



Alternative Credit World Ripe for Investment

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Towers Watson clients allocated \$21 billion to alternative credit globally in the past five years

ARLINGTON, Va.--(BUSINESS WIRE)--Oct. 12, 2015-- Alternative credit should play a more pivotal role in institutional investors' portfolios to reduce reliance on the equity risk premium and to drive investment returns, according to a research paper by global professional services company Towers Watson (NASDAQ: TW). In the paper, entitled [Alternative Credit: Credit for the Modern Investor](#), the company asserts alternative credit has been underexploited by the majority in the past, both in terms of asset allocation and implementation efficiency, and should be added to investment portfolios to improve investment efficiency and portfolio robustness.

"Investors have historically accessed alternative credit predominantly via hedge funds or small off-benchmark allocations within existing traditional fixed-income mandates," said Dan Lomelino, Towers Watson's head of North American credit. "In recent years, dedicated alternative credit specialists and strategies have emerged, making it more accessible. However, there is still a long way to go, as the opportunity remains underinvested and misunderstood by many institutional investors."

Towers Watson defines alternative credit simply as all credit that is not traditional investment-grade government or corporate debt. In the liquid area, this includes high yield, bank loans, structured credit and emerging-market debt; and in the illiquid area, it comprises asset classes such as direct lending, distressed debt and specialty finance. Since 2010, Towers Watson has conducted about 300 alternative credit searches totaling almost \$21 billion.

"Despite alternative credit strategies having been underexploited by investors at large, some of our clients have recognized the key part they can play in a portfolio's strategic asset mix and an area where active managers can make a big difference," said Lomelino. "That said, institutional investors' investment in alternative credit so far is a drop in the enormous \$40 trillion global credit market ocean."

According to Towers Watson, funding an allocation to alternative credit can come from either equities or traditional credit, or both. Funding from traditional credit has the merit of reducing the exposure to those credit asset classes (investment-grade credit in particular) where the asymmetry of investment returns is unattractive. Meanwhile, funding through reduced equity allocations can help improve the balance of portfolios by reducing the reliance on the equity risk premium. At various points over the last year, equity has represented the favored funding source, notably when stretched valuations, and overly optimistic earnings growth and profit margin retention have weighed on future risk-adjusted return prospects.

"Regardless of whether an allocation comes from equities or traditional credit, alternative credit can play a valuable role in providing added sources of return and improved diversity. This is particularly attractive against a backdrop of rich valuations in the majority of mainstream credit assets," said Lomelino.

Towers Watson Investment

Towers Watson's Investment business is focused on creating financial value for institutional investors through its expertise in risk assessment, strategic asset allocation, fiduciary management and investment manager selection. It has over 800 associates worldwide, assets under advisory of over \$2.2 trillion and over \$75 billion of assets under management.

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