Some alternative asset classes are synonymous with active management. The CAIA Association’s Level I book states that one of the characteristics of alternative assets is active management, and one of its goals is to add value through active management. Recent empirical evidence casts doubt on whether active management of equity portfolios can add value, especially after fees. These studies report that since 1926, 42.6% of US stocks, and since 1990, 61% of non-US stocks have had lifetime buy-and-hold returns that exceed the return on the one-month T-bill. Another study reports that since 1980, more than 66% of stocks belonging to the Russell 3000 underperformed the index. Finally, another set of studies reports that since 1990, about 80% of annual realized excess stock returns on US stocks have occurred on less than 2% of trading days. The implication is that active management of long-only equity portfolios is doubtful to add value consistently. The long-only manager must be skilled enough (a) to identify the less than 10% of stocks responsible for the bulk of market returns and (b) to be fully invested on those crucial days when equity markets provide the bulk of their returns.

The fact that average stocks perform poorly means that long–short positions are needed to add value and skill in identifying the stocks with poor prospects is of utmost importance. Further, it appears that buy-and-hold strategies that do not involve publicly traded equities could represent another source of value added by alternative investments. The overall lesson is that institutional investors should seek highly diversified long-only portfolios for publicly traded securities and allocate to active public equity strategies only if they have a firm conviction about the manager’s skill. Finally, these investors should have a meaningful allocation to non-publicly traded assets, from private equity and debt to real estate and infrastructure.

This issue of *The Journal of Alternative Investments* provides new insights into some of these asset classes. It covers private equity, hedge funds, and exchange-traded funds. However, the issue begins with two perspectives on the impact of the COVID-19 pandemic on markets and investments. In “The Ultimate Safe Haven,” Mike Nigro argues that perceived safe-haven assets are not guaranteed to produce positive returns in all market downturns. For example, non-cash safe haven assets can be wildly volatile and unpredictable during market crises, while cash exposes investors to currency and inflation risk. In selecting the safe-haven assets that best meet a program’s needs and long-term objectives, the author believes it is essential to understand the risk exposures that financial safe havens carry and to consider diversifying safe-haven exposure so as not to rely on a single asset for protection in a market downturn.

Jason Garick offers his perspectives on robust and effective risk management practices in “Post-COVID-19: Rising from the Ashes.” The author argues that by leveraging predictive analytics and big data, private equity funds’ operational risk professionals can substantially reduce operating losses of portfolio companies. The article briefly explains the strategies a general partner can implement across the

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portfolio companies to improve portfolio margin and accelerate earnings that track directly to the bottom line.

The article “Private Equity and the Leverage Myth” by Megan Czasonis, William Kinlaw, Mark Kritzman, and David Turkington discusses the challenges of applying traditional portfolio optimization techniques to private equity. The primary difficulty is the artificially low volatility of the reported returns. As readers of this journal are fully aware, this arises because private equity returns are based on appraised values of portfolio companies. As an alternative to observed volatility, some investors have argued that private equity volatility should be estimated as leveraged public equity volatility because private equity companies are more highly levered than publicly traded companies. However, this approach yields unrealistically high values for private equity volatility. The authors offer practical guidelines for leveraging public equity returns to come up with more realistic volatility estimates.

Christoph P. Wessendorf, Jared Schneider, Kai Shen, and Orestis Terzidis observe that the valuation of early-stage technology ventures sometimes is referred to as an art instead of as a science. However, an objective and practical valuation is critical to venture capitalists for making sound investment decisions. The article “Valuation of Early-Stage Technology Ventures: An Approach to Derive the Discount Rate” develops an approach to derive the discount rate that accounts for a missing data history and subjectivity in a venture’s early stage. This approach is based on previous research analyzing the impact of subjective determinants of a venture’s value. The authors report promising results that deal with the valuation of three early-stage technology ventures.

In “Venture Capital: An Analysis of Investment and Exit Pattern of Indian Firms,” Rakesh Kumar and Mohammad Firoz review the investment and exit patterns in India’s venture capital segment. Readers of this journal who are not familiar with the Indian IPO market will find the information provided here useful in developing venture capital investment strategies involving the emerging Indian private equity market. For example, the authors report that the information and technology-related industries hold 58.49% of the total investments made since 1998. Further, Indian VC firms exited mainly through initial public offerings, with merger and acquisition exit strategies being a distant second.

“Hedge Fund Alpha: Cycle or Sunset?” by Rodney Sullivan observes that the hedge fund industry has grown from $200 billion in assets under management around the turn of the millennium to now over $3 trillion. The author seeks to demystify hedge fund strategies by evaluating fund performance attributed to the markets and other well-known systematic factors, emphasizing outcomes before and after the 2008 GFC. Sullivan reports that after adjusting for the risk of stock and bond markets, hedge fund managers as a group have shown a marked decline in risk-adjusted alpha in the 10 years following the GFC. The article provides additional insights into the changes in the risk exposures of various strategies. Armed with the information provided by this study’s results, investors should be better positioned to make more-informed decisions in deciding hedge fund strategy allocations.

David Blitz and Milan Vidojevic offer one of the first comprehensive studies of risk–return patterns of exchange-traded funds (ETFs) in “The Performance of Exchange-Traded Funds.” The authors argue that while ETFs are commonly regarded as an efficient, low-cost alternative to actively managed mutual funds, their perceived
superiority is mostly anecdotal. The authors evaluate the performance of a comprehensive, survivorship-bias-free sample of US equity ETFs. They find that ETFs have collectively lagged the market by an amount similar to the widely documented underperformance of active mutual funds. The authors perform textual and regression-based analyses to identify factor ETFs and show that most of these have also failed to beat the market. They conclude that from a pure performance perspective, ETFs’ allure finds little support in the data.

In the final article of this issue, Jonas Tobias Schmitz investigates stock returns surrounding the date that an activist hedge fund begins to exit its position. The article “Does the Disclosure of a Hedge Fund Stock Sale Influence Respective Stock Returns?” focuses on the initial sale of a target’s stock. The author estimates abnormal returns on the target stock using factor models and compares its return with the S&P 500 Index’s performance. Further, the author shows that a hedge fund’s initial sale of a target’s stock leads to stagnating abnormal returns when activists are successful and negative abnormal returns otherwise. The results reported here have important implications for existing shareholders of the target company and those investors who attempt to benefit from cloning activists’ investment strategies.

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