Investor Guide
Multi-Strategy Alternatives

Key Ideas

• Multi-strategy alternatives seek to provide access to a collection of alternative investment strategies
• These strategies have historically offered attractive returns and seek to diversify investor portfolios
• We believe that combining these strategies into a multi-faceted approach is an efficient way to capture alternative returns

Please read important disclosures at the end of this paper.
What Are Alternatives?

Alternative investment strategies look beyond buying and holding stocks and bonds to help investors achieve their long-term goals. These strategies — which can involve alternative assets like commodities or currencies, or alternative tactics such as taking a position on an asset’s decline — are generally more flexible, may offer better diversification, and are increasingly accessible to individual investors.

Alternative strategies generally seek to earn money by capitalizing on opportunities when misperceptions or a lack of information lead markets to over- or undervalue assets that are relatively easy to trade. While many traditional managers may try to do the same (for example, a managed fund that attempts to beat the stock market), they often face constraints that may prevent them from fully capturing opportunities. These constraints may include being limited to investing in just one or a handful of countries, or just one asset class, or they may be unable to take a position against securities that may be overpriced. By contrast, many alternative strategies seek to position themselves to make money when markets are falling, as well as when they are rising.

The Multi-Strategy Approach to Investing in Alternatives

One approach to investing in Alternatives is to take a diversified approach by seeking to provide broad exposure to these strategies, which can be grouped into three broad categories:

- **Arbitrage**
  Seeks to capture a mispricing between two related securities. For example, shares of the same company could trade on different exchanges for different prices. By buying the cheaper one and shorting the more expensive one, this strategy seeks to earn money when the two prices converge to “fair value.”

- **Equity**
  Seeks to profit from market inefficiencies in individual stocks. For example, a stock’s price may be higher than the company’s intrinsic value and profitability indicate it should be. One could seek to take advantage of the market’s overvaluation by shorting the stock and profiting if the price decreases to its fair value.

- **Macro**
  Seeks to profit from inefficiencies and dislocations in global stock, bond, currency and commodity markets. For example, if European stock markets in aggregate appear “cheaper” than U.S. markets — that is, their prices are low compared with U.S. stocks with comparable earnings or growth — a macro strategy may take long positions in European indices and short positions in U.S. indices.
Why Consider Alternatives?

Many investors’ portfolios have traditionally relied on only two sources of returns: stocks and bonds. Alternatives seek to provide access to other sources of returns, with the potential benefits of reducing the risk of an investor’s overall portfolio, improving overall returns, or both.

Exhibit 2 | Comparison of Growth: Alternatives, Stocks and Bonds*
January 1, 1994–December 31, 2013

* Sources: Datastream, Credit Suisse, AQR. Past performance is not a reliable indicator of future of performance. Alternatives are represented by the Credit Suisse Hedge Fund Index, Stocks are represented by the MSCI World Index, and Bonds by the Global Barclays Aggregate Hedged Bond Index. Performance returns are presented in US dollars and gross of fees. Broad-based securities indices are unmanaged and are not subject to fees and expenses typically associated with managed accounts or investment funds. Investments cannot be made directly in an index.
Because alternatives seek to earn profits from opportunities that are distinct from equity and bond markets, they are among the more diversifying strategies available to investors. As such, they may offer additional benefits for risk management. Generally, alternative strategies seek to:

- Have low or modest correlations to stocks and bonds
- Offer protection when traditional markets struggle

**Performance in Different Market Environments**

Historically, many alternatives have also helped investors to reduce losses in weak economic environments, as highlighted in the chart below. Because different alternative strategies seek to capture different types of market opportunities, the combination tends to perform well across various market environments, providing additional portfolio benefits. For example, alternative investment strategies outperformed the stock market during both the tech bubble and the tech bust, and fared better than stocks in the financial crisis.

**Exhibit 3 | Comparison of Performance: “Stress Periods”***

<table>
<thead>
<tr>
<th></th>
<th>Alternatives</th>
<th>Stock Market</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tech Bubble (1/1/99–3/31/00)</td>
<td>29%</td>
<td>24%</td>
</tr>
<tr>
<td>Tech Bust (4/1/00–7/31/02)</td>
<td>5%</td>
<td>-37%</td>
</tr>
<tr>
<td>Financial Crisis (7/1/07–3/31/09)</td>
<td>-15%</td>
<td>-45%</td>
</tr>
</tbody>
</table>

* Sources: Datastream, Credit Suisse, AQR. Past performance is not a reliable indicator of future of performance. Alternatives are represented by the Credit Suisse Hedge Fund Index and the Stock Market is represented by the MSCI World Index Performance returns are presented in US dollars and gross of fees.

**Investing in Alternatives**

Institutional investors were among the pioneers in alternative investing and many have used alternatives in their portfolios for decades. High-net-worth individuals have increasingly invested in alternatives, and recently many of these strategies have been made available for a wider audience of investors. Accessible through wholesale fund offerings, these strategies have sought to become more “investor friendly,” with many offering lower minimum investments, improved liquidity, full transparency and no performance fees.

AQR is a pioneer in alternatives investing, and in managing alternatives portfolios for institutional and individual investors. In building a multi-strategy alternative portfolio, we seek to provide investors a collection of core strategies to capture a broad range of market opportunities. The goal of the multi-strategy alternative approach is to reduce the risk of an investor’s total portfolio, enhance its returns, or both.
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There is a risk of substantial loss associated with trading commodities, futures, options, derivatives and other financial instruments. Before trading, investors should carefully consider their financial position and risk tolerance to determine if the proposed trading style is appropriate. Investors should realize that when trading futures, commodities, options, derivatives and other financial instruments one could lose the full balance of their account. It is also possible to lose more than the initial deposit when trading derivatives or using leverage. All funds committed to such a trading strategy should be purely risk capital.

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The Credit Suisse Hedge Fund Index is separated into ten primary subcategories based on their investment strategy. The Credit Suisse Hedge Fund Index in all cases represents at least 85% of the AUM in each respective category of the index universe. The methodology analyzes the percentage of assets invested in each subcategory and selects funds for the index based on those percentages, matching the shape of the index to the shape of the universe. Fund weight caps may be applied to enhance diversification and limit concentration risk. The index is calculated and rebalanced monthly. Funds are reselected on a quarterly basis as necessary.

The MSCI World Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets.

The Barclays Capital Global Aggregate Bond Index provides a broad-based measure of the global investment-grade fixed income markets.

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