monitoring and advocating on a variety of proposed rules and guidelines as well as offering practical guidance that will enhance the operations of its alternative asset manager members in the region.

If you are an AIMA member operating in the UAE or are interested in what others are doing in the region, we would love to hear from you by contacting us on the following email address (info@aima.org).

Tom Kehoe

Global Head of Research and Comms, AIMA

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