The SMA Snapshot Report - Fall 2024

Seward & Kissel has advised the investment management industry for more than 75 years and we continue to be committed to understanding the dynamics of the investment fund marketplace, and bringing the latest industry color to our clients and friends.

Accordingly, this year, we are excited to release the fourth edition of The SMA Snapshot Report, which provides insights into the current state of the separately managed account (SMA) environment within the hedge fund market over the past 12 months. Set forth in the following pages are the Report's key findings.

I. Average Time in Business for Managers:

Similar to last year's Report, 95% of the hedge fund managers managing SMAs within the Report founded their business over two years ago ("mature managers"), and more than 90% of mature managers were founded over five years ago. Just 5% of the managers were founded less than two years ago ("newer managers"). These figures demonstrate a continuing allocation trend towards mature managers with respect to SMAs, which we first observed in our 2022 Report. These findings are supported by the results presented in our various other studies on side letters, new hedge fund managers, and established hedge fund managers, i.e., that newer managers appear more likely to offer founders classes, thus potentially obviating the need for many newer manager investors having to request SMA arrangements.

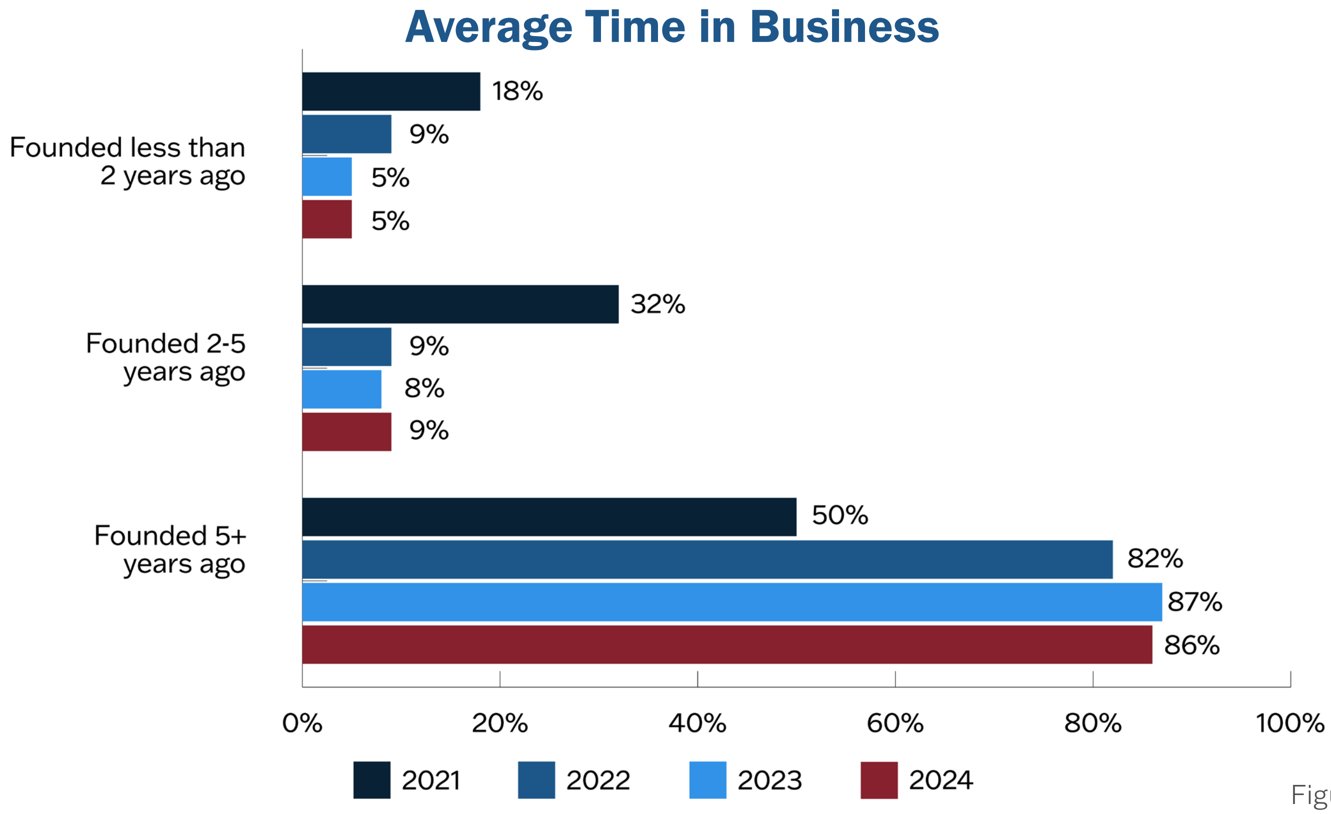

Figure: 1

II. Types of SMA Investors:

Investors into SMAs broke down into the following categories: 90% - funds (as compared to 75% in the 2023 Report) and 10% in the other category, such as pensions and endowments. Unlike the 2023 Report, there were no High-Net-Worth Individuals ("HNW")/Family Offices ("FO") represented.

With respect to newer managers, all newer manager SMA arrangements were with fund investors. The continued dominance of funds as SMA investors may be attributable, in part, to their abilities to best marshal the increased resources necessary to conduct diligence, source, and negotiate with managers in the current environment.

III. Investment Strategies:

69% of the SMAs had an equity-focused strategy (versus just 37.5% in the 2023 Report), 23% had a credit-focused strategy (compared to 50% in the 2023 Report), and the remaining 8% were in other strategies. The change with respect to equity and credit strategies may be due to an increased interest in certain equity strategies, such as technology, coupled with easing inflation, which may have dampened credit trade opportunities.

Approximately half of the strategies in the SMAs deviated from the manager's flagship strategy due to what appears to be investor desire for: long-only exposure, higher position concentrations, greater leverage, ESG considerations, or tax efficiency.

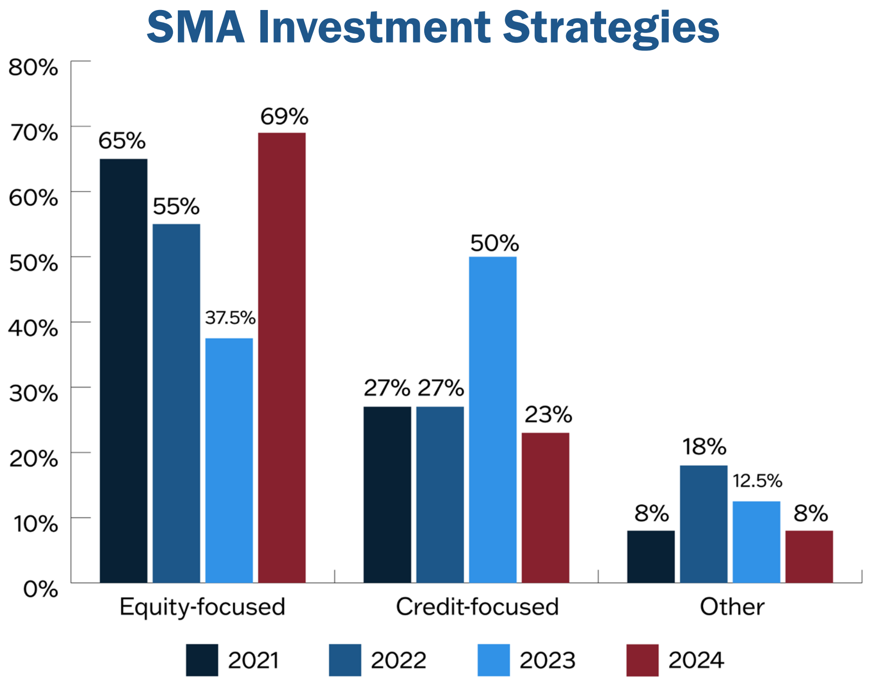

Figure: 2

IV. Account Size:

The size of allocations to mature managers increased again this year to an average account size of over $75 million (as compared to $65 million last year) and stayed about the same for newer managers at approximately $10 million.

Average Account Size for Managers ($USD millions)

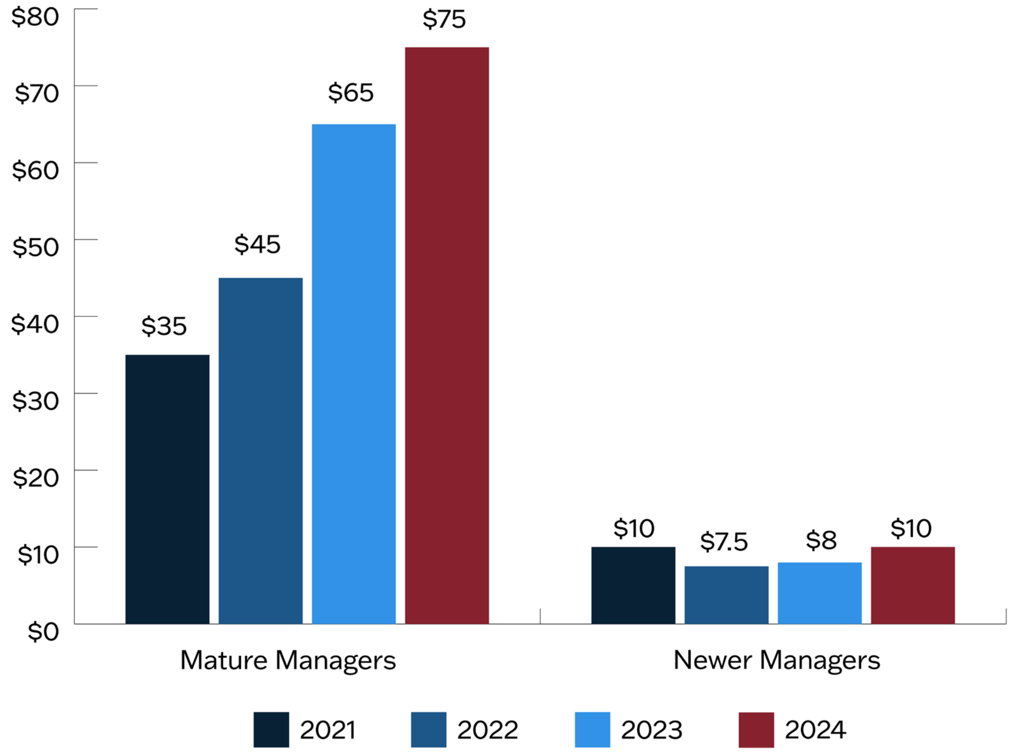

Figure: 3

V. Termination Rights:

In virtually all of the SMA agreements, clients were permitted to terminate on an average of 69 days' notice (as compared to 49 days in the 2023 Report), with 40% at month-end, 30% at quarter-end, and the rest at any time. In addition, managers were given the ability to terminate under the identical termination rights as their clients over 60% of the time (comparable to the 55% reported in the 2023 Report).

VI. Incentive Fees:

With respect to incentive fees, the SMA agreements broke down as follows:

- 9% charged no incentive fee (as compared to a significantly higher 50% in the 2023 Report);
- 18% charged an incentive fee of 10% or less (up from only 25% of the agreements in 2023);
- 9% charged a tiered incentive fee structure; and
- 73% charged a traditional 20% incentive fee (versus 25% in the 2023 Report).

The substantial changes over the 2023 Report with respect to the incentive fee rates charged (as well as the management fee rates charged, as discussed below) may reflect a shift in investor dynamics where investors were willing to pay higher incentive fees for performance, but pay less management fees to subsidize the manager's overhead.

VII. Management Fees:

The average management fee was 0.71% (down significantly from the 2023 Report's 1.25%); however, 30% of all SMA agreements had some form of tiered management fee structure typically tied to different AUM levels. In addition, 9% of the agreements charged no management fee.

VIII. Standard of Care:

Similar to the 2023 findings, except for SMAs with ERISA clients, all the remaining agreements contained a gross negligence standard of care (consistent with what is typical market practice for hedge funds).

IX. Most Favored Nations ("MFN") Provision:

There was a significant change in the number of SMA agreements containing an MFN clause, with almost 75% having such provisions (compared to only 20% in the 2023 Report). Each of the MFN clauses contained carveouts for insiders and larger investors, and usually those clauses only applied to other agreements with respect to substantially similar investment strategies.

Recognitions:

The Investment Management practice and partners have been widely recognized by industry organizations for our representation of investment managers, including but not limited to recognition by the following organizations: