Hedge Fund Outlook

Q3 2024

August 2024

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Q2 Hedge Fund Universe Review

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Q2 markets broadly followed Q1 trends, albeit in a more muted fashion

- **Equity L/S**: Performance dispersion led to strong HF alpha
  - Big Tech continued to lead the market
- **Event Driven/Credit**: Rebounding capital market activity provides a steady backdrop for event driven strategies while signs of froth are appearing in credit
- **Macro/CTA**: Momentum reversals over the month broadly led to losses for macro/CTA strategies
- **Relative Value**: Stable performance, with asset backed and corporates leading the way

Q3 performance has been mixed due to equity market rotation

2024 Hedge Fund Universe Returns	Q1	Q2	YTD
HFRI FoF Conservative	**2.6%**	**0.5%**	**3.15%**
HFRI FoF	**4.2%**	**0.6%**	**4.8%**
HFRI HF Composite (Fund-weighted)	**4.4%**	**0.7%**	**5.1%**
HFRI Equity	**5.1%**	**1.0%**	**6.2%**
Long/Short Directional	5.2%	0.9%	**6.2%**
Market Neutral	4.3%	1.9%	**6.3%**
Quantititative Directional	9.0%	2.3%	**11.5%**
Multi-Strategy	5.8%	0.2%	**6.1%**
HFRI Event Driven	**2.3%**	**0.5%**	**2.8%**
Activist	5.6%	-4.6%	**0.8%**
Credit Arbitrage	4.4%	1.6%	**6.1%**
Distressed	2.6%	2.0%	**4.6%**
Merger Arbitrage	0.3%	0.0%	**0.3%**
Special Situations	2.0%	0.5%	**2.5%**
Multi-Strategy	1.9%	1.5%	**3.5%**
HFRI Macro/CTA	**6.3%**	**-0.8%**	**5.4%**
Active Trading	3.1%	0.9%	**4.0%**
Commodities	4.5%	-1.0%	**3.4%**
Currencies	1.3%	-0.4%	**0.9%**
Discretionary Thematic	1.7%	1.3%	**3.1%**
Systematic	9.7%	-1.7%	**7.8%**
Multi-Strategy	4.4%	-0.6%	**3.8%**
HFRI Relative Value	**2.5%**	**1.4%**	**4.0%**
Asset Backed FI	2.4%	2.1%	**4.5%**
Convertible Arbitrage	4.3%	1.2%	**5.5%**
Corporate FI	3.2%	1.7%	**4.9%**
Multi-Strategy	2.3%	0.7%	**3.0%**
Sovereign Fixed Income	3.0%	1.6%	**4.6%**
Volatility Arbitrage	0.9%	0.6%	**1.5%**
Yield Alternatives	0.9%	1.5%	**2.3%**

Source: Bloomberg

Qualitative HF Alpha Drivers (9-12m view)

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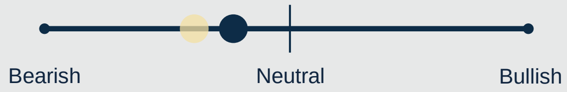
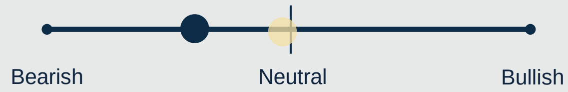
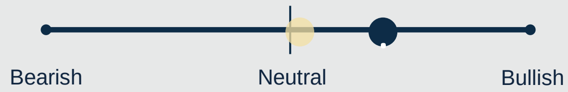
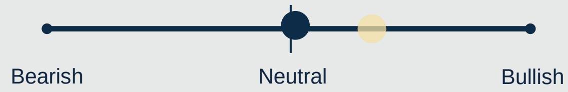
Factors	Comments	Historical Range
HF Supply v. Demand	• Less supply, even less demand • Multistrats frenzy has peaked • Redemptions from HF's because PE is not liquid • Investors pushing for better terms, hurdles & founders' fees	
Liquidity	• Slowdown in economy means traders pulling back • Markets exhibited risk-off behavior in August • High US deficit could affect Treasury market	
Corporate Activity	• Plenty of corporate refinancing boosting credit investors • PE still frozen, Private Credit lenders extending terms • Equity Capital Markets beginning to come back • Potential for pro-M&A policies in US	
Government Influence	• Markets impatient for Fed rate cut • Bank of Japan upset markets with rate increase on July 31 • Antitrust ruling against Google search engine monopoly • Consensus that budget deficits are stimulating markets • Europe will be first to cut rates	

● Current Quarter
● Previous Quarter

2024 Forecasts & Risks

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2024 Forecast

Multistrats growth slowing while sector is in the early stages of consolidation

- Citadel, Millennium and Point 72 set the standard, others second-tier
- Pace of asset growth at multi-PMs will slow as performance fades
- **Fever is breaking**

Markets are underpricing potential for volatility and hedge funds may benefit

- **Surprises around inflation, rates, and global economic data offer trading opportunities for hedge funds**
- **The effects of QT and financial tightening have yet to fully flow through**

Select green shoot market segments will remain buoyant regardless of overall macro conditions

- Distressed cycle for EM and European credit will last at least another year
- Buoyant activity in healthcare, energy, and tech will continue
- **AI is powerful**

Still finding single strategy hedge funds, not every strategy has been swallowed up by multimanagers

- Unlevered and less liquid strategies like emerging markets and distressed are not represented within multimanagers
- **Stream of mid-sized funds with investor-friendly terms**

Risks

Inflation trajectory

- Uncertain inflation trajectory in could influence Central Banks' hiking paths, creating range-bound, volatile markets

Tension over Ukraine, Middle East, Taiwan

- Surprises in outcome of battles could worsen geopolitical risks on the horizon

Market deleveraging

- Broad-based, disorganized deleveraging will have a very negative impact on hedge funds
- Levered strategies, usually uncorrelated ones, will suffer outsized losses
- **Multimanager portfolios use significant leverage**

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Considerations and risks related to asset classes:

Equity investments involve a high degree of risk. Equity securities may decline in value due to factors affecting securities markets generally, and equity securities generally have greater price volatility than debt securities/investments. Equity securities of certain jurisdictions may experience more rapid and extreme changes in value and may be affected by uncertainties such as international political developments, currency fluctuations and other developments in the laws and regulations of countries in which an investment may be made. There can be no assurance that return objectives will be realised and investors could lose up to the full amount of their invested capital. Fees and expenses may offset the trading profits.

Debt investments (such as, but not limited to, investment grade, high yield, emerging market debt, asset backed securities and insurance linked securities) involves special considerations and certain risks, including risk of default and price volatility, and such securities are regarded as being predominantly speculative as to the issuer's ability to make payments of principal and interest.

LDI and equity overlay strategies may invest and trade in many different market strategies and instruments (including securities, non-securities and derivatives) and may employ different investment, hedging, leverage and arbitrage methodologies, so the risks of those would be material to understanding the risks and benefits of the portfolio. Counterparty and ISDA arrangements may pose potential risk. Furthermore, derivative strategies may be exposed to the risk of market disruptions, volatility, and governmental interventions.

Illiquid investments (such as, but not limited to, private credit, private equity and infrastructure):

General/Loss of capital. Investment involves a high degree of risk. There can be no assurance that return objectives will be realised and investors could lose up to the full amount of their invested capital. Fees and expenses may offset the trading profits.

Limited liquidity. Investments in private markets may result in restricted liquidity since withdrawal rights are limited and interests are not freely transferable or redeemable. There is unlikely to be a secondary market for private market investments interests.

Volatility. Investment techniques used may include the use of leverage and derivative instruments such as futures, options and short sales, which could amplify the possibilities for both profits and losses and may increase volatility.

Hedge Fund investing is speculative and involves significant risk including the risk of losing some or all of the invested capital. Hedge fund strategies may participate in the buying and selling of equity and debt securities, private investments funds, non-readily realisable investments, illiquid investments suspension of trading, concentrated investments, developed and emerging market investments. Hedge fund strategies may be exposed to risks stemming from usage of leverage, derivatives, futures, options, over-the-counter derivative transactions. Counterparty and ISDA arrangements may pose potential risk. Furthermore, hedge fund strategies may be exposed to the risk of market disruptions, volatility and governmental interventions.

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Forward looking return, volatility, and correlation assumptions have been derived by SECOR, and are based on a combination of: a) the historic performance of each asset class based on what we consider to be appropriate indices or suitable proxies, and over a period that we consider to be appropriate in light of prevailing market conditions (typically 10 years); and b) our judgement in relation to how historic performance, and its various components, may differ in the future. This may include, for example, ad-hoc adjustments to reflect our view that markets are over or under valued.

The resulting assumptions are assumed to be appropriate for asset and liability projections over the medium to long term i.e. 10 to 20 years or longer, and are net of all ongoing management costs and fees.

Expected returns for an asset class are generally built up from and include an allowance for our projected return on cash, inflation, spreads, risk premiums, liquidity premiums, potential losses, valuation adjustments, alpha for active management, management fees, other ongoing costs, and any other factors that we may consider are appropriate for the asset class and/or prevailing market conditions. Expected returns generally <u>do not</u> allow for SECOR advisor or fiduciary management fees, or any transition or rebalancing costs between asset classes or an existing portfolio.

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