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YourQ&A: Will Institutions Shift Alts Investments?

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Question

Will this "crisis" affect an institution's asset allocation to alternative investments (hedge funds, private equity, etc)?

Third-Party-Marketer, Institutional, East Coast

Answer



Celia Dallas is head of published research and a managing director at [Cambridge Associates](#)¹.

We maintain our long-held belief that alternative investments play an important role in institutional investors' portfolios. In fact, as previously closed hedge funds open to new money due to redemptions and distressed investing opportunities, investors may have a unique opportunity to invest in top-notch funds. Furthermore, secondary markets may allow investors to obtain significantly discounted positions in alternative assets. However, it would be overly sanguine to assume that the landscape will remain unchanged. A number of managers already have fallen victim to market dislocations and consolidation will persist. Requisite skills for success are different today: managers using heavily-leveraged investment strategies are clearly at a competitive disadvantage in this environment.

Over the last decade, most institutional investors have increased allocations to alternative investment strategies, seeking diversification and return enhancement. The search for manager value added (alpha) fueled this move in an environment that saw high valuations dampen market return expectations (beta). Today, increasingly attractive equity and credit valuations raise expectations for returns from beta over the long term, although downside risk remains. The improved prospects for beta make manager selection in alternative assets critical, since beta exposures can be implemented relatively easily with low costs.

Answer



David Hammerstein is chief strategist at Yanni Partners, a division of GBS Investment Consulting, LLC.

The crisis will prompt institutions to rethink their asset allocations. These recent market events extenuate the potential degree of downside risk that's inherent in the markets, and the asymmetrical nature of capital market returns. These developments will prompt institutions to ensure a close integration of investment strategy development with their overall financial management. This will occur as institutions make sure portfolios are intertwined with the capacity to bear investment and liquidity risks.

Market conditions will also cause institutions to rethink their liquidity needs and their projected needs so they can ensure they have enough liquidity. No institution wants to be in a situation of having to sell equities in a down market. Always remember that it's vital to maintain a close link between liquidity management, cash management and the core asset allocation of the portfolio.

One asset class that is doing well in this market is U.S. Treasuries. On the alternative side, however, global macro strategies for hedge funds have done well. They have demonstrated some good diversification as opposed to other forms of alternatives.

YourQ&A is your opportunity to get your pressing questions answered by industry leaders.

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