A stellar performance for fund of funds in 2015

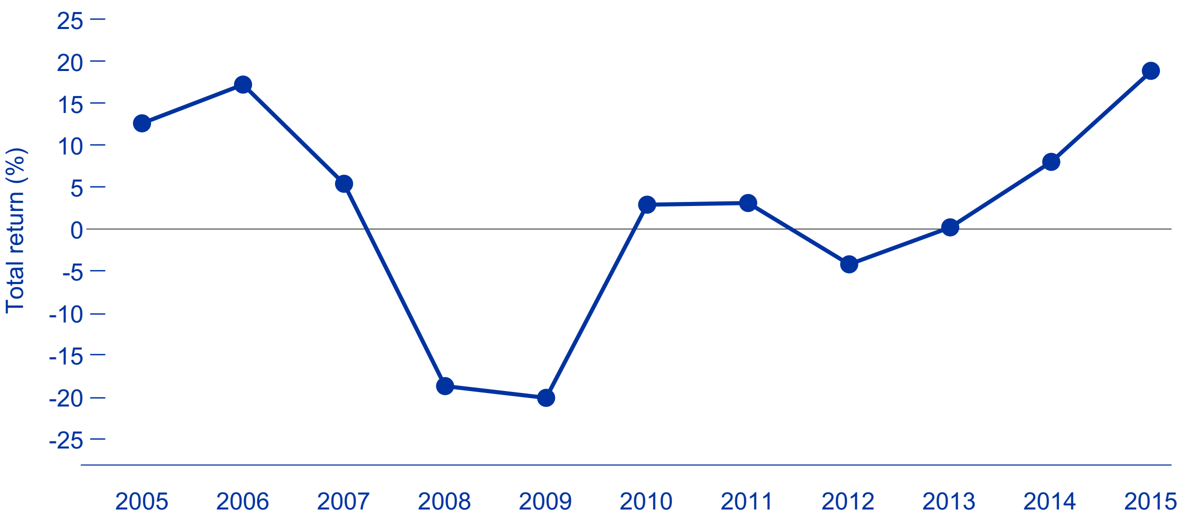
> Three consecutive years of solid growth for funds of funds
> Fund of funds delivered double-digit returns in 2015
> Vehicles that are large, core in style or have a global mandate outperformed the rest

Funds of funds account for 1.3% or €20.7 billion of the gross asset value (GAV) of non-listed real estate AUM worldwide according to the ANREV / INREV / NCREIF Fund Manager Survey 2016, cementing their significance as a route to non-listed real estate.

Three consecutive years of positive growth saw funds of funds achieving a solid double digit return of 18.7% in 2015. This is their strongest performance yet with core vehicles outpacing non-core ones and generating a solid total return of 20.4% compared with 13.4% for 2015.

Closed end vehicles have been steadily outperforming open end vehicles over the past few years. However, for the first time in seven years, funds of funds with an open end structure outperformed those with a closed end structure, and delivered a strong 19.4% in 2015 compared with16.1% for closed end vehicles.

Figure 1: Aggregate annual performance of funds of funds



Newer vintage vehicles, those with a year of first closing from 2008 onwards, outperformed older vintages, those with a year of first closing prior to 2008 by 11.9%, 25.7% compared with 13.8% respectively.

Vehicles with a non-European or a global strategy outperformed those with European mandates. Larger vehicles, those with a NAV greater than €300 million, delivered significantly stronger performance than those with a NAV of less than €100 million of NAV.

Despite the strong performance over 2015, operating fund of funds is not all plain sailing. A combination of changes in regulatory and supervisory regimes as well as shift in investor attitudes' towards greater control of their capital does have an effect in the overall proposition of fund of funds. However, these challenges notwithstanding, fund of funds continue to offer diversification, greater access to new products and markets, and the other associated benefits to investors especially those with limited capacity. This is reflected in the raising of new equity for these vehicles in 2015; of the total €123.6 billion capital raised in 2015, 4.0% was raised for fund of funds.

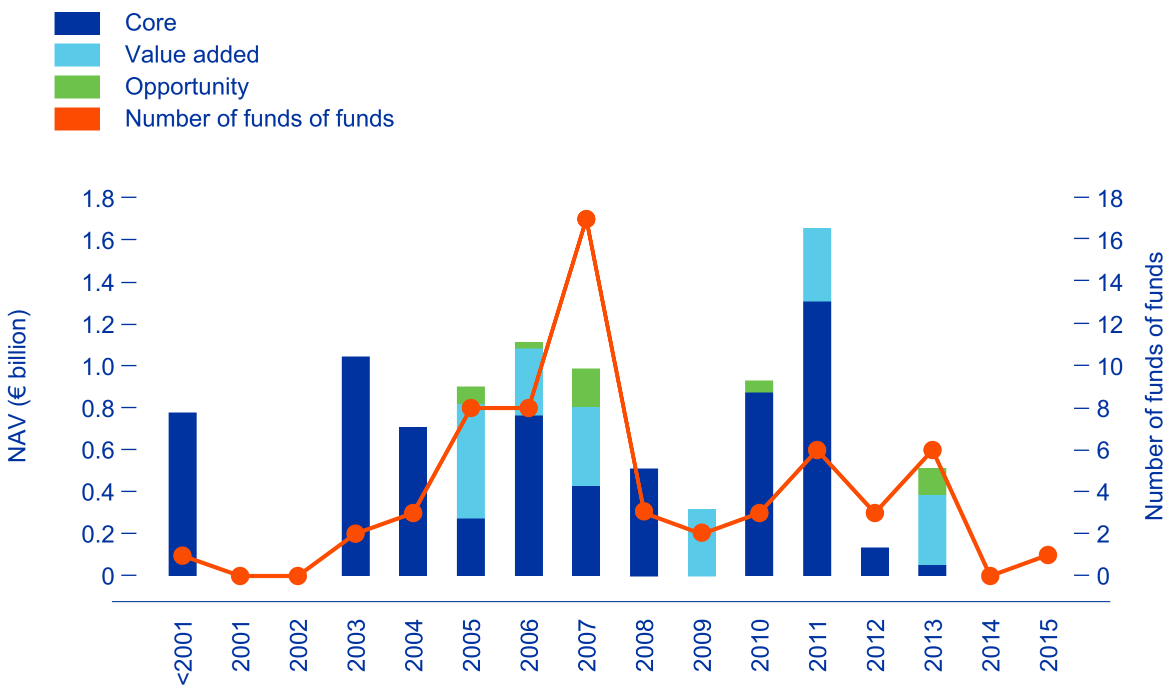
> 'As a group fund of funds delivered healthy performance in 2015'

Turning to the market landscape as represented by the Funds of Funds Vehicles Universe, which comprises 65 funds of funds collectively representing NAV of €9.6 billion as of Q2 2016, a series of interesting observations can be made.

In terms of style, the number of vehicles in the universe is almost evenly distributed among core (35.4%), value added (36.9%) and opportunity (27.7%). However, a closer examination of the split by NAV yields different results. The NAV picture shows that core fund of funds make up the largest share (71.8%) with the remaining 28.2% split between value added (23.1%) and opportunity (5.1%) vehicles.

New vehicles launches over 2010 to 2012 have also been dominated by core. However, this was not the case in 2013 when new vehicles launches were largely value added in style, following by opportunity with core making up the smallest share in value terms. Very few new vehicles have been launch over the past two years, none in fact for 2014, and only two in 2015.

Figure 2: New vehicle launches



Note: The sample is comprised of 63 vehicles representing a total NAV of € 9.6 billion.

With regards to terminations, the majority of fund of funds have no planned termination year, mainly because they have an open end structure with an infinite life span. Of the 23 vehicles without a planned termination year, the majority (87.0%) are open end and are mostly core in style (70.0%).

Further significant style differences emerge when the fund of funds universe is analysed by target net IRRs, target average total gearing as well as number of vehicles and managers invested in. In the first two instances, overall levels for non-core fund of funds are greater than those for core.

With their higher octane strategies non-core fund of funds have an average target net IRR exceeding a 10.0% threshold while it stands at 7.9% for core fund of funds. Similarly, the majority of non-core vehicles have an average total gearing exceeding 60.0% mark. It stands at under half, at 42.8% for core vehicles.

Conversely, the picture reverses when both number of vehicles and managers invested in are assessed. In both case core funds of funds opt for a greater number suggesting that core funds of funds pursue broader strategies and are much more diversified than their non-core counterparts. This may potentially explain their greater resilience to market volatility compared to non-core vehicles.

For further details contact research@inrev.org. The full report is available to members at inrev.org/library/publications