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NEW HEDGE FUND LAUNCHES FALL AS TOTAL CAPITAL INCREASES TO RECORD

Total number of funds dips below 10,000; Fees decline as performance decile dispersion steady

CHICAGO, (December 15, 2016) – Hedge fund launches declined in the third quarter, as funds again posted steady gains following the Brexit vote and leading into the surprise US Presidential election results. New launches totaled 170 in 3Q 2016, down from 200 in the prior quarter and 269 in 3Q15, 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 number of launches in 3Q16 represents lowest since 1Q09 and marks the fourth consecutive quarter of net contraction in the overall number of active funds. A total of 576 funds have launched in the first three quarters of 2016, a decline of over 200 from the 785 launches over the same period last year.

Hedge fund liquidations also increased in 3Q16, rising to 252 from 239 in the prior quarter, though nearly identical to the number of funds closed in 3Q15, when 257 funds liquidated. Through the first three quarters of 2016, liquidations totaled 782, which is on pace for the highest number of liquidations since the Financial Crisis. As previously reported by HFR, total hedge fund industry capital increased to a record of $2.979 trillion through 3Q16, surpassing the previous record of $2.969 trillion in 2Q15. The total number of hedge funds, including fund of hedge funds, declined to 9,925, falling below 10,000 funds for the first time since 2014.

Average industry-wide fees posted narrow declines from the prior quarter, although fee data was mixed on new fund launches. The overall average hedge fund management fee fell to 1.49 percent as of 3Q, a drop of 1 basis point (bps), while the average incentive fee declined 10 bps to 17.5 percent. Average management fee for funds launched in 2016 was a similar 1.48 percent, declining from 1.6 percent for 2015 launches. The average incentive fee for the vintage of funds launched in 2016 increased to 18.8 percent, up over 100 bps from 17.75 percent for 2015 launches.

HFRI performance dispersion was steady for 3Q though returns for both the top and bottom deciles rose over the prior quarter. The top decile of HFRI performance gained an average of +14.77 percent in the period, while the bottom decile declined -7.05 percent, increasing from averages of +13.74 and -7.6 percent, respectively, in 2Q16. Over the last four quarters, the top HFRI decile gained +29.54 percent, while the bottom decile fell an average of -15.57 percent, a dispersion of 45.1 percent, in line with FY 2015 dispersion.

Small and mid-sized hedge funds (AUM < $1 billion) outperformed larger, established managers (AUM >= $1 billion) for 3Q, but the performance differential narrowed YTD 2016. Funds with AUM below $1 b gained +3.0% in 3Q and +4.7 percent YTD, while funds with at least $1 b AUM advanced +2.5% in 3Q and +3.8 percent YTD. The HFRI Fund Weighted Composite (FWC) Index® gained +3.0 percent in 3Q16, contributing to a YTD return of +4.6 percent through November, topping the MSCI World Index over the same period. The HFRI Asset Weighted Composite (AWC) Index recovered losses through mid-year by gaining +2.2 percent in 3Q and is now +1.9 percent YTD through November.

"The total number of hedge funds has declined from its peak in 3Q 2015, even as industry capital has risen to record levels, with a large component of the recent consolidation occurring within the fund of hedge funds (FOF) space. Over the last year, as total industry capital increased by +3.4 percent, the number of single-manager hedge funds declined -2.5 percent, while the number of FOF's fell by -6.6 percent," stated Kenneth J. Heinz, President of HFR. "As a result of the overall increase of industry capital during this period of fund consolidation, the size of the average hedge fund has continued to rise, suggesting that investors are becoming more comfortable and willing to allocate to innovative, emerging managers as a complement to more established holdings. Investor risk tolerance has increased significantly since the US election, this combined with continued macroeconomic uncertainty and favorable political policy evolution is likely to drive industry growth into early 2017."

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