

## Asset Allocation post the Global Financial Crisis (GFC)

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As investors sift through the bitter ashes of their super funds after the end of the *annus horribilis* that was the 2008/09 financial year, some pointed questions are being asked of financial planners and fund managers. Unsurprisingly, these questions include the following:

"Why didn't you know this was going to happen?"

"Why didn't you go to cash at the start of the year?"

"How come all those supposedly non-correlated hedge funds have lost money just like the rest of the market?"

And so on.

Until recently it was generally felt that tactical asset allocation was a means by which declines in one sector of a portfolio could be offset by gains in another, with the (hopeful) result that overall losses wouldn't be sustained. Unfortunately for adherents to this theory, 2008/09 proved that sometimes conventional asset allocation is simply unable to prevent the negative results so many investors have recently experienced. But does this mean that we should pay less attention to it in the future? The answer to this is a qualified "No".

The main asset classes presented to investors usually consist of local and international equities, alternative assets (eg hedge funds and the like), bonds, listed and unlisted property funds and cash or cash equivalents. Of these, only two could have withstood the waves of selling share, commodity and property market withstood last year – very clever hedge funds and cash. And given how hard it is to pick truly clever hedge funds, cash remains the only surefire means by which investors can avoid losses.

Returning to hedge funds for a moment, the reason only a handful made money during the GFC was (a) most hedge funds, like most people, are actually long biased and (b) for varying periods over the past twelve months regulators around the world decided to ban the short selling of equities (thus depriving many hedge funds of their primary loss prevention tool). Two lessons to be learnt from this experience, therefore, are first always to beware of 'sovereign risk' in the form of unexpected regulations, and second to research alternative managers carefully to ensure they truly are capable of generating positive and uncorrelated returns.

So what of the argument that asset allocators should've pushed the majority of their clients' assets into cash before the financial world turned really nasty? Well, some might've done this, but for most such an option was never on their list no matter what the circumstances. Most of the time, investors who keep their money in cash run the risk of going backwards in real terms, ie seeing the purchasing power of their money being eroded by inflation. To be sure, when equity, property and money markets collapse simultaneously, then in the short term a heavy weighting towards cash will pay off.

The reality, however, is that such collapses occur sufficiently infrequently to make the 'all cash' option unsuitable most of the time. And if you're lucky enough to have a financial advisor who can pick the rare moments when cash is absolutely the right asset to hold – keep his or her identity a very closely held secret!