Global Macro: A Top-Down View

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RELATED FUND: Macro Allocation

Macro investing—which adopts a top-down view of the world to analyze broad trends and allocate risk across asset classes, geographies, and sectors—offers a liquid investment that aims to deliver strong risk-adjusted returns without relying solely on rising equity or bond markets.

What is Global Macro?

Global macro investors subscribe to a top-down view of the world instead of approaching research with a bottom-up lens. They analyze broad macroeconomic and geopolitical trends to construct a diversified investment strategy with risk allocated across geographies and exposures, including equities, fixed income, currencies, and commodities.

The goal: strong risk-adjusted returns without having to rely on rising equity and fixed income markets. Freed from adherence to traditional benchmarks, macro managers take risks only in those markets, currencies, or commodities they believe are adequately compensated.

While some global macro strategies may dynamically manage their equity beta profile (a measure of a strategy’s
sensitivity to the market), most macro strategies have a long-term beta expectation ranging from 0.0 to 0.5—a portfolio with a beta greater than 1 is more volatile than the market and a portfolio with a beta less than 1 is less volatile than the market.

The macro universe can mostly be broken down into two approaches to allocating risk across geographies and asset classes: systematic and discretionary.

Two Approaches: Systematic and Discretionary

Systematic
Rely on quantitative or technical models that allocate capital in a structured fashion with little to no subjective discretion (other than what is built into the models themselves).

Discretionary
Focus on fundamental research and the application of proprietary quantitative and qualitative assessments of economic, thematic, and political trends to subjectively allocate risk.

A Global, Multi-Asset Approach

Macro strategies offer a form of diversification that traditional investing strategies often struggle to provide.

Bottom-up investing certainly has its merits, and many portfolios are well-diversified from a bottom-up view. But introducing a top-down, multi-asset strategy can provide many benefits to a portfolio.

Economic, thematic, and political trends are often not isolated to one country, region, or asset class. Their influence may span geographies and cut across many markets and currencies simultaneously.

For example, the rise and fall of commodity prices over the past 15 years has affected many emerging and developed economies with consequences visible across these economies’ equity and fixed income markets and currencies.

A slowdown in Chinese growth has affected not only China and Greater Asia, but also China’s trading partners and commodity markets.

A global macro manager that incorporates the impact of these macro influences across all asset classes, regions, and sectors greatly enhances the total diversification of a portfolio.

Flexibility

Macro strategies are benchmark-agnostic, which means they only own those markets and currencies that appear to be cheap and/or adequately compensated, and avoid (or short) those which appear to be expensive and/or not adequately compensated.

Consider how this differs from a traditional (benchmark-relative, long-only) strategy. If a manager of such a strategy believes Japanese equities are overpriced, the portfolio will own fewer Japanese equities than the benchmark. But the portfolio still owns Japanese equities. Not only does the portfolio have exposure to an unattractive market, but the amount of risk the manager is willing or able to take in other more attractive opportunities is commensurately reduced. In contrast, a macro manager will either not own Japanese equities or
will establish short exposure to benefit from a current overvaluation and expected subsequent price depreciation relative to other more attractive markets.

Short exposures can also be used to isolate relative opportunities (positioned in opposition to a long position in another market such that the two—taken together—net to zero exposure) or to broadly reduce portfolio risk by decreasing beta, duration, or currency exposures.

Importantly, because true macro strategies are both multi-asset and multi-currency, macro managers can separate asset and currency decisions and are able to take risk exposures in opposite directions if so desired.

Taking the former example a step further, a macro manager may believe that the Japanese yen is undervalued at the same time the Japanese equity market is overvalued. The manager would thus take a long position in the yen while simultaneously shorting the equity market. This offers a dual benefit should both the equity market and the currency revert toward their fundamental values.

The Ability to Invest in Uncorrelated Exposures

Another advantage of macro strategies is their utilization of exposures that have little to no correlation with traditional markets, such as currencies and commodities. The inclusion of one or both of these risk exposures increases the breadth and diversification of a portfolio, which then enables macro managers to seek opportunities or mitigate risks where traditional managers may not be able to.

The Use of Expanded Instruments

Global macro managers also have access to an expanded pallet of instruments from which to choose to implement their views. They may use exchange-traded funds (ETFs) and index-level derivatives such as futures, forwards, swaps, and options.

Sometimes investors incorrectly equate derivatives with higher levels of risk. Derivatives can be used to both increase or decrease the intended risks of a strategy, and often represent the most efficient means of doing so.

Advantages of these instruments can include increased liquidity, lower cost, tax efficiency, the ability to short, greater precision, and even the ability to customize. They can also provide exposures (or payoff profiles) that traditional instruments cannot. For instance, options contain asymmetric payoffs, which can provide downside protection that traditional instruments lack.

Attractive Liquidity Profile

Lastly, a large hurdle to the majority of alternative investments is the liquidity profile. For investments like private equity, infrastructure, and real estate, an investor’s capital is often locked into the strategy for a long period of time, while other alternative strategies attempt to capture returns in assets that are inherently illiquid, such as distressed assets.

Global macro strategies, in contrast, typically have an attractive liquidity profile because the underlying markets and instruments used are all very liquid themselves. This can be a benefit for those investors who are seeking diversification without having to sacrifice liquidity.
Conclusion

Macro investors adopt a global, top-down view of the world in which they analyze broad macroeconomic and geopolitical trends to allocate risk across asset classes, geographies, and sectors in an unconstrained fashion. The outcome is a liquid strategy that aims to deliver strong risk-adjusted returns without necessarily relying on rising equity or bond markets. When included in a portfolio, macro strategies provide macro diversification that portfolios focused exclusively on bottom-up analysis lack, thereby improving portfolio performance through return enhancement or risk mitigation.
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