

HOW TO BUILD FROM THE BEAR UP

A MODERN GUIDE TO CONSTRUCTING RESILIENT PORTFOLIOS ACROSS MARKET CYCLES

It's time to change the way we think about bear markets.

Traditionally, bear markets have been viewed as periods of retreat. But what if we reimagined the bear not as a warning sign—but as a symbol of enduring strength, adaptability, and resilience? These are the very attributes needed in portfolio construction today. At our firm, this philosophy has guided our investment process for over two decades.

Below, we outline a six-step framework to help advisors and institutional investors build portfolios from the bear up—fortifying them with deeper diversification, enhanced risk awareness, and a modern allocation mindset.

Our goal isn't to predict the market. It's to prepare portfolios to perform through it.

STEP 1

TRANSFORM MARKET DISRUPTION INTO A STRATEGIC ADVANTAGE

Legacy asset allocation models are losing their efficacy in today's macro environment. The dual forces of sustained inflation and structurally higher interest rates have disrupted conventional wisdom. With upcoming changes to reporting requirements heightening transparency around fees and value delivery, there is a clear inflection point: the opportunity to differentiate by evolving your investment philosophy. Repositioning client portfolios with alternative strategies can both mitigate traditional risk exposures and elevate your value proposition in an increasingly competitive landscape.

Alternatives offer unique return drivers and risk management tools that help investors navigate this complexity, providing durable portfolio diversification beyond the limits of traditional asset classes.

STEP 2

RETHINK DIVERSIFICATION – BREADTH, NOT JUST DEPTH



The historic inverse relationship between equities and fixed income can no longer be taken for granted. Likewise, surface-level diversification—across geographies or sectors—offers limited protection when markets move in lockstep. True diversification requires structurally uncorrelated return streams. This means incorporating strategies that behave differently, not just look different.

Alternatives play a critical role in this process by providing genuine sources of uncorrelated returns, enhancing portfolio resilience and reducing dependence on traditional asset class dynamics.

STEP 3

DIAGNOSE AND DISMANTLE HIDDEN RISK EXPOSURES

Modern portfolio construction demands a granular understanding of cross-asset class risks. Interest rate risk, for instance, permeates far beyond fixed income. Equities, real assets, and even alternatives can be inadvertently exposed through correlations with macroeconomic factors.

Consider this illustrative case: In 2022, an advisor sought to eliminate rate sensitivity by exiting core bonds. However, reallocating into dividend-paying equities and real estate reintroduced rate exposure on the equity side—effectively contradicting the portfolio's intended positioning.

Sophisticated investors must move beyond correlation matrices and uncover latent risks across all dimensions.

Alternatives, when thoughtfully integrated, offer distinct sources of return and risk mitigation that enhance diversification and help manage these complex, interconnected exposures more effectively.

STEP 4

REDEFINE ALPHA IN THE AGE OF VOLATILITY



Alpha is no longer just about beating benchmarks – it's about delivering consistent, risk-adjusted outcomes with resilience across market cycles. In today's environment, investors must dissect what they're truly paying for: is the manager adding value through skill, or simply delivering market beta with a high fee? True alpha should be idiosyncratic, persistent, and uncorrelated—not the result of concentrated bets, style tilts, or macro exposure. With upcoming changes to reporting requirements driving transparency, advisors must justify every basis point. The future of portfolio construction lies in understanding how returns are generated, prioritizing quality, stability, and downside protection over short-term outperformance or high-fee illusions of skill.

Alternatives define themselves by consistently delivering this kind of alpha—offering genuine value through differentiated sources of return that are worth the fee, providing durable portfolio diversification and enhanced resilience that traditional assets alone cannot achieve.

STEP 5

ADOPT A TOTAL PORTFOLIO APPROACH

In today's market environment, you must take a modern approach to portfolio construction. A Total Portfolio Approach does away with traditional asset allocation buckets and looks at portfolios through a different lens. This means adopting an approach that focuses on equity risk more broadly – whether that's small-caps, value stocks or international growth. Instead, look at how every single investment in a portfolio contributes to the potential of achieving the portfolio's ultimate goals. That involves creating a factor risk model, which accounts for 90% of what drives markets (only 10% of a portfolio is influenced by the fund manager).

To that end, the traditional 60/40 stocks-to-bonds portfolio no longer works. To build from the bear up, you must take a more modern approach to asset allocation. Consider the 40/30/30: **40% Equities, 30% Fixed Income, 30% Alternatives**. By reframing your portfolio into goal-based classifications – enhancers, diversifiers, and inflation protectors, it will help you make shifts in your portfolio.

STEP 6

FORTIFY YOUR PORTFOLIO WITH LIQUID ALTERNATIVES



In the current investment landscape, constructing “fortified” portfolios—those that deliver superior risk-adjusted returns through effective volatility management and diversification of return drivers—is paramount. Achieving this requires exposure to assets with low or negative correlations to traditional equity and fixed income markets. This is precisely where alternatives demonstrate their value.

Institutional investors, particularly pension funds, have long employed hedge fund strategies—including long-short equity, alpha-generating, and market-neutral approaches—to mitigate correlation risk and enhance portfolio resilience. As liquid alternative vehicles have become increasingly accessible, they have emerged as essential components in building robust, diversified portfolios capable of withstanding varied market environments.

Alternatives continue to define the frontier of portfolio innovation and resilience deliver differentiated return streams and dynamic risk management.

See how

the world invests with alternatives