

# Liquid Alternatives Observer

## Quarter 4, 2023

### Morningstar Manager Research

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Simon Scott  
 Director, Alternative Strategies,  
 Global Manager Research  
[simon.scott@morningstar.com](mailto:simon.scott@morningstar.com)

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### Key Takeaways

#### Quarterly Performance

- ▶ Total net assets rose 6.3% to almost \$445 billion.
- ▶ Funds remain in outflows, while nontraditional exchange-traded funds gained assets.
- ▶ A spurt of activity in November and December helped most Morningstar Categories deliver positive quarterly returns.
- ▶ Systematic trend was the only category posting negative performance for the quarter and in 2023.
- ▶ Flows continue into hedged equity and equity market neutral strategies as investors seek certainty.
- ▶ Both uncorrelated alternatives and nontraditional strategies each saw more than \$4 billion of outflows for the quarter, and a combined \$30 billion outflow over 2023.
- ▶ J.P. Morgan continues to be the main beneficiary, increasing market share as BlackRock struggles.
- ▶ The bottom five strategies by outflows saw \$2.5 billion in assets depart over the quarter.
- ▶ Seven funds shuttered, two merged and continue to stagnate, with two products opened in the quarter.

#### Quarterly Overview

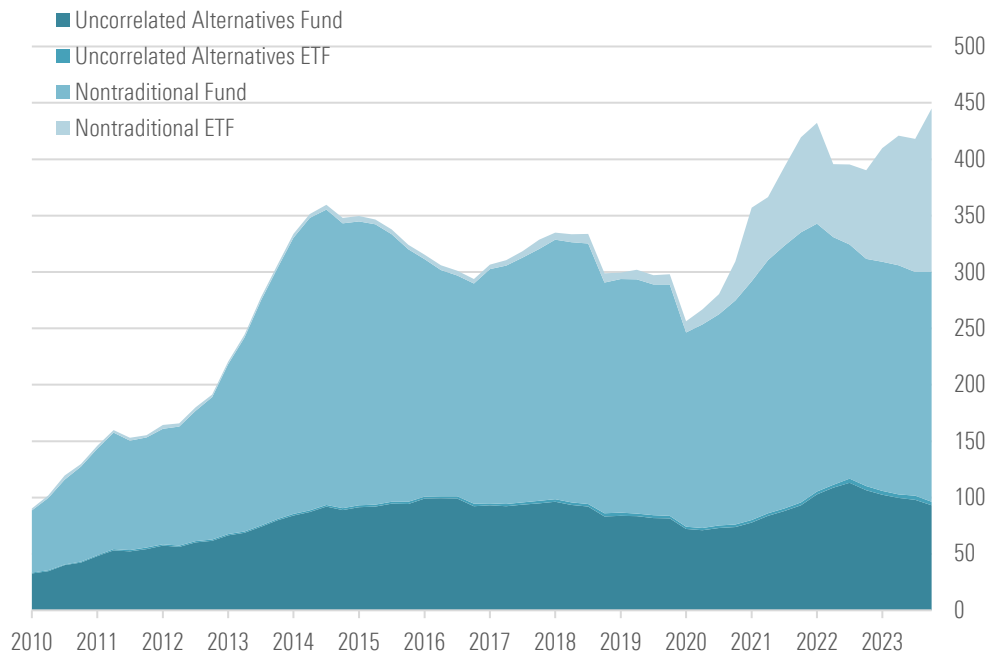
The "higher-for-longer" narrative that appeared at the end of the summer caused a stumble in equities and a bond selloff but started a rally in the U.S. dollar that continued into October. This persisted long enough for many managed futures funds to cut equities while shorting bonds and buying the dollar. November saw an about-face, as lower-than-anticipated Consumer Price Index figures and positive central bank commentary set equities and bonds soaring and a pullback in the U.S. dollar. Though this was positive for many directional strategies, quantitative trend and macro were caught flat-footed and gave back some the hard-fought gains after the Silicon Valley Bank crisis earlier in the year. Associated long energy positions also created headwinds during the quarter. The VIX declined 5 points over that period. Although this had an impact on options prices, many hedged equity strategies benefited thanks to their short options exposure. Higher overnight rates and coupons boosted convertible arbitrage strategies, with declining long-term rates and narrowing credit spreads enabling richer valuations. Both options trading and relative value strategies produced solid outcomes. A spurt in deals in November and December brought event-driven funds out of their 2023 slumber.

Despite a respectable year for many uncorrelated alternatives, investors pulled out over \$16 billion, largely from the lackluster event-driven category and in a reversal of the huge inflows we had seen in prior years for systematic trend. The continued interest in equity hedge strategies suggests one foot is being kept in markets as a lid is kept on recessionary talk, but valuations continue to remain high.

# Assets Under Management and Fund Flows

Total net assets for liquid alternatives and nontraditional strategies rose 6.4% during the fourth quarter to nearly \$445 billion. As with the prior quarter, much of this growth came from investor interest in higher-beta nontraditional categories. These offer more flexible allocations to traditional equity, rates, and credit markets, often with an income bent. Strong equity markets tempted investors back into the fray, but despite these gains in net assets, in aggregate both uncorrelated alternatives and nontraditional funds each saw more than \$4 billion in redemptions over the fourth quarter. Close to \$30 billion combined exited the space over the course of 2023.

**Exhibit 1** Total Net Assets for Uncorrelated Alternatives and Nontraditional Strategies (\$ Billion)



Source: Morningstar Direct. Data as of December 2023.

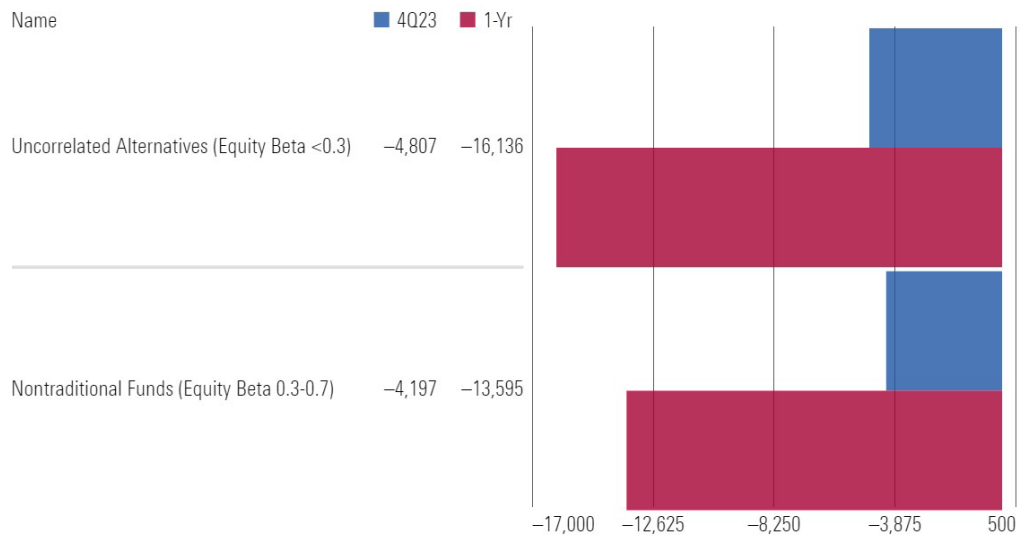
Equity market neutral was one of the only uncorrelated alternatives categories to see investor interest, rising by 6%. In asset terms, albeit from a low base, event-driven and equity market neutral ETFs both saw total net assets fall by more than 20%. Systematic trend continued to shed assets after the gains of recent years. A weak quarter, where funds struggled with sharp fixed income reversals, coupled with over \$2 billion in outflows, resulted in a 22% drop in net assets. Digital assets, buoyed by a triple-digit rise in the category average, saw fund assets soar by 75% and 55% in ETF assets.

**Exhibit 2** Total Net Assets (\$ Million) and 12-Month % Change for Morningstar Open-End and ETF Categories

Category	Dec-23	% Change
Derivative Income	72,198	64.8%
Options Trading	77,772	37.8%
Macro Trading	12,273	3.7%
Equity Long Short	22,413	0.4%
NonTraditional Bond	113,798	-0.3%
Equity Market Neutral	6,749	-2.3%
Relative Value Arbitrage	17,181	-5.9%
Multistrategy	27,912	-7.4%
Tactical Allocation	21,326	-20.5%
Systematic Trend	17,963	-22.2%
Event Driven	13,901	-30.7%

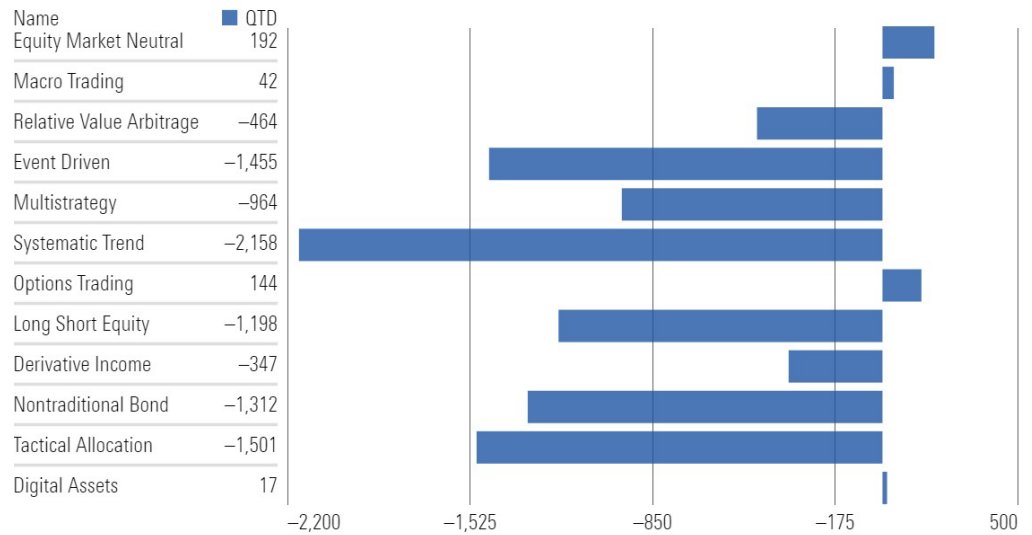
Source: Morningstar Direct. Data as of December 2023.

**Exhibit 3** Total Net Flows for Broad Alternative Groupings (Open-Ended Funds \$ Million)



Source: Morningstar Direct. Data as of December 2023.

**Exhibit 4** Morningstar Category Flows for the Quarter (\$ Million)

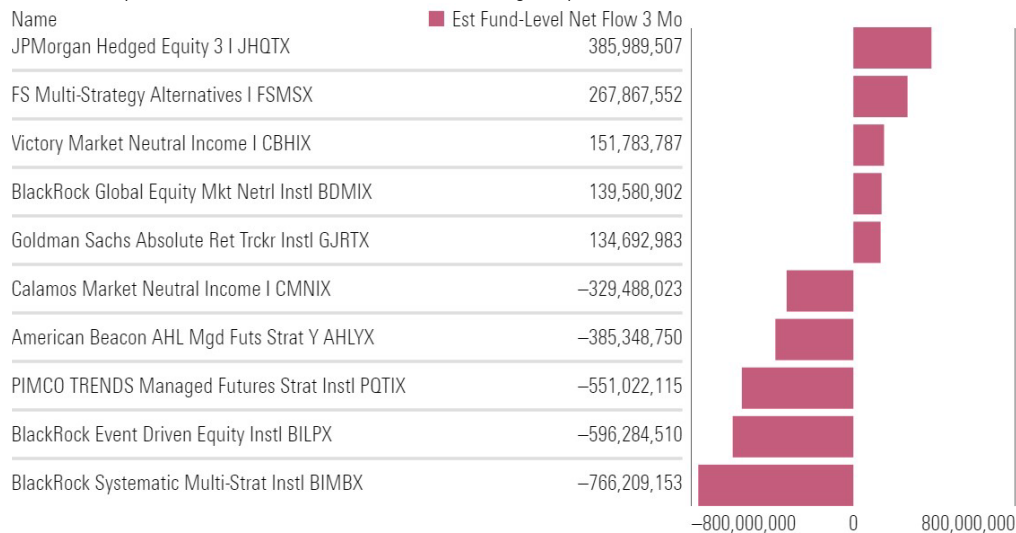


Source: Morningstar Direct. Data as of December 2023.

As equities roared, interest remained elevated in hedged equity offerings. Inflows were again dominated by J.P. Morgan, though this quarter saw a different series in its hedge equity product suite take the spoils. Investors were likely mixing their exposures across the differing options expiry dates offered in the various series. Equity market neutral also saw increased demand, with both Victory and BlackRock offerings receiving north of \$100 million of inflows for the quarter.

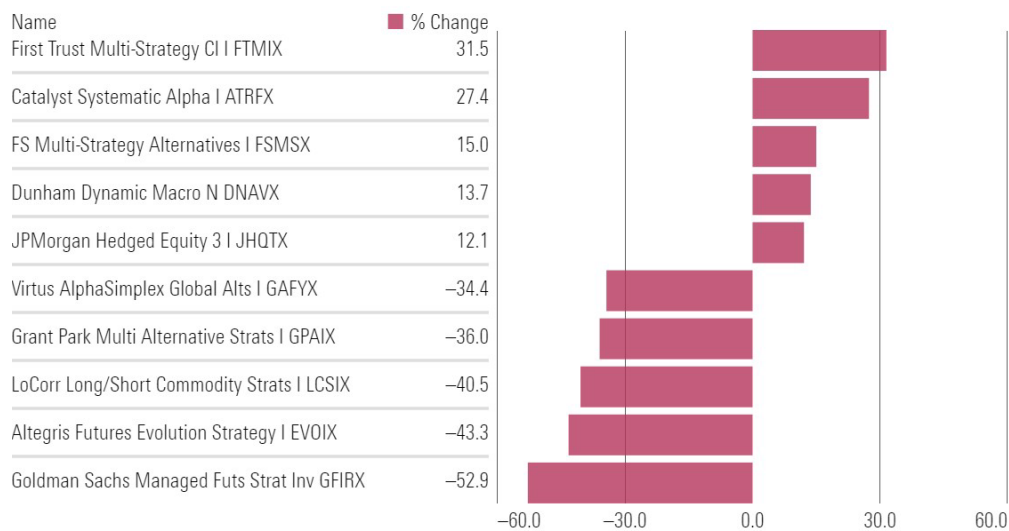
BlackRock's gain here was more than offset by outflows in two of its larger offerings. Although BlackRock Event Driven BILPX and BlackRock Systematic Multistrategy BIMBX are multibillion-dollar entities, managing \$600 million-\$700 million of redemptions in a quarter is still challenging. Systematic trend managers rounded out those seeing the largest outflows, with those running shorter-term signals suffering relative to longer-term peers. In percentage terms, a couple of multistrategy offerings received investor interest. This category has suffered for many years despite being the first port of call for many investors seeking an uncorrelated investment. First Trust Multistrategy FTMIX producing a 2023 return that exceeded the category average by some 250 basis points may help explain the allure.

**Exhibit 5** Top and Bottom Uncorrelated Alternative Strategies by Net Flows (\$ Million)



Source: Morningstar Direct. Data as of December 2023.

**Exhibit 6** Top and Bottom Uncorrelated Alternative Strategies Over \$50 Million by Net Flows (% Change)



Source: Morningstar Direct. Data as of December 2023.

Market share continues to be dominated by managers with large distribution footprints, long track records, and strong reputations. Seven years ago, J.P. Morgan, Neuberger Berman, and Virtus weren't in the top 10. During that period, Calamos and BlackRock were the big winners, each increasing market share by between 5% and 6%, while Natixis has seen its share fall by 10% and AQR by 20%.

## Category Performance

### Exhibit 7 Market Share by Firm Including Nontraditional Strategies

Branding Name	% Share
BlackRock	16.37%
JPMorgan	12.46%
PIMCO	9.12%
Calamos	4.71%
Goldman Sachs	4.23%
Columbia Threadneedle	3.98%
NAVigator	2.43%
Natixis	2.21%
Catalyst	2.19%
Neuberger Berman	2.14%

Source: Morningstar Direct. Data as of December 2023.

### Exhibit 8 Market Share by Firm Excluding Nontraditional Strategies

Branding Name	% Share
JPMorgan	18.08%
BlackRock	10.94%
Calamos	10.59%
Catalyst	5.04%
Natixis	4.87%
Virtus	4.17%
AQR	3.88%
Goldman Sachs	3.28%
Blackstone	2.87%
PIMCO	2.52%

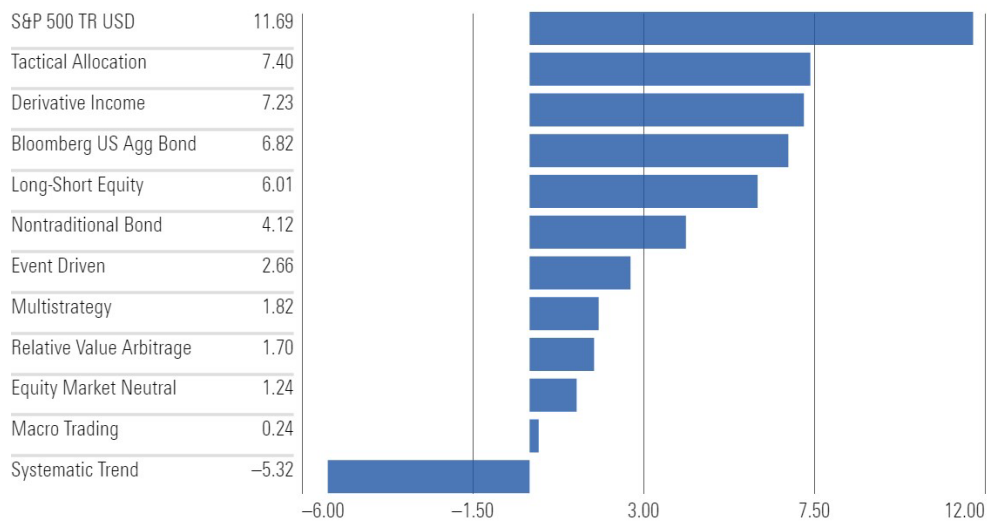
Source: Morningstar Direct. Data as of December 2023.

In a reversal of the third quarter, equities and bonds were both strongly positive for the fourth quarter. Most categories delivered in line with their levels of equity beta, though nontraditional categories containing traditional market betas in modified form slightly outperformed on a beta-adjusted basis.

Every liquid alternative category except systematic trend was positive for the quarter, though only three of the six surpassed Treasury bills.

Despite investors giving up the fight and throwing in their redemptions, event driven was the strongest uncorrelated alternative; the beleaguered strategy finally caught a break after the worst year for deals in a decade. A late spurt in deals allowed many funds to make up losses stemming from the second quarter. This late trading in November and December also buoyed convertible arbitrage funds, allowing relative value strategies to hit positive territory. Systematic trend funds suffered from the end of the "higher-for-longer" narrative in a rough year trading fixed income. This shock came just after many had largely made up big losses from the Silicon Valley Bank issues in the first quarter.

**Exhibit 9** Morningstar Category Quarterly Performance



Source: Morningstar Direct. Data as of December 2023.

Over trailing periods, market dispersion has led to higher total returns in liquid alternatives in recent years, but spreads over cash have remained in the expected range. Systematic trend is the only category with negative performance on a trailing 12-month basis, giving up some of the strong gains received during the previous three years. After losing 3.82% over the trailing 12 months, systematic trend three-year annualized returns have dropped from double-digit territory to almost mid-single digits. Yet most have still produced positive portfolio benefits.

**Exhibit 10** Morningstar Category Performance Metrics

Grouping	Name	Beta S&P 500 3 Yr	Alpha Balanced Index 3 Yr	Total Ret 1 Yr	Total Ret Annlzd 3 Yr	Total Ret Annlzd 5 Yr
Market	S&P 500 TR USD	1.00	5.76	26.29	10.00	15.69
Market	Bloomberg US Agg Bond	0.23	-6.24	5.53	-3.31	1.10
Market	Mstar US Mod Tgt Alloc	0.66	-0.10	16.75	3.57	8.84
Market	USTREAS T-Bill	0.00	0.00	5.11	2.07	1.84
Nontraditional	Options Trading	0.52	1.95	17.57	5.36	7.12
Nontraditional	Derivative Income	0.67	2.76	14.97	7.11	8.94
Nontraditional	Long-Short Equity	0.48	0.99	10.61	4.97	7.09
Nontraditional	Nontraditional Bond	0.17	-2.09	6.95	0.68	2.56
Nontraditional	Tactical Allocation	0.59	-1.59	10.74	2.13	6.23
Uncorrelated Alternative	Equity Market Neutral	-0.01	4.09	5.09	6.11	3.02
Uncorrelated Alternative	Event Driven	0.16	0.29	5.38	1.67	4.41
Uncorrelated Alternative	Multistrategy	0.20	0.69	6.24	3.67	4.13
Uncorrelated Alternative	Relative Value Arbitrage	0.13	-0.66	6.62	2.38	5.02
Uncorrelated Alternative	Systematic Trend	-0.11	3.77	-3.82	6.52	5.48
Uncorrelated Alternative	Macro Trading	0.17	-1.08	2.62	3.26	4.88
Trading	Digital Assets	2.65	37.41	155.38	4.00	21.46
Uncorrelated Alternative	Macro Trading	7.72	15.80	14.76	-3.58	0.37
Trading	Digital Assets	90.05	141.31	176.68	-77.10	0.34

Grouping	Name	Std Dev 3 Yr	Down Capture Ratio 3 Yr	Up Capture Ratio 3 Yr	Max Drawdown 3 Yr	Calmar Ratio 3 Yr
Market	S&P 500 TR USD	17.54	100.00	100.00	-23.87	0.42
Market	Bloomberg US Agg Bond	7.24	40.29	16.12	-17.02	-0.19
Market	Mstar US Mod Tgt Alloc	12.11	73.11	61.02	-20.14	0.18
Market	USTREAS T-Bill	0.68	-3.77	4.07	-0.04	56.53
Nontraditional	Options Trading	9.97	53.77	53.51	-13.92	0.39
Nontraditional	Derivative Income	13.48	66.68	65.53	-16.72	0.39
Nontraditional	Long-Short Equity	12.45	49.85	47.11	-12.76	0.34
Nontraditional	Nontraditional Bond	5.24	19.02	14.26	-8.47	0.06
Nontraditional	Tactical Allocation	12.51	67.39	51.57	-18.25	0.10
Uncorrelated Alternative	Equity Market Neutral	7.26	-14.52	9.56	-2.10	2.93
Uncorrelated Alternative	Event Driven	5.37	7.56	13.81	-4.02	0.69
Uncorrelated Alternative	Multistrategy	6.29	16.38	21.33	-5.34	0.62
Uncorrelated Alternative	Relative Value Arbitrage	3.91	7.34	10.44	-5.84	0.30
Uncorrelated Alternative	Systematic Trend	11.86	-21.90	0.44	-9.88	0.48
Uncorrelated Alternative	Macro Trading	7.72	15.80	14.76	-3.58	0.37
Trading	Digital Assets	90.05	141.31	176.68	-77.10	0.34

Source: Morningstar Direct. Data as of December 2023. Alpha calculated using the Morningstar Moderate Target Allocation Index as a base. Capture ratios use the S&P 500.



# Morningstar Analyst Rated Fund Performance

## Exhibit 11 Morningstar Analyst Rated Fund Performance

Name	Ticker	Morningstar Medalist Rating	Morningstar Category	Beta S&P 500 3 Yr	Alpha Balanced Index 3 Yr	Total Ret 3 Mo	Total Ret 1 Yr	Total Ret Ann 3 Yr	Total Ret Ann 5 Yr
BlackRock Global Equity Mkt Netrl Instl	BDMIX	Bronze	Equity Market Neutral	0.03	4.15	6.82	14.58	6.42	3.69
JPMorgan International Hedged Equity I	JIHIX	Silver	Options Trading	0.49	0.44	5.93	11.88	3.65	
JPMorgan Hedged Equity I	JHEQX	Silver	Options Trading	0.45	3.19	5.60	16.06	6.57	9.37
Parametric Volatil Risk Pm-Defensv I	EIVPX	Bronze	Options Trading	0.55	4.37	5.50	16.80	7.97	8.83
BlackRock Systematic Multi-Strat Instl	BIMBX	Bronze	Multistrategy	0.13	0.55	4.42	6.44	3.13	4.26
BlackRock Event Driven Equity Instl	BILPX	Bronze	Event Driven	0.11	-0.02	3.65	5.37	2.42	4.15
Calamos Market Neutral Income I	CMNIX	Bronze	Rel Value Arb	0.21	0.47	2.27	9.17	3.15	4.30
The Merger Fund I	MERIX	Bronze	Event Driven	0.04	-0.26	1.95	4.51	1.85	3.39
AQR Diversified Arbitrage I	ADAIX	Bronze	Rel Value Arb	0.15	0.14	1.55	4.51	2.41	7.85
BlackRock Tactical Opportunities Instl	PBAIX	Bronze	Global Macro	-0.01	1.46	-2.10	2.98	3.18	3.61
American Beacon AHL Mgd Futs Strat Inv	AHLPX	Bronze	Systematic Trend	-0.08	4.34	-2.77	-4.20	5.32	5.24
Abbey Capital Futures Strategy I	ABYIX	Silver	Systematic Trend	-0.15	4.57	-4.90	-3.27	5.41	6.59
JHancock Diversified Macro I	JDJIX	Bronze	Global Macro	-0.03	2.68	-6.53	2.76	4.11	
Virtus AlphaSimplex Mgd Futs Strat I	ASFYX	Bronze	Systematic Trend	-0.27	8.46	-6.78	-10.32	7.99	9.16

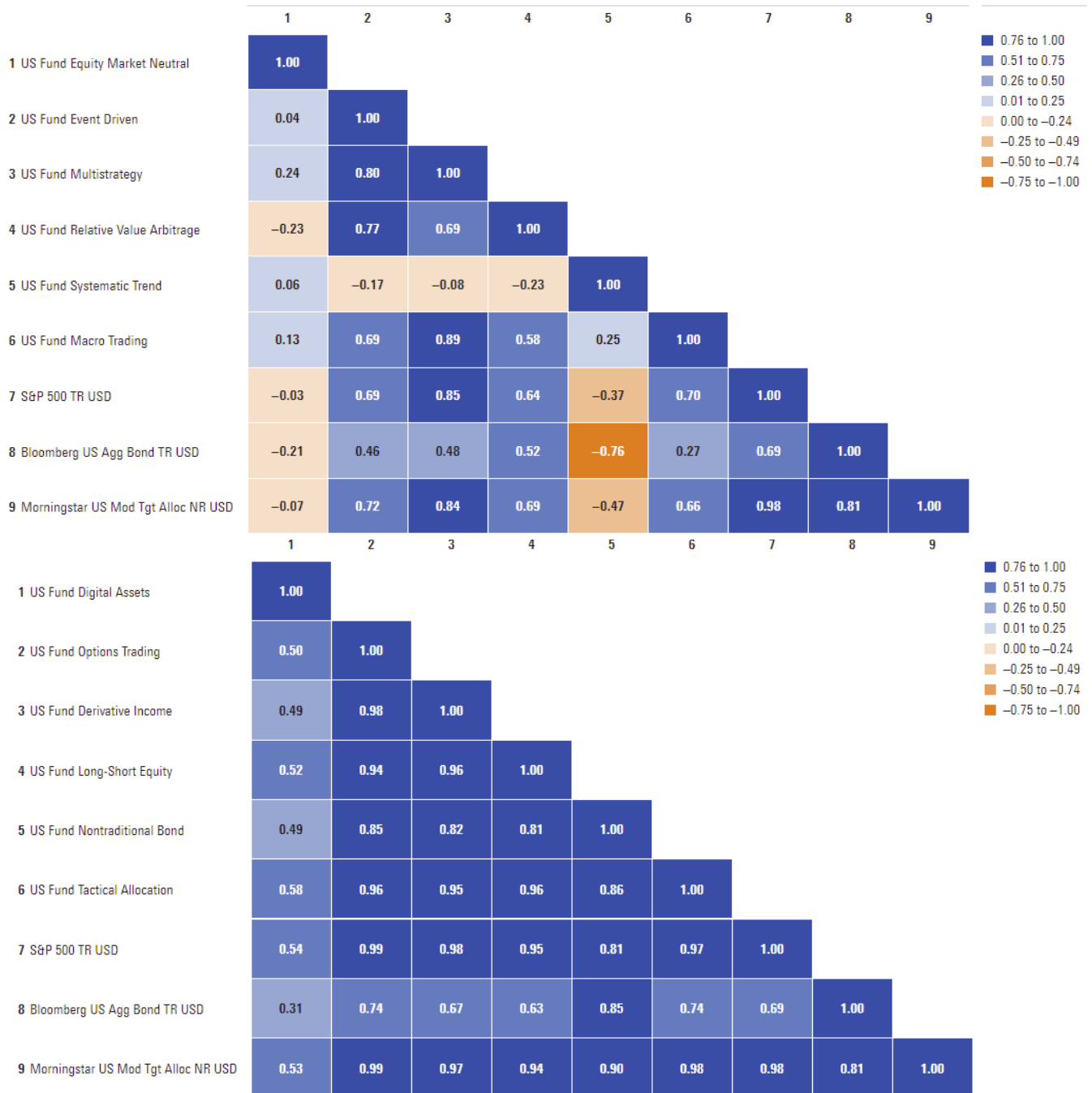
Source: Morningstar Direct. Data as of December 2023.

Funds with Morningstar Medalist Ratings of Gold, Silver, or Bronze were a mixed bag during the quarter. Strong performance was seen across several categories; the exceptions were quantitative macro and trend funds, which suffered in November's sharp fixed-income reversal. BlackRock Equity Market Neutral BDMIX and BlackRock Event Driven BILPX were standouts given their lack of structural equity beta. Over the whole of 2023, four categories produced double-digit returns. At the bottom end, trend followers all posted negative numbers, leading to a 25% dispersion across categories across 2023. Almost all strategies have been additive to a 60/40 portfolio, The Merger Fund MERIX was an exception, as its purer form of merger arbitrage struggled with the dry spell of deals.

# Correlation Matrix

**Exhibit 12** 3-Year Correlation of Uncorrelated Alternative and Nontraditional Morningstar Categories

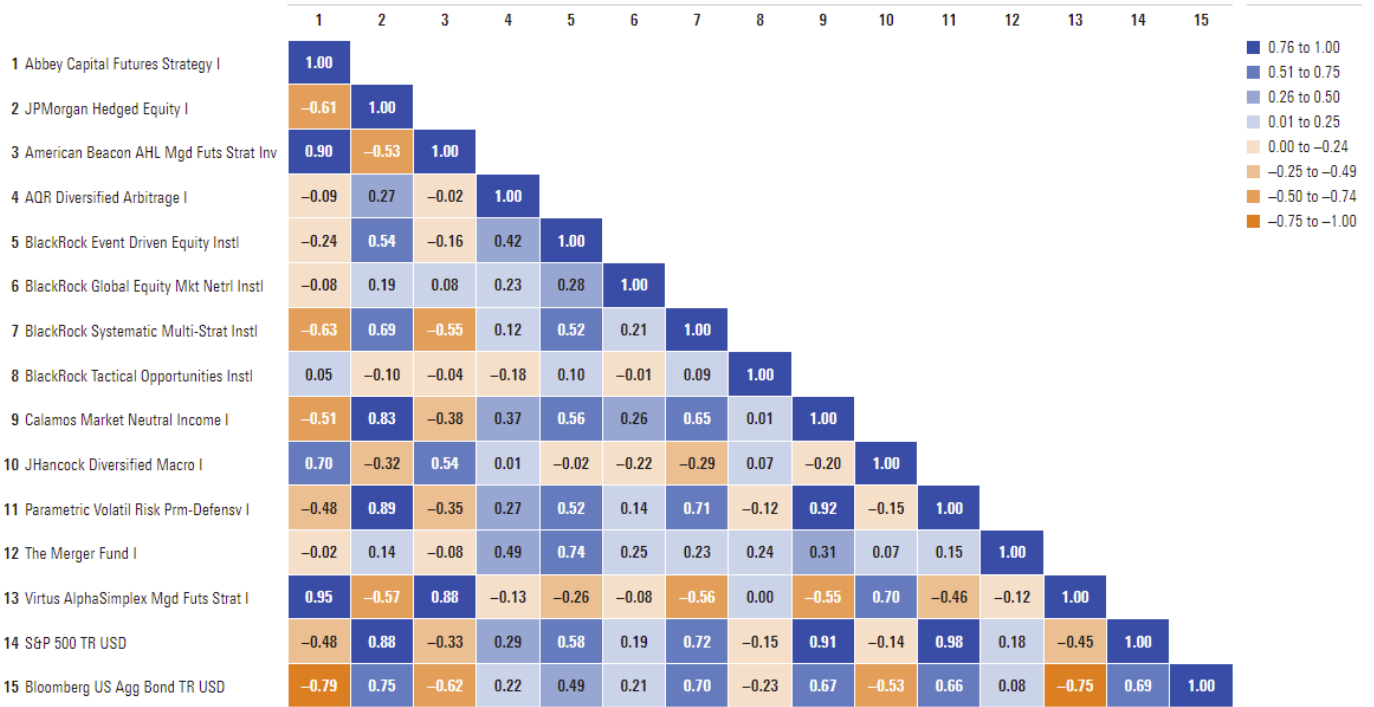
Start Date 3 Years Ago (01/01/2021) End Date Last Month End (12/31/2023) Currency Base Currency 4 More Settings



Source: Morningstar Direct. Data as of December 2023.

**Exhibit 13** 3-Year Correlation of Morningstar Analyst Rated Funds

Start Date **3 Years Ago (01/01/2021)** End Date **Last Month End (12/31/2023)** Currency **Base Currency** 4 More Settings



Source: Morningstar Direct. Data as of December 2023.

# Strategy Launches, Liquidations, and Ratings Changes

**Exhibit 14** Strategy Launches, Liquidations, and Mergers During the Quarter

Name	Morningstar Category	Firm Name	Inception Date	Obsolete Date	Obsolete Type
Cromwell Marketfield L/S C	Long/Short Equity	Cromwell Funds	05-Oct-12	17-Nov-23	Merged
Catalyst Systematic High Inc	Global Macro	Catalyst Mutual Funds	11-Apr-17	08-Nov-23	Liquidated
Catalyst Income and Multi-Strat	Global Macro	Catalyst Mutual Funds	14-Aug-15	08-Nov-23	Liquidated
Ziegler FAMCO Hedged Equity Instl	Options Trading	Ziegler	29-Nov-16	03-Nov-23	Merged
SilverPepper Merger Arbitrage Instl	Event Driven	SilverPepper	31-Oct-13	31-Oct-23	Liquidated
GMO SGM Major Markets I	Global Macro	GMO	23-Sep-20	10-Oct-23	Liquidated
GMO SGM Major Markets VI	Global Macro	GMO	01-Dec-15	10-Oct-23	Liquidated
GMO SGM Major Markets III	Global Macro	GMO	03-Oct-11	10-Oct-23	Liquidated
UBS Dynamic Alpha A	Global Macro	UBS Asset Management	27-Jan-05	10-Oct-23	Liquidated
Calamos Merger Arbitrage I	Event Driven	Calamos	29-Sep-23		NEW
Fidelity SAI Convertible Arb	Relative Value Arbitrage	Fidelity Investments	12-Sep-23		NEW

Source: Morningstar Direct. Data as of December 2023.

**Exhibit 15** Analyst Ratings Published During the Quarter

Name	Ticker	Morningstar Category	Medalist Rating	Parent Pillar	People Pillar	Process Pillar	Rating Date
AQR Equity Market Neutral I	QMNIX	Market Neutral	Neutral	Average	Above Average	Average	Dec-23
AQR Diversifying Strategies I	QDSIX	Multistrategy	Neutral	Average	Above Average	Average	Dec-23
AQR Alternative Risk Premia I	QRPIX	Multistrategy	Neutral	Average	Above Average	Average	Dec-23
AQR Managed Futs Strat HV I	QMHIX	Systematic Trend	Neutral	Average	Above Average	Average	Dec-23
AQR Managed Futs Strat I	AQMIX	Systematic Trend	Neutral	Average	Above Average	Average	Dec-23
AQR Style Premia Alternative I	QSPIX	Multistrategy	Neutral	Average	Above Average	Average	Dec-23
JPMorgan Hedged Equity 2 I	JHQDX	Options Trading	Silver	Above Average	Above Average	Above Average	Sep-23
JPMorgan Hedged Equity 3 I	JHQTIX	Options Trading	Silver	Above Average	Above Average	Above Average	Sep-23
JPMorgan Hedged Equity I	JHEQX	Options Trading	Silver	Above Average	Above Average	Above Average	Sep-23
JPMorgan Intl Hedged Eq	JIHIX	Options Trading	Silver	Above Average	Above Average	Above Average	Sep-23
Gateway Y	GTEYX	Options Trading	Neutral	Average	Above Average	Average	Sep-23
Parametric Volatil Risk Pm-Def	EIVPX	Options Trading	Bronze	Average	Above Average	Above Average	Sep-23

Source: Morningstar Direct. Data as of December 2023.

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Morningstar Manager Research Services  
ManagerResearchServices@Morningstar.com



22 West Washington Street  
Chicago, IL 60602 USA

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