

Investment challenges of today

The past 15 years have been extremely exciting in the world of finance. Markets have been pretty much on an upward trend, with a small hiccup in the stock markets along the way in 2001. Innovative products that allowed risks to be transferred across the financial ecosystem made it possible for financial institutions to generate record-breaking results year after year and bring about a new world order.

Despite this exceptional environment pure-play investment management firms that were limited to the equities markets were still struggling to generate the kinds of returns they were accustomed to prior to the crash of 2001, despite the Dow and a few other indices hitting all-time highs in 2007. The low interest rate environment that prevailed subsequent to the dot.com crash also forced numerous fixed income managers to journey beyond their traditional markets and look for spreads in new and upcoming economies. Many institutions increased their exposures to alternative investments, and even complex collateralized debt instruments. Nevertheless, for the ambitious investors the opportunities were extremely attractive. Commodities, for example, underwent explosive price appreciations, which allowed those that specialized in these markets to register unprecedented returns.

Of course, this world came to a dramatic halt in August 2007 and it has been on a downward spiral ever since, although it is not clear what will happen between the time this letter is written and when it is published in late November. Investment managers are now facing a very tough environment, with most expected to register significant falls in assets under management, be it due to price drops or liquidity extractions by investors. They are finding themselves having similar conversations with their investors that they were having in 2001, except that the world is a lot different now. A pending tragedy was postponed to today and it's time to realize its full impact.

That is why this issue of the Journal is extremely timely. The articles in this issue look at ways institutions can make their assets work harder, make suggestions about the kinds of investments that investors might not have considered previously, and prescribe institutional frameworks that are deemed necessary for protecting pensioners and their investments. Thanks to the papers in this issue we find out that despite the best assurances, investors are typically quite naïve in how they select investments. We also find out whether investment managers do perform as well as previous studies with methodological shortfalls claimed; and the answer is certainly no.

There is, of course, a silver lining. We read that investment committees can work if the structure is managed effectively. Alternative investment methodologies are also discussed and examined, and prescriptions are made concerning ways of improving the efficiency of the institution itself to extract more from each dollar under management.

The outstanding group of contributors to this edition probably never realized how timely their papers would be when they first thought about their submissions. We are grateful to them for helping us maintain the Journal's exceptional standards by submitting papers that are not only profound but also extremely practical in focus.

We hope that these articles help you in your own efforts to achieve the financial and economic efficiencies necessary to survive and perhaps even thrive in today's highly volatile environment. And as always, we hope that you enjoy reading this issue of the Journal and that you will continue to support us by submitting your ideas.



On behalf of the board of editors