
Morningstar and Barron's

2013–2014 Alternative Investment Survey of U.S. Institutions and Financial Advisors

- ▶ Survey aims to capture trends in alternative investing among institutions and advisors.
- ▶ This was the eighth annual nationwide survey.
- ▶ 372 institutional investors and 301 advisors participated.
- ▶ Institutional survey included 19 questions; advisor survey had 26.
 - ▶ Surveys included five free-response questions tackling new topics, such as alternative fixed-income products, manager due-diligence process, hedge fund advertising, and alternative benchmarks.

Long-short equity strategies continued to lead the way; interest also turning to multialternative and nontraditional bonds

- ▶ Organic growth rates for mutual funds rose to eye-popping levels. Long-short equity funds rose by more than 80 percent in 2013, followed by non-traditional-bond and multialternative funds. Advisors and institutions both cited long-short equity and multialternative as top strategies for investment over the next five years.
- ▶ Assets surged in the non-traditional-bond category in 2013 as more than a fourth of advisors cited a poor bond market outlook as a principal reason to invest in alternatives. Advisors and institutions indicated, by a significant margin, that they valued fixed-income alternatives more for their low correlation than their yield and interest-rate hedging.

Mutual funds accelerate as vehicle of choice for alternative strategies; investments concentrated in few funds

- ▶ Mutual funds continued to make gains across the board as a preferred means for accessing alternative strategies. Mutual funds jumped to 73 percent from 57 percent in last year's survey as the stated vehicle of choice for advisors to gain access to long-short equity or debt strategies and to 48 percent from 32 percent for institutions accessing managed-futures strategies.
- ▶ Assets in alternative mutual funds are extremely concentrated. As of May 2014, almost half of all alternative mutual fund assets were concentrated in the 10 largest funds.

Still interest and perceived value in alternatives, but enthusiasm may be moderating; fees remain a concern

- ▶ Alternative investments remain important for both advisors and institutions with more than half indicating that they were as important or more important than traditional investments, but enthusiasm may be cooling. Fewer institutions and significantly fewer advisors cited alternatives as “much more important” than traditional investments in this year’s survey than they did in 2010.
- ▶ After record inflows into alternatives in recent years, growth in alternatives may start to ease, especially for advisors. In the 2010 survey, more than half of advisors said they expected to increase their allocations to alternatives by more than 10 percent per year; only 39 percent said the same this year.

- ▶ Advisors and institutions say the biggest sticking point for buying alternative investments is still their relatively high fees.

Manager experience trumps “skin in the game” when it comes to investment selection; standard benchmarks still the standard

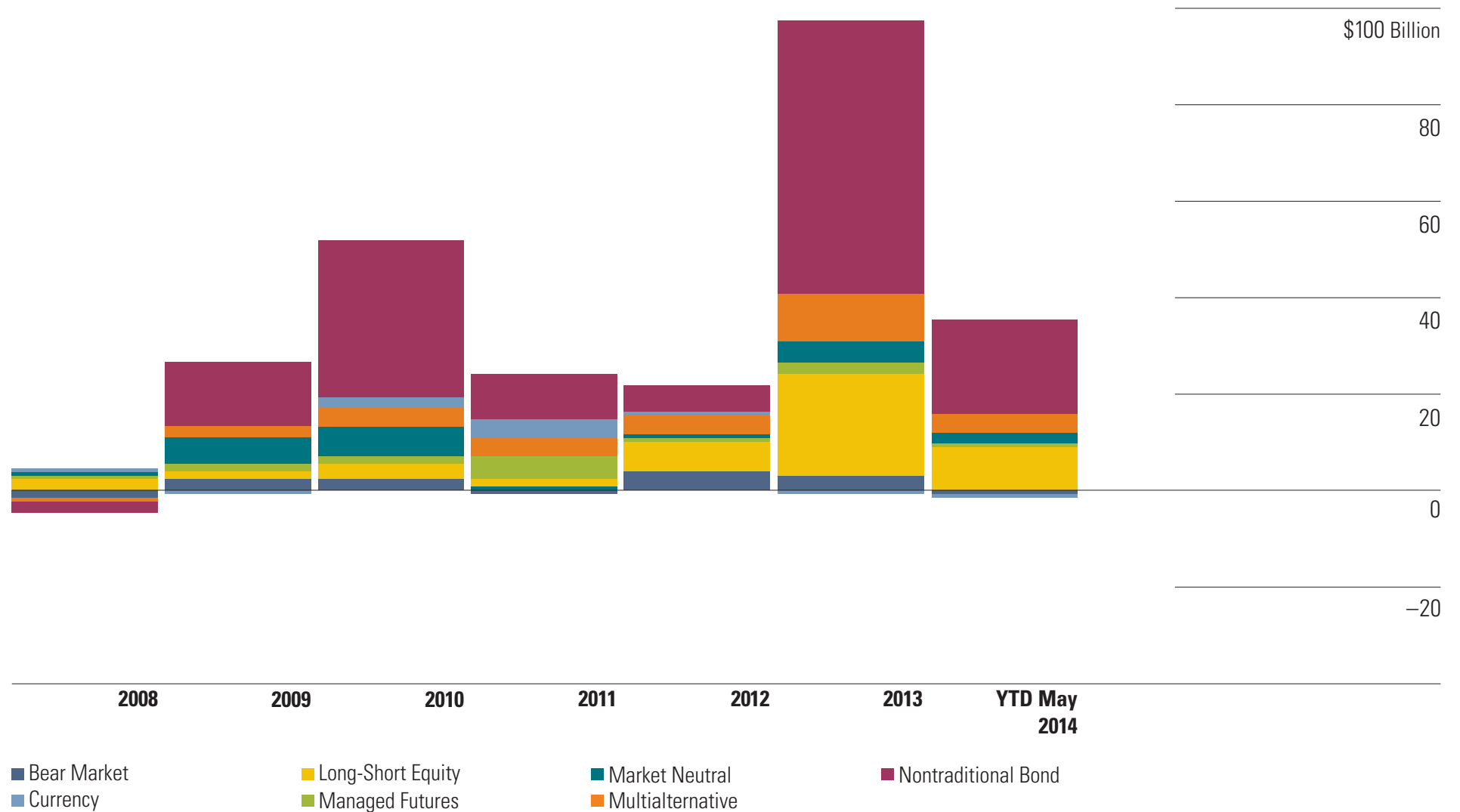
- ▶ When selecting alternative products, both advisors and institutions agree that manager experience trumps other evaluation metrics, such as a manager’s investment in the strategy and the amount of a firm’s assets in alternatives. Institutions also placed emphasis on investment process while advisors were more concerned with fees.
- ▶ Suggesting that there is opportunity for new players to enter the alternatives space, only about 6 percent of both advisors and institutions said they consider a firmwide core competency in alternatives an important factor in selecting a strategy.

- ▶ Surprisingly, standard benchmarks, such as the S&P 500 Index, are the most common forms of alternatives benchmarking. Peer groups and risk-adjusted analysis follow close behind as benchmark options.

- ▶ Alternative Mutual Fund and ETF Growth
- ▶ Past and Future Alternative Investment Growth
- ▶ Alternative Investment Drivers and Deterrents
- ▶ Hot Topics in 2013–2014
- ▶ 2013–2014 Survey Participation
- ▶ Defining Alternative Investment Strategies

Alternative Mutual Fund and ETF Growth

Alternative Mutual Fund Flows



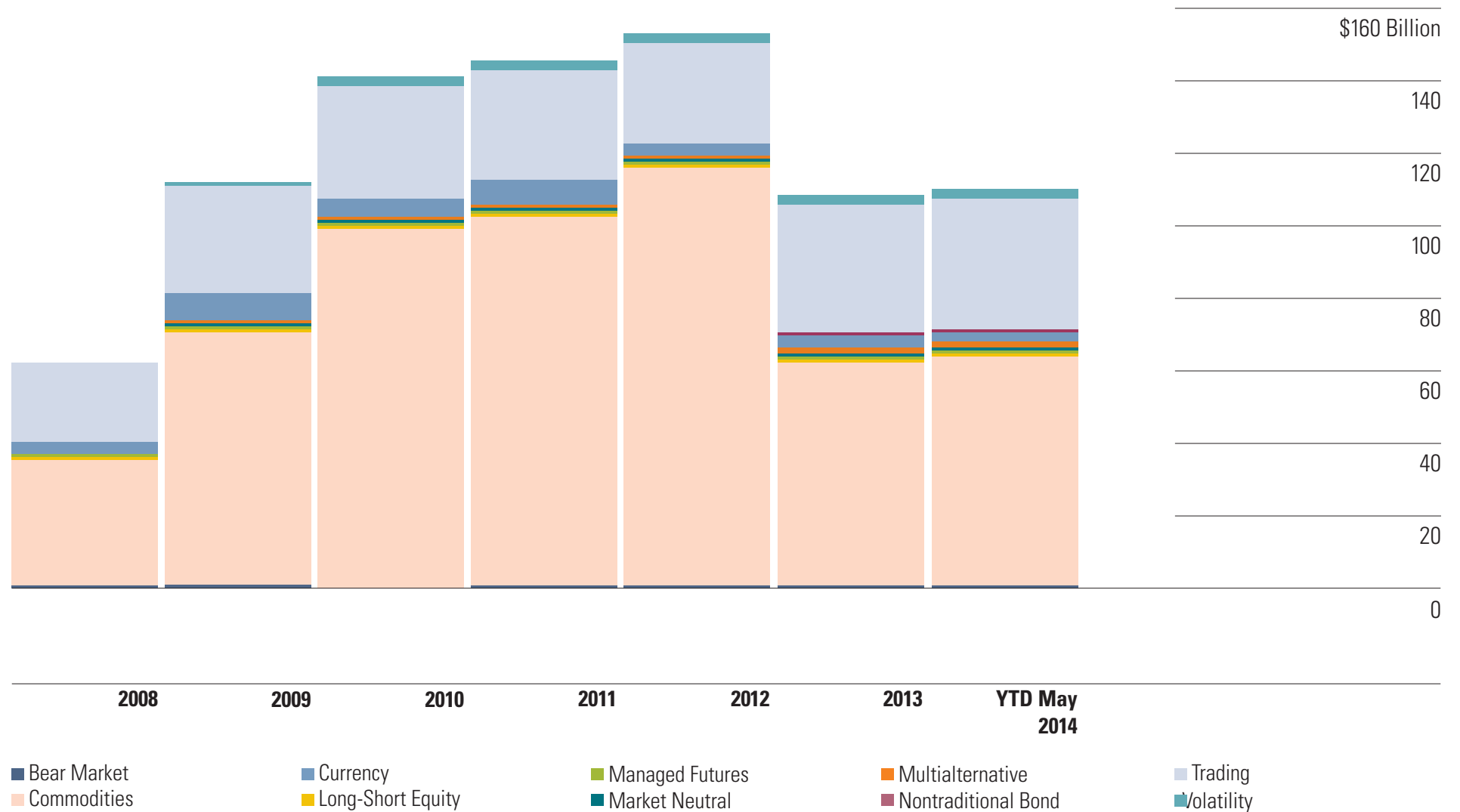
Total Net Assets in Alternative Mutual Funds



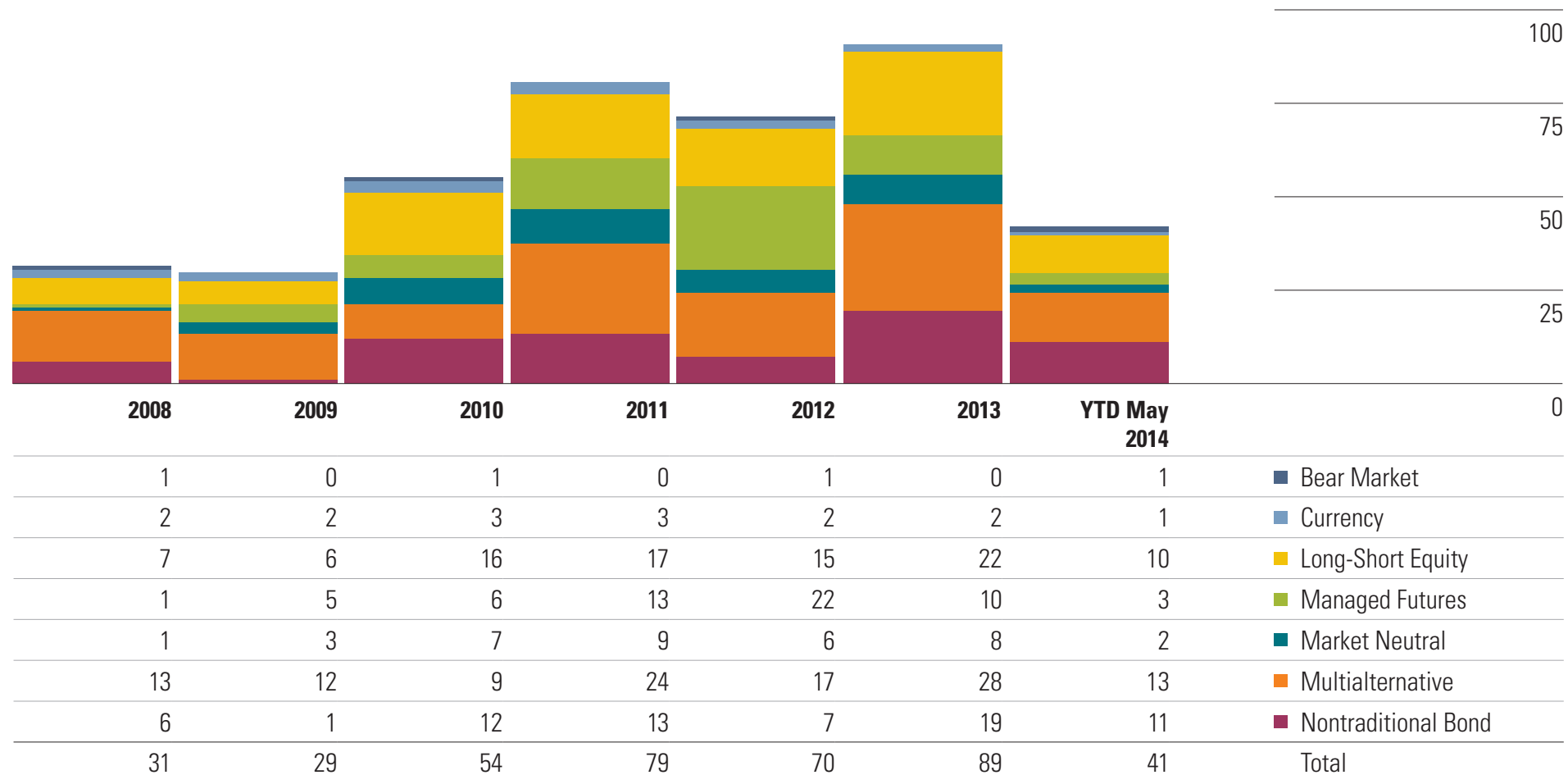
Alternative ETF Flows



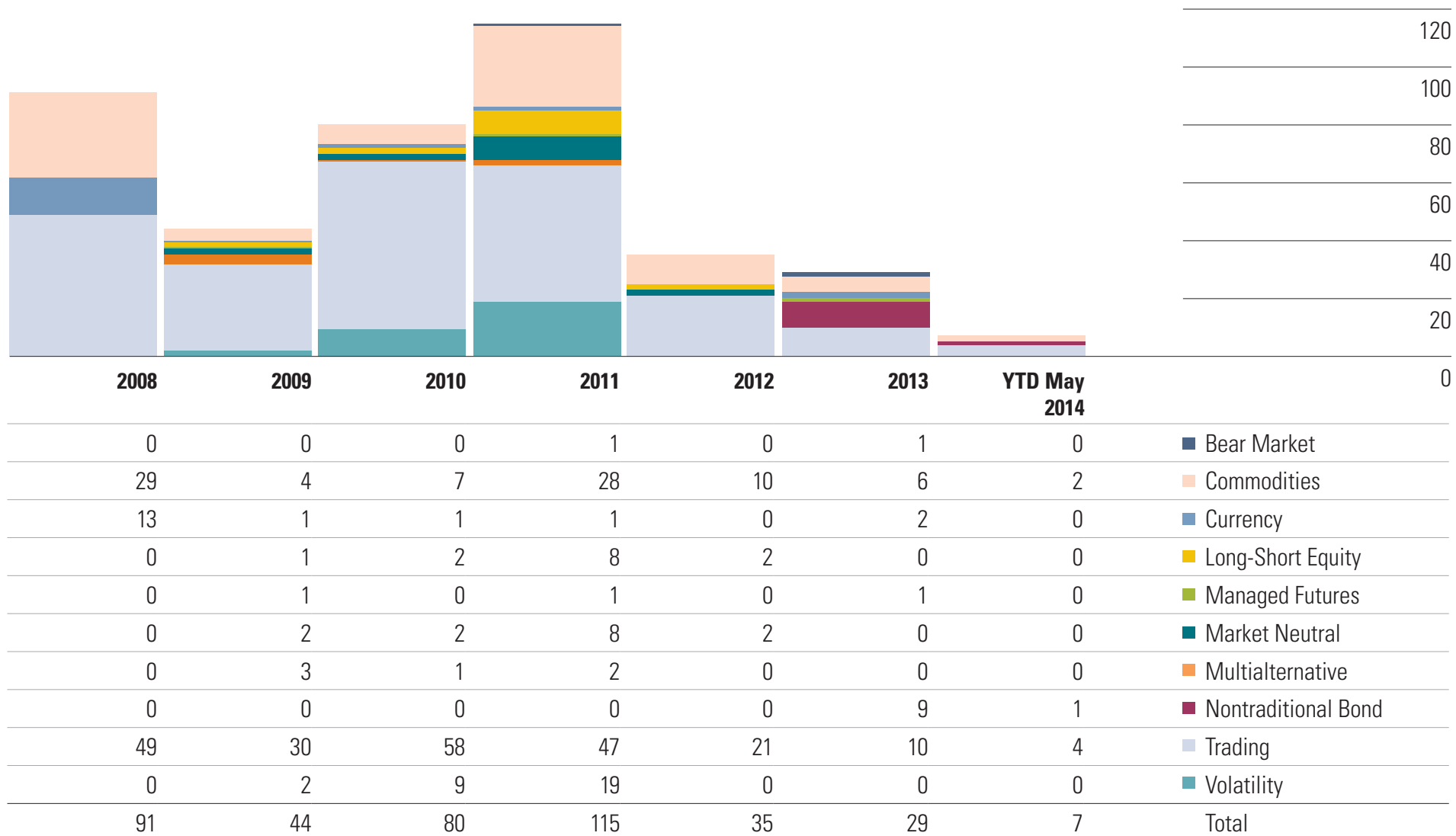
Total Net Assets in Alternative ETFs



Alternative Mutual Fund Launches by Category



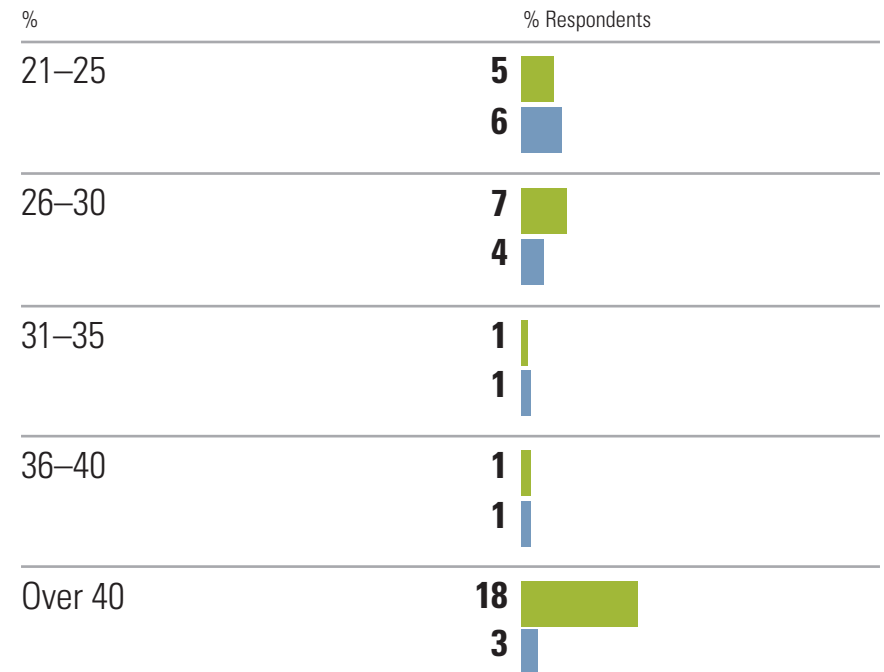
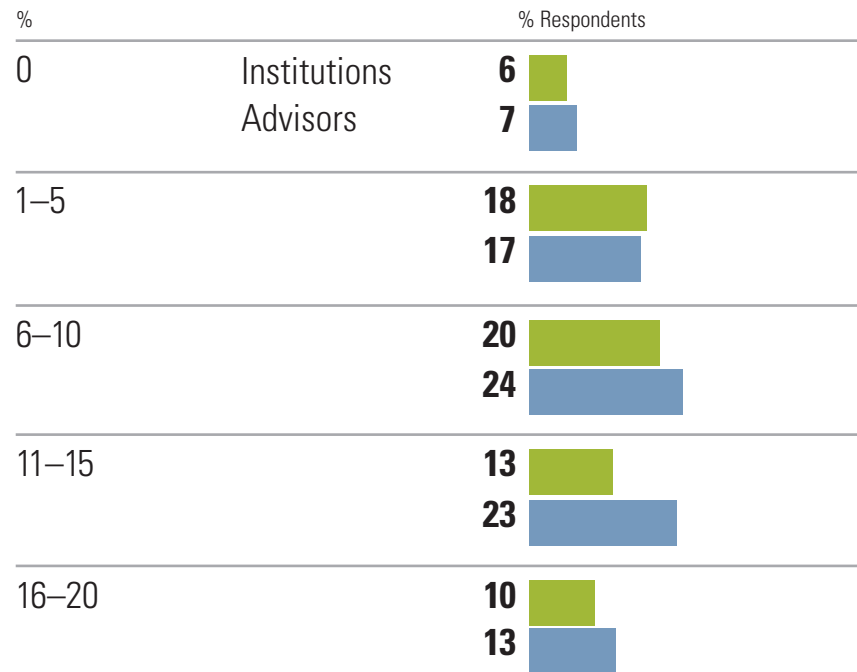
ETF Launches by Category



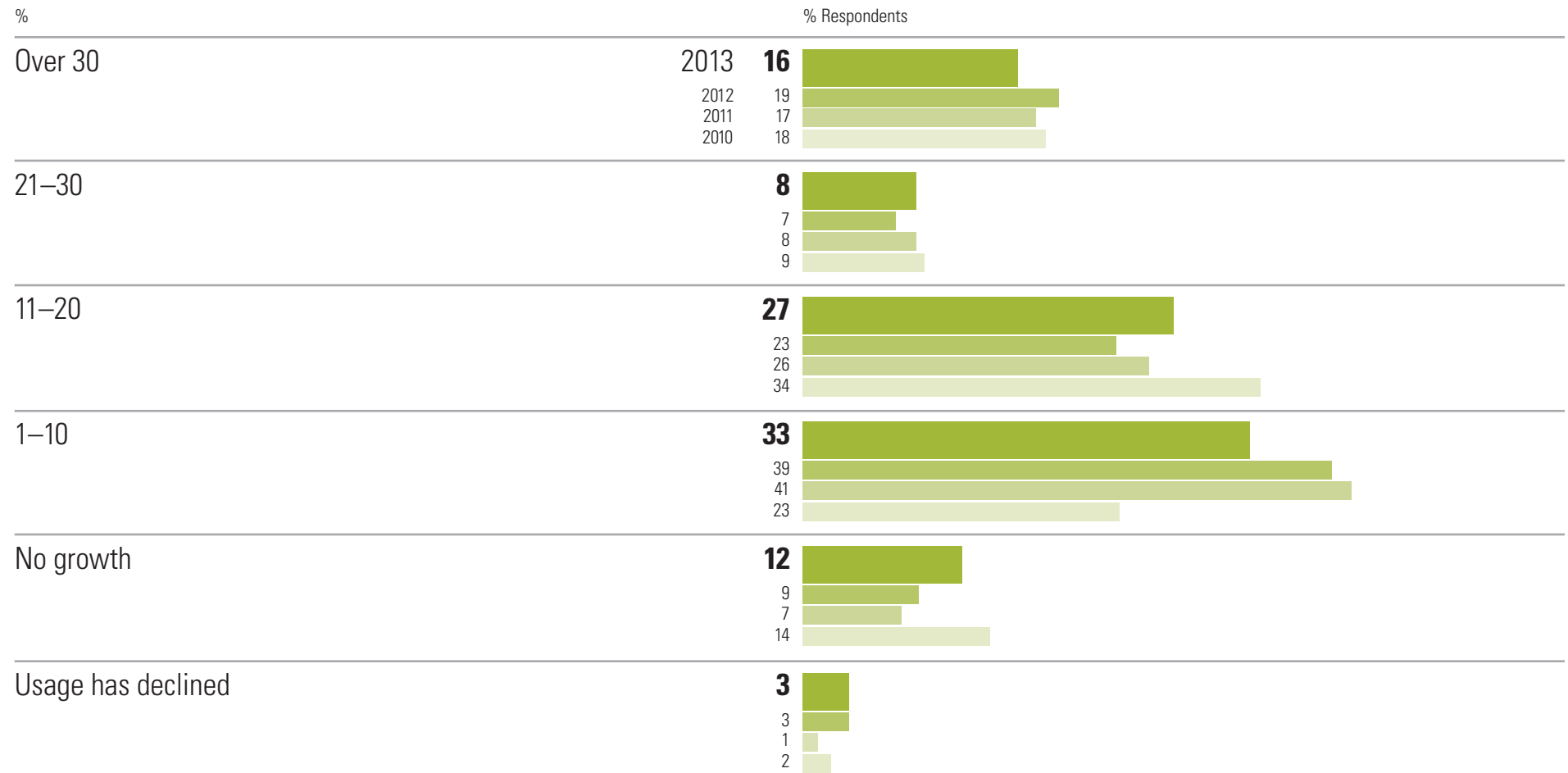
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Past and Future Alternative Investment Growth

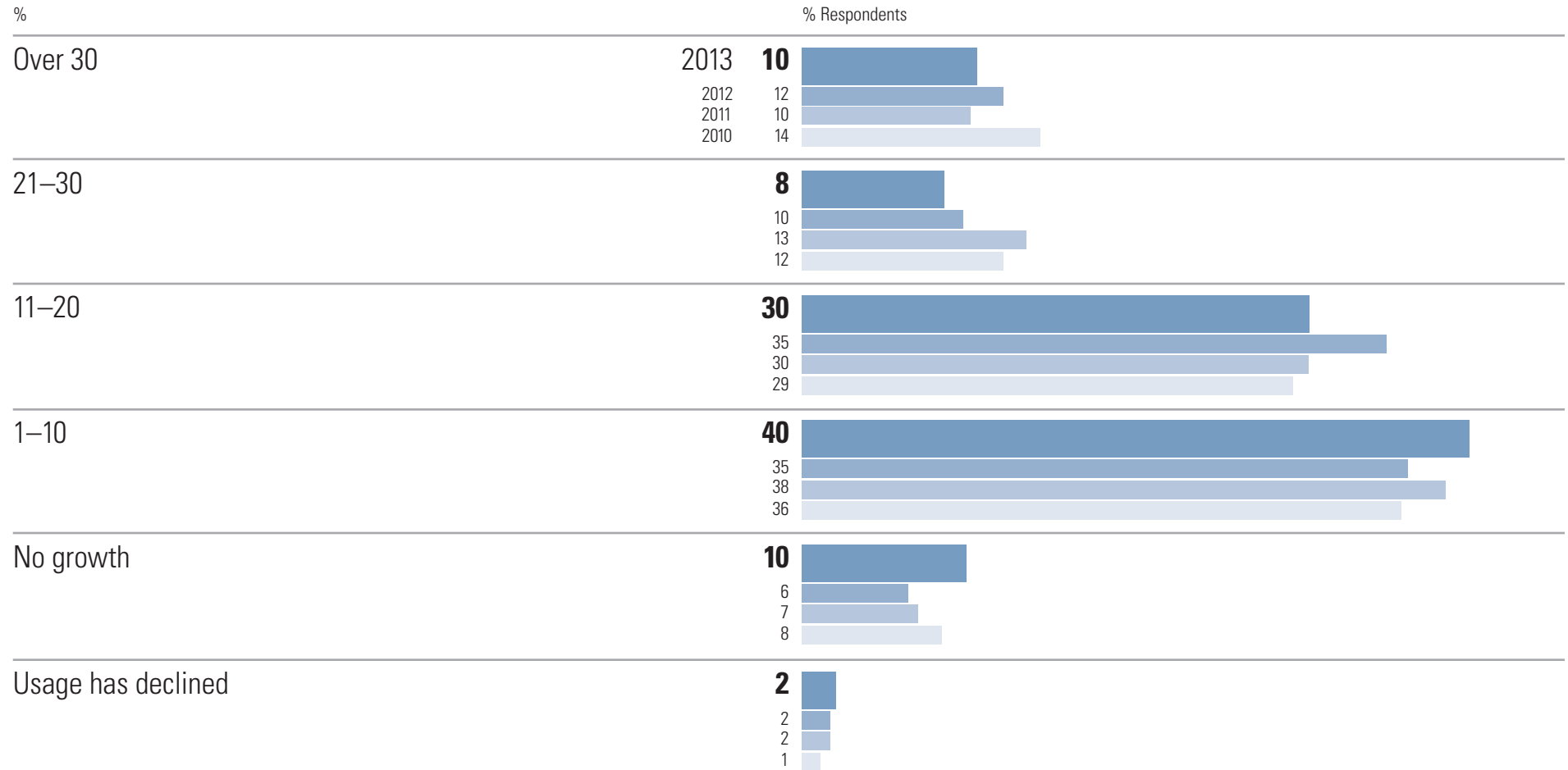
Institutions and Advisors: Allocation to Alternative Investments in 2013



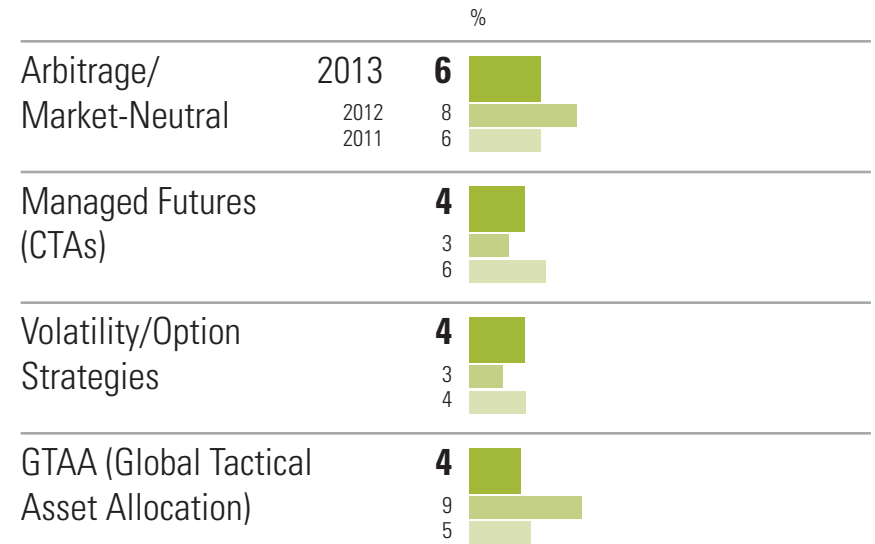
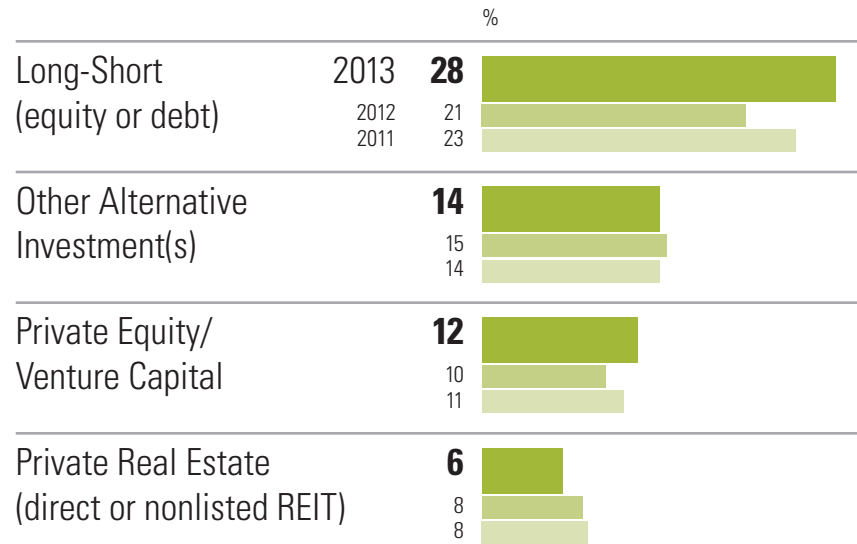
Institutions: Estimated Average Annual Growth in Alternative AUM Over Past Five Years



Advisors: Estimated Average Annual Growth in Alternative AUM Over Past Five Years

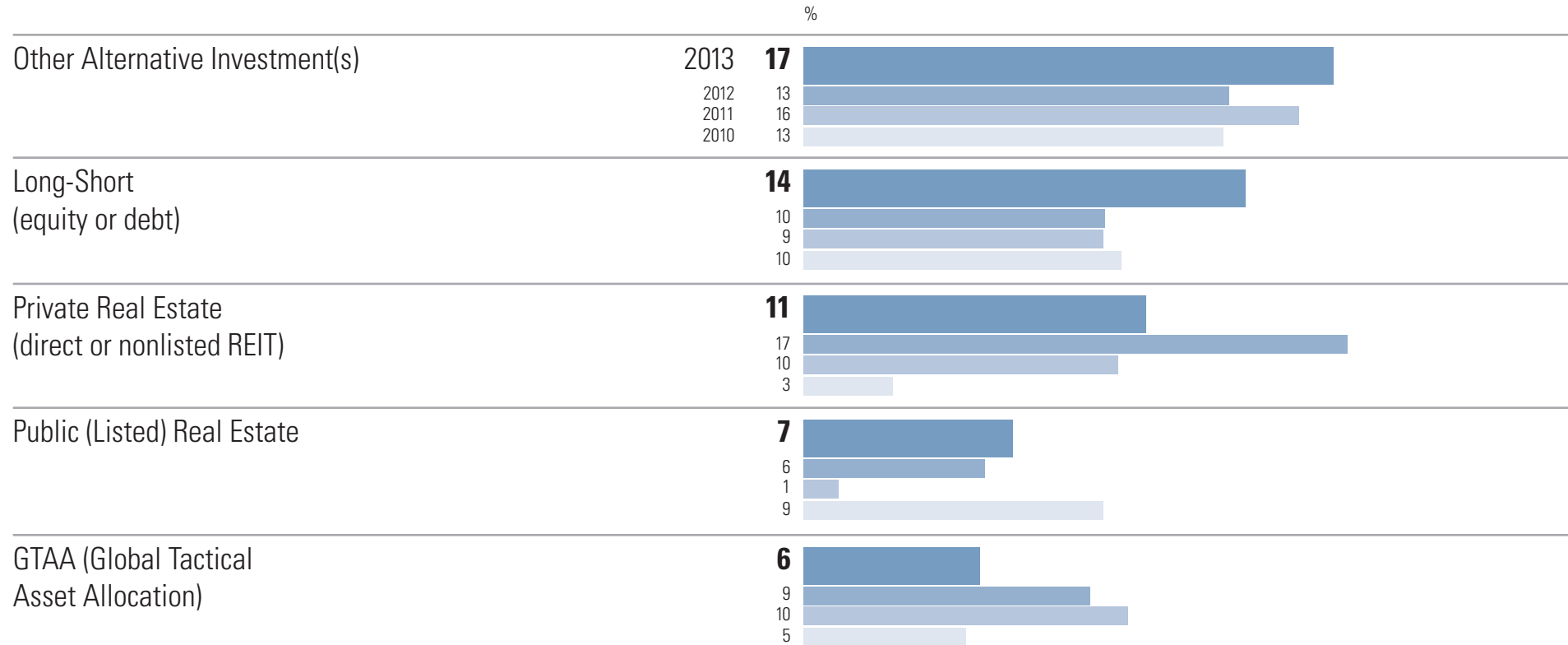


Institutions: Strategies Representing Largest Alternative Allocation Over Past Five Years



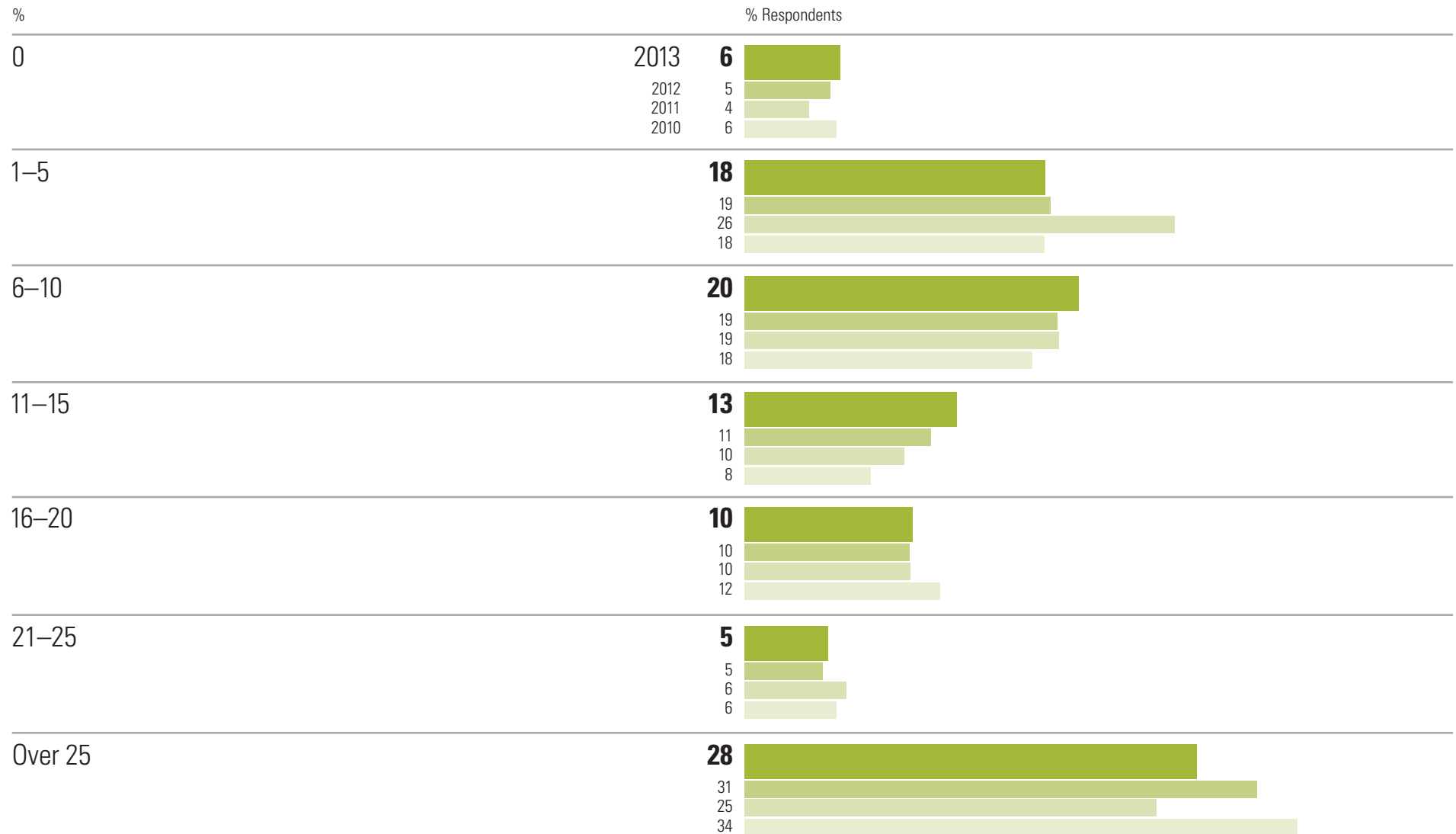
- ▶ Multistrategy
- ▶ Funds of Funds and Hedge Funds
- ▶ Absolute Return
- ▶ Global Macro Strategies
- ▶ Event-Driven
- ▶ Absolute Return
- ▶ Master Limited Partnership
- ▶ Business Development Companies
- ▶ Structured Credit

Advisors: Alternative Strategy That Provided Greatest Growth to Business Over Past Five Years

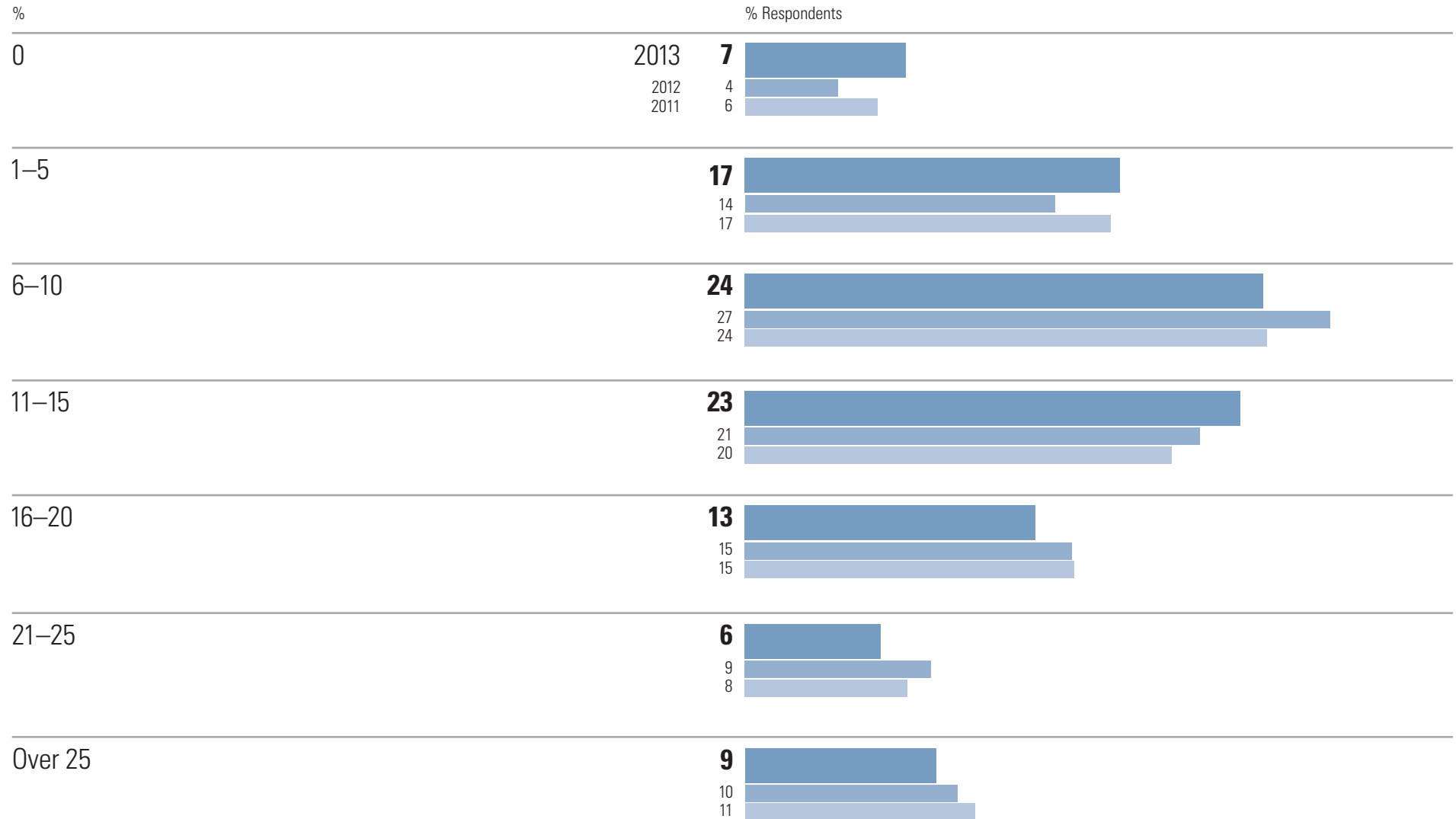


- ▶ Multistrategy
- ▶ Absolute Return
- ▶ Business Development Companies
- ▶ Funds of Funds and Hedge Funds
- ▶ Master Limited Partnerships
- ▶ Structured Credit
- ▶ Event-Driven
- ▶ Direct Participation Program
- ▶ Global Macro

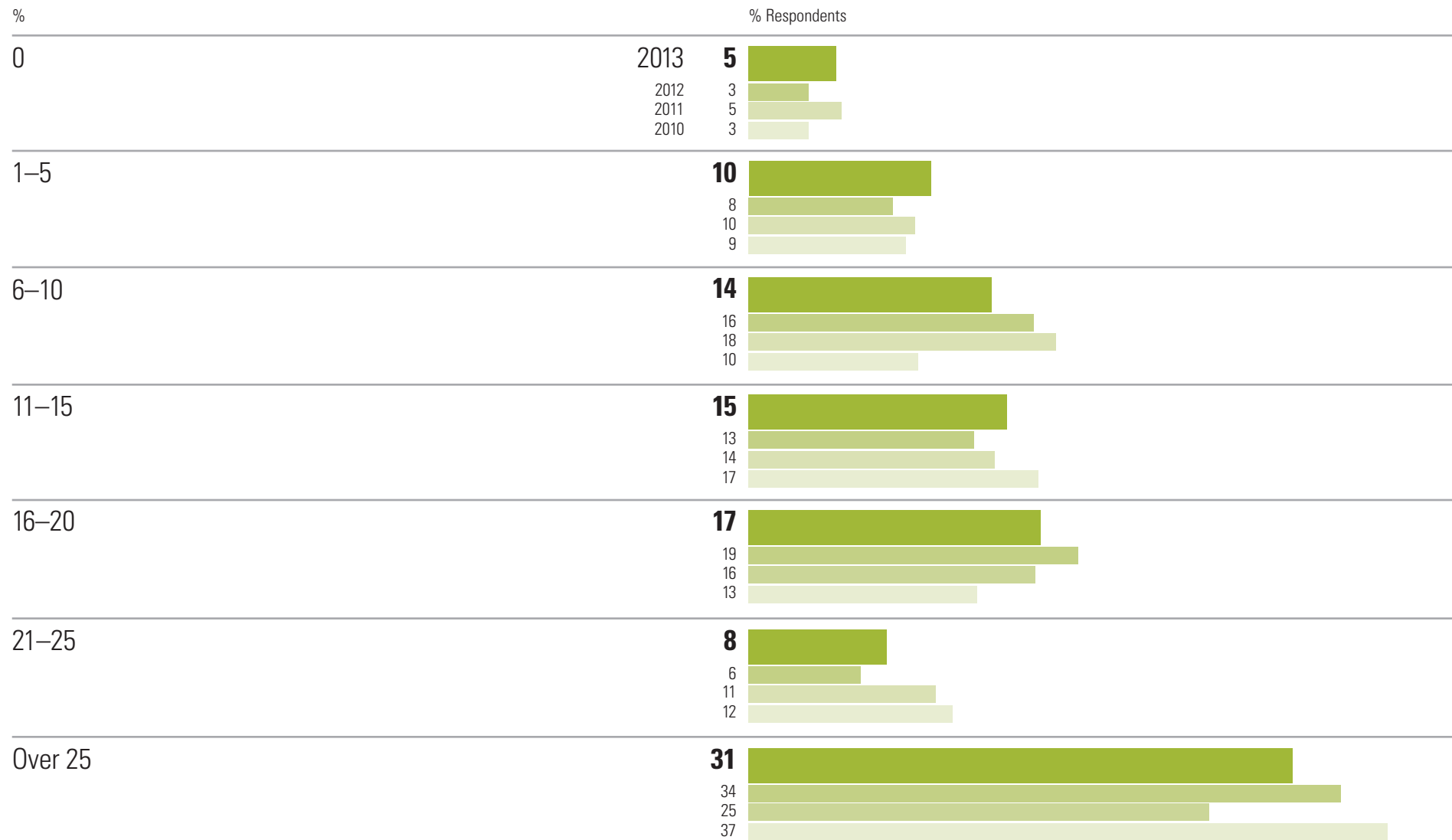
Institutions: Allocation to Alternative Investments Over Time



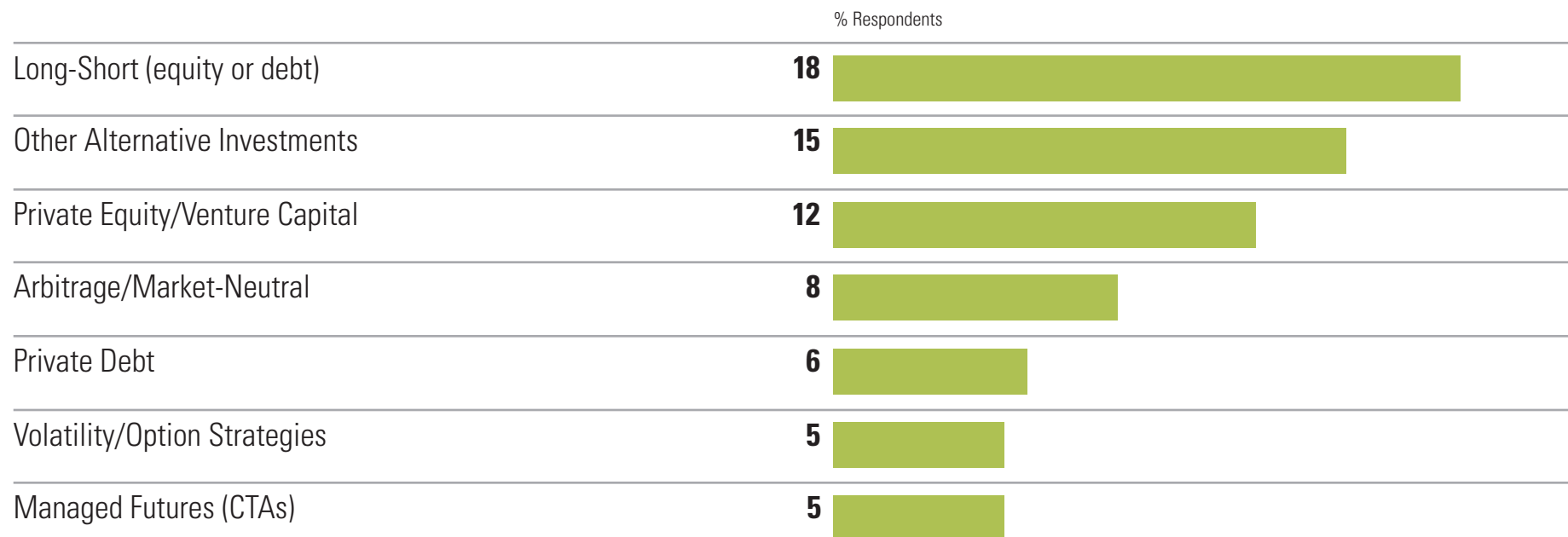
Advisors: Allocation to Alternative Investments Over Time



Institutions: Allocation to Alternatives Over the Next Five Years



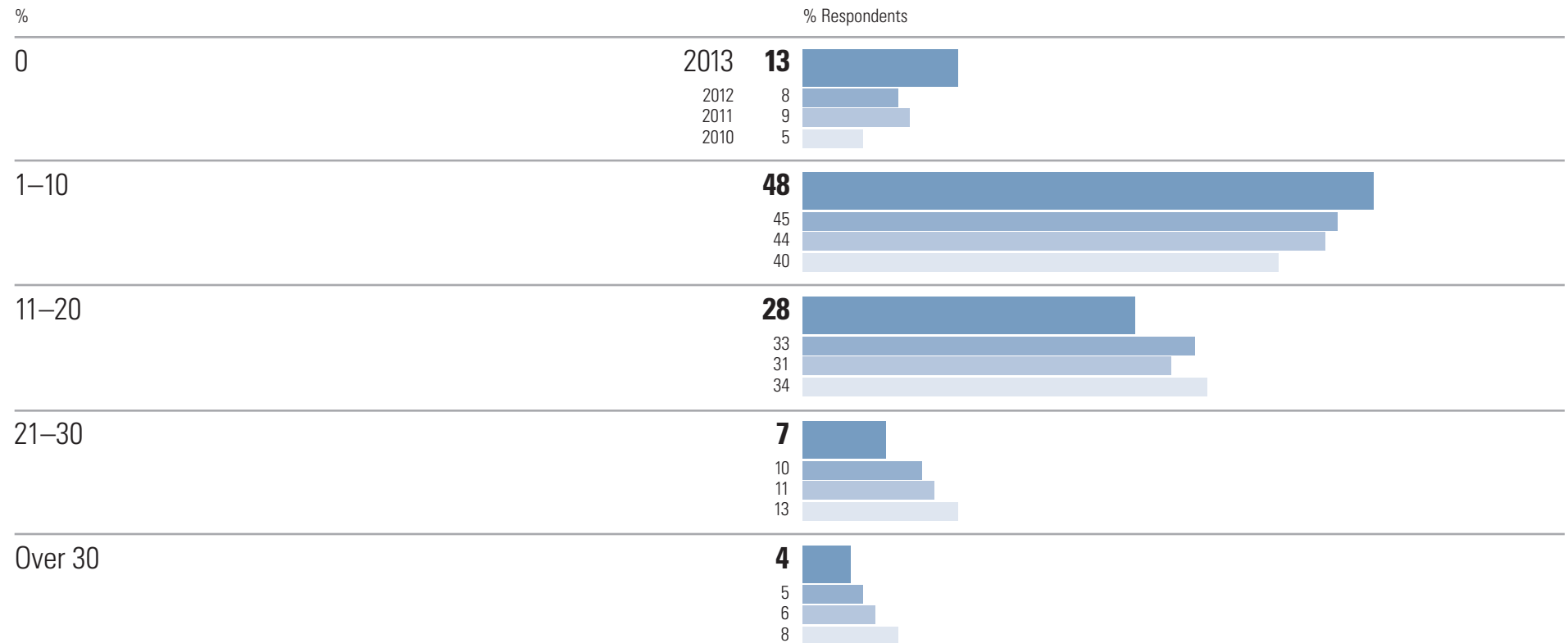
Institutions: Top Alternative Strategies for Increased Allocation



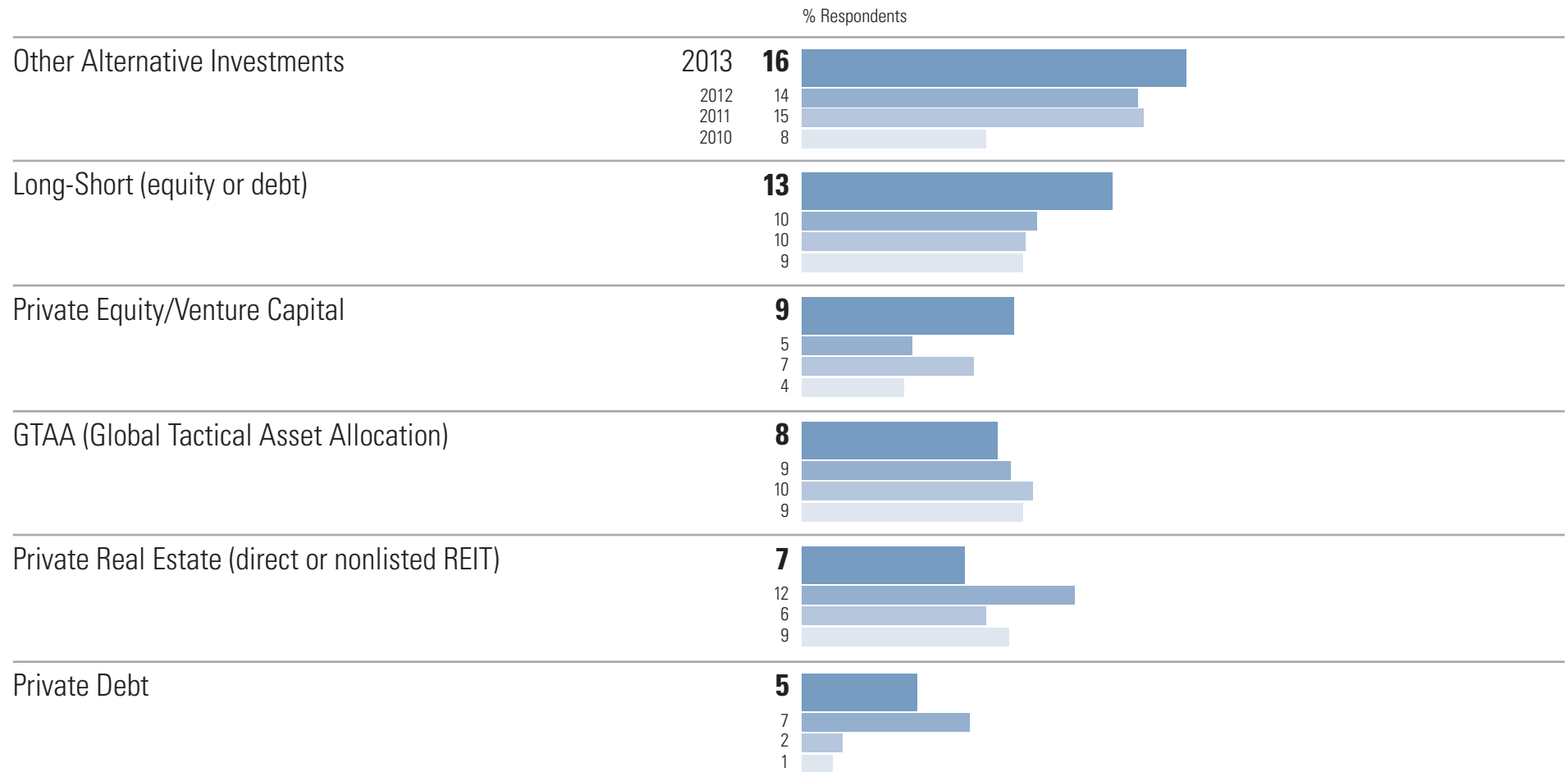
Institutions: Other Top Alternative Strategies for Increased Allocation

- ▶ Insurance-linked securities
- ▶ Multistrategy
- ▶ Liquid alternatives
- ▶ Global macro
- ▶ Hedge funds

Advisors: Anticipated Annual Growth in Alternative AUM



Advisors: Top Alternative Strategies for Growth of Business



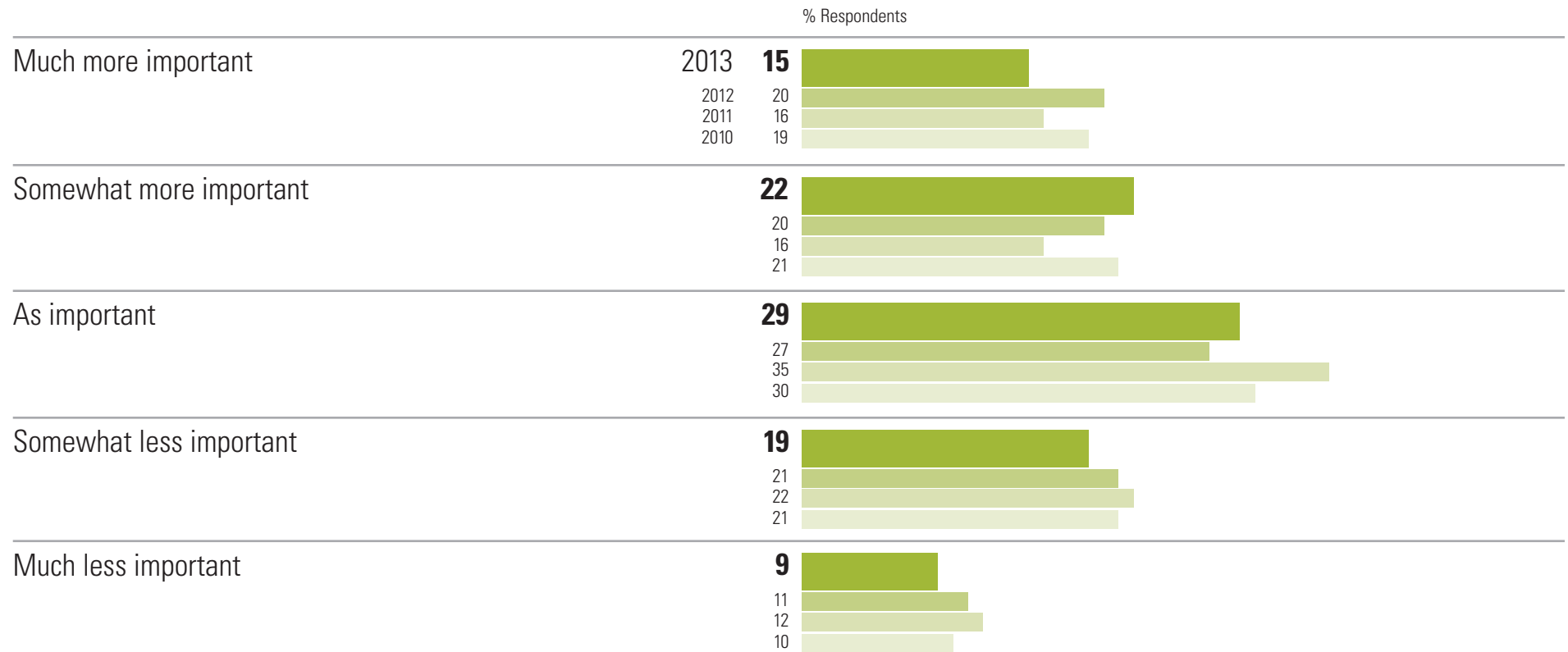
Advisors: Other Top Alternative Strategies for Increased Allocation

- ▶ Business Development Corporations
- ▶ Absolute Return
- ▶ Multistrategy
- ▶ Global Macro

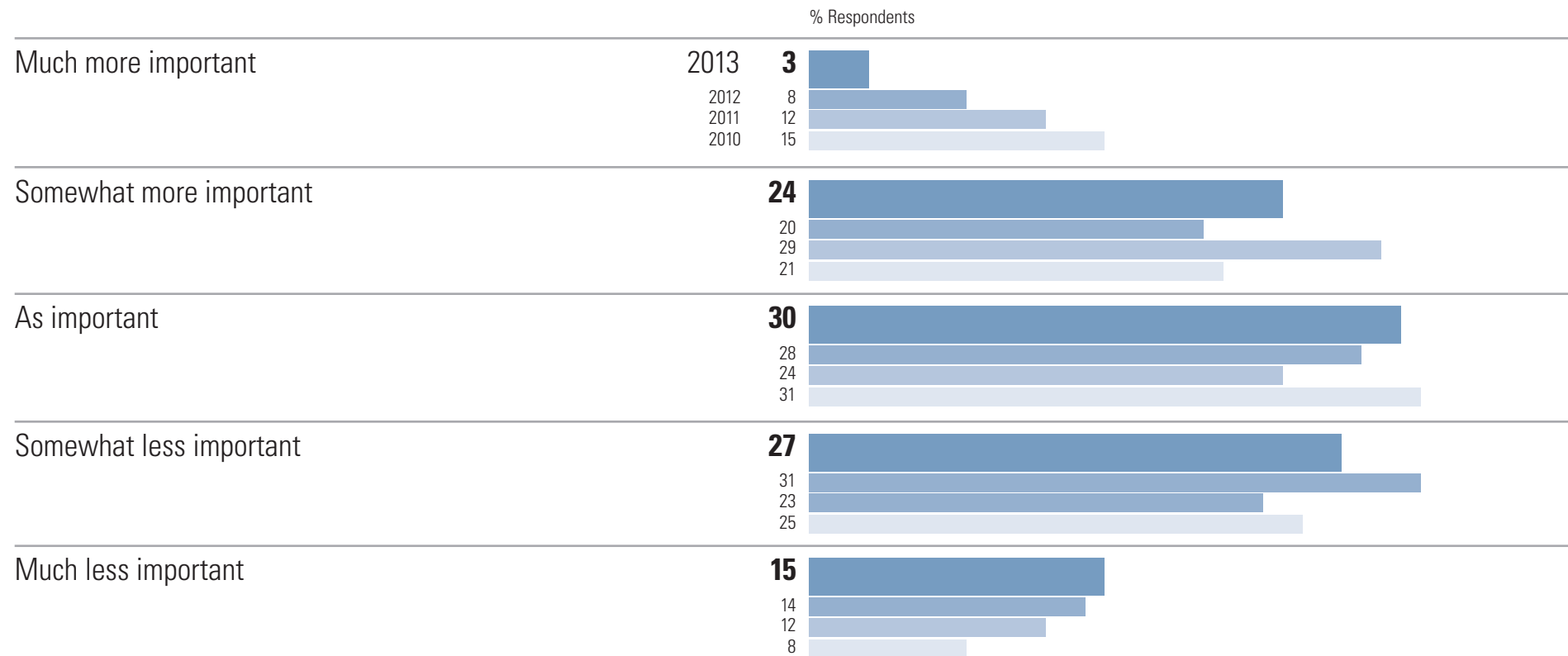
- ▶ 60% of advisors allocate between 6% and 20% to alternatives, while a large portion of institutions (18%) allocate more than 40% to alternatives.
- ▶ Long-short strategies have continued to dominate institutional and advisor alternative allocations over the past five years and gained in importance, in 2013, compared with prior years.
- ▶ The survey shows a softening of “extreme” users of alternatives, as the number of advisors and institutions who allocate more than 30% to alternatives has declined over the years.

Alternative Investment Drivers and Deterrents

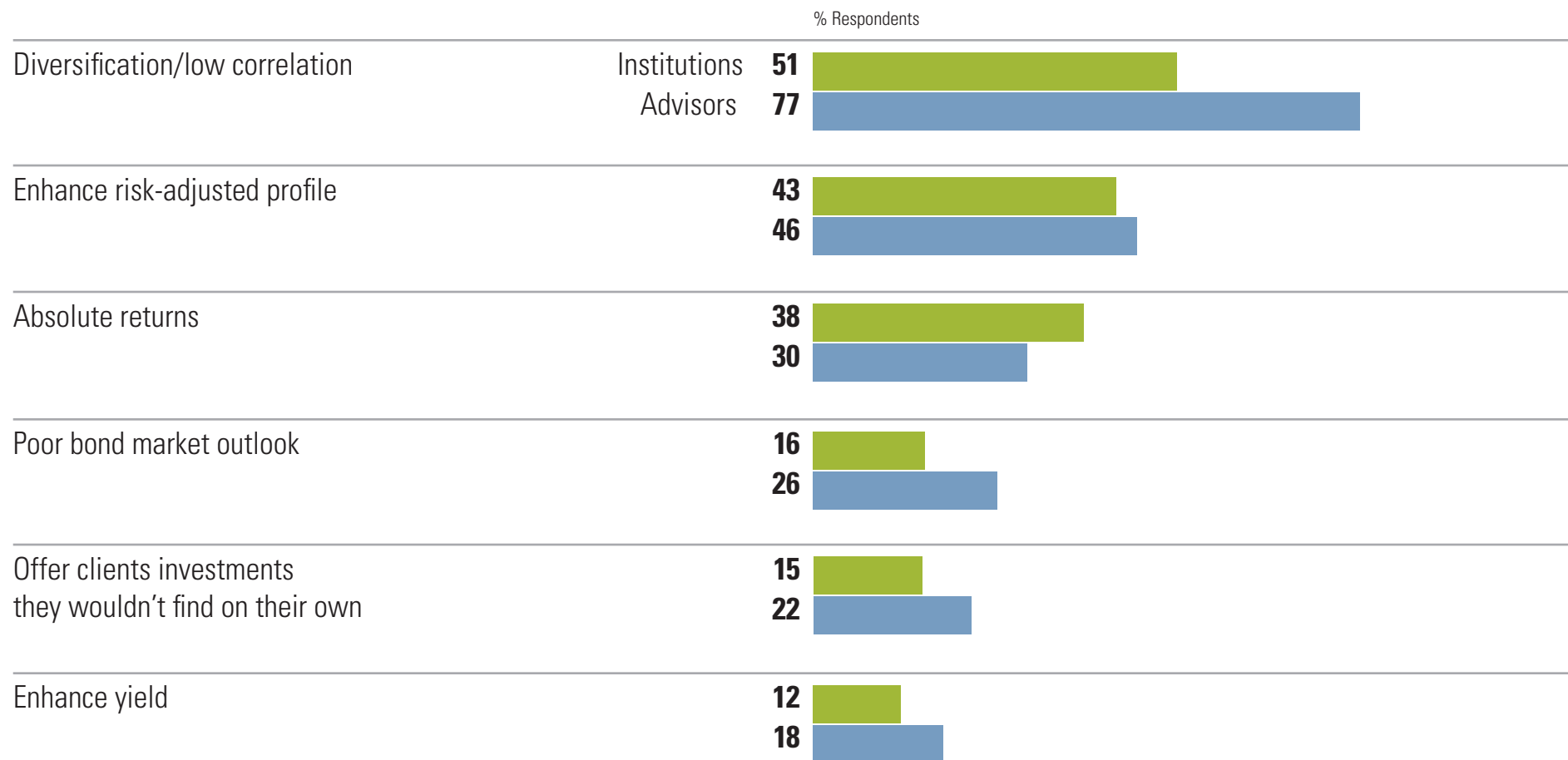
Institutions: Importance of Alternative Investments Relative to Traditional Investments



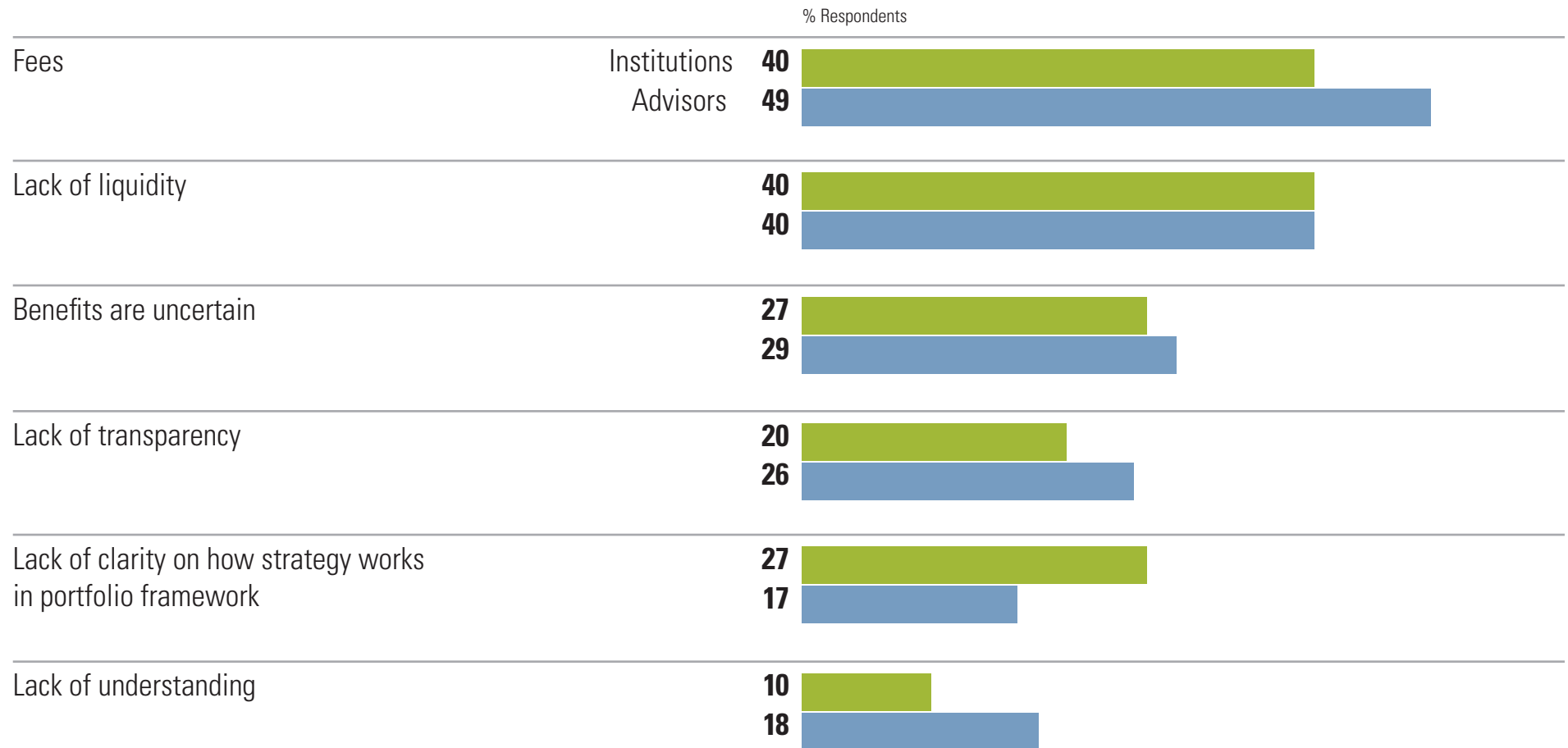
Advisors: Importance of Alternative Investments Relative to Traditional Investments



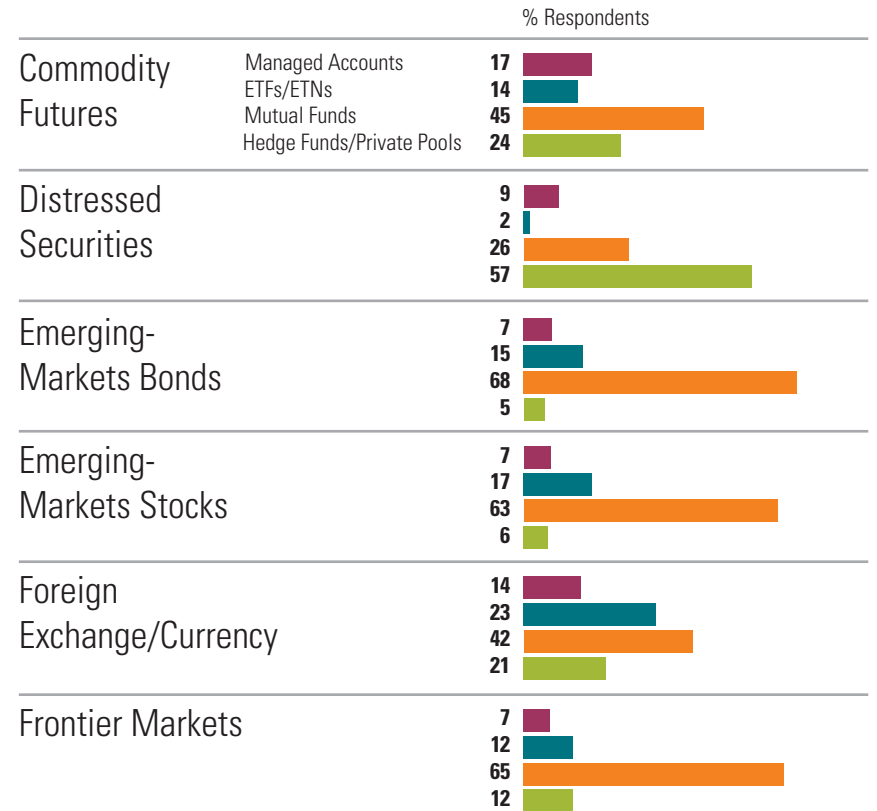
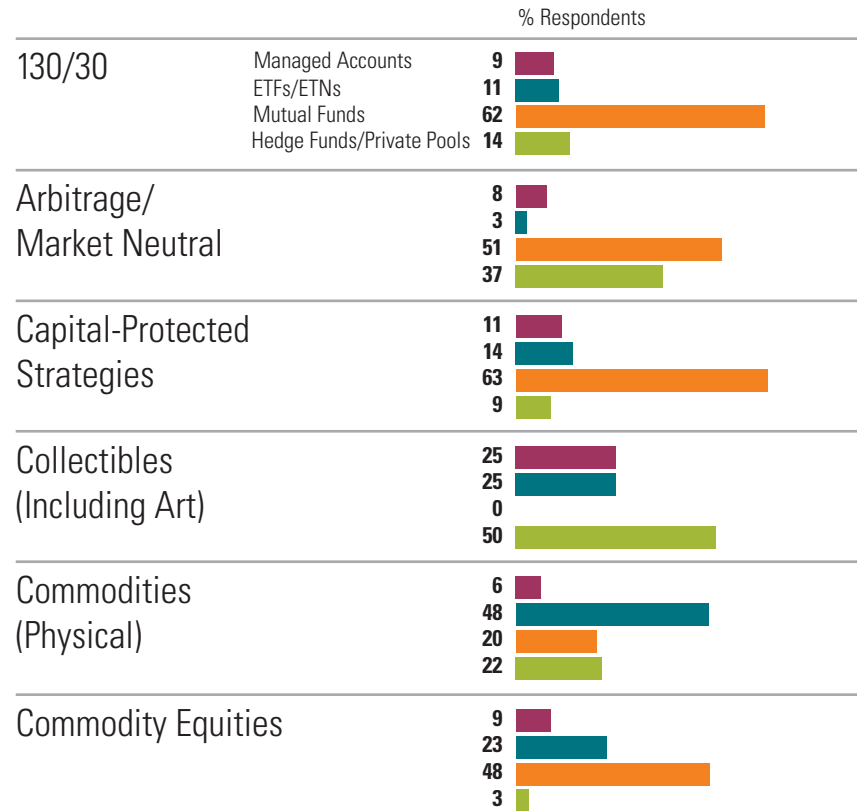
Institutions and Advisors: Top Drivers of Investments in Alternatives



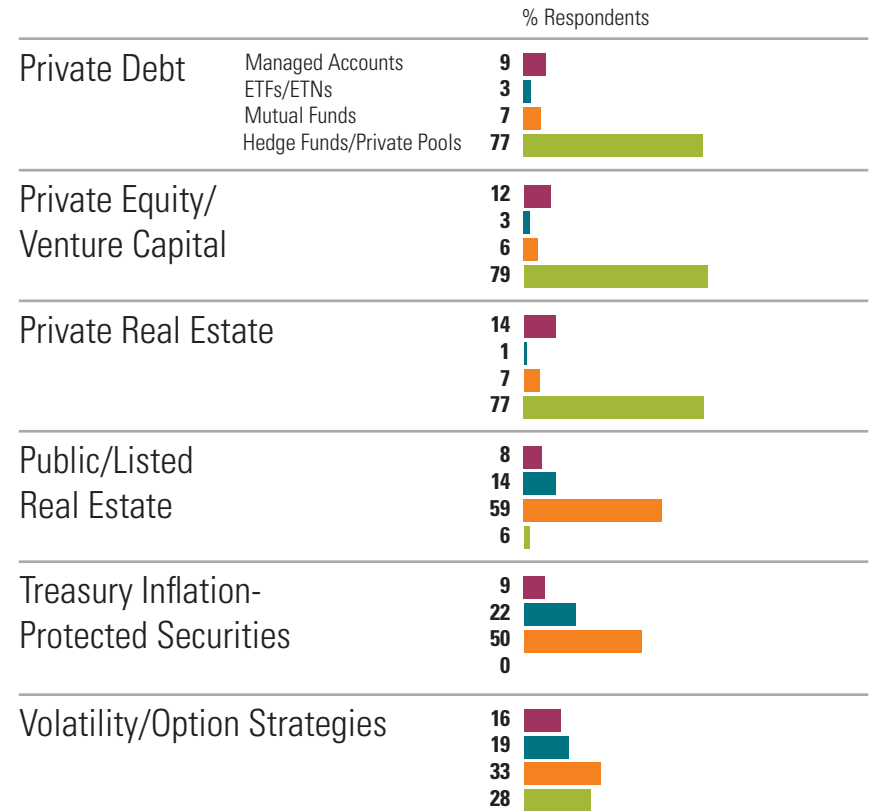
Institutions and Advisors: Top Reasons to Hesitate Investing in Alternatives



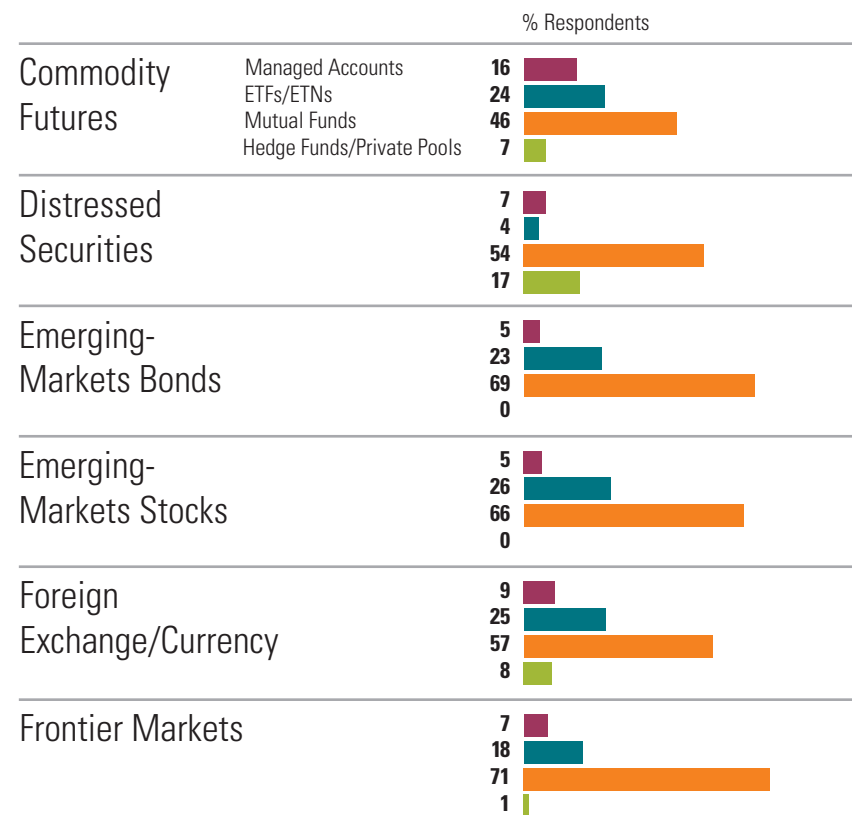
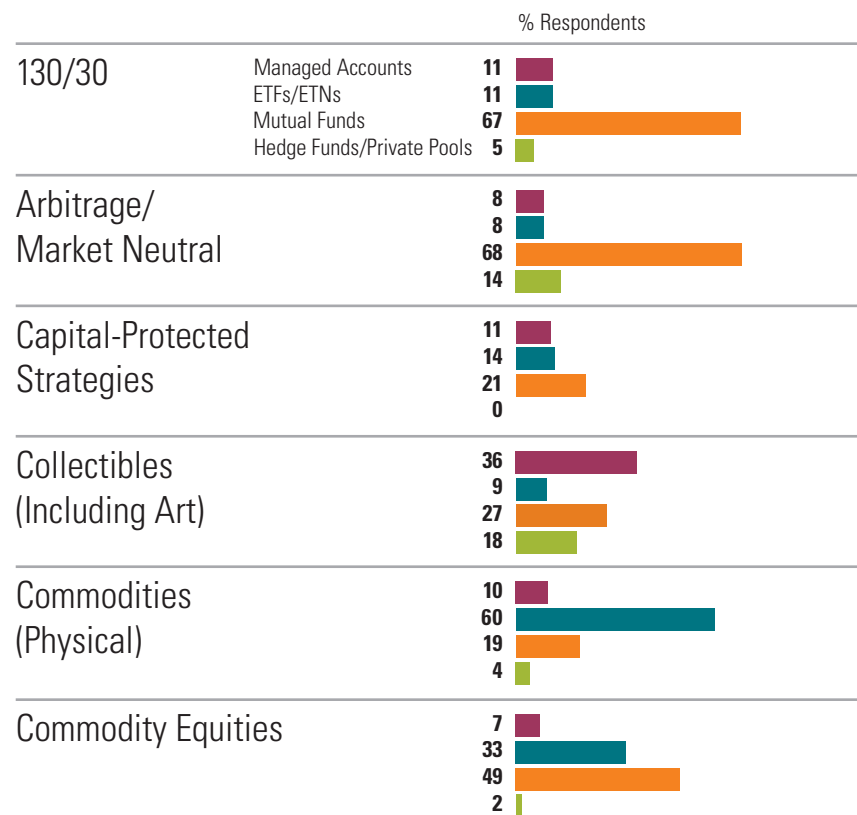
Institutions: Investment Vehicles Used to Gain Access to Alternative Strategies



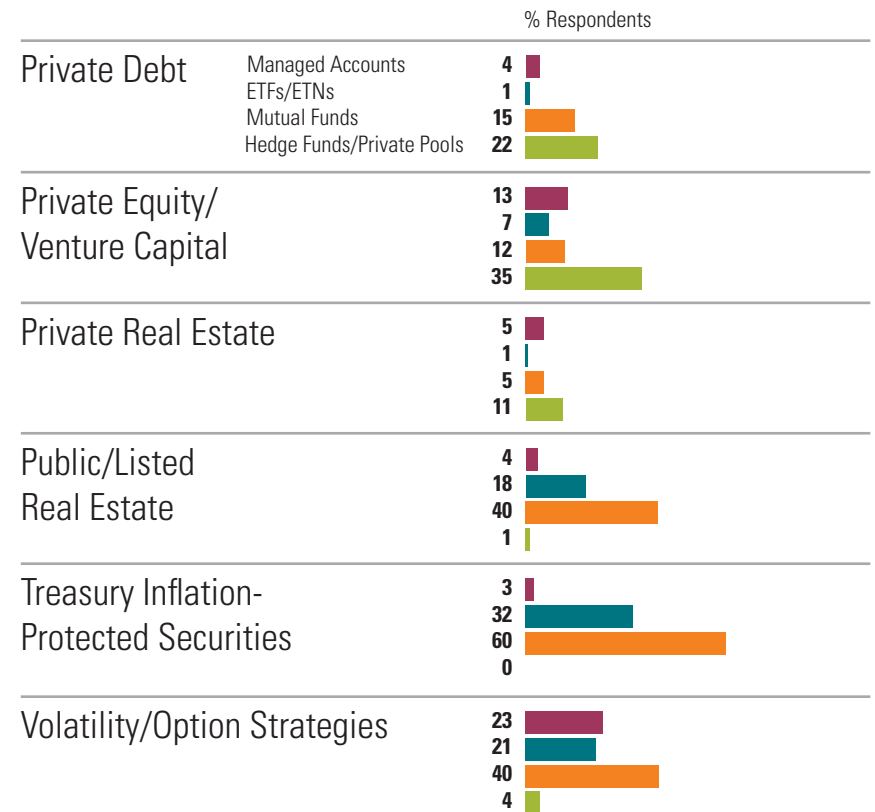
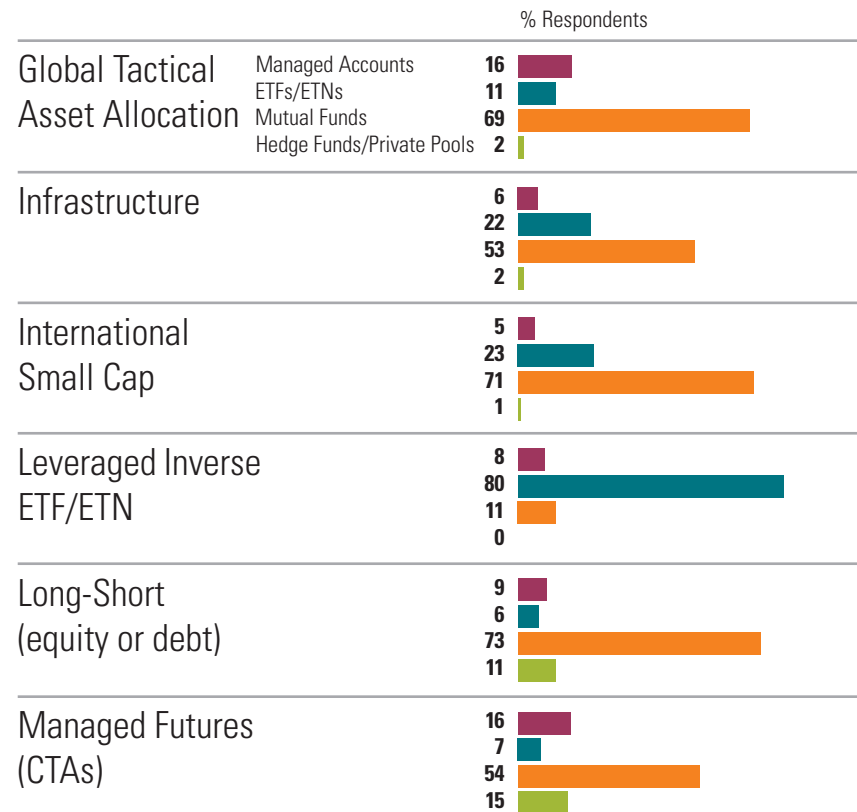
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Advisors: Investment Vehicles Used to Access Alternative Strategies



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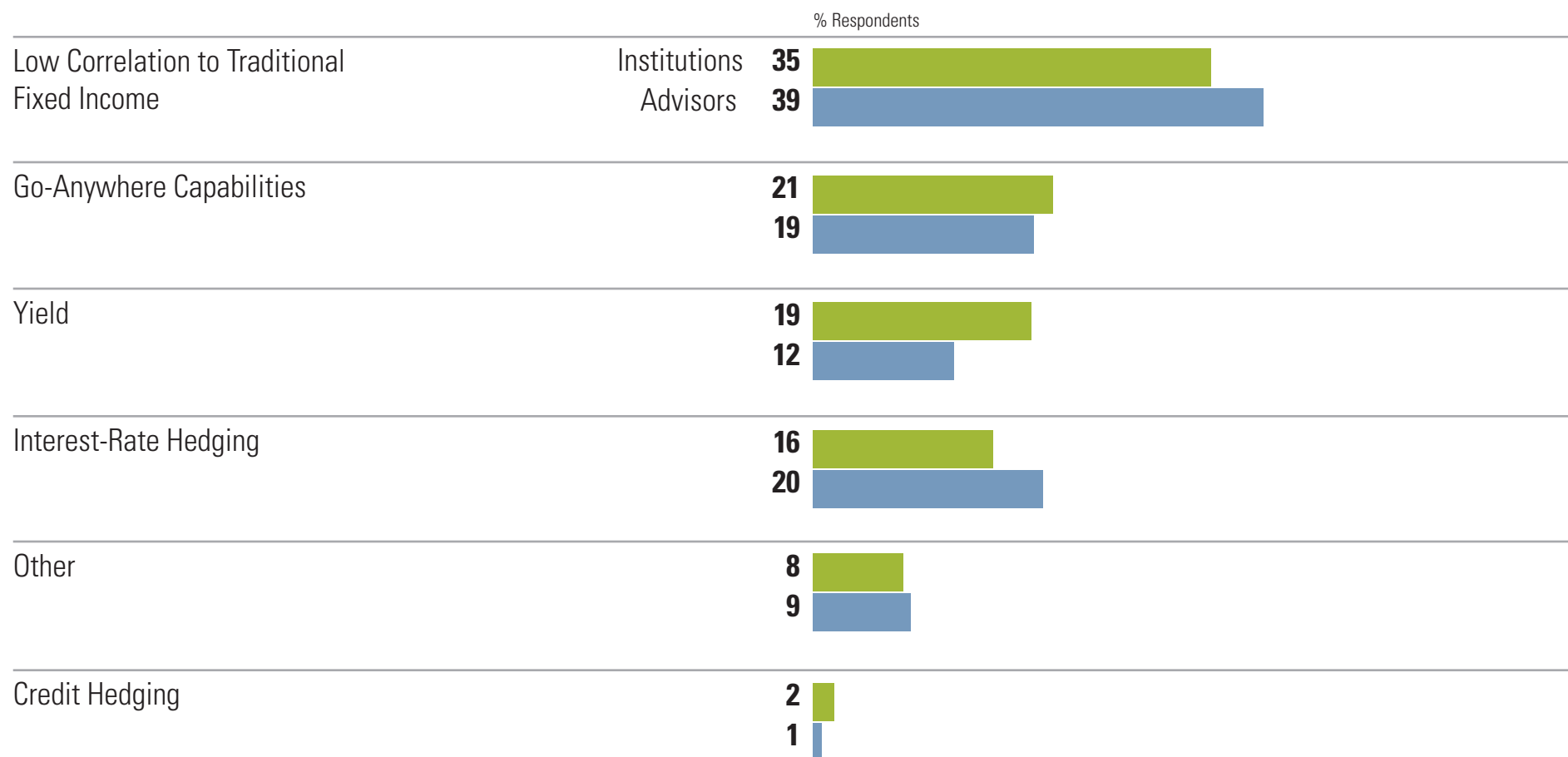
- ▶ Advisors no longer consider alternatives to be “much more important” compared with traditional investments, as alternatives have increasingly gained a core foothold in portfolios.
- ▶ Both groups still consider diversification/low correlation to be a primary benefit of alternatives.
- ▶ Poor bond market outlook has been gaining traction as a rationale among advisors and institutions, as investors are seeking cover from a possible interest-rate increase.
- ▶ Many advisors consider mutual funds to be the primary vehicle to gain access to alternatives, while institutions also heavily use mutual funds for many alternative strategies.

- ▶ Alternative Fixed Income
- ▶ Manager Due-Diligence Process
- ▶ Hedge Fund Advertising
- ▶ Alternative Benchmarks

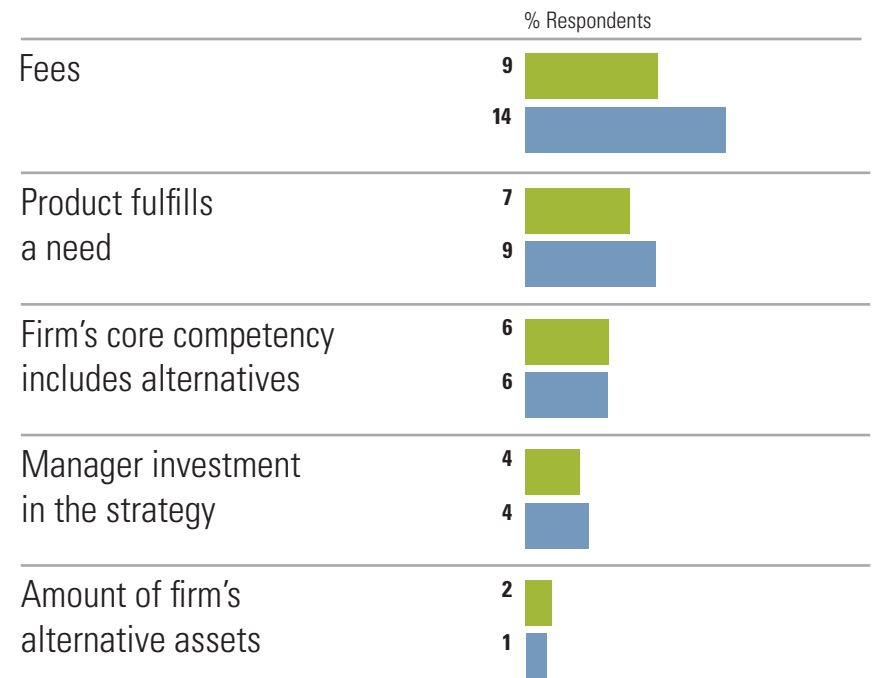
On a scale of 1 to 10, how interested are you, or by extension your clients, in alternative fixed-income substitutes, such as funds that can hedge credit risks and/or protect against rising interest rates? 10 indicates that these funds are pivotal, while 1 represents no interest.

Institutions on average voted 6.5, while advisors averaged 6.4

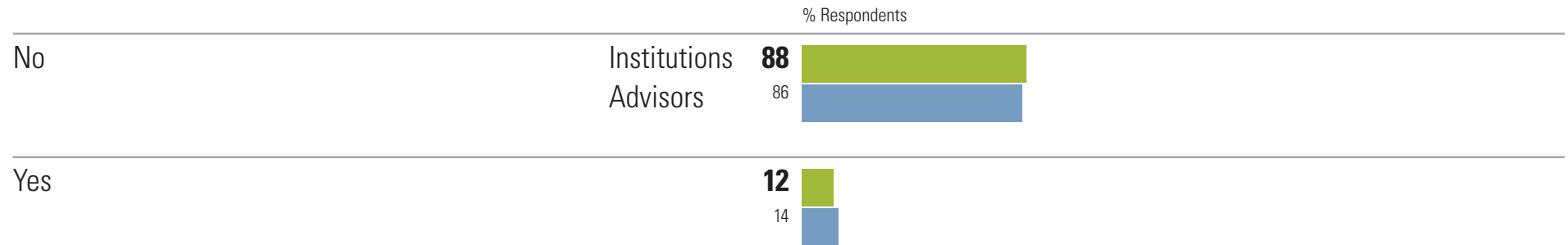
What do you value most in an alternative fixed-income product?



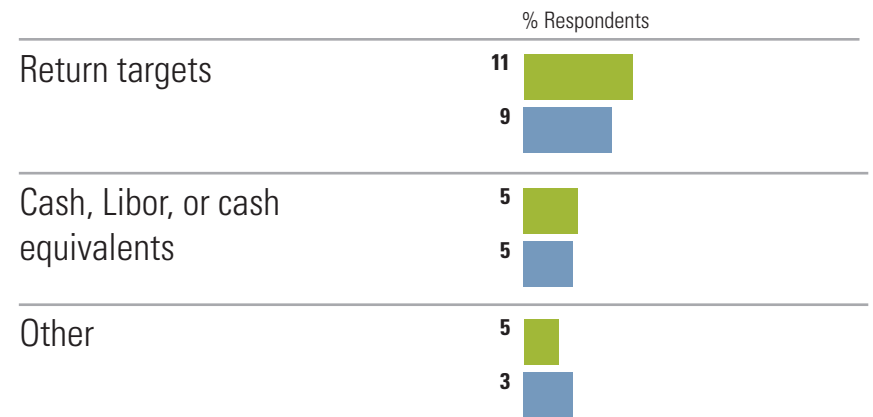
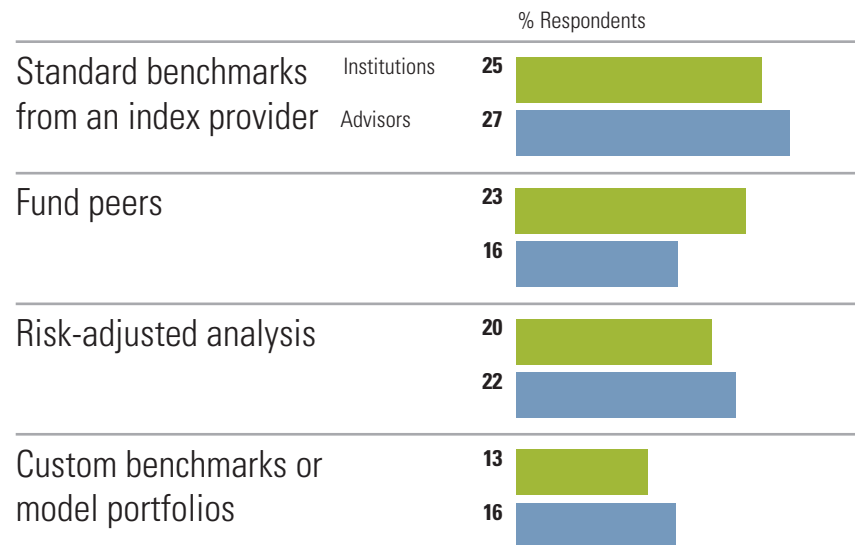
When selecting alternative products, which factors are more pertinent to your decision-making process (pick three)?



Will lifting the ban on hedge fund advertising affect your business?

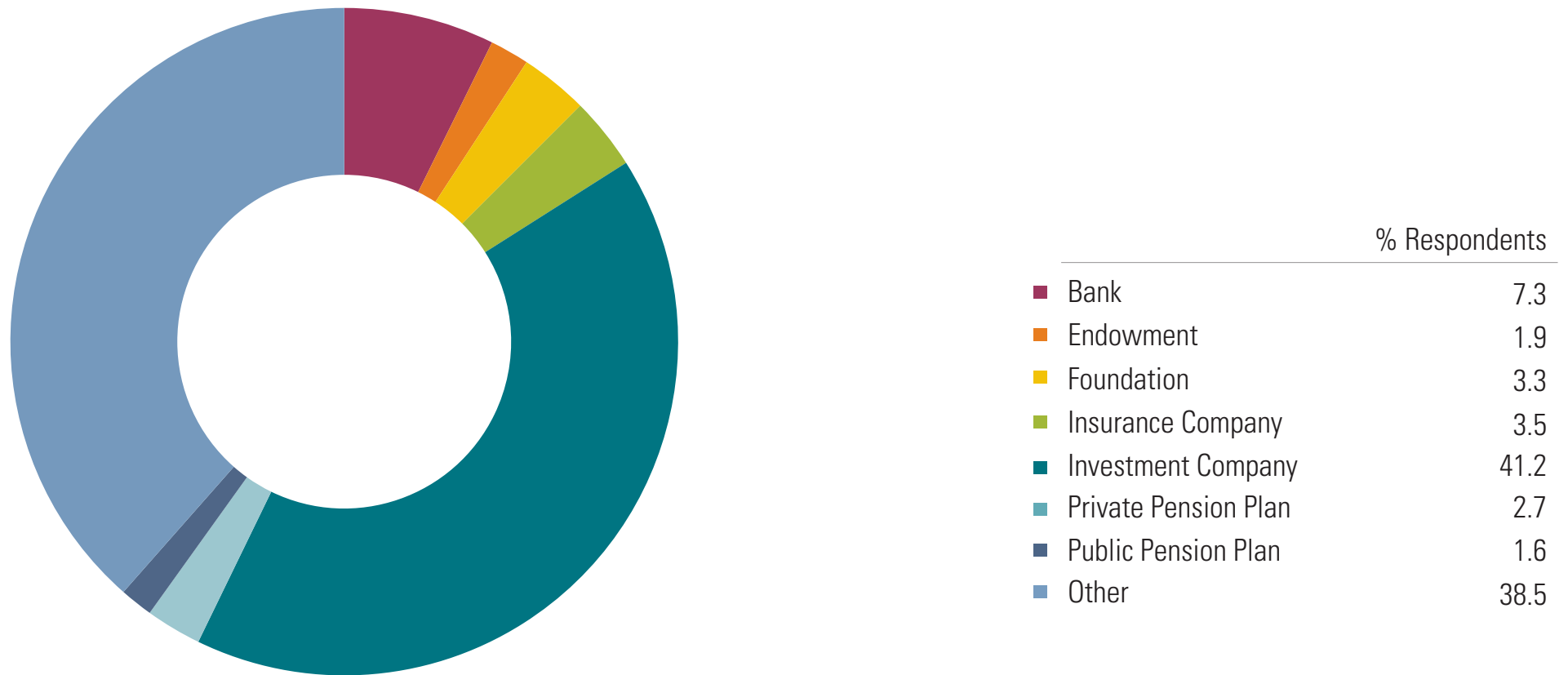


What types of benchmarks does your firm use to compare its alternative investments?

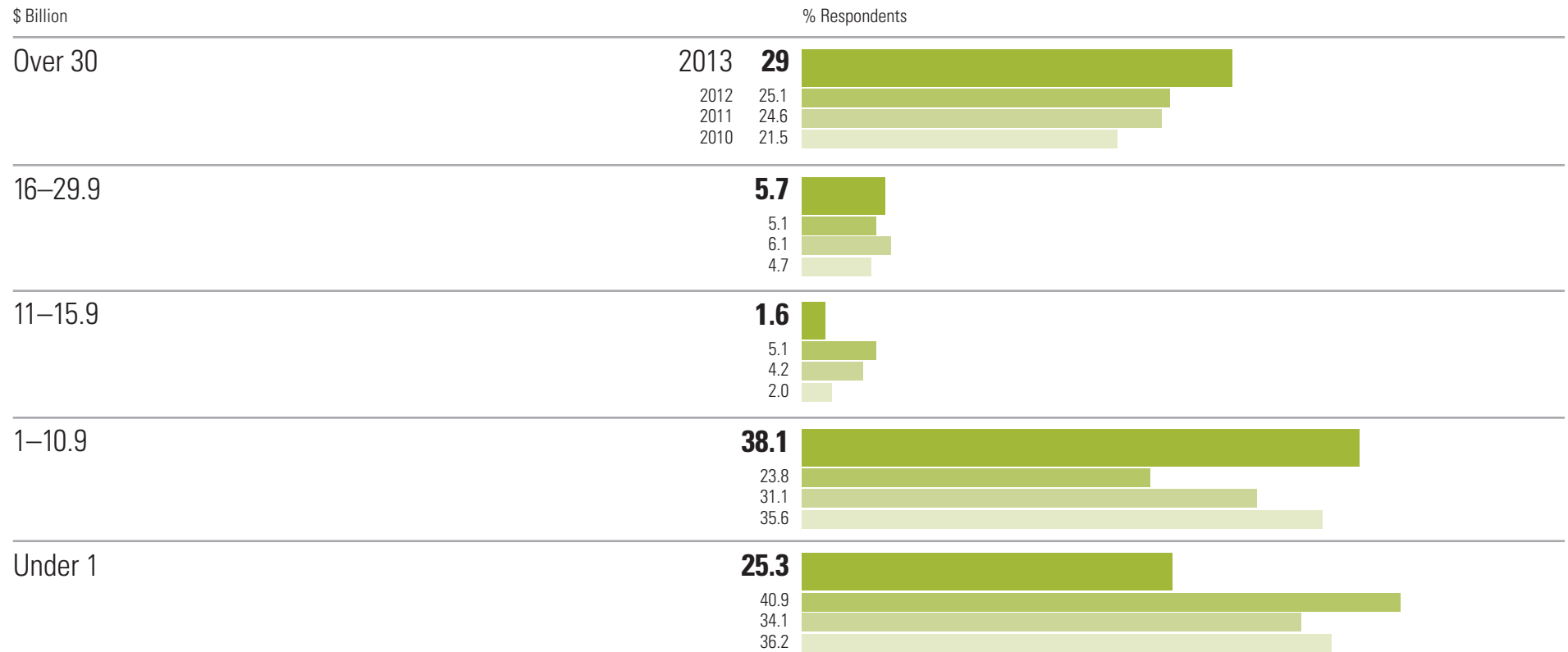


2013–2014 Survey Participation

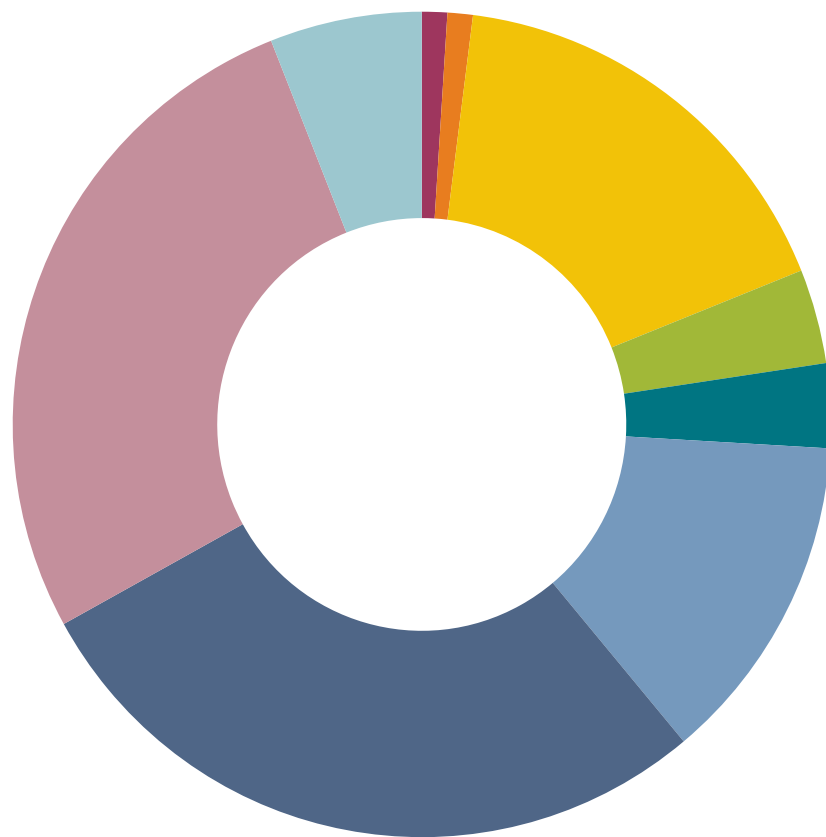
Institutions' 2013–2014 Survey Participation: 372 Responses



Institutions' AUM Compared With Previous Years

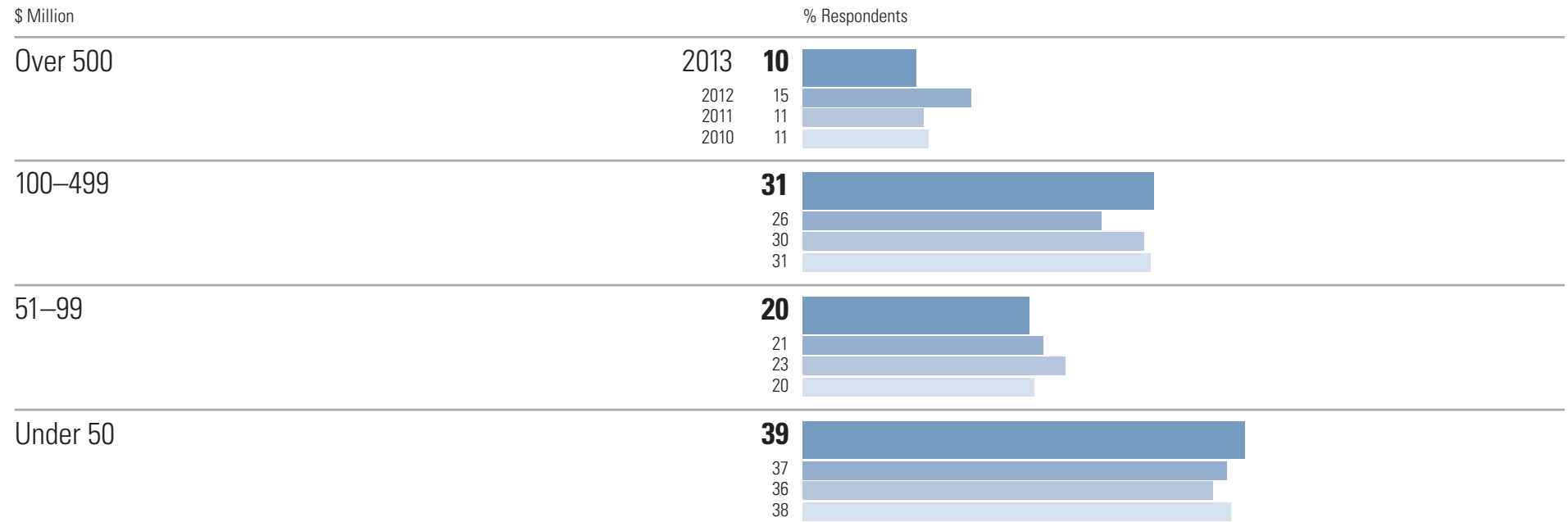


Advisors 2013–2014 Survey Participation: 301 Responses

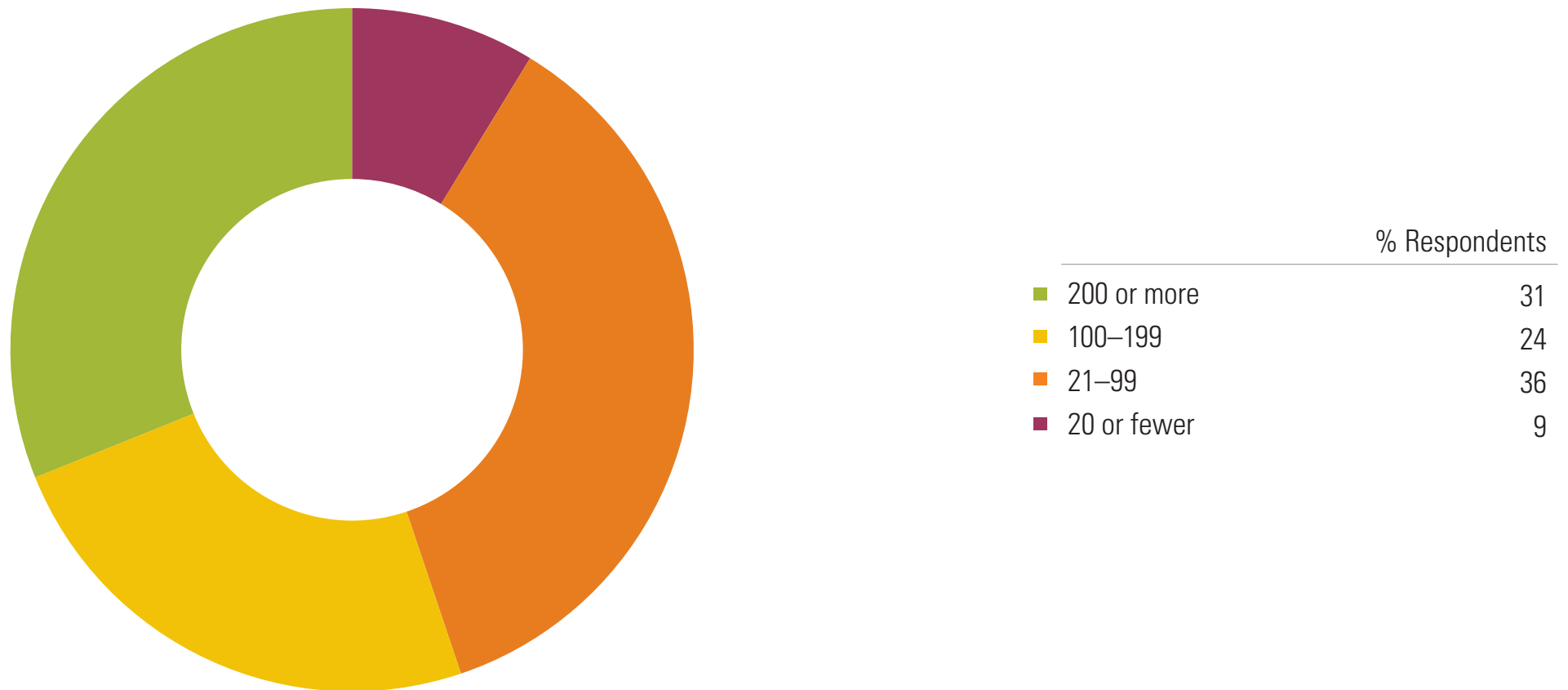


	% Respondents
Bank	3
Financial Planner	13
Independent	17
Insurance	4
Other	6
Regional	1
RIA- SEC Registered	28
RIA- State Level	27
Wirehouse	1

Advisors' AUM Compared With Previous Years



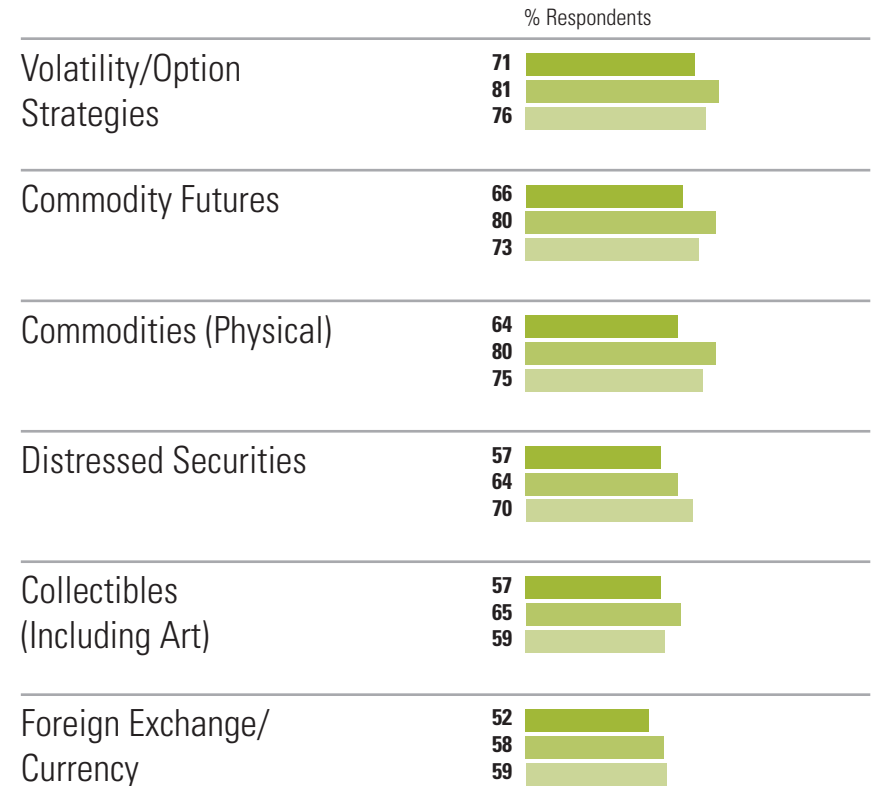
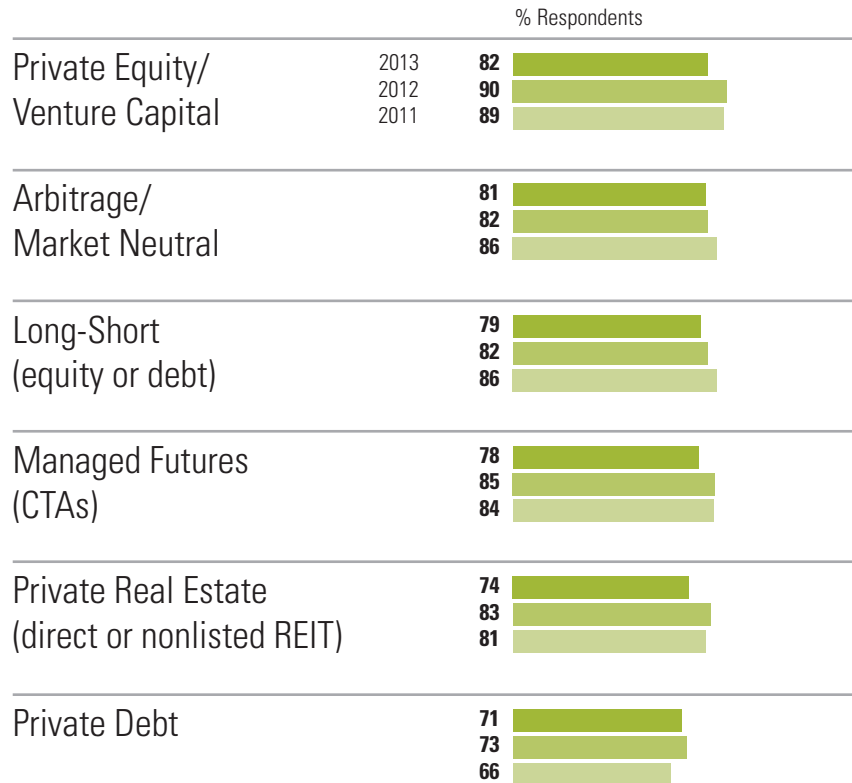
Advisors 2013–2014: Most Serving 100 or More Clients



Defining Alternative Investment Strategies 2013–2014

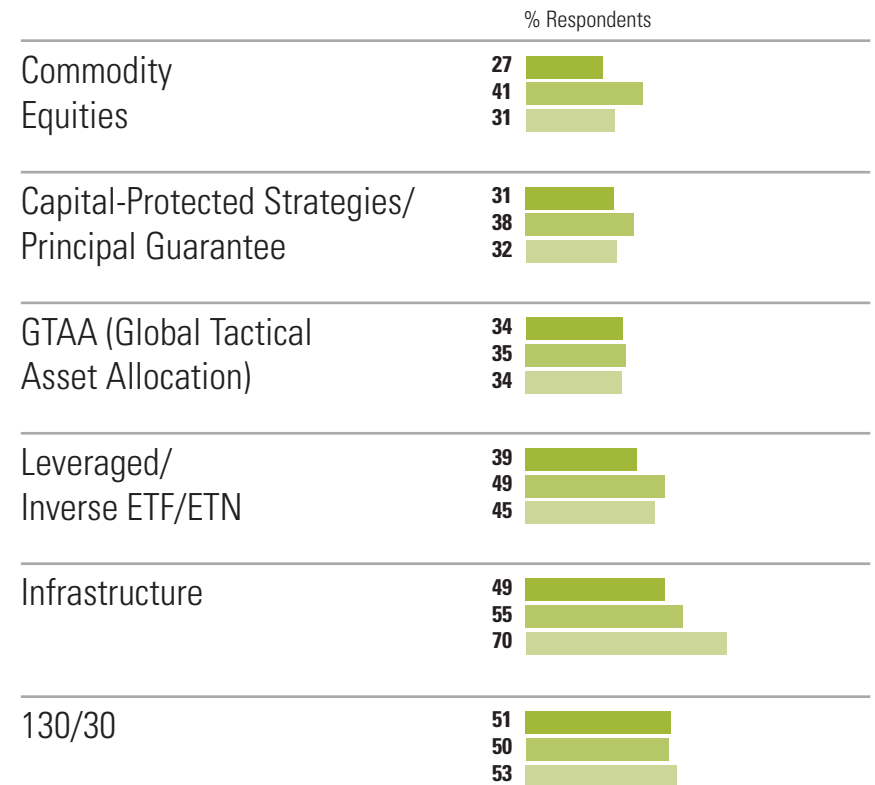
Institutions: What Are Alternative Investment Strategies?

Top 12, Ranked by 2013–2014 % Agreement



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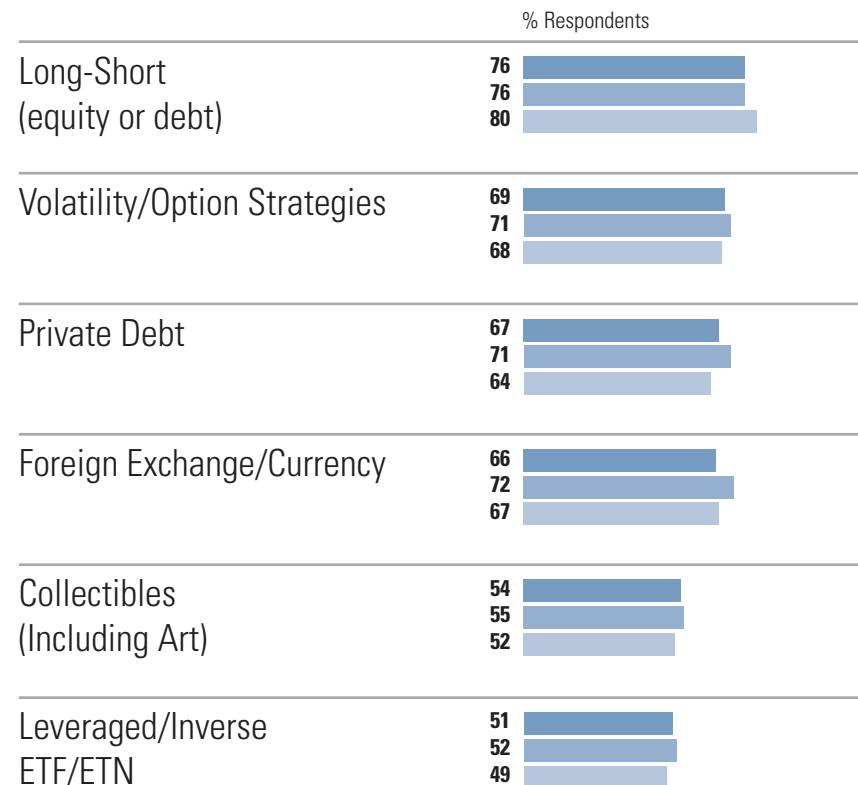
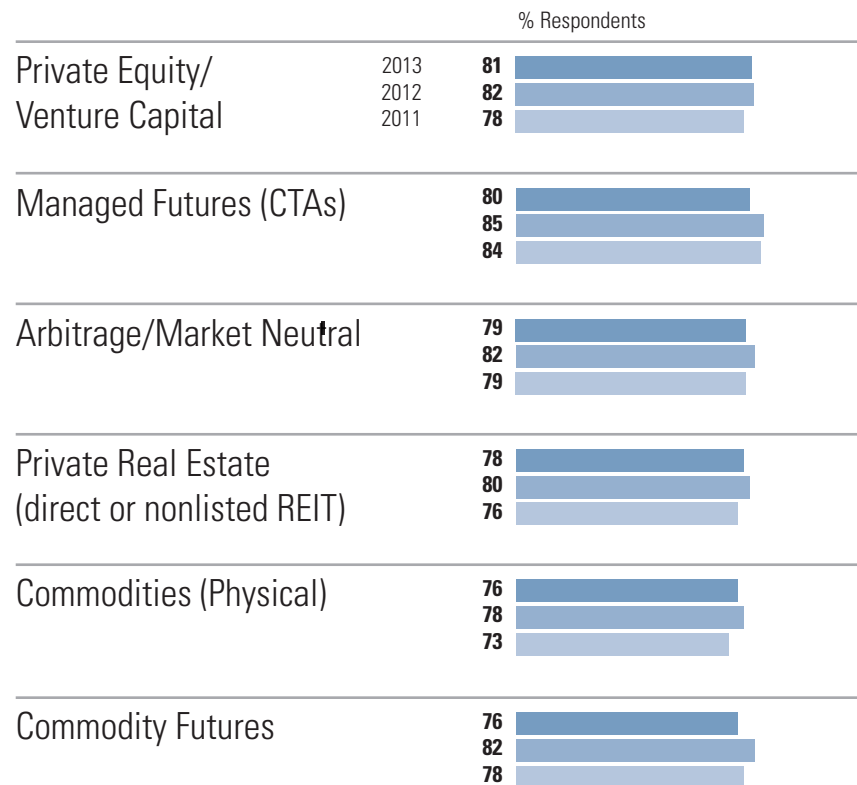
Bottom 12, Ranked by 2013–2014 % Agreement



- ▶ Event-driven, equity market neutral, structured products, bank loans
- ▶ Natural resources and timberland
- ▶ Absolute return
- ▶ Long-short equity, merger arbitrage, liquidations and trade claims, global macro
- ▶ Risk parity
- ▶ Global macro
- ▶ Hedge fund replication

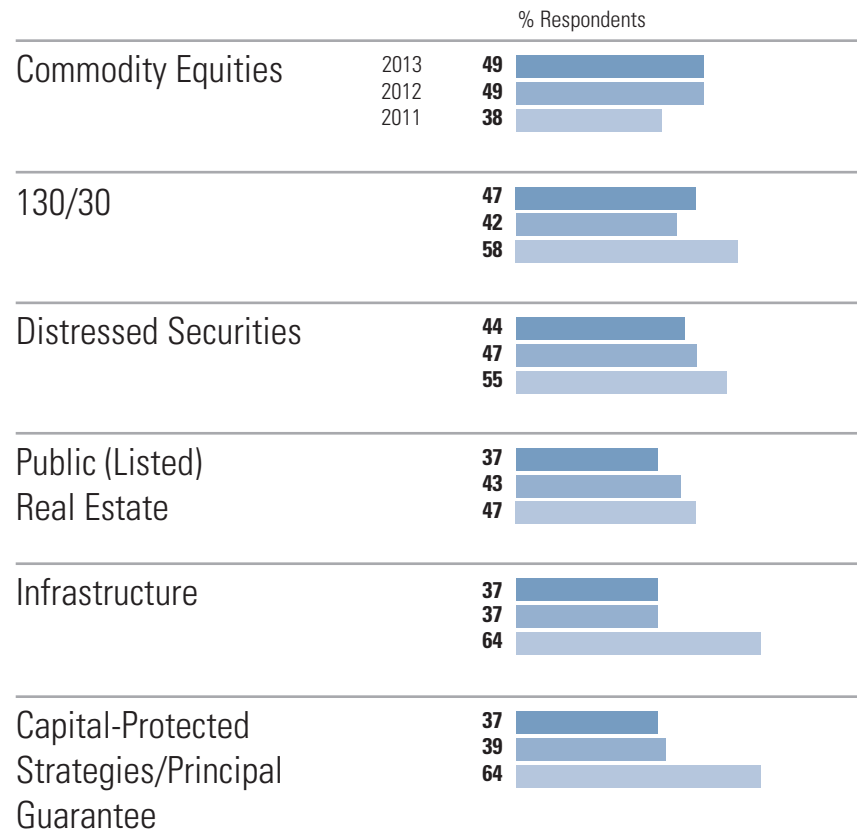
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Top 12, Ranked by 2013–2014 % Agreement



Advisors: What Are Alternative Investment Strategies?

Bottom 12, Ranked by 2013–2014 % Agreement



- ▶ Absolute return
- ▶ Master limited partnership
- ▶ Business development companies
- ▶ Leveraged ETF funds
- ▶ Options strategies
- ▶ Multiasset options

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