

ASSET CLASS

“MANNA”

Asset Class as defined by Investopedia : “A group of securities that exhibit similar characteristics, behave similarly in the marketplace, and are subject to the same laws and regulations. The three main asset classes are equities (stocks), fixed-income (bonds) and cash equivalents (money market instruments)”

Do you agree with the definition above and is this how you would define “asset class”?

Before I answer your question, we need to talk about why the definition is relevant. Investors desire diversification, which can be achieved by investing in multiple asset classes that are uncorrelated to each other.

An asset class should not be limited to securities alone. For example, derivative financial instruments, collectibles, and horses are not securities but are asset classes. Asset classes may exhibit low correlation to other asset classes, but it is not a requirement. For example, say German bonds and Korean equities were highly correlated, I doubt that anyone would consider them part of the same asset class.

I would classify investments as either traditional or alternatives.

So then, what are traditional assets?

Traditional investments include equities, fixed income, and cash equivalents. Alternatives include:

- Hedge funds
- Real estate/oil & gas
- Private equity/venture capital/LBO
- Commodities/Currencies
- Derivative financial instruments
- Classic cars/horses
- Collectibles
- Anything else that is not “traditional”

Would you say “traditional” investments trade in increasingly efficient markets (diminishing risk premia) vs. alternatives (majority are still inefficient – and offer risk premia).

As more capital infuses the latter market, the efficiency gap between the two is diminishing. After all, hedge funds, for example, exploit market imperfections, which, therefore, make the markets, in which they trade, more efficient.

Is it possible to regulate investing in horses? Or cars? How relevant is the issue of regulating assets?

The roles of regulation include protecting investors from fraud, and maintaining the integrity and stability of markets. Of course, it is possible to regulate assets, but with government's limited resources, it may be more practical to focus on the investment vehicles and the markets rather than the assets themselves. In any case, whether an asset or industry is regulated should have no bearing as to whether it is part of an asset class.

What differentiates an asset class from an “investment vehicle”?

An investment vehicle is an investor.

Are investors “asset classes”?

Would you call pension plans, university endowments, and Bill Gates asset classes?

An investment vehicle is a business model that contractually governs the relationship between the investor and the manager of such vehicle.

Equities, bonds, cash (and its equivalents): is “everything else” a permutation, combination and re-packaged version of the former?

Absolutely not. For example, “classic cars” should be uncorrelated to equities, bonds, and cash.

How would you christen “something” that provides “superior”, risk-adjusted returns, no or low correlations to financial market instruments, achieves diversification, is liquid, regulated, has no capacity constraints...?

I'd call it “manna.”



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