



Global Asset
Management

Shifting strategies:

How the world's largest institutions are
embracing fixed income hedge funds

Executive Summary

A new global research report from RBC Global Asset Management gathered insights from 450 of the largest institutional investors in the world, and findings show that sentiment towards fixed income hedge funds is improving. This is fueled by these funds' strong returns, competitive fees, and enhanced liquidity. But investors still have some reservations, and assets under management (AUM) and a long track record are critical.

With economists expecting interest rates to remain elevated in the medium term and market volatility to persist, we wanted to find out which trends and priorities are shaping investor sentiment and their decision-making, particularly in relation to alternative forms of fixed income. What are their performance expectations? Which selection criteria are they using? And how are macroeconomic factors and geopolitics affecting their choices?

Our research report reveals that investors are expecting geopolitical uncertainty, continuing high interest rates and equity market volatility to have a strong impact on the fixed income asset class over the next 3 to 5 years. Against that backdrop, investors are turning to alternative investment strategies to generate returns – and fixed income hedge funds in particular are becoming a core component of global asset allocation strategies.



Key finding 1

Growing confidence in fixed income hedge funds has led to mainstream adoption

70% of the largest investors invest in fixed income hedge funds

Key finding 3

Institutional investors are bullish about the return potential from fixed income hedge funds

63% expect fixed income hedge funds to deliver 10%+ returns per annum

Key finding 2

Strong performance, flexible fees, and increased liquidity underpin investor sentiment

62% of hedge fund investors expect to increase their allocation in the next 12 months – seven times more likely than to decrease it

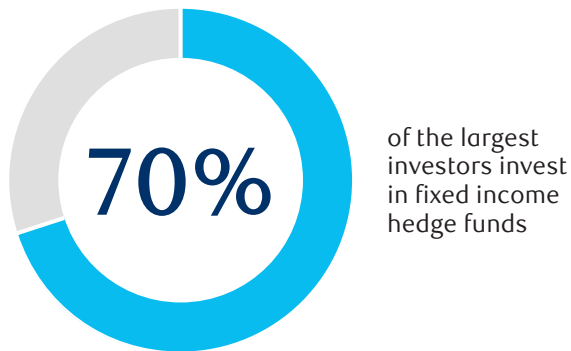
Key finding 4

Institutional investors favor established hedge fund strategies with strong track records

61% rank AUM as a priority when selecting a hedge fund manager

Key finding 1

Growing confidence in fixed income hedge funds has led to mainstream adoption



Investing in hedge funds has become mainstream among asset owners and wealth managers:

60% of investors have allocated capital to hedge funds

Among these investors,

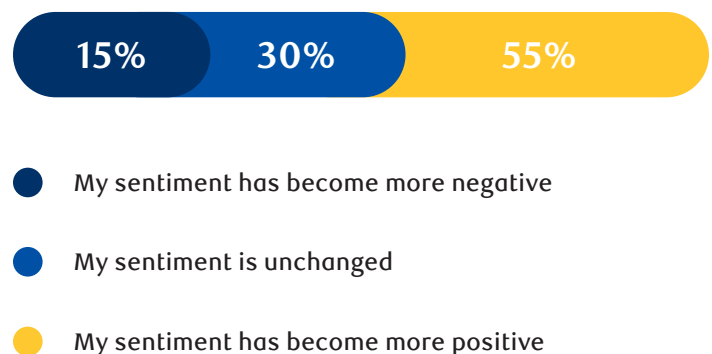
84% invest specifically in fixed income hedge funds

Adoption of hedge funds is consistent across the regions explored globally, except for Germany, where allocations are lower. Amongst hedge fund investors, more than three quarters in each region invest in fixed income hedge funds. Institutions with more than US\$100 billion in AUM, which have greater resources and risk tolerance, and the expertise to navigate complex strategies, are most engaged: 78% invest in hedge funds, and 90% of those invest in fixed income hedge funds.

Investor sentiment towards fixed income hedge funds has improved globally: 55% of those investing in such funds say they have taken a more positive view of them over the past 3–5 years, compared with 15% whose opinion has worsened and 30% whose opinion has not changed. This means that investors are three and a half times as likely to have a positive opinion on fixed income hedge funds than to have a negative opinion.

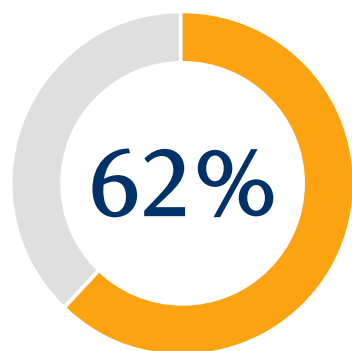


More than half of investors now have a better opinion of fixed income hedge funds



Key finding 2

Strong performance, flexible fees, and increased market liquidity underpin investor sentiment



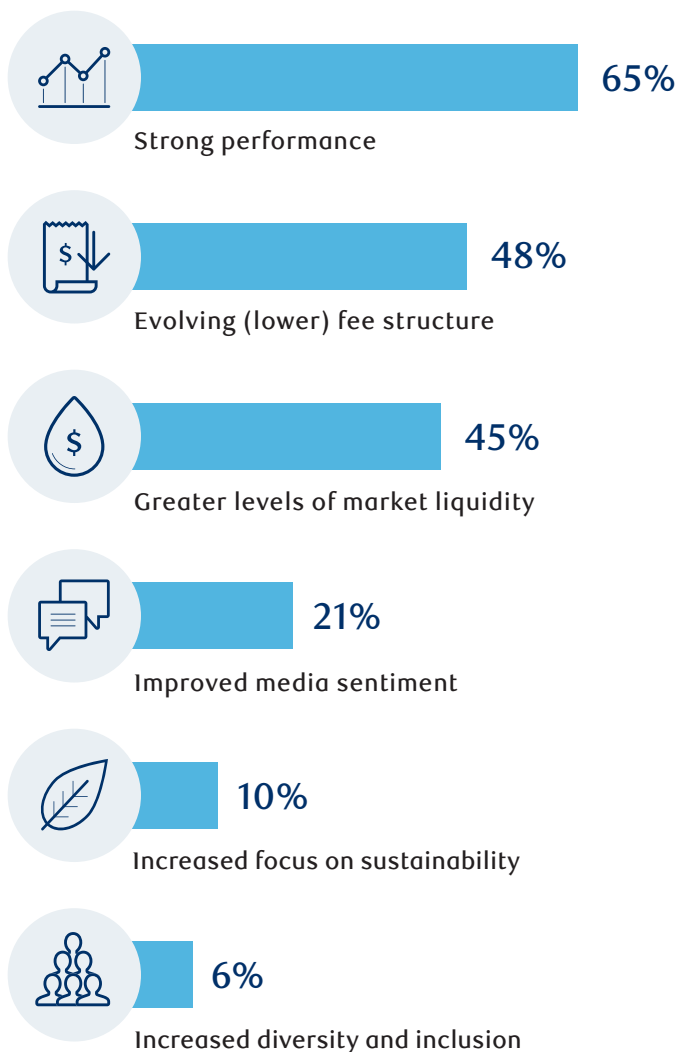
of hedge fund investors expect to increase their allocation in the next 12 months – seven times more likely than to decrease it

Among investors with more positive opinions of fixed income hedge funds, 65% say this is because of strong financial performance. This is more keenly felt in Asia (84%) and in the US (70%) than in Europe (57%).

With more managers willing to move away from the traditional '2% management fee + 20% performance fee' arrangement, lower fee structures are investors' second most important reason to be positive about fixed income hedge funds (48%). This is especially valued by wealth managers (69%) and smaller institutions with AUM of between US\$5 billion and US\$29 billion (67%).

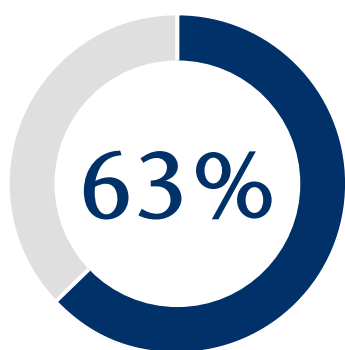
Investors' third most important reason to be positive about fixed income hedge funds is market liquidity. Increased competition has led managers to introduce more flexible redemption terms, which has improved market liquidity, and this is a benefit for 45% of investors. This rises to 53% of US investors and 55% of institutions with AUM of between US\$30 billion and US\$74 billion.

Performance is investors' top reason to feel positive about fixed income hedge funds



Key finding 3

Institutional investors are bullish about the return potential from fixed income hedge funds



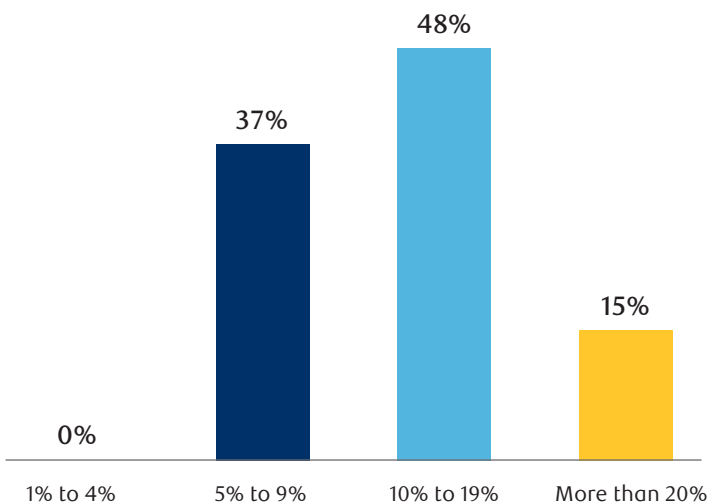
expect fixed income hedge funds to deliver 10%+ returns per annum

Investors have high expectations of annual returns from their fixed income hedge fund investments: 63% aim for returns of 10% per annum or higher. This increases to 75% among wealth managers. At the higher end, 15% of investors globally expect annual returns to exceed 20%, with European investors the most bullish (21%).

Although 62% of investors worldwide say that the past performance of their portfolios have met or exceeded their future return expectations, 38% say they have fallen short. US investors (44%) and institutions with AUM of between

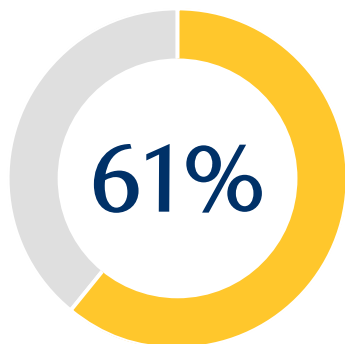
US\$30 billion and US\$74 billion (46%) are the most likely to report a negative disparity. Nevertheless, the outlook remains optimistic. With interest rates high, investors seem to anticipate greater yields from fixed income instruments and opportunities for skilled fund managers to exploit pricing inefficiencies.

The majority of investors expect double digit returns from their fixed income hedge funds



Key finding 4

Institutional investors favor established hedge fund strategies with strong track records



rank AUM as a priority when selecting a hedge fund manager

When investors assess potential allocations to fixed income hedge funds, investors across regions and investor types consistently prioritize two factors: the asset class (69%) and predictability/volatility of returns (59%).

These factors are especially critical for wealth managers, who use them to align investments with client objectives and risk tolerances while ensuring consistent performance: 77% of wealth managers prioritize the asset class, and 69% focus on returns predictability.

Investors also say that size of fund AUM and a long track record are crucial criteria when choosing individual funds.

61% say that fund AUM size is their top priority when they select a hedge fund – ahead of its fees and the manager’s past performance

Only 25% of investors are willing to consider a first-time fund

Investors are prioritizing fixed income hedge funds with significant AUM



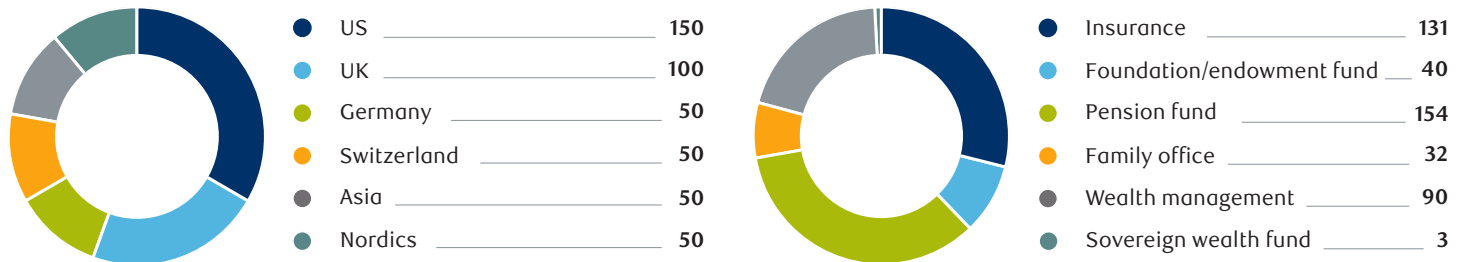
These preferences underscore investors' demand for large-scale, established and reliable investment strategies when it comes to fixed income hedge funds.





Additional information

Just after the November 2024 US presidential election, RBC Global Asset Management gathered insights from 450 senior institutional investment decision-makers across the US, Europe, and Asia who manage assets of between US\$5 billion and more than US\$100 billion.



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