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HEDGE FUND LAUNCHES INCREASED HEADING INTO 2023 AS MACROECONOMIC, FINANCIAL RISKS SURGED

Liquidations steady to conclude volatile 2022; Fund managers position for volatility & risk in 2023

CHICAGO, (March 31, 2023) – New hedge fund launches were on the rise in 4Q 2022 as the industry headed into 2023, rising from the lowest level since 4Q 2008 in the prior quarter as investors positioned for increased likelihood of economic recession and prior to a sharp rise in financial risks in banks associated with the sharp increase in interest rates over the past year, according to the latest *HFR Market Microstructure Report*, released today by HFR®, the established global leader in the indexation, analysis and research of the global hedge fund industry.

The estimated number of new hedge fund launches increased to 96 in 4Q22, an increase from the historic low of 71 launches in 3Q22, which had represented the lowest launch rate the depths of the Global Financial Crisis in 4Q08. The number of hedge fund liquidations was steady over the prior quarter, as an estimated 144 funds closed their doors in 4Q22. For the full year 2022, an estimated 432 total new hedge funds launched, while an estimated 571 funds liquidated.

The HFRI 400 (US) Fund Weighted Composite Index has gained +2.0 percent YTD through February, led by Event Driven and Equity Hedge strategies. The investable HFRI 400 (US) Event Driven Index has led strategy gains to begin 2023, gaining +3.0 percent YTD through February driven by an uptick in M&A, Shareholder Activist, and Special Situations campaigns.

The performance dispersion of the HFRI Fund Weighted Composite Index® (FWC) elevated slightly from the prior quarter, as the top decile of index constituents returned an average of +18.2 percent in 4Q22, while the bottom decile declined by an average of -9.7 percent, representing a top/bottom decile dispersion of 27.9 percent, compared to a top/bottom dispersion of 25.2 percent in 3Q22. For the full year 2022, the top decile of FWC constituents returned an average of +28.8 percent, while the bottom decile declined by an average of -34.0 percent, representing a top/bottom decile dispersion of 62.8 percent for the year.

Hedge fund fees remained steady and mixed to conclude 2022, with the average industry-wide management fee unchanged from the prior quarter at an estimated 1.35 percent, while the average incentive fee fell by 2 bps to 15.99 percent; both estimated fees represent their lowest levels since HFR began publishing these estimates in 2008.

For funds launched in 4Q22, average management fees declined 17 bps from the prior quarter to an estimated 1.18 percent; for all funds launched in 2022, the estimated management fee remained steady over the prior year, increasing only 1 basis point to 1.34. Average incentive fees for funds launched in 4Q22 was an estimated 17.68 percent, up from the prior quarter estimate of 17.23 percent; for all funds launched in 2022, the average incentive fee increased to 17.74 percent from the 2021 estimate of 16.57 percent.

"Hedge funds navigated an acceleration of the volatility to conclude 2022, with intense risk-on and risk-off market cycles punctuating a year dominated by increased risk of economic recession as a result of a sharp increase in interest rates necessary to tame generational inflation. The increase in launches and steady level of liquidations indicates institutions are increasing commitment to hedge funds, with institutions looking to pare back high beta equity and illiquid private equity holdings in favor of opportunistic, specialized, defensive portfolio positions," stated Kenneth J. Heinz, President of HFR. "Despite the increase, launches for the full year 2022 remain near historical lows, and increased sensitivity to financial risk by institutions as a result of bank failures may contribute to a continuing challenging launch environment to begin 2023, despite strong performance through 1Q23.With a cautious, yet opportunistic, eye towards the risks and reward continuum looking into 2023, institutions are likely to increase their exposures to hedge funds, both established and newly launched, which have demonstrated their robustness through several recent years of dislocations and intense volatility across the range of asset classes."

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