

HEIDRICK & STRUGGLES

Hedge Fund Industry Trends: 2009 and Beyond



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General Market Observations

- Tremendous turnaround year for hedge fund survivors, marking their best returns in 10+ years, with average returns estimated at 15%-20%, and approximately half of survivor funds 'underwater' having reached their high-water mark.
- By Nov. 2009, industry re-crossed \$2 trillion mark, largely due to performance versus net inflows. After first four months of net outflows, 2009 ended with eight consecutive months of investor inflows, *estimated at \$150 billion* (versus approx. \$1 trillion of outflows in 2008 and 2009).
- Hedge fund net inflows expected to increase as funds of hedge funds, pensions and endowments continue to reduce cash reserves. Sovereign wealth fund allocations also being watched with keen interest. And according to a recent *Morgan Stanley Quarterly Investor Survey*, blue chip managers will once again close their funds to new capital.
- But Pyrrhic victory for the industry on the whole. Over 20% of hedge funds shut down in past two years, with approximately 1,500 liquidations in 2008 and 900 in 2009. Additional firm closures are expected in Q1 2010; in particular those firms under \$1 billion and underwater are especially vulnerable. "Just about all long/short candidates approached about an opportunity were willing to listen as long as the hiring firm had stable capital," says one search consultant. Direct impact on talent flow in 2010 as top talent seeks high quality stable firms and platforms in what is expected to be a very bullish Q1 hedge fund labor market.
- New hedge fund launches exceeded number of liquidations starting in Q3 2009, with 224 launches in Q3 and over 550 in 2009 (versus 1,400 launch average for 2002- 2007). Most launches were Equity Long/Short funds, but approximately 65 Macro launches as well, and an increase in Event Driven start-ups as M&A activity expected to continue to rebound in 2010. Reputations and track records of start-up managers at all time high – due in large part to hedge fund scandals and to very poor 'absolute return' performance in 2008 for many managers – making it tough for all but the bluest chip managers to raise significant capital.
- Risk-reward return profile of hedge funds in 2009 more in line with expectations: Hedge funds hedging in down and up markets. Market and traditional asset management performance negative through H1 2009 while hedge fund performance through H1 2009 was positive. In H2 2009, survivor hedge funds performance nearly in line with broader indices.
- Strategies for which most investment professional hiring occurring: Liquid and low leverage strategies in general, in particular Macro, Credit/Debt, Long/Short Equity, CTAs, high frequency trading, quantitative strategies.
- Senior top talent available inventory decreasing as hedge fund investment professionals re-surface at other hedge funds, proprietary trading banks, asset management firms, pensions, endowments, foundations, family offices, incubation/seeding platforms, sovereign wealth funds and most recently the SEC. Disproportionate inventory

reduction for Long/Short Equity PMs, Credit/Distressed and Macro PMs relative to other strategies.

- Year 2009: Asset building/Re-building Frenzy, through 1) Retaining assets, 2) Fresh money with a high-water mark re-set, 3) New distribution channels.
- Hedge funds attracting capital by: 1) Performing well and having strong perceived infrastructure/operations; 2) Hiring marketing personnel; 3) Strategic CIO hires/merging endowments into hedge funds (ex: Perella Weinberg/University of Colorado); 4) Entering CIO outsourcing business; smaller endowments more likely to consider outsourcing options; 5) Launching new products to reach new/retail client bases. For example: UCITS funds (Ex: Marshall Wace, Brevan Howard, Blacksquare, etc. and fund of funds targeting UCITS funds); 6) Setting up Long/Short Equity mutual funds (GLG, Cantillon, Two Sigma, Bull Path, AQR, Lauren Templeton, etc); 7) Setting up structures and transparency and liquidity terms that investors favor; 8) Continued activity regarding Separately Managed Accounts (SMAs) for hedge funds and fund of funds.
- SEC's recent focus on enforcement of already existing trading rules and newly-established Division of Risk, Strategy, and Financial Innovation auguring in a new era of increased government enforcement, and commitment to better understanding/review of risk management, structured finance and corporate transactions. Hiring hedge fund and markets specialists/veterans whose skills are on par with those in industry expected to continue in 2010.
- Hedge fund fees are not changing materially for survivors who are performing well. Changes for hedge fund business model generally incremental. More substantial changes around liquidity, leverage, redemptions/gating and transparency. Key decisions being made re: outsourcing versus self-administration of back/middle office processes/reporting especially in attempts to attract/keep investors.
- Hedge funds have meanwhile suffered in terms of reputation first due to poor 2008 'absolute return' performance, then due to handling of investor redemptions and suspensions/gating, also due to large number of firm closings, and also to series of scandals. This despite the fact that hedge funds performed twice as well (half as badly) as the broader markets and many of the traditional asset managers on average in 2008 and nearly as well as broader markets in bull market run for 2009, and much better than broader markets in H1 2009. Lifting of gates in Q3, Q4, along with strong 2009 hedge fund performance, should ease some of the reputation damage. In addition, it is estimated that hedge funds provided 40% of bailout money/capital infusions to help stabilize banks. Hedge funds remain top investment bank client.
- From talent perspective, real beneficiaries of severe hedge fund disruptions: hedge funds perceived to be stable, well-organized, well-managed and well-aligned internally and with investors; post-TARP proprietary trading desks at banks that earlier in 2009 had lost "strong revenue generators" and witnessed "exodus" of top talent. Also expect continued hedge fund hires by asset management firms, some pensions, endowments, and foundations, some family offices and incubation/seeding platforms, some sovereign wealth funds and the SEC.

Search/Recruiting Activity

- Q1: Little/no search activity post Lehman demise and little emerging manager/hedge fund activity. Exception: The relatively few funds that performed between -5% and positive performance in 2008 have been making hires since beginning of 2009. Bridgewater, Brevan Howard, Millennium, Moore Capital, Diamondback, Paulson & Co, King Street, Soros, BlueCrest, Balyasny, etc. Some funds that did not perform well but that are very well known with long histories/track records and large asset bases also hired actively.
- Q2: Hedge funds started to make hires; pick-up in hedge fund formation activity. Still some 'waiting for the dust to settle' and 'fence-sitting.'
- Q3: Employers who held onto the viewpoint that "the talent pool will only get richer over time" more active in hiring and taking advantage of the available talent. In addition hedge funds now competing for talent with non-hedge fund firms: no more fence-sitting except for funds with <=\$2 billion and still significantly underwater. Active summer in terms of hiring and fund launches. Meanwhile bank brain drain: Hedge fund launches from every major bank (DB, Citigroup, CS, GS, x-Lehman/Barclay's, Soc Gen, Macquarie, etc); pay and trading concerns drive traders from banks.
- Q4: Significant increase in hedge fund hiring across all functional roles, especially portfolio management and marketing/distribution. Talent inventory for Senior Long/Short Equity talent decreases significantly, we estimate over 80% of Long/Short Equity PM and Global Macro talent and Marketing/Distribution professionals re-absorbed and in good/stable employment situations; around 50% available Event-Driven Senior talent re-absorbed into similar such situations.
- Q4 and 2010: Post-TARP bank brain-drain reversal of fortune. Continued significant increase in hiring at most large banks/proprietary trading firms; hedge fund talent also being absorbed by asset management firms, family offices, pensions, endowments, foundations, incubation/seeding platforms, sovereign wealth funds (ex: C.I.C and S.A.F.E.) and most recently the SEC. We expect compensation bidding wars to return in 2010 though not at the levels prior to Summer/Fall 2008.
- Long/Short Equity talent being absorbed throughout the industry, from the largest firms (SAC, Millennium, Citadel, etc.) to proprietary trading banks, asset management firms, sovereign wealth funds and seeding/incubation platforms. Global Macro talent being absorbed by large macro firms (Brevan Howard, Moore Capital, etc) and by estimated 65 new Macro fund launches in 2009.
- Emergence/Re-emergence of Seeding funds: Blackstone Alternative Asset Management and Morgan Stanley's newly launched incubation vehicle in Q4 and numerous other incubation funds. Also, significant lift in funding of emerging managers by legends of the industry: Tiger Management/Julian Robertson, Soros/George Soros, SAC/Steven Cohen, Millennium/ Israel Englander, Blackstone, Man Group, Citadel/PioneerPath Capital. Seeding platforms and incubation platforms actively set for 2010 deals.

- Top tier, new fund launches in Equities, Macro, Commodities, from best pedigreed players: Tudor, Raptor, Moore SAC, Pequot alumni, etc. Only ‘A’ players getting funded, ‘B’ players no longer getting funded. Shift however from 2008 multi-billion dollar launches to 2009 hundred million dollar launches. We expect to see recently launched funds reach the billion dollar mark more regularly in 2010, though not with the frequency of 2008 launches and as a result of performance combined with raises.
- Well-known existing high profile hedge funds launching new funds: AQR, Brevan Howard, Paulson & Co, Marathon Asset Management, Citadel, Harbinger, Kellner Dileo, Ospraie, Tontine Partners, Raptor Capital, Noble Partners, Caxton.
- Throughout the year we have also seen continued activity in classic Business Development/Strategic Planning roles. These BD roles continually evolving as the industry evolves. In BD roles, candidate typically spending portion of time on core internal operations, from marketing to operations and personnel, and majority of time on new business development – from seeding deals, to strategic fund raising, and associated new structures (ex: UCITS, Long Only funds, SMAs, global initiatives, etc) to tap into new assets and allocations. Such BD roles are sometimes held by the current or incoming firm or divisional COO.
- Marketing/distribution hiring has been extremely active throughout the year -- with continued need for experienced sales and marketing professionals -- as firms hoping to capture sidelined assets, new assets (ex: retail) and assets from poorer performing funds. Firms are gearing up for the “best fundraising opportunity in two years.” Demand for marketers with corporate and public plan track records is very high.
 - Q4 hiring included: Kane Anderson, Highbridge, OchZiff, Atlantic, Jana, Lanexa, DE Shaw, Bridgewater, AQR, Fir Tree, Citadel, Millennium, Blackstone (BAAM), Carlson Capital, Marshall Wace, MSD Capital, New Mountain Capital, Renaissance, Marathon, Blue Mountain, Stonewater Capital.
- Q4 functional/asset areas with pick-up in opportunity after significantly decreased activity:
 - HR: By Q2 2009 the number of dedicated HR/recruiting personnel within hedge funds had contracted significantly; many hedge funds laid off all but their most senior HR/recruiter personnel; In some cases, valued HR/recruiting personnel shifted into other roles (special projects, investor relations); Several of the largest and most sophisticated in-house recruiting teams within the hedge fund community were downsized by 40+%; By Q3 2009 downsizing had stopped, but most hedge funds had no plans to grow their HR/recruiting teams through the remainder of 2009. Bank and hedge fund human resources and recruiting hiring picked up slightly from what has been an essentially contracting market for much of the year. More hiring expected in 2010 for these functional roles.
 - IR: Client interest in Investor Relations picked up in Q4 as well after several quarters of slow hiring activity, especially when compared to marketing/distribution.
 - More mandates for movement and upgrades in COO, CFO, and COO roles.

- Fund of hedge funds situation has improved in Q4 after very tough year, though core fund of fund value propositions in need of fundamental re-evaluation. Little activity in fund of fund hiring, with a few exceptions among the largest fund of funds. Globally we are seeing consolidation and emergence of 'Top 5' fund of funds that are actively hiring and growing.

Asia



- Growth has reemerged in the Asia hedge fund space with the Asia Region (ex-Japan) witnessing the most dramatic turn-around of any region.
- Widespread retrenchment from Asia in Q1, Q2 2009, a number of global funds closed offices or reduced their presence in Hong Kong & Tokyo. By Q2 2009 very few global funds remained with an Asia presence. In Q3, some large non-Asia firms focused/re-focused on Asia/Middle East again: Brevan Howard, DE Shaw, Millennium, OZ, SAC, Gottex, etc.
- Q4: Asia took the global lead for fund launches which re-emerged at a faster clip than in any other region. According to industry figures, there were 50+ Asia-focused hedge fund start-ups in 2009. Deutsche Bank has been tracking 45-50 Asian hedge fund startups that have or will have started investing in 2009 through Q1 2010. While Asia start-ups average asset size remains small (up to \$25 million), a number of managers have started with \$200-\$300 million: including Nick Taylor/Citadel, at \$220 million; Senrigan at \$220 million+.
- Asia leads HF recovery as the strongest performers rising 34% (ex-Japan). Hong Kong is the most active place in Asia while Australia is growing and Japan remains quiet, according to prime brokers and executive search consultants.
- In addition to new launches, there is renewed interest from overseas funds, primarily Long/Short Equity, looking to base research and trading capability on the ground in Asia.
- Increased attention on Asia Event-Driven investment strategy: new and existing funds marketed themselves as event-driven funds at Goldman Sach's Asia Hedge Fund conference (10th/11th Nov, Tokyo), those participated in the event-driven panel were Matchpoint, Black's Link, Isometric, Front Point, Owl Creek, York, and Thaddeus. Japanese platform Sparx is also in the process of revamping its event-driven arm.
- Stark Investments, \$7 billion manager based in Milwaukee, is preparing to open a Hong Kong office after its Asia team spun off an independent firm. Neuberger Berman is considering providing start-up capital to hedge funds in Asia as it expands in the region. Fortress considering acquiring Galleon staff.
- Significant attention is still focused on the new 'second generation' home grown Asia Equity & Credit funds that are emerging. Previously many Asia offices of global funds had been formed by a non-Asia portfolio manager moving from overseas. The one to two winners out of the five or so that are launching in equity and in credit will likely go on to dominate the Asia landscape in two to three years' time.

- Difference between these funds & the prior generation is that they are generally being founded by very experienced Asia portfolio managers/prop traders. Example: Equity/Event-driven: Nick Taylor (ex Citadel/CS Modal), Paul Penkert (ex Lehman prop), Shafiq Karmali (ex GSPS), Hari Kumar (ex TPG-Axon/GSPS). Credit/multi-strategy: Mark Devonshire (ex Merrill prop), Edwin Wong (ex Lehman prop), Raaj Shah (ex OchZiff), Adrian Pizer (ex UBS prop), Teall Edds and Stuart Wilson (ex Stark Investments). Another major difference is the type & size of launch, most of the above are launching with app. \$50 million and looking to grow via performance versus taking seed deals.
- Chinese sovereign wealth funds hire senior US hedge fund talent: C.I.C. taps Ex-Tudor Manager to Run its Portfolio; Pimco Hedge-Fund Manager Zhu Joins China's State Administration of Foreign Exchange (SAFE). Meanwhile large Chinese institution "on the prowl" to acquire as many as five US hedge fund operators, search for managers with at least \$500 million AUM.
- Asia fund of funds have seen consolidation: PAAMCO acquired KBC's Asia FoF, Duet acquired Investor Select Advisors, and other FoFs are in active talks with potential buyers.



Europe

- Most strategies in Europe have rebounded very well in Q4, and assets continue to return to many of the larger European funds. The rebound from previous quarters has been dramatic. The following firms for example had all lost more than 50% of their assets in the first half of the year: Bluebay, GLG, Marshall Wace, Polygon, RAB and TCI. And there are numerous examples of London offices of US funds having closed down in the first half of the year.
- Strong performance into Q4 from many of the leading European multi strategy hedge funds: BlueCrest's Capital International fund understood to be up 41% (December), CQS' Directional Opportunities Fund up 48% (December), and Jabre's Jabcap Multi Strategy flagship fund is up 70% through November 2009.
- Several big name funds have returned to the market to invest in new investment talent - Millennium, TCI, Tudor, Moore, BlueCrest, Soros, SAC. Similarly, several of the bank prop desks are staffing up in Europe. Particular focus: Event driven and Equity Long/Short.
- Long/Short Equity was the most popular strategy with investors, as with all regions. Event driven strategy also on the rise.
- European assets are returning to the fund of funds market but, as with US, there is heavy concentration of allocations to the more established institutional US players: Blackstone, Ivy, PAAMCO, Grosvenor, Mesirov. At fund of funds level we have also seen an increase in demand for operational due diligence professionals and a general overhaul of this function.
- Increased number of European search mandates on the investment side, with continued activity coming from COO, CFO, risk, compliance/legal and marketing/client servicing.
- Until Q4, a dearth of large European hedge fund launches. While Asia took the lead in the number of Fund Launches, European startups are now attracting the most interest from investors, according to data compiled by DB PB unit. Europe's average asset size for fund launch: \$150 million - \$300 million vs \$25 million - \$50 million in US.
- Tyrus Capital, which is being launched by Tony Chedraoui and his team from Deephaven, one of the larger launches. Much anticipation around Belay Partners, the new long short fund being launched by Harry Tyser (ex New Star and Marshall Wace) and Daoud Zekrya (ex Marshall Wace).
- There remains strong demand for marketers and several of the leading European and US funds operating in London are searching for marketers. According to many of our marketing and capital introduction sources, Q4 has seen more capital returning to hedge

funds than any other quarter this year. Many top funds are closed having reopened briefly following a wave of redemptions earlier in the year.

- In addition to hiring marketing talent, another means of attracting capital is through UCITS versions of funds. Growing opportunity to offer absolute return product sales into private clients and small institutions via UCITS: Brevan Howard, GLG, Marshall Wace, Blacksquare have all set up UCITS versions of their funds.
- Like the US, Europe has seen an increase in the level of activity of family offices, endowments, foundations and pension funds. However, relative to the US, investments are being made more at a fund level rather than direct investments.
- London remains the European hedge fund center, however considerable number of London-based hedge funds are considering partial or entire relocation outside of London and the EU. The destination of choice at this stage is Switzerland. BlueCrest announced earlier in the quarter that they intend to relocate 50 of their staff to a Geneva office. We understand that Brevan Howard also intends to open a Geneva office in the near future.
- As governance becomes increasingly important we have witnessed an increase in demand for non executive directors/chairmen and independent advisors.

Front Office Compensation Activity

- *In 2009, compensation bands for senior level portfolio management and marketing/distribution roles broken and depended on whether fund was underwater or not, and whether underwater fund had modified high-water mark or not.*
- *Formulaic payout structures for PMs remain strong and expected to continue to remain strong in 2010 as various platforms compete for and retain senior investment talent.*
- *Guarantees in 2009 much less prevalent than in the past, though still for senior level/best marketing talent, especially in instances where candidate received multiple offers. Strongest 5-10% of senior marketers secured significant guarantees, with another 20-30% of mid-to-senior hires having secured minimum floors.*
- *Return of guarantees expected in 2010, although increase in clawbacks and deferrals also expected. Also, factors other than compensation continue to influence individuals for all roles as stability of hedge fund capital base, management expertise/reputation and alignment between allocators/investors and both GPs and Employees assumes greater significance.*

Compensation: Sales/Marketing

How are compensation packages being structured?

Base salary: The majority of sales & marketing professionals who accepted offers in 2009 did so within a base salary range of \$150,000 - \$250,000. On average base salaries have held steady from 2008 levels, though many individuals experienced an increase or decrease, depending on the type of firm they were transitioning to.

Guaranteed bonuses: A small percentage of mid to senior level candidates secured a significant guaranteed bonus. Seven figure guarantees for 2009 were reserved for the top 5 - 10% of senior level talent, with multi-year guarantees secured in just a handful of situations. Typically these seven figure guarantees were offered to highly regarded heads of distribution or individual contributors who had discernable and successful multi-year track records of raising assets even in difficult markets, and who joined firms at the front of the pack from a performance and pedigree standpoint. These seven figure bonus guarantees ranged from \$1 million to \$3 million per year.

Minimum bonus floors: These were secured in 20 - 30% of job moves. Typically, candidates regard these floors as an insurance policy and gesture of strong intent, but these offers do not make them 'whole' from their previous compensation levels. Any potential upside beyond the minimum floor will be discretionary. Minimum floors ranged from \$200,000 - \$600,000.

Discretionary bonus: The majority of sales & marketing talent (60%) accepted offers of base salaries plus a purely discretionary bonus. Expectations for these discretionary bonuses are all over the map, and largely reflective of uncertainty around Q4 fundraising and fund performance for the remainder of the year.

Commission bonus: In 10 - 15% of situations, a formulaic / commission structure will be the sole determinant or a component of an individual's end of year bonus. The debate continues about whether these commission structures result in better fundraising performance and whether they are being implemented to a greater or lesser degree – we were not able to determine market consensus on this issue.

Equity: It remains extremely rare for candidates to be offered equity walking in the door, with the exception of senior individuals entering into highly entrepreneurial situations. A small percentage of sales and marketing professionals expect discussions around equity to be on the table after one or two years with the firm.

Compensation: Portfolio Managers

How are compensation packages being structured?

Base salary: The majority of PMs who accepted offers in 2009 did so within a base salary range of \$150,000 - \$300,000. On average base salaries have held steady from 2008 levels.

Payout salary: The majority of PMs who accepted offers in 2009 did so with a payout formula of 12%-20% of the P&L, with a large number of funds paying at the 15% mark. These relatively high payouts have remained in tact/have not changed since 2007-2008 when many of these ranges were originally set to attract/retain PM talent. At the larger more established firms, PMs do not assume netting risk, and therefore can earn a payout even if other teams perform poorly.

Allocations: Range from \$50 million - \$500 million, mostly in the range of \$75 million - \$350 million.

Expense allocations: Most funds allocate expenses to PMs. Expenses can include cost of capital, compensation for team members, and variable costs associated with running a PM's P&L. Overhead/seat charges are rare.

Guaranteed bonuses: A very small percentage of senior level candidates secured a significant guaranteed bonus.

Minimum bonus floors: A very small percentage of senior level candidates secured a significant guaranteed bonus.

Discretionary bonus: PMs at established funds in excess of \$10 billion sometimes participate in profit sharing pools.

Equity: It remains extremely rare for candidates to be offered equity walking in the door at large and/or established funds.

Hedge Fund Talent Flow 2010

With significantly increased competition for top hedge fund talent in Q4 2009 and an active hiring market expected in Q1 2010, especially at hedge funds, proprietary bank desks, and hedge fund incubation/seeding platforms, we expect to see a clear talent flow trend where hedge funds with certain characteristics will lose their senior most talent and where others will retain their investment professional talent.

Based on a Q4 2009 survey of Long/Short Equity PMs in the industry, we have divided firms into two categories.

I. FIRMS WHERE TALENT IS STABLE

The following characteristics are shared by firms from where it is difficult to pull talent:

- 1) **Strong individual performance** (and strong firm performance when manager netting risk exists)
- 2) **Fair /well-run management, good and transparent work environment and interests well aligned between GPs, LPs and employees**
- 3) **P&Ls/books not heavily restricted; Relative autonomy**
- 4) **Access to sizeable capital that is stable**
- 5) **Lucrative/competitive payout models**

Succession Planning and Location in some instances is also a key factor. Some PMs aspire to eventually run a firm so succession planning may be a factor. Location can also be a factor. California (SF, LA) and Boston locations, for instance, are geographies where it is sometimes difficult to relocate talent. Though it should be noted that 2009 saw a significant number of candidates making geographic moves for the right opportunity given that opportunities were few and far between.

In most cases it is very difficult to pull out a strong performer especially when a firm provides most/all five pros listed above. One PM said he would be "shocked" if anyone from his firm raised their hand for another opportunity because they have all the pros discussed above. A PM at another firm but in a similar situation said everyone seems "glued to their seat" and very happy. A Sector PM at this same fund said "I am never leaving as long as they have me." At yet another firm with stable capital (significant portion is GP money), a PM would not consider a move unless the opportunity had \$1 billion of capital with good economics and a good work environment (simply little incentive to leave).

So what would it take to pull a strong performer from such a situation that meets most/all of the criteria he/she find important?

In a case where most/all pros are offered, a 'game changing' opportunity would be needed. Examples of game changers:

- Very significant increase in capital allocation or responsibility
- Upgrade to more distinguished top-tier institution/firm with many/most of the factors listed above
- Opportunity to build firm as well as invest, and/or opportunity to be key part of a firm's succession plan
- Opportunity to serve a cause while investing: Major endowments, sovereign wealth funds, and the SEC have made key hires in 2009 where candidates were attracted to the cause /mission associated with the institution as well as the investment opportunity
- Significant/sufficient capital to start own fund or significant allocation on a well managed platform with competitive and transparent economics

II. FIRMS WHERE TALENT IS VULNERABLE

Clearly, these firms would lack some or all of the five characteristics of firms from where talent is stable. However, in surveying PM candidates we identified the following eight key characteristics of firms where talent is not locked in.

- 1) **Firm underperformance:** Clearly a main driver of talent flow: However there are two types of underperformance. PMs underperformance and/or firm underperformance but where the PM has performed well. Please note that for this Report we focus on the latter situation only, though it should be noted the former situation – PM underperformance – is often what causes the most noise in the marketplace and these candidates make use of the factors listed below as reasons for wanting to seek new opportunities.

The easiest targets are firms that have not reached their high-water mark. We have found that loyalty to a firm lasts about two years (two consecutive years of little/no bonus with uncertainty regarding year three bonus) unless one is a senior member of the firm where significant personal wealth accumulation has already occurred. In 2010, many funds will have reached this two year mark.

- 2) **Firms without formulaic payouts for PMs:** Situations where there was no formula but more of a handshake deal or subjective payout. Given the opportunities that will be available in Q1 2010 and given recent events, this type of deal could be less acceptable for many high performing PMs.
- 3) **Firms where portfolios are shared:** While not eager to leave, most candidates who share a portfolio are open to discussions. High performing PMs perceive a mismatch between economics and contribution levels for higher level performers, though it should be noted that no mismatch is perceived when firm performance exceeds individual PM performance.
- 4) **Traditionally centralized structures:** A structure where PMs don't run specific books but instead contribute their sleeve to a multi-strategy fund or to a Senior PM/Founder/CIO. People here may be inclined to look for portfolio autonomy elsewhere. Some Senior Analyst/ Junior PM level talent may face a cap on development and autonomy at certain firms as well. Several PMs and Analysts

explicitly thought highly of their current firm but knew they would not get their own books so are open to discussions.

- 5) **Firms with dramatic top-down changes to structures:** Firms where trigger-pulling responsibility was yanked from individual PMs and former PMs were asked to work as Analysts contributing ideas. This change typically took place during times of poor performance/market turn. During the downturn some firms changed their PM compensation structure from formulaic to an entirely discretionary model. In another instances, some firms responded to market conditions by standardizing previously non-standard payouts/contracts.
- 6) **Placeholders:** Firms which are somewhat outside the norm for hedge fund PM talent but who have housed successful PMs from firms that shut down. Now that the market is in recovery, those PMs may want to get back to a hedge fund.
- 7) **Firms under \$1 billion:** Individual and team moves from firms with lower capital and capital raising trouble to multi-billion dollar firms. Exceptions are the more recent 2009 start-ups with sizeable assets under management.
- 8) **Hedge funds undergoing significant internal 'event driven' structural change:** Mergers and acquisitions within the hedge fund industry will, unless handled well, create instability for individual P&L performers and lack of clarity. Lack of clarity/vision or lack of communication from the top down during such extraordinary internal events/times makes top talent especially vulnerable: Employees become unsure of what economics will look like; some concerns around stability of capital and management.

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