DeMarche

Insight Paper: Alternative Investments Workshop Summary

"The Evolution of Alternatives," Christina Danner, CFA, Senior Consultant, April 2018

As part of our 2018 DeMarche Programs in Finance and Investments Series, we recently hosted several workshops on Alternative Investments. The secular bull market for fixed income is over now that interest rates have stopped declining. And with stocks up nearly 300% since 2009, many expect a challenging market environment for the years to come. Institutional investors are increasingly utilizing alternatives in their portfolios to mitigate risk and enhance return. Below is a summary of some key takeaways from the workshop.

Alternatives are defined as non-traditional asset classes/strategies (not stocks, bonds, or cash. They are investments that are often not suitable for a typical investor. They are usually available only to "accredited investors" and typically are subject to less regulation (although SEC/NASD still play an active role). Common alternatives used by institutional investors include Private Equity, Real Estate, and Hedge Funds.

A reasonable case for investing in Alternatives can be made today. Because they are less understood, their markets are less efficient, providing opportunities for alpha. Additionally, we are seeing decreasing management fees and improving transparency. ESG-focused investors are finding that "Impact" investing is possible, and alignment of interest is often improved. Finally, weak correlation with other investments improves portfolio diversification and enhances the risk/return equation.

It is understandable that investors have issues and concerns about these markets. There is an increased complexity of strategies and agreements/contracts, and additional due diligence is required. An investor must get comfortable with higher fees, less liquidity, and greater performance dispersion compared to traditional assets. Four investment managers discussed their strategies, and highlights follow:

Palmer Square Capital Management, *"Alternative Credit: Comprehensive View of Collateralized Loan Obligations (CLO)."* A CLO is a diversified pool of institutional floating rate large bank loans. Key features of senior secured loans are: senior claim on assets, covenant protections, floating rate, short duration, low interest rate risk, low default rates, and significant yield potential.

Manulife Asset Management, *"Global Timberland and Farmland Investments."* Timberland and farmland are real assets managed by the private markets natural resource group. Investments are made in various forest types (softwood/hardwood plantations, mixed natural forest) and crop types (annual row crops and perennial permanent crops). Timber and farmland are natural real assets with a biological growth component, similar investment characteristics, and return. They provide diversification benefits, inflation protection, good cash yields, and the ability to contribute to ESG/impact investing goals.

Private Advisors LLC, *"Opportunities in Small Company Private Equity."* The typical portfolio attributes include first institutional capital, established businesses, strong product/service offerings, and returns generated via business building. Strategies include buyouts, growth equity, and turnaround/distressed. Companies range in size from $10-200 million enterprise value.

Gresham Investment Management, *"Commodities Explained."* The role of commodities in a portfolio is commonly recognized/accepted as a means of portfolio insurance against inflation. The asset class is currently attractive because of relative valuations, improving economic conditions, rising interest rates/inflation, and growing global population.

If you would like to receive more detailed information on our discretionary consulting services, please contact Tom Woolwine, President, at (913) 384-4994 or twoolwine@demarche.com.