

# If the World Has a Problem We Have a Solution—Live at the *Financial Advisor* ‘Inside Alternatives’ conference

By Andy Martin



Ali Motamed (Boston Partners), Ben Hunt (Salient Partners), Jack Rivkin, (Altegris), Evan Siminoff (*Financial Advisor*)

What do Greece, China, the Euro, massive world debt, and an exhausted US stock market have in common? Alternative investments will make it all better. This was the message from the 6<sup>th</sup> Annual ‘Inside Alternatives’ conference sponsored by *Financial Advisor* and *Private Wealth* in Denver July 13-14.

Any conversation about world troubles, of course, has to start with the Hellenes. As Ben Hunt, Ph.D., Chief Risk Officer of Salient Partners remarked, “Greece is a game of chicken. The game of chicken is not a test of capabilities, but a test of will. And it is going to spread beyond Greece, perhaps to Russia, the US and elsewhere.” His wariness was not reserved for Greece. Overall “we have much more debt than we had in 2008.” We are going the wrong way. “What we are seeing today is unlike anything we have seen. We really have to go back to the 1870s and 1930s to understand it.”

Dr. Hunt’s co-panelists were similarly foreboding. Ali Motamed, portfolio manager at Boston Partners criticized our lack of long-term vision. “We are short-sighted; we are running while looking at our feet.” Instead we should “Be opportunistic and look at the long-term horizon.” But, he reasoned, maybe there is some justification for our short-sightedness. “A 1% increase in rates would raise borrowing costs 15%-18% which takes out M&A activity, share re-purchases, and other corporate financing.” Thus, “right now is the time to be conservative.” An unexpected message coming from an alts manager.

A consistent theme running through the conference was the notion that we are in a secular low-growth environment and the only way out is alternatives. Altegris CIO Jack Rivkin, cautioned the audience of advisors, “Past performance is no guarantee of future returns is absolutely true...We are in a new game, a global slow-growth period for the next five to ten years.” Rivkin couldn’t resist traveling back to Greece. “If Greece is Bear Stearns, who is going to be Lehman?” This new game, he implied may likely see a major country failure.

The second theme was “divergence.” Divergent markets, public policy, and strategies which lead inexorably to the solution, or as Hunt offered, “Divergence leads to opportunities in alternative strategies.”

Alternative to what? Any discussion about alternatives has to start (correctly or not) with the assumption that heretofore we have lived exclusively in a stock and bond world. It would seem that this is the case but as John Cadigan of Behringer Securities said, “The first long/short strategy was created in 1949, which pre-dates Markowitz’s Modern Portfolio Theory.” Even so the dominant investment choices among average investors are still largely stocks, bonds, and cash. McKinsey & Company estimates that there was \$7.2 Trillion in alternative investments in 2013, only 10.7% of all managed assets, however alternatives grew at twice the rate of traditional investments from 2005 to 2013.

What is an alternative investment? Alts can be asset classes such as real estate, commodities, or other derivatives. They can be strategies like long/short, real return, hedged, leveraged ETFs, or volatility proxies. Or they can be investment vehicles like private equity, P2P loans, bitcoins, non-traded REITs, structured notes, leveraged loans, or limited partnerships. You can see we get to 31 flavors pretty quickly because there are scores of items that we could add to this list.



Ryan Tagal (Envestnet), John Cadigan (Behringer Securities), Jason Cross (Whitebox Mutual Funds), Bo Brustkern (NSR Invest), Bill Miller (Brinker Capital)

Among those 31 flavors the audience heard from Envestnet, Behringer Securities, Whitebox Mutual Funds, NSR Invest, Brinker Capital, and some forty other asset managers. Whitebox Mutual Funds Head of Equity, Jason Cross, Ph.D., started with something that was probably on the minds of all the panelists. “We reject MPT (Modern Portfolio Theory), that the only way to get higher returns is through adding risk.” Behringer Securities, Head of National Sales, John Cadigan doubled down on Dr. Cross’s comment with, “If you are allocated to the 60/40 (60% US stocks, 40% US bonds) model you are whistling by the grave yard.” However, Brinker Capital CIO Bill Miller alerted advisors that alternatives are not a sure thing when it comes to diversifying a portfolio since “REITs can either act as stocks or real estate.”

I believe the conference could have used more comments like Bill Miller's. Wellington Management, for example, the inventor of the much lampooned (by various speakers) 60/40 model, didn't grow to \$939 billion AUM by being what speaker John Mauldin called traditional asset managers: "prison guards of the past." In fact the "Wellington" model has outperformed the original S&P 500 fund since inception and done so with less risk. Alt that.

And as Leon Neumann, Treasurer at The Navigators said, "We need to evaluate what they're saying vs. what they're selling." He was remarking that often it was hard to separate marketing from educating.

However, there were many good ideas. For example Bo Brustkern, Co-Founder & CEO of Denver, Colorado based NSR Invest has a novel way to harvest fixed-income returns without the overt pricing risk that bond investors face. His firm helps financial advisors intelligently access peer-to-peer loans for their clients. Investors become banks of sorts rather than potential victims to bond price weakness. One could build the case that this strategy could be low correlated to the aggregate bond markets.

Echoing a major theme of the conference—that the US is in a long-term low-growth environment, author, CNBC senior contributor, and former Bear Stearns chief economist Larry Kudlow, spoke to the room of over 500 financial professionals. Kudlow's message was simple: "Our biggest challenge is that we have to grow faster...we are capable of growing at 4-5% for long periods of time." He then gave examples from the 1960s, 1980s, and 1990s to illustrate.

In a defense of our beleaguered world economy Kudlow added, "In the last 30 years, with the rise of Capitalism around the world one billion people have risen from one dollar a day earnings to the middle-class.



Larry Kudlow (CNBC Senior Contributor)

They are not gaining ground because of government policies, but because of economic freedom."

However, unfortunately all roads lead back to Greece. Kudlow's take? "Greece owns the means of production; Greece is a Socialist country; how's that working for you?" Kudlow's solution is not more debt, as European creditors recently approved. Instead Greece should "sell off all of its state owned business" he said to applause. And as a sort of reminder of why we are here Kudlow concluded, "The stock market is, in effect, the chronicler of wealth and economic freedom."

Wealth and economic freedom may be in jeopardy with what ails our world economy, but most present believed that alternative investments may be a potent elixir.

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