BAI INVESTOR SURVEY 2022

Alternative Investments
- Navigating the Storm -

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Introduction

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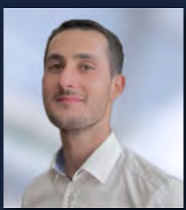

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The Bundesverband Alternative Investments e.V. (BAI) presents the 2022 BAI Investor Survey, the 9th and with 106 participating German institutional investors combining more than € 2.1 trillion AuM the most comprehensive BAI survey to date. In addition, for the 2nd time, we surveyed 101 BAI member companies, such as global asset managers and service providers combining more than € 2.5 trillion AuM, to compare the views of the buying with the views of the selling side. This report highlights our annual survey results to provide you with a deeper understanding of how and why institutional investors in Germany invest in alternative assets – not just today but also in the future.

The BAI Investor Survey has been an essential component of BAI's research activities since 2013. The framework for institutional investments in Germany is subject to constant dynamic changes. Therefore, the range of questions is continuously updated and adjusted to meet the needs of the investors and BAI member companies. Inflation and a change in central bank monetary policy keep investors on edge. Simultaneously the realignment of portfolios from an ESG perspective continues. Furthermore, progress in regulation lead to new challenges and opportunities, which have been systematically captured in the survey once again.

The objective of our association's work is to improve public awareness, create internationally competitive and attractive conditions for alternative investments, and represent the industry's interests to politics and regulators. The BAI's annual investor survey helps increase alternative investment market transparency. The results will hopefully serve as a valuable source of information for you but are also highly relevant to our associations' work as they give substantial weight to our arguments in exchange with regulators. Founded in 1997 in Bonn, the more than 270 BAI members are active in any professional alternative investments business field.
The members' directory can be found here.

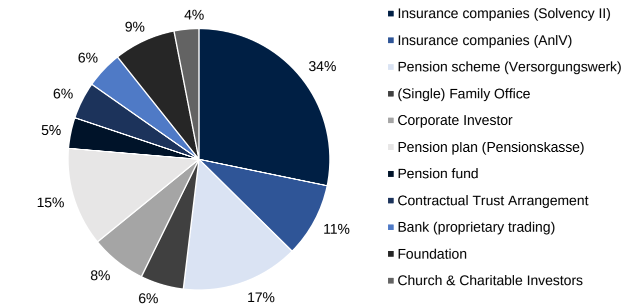
Sincerely,

Bundesverband Alternative Investments e.V. (BAI)

Explore further BAI publications

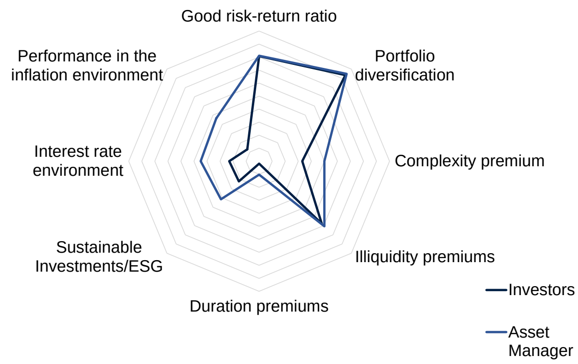
Highlights (1/2)

Investor Types

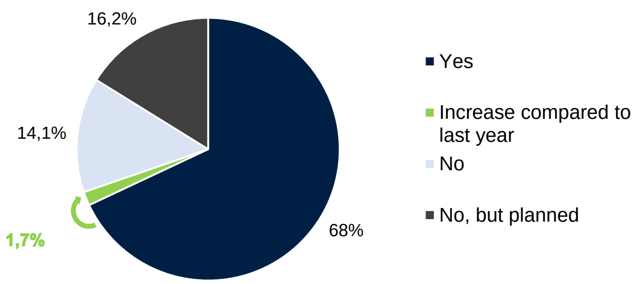


* Multiple answers were possible

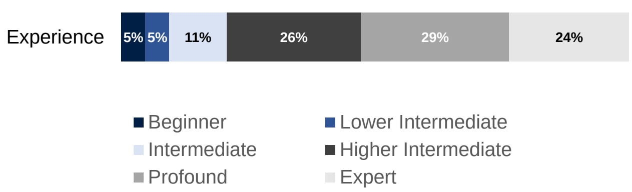
Main Reasons for Alternatives



ESG Strategy

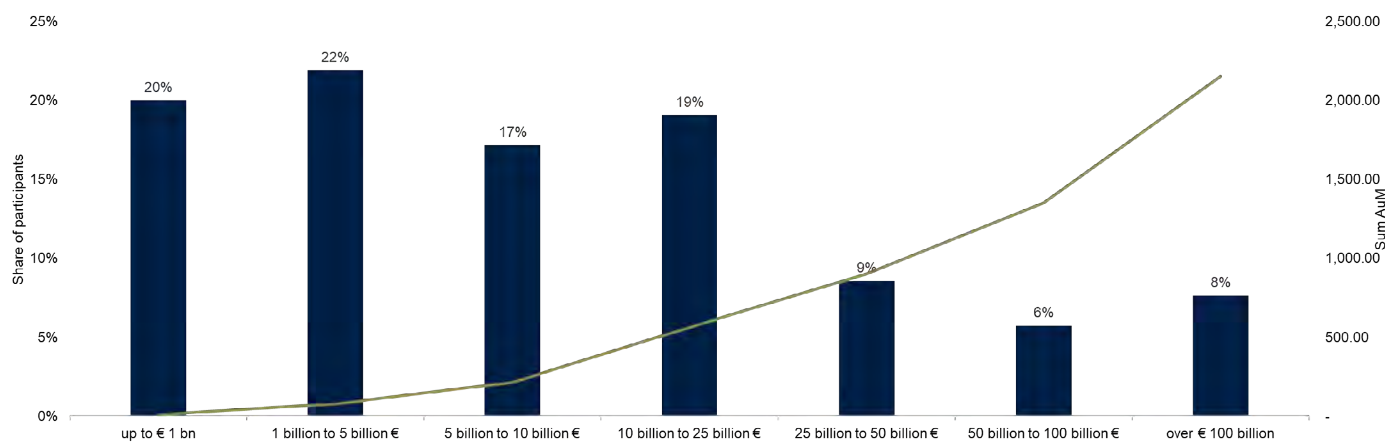


Investor Experience

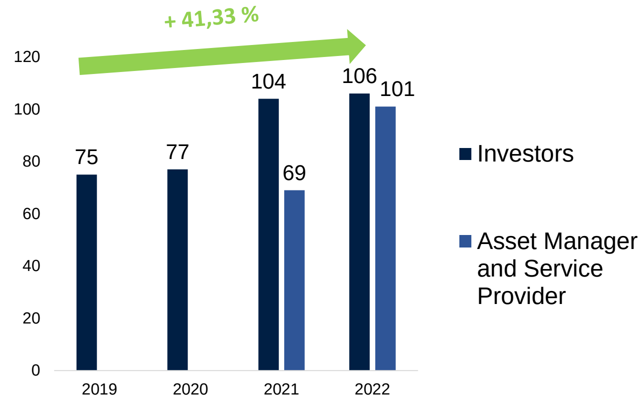


- Record participation with 106 institutional investors and 101 asset managers & service providers
- Average AI portfolio allocation increases to 23,2%
- Significant growth in almost all alternative asset classes, especially in infrastructure investments, but German fund structures have almost no relevance
- Vast majority already invested in the green & clean energy sector
- More than two-thirds pursue a distinct ESG strategy
- Portfolio diversification: 50 % invested in at least five different alternative asset classes

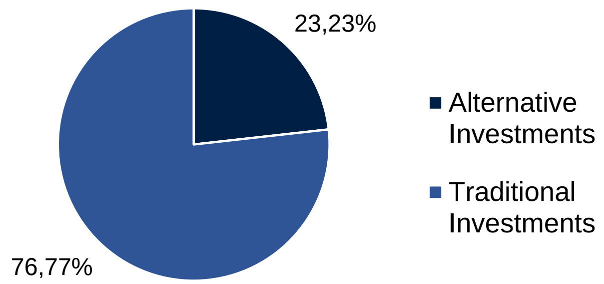
AuM



Participants

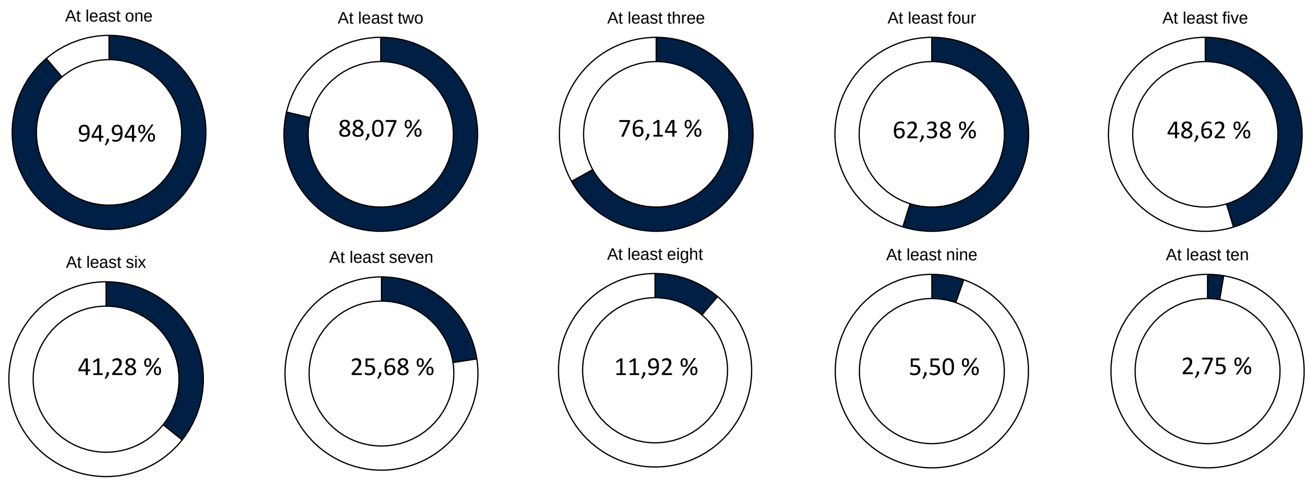


Allocation 2022

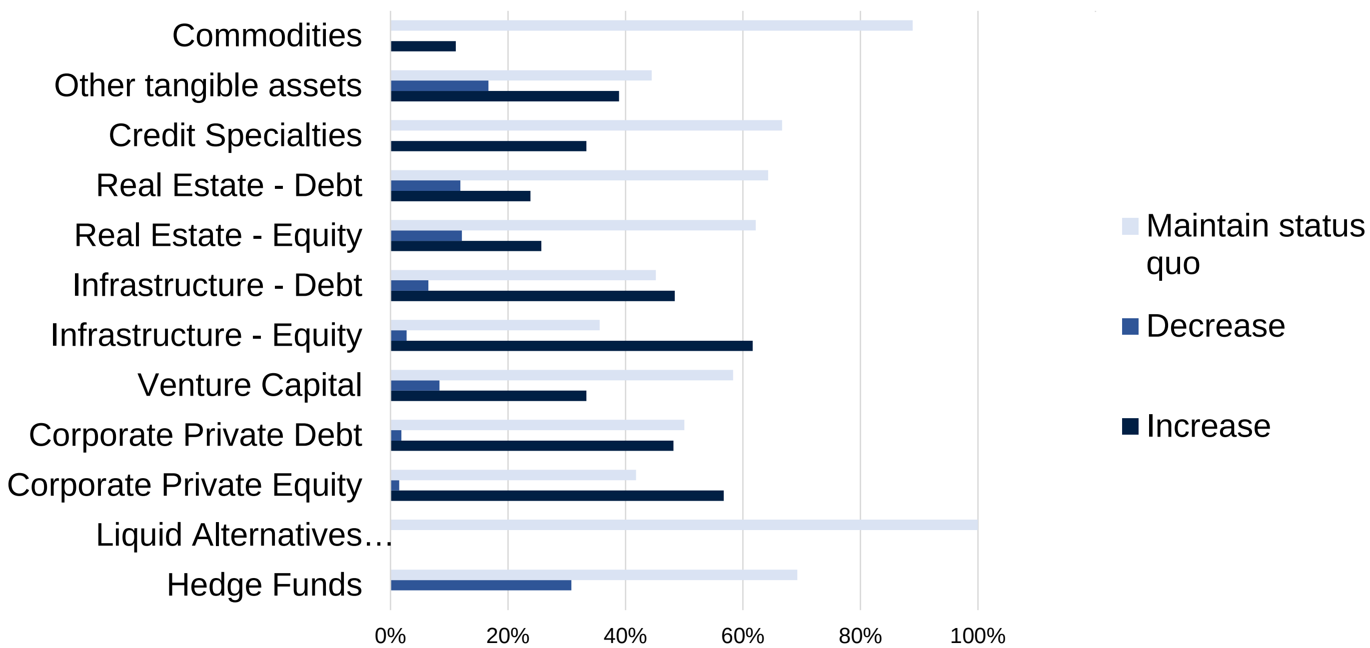


*New Methodology, including the distribution of assets under management among investors. This reflects a more accurate way of computing the most important key number.

Number of Alternative Asset Classes invested in



Planned Changes in the Asset Allocation



Content

Methodology

Based on the BAI definition of alternative investments, as shown in the BAI "Alternative Investments Navigator," we cluster alternative asset classes into hedge funds, liquid alternatives (mainly UCITS), private equity (in detail: corporate private equity, venture capital, infrastructure equity, and real estate equity), private debt (in detail: corporate private debt, infrastructure debt, and real estate debt), credit specialties (such as ILS and trade finance), other real assets (such as farmland, timberland, aviation, and shipping), commodities, and crypto assets. Like in previous years, we have used this definition consistently in our report.

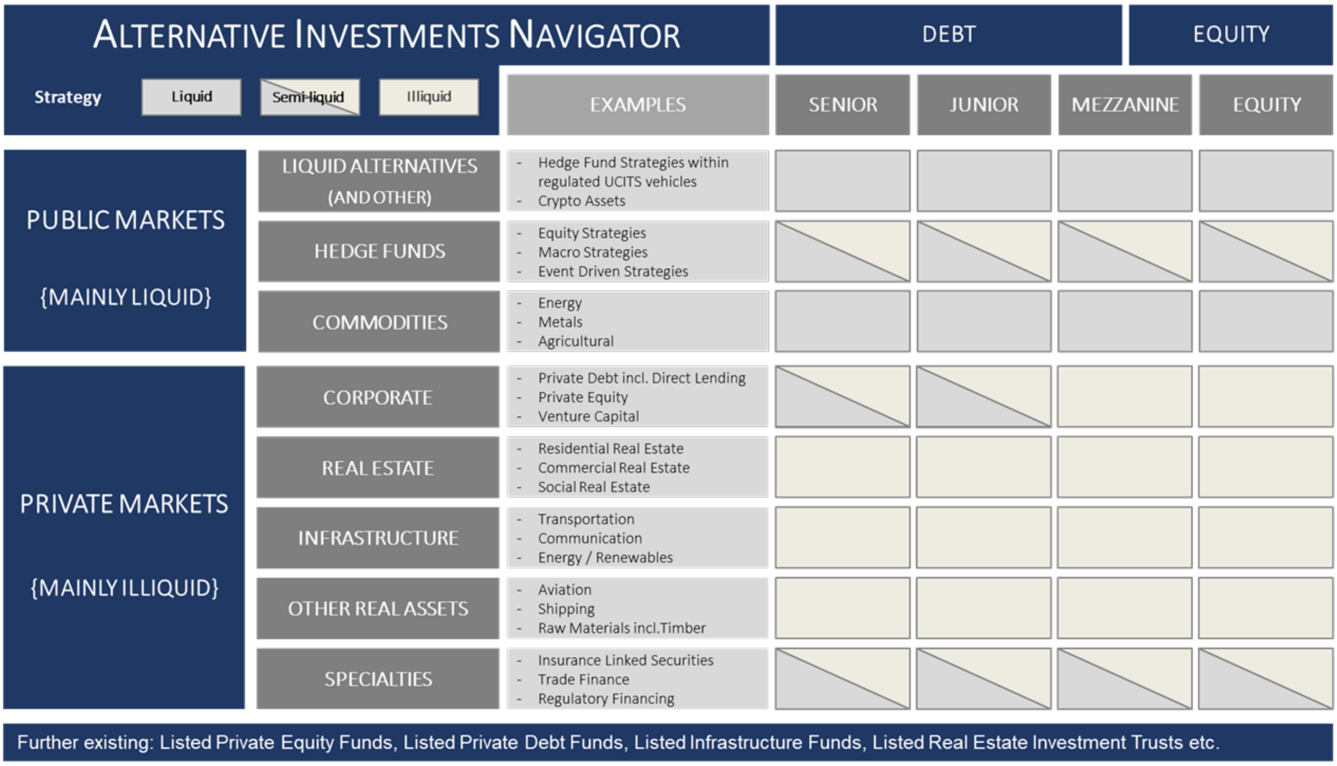


Figure 01

Cross-section of Investors & Assets under Management

106 institutional investors across Germany participated in the 2022 BAI investor survey, including insurance companies, pension funds, pension plans & CTAs, pension schemes, corporates, traditional banks (proprietary trading), family offices, church & charity investors, and foundations. For 101 globally operative asset managers, providers of alternative markets products, members of our association, we have initiated a survey in parallel. In part, we mirror the results of the two surveys to gain further exciting insights.

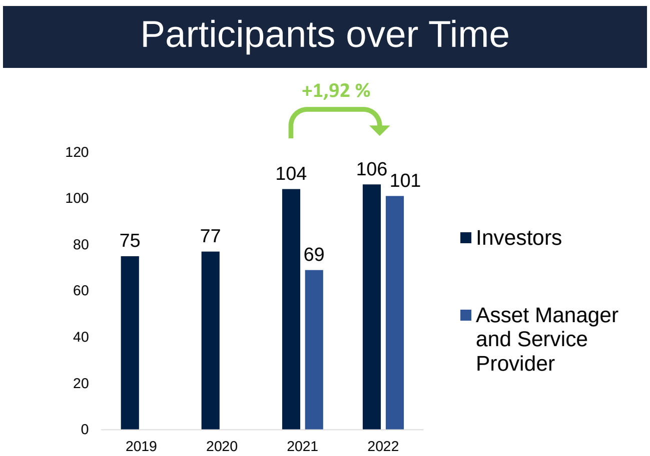


Figure 02

To ensure that no investor, as well as no asset manager or service provider, participates more than once, survey invitations were only sent to one selected contact person from BAI's partners' network.

The participating investor groups are characterized by their heterogeneity. More than three-quarters of the respondents represent insurance companies (45 %), pension plans (15 %), or pension schemes (17 %). Therefore, the amount of assets under management (AuM) varies significantly among the investors, from less than one billion to well above €100 billion.

The average participant manages more than €20 billion AuM. Not only has the number of participants increased continuously over the last years. We estimate the total AuM of the participant investors at more than €2,150 billion, which once again is a significant increase compared to previous years.
This is due to the development of the investor network and an increase in participants with high volumes of AuM, such as insurance companies and pension funds.

By its very nature, the structure of the participating investors could be a limitation of the study. In addition, the results of the BAI investor survey might be positively influenced by a self-selection bias, as investors from the BAI network are naturally more committed to alternative investments than the overall population of investors.

However, with 106 institutions and more than €2,150 billion AuM, we cover a substantial and highly representative part of the investor landscape in Germany. Consequently, we are convinced that the results of the participating investors are robust and that they accurately reflect the population and the investment behavior of the German institutional investor landscape.

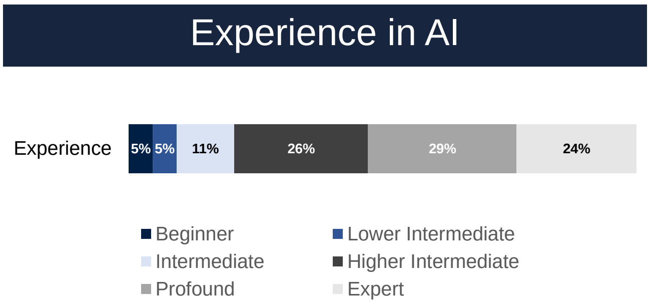


Figure 03

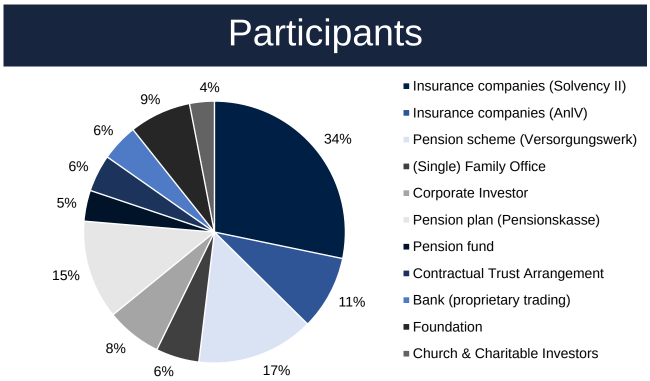


Figure 04

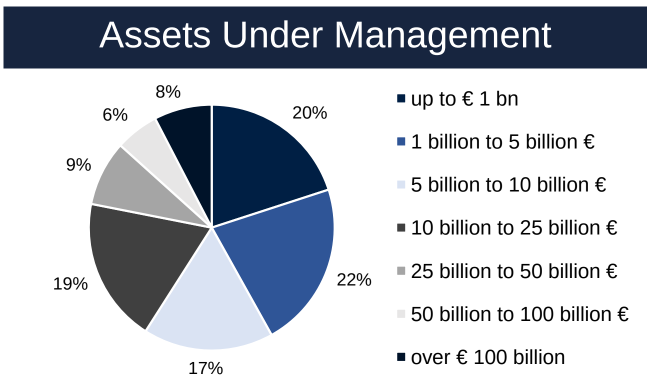


Figure 05

Alternative Investments Portfolio Allocation

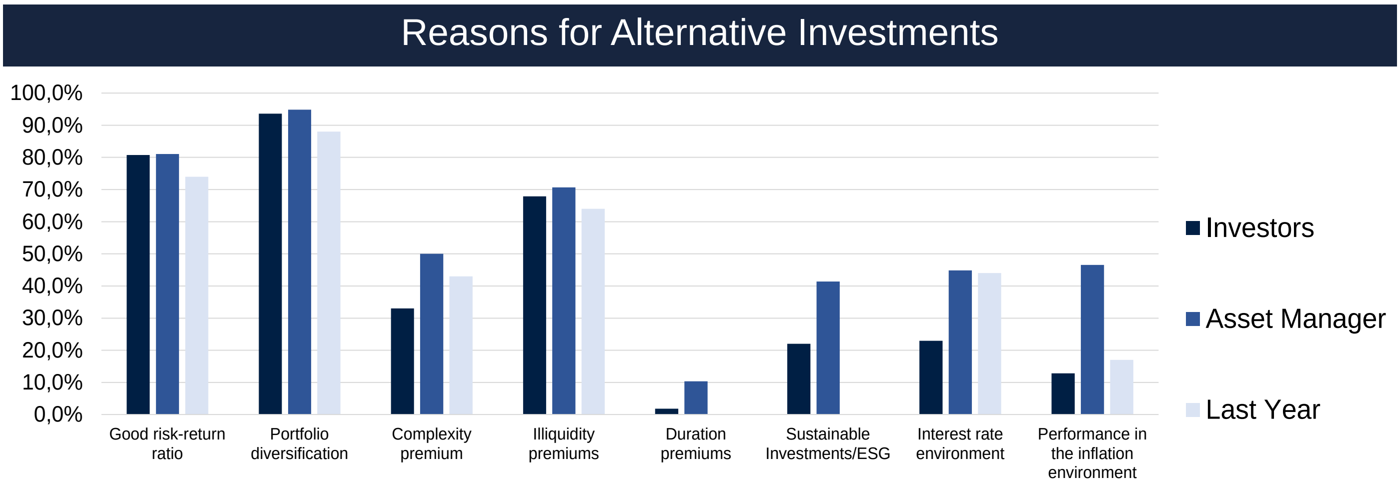


Figure 06

Investors were asked to name their primary reasons for allocating to alternative asset classes. We also asked asset managers why they think institutional investors invest in alternatives. The emphasis has shifted even more strongly to portfolio diversification compared to previous years. The undoubtedly positive experience of investors in terms of the risk-return ratio of their alternative investments can explain the stable allocation in times of market turbulence and inflation. Illiquidity and complexity premiums remain convincing reasons for investments in alternatives. Private markets are also emerging as a catalyst for achieving ESG goals, for example through impact investing. On the other hand, investors are returning to the bond market as interest rates rise.

Alternative asset classes are an established part of the portfolio for most investors. 94% of German institutional investors are allocating at least to one alternative asset class. Most can already report a diversified portfolio with several alternative asset classes.

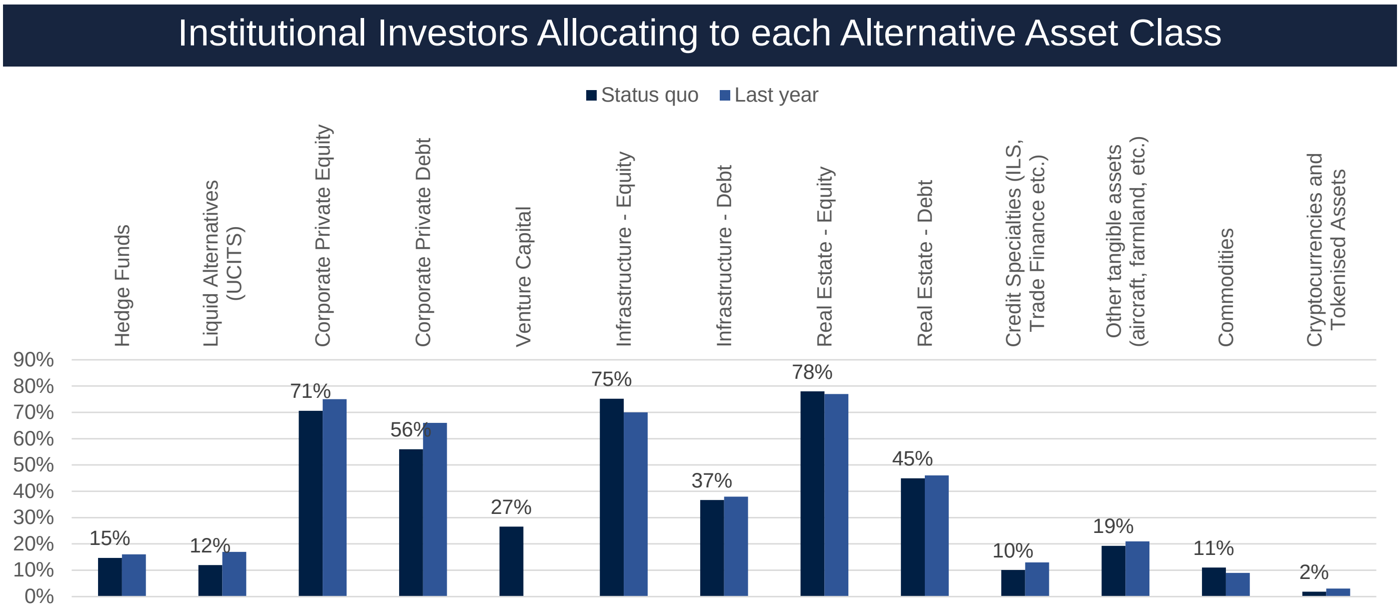


Figure 07

* no data for venture capital 2021

Expected Returns (EUR)

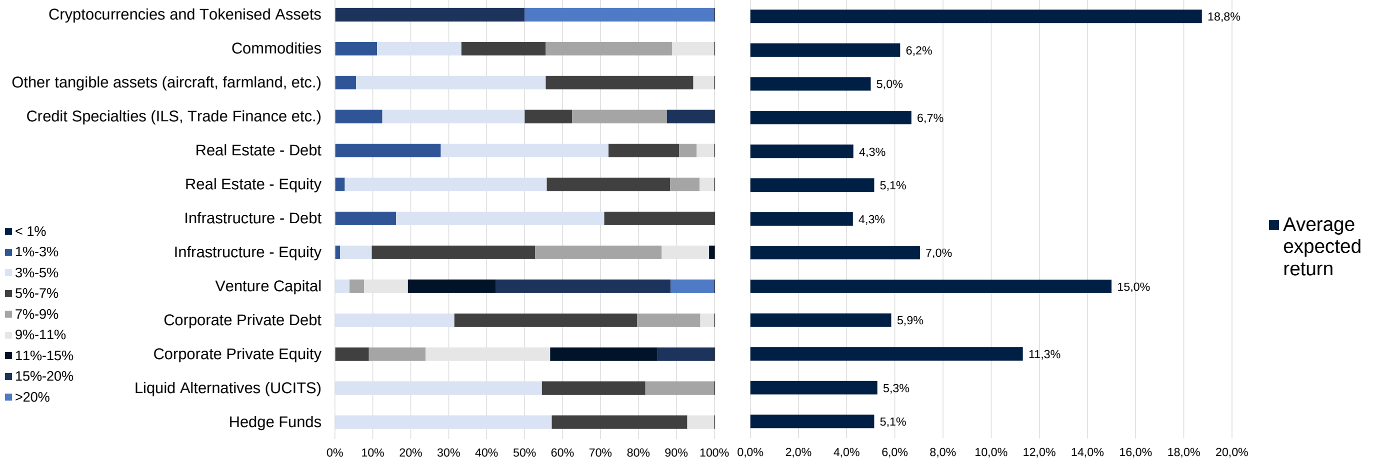


Figure 08

In recent years, hedge funds, liquid alternatives, and commodities have had a difficult time in Germany. As a result, investors have withdrawn from these asset classes. However, the portfolio allocation has now stabilized. We even see a slight increase in commodities and demand for absolute return strategies. This trend reversal is also related to the current volatile market environment, high inflation, and rising interest rates. We address this topic in detail later in the report.

On the other hand, private equity investments in corporates (71 %), infrastructure (75 %), and real estate (78 %) are an integral part of investors' portfolios. We see only slight year-on-year fluctuations in all asset classes compared to last year's results. The number of institutions invested has remained remarkably stable, which is also true for private debt asset classes.

„With venture capital, we intend to further diversify our well positioned private equity portfolio in the near future" - large pension scheme -

Entry Path per Asset Class

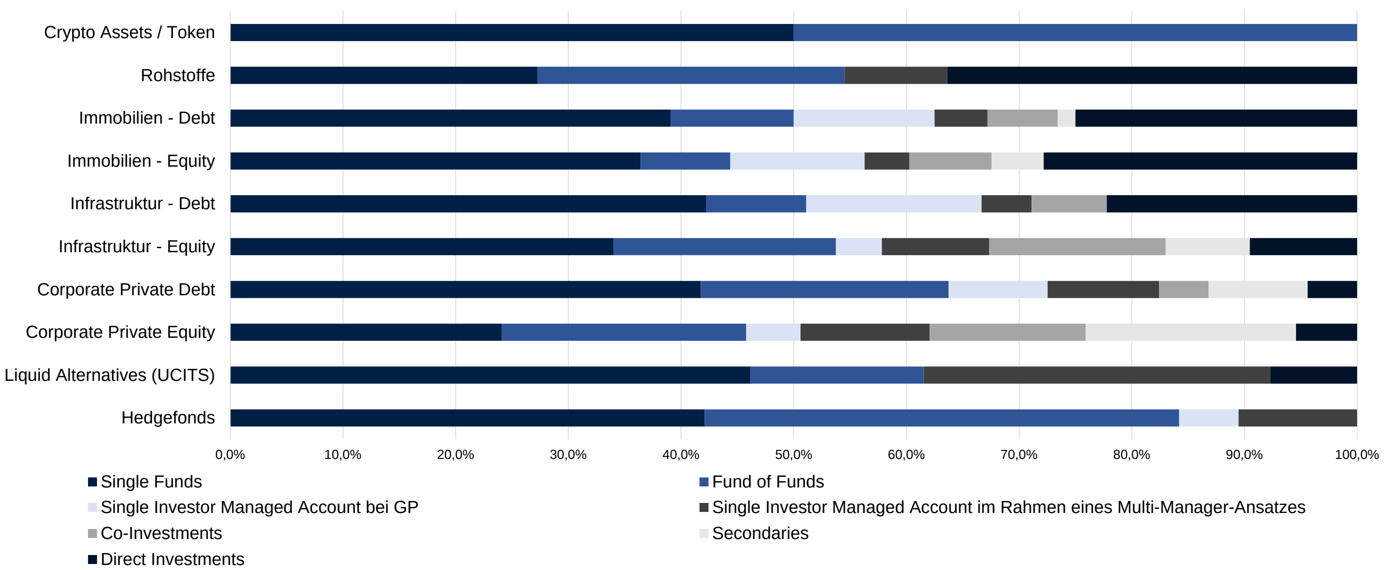


Figure 09

All in all, investors are catching their breath after 2021 showed substantial increases in debt asset classes. By contrast, the outlook for 2023 is again very positive.

„We would like to add private equity to our portfolio, not only to capture illiquidity and complexity premiums, but also to make impact investments.“ - medium-sized insurance company -

Corporate private debt and infrastructure debt are the asset classes most investors want to build up an allocation. It is striking that, across all asset classes, private market debt investments will continue to catch up to their equity counterparts over the upcoming years. Moreover, we expect many investors to further diversify their portfolios with entries into corporate private equity, especially venture capital, infrastructure equity, and real assets such as timber or farmland.

Alternative investment allocation in 2022 and beyond

In line with the standardized definition of asset classes, investors were asked about their allocation to alternative investments. To gain a deeper understanding of the demand for alternative investments, we estimated in detail the current and future portfolio allocation for the average institutional investor in Germany to alternative investments. We consider non-alternative investments as traditional investments, such as listed equities, corporate and sovereign bonds, and cash, but do not further discuss or quantify them. We weight the average alternative allocation of a portfolio by the assets under management so that larger investors have a higher impact on the average alternative investor allocation. As a result, a comparison with previous years‘ results is only possible to a limited extent, as we formed average values in previous years without considering the investor‘s assets under management.

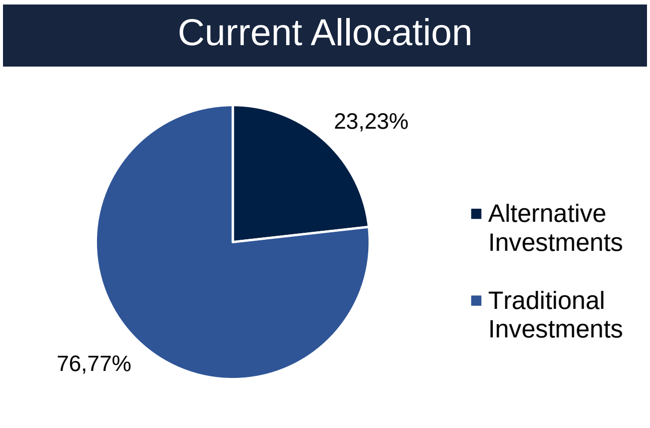


Figure 10

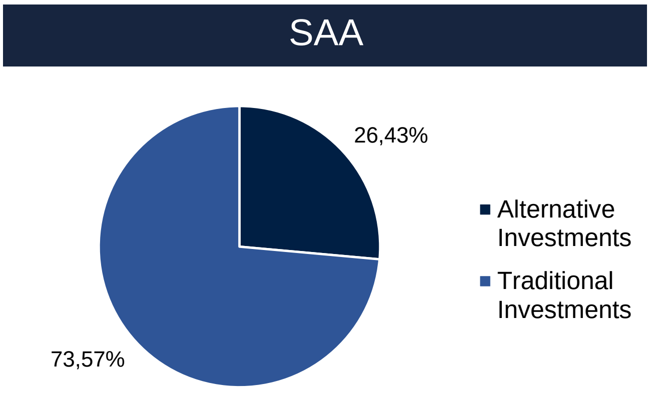


Figure 11

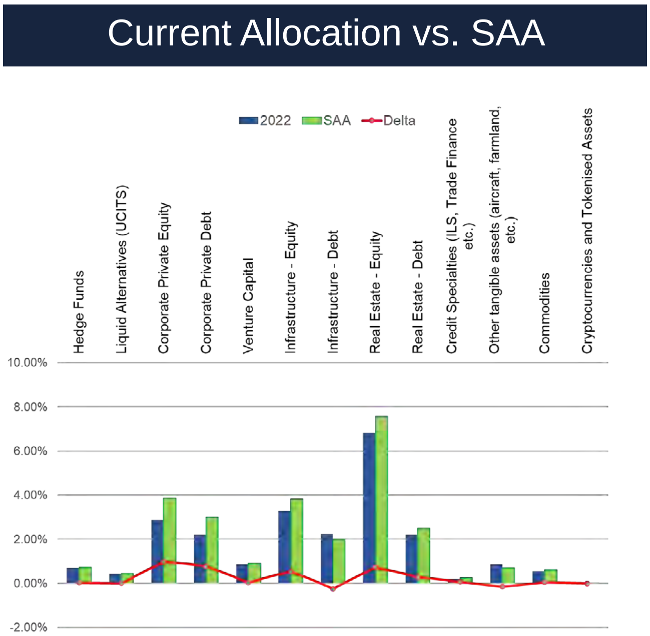


Figure 12

Our estimated alternative investments portfolio allocation reflects the growth of the alternative investments market based on the information provided by the respondents. On average, about 23.2 % of the portfolio is invested in alternatives. Figure 12 shows a breakdown of the average portfolio share per alternative asset class. Based on the investors' sentiment, as already stated in last year's survey, the expansion of the alternative investments' portfolio shares will continue next year, as the growth momentum of equity as well as debt investments in corporates, infrastructure, real estate and other real assets will most likely carry on. We asked investors about their expected strategic alternative asset allocation to identify medium-term trends in the market. Our survey results show that the split between traditional and alternative investments continues to become more and more aligned.

„An investment in private debt is considered primarily for reasons of diversification and the good risk-return ratio."
- small foundation -

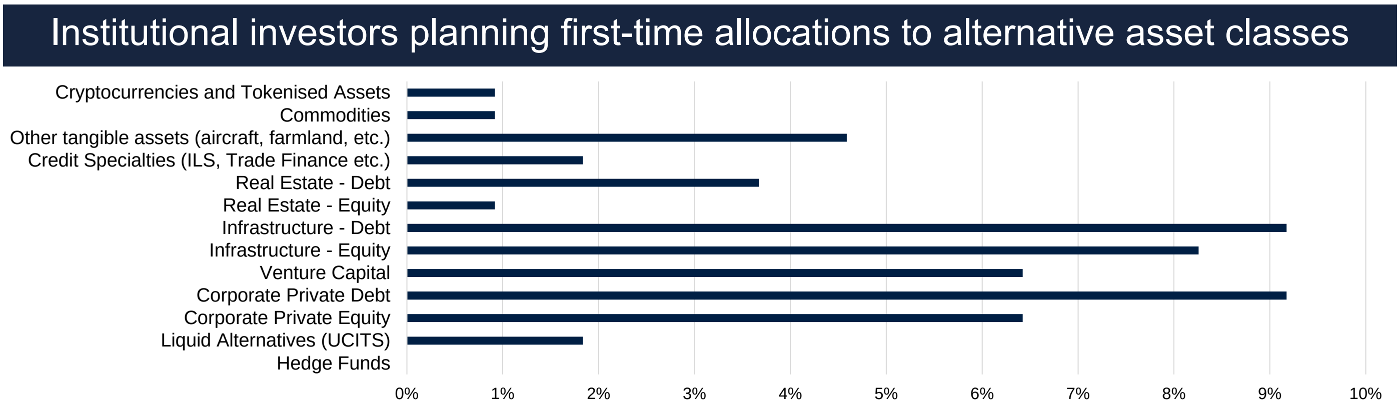


Figure 13

We expect the average institutional investor in Germany to expand the exposure to alternative investments from 23,2 % to over 26,4 % in the next few years. This corresponds, in line with last year's survey result, to an estimated yearly growth rate of the entire alternative investments industries share in institutional investors' portfolios in Germany between 3 % to 6 % in the upcoming years while keeping various exogenous incalculable variables in mind. Therefore, we stand by our long-term alternative investment allocation growth-rate forecast despite 2022 being found just under the specified 3 % to 6 % range. The statements on planned entries and the high, steadily increasing alternative SAA allows us to look to the future optimistically.

„A recession, with all its disadvantages, can nevertheless open up good opportunities for us to enter the private equity asset class"
-small pension fund -

Alternative Assets in Detail

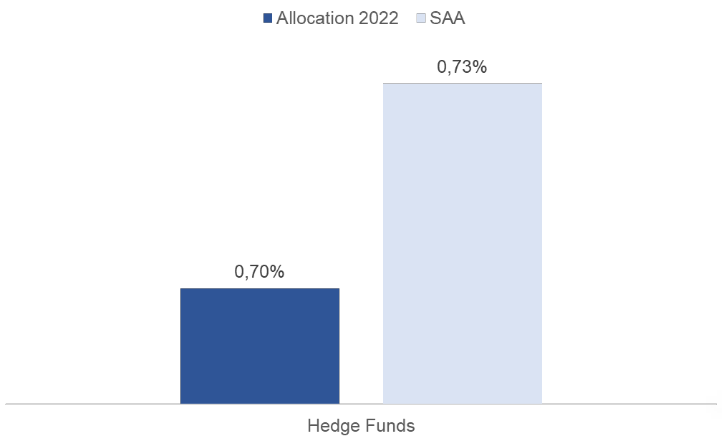
Hedge Funds & Liquid Alternatives

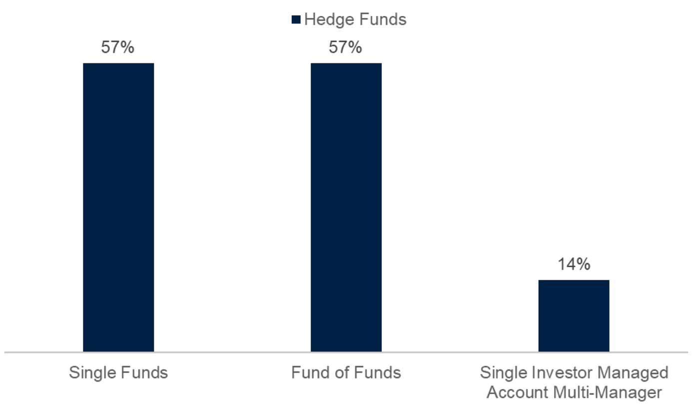
Hedge funds and Liquid Alternatives are gaining in importance as the economic environment and capital markets shift to a more volatile state. Being the most robust alternative investment in times of stagflation, institutional investors keep their hedge fund exposure reasonably constant, which is a positive turnaround for Germany compared with the previous years.

HEDGE FUNDS

Invested participants **~15%**

Expected avg. return **~5.1%**

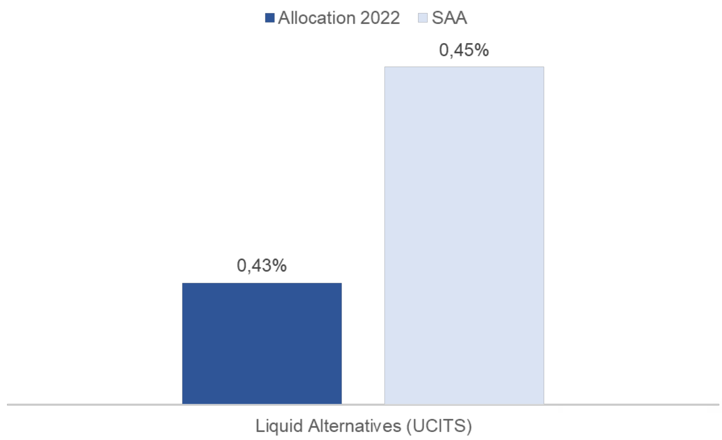


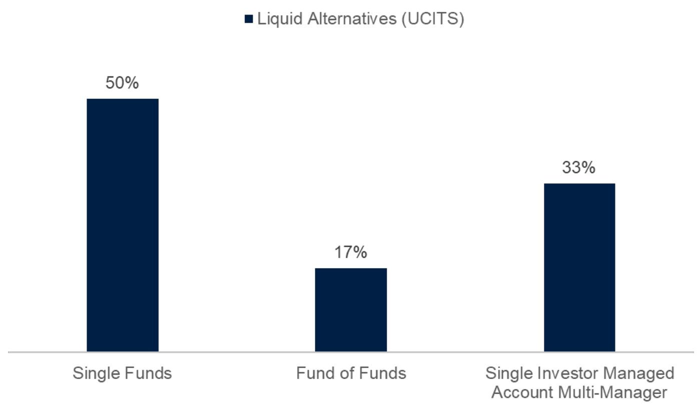


LIQUID ALTERNATIVES

Invested participants **~12%**

Expected avg. return **~5.3%**





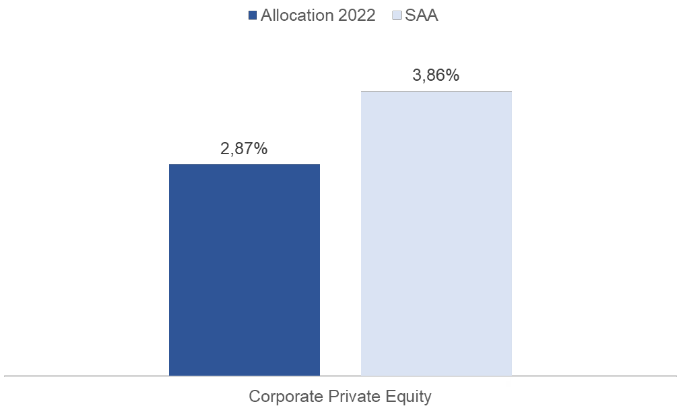
Corporate Private Equity & Private Debt

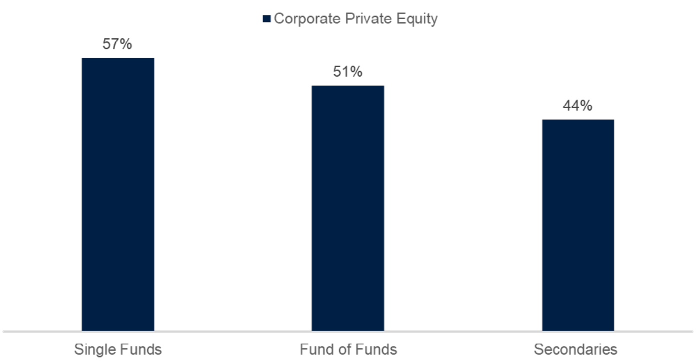
Private equity remains one the most prevalent asset class in institutional investors‘ portfolios, while the corporate debt counterpart continues its‘ catching up. Even though corporate private equity and debt are facing more challenging times from the current inflationary, fiscal, and monetary circumstances, most investors plan to increase their exposure to the historically performant asset classes.

Private Equity

Invested participants ~71%

Expected avg. return ~11.3%

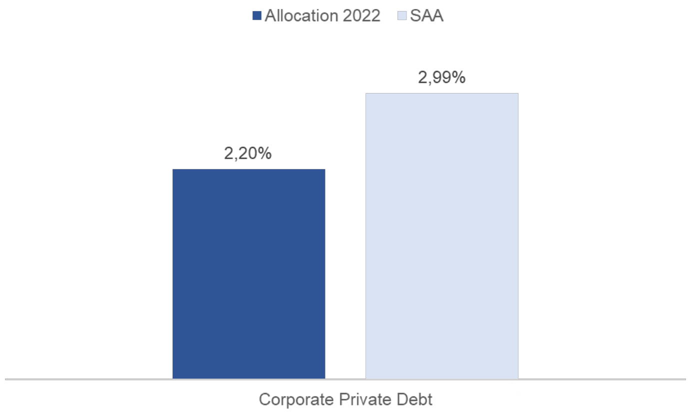


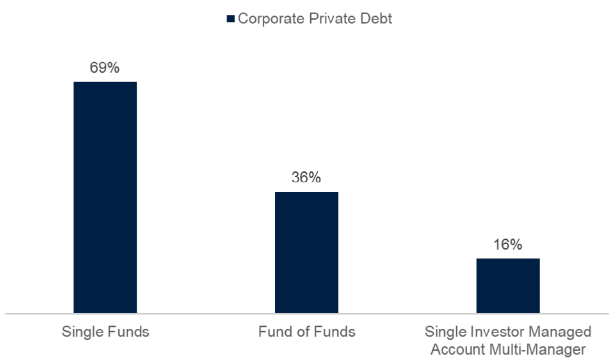


Private Debt

Invested participants ~56%

Expected avg. return ~5.9%

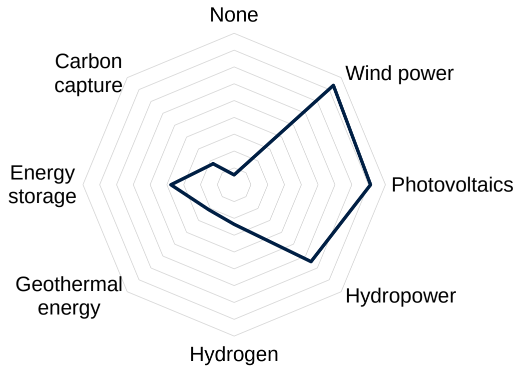




Infrastructure Equity & Infrastructure Debt

Clean & Renewable Infrastructure Investment Allocation

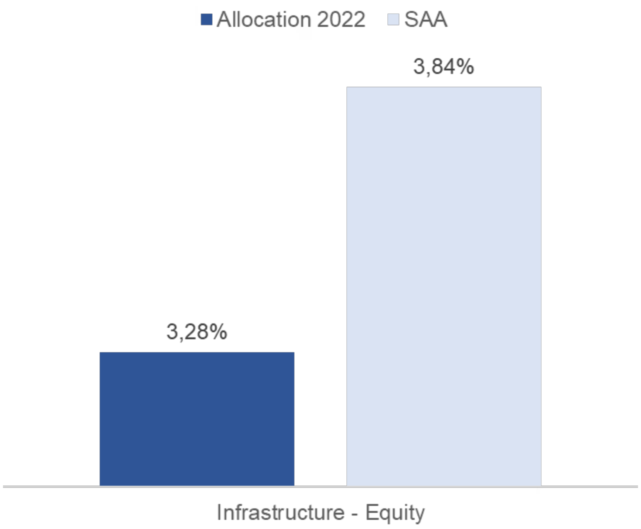
Infrastructure investments are well established in the portfolio of institutional investors. Low demand elasticity and typical free floats are welcomed yield drivers in times of high volatility. Moreover, in recent years the importance of infrastructure investments, regardless of debt or equity, increased significantly due to its crucial role in mastering ESG conformity.

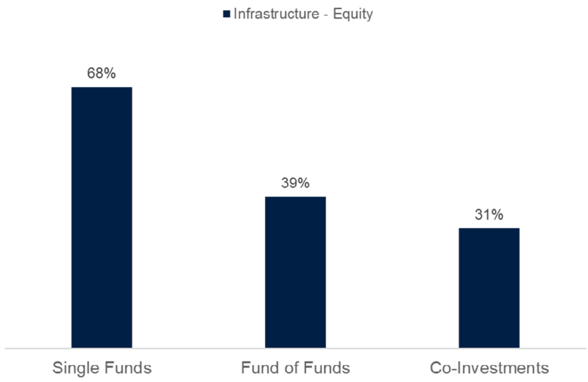


Infrastructure Equity

Invested participants ~75%

Expected avg. return ~7%

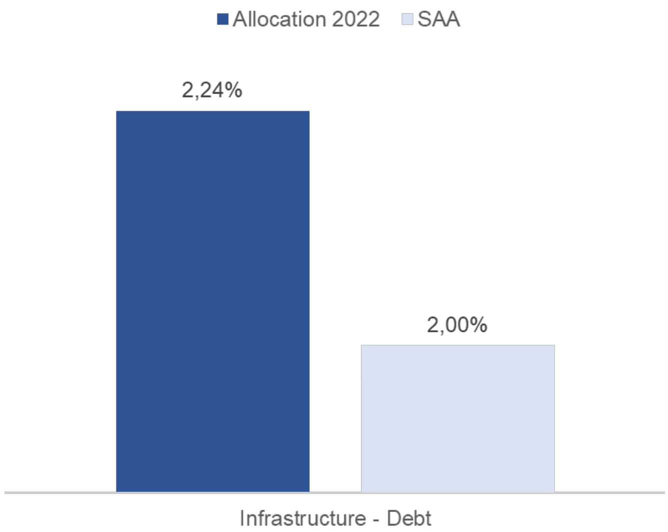


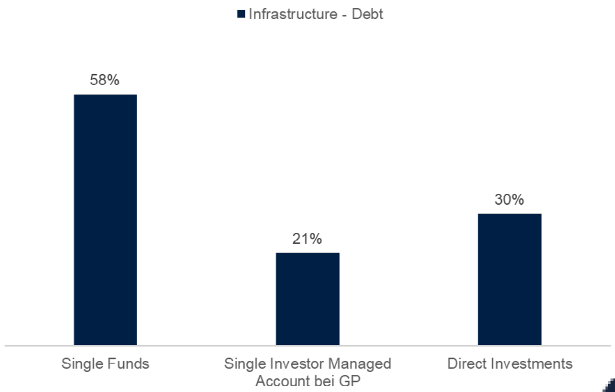


Infrastructure Debt

Invested participants ~37%

Expected avg. return ~4.3%



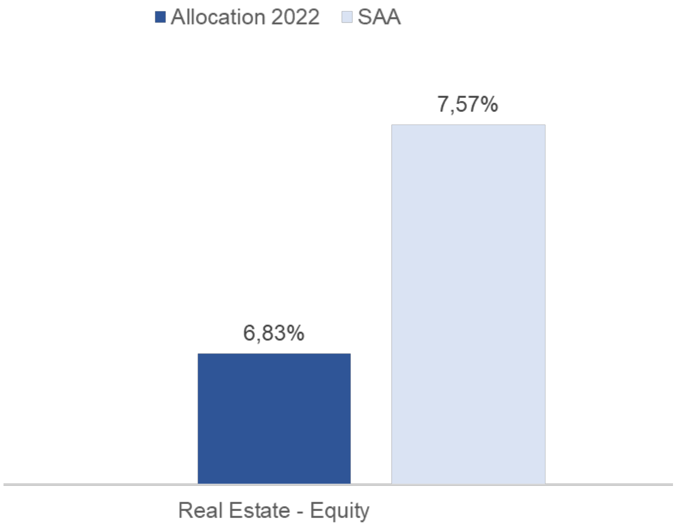


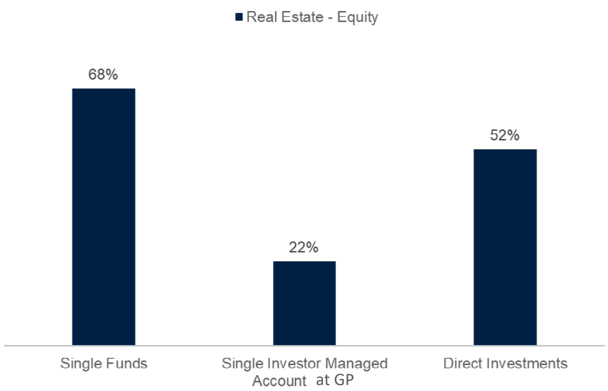
Real Estate Equity & Real Estate Debt

Real Estate Equity

Invested Participants **~78%**

Expected avg. return **~11.3%**

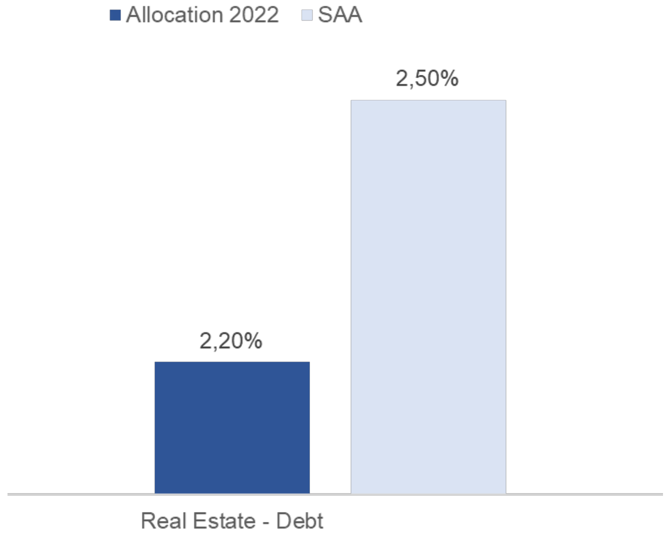




Real Estate Debt

Invested Participants **~45%**

Expected avg. return **~5.9%**

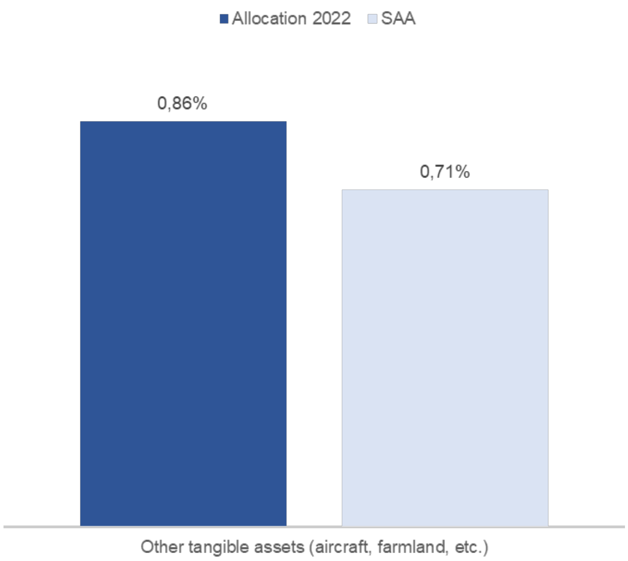


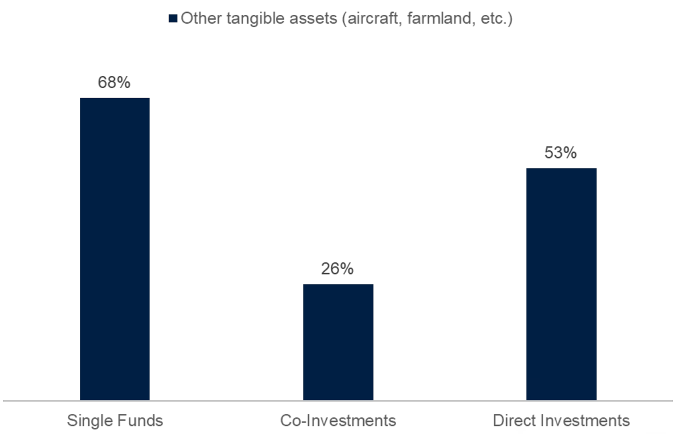
Other Tangible Assets and Commodities

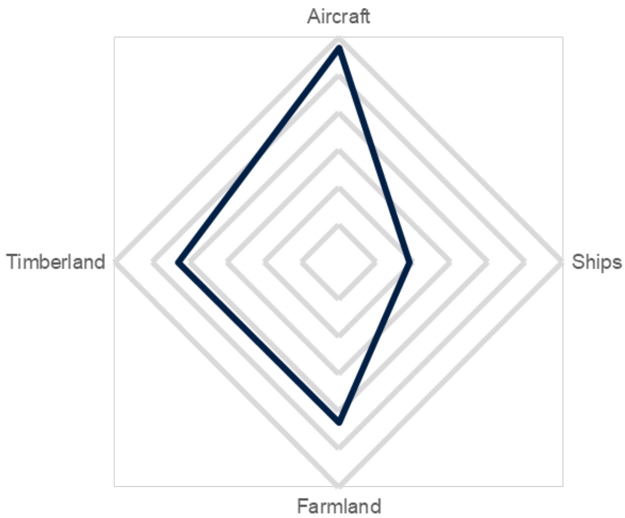
Other Tangible Assets

Invested Participants **~19%**

Expected avg. return **~5%**



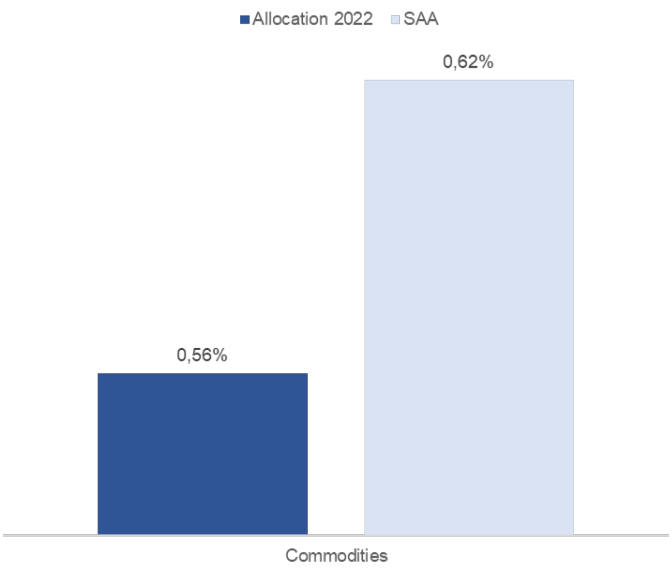


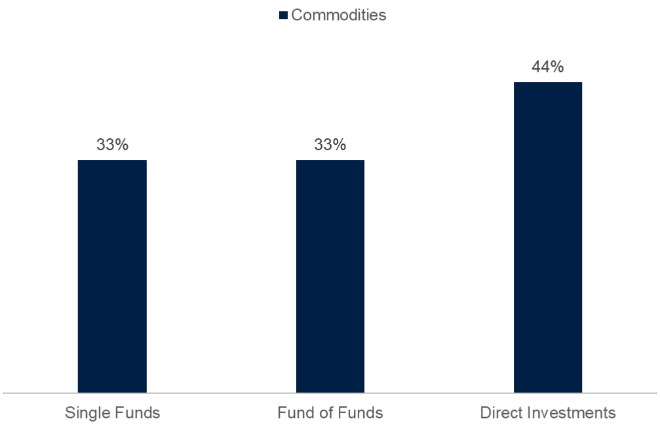


Commodities

Invested Participants **~11%**

Expected avg. return **~6.2%**



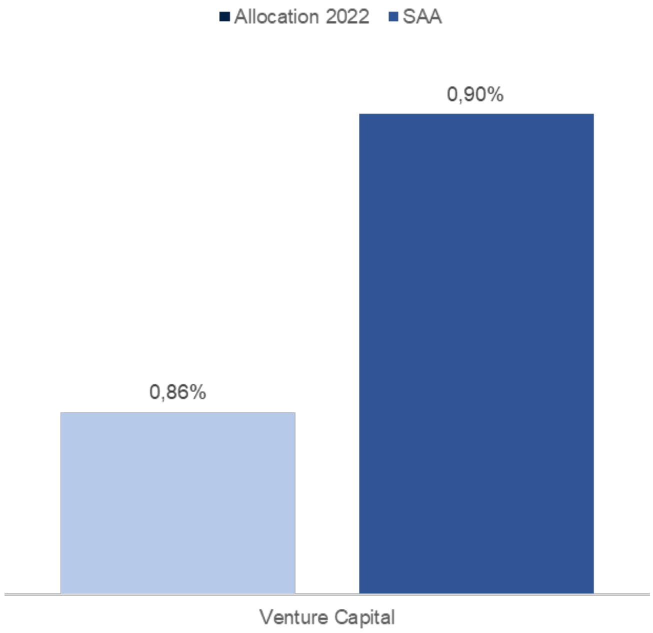


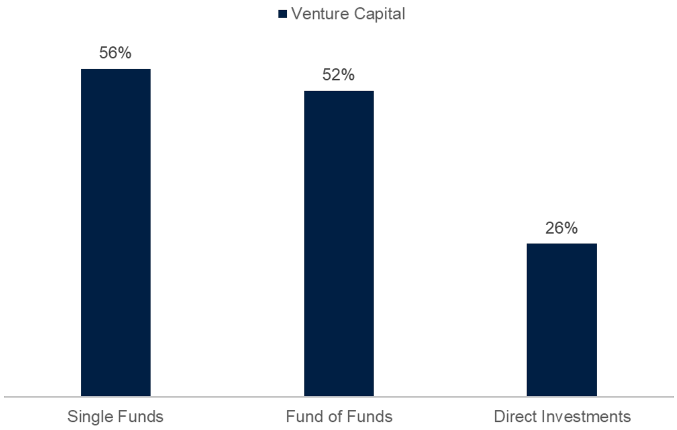
Venture Capital and Credit Specialities

Venture Capital

Invested Participants ~27%

Expected avg. return ~15%

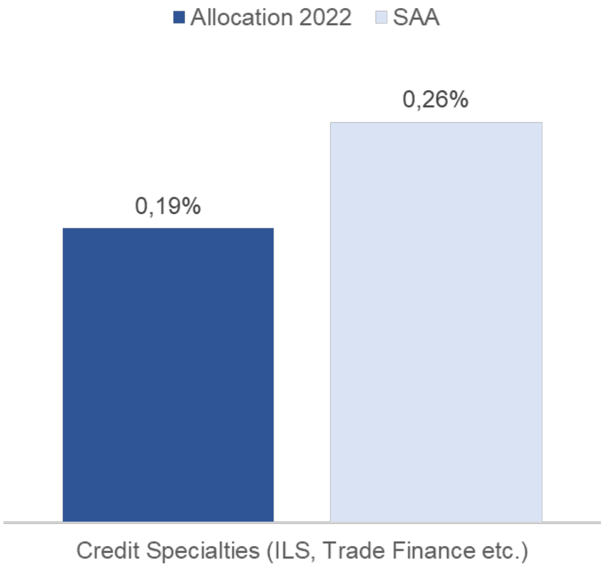


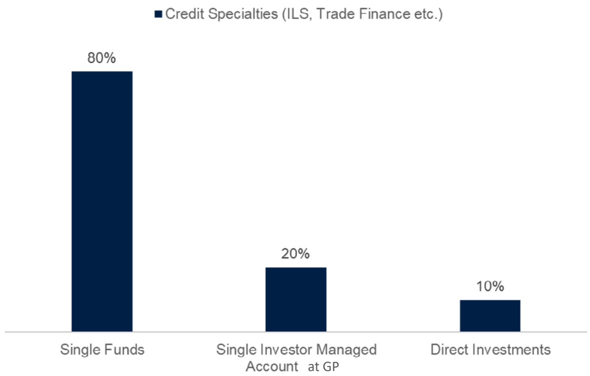


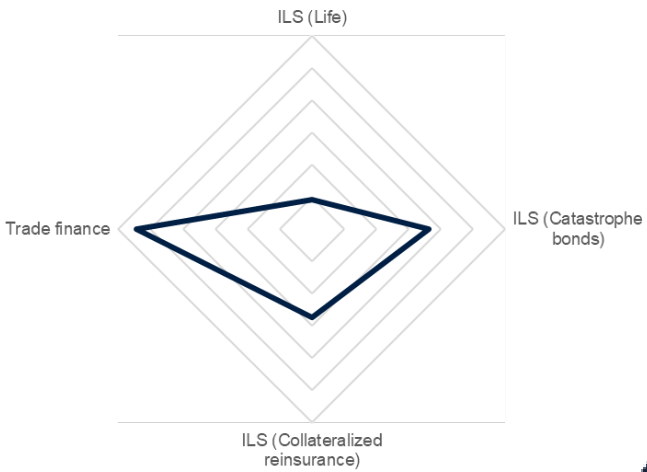
Credit Specialities

Invested Participants ~10%

Expected avg. return ~6.7%







Alternative Investor Landscape

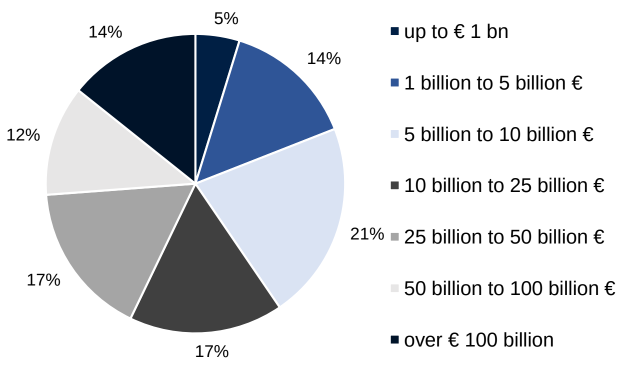
Insurance companies

Highlights

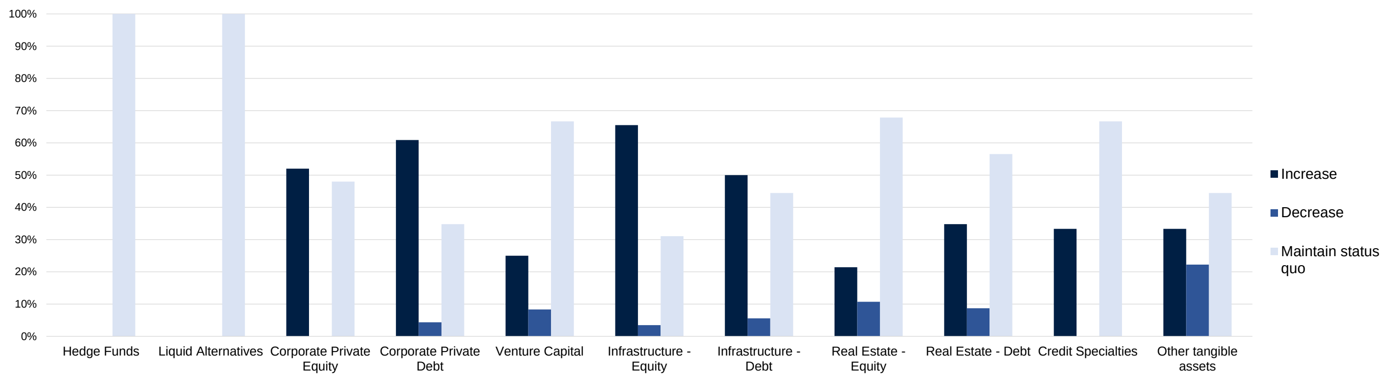
Average Size

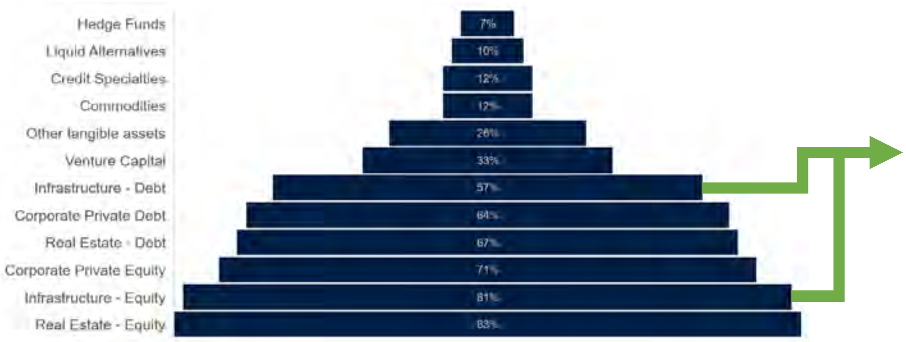
~ 34 Mrd. € AUM

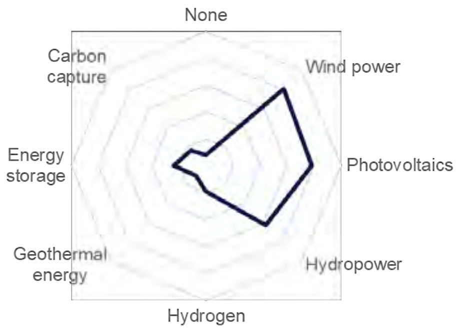
AuM



SAA Changes and Investors Allocating to each Alternative Asset Class







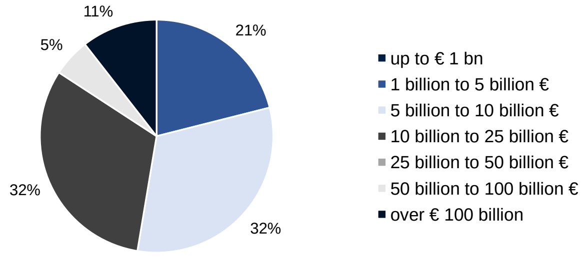
Pension Schemes (Versorgungswerke)

Highlights

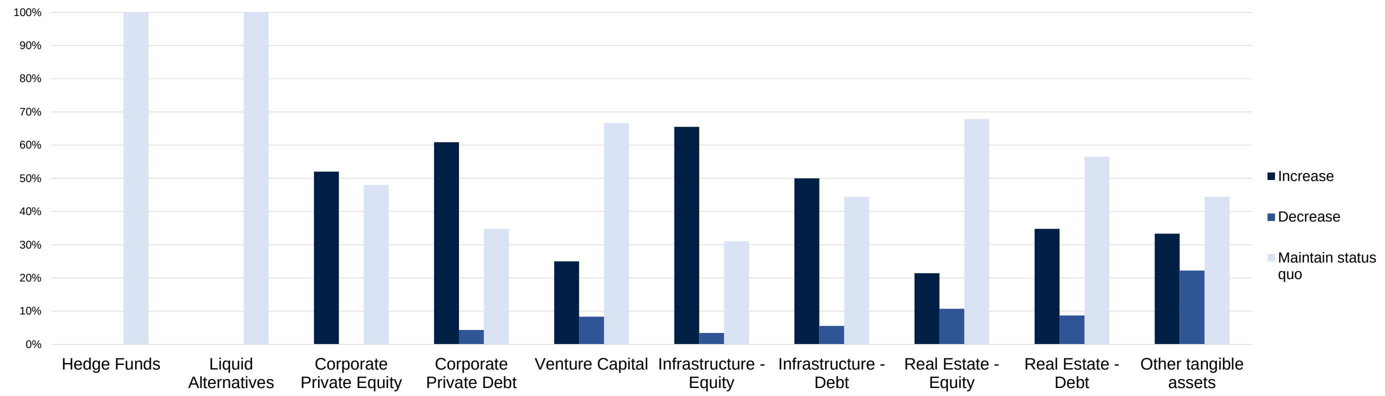
Average Size

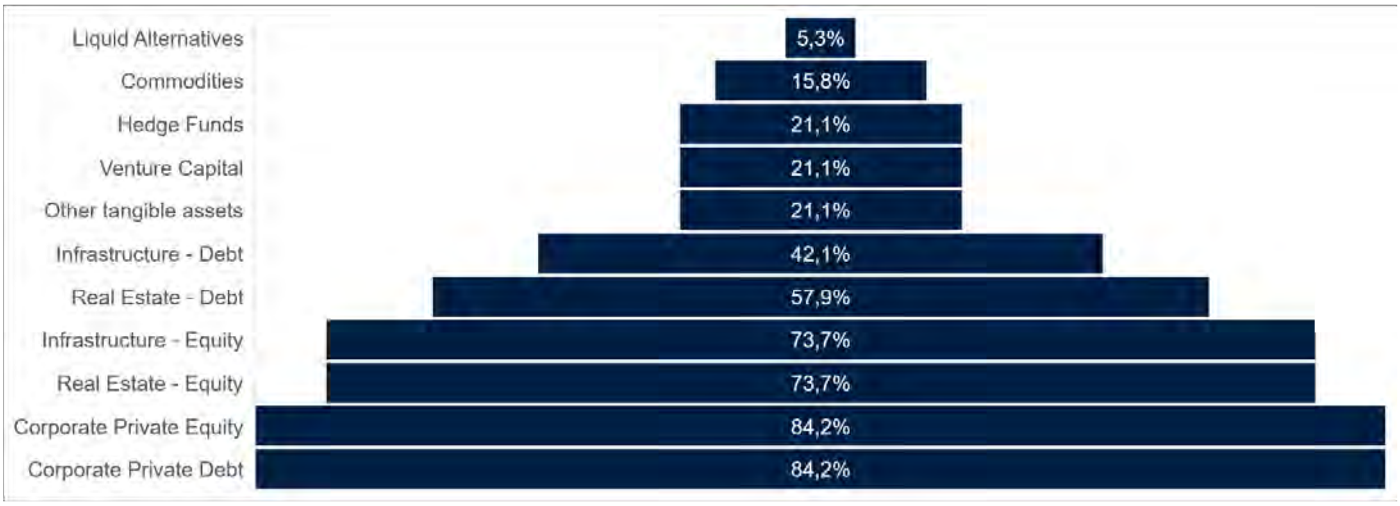
~ 23 Mrd. € AUM

AuM



SAA Changes and Investors Allocating to each Alternative Asset Class





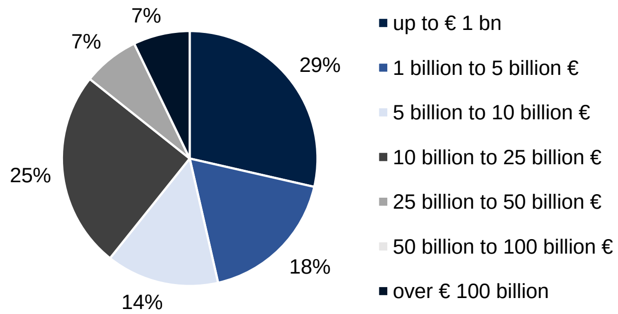
Pension Funds, Pension Plans, CTAs and Corporate Investors

Highlights

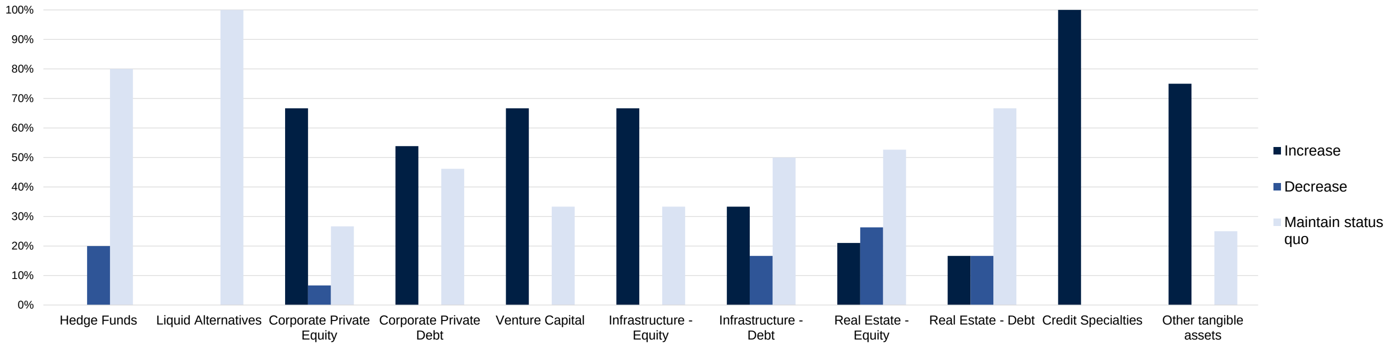
Average Size

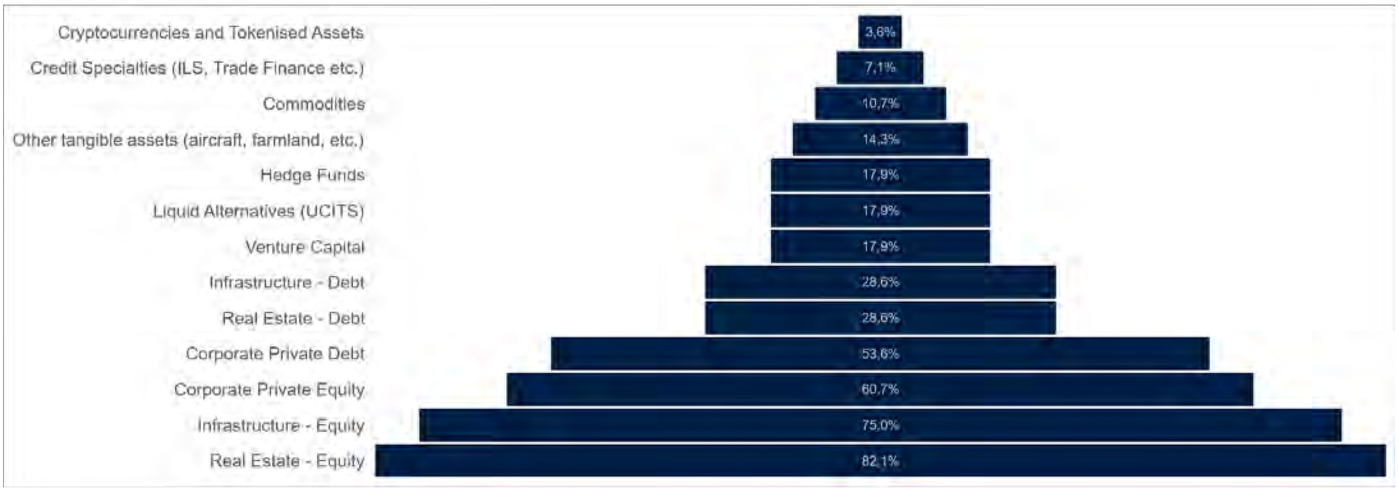
~ 16 Mrd. € AUM

AuM



SAA Changes and Investors Allocating to each Alternative Asset Class

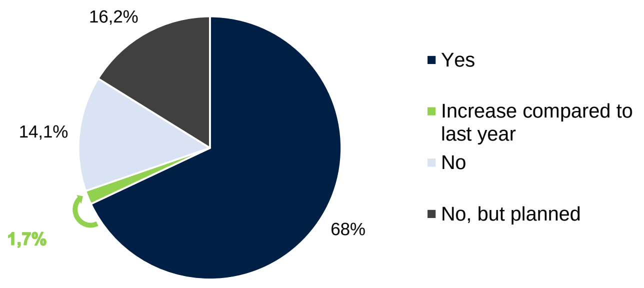




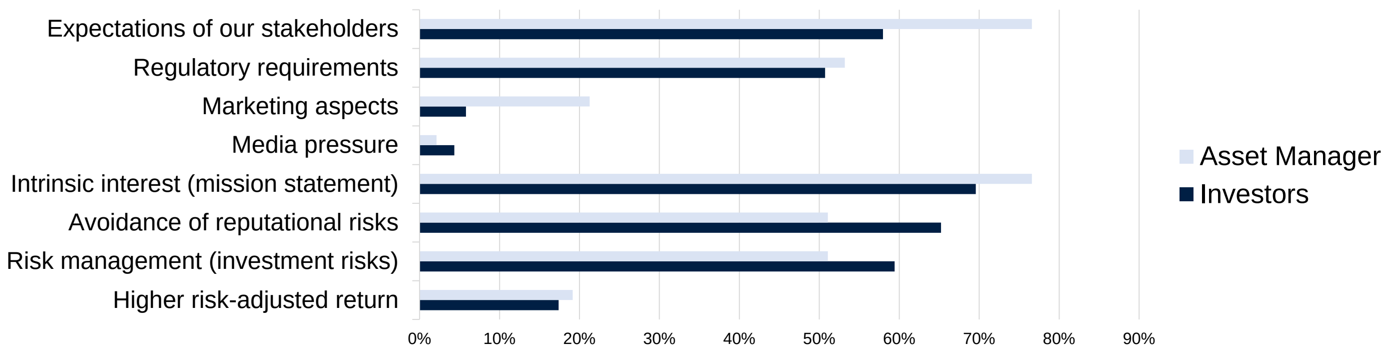
ESG - Alternative Investments Perspective

Besides hot topics such as inflation, rising interest rates, and economies at risk, one other subject is essential to the entire industry: ESG. There is no doubt that ESG will become an even more significant part of the industry in the future with the progress of the EU Sustainable Finance Initiative.

Investors pursuing an ESG strategy



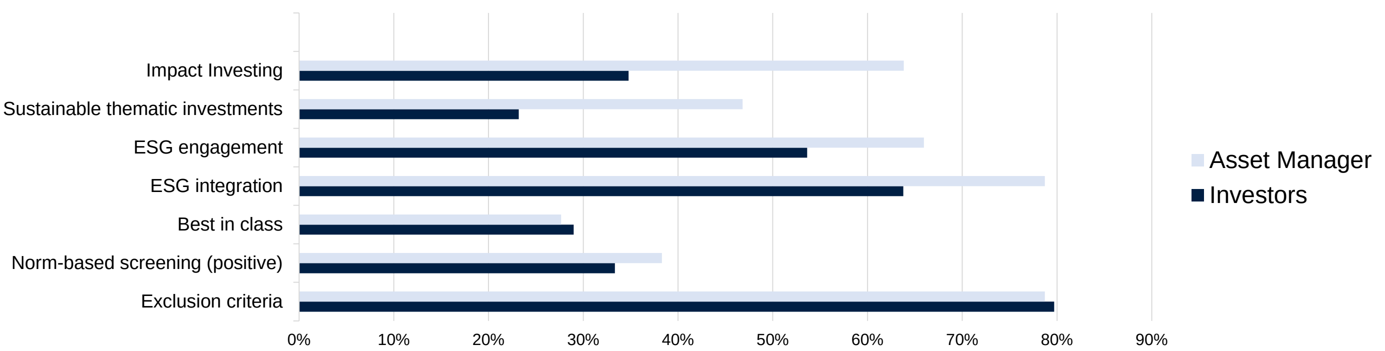
Reasons for Investing in ESG compliant AI



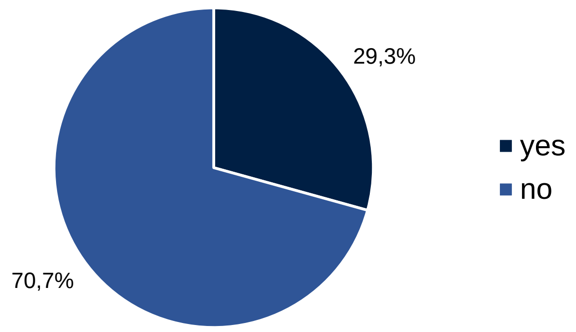
„We pursue an ESG strategy as part of our overall strategy. The focus remains on the risk/return ratio. If there are ESG alternatives that do not conflict with our strategy, the investment is made with an ESG focus.“

- large pension fund -

ESG Strategies



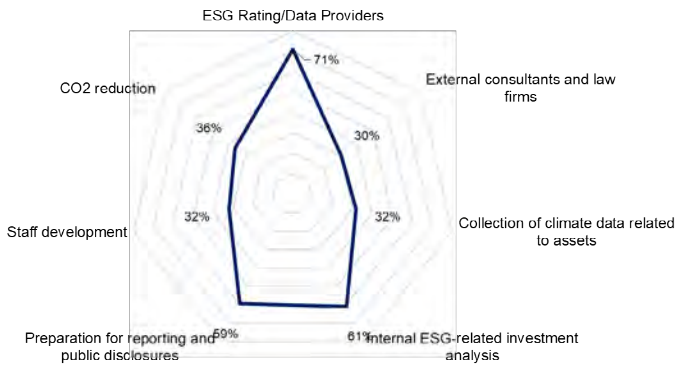
Does ESG compliance lower returns?



„Asset management should not compete with our foundations' project work. For this reason, we pursue specific S and G goals."
- small foundation -

„Lack of standards, many mandated asset managers, and poor data availability makes it difficult to implement a consistent ESG strategy."
- large pension scheme -

Used Measures and Analyses



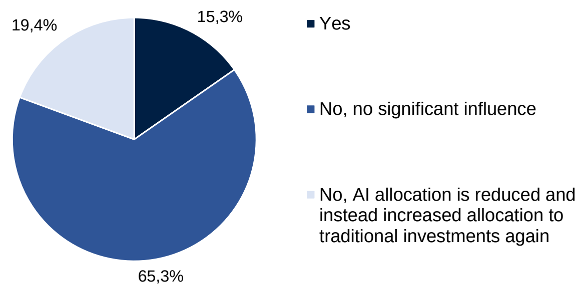
Already more than two-thirds of investors pursue a distinct ESG strategy on the investment side. A slight increase compared to the previous year. One-third of the respondents assume that ESG-compliant investments will mean sacrificing returns in parts.
The primary drivers for ESG-compliant investments are intrinsic interests, stakeholders' expectations, avoidance of reputational risks, risk management, and regulatory requirements. This is true for both investors and asset managers.

„Infrastructure managers can already offer a very high level of ESG transparency, as can some European PE managers. US managers are lagging behind."
- large corporate investor -

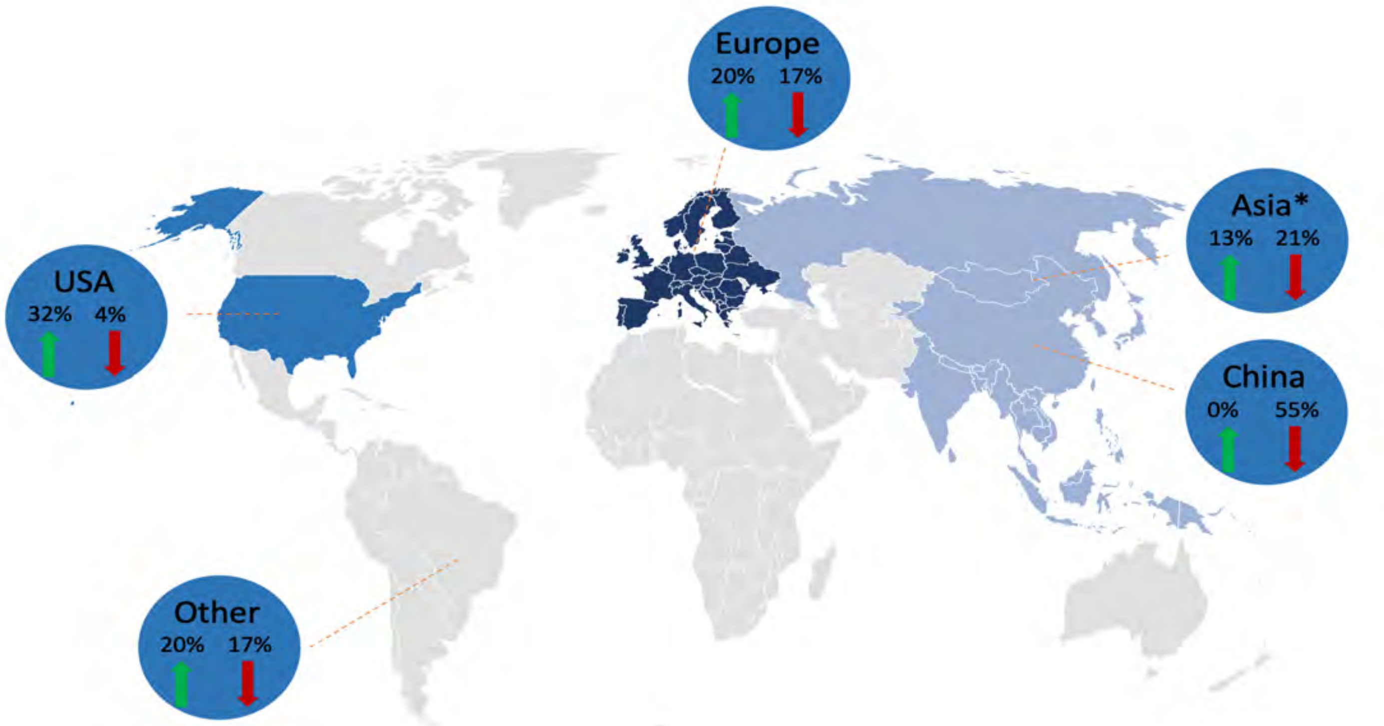
Inflation and Alternative Investments

This year's hot topics are the central bank's behavior, inflation, and market volatility. In the series „Interest rate turnaround and inflation" (Asset Allocation), we shed light on the implications for investors, asset managers, and service providers operating in alternative investments. The first paper, published in September, addresses the potential impacts on asset allocation. Equity and bond markets suffer from the stagflationary environment, while alternative markets remain relatively resilient. Currently, valuation adjustments remain to be seen until the end of the year.

Do inflation and rising interest rates cause a shift in SAA towards AI?



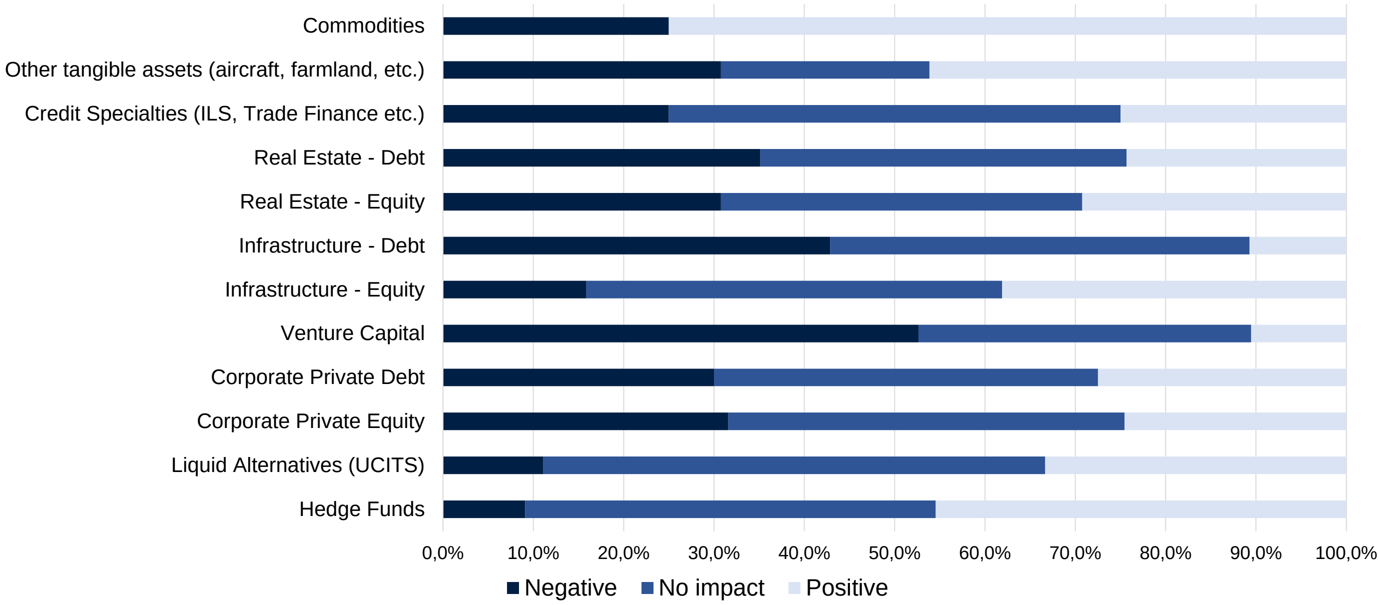
Influence of Geopolitical Crises on Global AI Allocation



* Asia excluding China

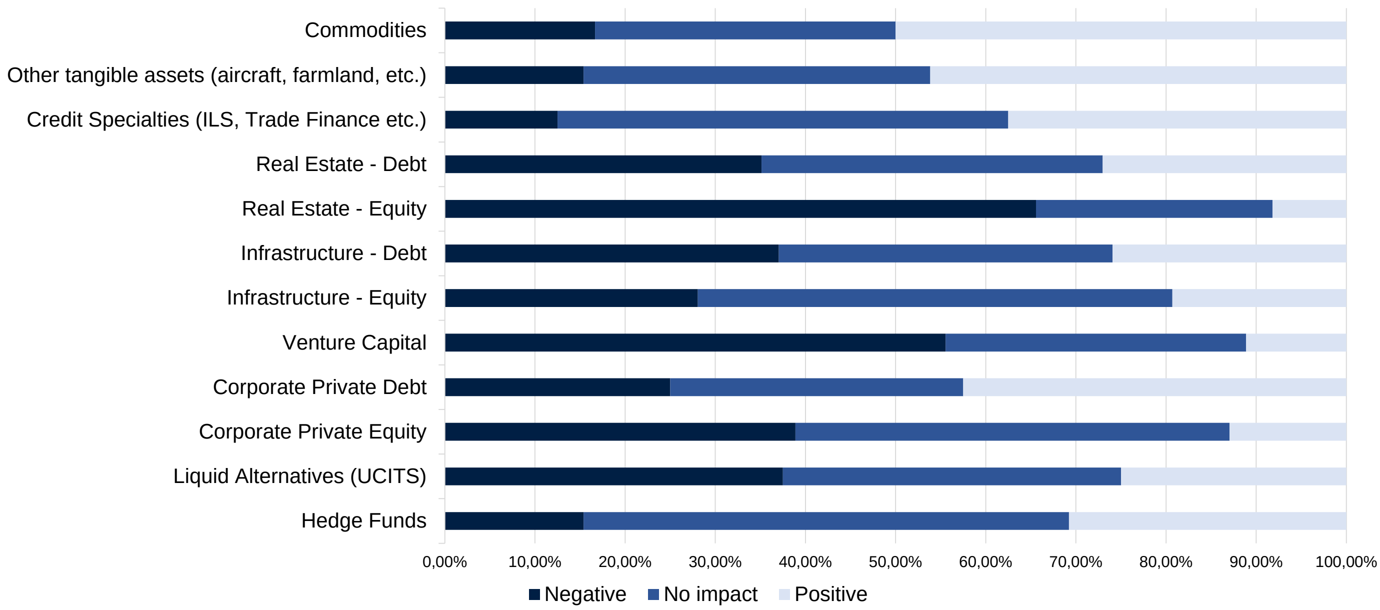
Most German investors (about 2/3) do not plan to shift their strategic asset allocation (SAA) between alternative and traditional assets because of high inflation rates and ECB's interest rate turnaround. A detail to point out is that a shift to Alternatives is observable for smaller and middle-sized investors. The multi-layered problem, disruption of global supply chains, influenced by China's zero Covid policy, the war in Ukraine, and the consequences, leads many investors to rethink their global allocation. As investors re-evaluate geopolitical and supply chain risks, they reshuffle their assets away from the Chinese market. One profiteer in terms of a higher allocation remains the US market, while all other markets remain stagnant in asset allocation. We separately queried the investor's thoughts about the effect of inflation and the current interest rate regime on the different asset classes. Sustained elevated inflation could burden equity projects if they fail to forward high prices. The effect on debt-related assets is more nuanced, depending on various factors such as the free float, the cash flow, default risks, and contractual obligations.

Impact of a persistant high Inflation



Proven to be resilient to elevated inflation are commodities, as they are technically interconnected to inflation and hedge funds & liquid alternatives, as they can deploy financial options to hedge. With rising interest rates, this year's monetary policy regime imposes a challenge across asset classes. As a result, growth-dependent assets, with riskier cash flows in the future and elastic counterpart demand, such as venture capital, may suffer, while infrastructure projects hold up comparably well. Once again, hedge funds and commodities seem suited to handle this turbulent market phase. An interpretation of relative strength remains difficult for a stagflationary scenario, meaning the combination of elevated and sustained inflation combined with a shrinking GDP. To correctly rank the relative strength of the individual asset classes, we used the investors' answers to form a regularized and standardized ranking. Hedge funds remain their edge over other asset classes in a stagflationary scenario, while commodities and other tangible assets perform comparably well. According to institutional investors, corporate private equity, in line with public equity, is expected to perform relatively worst compared to all other asset classes.

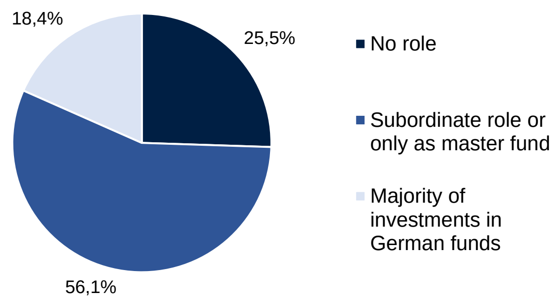
Impact of ECB's Monetary Policy and Rising Interest Rates



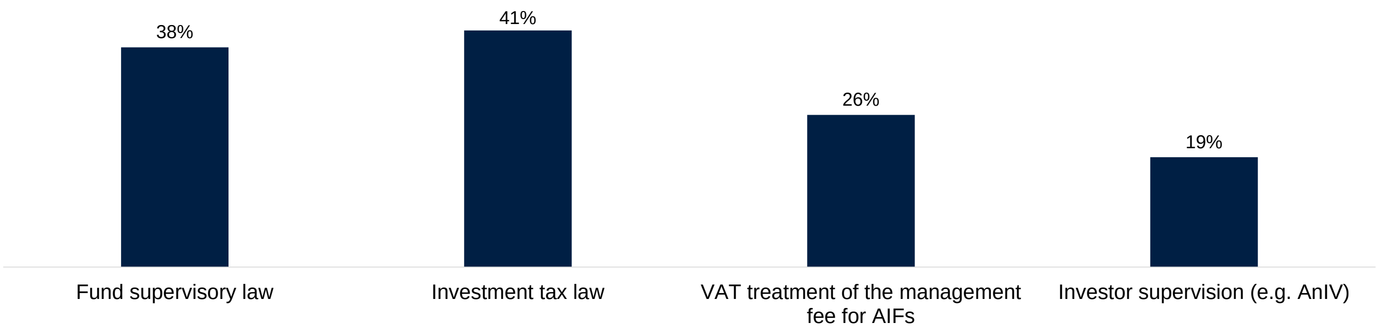
Law & Regulation

Portfolio expansion and structuring have always been significantly influenced by supervisory and tax law. Investment funds continue to be the preferred access route, especially for alternative investments, as this year's survey again confirms. With regard to the dominance of foreign, predominantly Luxembourg vehicles in fund structuring in the field of alternative investments, this year's survey asked for causes, especially since there have recently been various efforts to improve both tax law and supervisory law in Germany, in order to strengthen the German domicile.

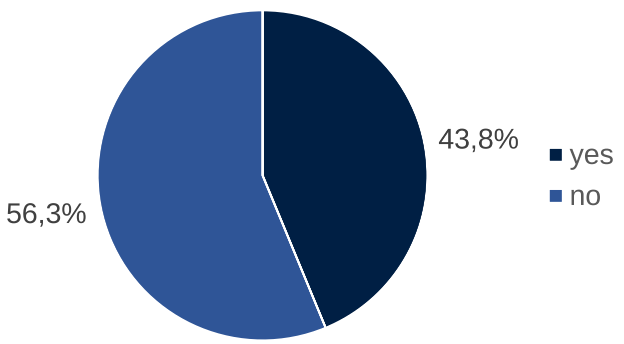
Role of German domiciled Funds in the AI Portfolio



Reasons against using German domiciled AIFs



In your opinion, are the different alternative investment strategies adequately reflected in the investment catalogue of AnlV?

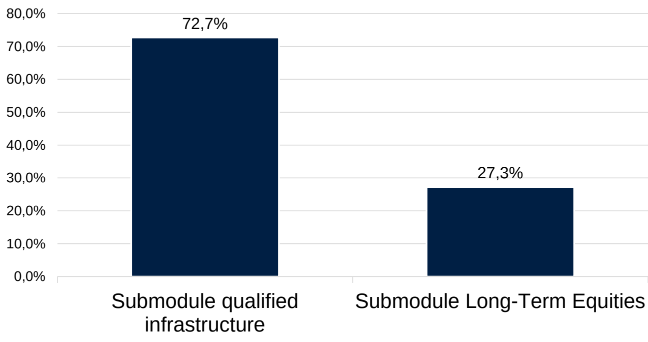


However, the assessment in this respect is also rather sobering from an investor's point of view. More than 80% of the investors surveyed stated that German fund structures play no or only a subordinate role for investments in alternative investments, at best in the context of a master fund. The main reasons against this from the investors' point of view are still investment tax law with 41% and investment supervision law, i.e. the KAGB, with 38%. More than a quarter of participating investors also criticize the unequal treatment of funds in the taxation of the management fee, which is generally not granted to AIFs - with the exception of open-ended special AIFs with fixed investment conditions - and thus puts them at a competitive disadvantage. The supervisory regime for the investors themselves is also criticized, especially with regard to the AnlV.

With regard to alternative investments, especially infrastructure and private debt, the general attribution to the risk capital ratio (especially as equity-like risks are regularly assumed and applied) does not reflect the reality in the investors‘ porfolio.
Among Solvency II investors, it is interesting to note that the options for SCR optimization introduced in the recent past, which also relate to investments in alternative investments, are being used. Thus, almost ¾ of the relevant investors use the sub-module „Qualified Infrastructure“ and almost 30% already use the sub-module „Long-term Equities“.

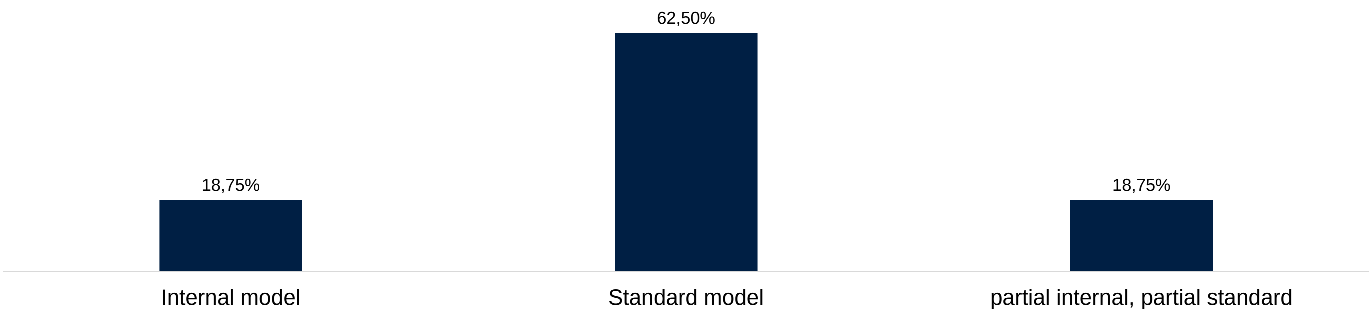
With both modules, capital adequacy can be significantly reduced compared to the general modules provided by the standard model under Solvency II, which is used by 2/3 of the respondents. The introduction of both modules is also largely due to the commitment of the BAI.

Sub-Models used for SCR Optimisation



In the end, however, it remains the case that at least German fund structures play no or only a subordinate role for investments in alternative investments and that there is a further and clear need for reform here, not only with regard to funds themselves, but also in the supervisory law for investors, in particular the AnlV, which no longer adequately reflects the investment reality of institutional investors.

Model used for SCR Optimisation



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