GCM Grosvenor

STRATEGIC INVESTMENTS

In Brief

Q&A: Multi-Asset Investing

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Past performance is not necessarily indicative of future results. No assurance can be given that any investment will achieve its objectives or avoid losses.

Multi-Asset Investing
An Alternative Approach

As financial markets have continued to evolve, alternative investments have come to represent a key component of many institutional portfolios. Consistent with this evolution, an increasing number of investors and their consultants have begun to embrace a multi-asset approach to investing by relaxing some of the constraints imposed upon their managers. While the traditional "silo" approach to asset allocation remains largely intact, we believe the potential benefits of allowing managers to operate under more flexible, opportunistic mandates is increasingly apparent. Over the past several years, there has been a proliferation of these multi-asset class offerings. However, not all programs are alike and investors are cautioned to look under the hood.

In this edition of "In Brief," we discuss the benefits of a multi-asset approach, some key differences among programs, and investors' commonly-asked questions.

Q CONSIDERABLE ATTENTION HAS BEEN GIVEN TO MULTI-ASSET INVESTING IN RECENT YEARS. WHAT EXACTLY IS MEANT BY "MULTI-ASSET INVESTING" AND WHAT ACCOUNTS FOR THE INCREASED LEVEL OF INTEREST?

There is a wide spectrum of multi-asset solutions in the market, so it is difficult to generalize. That said, the basic premise is simple and has a lot of intuitive appeal.

Historically, the asset allocation process has grouped managers into discrete buckets based upon underlying exposures or market betas. This process is somewhat rigid as managers are subject to a number of constraints specified in the investment mandate. A multi-asset approach typically relaxes some or all of these constraints by allowing the manager greater flexibility in making tactical asset allocation decisions.

The earliest multi-asset programs generally took the form of "balanced portfolios" in which the manager combined either active or passive exposure to publicly-traded stocks and bonds in a single portfolio. In this sense, the resulting portfolio represented a collection of various market betas and the investment manager sought to add value through both tactical asset allocation and individual security selection.

With the widespread adoption of financial derivatives and alternative investments, the opportunity for skilled managers to add value through a multi-asset approach has increased immeasurably.

We believe a multi-asset approach that incorporates alternative investments allows for a richer opportunity set and additional levers with which to manage downside risk.

Q WHY SHOULD INVESTORS CONSIDER A MULTI-ASSET APPROACH IN THEIR PORTFOLIOS?

The process of grouping assets or managers into discrete buckets creates opportunities for those with the ability to invest in a less-constrained or unconstrained manner. As market prices ebb and flow, relative values change

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across asset classes as well as up and down the capital structure. There are often multiple ways in which to structure an investment. A multi-asset approach generally provides managers additional degrees of freedom, allowing them to select what they believe is the optimal expression for a particular investment theme.

In addition, multi-asset investing allows capital to be moved more seamlessly and opportunistically in response to changes in the market environment. This can avoid significant friction costs (both trading and opportunity costs) that occur when investors choose to move assets from one manager to another as part of a reallocation program.

We believe that multi-asset investing becomes more interesting when alternatives are incorporated into the mix. An unconstrained mandate may allow the manager to (i) invest in multiple asset classes, across the liquidity spectrum and up and down the capital structure, (ii) hold long or short positions, and (iii) utilize leverage and a broad range of financial derivatives for hedging purposes. Such investment flexibility is likely to produce a fundamentally different risk/return profile relative to other multi-asset programs consisting of long-only bond and equity exposures.

Q HOW DOES YOUR APPROACH DIFFER FROM OTHERS IN THE MULTI-ASSET SPACE?

First and foremost, we are active investors across the full spectrum of alternatives including hedge fund strategies, private equity, infrastructure and real estate. We believe we have a unique vantage point as we sit at the intersection of a tremendous amount of market intelligence and deal flow across our entire platform. Very few firms possess the requisite platform and capability to source from such a broad range of investment opportunities and execute in both public and private markets.

> Multi-asset investing allows capital to be moved more seamlessly and opportunistically in response to changes in the market environment.

Beyond that, there are two additional points that we think differentiate our approach from many others in the market. First, we invest in an unconstrained fashion – in both public and private markets across different asset classes, sectors, regions, financial instruments, and the entire liquidity spectrum. Second, we have a flexible implementation model and are agnostic about the execution method – which may be via direct investment or by co-investing alongside a manager.

We are careful to ensure that the term of the liabilities is consistent with the term of the underlying assets held. Having longer term capital allows us to embrace complexity and act as liquidity providers during periods of market dislocation where one is being adequately compensated. We believe successful investing often requires one to be somewhat contrarian in nature and/or willing to move out the liquidity spectrum.

Q HOW SHOULD INVESTORS THINK ABOUT INCORPORATING MULTI-ASSET PROGRAMS INTO THEIR OVERALL PORTFOLIOS? HOW DO YOU THINK ABOUT THE RISK AND LIQUIDITY PROFILE OF YOUR MULTI-ASSET PORTFOLIOS?

Multi-asset investing, by definition, is an attempt to move away from the more rigid style boxes that have been common in asset allocation for several decades. However, most institutional investors and their consultants continue to operate within such a structured framework. For investors who have embraced the multi-asset approach, we find they often include this type of exposure within an "opportunistic" bucket of their portfolios.

With respect to the liquidity profile, given the range of asset classes in which we invest, we think of these multi-asset programs as somewhat less liquid than a pure hedge fund program and somewhat more liquid than a private equity program. That said, we believe investors may be better served to focus on the intended outcome rather than the headline label.

Q IS THIS IS A GOOD TIME TO INVEST IN MULTI-ASSET PORTFOLIOS?

Unlike long-only equity and bond investing, we do not believe there is necessarily a good or a bad time for multi-asset class investing. By its very nature, we believe a multi-asset approach provides a richer opportunity set with potential to extract alpha from relative value trades and better manage downside risks. If structured appropriately, we believe a well-managed multi-asset class program opens up a range of opportunities and allows for a more tactical approach to investing.

At this stage of the cycle, we do not believe investors can continue to ride the equity, fixed income or credit beta trade and investors need to think about how returns can be manufactured. Many of the multi-asset offerings in the market are simply a collection of a firm's various bond and equity products and, as such, are largely beta-driven. We believe that investors who adopt a more opportunistic, off-the-run approach and are willing to move out the liquidity spectrum will be appropriately rewarded.

We believe we have a unique vantage point as we sit at the intersection of a tremendous amount of deal flow across the alternatives universe.

Q WHAT ARE THE CRITICAL INGREDIENTS FOR SUCCESS IN MANAGING A MULTI-ASSET PORTFOLIO?

Quality and quantity of deal flow is critical, as is the ability to execute quickly and efficiently. Successful programs require a depth of resources and expertise to source, diligence, execute and monitor an array of investments across markets. One of the most common questions among large institutional investors is whether to "build" or "buy" this capability.

By and large, investors have come to recognize the merits of a multi-asset approach and are drawn to the opportunistic nature of these programs. However, they often become quickly overwhelmed by the sheer volume of deal flow shown to them as they lack the necessary internal resources or expertise to efficiently process, diligence and execute in a timely manner.

Q HOW SHOULD ONE THINK ABOUT BENCHMARKING PERFORMANCE OF MULTI-ASSET PORTFOLIOS?

This often depends upon the composition of the underlying assets. Most of the earlier programs that consisted of long-only stock and bond exposures were benchmarked on a relative basis to a weighted average return of the underlying assets (e.g., 60/40 stock/bond mix). With the expansion of these mandates to include alternative investments, there has been a shift to an absolute return orientation.

The ability to be either long or short, and to utilize leverage as well as a wide variety of derivative instruments, gives rise to a fundamentally different risk/return profile for which a specific absolute return benchmark tends to be more appropriate. This is often expressed as either a spread to risk-free rates (e.g., 90-Day U.S. T-Bills + 1,000 basis points) or some measure of inflation, such as CPI. ■

ABOUT GCM GROSVENOR STRATEGIC INVESTMENTS

Our Strategic Investments Group is a dedicated investment team that assesses the relative value of opportunities across GCM Grosvenor's global investment platform and executes what it believes to be the best opportunities, generally via direct investments and co-investments. The team constructs and manages opportunistic multi-asset class commingled funds with distinct risk/return profiles.

ABOUT GCM GROSVENOR

With approximately $50 billion in assets under management, GCM Grosvenor is one of the world's largest and most diversified independent alternative asset management firms.

GCM Grosvenor has offered alternative investment solutions since 1971. The firm is headquartered in Chicago, with offices in New York, Los Angeles, London, Tokyo, Hong Kong and Seoul. GCM Grosvenor serves a global client base of institutional and high net worth investors.

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