Walkers

Fundamentals Asia

White Paper | 2024

Welcome to our White Paper for 2024

Each year, we analyse key data from new client funds to draw insights from the launch documents. Supported by industry comparisons and client feedback, our annual white paper reveals all on the market's state of play.

We're also able to use our footprint in Asia to extract and analyse the same data points across the investment funds market in that region to compare and, where appropriate, contrast how funds launched by Asia-based managers are offered against the North American market.

Where funds are found

Based on data from the Securities Investment Commission (SEC) Division of Investment Management Analytics Office, Cayman remains the dominant jurisdiction for fund formation outside of the United States, accounting for over 68% of funds.

While Cayman held steady, it's interesting to note that Luxembourg's share increased from around 8% to around 11%, while jurisdictions categorised as "Other" (which would include Hong Kong and Singapore structures) dropped by around 14% to 8%.

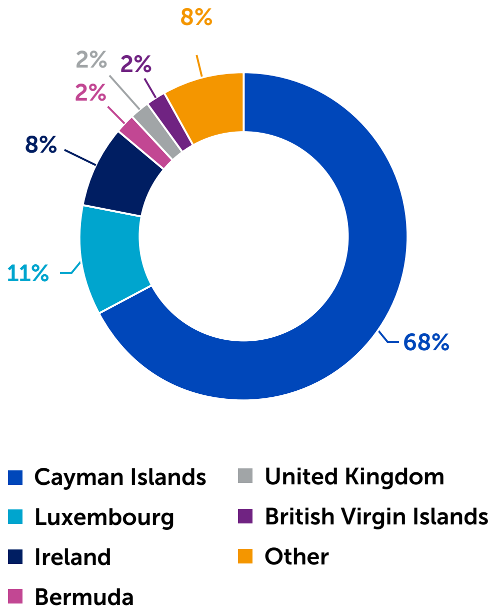
This may be taken as an indication that the "new kid on the block" structures introduced in those jurisdictions are failing to gain international traction.

Consistent with the stable position of the Cayman Islands as a funds jurisdiction, the Cayman Islands Monetary Authority (CIMA) reported growth in both the number of mutual funds and private funds registered with it.

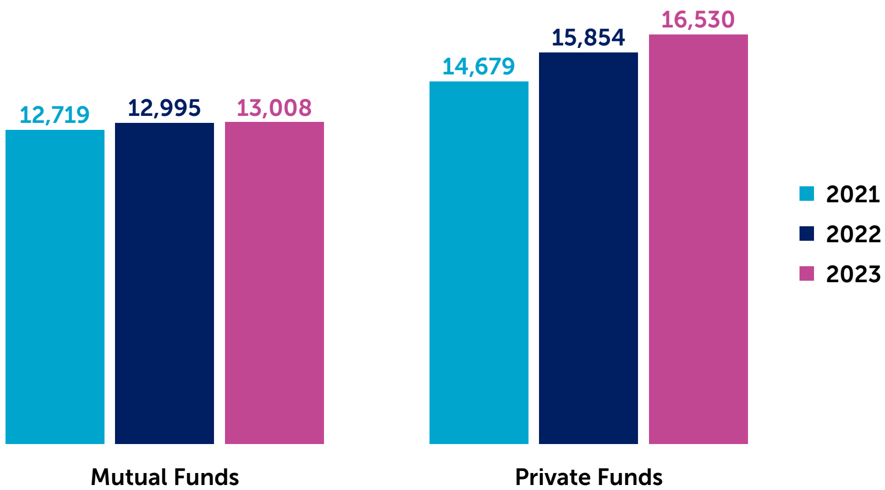
On the mutual funds side, the total registered increased by a modest amount from 12,995 in 2022 to 13,008 in 2023. New fund launches surpassed the number of funds deregistering in the period, which we understand is contrary to the global trend.

What is definitively more positive is the continued growth of "private funds" in Cayman – which cover closed-ended vehicles including private equity, real estate, venture capital, infrastructure and private credit funds. Even though these funds typically have a defined term, so there is natural attrition, there was steady 4% year-on-year growth leaving Cayman with 16,530 private funds registered with CIMA. This may not be the booming growth we've seen in years gone by, but it's a steady gain in a challenging fundraising year.

Cayman remains king



Cayman Islands Registered Funds



Fundraising

However, that growth shouldn't be interpreted as an indication that fundraising both globally and regionally wasn't difficult.

With closed-ended side funds, the observation globally before last year was the gap between first and final closing would be 12 months or less in 78% of cases.

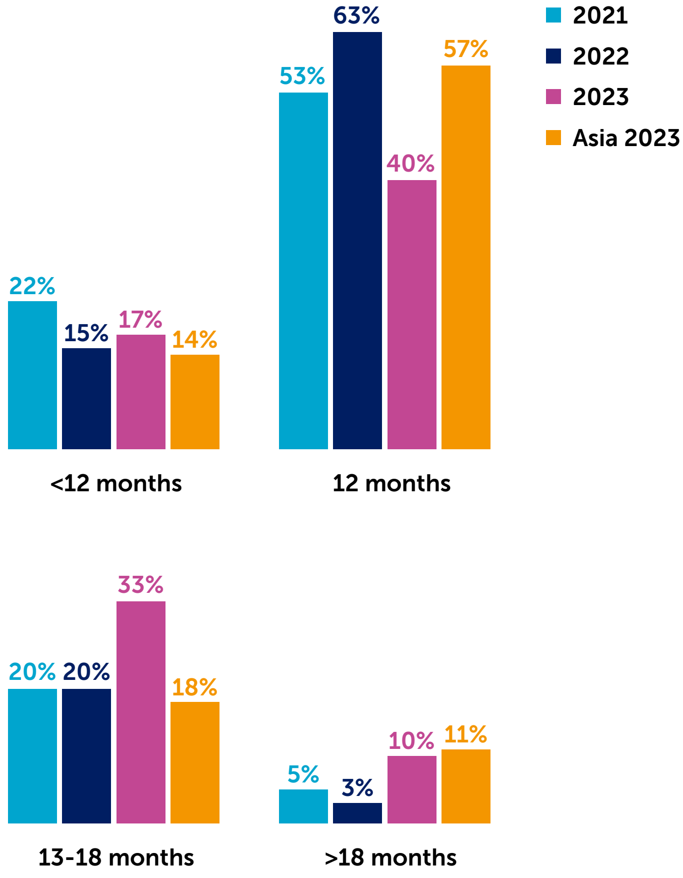
Flash forward to 2023, which signalled challenges in getting cheques through the door, this dropped to 57%. Funds having a commitment period of over 18 months, more than doubled year on year.

However, reassuringly for Asia managers, this trend was not as prevalent in the region: over 70% of funds raised by managers in Asia had a commitment period of 12 months or less.

This is a strong indicator that Asia managers can hit their fundraising targets faster than the global average, which was also a feature of last year's data.

Private Funds Offering Periods

Period between first and final closing



Fund Sizes

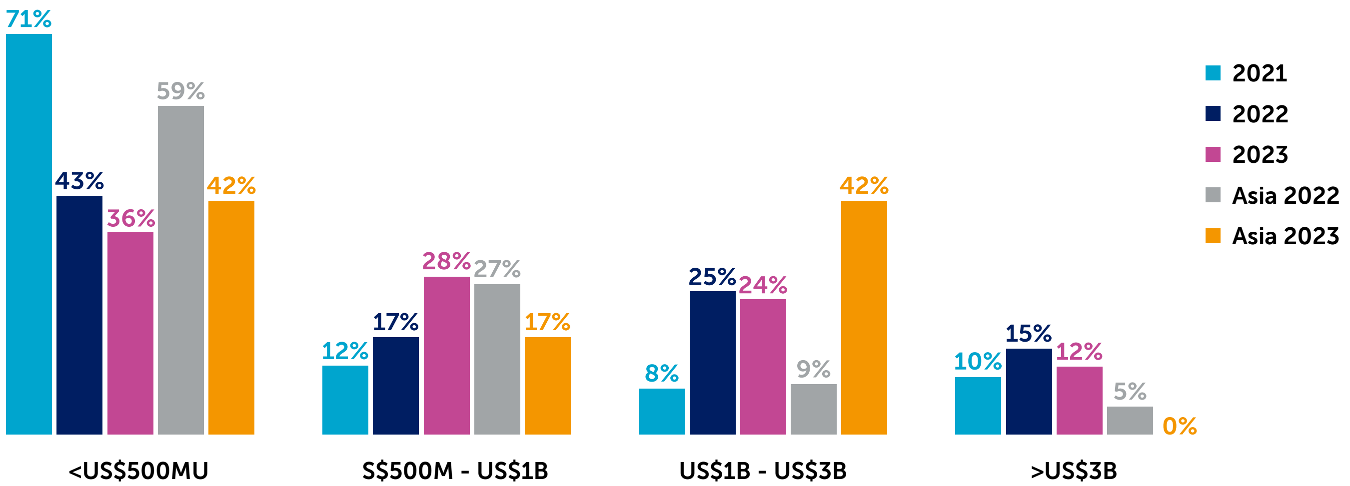
If fundraising is hard-won, we would also expect to see target fund sizes also decrease.

However, with closed-ended funds, the trend over time globally has been a shift away from the sub-US$500m target bracket to more funds targeting between US$500m to US$1bn range. There's also unsurprising resilience in the mega-fund range, dominated by household names raising later vintages.

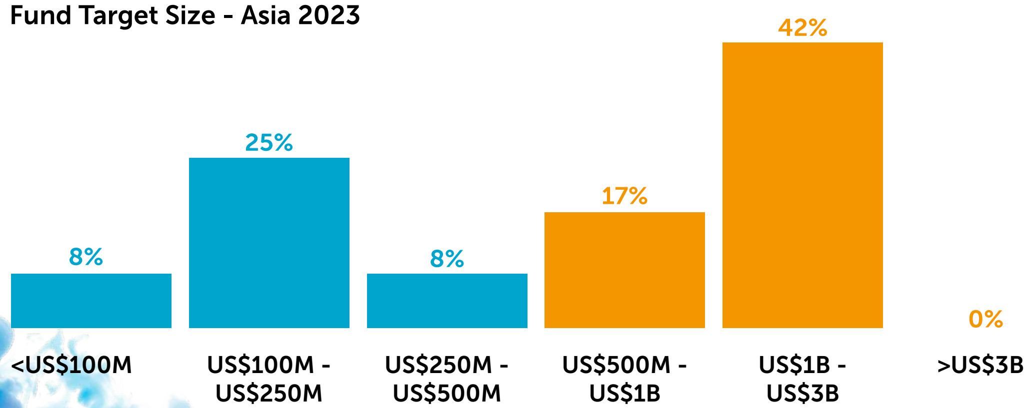
If you extract the data from Asia, this trend is actually more pronounced. Whereas the bulk, 59% of private funds in 2022 targeted sub-S$500m, in 2023 there was a real gravitational pull towards the US$1bn target mark, with a year-on-year increase from 14% in 2022 to 42% in 2023. Although admittedly, these were almost all funds on their third vintage or higher and we do see higher vintages being able to more readily target higher amounts than their start-up peers.

If this data is broken down further for 2023 and we look at the 41% of funds that targeted under US$500m, the majority of those funds were in targeting US$100m to US$250m raises.

Fund Target Size



Fund Target Size - Asia 2023



Strategies – Closed-Ended

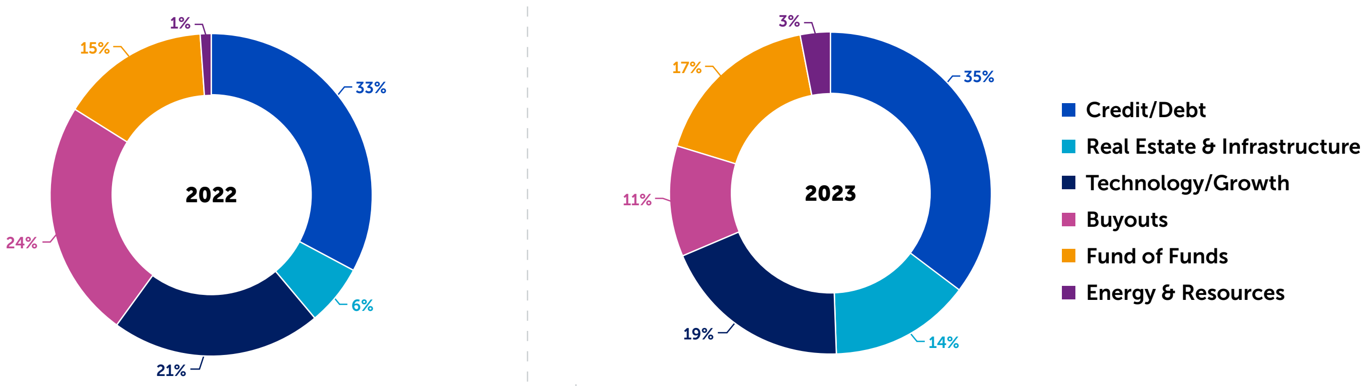
Turning to global strategies, with closed-ended funds the focus remained heavily on private credit garnering 35% of new raises, with buyout funds dropping from 24% to 11% of the number of funds raised.

This is unsurprising given that interest rates have continued to be a pull factor for subscriptions into private credit and rates have continued to make it harder for buyout funds to finance deals.

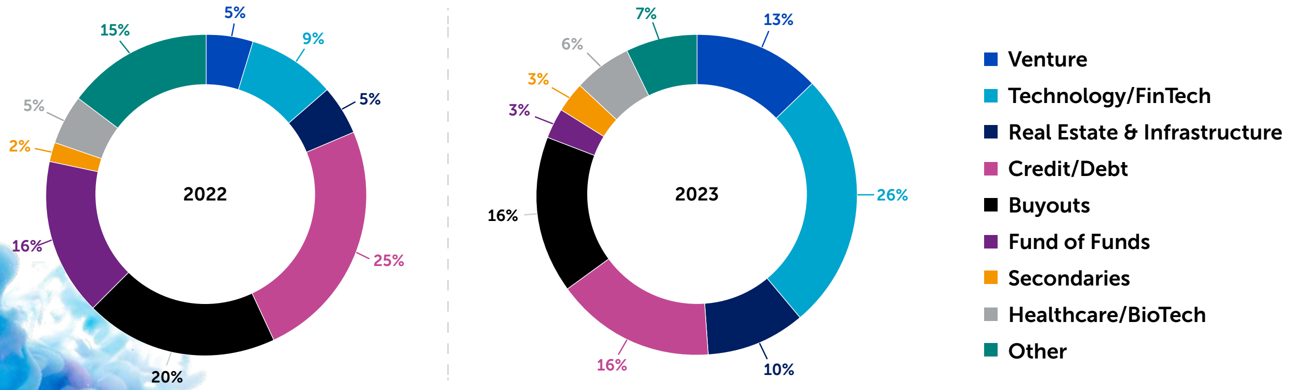
However, the position in Asia is slightly different. Our data indicates that the number of private credit funds launched slipped year on year from 25% to 16%. The more popular strategies in Asia were tech, which jumped from 9% to 26% in 2023, and tech-focused venture capital which nearly tripled from 5% to 13%. Another notable increase was the number of funds focused on real estate and infrastructure, doubling from 5% to 10%.

Based on our discussions with clients, we understand that the popularity in technology and venture capital funds was due to a combination of perceptions that valuations in the space were good, and that there's a solid supply of attractive target companies emerging in the space (including electric vehicles, artificial intelligence, battery technology, fintech and healthcare tech).

Strategies - Global



Strategies - Asia



Strategies – Open-Ended

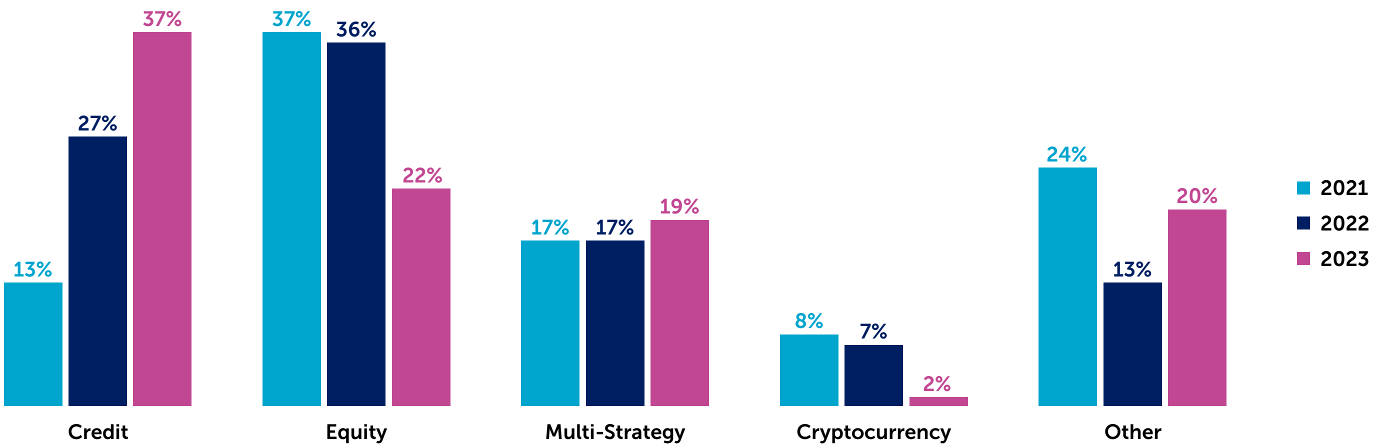
Turning to mutual funds, at the global level private credit was again popular for the second year in a row, rising from 27% to 37% of the market, overtaking equity-based strategies which dropped from 36% to 22%. Multi-strategy funds increased their share slightly and after the scandal-ridden 2022, interest in crypto funds was markedly muted.

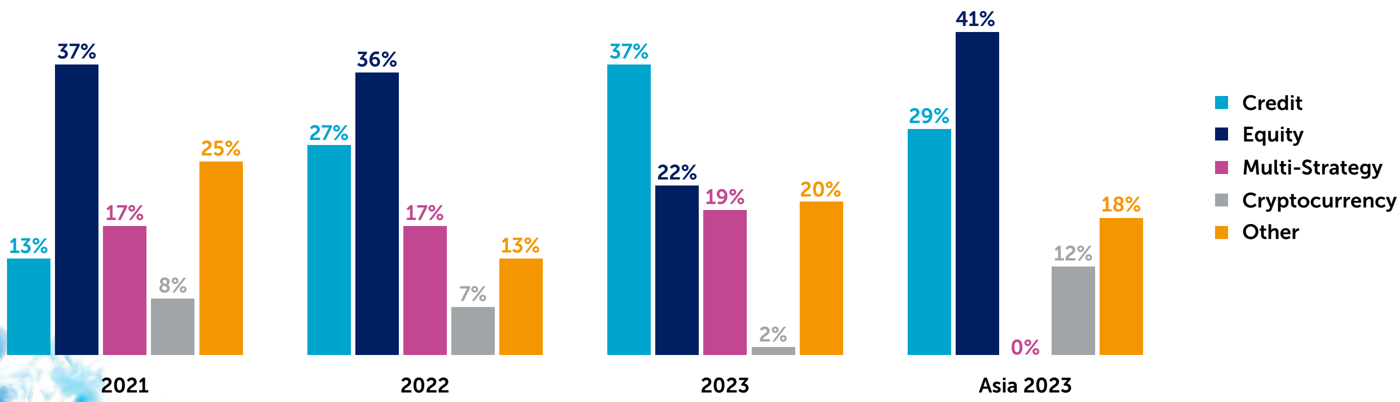
However, on the Asian side of the Pacific Ocean the experience was, again, different. Credit funds were a distant second place to the traditional, regional favourite of long-short equity strategies at 29% compared to 41%, and the number of crypto funds raised appeared to grow year-on-year based on Walkers' market position.

It's important to note that although credit isn't the top strategy in Asia, it's on the rise. The data demonstrates an increased slice of the market from a 7% share of funds raised to 29%.

This can be attributed to many factors, including regional upskilling in the credit space and clients that are established US players increasing their Asia footprint. We wouldn't be surprised to see a continued trend upwards here in 2024, as well as an increase in the number of multi-strategy funds launched regionally.

Hedge Fund Strategies





Liquidity and Gates

Staying with hedge funds and pivoting to examine liquidity, again we see that the Asia experience is slightly different from that seen in the US market. Our Cayman Islands team, which primarily looks at US raises, saw that 40% of hedge funds had lock-ups and 40% had gates. However, in Asia in 2023, 70% of newly launched hedge funds had lock-ups and 67% had gates.

We think this higher likelihood to include lock-ups, which were an even mixture of hard and soft lock-ups, in fund terms can be explained to some extent by launches in Asia having a higher likelihood to be by start-up managers with lower AUM and limited track record.

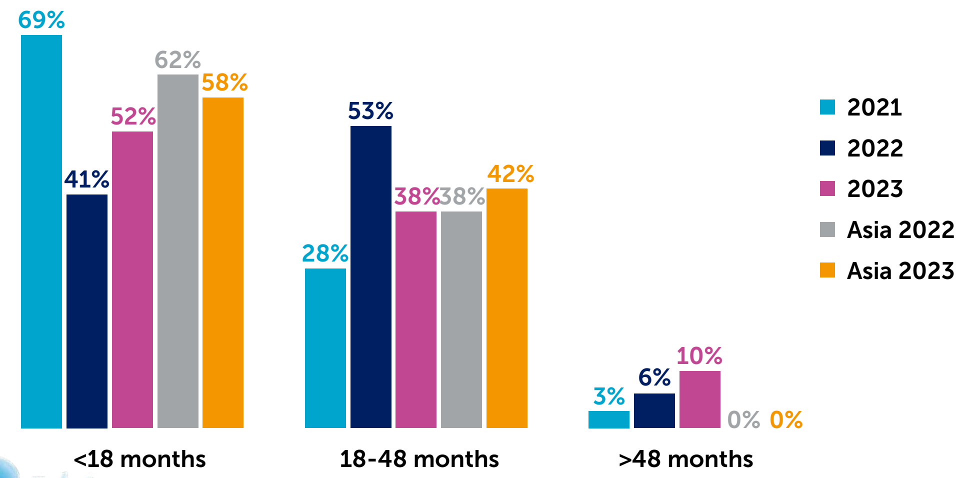
The result is that relatively small or few redemptions can create material stress on the fund. As such, a lock-up period, at least on early share classes, is perceived as necessary to ensure the long-term viability of the fund. This is typically accepted by early investors and seeders, taking a longer-term view of the managers.

We note that we don't interpret the length of lock-up periods data above as showing a correlation between Asia-based funds and US-based funds. Instead, we see that the length of lock-up periods and other liquidity constraints tends to correlate to strategy and portfolio construction.

Similarities between regions above appears to be partially coincidental, and partially reflect the market share increase of credit funds which represented 29% of new launches in Asia in 2023, which is closing in on the 37% market share observed by our Cayman Islands team.

As to the redemption fees charged on soft lock-ups, in 85% of cases in Asia, redemption fees in 2023 were less than 2%. However, in the US it was the opposite. 85% of new funds implementing soft lock-ups had a redemption fee of over 2%, with some much higher in the 6-10% range.

70% of Funds in Asia use Lock-ups



Liquidity and Gates (cont.)

Turning to redemption gates, one clear trend at the global and regional level is that the dominance of investor-level gates over fund-level gates has fallen over the past few years. However, globally the trend in 2023 was a preference for investor-level gates over fund-level gates (53% versus 41%).

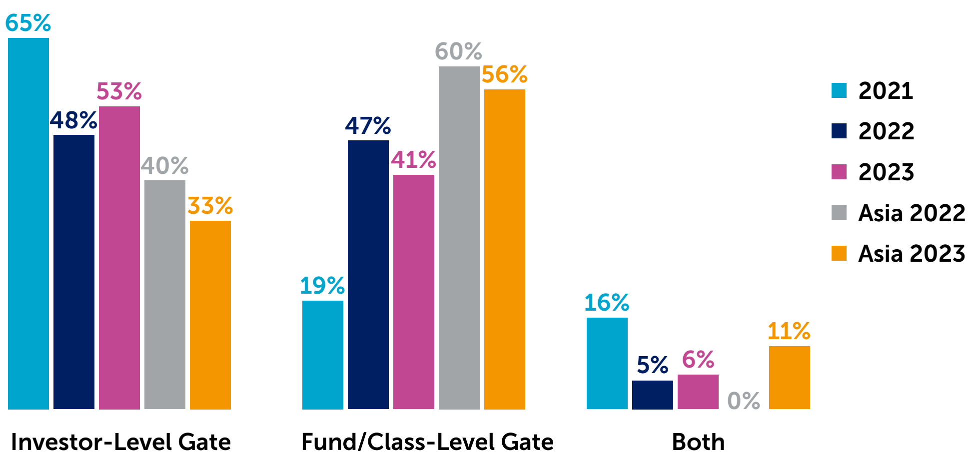
Conversely, in Asia, there is a preference the other way round: the data showed 56% imposing fund or class level gates versus 33% with investor level gates. It's also much more common in Asia to see both investor level and fund/class level gates being used (11% versus 6% globally).

In summary, liquidity restrictions seem to be materially more acceptable for investors' Asia-managed funds than for their US-facing counterparts.

Finally, with liquidity, there has been a decline in the use of side pockets in Asia from 56% to 38%. It's important to note that this data doesn't contradict the general trend of Asia managers using tools to restrict liquidity.

Instead, there's a correlation between using side pockets and strategy. It's much more common for funds running an equity strategy flexibly use side pocket illiquid assets than those running a debt strategy. Over 80% of the equity funds launched in 2023 had side pockets: the decrease in the percentage of funds, overall, using this tool reflects the increase in credit funds which are less likely to adopt the flexibility to use side pockets.

Redemption gates



Fees

We continue to hear that the "two and twenty fee model is dead". However, this isn't supported by data for Asian fund raises.

On the global stage, management fees continue to face downward pressure. Worldwide, on the open-ended side in 2023, 84% of new funds have management fees of less than 2%. Only 16% had 2% or higher.

However, in newly launched funds from Asia, almost 70% of funds had management fees of 1.5% or higher on their main share class. 31% were able to extract 2% management fees.

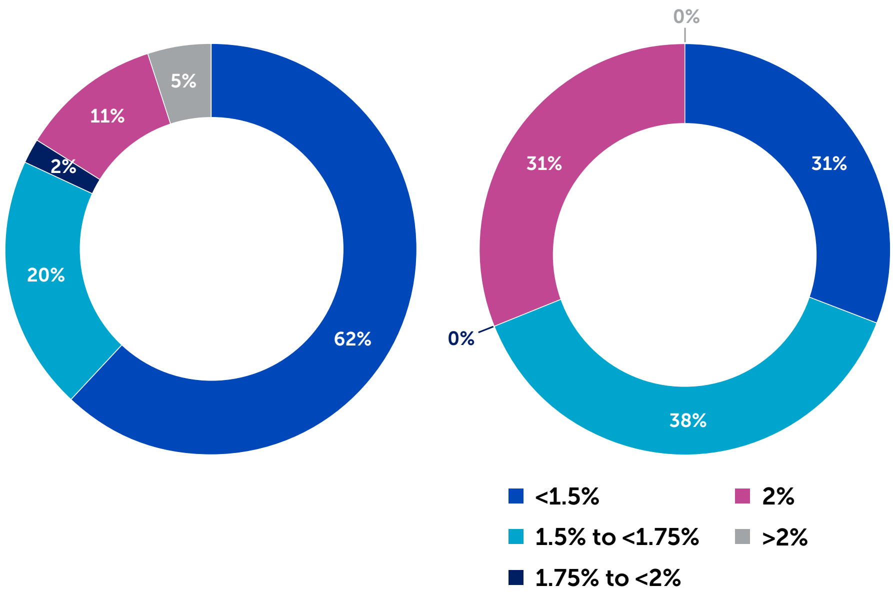
This is lower than the 36% seen in 2022 and is probably a function of relative AUMs. But it appears as though Asia-managed funds are three times more likely to command a 2% management fee than their US counterparts.

In the closed-ended space, although globally 2% fees came under stress with funds charging less than 2% trending upwards to 70% and funds charging more than 2% trending downwards 30%, in Asia the trend was reversed. Funds charging less than 2% fell from 52% and those charging more rose from 48% to 59%.

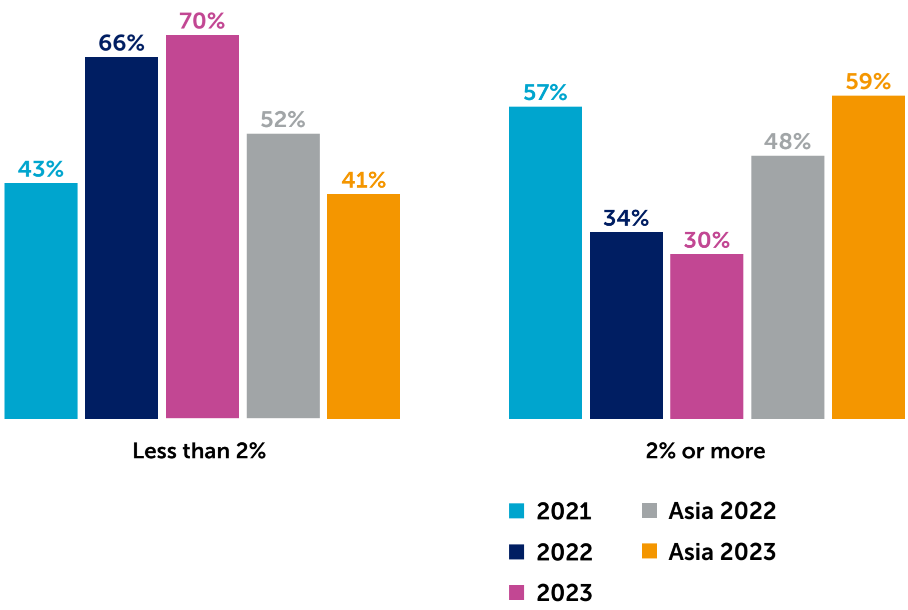
However, the news isn't positive across all strategies. Real estate fund managers were almost exclusively asking for 1% or less. Credit funds were charging management fees of between 1% to less than 2%. Technology, fintech and venture funds brought the average up, with all funds launched with these strategies where our firm acted as Cayman Islands legal counsel asking for at least 2% management fees.

Global Management Fees 2023

Asia Management Fees 2023



Close-ended management fees hold steady in Asia



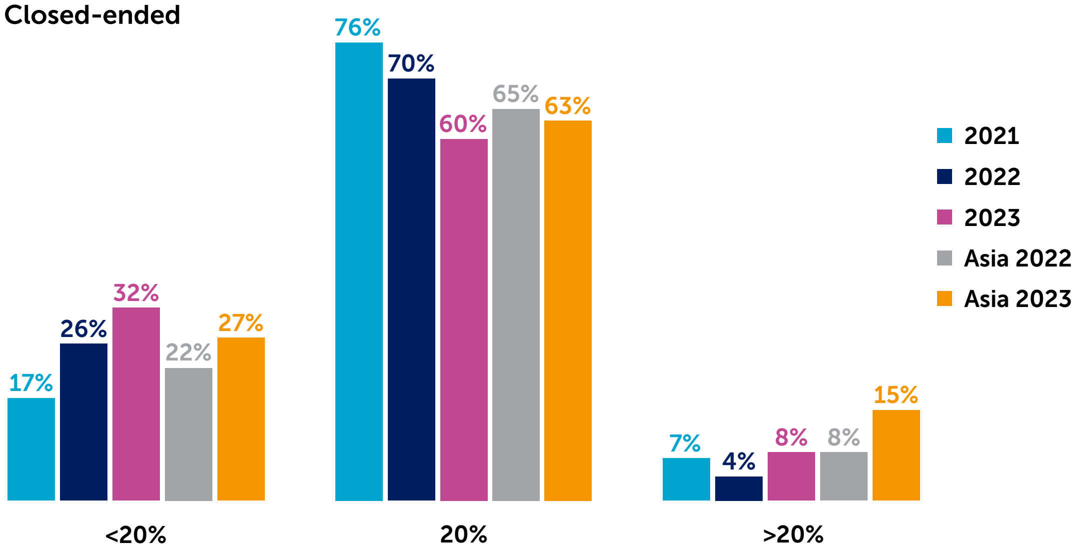
Fees (cont.)

This apparent absence of downward pressure carries over to the carried interest. A carry rate of 20% or more was present in 78% of fund documents for Asia-launched funds in 2023, increasing from 73% in 2022.

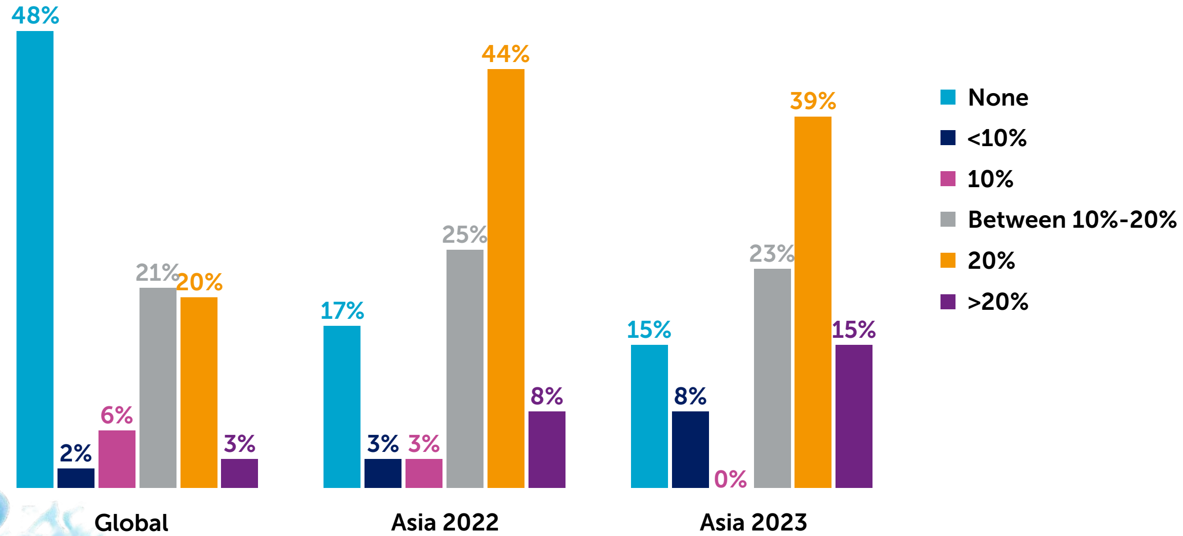
In summary, Asian managers were materially more likely to be able to deploy the "two and twenty model" in the closed ended space than North American managers.

The outcome was similar for hedge funds. In 2022 and 2023 Asian funds were more likely than not to charge performance fees at 20% or higher. An increasing number year on year were able to take fees above that 20% benchmark, rising from 52% to 54%.

Closed-ended



Open-ended 20% performance fee

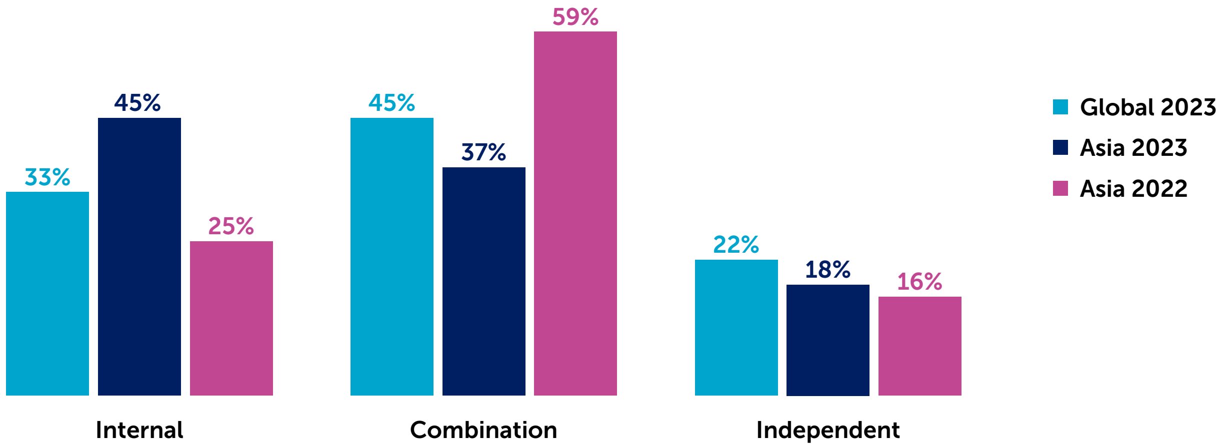


Corporate Governance

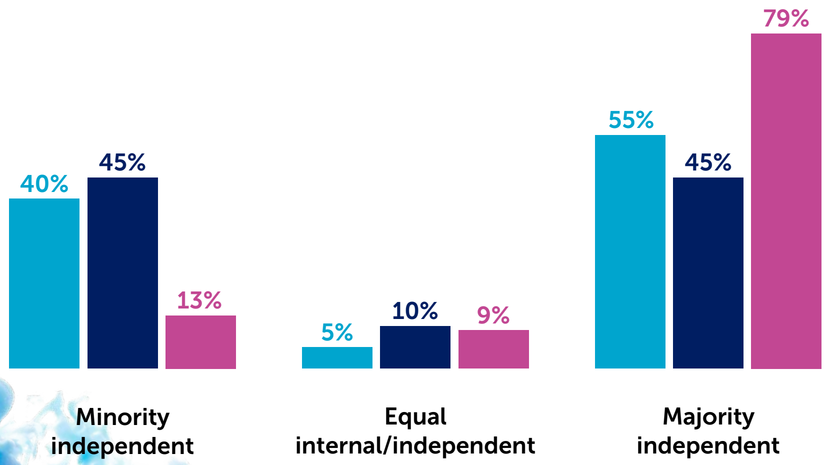
The last metric to discuss is corporate governance, and specifically board composition. In this respect our data has revealed an interesting swing away from independence on fund boards in Asia, which we weren't expecting. For the first time, we saw a decrease in boards with independent directors in Asia.

Boards populated by internal staff also became more prevalent in Asia than the global average. Comparing year-on-year in Asia, this decline is even more pronounced. When looking at combination boards, Asia has dropped from 59% to just 37%.

Are the Fund's Directors internal, independent or a combination of both?



What is the combination of the Fund's Directors?

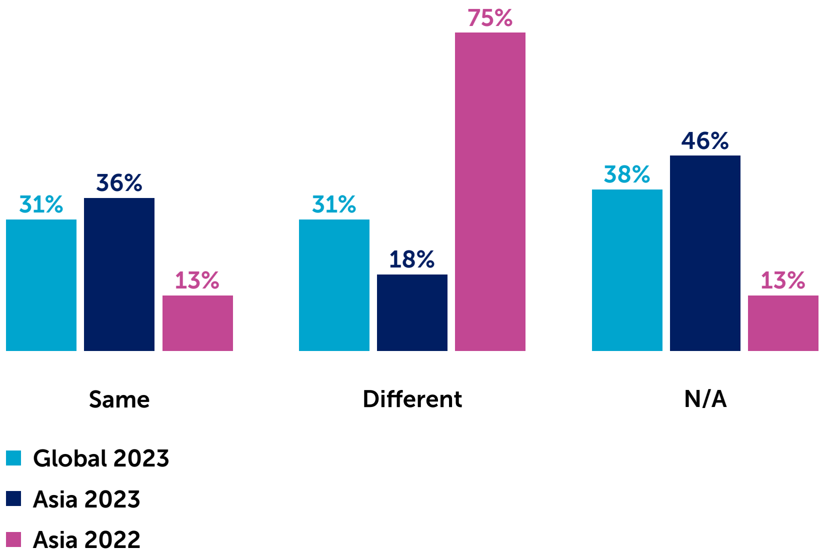


Corporate Governance (cont.)

This theme continues when looking at how 'independent' the independent boards are, with a trend towards using the same service provider to populate the boards in Asia.

Given the global trend towards investors demanding better oversight and governance, combined with increased regulatory scrutiny and focus on governance processes and procedures, we don't think this trend will continue.

Are the Fund's Independent Director all from the same service provider or different service providers?



Concluding Remarks

Although 2023 will be remembered by many as challenging, both in fundraising and performance, the data we've collated suggests there are reasons to be cheerful.

Managers in Asia have the ears of those investors needing to be able to implement liquidity restrictions, at least in relation to open-ended funds. What's more, across the board there seems to be an acknowledgement that the hard work and entrepreneurial spirit that characterises the Asian funds market should be rewarded with appropriate fee levels.

With those takeaways in mind, we remain positive that the years ahead will continue to see vitality in the regional industry, and we look forward to being a part of it.

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