Women in Alternative Investments:

A Marathon, Not a Sprint

For women fund managers, endurance trumps pace.
“... the pace of women entering the alternative investment portfolio manager ranks has not been brisk, but it does appear to be steadily improving. As more women-run funds become available, more investors are able to consider women-owned or -managed funds for investment.”
In many ways, investment management is like an endurance race. The art of generating returns for investors requires fortitude and persistence, as well as the ability to constantly adapt to different market terrains. Maintaining your pace on a long-distance run takes a sort of discipline and determination with which many investment managers are familiar. It may not always be pretty — but in the end, it’s all about successful results.

In our third annual “Women in Alternative Investments” report, it is clear that investors, private equity, venture capital and hedge funds see many of those endurance characteristics magnified for women in the alternative investment industry. The race seems longer, the pace slower, and the finish line further away.

However, while perhaps not as speedy as some would like, diversity mandates, as well as demonstrated outperformance by women managers, are driving investors to increase allocations to women-run funds. In fact, nearly 25 percent of the investors polled for this report indicated they would increase their allocations to women-owned or -managed funds in the coming year by some margin.

In turn, more women anticipate launching their own fund in the coming years — 17.5 percent in our 2013 survey versus 14.2 percent in 2012. Certainly, the pace of women entering the alternative investment portfolio manager ranks has not been brisk, but it does appear to be steadily improving. As more women-run funds become available, more investors are able to consider women-owned or -managed funds for investment. A slow, but steady, virtuous cycle is born.

Henry Ford once said, “The competitor to be feared is one who never bothers about you at all, but goes on making his own business better all the time.” Indeed, in the alternative investment industry, the women we polled are clearly focused on running their own race. Our respondents are targeting above-average returns in 2014 — more than 50 percent of the respondents polled hope to generate returns of 10 percent or more next year. More than three-quarters of those polled plan to raise new investment capital in 2014, while another 45 percent hope to launch a new fund in the next 12 months. Each one of these steps brings them inexorably closer to the finish line, even if it appears distant at times.

We are very pleased to share the results of our third annual “Women in Alternative Investments” study with you. We hope that this report will continue to increase the dialogue between investors, managers and other industry participants, and encourage you to contact us directly with questions or for a more in-depth discussion of our findings.

Sincerely,

Rothstein Kass’ 2013 Women in Alternative Investments Research Committee
Key Findings

- Roughly 93 percent of the investors polled have no specified mandate to invest in women-owned or -managed funds.

- “Lack of supply” of women-owned or -managed funds was cited as one of the most common reasons why investors do not have specific women-owned or -managed fund investment mandates.

- The lion’s share of investors, 73.5 percent, anticipates that their allocations to women-owned or -managed funds will remain the same in 2014. However, 24.5 percent expect allocations to increase somewhat, and 2 percent expect allocations to women-owned or -managed funds to increase significantly.

- For the six and a half years ending June 2013, the Rothstein Kass Women in Alternative Investments (WAI) Hedge Fund Index returned 6 percent, while the S&P 500 gained 4.2 percent and the HFRX Global Hedge Fund Index dropped -1.1 percent during the same period.
• Although performance comparisons are more difficult in the private equity space, a small sample of women-owned or -managed private equity funds reported net returns of 14.8 percent in 2012, topping the Cambridge Associates LLC U.S. Private Equity Index® return of 13.8 percent.

• A higher percentage of the respondents indicated that their five-year career goal was to be managing their own fund: 17.5 percent in 2013 versus 14.2 percent in 2012. Access to seed capital or networks for raising capital were the two most dependent variables cited, with more portfolio experience and a portable track record ranking as the next most critical factors.

• Most of the respondents across the demographic groups in our survey disagree or strongly disagree with the statement that there will be fewer attractive investment opportunities for alternative investment firms in 2014.

• Competition for deals was chosen as the most pressing issue facing private equity and venture capital funds in 2014 by investors and private equity respondents, while exit opportunities ranked first among venture capital respondents.

• An astonishing 81.5 percent of hedge fund respondents will be on the fundraising trail in 2014, while 75.3 percent of the private equity respondents plan to join them.

• Unlike last year, pension funds did not make the top funding sources for hedge funds or venture capital funds in this year’s report. Even though many of the respondents continue to become aware of “diversity” mandates at pension funds, those assets may be directed through funds of funds.
Methodology

To create the 2013 Rothstein Kass “Women in Alternative Investments” (WAI) report, we relied on the following information:

• A survey performed by Rothstein Kass in September and October 2013. The survey, which was conducted over a period of five weeks, captured the sentiments of 440 senior women in the alternative investment industry, including fund managers, investors and service providers.

• Responses from the survey were analyzed and aggregated to create summary results.

• Responses were also broken down by several key demographic groups. These results were then compared to provide additional granularity. Demographic groups that were considered separately included:
  – Hedge funds/funds of hedge funds/Commodity Trading Advisor (CTA) firms (“hedge fund respondents”)
  – Private equity/private equity funds of funds/private equity fund sponsors (“private equity respondents”)


• Venture capital firms (“venture capital respondents”).
  (Due to lighter participation by women in venture capital, these numbers may not be statistically significant. We do believe, however, that they are directionally correct based on our interactions within the industry.)
• Investor firms (“investors”)
• Emerging funds — All hedge fund, private equity and venture capital respondents with less than $150 million under management
• Large funds — All hedge fund, private equity and venture capital respondents with more than $500 million under management
• Young funds — All hedge fund, private equity and venture capital respondents with less than three years of operating history
• Established funds — All hedge fund, private equity and venture capital respondents with more than five years of operating history

• Survey participants were asked to provide additional thoughts throughout the survey. Their comments have been included in this report where applicable.
• A Rothstein Kass Women in Alternative Investments (WAI) Hedge Fund Index was created for performance analysis on the hedge fund component of the WAI universe. It was constructed based on 82 hedge funds that have reported monthly performance to either HedgeFund.net or the Hedge Fund Research databases. Funds were selected based on individual knowledge of women-owned or -managed status, or based on the presence of female principals listed in the Hedge Fund Research diversity category listing. No adjustments were made to account for survivor bias due to the scarcity of available information on defunct women-owned or -managed funds.
• Research on investor mandates was conducted using the FINsearches database and the Internet.
• Rothstein Kass principals were asked to weigh in on subjects on which they are experts.
• Industry publications, articles, studies and white papers were used in developing this report.
• Ongoing conversations with clients and other industry participants provided additional insights.
• Please note that some statistics have been impacted by rounding.
For women in the alternative investment industry, 2013 was a year of highs and lows. Indeed, the year started out on a high note. When the inaugural Rothstein Kass WAI Hedge Fund Index was released in January 2013, the press jumped at the data. The story that women-run hedge funds had outperformed the universe at large appeared in major outlets including CNBC, The New York Times, NPR’s Marketplace, Yahoo! Finance and a host of others, drawing industry and investor attention to what many had suspected for a long time: Women portfolio managers can and do produce stellar returns for their investors.

Any triumph women felt was short-lived, however, as only three months later, one of the industry’s best-known figures, Paul Tudor Jones, was widely quoted stating that motherhood and investing simply don’t mix. “As soon as that baby’s lips touched that girl’s bosom, forget it,” said Jones, as he pointed toward his own chest during a talk at the University of Virginia. “Every single investment idea … every desire to understand what is going to make this go up or go down is going to be overwhelmed by the most beautiful experience … which a man will never share … ,” said Jones.

Now, to be fair, Jones was just as pessimistic about the performance of male money managers during major life-changing events, such as divorce. However, his remarks about women money managers touched off furor and debate in the industry that is generally reserved for more private, off-the-record conversations.

Despite the controversy, investors continued to discuss and implement “emerging manager” programs, although perhaps not at the pace many had hoped at the beginning of the year. Exhibit 1 provides a sample of some of the diversity investing activity that was reported at the time this report was written.
Investors and women-owned and -managed funds are faced with an interesting dilemma of which comes first, the chicken or the egg,” said Kelly Easterling, principal-in-charge of Rothstein Kass’ Walnut Creek, Calif., office. “One of the reasons that investors are not able to invest in diversity funds is the lack of diversity funds available for investment. Without a large supply of funds, it’s difficult to achieve appropriate portfolio diversification or, for that matter, put enough money to work to move the performance dial. On the other hand, until there is more money flowing to women-owned and -managed funds, it’s unlikely that there will be a stampede of new fund launches. Unfortunately, that paradox slows the process down for both sides of the equation.”

At the same time, many of the women polled for our survey continue to believe that performance, not affirmative investing, is the key to increasing women-owned and -managed fund assets under management. “I think good returns, having a large investment in the funds and being a good fiduciary are what attracts capital,” said one respondent. “My gender gets me noticed sometimes because there are so few women hedge fund managers that manage over $1 billion, but I have never heard any overt reference to my gender as a plus or minus. My guess is that it is harder to compete if you are not a standout performer.” Another respondent put it even more pointedly: “Giving money to women-owned firms is not the way forward — rather it is to look broadly and include [women] in the search. … I would rather see women-dominated firms grow because they perform better.”

Indeed, especially in recent months, performance is the name of the game, as alternative investment funds struggle to keep up with a seemingly unstoppable equity market benchmark. However, regardless of whether superior performance drives allocations, or whether diversity mandates pave the road to investment, the women-owned and -managed investing race is proving to be quite the marathon, rather than a sprint.

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<th>Exhibit 1 – Diversity Investing Activities in 2013¹</th>
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<td><strong>Entity Name</strong></td>
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<tr>
<td>Dallas Employees’ Retirement Fund</td>
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<td>State of Connecticut Retirement Plans and Trust Funds</td>
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¹Source: Rothstein Kass analysis of FINsearches.com data
Demographics

The Rothstein Kass “WAI” study encompasses feedback from a diverse group of industry participants. Exhibit 2 shows the breakdown of survey respondents, which was led by hedge fund respondents (hedge funds/funds of funds/CTAs) at 40.7 percent. Private equity respondents (private equity/funds of funds/fundless sponsors) and venture capital respondents represented 25.2 percent and 7.5 percent of the surveyed population, respectively, while “Other,” which included service providers, made up 12.3 percent of our sample. We also polled investors, who comprised 14.3 percent of our survey respondents, in an attempt to ascertain their allocation plans and attitudes toward women-owned and -managed funds.

Most of the survey respondents represented stand-alone firms (72.9 percent), with only 13.7 percent being part of a larger institution (Exhibit 3). Of the fund constituents, hedge fund respondents were the most likely to be stand-alone firms (90.5 percent) and private equity respondents were the least likely (83.6 percent). Emerging fund respondents were slightly more likely to be a stand-alone firm than large fund respondents (88.9 percent versus 86.5 percent). Likewise, young funds were the most likely to represent independent firms, at 92.3 percent. Investor respondents were the most likely to be part of a larger institution, with 68.2 percent indicating they are not independent firms.
Survey respondents overall were almost equally likely to represent firms with under $1 billion assets under management (AUM) as they were to represent firms managing $1 billion or more (Exhibit 4). Investors were the least likely to have less than $1 billion AUM (81.8 percent reported over $1 billion AUM), while 46.3 percent, 59.4 percent and 36.4 percent of the hedge fund, private equity and venture capital respondents, respectively, represented firms with $1 billion or more AUM. Hedge fund respondents were the most likely to have less than $150 million AUM, at 27.4 percent, while young firms were predictably the most likely to qualify as “emerging” (81.6 percent). Roughly 24.2 percent of venture capital respondents and 15.1 percent of private equity respondents manage less than $150 million. Less than 10 percent of the investor respondents manage a similar amount.

Meanwhile, Exhibit 5 shows that nearly half of the respondents represent firms with 25 or fewer employees (48 percent). Investor respondents were most likely to hail from larger firms, with 47.7 percent representing firms with 100 or more employees. Approximately 30.8 percent of investors employ 25 or fewer employees, while 63.1 percent of hedge funds, 60.6 percent of venture capital funds and 41.4 percent of private equity funds hail from similarly sized firms. One hundred percent of the young funds also represented small funds in terms of employees, while funds managing less than $150 million were nearly 90 percent likely to also represent small firms.
Most of the survey respondents represented firms that have long tenures. Nearly 80 percent of those polled represented firms that have been in operation more than five years, while only 2.3 percent hail from firms that have been up and running for less than one year (Exhibit 6). The hedge funds in our survey were the most likely to represent newer firms, with 14.7 percent of those polled in operation less than three years. Private equity and venture capital firms were the second and third most likely to represent nascent firms, with 10 percent and 6.1 percent reporting in that category, respectively. Firms in the 2013 study were slightly less likely to represent newer firms than those in the 2012 study, when over 3 percent of the firms polled had less than one year's operating history.

Much like the firms polled, the women in our survey generally have long tenures in the financial services industry. Approximately 70 percent of those polled have 11 or more years of experience in the industry (Exhibit 7). Only 3.6 percent of those polled have been in the industry for less than two years. Many of the respondents also have investment experience outside of the alternative investment industry. In fact, 52.3 percent of the survey respondents sit on one or more boards, although female public corporate board participation remains low, at only 2.7 percent of those polled (Exhibit 8).
In addition, roughly one out of three women in our survey sits on their firm’s investment committee (Exhibit 9). The respondents were most likely to sit on their firm’s investment committee if they hailed from an investor firm (46.2 percent) or from a venture capital firm (42.9 percent). Meanwhile, 31.3 percent and 32.5 percent of the hedge fund and private equity respondents, respectively, sit on their firm’s investment committee.
As with last year’s study, women remain more common in financial, compliance or operations roles within the alternative investment industry. The women in our survey hold the highest percentage of C-level jobs within the financial suite, at 39.7 percent, followed closely by C-level compliance and C-level operations, at 38.1 percent and 34.3 percent, respectively (Exhibit 10). Women were least likely to hold C-level technology positions within their firms, with only 8.2 percent of those responding indicating those positions are held by women.

The women in our survey indicated that CIO and CEO positions are held by women at 22.5 percent and 17.2 percent of the firms polled, respectively. Women were most likely to be found in the CEO position at hedge fund respondent firms (23.2 percent) or investor firms (17.5 percent) and were least likely to hold the CEO position at venture capital respondent firms (9.7 percent). Investors were the most likely to employ a female CIO, at 33.9 percent, followed by venture capital, hedge funds and private equity at 28.1 percent, 21.4 percent and 17.3 percent, respectively. Young funds across the fund groups were more likely to have a woman at the investing helm than established funds, with 29 percent and 16.2 percent, respectively, employing a female portfolio manager/CIO.

Unfortunately, the percentage of women comprising the majority of a firm’s investment committee continues to remain somewhat stagnant, with 9.4 percent of firms reporting that women represent 50 percent or more of their investment committees (Exhibit 11). Women tend to be better represented on the investment committees of investors, hedge funds and venture capital firms, with 14.1 percent, 12.3 percent and 12.1 percent, respectively, indicating they have 50 percent or more women on the investment committee. As in last year’s study, private
equity funds remain behind the curve on this trend, with only 2.7 percent of those polled indicating that their firm’s investment committee is comprised of 50 percent or more women.

Across the various alternative investment segments, roughly 42 percent of the respondents polled indicated that their firm has no female general partners (GPs) (Exhibit 12). While hedge funds remained the most likely respondents to indicate they have no female GPs, at 51.2 percent, they are also the most likely fund respondent group to indicate they have 50 percent or more women GPs, at 16.1 percent. Young funds were the most likely respondents to indicate they have 50 percent or more women GPs (24.3 percent), while only 3.7 percent of the large funds reported the same.

Finally, we asked survey participants whether their firm is women-owned or -managed. Only 15.5 percent of those polled indicated their firm is women-owned or -managed (Exhibit 13). Hedge fund respondents were the most likely to reveal women-owned or -managed status, at 21.4 percent. Roughly 15.6 percent of the venture capital firms stated they are women-owned or -managed, while only 10.2 percent of the private equity firms polled indicated the same.
Those polled for the 2013 WAI study appear to be fairly optimistic about the opportunities available for alternative investment firms in 2014 (Exhibit 14). Few seem to agree or strongly agree with the statement that there will be fewer attractive investment opportunities in 2014 than in 2013. Venture capital firms appear to be the most enthusiastic about potential opportunities in the alternative investment space overall, while investors and hedge funds appear to be a bit more sanguine. Interestingly, however, investors, private equity and venture capital respondents also generally agree that it will take longer for investment positions to yield positive results in 2014 than in 2013 (Exhibit 15). Hedge funds, likely due to their more liquid investments, were the lone holdout in the survey, with nearly half disagreeing with this statement.
Hedge Funds/Funds of Hedge Funds/Commodity Trading Advisors

Looking at various alternative industry segments, it appears that many of those polled are reasonably optimistic about the future. Admittedly, 2013 was somewhat of a mixed bag for the hedge fund industry. On one hand, hedge fund assets continued to grow, increasing by $40 billion through the second quarter to peak at a record $2.41 trillion, according to Hedge Fund Research, Inc. (HFR). Furthermore, the total number of hedge funds increased to a new high of more than 10,000 funds for the first time since 2006.

At the same time, however, somewhat lackluster returns have caused hedge funds to be hit by almost incessant negative rhetoric in 2013, culminating in the July 2013 Businessweek article, “Hedge Funds Are for Suckers.”

It is undoubtedly true that the average hedge fund has lagged the S&P 500 in recent months and years, giving rise to a wave of media and investor dissatisfaction. Perhaps it is no wonder, then, that performance predictions for hedge funds for 2014 proved a bit difficult for many of those polled. The majority of hedge funds polled (40.8 percent) are predicting slightly better or much better returns in 2014 (Exhibit 16), while 21.2 percent of investors foresee the same.
Hedge Funds/Funds of Hedge Funds/Commodity Trading Advisors (continued)

Because hedge funds/funds of hedge funds/CTAs are the sole segments within the alternative investment universe that have regular monthly return streams, we were able to analyze the performance of women-owned or -managed funds in order to put their returns into perspective versus the S&P 500 and the hedge fund universe overall. The Rothstein Kass WAI Hedge Fund Index (Exhibits 17 and 18) is comprised of 82 funds we believe qualify as women-owned “diversity” funds. Funds were categorized as women-owned diversity funds based on our knowledge of the hedge fund landscape and/or information found within the HFR database. After funds were identified, a non-weighted monthly index was created using performance figures from HedgeFund.net and/or HFR.

No adjustments were made to the WAI Index (or the HFRX Global Hedge Fund Index) to account for survivor bias due solely to the difficulty of identifying defunct women-owned funds. Returns for the index were calculated for the six and a half years ending June 2013.
There are a number of reasons why women-owned and -managed funds are able to produce excess alpha over the alternative investment universe at large,” said Meredith Jones, director at Rothstein Kass. “Certainly, fund size can play a role, as it is a well-known fact that smaller funds tend to outperform larger funds. However, the success of large women-owned or -managed funds means that explanation is partial at best. Another simplistic explanation is ‘risk aversion.’ In fact, the truth is that women often perceive risk differently than men and, as such, tend to manage their portfolios differently. Studies have shown that women trade less, are less apt to market time and have less ego involved in their investments than their male counterparts. The result is less performance slippage from frequent trades, a diminished tendency to sell at the bottom and a more consistent application of their strategies. Over time, this can add up to a meaningful and persistent performance differential.”

Although year-to-date figures for the Rothstein Kass WAI Hedge Fund Index are not as impressive as 2012 gains, for the six and a half years ending June 2013, the WAI Index outperformed both the HFRX Global Hedge Fund Index and the S&P 500, with dividends reinvested. In Exhibit 18, one can see a nearly 2 percentage point differential between the WAI Index and the S&P 500, and more than a 6 percentage point differential between the WAI Index and the HFRX Global Hedge Fund Index.

The Rothstein Kass WAI Hedge Fund Index also exhibited the highest percentage of positive months, at 62.8 percent, edging the S&P 500’s 61.5 percent and the HFRX Global Hedge Fund Index’s 55.1 percent positive months. The largest monthly loss is most appealing for the WAI Index, coming in at only -7.6 percent. In comparison, the S&P 500 experienced losses of twice that amount during the same period.

Assuming that women-owned or -controlled funds do have a better 2014, as they largely expect, the coming year could be a promising one for the hedge fund respondents in our survey. In fact, 53.2 percent of the hedge fund respondents are targeting a return of 10 percent or more in 2014 (Exhibit 19). An additional 32.7 percent are targeting a return of 5 percent to 10 percent for the year.
Much like last year's study, investors remain staunchly optimistic about the performance of private equity investments (Exhibit 20). None of the investors polled expect the performance of private equity investments to be much worse in 2014 than in 2013, and more than 44 percent anticipate that performance will be slightly or much better in 2014. Interestingly, investors appear to be even more confident about future returns than private equity industry participants, who were nearly evenly split between those who believe performance will remain much the same as it was in 2013 and those who believe it will be slightly better or much better in 2014.

Unlike the hedge fund segment, we do not have the ability to easily measure the performance of private equity respondents in prior or current years. In the small sample of women-owned or -managed fund performance we were able to glean, women-owned or -managed funds outperformed the universe at large in 2012, the most recent year for which we have figures. Based on the self-reported results of six women-owned or -managed private equity funds, the WAI Private Equity Fund Index returned 14.8 percent. In comparison, Cambridge Associates LLC reported that for the year ending December 31, 2012, their private equity index returned 13.8 percent.
Venture capital and private equity are an interesting study in contrast,” said Andrea Kalliaras, a principal at Rothstein Kass. “In recent years, both have been hit by many of the same issues: decreased deal flow, fewer exits and investor aversion to illiquidity. Interestingly, the private equity industry has continued to flourish, with sustained and increasing investor interest, while venture capital has continued to experience contraction. Easier access to funding through Kickstarter and other crowdfunding platforms — combined with lower technology and other startup costs — has reduced reliance on venture capital, squeezing that end of the private equity spectrum. Meanwhile, private equity funds have turned to co-investment and other forms of ‘opt-in’ investing to increase palatability. It will be interesting to see how their futures play out in the coming months and years.”

Despite a somewhat measured outlook for 2014, private equity respondents seem confident about 2014 returns. Nearly 62 percent of those polled are targeting returns of 15 percent or more in 2014, while another 23.8 percent are targeting returns of 10 percent to 15 percent (Exhibit 21).

Unlike last year, the venture capital respondents seem to be the most certain that their industry will experience a turnaround in 2014. More than 53 percent of those venture capital funds polled anticipate that performance will be slightly better or much better in 2014 (Exhibit 22). Investors, on the other hand, are the least confident about venture capital performance in 2014, with 7.8 percent of those polled anticipating that it will fare much worse in 2014 than in 2013. One respondent stated, “Returns have not beat equity markets in a very long time. [The] question is should [one] continue to invest. Also, venture companies need less money so funds sizes need to be smaller.”
The venture capital funds polled are targeting strong returns in 2014, with 60 percent aiming for returns of 15 percent or more (Exhibit 23). Venture capital respondents, however, are the most uncertain about their targeted returns for 2014, with nearly 17 percent of those polled indicating uncertainty, compared with 7.2 percent of private equity respondents and 10.9 percent of hedge fund respondents.

Anxiety about exit opportunities is a likely cause of return uncertainty for many venture capital firms (Exhibit 24). Although venture capital firms completed a similar number of exits in 3Q 2013, at 131, the dollar amount of those exits represented a 23 percent drop from the same period a year ago, according to PitchBook Data, Inc. Looking at 2012, venture capital M&A exits declined by 10 from the same period in 2011, while there were three fewer venture-backed IPO exits, according to Thomson Reuters and the National Venture Capital Association.

While investors were also concerned about exit opportunities, with 27.5 percent citing them as the most pressing issue facing private equity and venture capital funds in 2014, they were more troubled by increased competition for deals. Roughly 31.4 percent of the investors polled thought competition for deals would be an issue in 2014. Roughly one-third of the private equity respondents were in agreement, dwarfing their next biggest concern, which was exit opportunities, at 17.9 percent.
It is interesting to note that competition for deals is expected to be problematic when many of those polled also anticipate that deal flow will improve in 2014 (Exhibit 25). Only 2.1 percent of the private equity respondents thought that deal flow would be much worse in 2014 than in 2013, while no venture capital respondents agreed with that sentiment. Indeed, the lion’s share of both groups anticipates improved deal flow in 2014.

Perhaps improved deal flow will have a positive impact on the perception of company valuations. More than half of those polled believe that company valuations are unattractive or slightly unattractive (Exhibit 26). Just over 6 percent of the venture capital respondents believe that valuations are very attractive, while 4.4 percent of the private equity respondents agree. No investors believe that valuations are very attractive, while just under a third believe that valuations are attractive. Several respondents pointed out that the perception of company valuations was linked to where a firm was in the lifespan of its funds. “Valuations [when] selling companies are quite attractive now. This means that valuations at acquisition are decidedly high. We are selling more than buying at present, so [this is a] good market for us,” stated one respondent. This sentiment was echoed by several other firms.
When asked what strategies within the alternative investment industry would perform best in 2014, almost none of our respondents agreed, and the fund respondents largely didn’t concur with the investor respondents. While long/short strategies took first place overall at 30.1 percent (Exhibit 27), responses varied widely among the various demographic groups. Hedge fund respondents predicted long/short investing would emerge victorious in 2014, while, perhaps unsurprisingly, private equity and venture capital respondents chose leveraged private equity (39.2 percent) and early-stage investing (78.6 percent), respectively. Investor respondents were evenly split between emerging markets and distressed strategies (tied at 37.2 percent). Young funds and established funds agree that long/short investing would be the most successful strategy in 2014, while emerging funds and large funds diverged. Emerging funds predict long/short strategies will carry the year (42.1 percent), while large funds are looking to growth-stage venture capital (30.4 percent) for superior returns.
Managing an Alternative Investment Firm in 2014

As in last year’s study, core investment functions are not the most pressing concern of the majority of those polled, despite any performance and market uncertainty. Capital raising continues to be the most pressing fund management concern heading into 2014 (Exhibit 28). Regardless of the industry segment they represent, roughly two-thirds of the funds polled believe that increasing AUM is their most challenging function. Unlike last year, all three segments are also in agreement about their second most challenging issue: core investment functions. Last year, venture capital and private equity respondents cited core investment functions as their most pressing issue, while hedge funds were more focused on the changing regulatory environment. Now that most managers have met the demands of the new regulatory regime for the time being — and recalling that hedge fund returns, deal flow and the exit environment have been a bit uninspiring — our respondents are returning their attention to their core fund management functions.

Exhibit 28 – Most Pressing Fund Management Concerns

- Core investment functions: 36.7% (Hedge fund/CTA), 37.7% (PE/FS), 34.4% (VC)
- Capital raising: 70.9% (Hedge fund/CTA), 64.7% (PE/FS), 62.0% (VC)
- Regulatory changes/ Uncertain regulatory environment: 29.7% (Hedge fund/CTA), 31.8% (PE/FS), 27.5% (VC)
- Becoming more technologically sophisticated: 12.7% (Hedge fund/CTA), 5.9% (PE/FS), 3.4% (VC)
- Increasing visibility, PR or advertising: 12.7% (Hedge fund/CTA), 17.7% (PE/FS), 10.3% (VC)
- Other: 3.8% (Hedge fund/CTA), 4.7% (PE/FS), 13.7% (VC)
Fundraising in 2014

With fundraising at the forefront of our respondents’ minds, we inquired about their upcoming capital-raising plans. More than three-quarters of those polled plan to raise capital in the next 18 months (Exhibit 29). An astonishing 81.5 percent of the hedge fund respondents will be on the fundraising trail in 2014, while 75.3 percent of the private equity respondents plan to join them. Roughly 60 percent of the venture capital respondents plan to raise new investment capital in 2014. Approximately 83 percent of the emerging funds polled plan to pursue new assets in 2014, and, perhaps surprisingly, nearly 75 percent of the large funds polled plan to raise capital in 2014 as well.

Despite plans to raise assets, fewer firms are planning to launch new funds in 2014 than in last year’s study (Exhibit 30). Private equity funds will be the most aggressive about launching new funds, with 62.5 percent of those polled planning to do so. Meanwhile, only 35.1 percent of the hedge fund respondents plan to launch a new fund in 2014. Established firms were the most likely of the age groups to be planning to launch a new fund, with 47.2 percent stating they had plans to start one.

Despite the appearance of emerging manager mandates that have the potential to drive capital to women-owned and -managed funds, high-net-worth individuals and family offices remain the most fruitful sources of investment capital according to respondents (Exhibit 31). Hedge fund and venture capital respondents were most likely to cite high-net-worth individuals as their most useful source of capital, at 52.6 percent and 70 percent, respectively. Meanwhile, private equity respondents named pension funds as their most fertile investor group (58.2 percent). Not surprisingly, the large funds polled agreed that pension funds were their most important source of capital (54.7 percent), while emerging funds cited high-net-worth individuals (81 percent).
Unlike last year, pension funds did not make the top funding sources for hedge funds or venture capital funds in this year’s report. Even though many of the respondents continue to become aware of diversity mandates at pension funds (Exhibit 32), there appears to be a growing sense that these mandates may not deliver much direct opportunity. “They talk the talk but do not walk the walk. No real investment takes place if the firm is emerging and female,” said one respondent. Another respondent echoed that sentiment, stating that diversity mandates “seem to be urban [legend].” Still, others expressed frustration with how emerging manager programs evolve over time. “The larger issue is that the definition of ‘emerging manager’ often has come to include ‘early-stage white male who has just spun out of the prop desk at Goldman,’” said one respondent.

Funds of funds were the second most common entity where survey respondents saw diversity or emerging manager mandates. Given that the drive toward including more women-owned and -managed investments is still in its nascent stage, fund of funds mandates may be the way forward for many of the firms in our survey. When institutional investors first dipped their toes in the alternative investment water nearly a decade ago, funds of funds were often a preferred vehicle for investment. Now that pensions, endowments and foundations have more experience with hedge funds, private equity and venture capital, they are increasingly going direct to the individual fund managers, eschewing the fund of funds structure. Adding fuel to this theory are our respondents’ comments. “We are currently working on an FOF mandate for WMBE [women and minority-owned business enterprise] managers,” said one respondent. “I represent a fund of funds with public pension funds allocating capital to my firm to find and invest in women-owned firms,” said another.
As in last year’s study, the vast majority of respondents, 80.3 percent, have not received any emerging manager funding (Exhibit 33). A slightly higher percentage of the firms polled this year have received funding through an emerging manager program: 8.5 percent versus 5 percent in last year’s study. Although venture capital firms were the diversity mandate winners last year, this year, 10.2 percent of the hedge fund respondents stated they received allocations through an emerging manager program. In comparison, 6.7 percent and 6.4 percent of venture capital and private equity funds, respectively, have received this type of allocation.

To Certify or Not to Certify?
A small number of respondents continue to maintain national certification as a woman-owned business from the Small Business Administration (SBA), while a slightly higher number of respondents indicated they have state or local certification (Exhibit 34). Despite this small uptick in registration, some respondents expressed frustration with the certification process. “…[W]e will not renew as it is time-consuming and there is no benefit in over seven years from this [designation],” said one respondent. Another stated, “We would qualify, but we haven’t bothered to do so.”
Obviously, investor sentiment is the single biggest key to successful capital raising. Regrettably, the vast majority of investors do not have a specific mandate for women-owned or -managed funds (Exhibit 35). However, the lack of an official program does not necessarily suggest that investment into women-owned or -managed firms is not taking place. “Two of our 10 portfolio companies have women CEOs, but it’s not a mandate,” said one respondent. “We back the best people we can find and definitely look for strong women candidates whenever possible,” they continued. Other investors state they are precluded from officially participating in diversity mandates. “We invest in women-owned firms; due to [California] Proposition 209, we are prohibited from affirmatively selecting on this basis,” stated another respondent.

Other investors provided a variety of reasons why no women-owned or -managed investing mandate is in place (Exhibit 36). While “Other,” which encompasses issues such as Proposition 209, was the clear choice among the investor respondents, the second biggest factor for the lack of diversity mandates is simply the small supply of women-owned or -managed funds. This creates an interesting “chicken or the egg” paradox that could be difficult for the alternative investment industry to overcome. More money cannot flow to women-owned or -managed firms due to a lack of capacity and diversification opportunities, but women may remain loath to launch funds in an environment where capital raising will be a constant struggle. One respondent lamented, “It’s just too hard, too expensive, too risky to launch a fund today. We are all too beholden to our biweekly paycheck. Sadly, there’s a lot of talent on the bench that could do great things.”
Despite this predicament, there is some light at the end of the tunnel. Exhibit 37 shows investor expectations for women-owned or -managed fund allocations for the next 18 months. While the lion’s share of investors (73.5 percent) anticipates that their allocations to women-owned or -managed funds will remain the same, 24.5 percent expect them to increase somewhat, and 2 percent expect them to increase significantly.

Exhibit 37 – Expectations for Women-Owned or -Managed Fund Allocations for the Next 18 Months
Additional Business Considerations

While a majority of respondents (46.4 percent) believe the regulatory scrutiny on alternative investments has been as extensive as expected (Exhibit 38), nearly as many respondents (44.7 percent) continue to be surprised by its intensity. Unlike last year’s study, hedge fund respondents appear to be the most surprised by the amount of regulatory focus (56.9 percent), while venture capital and private equity respondents remain more blasé. Just over 11 percent of the investor respondents feel that regulatory scrutiny has been less extensive than expected.

Most of the funds polled believe that the Jumpstart Our Business Startups (JOBS) Act, which was enacted in mid-2012, will have no impact on their marketing and investing operations (Exhibit 39). One respondent stated, “The JOBS Act increases expenses associated with regulatory compliance, but does not increase opportunity as it is too risky to adhere to 506c.” Others were even more concerned about the legislation. “I think [the JOBS Act] is muddying the waters on both [investment and marketing], and ultimately will backfire with small unsophisticated investors getting hurt, boomeranging us back into overregulation,” said one respondent.

Of those who believe the JOBS Act will improve their investment or marketing efforts, venture capital respondents are the most upbeat about the JOBS Act positively affecting their investments. Roughly 11 percent stated that the new legislation will improve that side of the business, likely through easier IPO activity for smaller portfolio holdings. Hedge fund respondents are the most excited about new opportunities for marketing under the JOBS Act, with 12.5 percent stating that the latitude around the JOBS Act will improve their capital-raising efforts.

“One might think that the implementation of the JOBS Act would help bridge the fundraising gap between women- and male-run funds. Thus far, however, we have not seen many of our alternative investment clients taking advantage of the JOBS Act, at least on the marketing side of their businesses,” said Stacey Schell, a principal at Rothstein Kass. “While the ability to market to potential investors outside of their networks might seem like a boon for private equity, venture capital and hedge funds, particularly those run by women who have historically had smaller investor networks available for fundraising, much of the industry remains cautious. Until the industry has some additional clarity about how funds relying on the JOBS Act will fare, it’s unlikely that we will see a rush to advertise.”

Exhibit 38 – Perception of Regulatory Focus

Exhibit 39 – The Impact of the JOBS Act
The Role of Gender in the Alternative Investment Industry

In addition to providing a view into the investment and business outlook of women in the alternative investment industry, this study strives to understand the evolving roles and opportunities for women in hedge funds, private equity and venture capital. In prior years, roughly two-thirds of the women polled agreed or strongly agreed that their gender made it harder for them to succeed in the alternative investment industry. This year, that percentage dropped a bit to 61.3 percent, although the comments of the women polled continue to exhibit what appears to be long-standing frustration (Exhibit 40).

“Although I have absolute confidence in my abilities, the fact that this industry is run like a country club — at best, locker room at worst — makes it difficult to be seen as anything other than an object for amusement. Women just aren’t taken seriously and if you somehow make it into one of these places on your credentials, you are relegated to tasks no one else wants to do,” said one respondent. “I have worked in several male-dominated firms. Typically, I see women only in a marketing role, which reinforces the stereotype of marketing ‘girls,’” said another respondent.

When asked whether there would be more women-owned or -managed fund launches, respondents were also somewhat pessimistic. Last year, roughly 45 percent of the respondents thought there would be an increase in women-owned or -managed funds. This year, that number dropped to about 40 percent.
Interestingly, investor respondents are among the most optimistic about an increase in the female ranks, with 57.7 percent agreeing or strongly agreeing that there will be more women in the alternative investment industry in 2014 and beyond, and 43.1 percent agreeing or strongly agreeing that there will be more women-owned and -managed fund launches in 2014 and beyond. Of course, since their sentiment and dollars tend to encourage or discourage fund launches and hiring practices, they may be the most prophetic of the respondent groups.

Still, there is definitely a perception that being a woman in the alternative investment industry is not an easy path, as evidenced by our respondents’ comments throughout the survey. Supply, desire and access to investor capital were the most commonly cited reasons why there aren’t more women in the hedge fund, private equity and venture capital ranks (Exhibit 41). “The men I work with, who are general partners of the firm, don’t socialize with female executives. Often, we recruit people to join our firm because they are well known to us. If they don’t get to know women they aren’t likely to hire any,” said one respondent regarding the supply issue. Another hoped for an investor-led revolution, stating, “Fundamentally, if the state pension funds and institutional investors demand advancement of women and minorities, it will happen.” Finally, many of the respondents talked about the “old boys’ network” and the “subtle ways women are discouraged from participating in finance.” Overall, despite the progress that has been made, it seems most believe there is still quite a long way to go.
One might hope that the increase in emerging manager mandates will solve at least the demand side of the equation. However, many of the respondents are uncertain whether emerging manager mandates will have an impact on demand for women-owned and -managed funds in the next 12 to 18 months (Exhibit 42). Again, the investors are the most optimistic that diversity mandates will impact the number of women-owned and -managed funds, at 34 percent.

As in last year’s survey, respondents indicated that their most important asset is their professional networks (Exhibit 43), and several of the comments provided throughout the survey echoed this sentiment. “The importance of networking, both within the female investment community and more broadly, cannot be stressed enough as a key to success,” stated one respondent.

Exhibit 42 – Emerging Manager Mandates Will Increase Demand for Women-Owned or -Managed Funds in the Next 12 to 18 Months

Exhibit 43 – Factors Most Critical to Professional Success

- Strong professional networks: 52.6%
- Willingness to take risk: 50.6%
- Strong personal and support networks: 49.1%
- Strategic career planning: 44.3%
- Strong mentoring relationships: 41.4%
- Stellar fund performance: 20.1%
- Access to capital: 15.5%
- Other: 5.5%
Closely following professional networks as the second through fifth most critical factors were: willingness to take risk, strong personal and support networks, strategic career planning, and strong mentoring relationships. Very surprisingly, stellar fund performance came in a distant sixth place. Perhaps this respondent articulated the reason: “I think if a man launches a new fund, it is much easier for him to get capital. Zoe Cruz, a top Morgan Stanley woman, couldn’t raise enough funds for critical mass. With her track record, if she were a man she would be funded. There is sexual bias in the finance industry. Another woman manager with a great distressed track record barely broke $1 billion of capital.”

Despite some of the frustration expressed throughout the survey, a higher percentage of respondents this year indicated that their five-year career goal is to manage their own fund: 17.5 percent versus 14.2 percent in 2012 (Exhibit 44). However, as Exhibit 45 shows, many of those women will require certain conditions to be met before proceeding down that particular road. The majority of respondents appear to be concerned with capital-raising issues, followed closely by track record concerns.
Conclusion

There continue to be signs of increased interest in women-owned and -managed alternative investment funds. As we noted in last year’s study, there is little doubt that momentum is building, but it is also true that any movement is still in its earliest stages. Many of the women with whom we speak are increasingly annoyed with the pace of progress, although nearly all are staying the course for now.

Certainly, improvement will continue to be driven by investor demand for more diversity within their portfolios. In the meantime, there is a growing body of research that shows women portfolio managers tend to outperform. As a result, if diversity doesn’t drive investors to seek women-owned and -managed funds, the search for alpha will undoubtedly lead them there. At the end of the day, the combination of outperformance and diversification will drive allocations, fund launches and hiring within the alternative investment industry. At Rothstein Kass, we look forward to continuing to monitor these trends.

Thank You

Rothstein Kass would like to thank the following organizations and their members for supporting and contributing to this report: 100 Women in Hedge Funds, Texas Wall Street Women, Falk Marques Group and High Water Women.

Further Reading

Rothstein Kass makes an effort to include the perceptions of women in its general industry surveys throughout the year. For more information on women in the alternative investment industry, please see the following 2013 reports: “Water, Water, Everywhere” (Hedge Funds) and “On the Ascent” (Private Equity).
Author and Contributors

About the Author

Meredith Jones is a director at Rothstein Kass responsible for generating research and content on the alternative investment industry by and on behalf of the firm. She also provides business advisory services to the firm’s clients. Meredith has more than 15 years of experience in the alternative investment industry, with extensive expertise in research, writing, consulting, marketing, business development, due diligence, index construction and asset allocation. Her research has been published in a number of books and journals and in the international press.

Meredith can be contacted at: 972.581.7066 or mjones@rkco.com

About the Contributors

Kelly Easterling is an audit principal and principal-in-charge of Rothstein Kass’ Walnut Creek, Calif., office. In addition to her management responsibilities, Kelly specializes in serving clients across the financial services industry, including domestic and offshore funds, commodity pools, private equity partnerships and funds of funds. She advises clients on initial organizational structure and documentation, supervises audits and consults with management regarding various operations and audit matters. Kelly is also significantly involved in Rothstein Kass’ women’s initiative, LIFE (Leadership, Inspiration, Family, Empowerment), where her focus is to expand the program externally by driving strategic relationships in the industry and building business opportunities.

Kelly can be contacted at: 925.952.8008 or keasterling@rkco.com

Andrea Kalliaras is an audit principal at Rothstein Kass. Andrea specializes in audit, accounting and business consulting services for private and public entities, providing clients with her technical acumen as well as a holistic understanding of their business. Andrea has over 15 years of experience working with domestic and international private equity funds, funds of funds and management companies. She has expertise in analyzing clients’ determination of fair value of debt and equity investments for private equity and venture capital funds. In addition, she supports clients with business strategies and internal processes, cash flow solutions and financial forecasting.

Andrea can be contacted at: 973.577.2244 or akalliaras@rkco.com

Rosalie Mandel is a principal at Rothstein Kass. Rosalie specializes in audit, general accounting and business consulting services for private entities. She is also principal-in-charge of LIFE (Leadership, Inspiration, Family, Empowerment), Rothstein Kass’ women’s initiative. LIFE is dedicated to helping women reach their full potential by fostering leadership opportunities, creating new business development platforms and facilitating mentoring relationships. She has been recognized as one of “New Jersey’s Best 50 Women in Business” by NJBIZ business journal and as a “Woman of Note” by the New Jersey Society of Certified Public Accountants. She was also named a “Working Mother of the Year” by Working Mother magazine in 2012.

Rosalie can be contacted at: 973.577.2316 or rmandel@rkco.com

Stacey Schell is an audit principal based in Rothstein Kass’ New York office. Stacey provides financial reporting, tax and accounting services to clients in the financial services industry. She specializes in domestic and offshore investment partnerships, master feeder structures and funds of funds that employ a variety of investment strategies.

Stacey can be contacted at: 917.438.3996 or sschell@rkco.com
About Rothstein Kass

Rothstein Kass provides assurance, tax and advisory services to hedge funds, funds of funds, private equity and venture capital funds, broker-dealers and registered investment advisors. The firm is recognized internationally as a top service provider to the industry, and consults on a wide range of organizational, operational and regulatory issues. The firm also advises on fund structure, both inside and outside the United States, compliance and financial reporting, as well as tax issues from a federal, state, local and international compliance perspective.

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