

Outlook for Alternatives: 2021 and Beyond



1. **ALPHA:** The last decade produced excellent returns from indices - both equity and fixed income. Returns in the next decade will best be captured by alpha strategies. Alpha is finite, difficult to source, due diligence, and harvest. Strategies have higher fees, higher minimums, leverage, illiquidity, and often key man risk. We recommend that Alpha strategies be a significant portion of an investment portfolio, reducing both beta and cash.
2. **SEARCH FOR YIELD:** There is an unrelenting demand for yield caused by “lower for longer” global monetary policies, aging demographics, and lower inflation due to technology. It is critical to focus on free cash flow after full allocation for expenditures including for competitive innovation. Areas of interest include niche private credit, specialized real estate (workforce housing, self-storage) and infrastructure (data storage, last mile delivery, 5G buildout). We believe there will be market consolidation and significant compression in niche real estate cap rates.
3. **CYCLE OF INNOVATION/DISRUPTION:** We are in the early stages of a long wave cycle of innovation of new technologies resulting in the creation of new business models, the application of technology to existing ones, and the disruption of many companies (malls). The key aspect is that the change is exponential and the first mover advantage/time to capture market share is critical. We recommend venture capital, with its focus on innovation, and hedge funds that seek to compound returns from the long exposure while generating returns/hedges from secular and cyclically challenged companies.
4. **GENOMIC REVOLUTION:** This is our best idea for the next decade. The cycle was launched with the decoding of the human genome in 2003 and accelerated with the introduction of CRISPR-CAS9 in 2013. The technological advances in data device capture, cloud storage, AI/machine learning for interpreting data and providing analysis – are working together to create the roadmap for delivering customized healthcare. AI will be

an essential element in reducing costs in disease prevention and drug development. While secular themes can be captured with indices, biotech has high volatility; a superior Sharpe ratio can be produced with hedge funds using sizing strategies, optimal entry and exit points, private investments (opt-in), platform companies (RCKT), and hedging.

5. **4th INDUSTRIAL REVOLUTION:** Over the next decade, the adoption and acceleration of many technologies, specifically 5G, AI, and Quantum Computing, will dramatically affect future industries including autonomous driving, robotic manufacturing, logistics, digital healthcare, drone delivery, gaming, education and AR/VR experiences. The pandemic exposed the risks inherent to the global supply chain; future policies will focus on reshoring critical industries (manufacturing, pharmaceuticals) using AI and robotic solutions. Business functions will be digitized, stored in the cloud, analyzed by AI, thus enhancing the quality of products and services while lowering the cost to the consumer.
6. **CYBERSECURITY:** The internet was built as an open system and thus will never provide the required level of security to protect vital industries (electrical grid) and services (IoT devices, autonomous vehicles). There is an ongoing battle between cybersecurity providers and hackers – tech savvy individuals, organized crime, and government sponsored/military groups. Technological innovations as exemplified by deep fake videos make it increasingly difficult to distinguish between actual sources and imitations. Quantum computers, while early in development, are one solution for providing secure passwords. We recommend cybersecurity-dedicated funds and quantum computing VC opportunities to capture this theme.
7. **CHINA:** China is currently the second largest economy in the world and will overtake the US in the next decade. Its centralized government has set a goal for China to be the global leader by 2030 and dominate certain global markets. For China's system of control to be effective it needs citizen surveillance, border security, and military superiority. In order to keep its massive population content, it needs to provide access to essential services (healthcare, transportation) while lowering costs (food). The government is providing significant funding for AI to both university research centers and individual companies. Currently the US and China are roughly on par in their AI research and capabilities. This balance will skew decidedly towards China in the coming decade due to its unfettered access to data, central government funding, and the large number of PhD graduates focused on this space. We have identified investments that are targeting this opportunity.
8. **COMMODITIES:** Commodities are currently valued at an all-time low relative to the S&P 500 (since the GSCI index was first established in 1970). Much of this decline has been due to the decline in the price of oil and the strong performance of the technology leaders in the S&P. Transitioning to a digital world, there will be a decline in demand for many commodities, specifically oil, and measuring consumption for many developed economies (GDP) is not necessarily the right metric to determine the output of economies/societies.



This view needs to be balanced by the projected increase in global population to 10B by 2050 and the transition of billions of people in the emerging markets to a higher standard of living and consumption.

9. **ESG/CLIMATE CHANGE**: The current warming of the planet is environmentally unsustainable and will require dramatic changes to the burning of fossil fuels, food production (meat), the destruction of the rain forests, and the dumping of plastic in the oceans. The Biden Administration will be a positive catalyst for the climate change agenda including tax incentives for renewable energy. To solve the problem will require broad-based adoption from consumers. Companies will be tasked by investors (specifically pension funds/BlackRock) and held accountable (valuations) to identify and track ESG progress. The changes required to slow and stop the increase in global temperatures will be challenging in many democratic societies.

10. **ARTIFICIAL INTELLIGENCE**: AI/Machine Learning is the primary driver for exponential change in the next decade. If you take away one idea from this Outlook, it is that the implementation of AI will create an insurmountable advantage to those countries and companies that are the first movers. Given AI's capability to teach itself in a narrow context (Deep Mind, the game of Go, and AlphaGo Zero), our outlook is that by 2030, China and the US will dominate the world economy and effectively be the co-global economic and military superpowers.