

Quick Take: Low Volatility to Diversify Trendy Hedge Fund Longs?

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In 2021, low-vol has complemented popular hedge fund longs

- The recent volatility among popular hedge fund positions has made for dramatic headlines. On days of forced short covering in late January, even common hedge fund *longs* generated large realized negative active returns, as leveraged long/short investors raised cash or adjusted positions to maintain notional balance.
- Active returns of low-beta equity portfolios were nearly the *mirror image* of hedge fund long active returns. (Top chart.) We expect low-beta equities to continue to benefit, on a relative basis, on days of hedge fund distress and pressure on hedge fund long holdings.

Long-term perspective

- Over the long term, long/short equity hedge funds have tended to be long high-beta stocks. Consequently, the excess returns of their *longs* have been negatively associated with the excess returns of low-volatility portfolios. (Bottom chart.) The correlation between monthly excess returns of the Goldman Sachs Hedge Fund VIP Index* and the MSCI U.S. Minimum Volatility Index is -0.41.

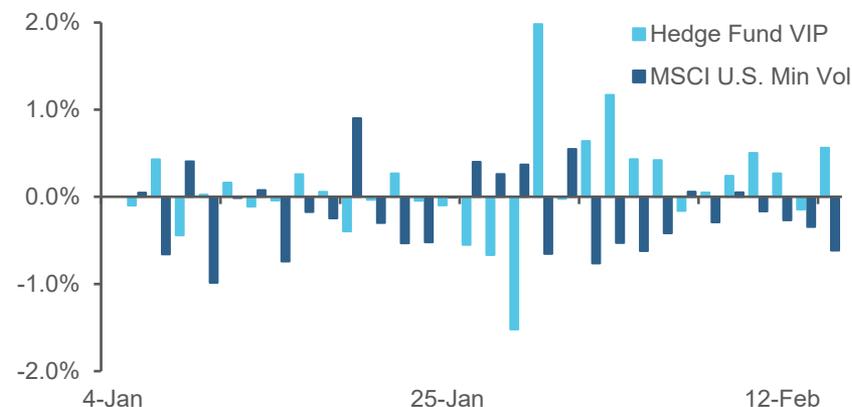
A diversification opportunity?

- While low-volatility strategies have underperformed the market and risk-seeking styles recently, low-vol has delivered a more stable path to excess returns for decades. We believe that the underlying behavioral and structural drivers that have contributed to low-vol's long-term success remain in place.
- As such, we see opportunity in pairing low-vol strategies with concentrated risk-seeking managers, to diversify risk associated with popular positions while adding an additional long-term and lower-beta return premium.

* The Goldman Sachs Hedge Fund VIP Index delivers exposure to a collection of equity securities expected to be most influential of the returns of long portfolios of hedge funds.

Hedge Fund Longs and MSCI U.S. Min Vol Index: Active vs. MSCI USA

Daily Active Returns (2021)



Average Low Vol Monthly Active Returns by HF Long Active Return Quartile (2008 - Jan 2021)



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