



Alternative Asset Management Industry 2015 Industry Update

Convergence is pleased to present our 2015 annual research insights into the Alternative Asset Management Industry¹. Our data and analytics are sourced from 15,000 Form ADV's and Brochures filed by Non-Exempt and Exempt Investment Advisors for the 12 months ended March 31, 2015. Our report focuses on business trends among alternative asset managers along with related assessments of changes in operating complexity and risk, and changes in operating productivity. During the first quarter of 2015, 11,981 Advisors filed updated ADV's, or 79% of all advisors. And during the year, 21% of all Advisors filed updates citing material changes to their business model.

The proliferation of new products and new distribution channels along with increased demands for transparency has significantly altered the demands on the infrastructure² of alternative asset managers. These trends lead to greater operating “complexity”, which results in more process requirements and higher operating costs in order to address a higher level of operating risk. It has become increasingly common for investors and allocators to spend more time and attention on operations-related due diligence efforts than on portfolio management matters. Convergence has developed proprietary methods to collect and enrich data to help managers, investors and service providers understand levels of operating risk within and across managers of different sizes and investment styles.

Complexity = Risk = Additional Work = Cost (™)

The Convergence Complexity Index (CMDX-CI™), tracks 15 complexity factors that provide insight into the complexity in the Alternative Asset Manager and how those organizations compare to others in the industry with the same level of complexity. Together with our Staffing and Productivity benchmarks we can correlate complexity, operational workload /cost, risk and productivity. With our analysis, Managers and Advisors are able to put increased focus on defining their current operating metrics, establish clear operations-related objectives, and see a clearer path to supporting the firm's growth plans. At Convergence, we believe these insights will support asset gathering activities, help improve operating margins, and reduce operating risk profile.

For additional industry insight and information, contact us, or go to www.convergenceinc.com.

¹ An Alternative Asset Manager is defined as an RIA that advises Private Funds and where the aggregate value of net private fund gross assets under management exceeds 50% of the Advisors total Regulatory Assets under Management

² Infrastructure refers to all non-investment functions and includes investment operations, fund and firm accounting, tax, risk management, compliance, legal, technology, marketing, investor relations and human resource personnel.

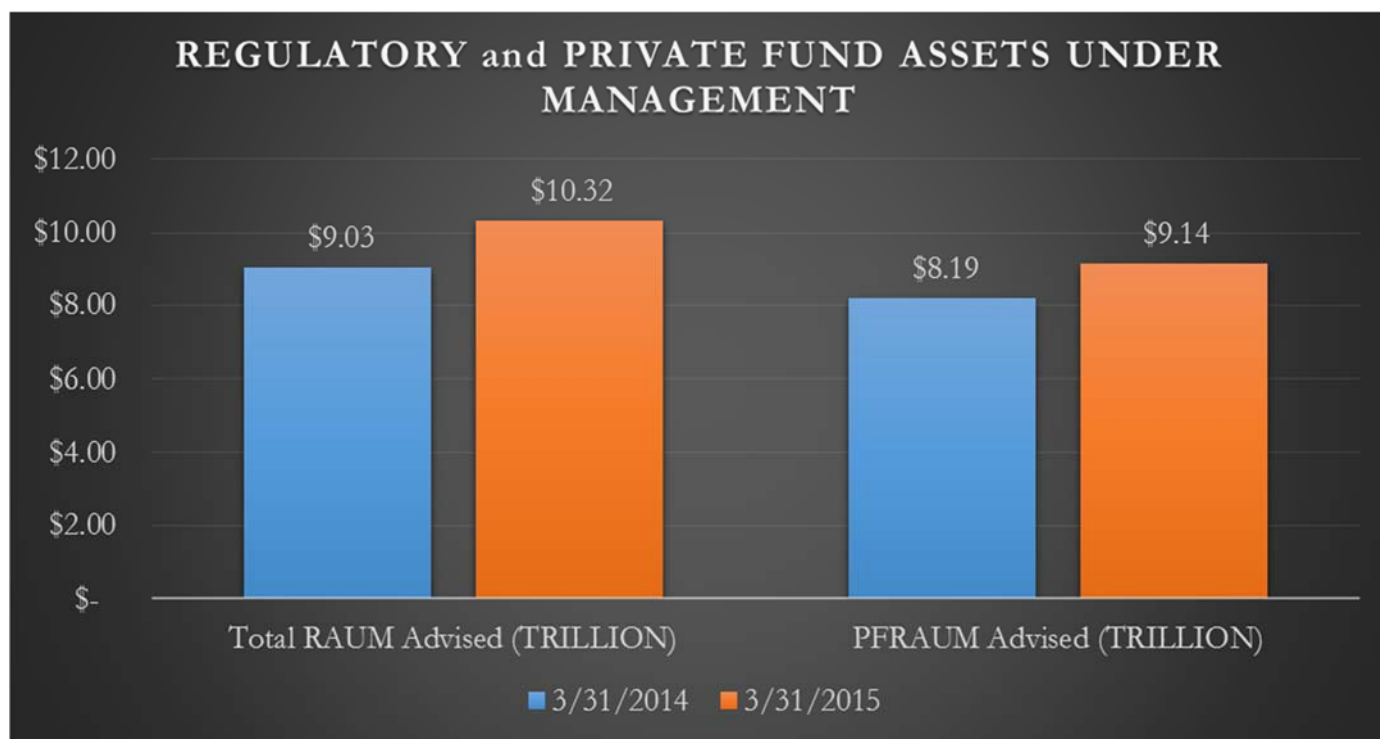
Overall Industry Growth

“Strength and growth come only through continuous effort and struggle”

- Napoleon Hill

Despite the widely reported record number of hedge fund closures in 2014, it was also a record year for new fund launches and overall asset growth. The Alternative Asset Management Industry (defined as Unique Managers³ reporting more than 50% of RAUM as Private Fund RAUM) continued its growth into 2015 with Total Regulatory and Private Fund Regulatory Assets under Management growing to \$10.3 trillion and \$9.1 trillion, respectively. The number of Private Fund Managers grew 11.5% to 4,448 and the number of Private Funds they directly advise grew 22.5% to almost 30,000.

Alternative Asset Managers also augmented their breadth of investment strategies and fund structures they advise, with 2% experiencing a re-classification by Convergence of their Primary Investment Strategy⁴ and 11% experiencing a re-classification of the Primary Fund Type⁵ they operate.



³ Unique Managers are groups of affiliated Advisors identified and aggregated by business rules and technology owned Convergence

⁴ Primary Investment Strategy is defined by Convergence based on the dominant asset classes used by the Advisor to generate investment returns.

⁵ Primary Fund Type is defined by Convergence based on Total Private Regulatory Assets under Management by Fund Type/Total Private Fund Assets under Management.

Leadership and Staffing

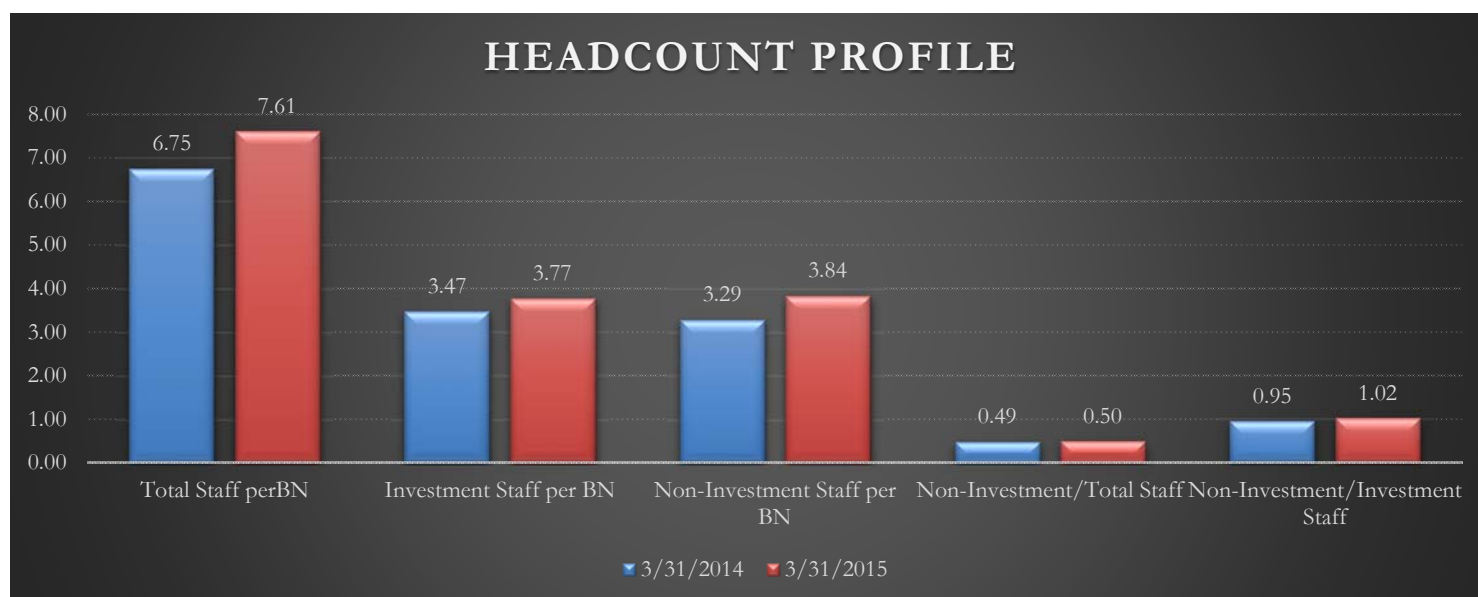
***“Lead me, follow me or get out of my way!”
– General George Patton***

Total headcount across the Alternative Asset Management Industry grew to 78,559, or 12.7%. This growth in staff is reflective of the growth in funds advised, the broadening of fund structures to capture new distribution channels and the management of increased business complexity. Staff growth of Investment Professionals was 8.8% to almost 39,000, representing 49.6% of total staff. This growth rate was outpaced by that of Non-Investment Professionals which grew at a rate of 16.8%, despite the fact that a large percentage of the middle and back-office operations are outsourced to third party service providers.

Total headcount per billion dollars of Regulatory Assets under Management increased to 7.6, or 12.7%. Growth occurred in the front and back office with Investment and Non-Investment Professionals per billion dollars of RAUM both increasing to 3.8, but growing at rates of 8.6% and 16.8%, respectively. Convergence believes there is a direct correlation between front office growth, investment complexity and operating risk. Middle and Back-office staff levels increased significantly, and can be attributed to increased compliance costs, technology costs and the ever-challenging ‘right mix’ of in-house and outsourced work.

The C Suite isn’t so ‘Sweet’

A number of managers reported changes at the top in 2015, with 5% of Managers reporting a change in name at the Chief Executive Officer level. We saw approximately 600 changes at the top, and another almost 1,000 changes combined at the COO, CFO, and CCO levels. The rate of changes reported at the COO, CFO, and CCO level were each approximately 2%. We expect to see a higher level of turnover at the COO level as infrastructure optimization becomes critical.



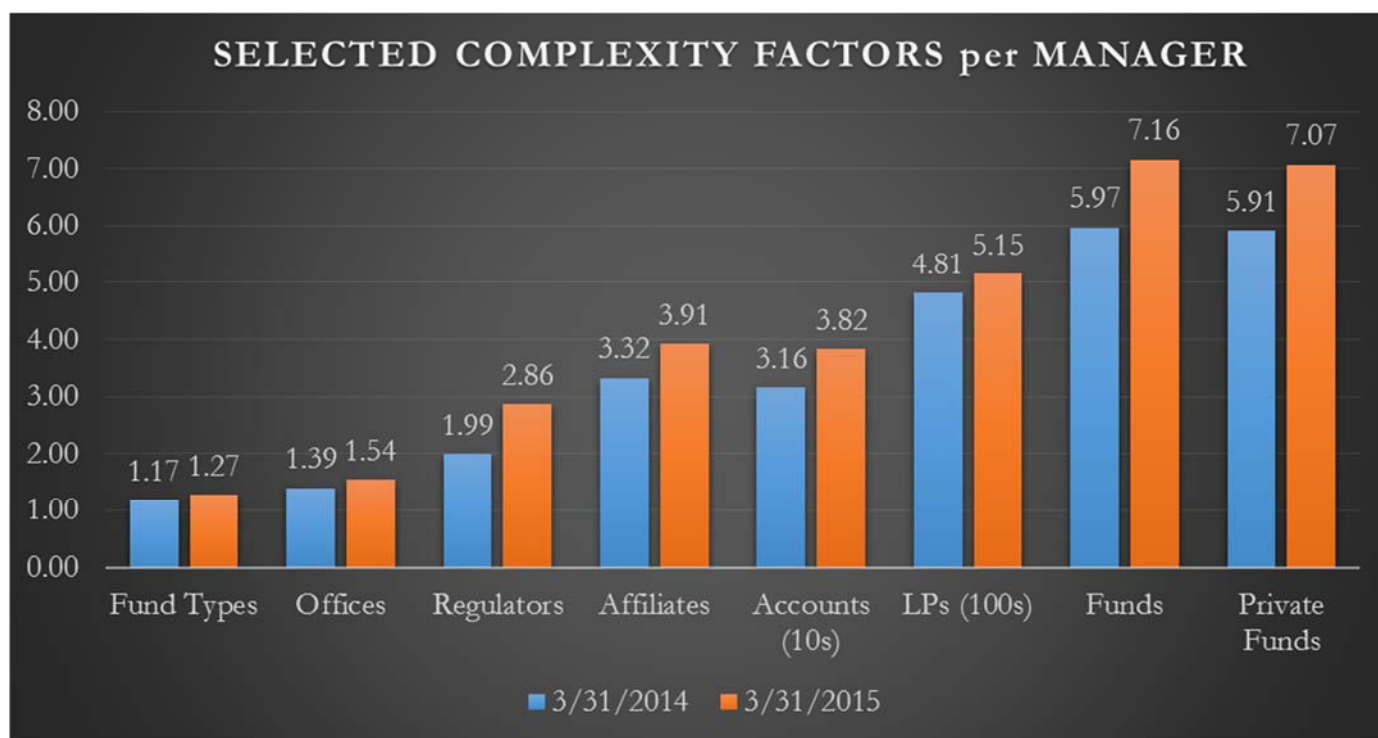
Business Complexity and Risk

“Out of clutter, find simplicity. From discord, find harmony. In the middle of difficulty lies opportunity”

– Albert Einstein

Many Advisors state that their ability to generate consistent alpha is a direct function of their ability to manage complexity. With 15,000 Advisors providing alpha and beta solutions to investors, quality investment ideas are scarce, thus requiring more Advisors to seek complexity. Investment and business model complexity increases the Advisor’s operating risk profile which directly impacts the amount of work and cost the Advisor must bear to mitigate the risk. Convergence’s proprietary complexity models track the relationship between these 4 major factors. The Convergence Composite Complexity Index (CXI) is derived from 15 features of the Advisors business model.

The un-weighted CXI rose to 39.6, or 17.1%, driven by double-digit changes in the average number of funds, fund types, regulators and office locations for all Alternative Asset Managers in our database. Managers are adding new strategies and fund types to deliver the returns and alpha expected by their investors. And to cope with the increased workload, Managers are changing existing and using more service providers.



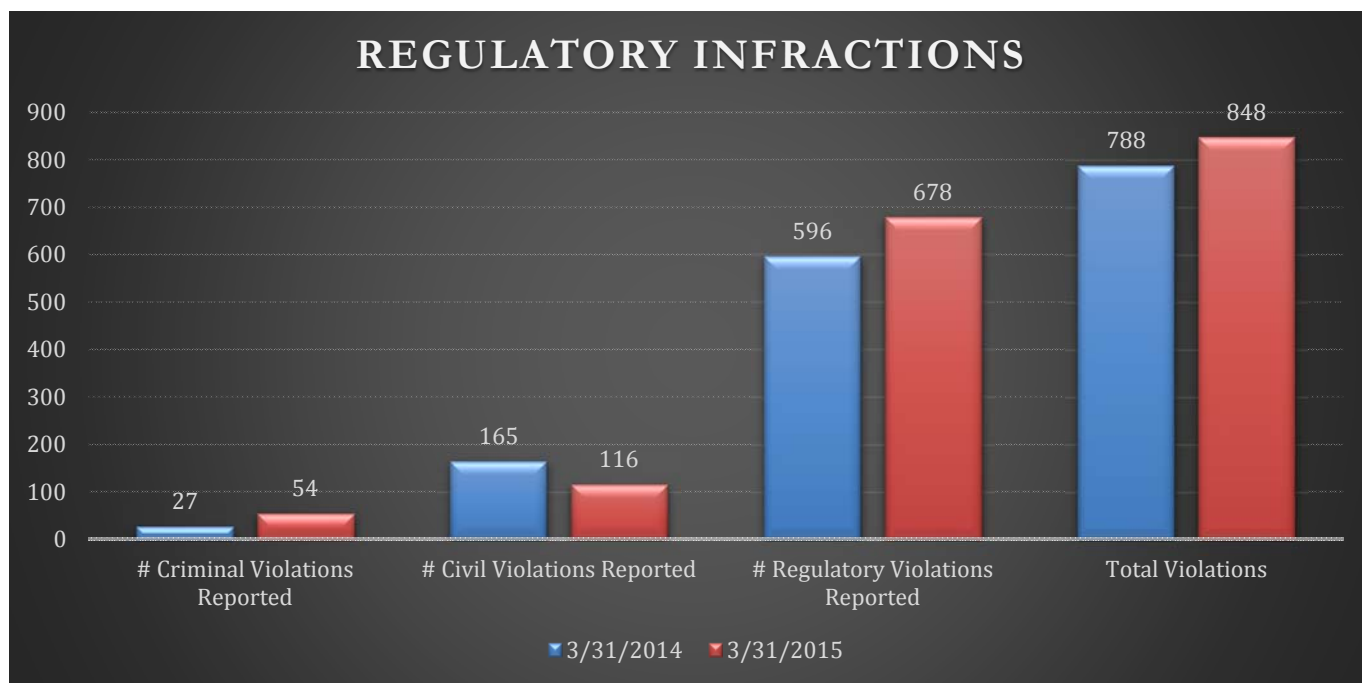
Industry Regulation

The regulatory environment is expanding with oversight from 619 authorities.

As expected, the regulatory environment has continued to grow and intensify. The average number of regulators disclosed per Manager grew 43.7% to 2.9 in 2015 versus 2.0 in 2014. This increased level of regulation largely stems from new jurisdictions where business is being conducted in order to expand new product and asset gathering activities. The number of non-US office locations per manager grew by 10%, further validating the broadening of the regulatory web in which managers conduct their business.

Additionally, the number of regulatory violations reported by managers grew 8.0% overall to 848. While the absolute number of criminal violations is small relative to total regulatory violations (about 8.3% of the total), criminal violations disclosed by Advisors are double the level of the prior year.

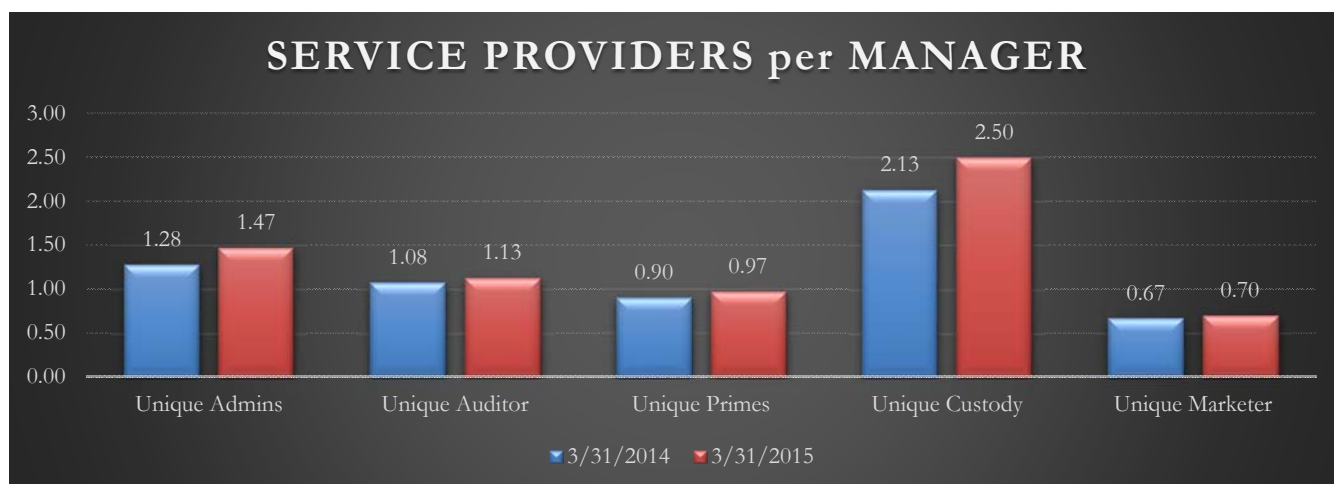
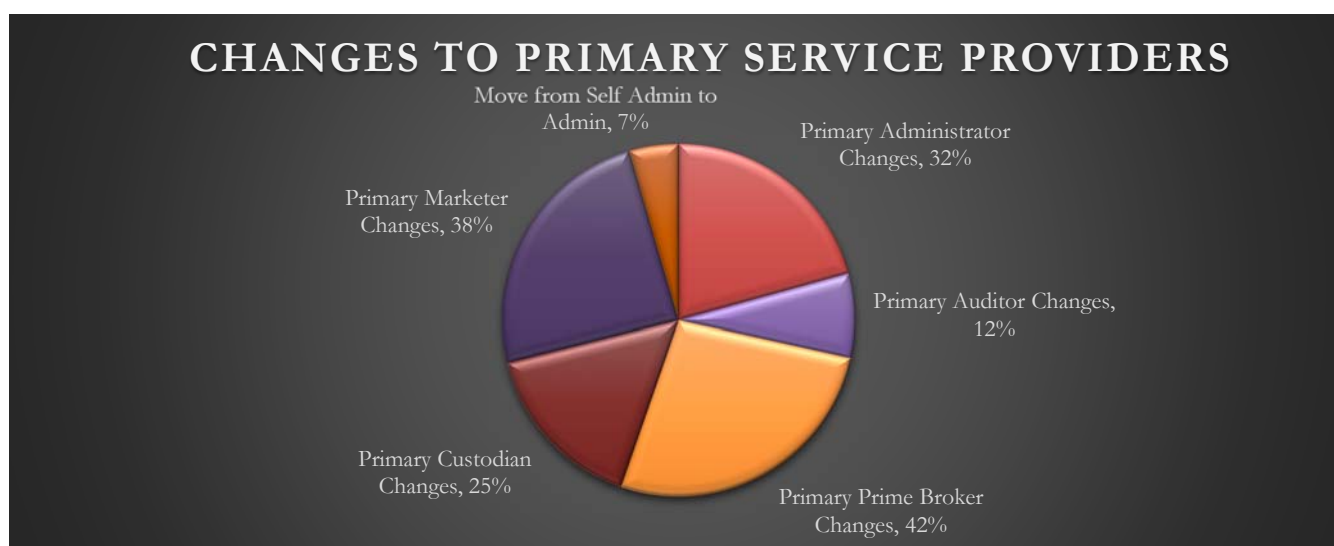
Additionally, about 3% of all Managers changed their registration status from Non-Exempt-to-Exempt driven by reductions in RAUM and firm closures, while about 5% changed their status from Exempt to Non-Exempt driven by growth above the RAUM hurdle rate and/or changes to their Fund Type and number of PE or VC funds managed.



Service Providers

The Service Provider Shuffle is on!

The Convergence Service Provider Index rose to 6.8, or by 11.7%, driven by Managers expanding the number of Administrators, Auditors, Prime Brokers, Custodians and Marketing firms with whom they do business. Driven by product changes and complexity, managers are adding service providers to manage and grow their business. The changes to a Manager's "Primary Service Provider" designation suggests Managers are willing to re-allocate business to service providers who meet their needs. The most significant changes we observed to the "Primary Service Provider" designation occurred within the Prime Brokers, Primary Marketers and Primary Administrator categories where the "Primary Service Provider" designation changed at a rate of 42%, 38% and 32% of Managers, respectively. Convergence expects that this "service provider shuffle" will continue as there continues to be consolidation among service providers, particularly in fund administration.



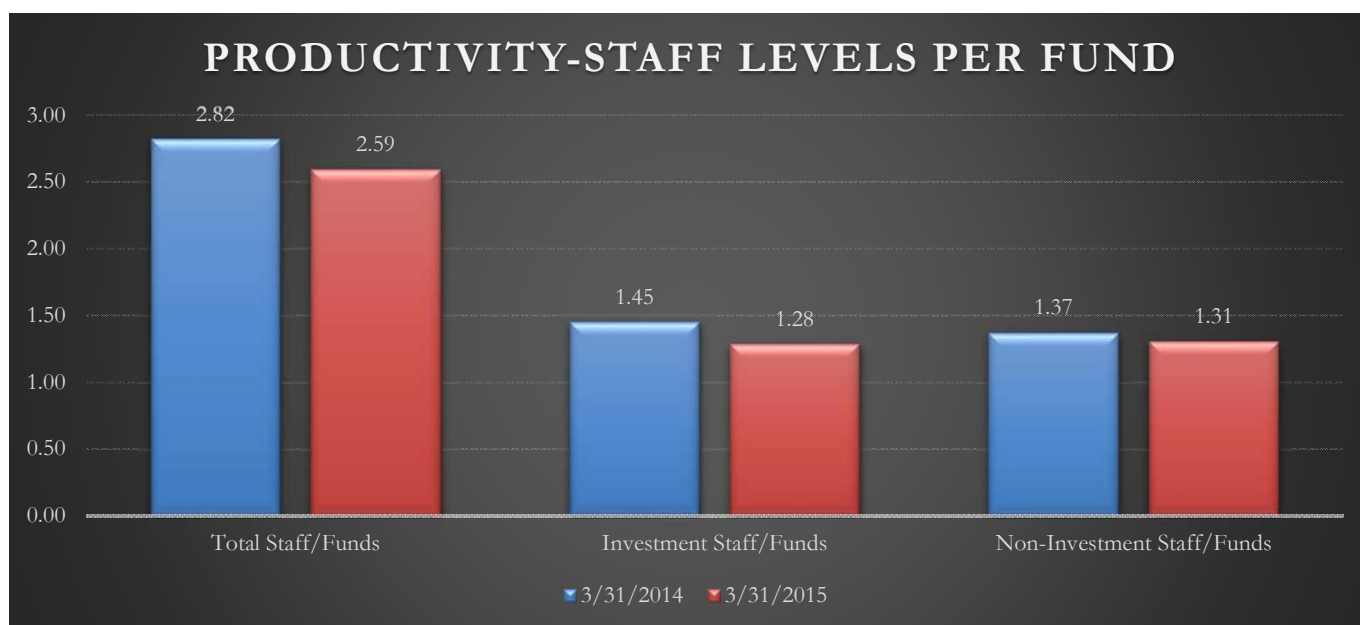
Operating Productivity

“You cannot mandate productivity; you must provide the tools to let people become their best”

- Steve Jobs

Despite the 12.7% growth in overall staff, the number of staff required to support each fund declined by an average of 8.1% year-over-year, suggesting that Managers are using more technology, more effective technology, or are outsourcing more activities, to manage the growing size and complexity of their business. Productivity gains were seen in both the front and back-office with gains of 11.3% in Investment Professionals per Fund and 4.8% in Non-Investment Professional per Fund, respectively. While staff per fund is not the only productivity measure Convergence follows, we believe it to be a solid indicator of a positive trend that we will track closely in the months to come.

Higher levels of productivity may suggest improved profitability across the industry, as measured by net management fees. Of course, managers that lower fees may be losing the benefit of this newly minted scale. Advisors and Administrators continue to focus on scaling people and technology in order to improve upon infrastructure alpha.



Convergence will continue to monitor and update all of the aforementioned industry trends to ensure that Managers and Service Providers have clean empirical data to help them focus their efforts on growing assets, maintaining or improving margins and lowering the operating risk driven by business complexity, regulation and greater calls by investors for increased transparency.