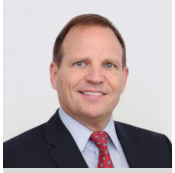
Market Update January 2025

When things turn out differently than you think

The US stock markets are being fuelled by the euphoria of lower interest rates, lower taxes and deregulation. In addition, the Trump administration's protectionism is intended to support the domestic economy and impose significant tariffs on competitors. Accordingly, the 20 largest banks on Wall Street expect the S&P 500 to rise by an average of +12% in 2025.

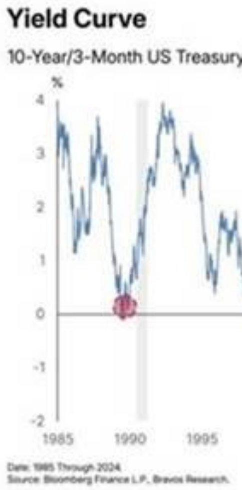
In our view, this ignores a number of important factors. Equity markets have performed exceptionally well over the past five years, gaining over +70% in USD terms, including 2022, as measured by the MSCI World Total Return Index. Secondly, a trade war would also be very damaging to the US economy, especially as the US government is increasingly tangling not only with China, but also with Europe, Canada, Mexico and other key partners.

Finally, interest rates have recently emerged from a prolonged phase of inverse yields, which has always signaled a recession over the past 40 years (see chart).



Stefan Steiner

So will things turn out differently than you think? We recommend reducing equities and increasing uncorrelated hedge fund strategies in order to reduce a potential loss of capital.



In the spotlight

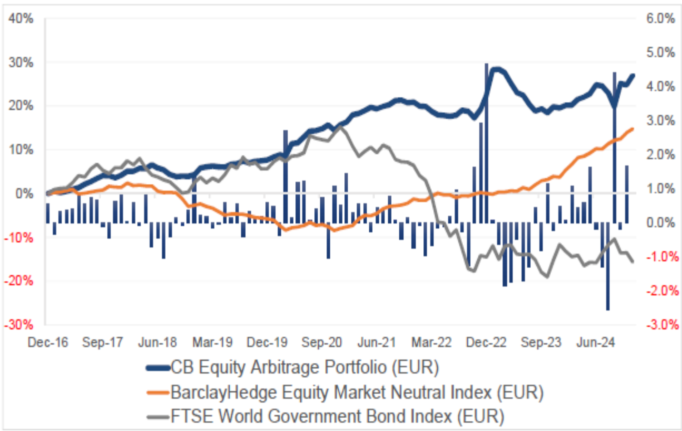
Equity Arbitrage

We see good potential for our equity arbitrage strategies, which will benefit from higher interest rates and expected market volatility. The CB Equity Arbitrage Portfolio (EUR) certificate had held up well in a bad equity year like 2022 and delivers a steady return above the risk-free rate in a normal year. The return of +6.2% in EUR for 2024 was decent and we expect a high single-digit return again in 2025, by and large regardless of the direction of the equity markets. The certificate has definitely more upside potential than fixed income investments in EUR for 2025

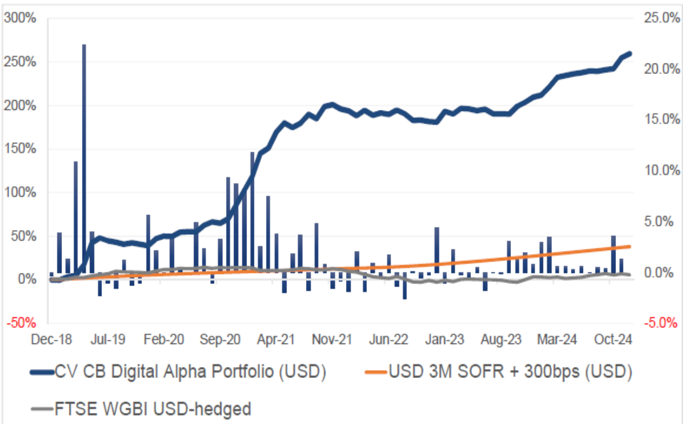
Digital Alpha Arbitrage

After a strong year for Bitcoin and other digital assets, the risk of setbacks has increased. Our long-biased CV CB Digital Asset Portfolio (USD) certificate delivered a good return of +27% in 2024. Now, we recommend allocating a little more conservatively and considering the CV CB Digital Alpha Portfolio (USD) certificate. The high volatility in the sector opens up many interesting arbitrage opportunities that yield good returns. The certificate hardly lost any money in 2022, when Bitcoins suffered a drawdown of –65%, and was up +16.1% in USD last year.

Cumulative returns since January 2017



Cumulative returns since January 2019



Addressing Challenges

In an increasingly complex market environment where traditional investment strategies are reaching some extremes (e.g. valuations), we provide asset managers with access to diversifing multi-manager portfolios. As specialists in liquid alternative strategies, we focus on meeting investors' needs—regardless of market conditions.

High volatility, limited market access, cost pressures, and the expectation of delivering stable returns are clear challenges. By using Actively Managed Certificates (AMCs), we make these multi-manager portfolios available quickly, efficiently, and cost-effectively. Strategies that were once reserved for institutional investors are now easily accessible.

Proven Solutions for Clients

Using three extremely successful strategies that we have implemented at the request of various clients, we show what challenges asset managers have to overcome in different markets - and how we have solved them:

- China: The market is characterized by high volatility and significant downside risk. ETFs tend to be too volatile, while direct investments in the region are often difficult to access. The AMC CB Greater China Portfolio (USD) has delivered an absolute return oriented exposure to China with much less downside.
- Commodities: Traditional investments, such as tracker ETFs, often suffer from structural weaknesses, including the "rolling effect" of futures and one-sided long positioning, which can lead to significant losses in falling markets. The AMC CB Global Commodity Portfolio has performed in up and down commodity markets.
- Digital Assets: Young, inefficient markets like cryptocurrencies offer great potential but are often avoided due to extreme volatility and uncertainty. The AMC CV CB Digital Alpha Portfolio has taken advantage of market inefficiencies to deliver positive returns with very low volatility.

Expanding Opportunities for Strategies

Our multi-manager approaches are highly adaptable and allow for the implementation of virtually any investment theme or traditional long-only strategy—enhanced with effective downside protection. Whether it's macroeconomic trends, corporate events, or market-neutral arbitrage, the possibilities are broad and customizable.

Armin Vogel

Thanks to this flexibility, strategies can be tailored to meet specific goals and requirements. These approaches provide a robust foundation for diversification and attractive returns—flexible and bespoke to your needs.

Why AMCs Are very suitable

AMCs enable asset managers to execute strategies quickly, flexibly, and efficiently through a simple and cost-effective setup process. Fees include a one-time setup cost of USD 2,000, annual administration fees of 30 basis points, and a management fee ranging from 0.5% to 1%, which can incorporate a performance-based component.

Their adaptability allows strategies to be adjusted or liquidated easily, ensuring portfolios remain aligned with changing market conditions or client objectives.

Another key advantage is the independence of the issuer, which we established to exclusively focus on this role. The issuer is free from any other business activities, especially banking, thereby significantly minimizing counterparty risk.

For clients who prefer a different structure, these same strategies can also be implemented in a fund format, offering multiple share classes to accommodate a variety of investor preferences. Regardless of the format, AMCs and funds alike provide tailored solutions to meet the diverse needs of modern asset managers.

Simplicity and Specialization in Action

What makes the AMCs advised by Crossbow unique, is the combination of simplicity and specialization. As independent advisors, we remain in the background while you benefit from our deep expertise. Our strategies are flexible, quick to implement, and provide access to specialized markets that are often not covered by traditional ETFs or funds.

Whether you're building a defensive portfolio for volatile markets or targeting innovative growth sectors, AMCs provide your clients with exactly what they seek: stability, performance, and access to a new dimension of investment opportunities.

If you're interested in tailored solutions or would like to learn more about our approach, we are happy to assist. Please contact me at av@cb-partners.com.

Top Hedge Fund Industry Trends for 2025

As the hedge fund industry evolves, Don A. Steinbrugge highlights pivotal trends shaping its trajectory in 2025.

1. Increased Customization: Institutional investors are prioritizing tailored solutions such as separately managed accounts (SMAs) and co-investments to improve cost efficiency and risk control.
2. Focus on Sustainability: ESG (Environmental, Social, and Governance) integration is becoming a cornerstone of investment decisions, with managers aligning ESG strategies with performance objectives attracting significant inflows.
3. Consolidation and Scale: Larger, well-established hedge funds are gaining dominance as smaller funds struggle with rising operational costs and regulatory pressures.
4. Technology and AI: The adoption of artificial intelligence and machine learning is transforming investment processes, with advanced algorithms offering competitive advantages.
5. Strength in Private Markets: Private markets, including private equity, credit, and venture capital, are gaining traction as traditional asset classes underperform in uncertain economic environments.
6. Increased Regulatory Demands: Heightened regulations require hedge funds to adapt their strategies and internal processes to ensure compliance.
7. Demand for Liquidity: Investors are increasingly favoring liquid investment strategies that offer flexibility and quicker access to capital.
8. Fee Pressure: There is a shift toward lower management fees and a stronger focus on performance-based fee structures.
9. Enhanced Risk Management: Advanced risk management techniques are being adopted to address rising market volatility and complex macroeconomic conditions.
10. Specialized Strategies: Niche strategies, such as sector-focused funds or thematic investing, are becoming more popular as investors seek higher returns in less efficient market segments.

In summary, 2025 presents significant opportunities for adaptable, forward-thinking hedge funds. Firms that align with investor priorities in customization, ESG, and technological innovation while navigating economic and regulatory challenges are set to excel.


Armin Vogel

Optimal Hedge Fund Allocation

The study authored by Gregory W. Brown, Juha Joenväärä, Christian T. Lundblad, and Richard Maxwell examines the optimal allocation of hedge funds in a diversified portfolio of stocks and bonds. It emphasizes the diversification benefits hedge funds can provide, even in scenarios where they generate minimal or no alpha. Using extensive data spanning 30 years, the authors analyze the role of hedge funds in improving risk-adjusted returns and explore how allocations vary based on different investor preferences and market conditions.

The findings highlight that hedge funds, under the assumption of zero alpha, can still merit significant allocations (around 20%) for investors with constant relative risk aversion. Equity and event-driven hedge fund strategies provide the greatest diversification benefits, while global macro and managed futures strategies are less effective. However, the allocation to hedge funds is highly sensitive to alpha assumptions. Allocations drop to zero if alpha falls below -1%, while alphas exceeding 2% can lead to almost full portfolio allocation toward hedge funds.

The study also addresses practical constraints, such as the cost and risk of investing in a limited number of hedge funds rather than a broad index. It finds that reducing the number of funds from 30 to 5 significantly increases the likelihood of hedge funds lowering investor utility, due to reduced diversification. Additionally, institutional-quality hedge funds, often excluded from standard commercial datasets, are shown to outperform their peers with higher alphas and lower correlations, offering superior diversification and risk-adjusted returns.

In conclusion, the study underscores the importance of considering alpha assumptions, strategy-specific benefits, and practical constraints in determining optimal hedge fund allocations, while emphasizing the value of institutional-quality funds in enhancing portfolio performance.

If you would like to receive the above mentioned papers, please contact Armin Vogel at av@cb-partners.com.