



Avengers, alternatives and a fresh investment environment

Few would have predicted the turbulent evolution of Marvel Comics – from bestseller through bankruptcy to box office smash – would pre-empt the path of financial markets. But the investment world also featured 90s hysteria, early 00s excesses and a game-changing blow-up in the form of the global financial crisis. For Marvel, the outcome was a reformulation from paper to cinema must-see; in the investment world, we are seeing the revision and reboot of alternative investments.

In 1991, I was 14 years old and Marvel Comics published X-Men #1. It was the second series by the iconic group, written by industry veteran Chris Claremont, and pencilled by up-and-coming artist Jim Lee. The comic-book sold 8.2 million copies and still holds the record for the best-selling single-issue comic of all time.

Several trends facilitated this success. First, a new group of artists had begun to bring showmanship never seen before to the comic book market. Second, the rich valuations that early issues of classic comic-books reached induced a tremendous misread by collectors, who started hoarding anything that showed a #1 on the cover – with

PUBLISHED
July 2018

READ TIME
10 mins

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 Alternatives to core fixed income

publishers responding by launching scores of #1s every year.

When a little older and at university, I wrote a piece for my microeconomics class titled 'The crisis of the American comic-book market'. By then, the comic market had been shattered as the spectacular drawings led to a style-over-substance approach, which soon lost readers' interest. Most of the star artists had left Marvel Comics to pursue their own venture, Image Comics. Opportunistic hoarders ceased their stockpiling when they saw that they could no longer get any material money for #1 issues, and publishers were drawn into an industry-wide crisis. Together with some poor acquisition decisions, this crisis led to Marvel Comics filing for bankruptcy in December 1996.

From bankruptcy to box-office smash

Fast forward 20-odd years later and Marvel is re-born as a premium entertainment franchise. While fashion and hype may have aided its resurrection, a number of factors firmly contributed to its

successful transformation from 90s publisher to modern-day cinema phenomenon.

First, they recruited talent, with many of the actors in the Marvel roster being Academy Award winners and nominees. They used a variable compensation scheme to keep Robert Downey Jr in the stable at an early stage. Second, they had a long-term plan. The Marvel team built momentum over a complex inter-connected series of instalments. The result was a loyal fan base, which, combined with films that merit entertainment value on a stand-alone basis, proved a winning formula. Additionally, they got tactical. Pulling forward the 2018 release date of the Avengers title 'Infinity War' by a few weeks likely contributed to the movie's record-shattering box office performance. Continued feedback on early versions help them finesse the final cut – and the differences between the trailers and the movie itself provided fuel for podcasters and bloggers, feeding the publicity machine.

Movies & investment managers

But you are probably wondering, what has all this got to do with alternative investments? The mid-00s hedge fund market had several features that reminded me of the hysteria of the American comic-book industry during the 90s. The barriers to entry were low, fed by loose regulation and capital eager to jump into the latest fashions. The longest-standing managers could afford to be selective in the capital that entered their funds, and the portfolio managers were often elusive. Hedge funds ultimately became synonymous with a certain lifestyle. Some products were launched with enormous liquidity mismatches, poor corporate governance structures and beta often sold as talent, echoing the style-over-substance phase that pre-empted the demise of Marvel.

The blow-up

And then the crisis came. Many fund of funds saw investors rushing to the doors, causing a pile up in redemption notices. For non-US dollar based investors, the sharp strengthening of the greenback



involved high FX hedging cash flows at the worst possible time. More redemptions ensued. Those funds that saw the liquidity of their holdings evaporate, or which faced redemptions or margin calls on portfolios that had never been liquid, gated their investors, suspended redemptions or created side-pockets. Many an investor lamented not having read their fund prospectus in full, as such documents outlined that managers did in fact have the ability to do as they saw fit – with their actions not always in line with investor interests.

Once the dust settled, it became clear that both alternative and traditional asset classes had been severely hammered. Many investors had lost not only their capital, but also their confidence.

Interest then turned to opportunistic investments, either in public or private form, into assets that had been thrown out with the bathwater as the proverbial baby. As central bankers eased liquidity to unprecedented levels, all ships were lifted by the rising tide. Beta products had great years on the back of central bank purchase programmes crowding out investors, first from the safest assets, then from riskier paper.

A phoenix rises from the ashes

Alternatives used this time to reform. A proper regulatory framework was built, with most US hedge fund managers now US Securities & Exchange Commission (SEC) regulated, and UCITS structures being the vehicle of choice for European investors. Standards of corporate governance have risen, and operational due diligence is now a deeper, more sophisticated effort for most investors than what it was before the crisis. Managers have invested in infrastructure, risk systems and operational teams. The market has become more solutions and client-oriented with greater transparency, moving away from the opaque, one-size-fits-all model of the past.

Concurrently, the barrier between traditional and alternative strategies has blurred. Some traditional managers have incorporated elements from the alternative toolkit, and some alternative managers are now more honest about their exposure to traditional assets.

Alternatives in the new world

Now the global economy is shifting in reaction to the ending of the multi-decade rally in bond yields, we believe alternatives are better positioned to be able to take advantage of a more discriminate market. Increased dispersion and higher volatility will likely ensue in a rising risk environment, disrupting the current negatively correlated relationship between equities and bonds. All these factors play in favour of using the alternatives toolkit instead of pure long-only strategies.

The reformed role that banks play in the post-crisis world also leaves room for alternatives, both as lenders to now-orphaned borrowers and as investors in more complex banking capital structures. With the shifting economic environment, the appropriate toolkit, better corporate governance, more seasoned managers, more demanding investors and better-equipped regulators, we believe alternatives are poised to take a starring role in the next chapter of the financial storyline.

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