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Ultra high net worths seize on alternative investment protection

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Jamie Dimon’s alternative investments summit had 200 guests, representing $483bn in net wealth. Source: Supplied

IT is no secret that the key conversation in Australian ultra high net worth wealth advisory at the moment is based around what’s known as “alternative investments”.

This should not come as a surprise considering the particularly precarious international backdrop.

Australia’s global private banks and wealth advisory firms are working closely with family offices and UHNW individuals on a wide array of alternative asset allocations in a direct effort to ensure meaningful returns, come what may, this year.

In understanding the current investment trends within the alternatives space, it is imperative to appreciate why this asset class appears particularly attractive to an investment community known for its conservativeness, risk aversion and preference for liquidity over illiquidity.

Alternative investments, which include private equity, hedge funds and “real assets”, have been customarily favoured in volatile times because their expected returns claim lower correlations to the traditional asset classes of equities, bonds and cash.

Within a year in which all three of these traditional allocations are under considerable pressure, alternatives become an important portfolio keystone.

Koby Jones, managing director of the SILC Group, notes that "as a specialist alternatives solutions provider, we are seeing a heightened interest for alternatives in Sydney, Melbourne and Perth from family offices, largely because of growing concerns about traditional investments in 2015".

Jones goes on to add: "These clients are also well allocated to real estate and real assets such as their family's businesses, so other solutions such as specialist hedge fund managers and wholesale private equity opportunities become attractive in this landscape."

At the recent premiere alternatives event — Jamie Dimon's JPMorgan Private Bank "Alternative Investment Summit" in Key Biscayne, Miami, Florida — the following investable themes and key takeaways were identified.

Of the approximately 200 attendees representing $US375 billion ($483bn) in net wealth, 66 per cent of the audience thought oil would remain range-bound for the coming year; 55 per cent thought the same for global equities; and 58 per cent believed central bank divergence would be the biggest story of this year.

Meanwhile, alternative managers focusing on credit markets suggested the two key investable themes for this year were found in European credit and energy markets.

● On European credit, subdued growth in Europe creates compelling credit opportunities particularly because banks continue to shed non-core loans at an accelerated pace.

Eurozone banks have reduced medium-term lending by about €135bn ($198bn) since 2014.

● On energy markets the consensus was that the energy price decline is creating a once-in-a-decade opportunity to build and create the next generation of leadership in that industry.

Summit panellist David Weindreich of Och-Ziff Capital Management Group, a leading global alternative asset manager, commented: "The right play was that which focused on the longer-term opportunities, so that you don't have to be right on directionality (in the short-term)."

Not surprisingly, technology was also a key thematic identified at this year's summit and the point was made that every company in every industry is being disrupted by technology — the winners will be those who use technology to their advantage.

Drawing on these comments, trends and timely sentiments, family offices and sophisticated wholesale investors are currently being presented diversified hedge fund solutions as a way to achieve asymmetric returns (investment returns which are unevenly distributed) using strategies and approaches that simply do not exist within traditional equity or fixed-income investing.

As you can see from the graphs above truly diversified hedge fund portfolios historically provide much sought after downside protection when markets go awry.

This matters greatly to Australian family offices, who as noted earlier, alongside their global peers, believe the biggest story of 2015 will be the divergence of central banks, with the US Federal Reserve expected to lift interest rates while the ECB, Bank of Japan and others are widely expected to continue loosening them.

Private equity investments, another category of alternatives, can also be an attractive long-term complement to a traditional listed equity allocation.

Private equity funds are long-term pooled investment vehicles that acquire, manage and monetise portfolios of privately held companies, debt securities and other opportunities not broadly available to retail investors.

With an increasing sophistication within these funds in recent years, many private equity managers in 2015 have targeted investments across the energy value chain in the North American energy sector. This is by no means a new thematic but it is one receiving renewed interest.

In addressing family offices' concerns regarding liquidity, when making such styles of investments, Sam Edwards, regional head of alternative investments at HSBC Private Bank believes that "liquid alternatives" or "liquid alts" may be the solution for these investors moving forward.

Liquid alternatives are a subcategory of alternative investments that provide daily liquidity and can often be tradeable on global bourses.

What makes them attractive to these conservative groups is that they are considered to be return streams and not necessarily strategies per se.

This distinction is important when considering volatility, costs and ongoing management.

Investing in liquid alternatives helps deliver a return stream that is not driven by shifts in the economic outlook or directionality of the markets but rather by the dynamics of the investment decisions.

These investment decisions may be discretionary in nature (a manager electing to invest in one currency relative to another) or systematic (a structured, repeatable investment process to generate return streams uncorrelated to investable markets).

Seeking out such examples of additional alternative investments does not mean that the global investor should under-allocate or sell down existing traditional asset class investments but it does mean a rethink surrounding their existing mix.

Alternative investments are important to the global investor and ignoring this trend and misreading the winds could well be a costly mistake.

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