MEKETA

1Q 2025 MEETING OF THE MINDS

From Trade Wars to Wildfires

With the Marketable Alternatives Team

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The first quarter of 2025 delivered a potent mix of geopolitical escalation, technological disruption, and environmental catastrophe—all of which had material impacts on public markets and the alternative strategies we monitor.

From escalating trade tensions and "Liberation Day" tariff shocks, to the emergence of DeepSeek's low-cost AI model and devastating wildfires across California, the landscape for Marketable Alternatives has been defined by dispersion, volatility, and uncertainty.

In this edition of Meeting of the Minds, our Marketable Alternatives (MALTS) research team unpacks these events and explores how hedge fund strategies, insurance-linked investments, and global macro themes have evolved. As always, we focus on maintaining a long-term view while helping clients navigate the near-term noise with strategic clarity and manager insights.

Trade Wars/Tariffs

The Trump administration's first full quarter in office ushered in a wave of uncertainty around changes to the global economic and political landscape, stoking volatility across many markets and hedge fund strategies. Trade war concerns came to the forefront as the administration implemented, proposed, and revised a series of tariff measures—culminating in the April 2nd announcement of "Liberation Day," which included calls for broad tariffs aimed at addressing perceived imbalances in US trade relationships.

The Office of the United States Trade Representative stated these tariff rates are the numbers "necessary to balance bilateral trade deficits between the US and each of our trading partners" and that "tariffs work through direct reductions of imports".[1]

[1] Source: https://ustr.gov/issue-areas/presidential-tariff-actions

FIGURE 1
Reciprocal Tariffs

Country	Tariffs Charged to the USA	USA Discounted Reciprocal Tariffs	Country	Tariffs Charged to the USA	USA Discounted Reciprocal Tariffs
Argentina	10%	10%	Madagascar	93%	47%
Australia	10%	10%	Malaysia	47%	24%
Bangladesh	74%	37%	Morocco	10%	10%
Botswana	74%	37%	Myanmar (Burma)	88%	44%
Brazil	10%	10%	New Zealand	20%	10%
Cambodia	97%	49%	Nicaragua	36%	18%
Chile	10%	10%	Norway	30%	15%
China	67%	34%	Pakistan	58%	29%
Colombia	10%	10%	Peru	10%	10%
Costa Rica	17%	10%	Philippines	34%	17%
Côte d' Ivoire	41%	21%	Saudi Arabia	10%	10%
Dominican Republic	10%	10%	Serbia	74%	37%
Ecuador	12%	10%	Singapore	10%	10%
Egypt	10%	10%	South Africa	60%	30%
El Salvador	10%	10%	South Korea	50%	25%
European Union	39%	20%	Sri Lanka	88%	44%
Guatemala	10%	10%	Switzerland	61%	31%
Honduras	10%	10%	Taiwan	64%	32%
India	52%	26%	Thailand	72%	36%
Indonesia	61%	32%	Trinidad and Tobago	12%	10%
Israel	33%	17%	Tunisia	55%	28%
Japan	46%	24%	Turkey	10%	10%
Jordan	40%	20%	United Arab Emirates	10%	10%
Kazakhstan	54%	27%	United Kingdom	10%	10%
Laos	95%	48%	Vietnam	90%	46%

Source: White House.

Note:Hours after the announcement the White House confirmed internet speculation on a formula used to calculate their "reciprocal" tariffs, focusing on trade deficits as one of the main inputs. The Office of the United States Trade Representative published the "Reciprocal Tariff Calculations" saying that the announced tariff rates were the numbers "necessary to balance bilateral trade deficits between the US and each of our trading partners" and that "tariffs work through direct reductions of imports". The formula below was used to calculate the resulting tariff announced by country, which effectively represents US trade deficit with the foreign country divided by total good imports from that country. That result is divided by 2, and the outcome is the resulting tariff.

$$\Delta\tau_i = \frac{x_i - m_i}{\varepsilon * \varphi * m_i}.$$

In an era marked by shifting global alliances, fragile supply chains, and renewed focus on domestic manufacturing, the language of tariffs and trade imbalances has once again taken center stage. As policymakers look to reposition national economies for resilience and control, a familiar philosophy has re-emerged under a new name: Modern Mercantilism.

Modern Mercantilism refers to a newer version of 19th/20th century mercantilism that favored strong trade balances and focusing on national wealth, among other protectionist ideals. This was once popular over a century ago in the US (see President McKinley's use of tariffs, the Smoot/Hawley Tariff act, etc). Tariffs drive government revenue higher and reduce the trade deficit by reducing imports but are likely to have several negative impacts for consumers. They are often cited as an effective tax on the consumer, as the importers paying tariffs will likely pass that cost on.

> In its April 3rd edition of its daily publication Daily Observations, Bridgewater Associates called Liberation Day, "the latest step forward" in Modern Mercantilism."[2]
>
> **- RYAN LOBDELL**

A concerning aspect of the tariff rhetoric is the broad uncertainty surrounding it. It remains unclear how long the current levels of tariffs will be kept in place, how negotiations between the United States and its trading partners will unfold, whether retaliatory responses will result in further escalation, and what legal barriers the Trump administration may face if the executive order is challenged in court.

For businesses relying on scheduled imports, attempting to time when costs may rise and how to effectively change their pricing models to accommodate those rising costs is nearly impossible. One of the easiest paths to take is to pause production until there is clarity on the costs, to help enable more informed decisions on where to source inputs and manufacture products. This delay in investment poses a threat to US GDP.

If tariffs became the Trump administration's main foreign economic policy tool, they would likely be a significant headwind to US assets and US consumers. Many MALTS managers we have spoken to see the news as generally anti-dollar, anti-US growth, positive safe-haven assets like Yen/Swiss Franc, and US and German government bonds. A common refrain from investment managers is that from uncertainty or volatility comes opportunity. One positive quality we seek in managers who attempt to profit from global macroeconomic positioning across equities, interest rates,

[2] Source: Bridgewater Associates, April 2025.

https://observatory.bwater.com/document/bdolive/2025/04/bwam040325?referrer=email_bdo.bottom

It is difficult to predict if volatility across markets will dampen or accelerate in the near term, and we are admittedly not in the business of market timing.

currencies, and commodities, is that they carry optionality. They may have themes they are looking to trade around, but several groups often structure trades so that the strategy should profit in multiple scenarios. It is our team's goal to have relationships with skilled managers that we believe are highly capable of capitalizing on evolving markets and the dispersion that comes from paradigm shifts.

Tariff-related volatility and the unwinding of crowded equity positions by hedge funds created a challenging environment for many multi-strategy, equity long/short, and market neutral strategies. Selling pressure, particularly in early-March, was amplified by hedge funds bringing leverage down from levels which were elevated coming into the year, resulting in momentum rolling over and the underperformance of high-beta and AI-related stocks.

Commentary from sell-side firms and managers suggests that deleveraging pressure was particularly acute from March 6th, through March 10th 2025, with comparisons made to de-risking seen in January 2021 when hedge funds rushed to cover short positions in "meme stocks". The spread between hedge funds' most popular longs vs. their most shorted stocks, as measured by the GS HF VIP vs VIP Short index (GSTHVIPP), fell 5.4% during this period, and ended the quarter down 6.1%.[3]

It is difficult to predict if volatility across markets will dampen or accelerate in the near term, and we are admittedly not in the business of market timing. Meketa Investment Group's asset allocation approach strives to help our clients over the long-term, understanding that there may be volatile periods during that long-term investment horizon. Our team's work on Risk Mitigating Strategies ("RMS") attempts to help clients address the effects of both high volatility environments and protracted, lower volatility drawdowns that negatively affect the public equities and fixed income that make up a large portion of most institutional investors' portfolios.

[3] Source: Goldman Sachs , April 2025.

DeepSeek AI

Near the end of January, a Chinese Artificial Intelligence ("AI") company called DeepSeek launched its latest AI model, R1. The company spun off from a Chinese hedge fund known as High-Flyer. DeepSeek claimed that its new model was strong at problem-solving and developed at a much lower cost than Western competitors, such as OpenAI. This news triggered volatility across the tech sector, as DeepSeek's announcement challenged conventional thinking that it took cutting edge technology and high expense to train models at the highest levels. The market's panic was short-lived, as implied volatility did not spike, and instead there was a notable increase in stock dispersion. While what the media was making of DeepSeek felt like more of a short-lived news story than a foundational change in AI technology, it was worth us surveying several managers on their thoughts.

Perhaps unsurprisingly, there is no clear consensus on what DeepSeek's technology means for the future of generative AI. Some believe that the lower cost structure could be disruptive to incumbents, while others believe that the stated $6M cost is categorically false. The truth is likely somewhere in the middle; that the cost was higher than the $6M making headlines, but lower than what others have spent. Some estimates put this number well over $500m. DeepSeek did continue the momentum of open-sourced models, which allow users to distribute and edit code. Open-source models are cheaper and more customizable, while closed-source models have higher security and generally require less technical expertise.

One broadly shared view is that the lower cost profile will increase adoption and demand. Several managers noted that cloud providers like Microsoft, Google, and Amazon are positioned to benefit from the increase in computing demand.

At the same time, others emphasized that it remains nearly impossible to know who the winners and losers in the artificial intelligence ecosystem will be today. What is also agreed upon is that there is likely a shift to come from the value in this technology from hardware to software. After the internet or mobile computing became popular, hardware companies, like semiconductor manufacturers, were early winners in share price. The true economic beneficiaries though, were the software and/or service companies that created systemic changes in human behavior, such as Google with search or Apple with the iPhone.

Many believe that this will happen within the artificial intelligence ecosystem. Those that stand to be the long-term winners will be those that find ways to utilize AI in an application / service that end-users can seamlessly use to ultimately have an easier, more productive life. Our team will be closely monitoring the supply chain in both the hardware and software verticals. We will also be asking our managers that invest in this space to explain to us their portfolio construction given the dynamism of where value may sit from the hardware to software investment opportunity set. Given the stock market leadership of hardware names like Nvidia, there remains the opportunity for large tracking error swings for those clients who may benchmark a long-short equity investment against the S&P 500 or other indices where chipmakers can heavily influence gains or losses at the total index level.

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Los Angeles Wildfires

The recent Los Angeles wildfires, which began on January 7, 2025, driven by severe winds and dry vegetation, caused extensive damage across the region. The largest fires, the Eaton and Palisades Fires, along with several smaller fires, prompted the evacuation of more than 200,000 residents and resulted in the destruction of thousands of structures. Coincidentally, our team had visited the Palisades for an investment due diligence meeting in January 2024. A year later, the street this meeting was on, Via De La Paz, was largely reduced to rubble.

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Beyond the clear human toll, the wildfires also had implications for our research efforts, particularly in the insurance-linked strategy space. **Insurance-linked strategies**, commonly referred to as "ILS", generally derive return and risk from property damage insurance contracts related to natural catastrophes (e.g., earthquakes, hurricanes, etc.). When these natural catastrophes occur and create claims by policyholders, investors may be liable for the payouts. When no events occur, investors pocket the premium associated with the policy. Our team mainly views the benefit of an investment in the ILS space as being totally uncorrelated to financial markets, while also providing attractive yield potential.

Conversations with ILS managers indicate that the financial impact on the insurance market has been significant. Insured losses have been estimated around $35 billion, making this a major event comparable to the impact that Hurricane Katrina had on the ILS market. Performance can be affected by multiple factors, but most notably by portfolio exposure to global natural catastrophes. Some funds may diversify broadly across the world, while others may focus more on one region and catastrophe type, like Florida hurricane exposure (higher yield potential, but higher expected loss potential per event).

According to Artemis.bm, LA wildfires created significant dispersion in the ILS Advisers Fund Index, which, over the month of January 2025, lost about 2%. The ILS Advisers Fund Index tracks the performance of participating Insurance Linked Investment funds.[4] With 100% of the indices' funds having reported January returns, the difference ranged from +0.9% to -18.9%. We believe this underscores the importance of diversification—both within an ILS allocation and across an entire hedge fund program.

4 Source: Artemis.bm. The index comprises an equally weighted index of 37 insurance-linked investment funds.

Nothing but the Hits

Quick hits from the Marketable Alternatives Team. Short takes on themes we're tracking, what managers are saying, and corners of the markets we've been exploring lately.

Liquidity Is Having a Moment

With rising private market allocations and tighter capital call timelines, many investors are rethinking how liquid their "total" portfolios really are. Where will rebalancing capital or beneficiary payments come from in a drawdown?


ZACK

Total Portfolio Approach (TPA) Gets More Airplay

More managers are launching products aligned with the growing interest in Total Portfolio Approach—a strategy that emphasizes risk and return drivers over asset class silos. Popularized by the CAIA Association and several large non-U.S. allocators, TPA focuses on how investments contribute to total portfolio goals. Meketa's own **Functional Framework** reflects a similar philosophy: it's not about where an asset lives, but what role it plays. Not a one-size-fits-all model—TPA requires aligned governance, collaboration, and an educated boardroom.


SAM

Pass-Through Fees: In the Spotlight

Multi-manager and multi-strategy funds made headlines this quarter, particularly around the use of pass-through fees. While these expenses can be hefty, some argue they are necessary to retain talent. A number of institutional investors now incorporate profit retention thresholds in diligence—excluding funds that don't pass enough back to the end investor.


RYAN

Fees, Flexibility, and Hurdles - Oh My

Investors continue to push for innovation in fee structures: think "management fee or performance fee," "all performance, no management," or declining flat fees as AUM scales. There's also growing pressure to include hurdle rates—whether tied to cash or a benchmark like the MSCI ACWI.


SAM

Quiet Heroes

Strategies like trend following, global macro, and long volatility often hold large percentages of unencumbered cash. That unused cash typically gets invested in money market instruments—which can yield benefits to the end investor in today's rate environment.


ZACK

Discretionary vs. Systematic Long-Short Equity: A Performance Gap Emerges

Goldman Sachs data shows a stark divergence: through April 7, discretionary long/short strategies were down ~5.9% YTD, while systematic long/short were up ~10%.[5] Stay tuned—this could shape allocation decisions for the rest of the year.pass enough back to the end investor.

RYAN

Trend Following: Tough Q1, Wide Dispersion

The SG Trend Index was down 4.7% in Q1.[6] Funds that incorporated non-trend signals—like carry or seasonality —fared better. Returns ranged from -11% to +6%.

SAM

Carbon Confusion Continues

On March 12, California's Air and Resource Board delayed release of its Initial Statement of Reasons (ISOR), adding volatility to the California Carbon Allowances (CCA) market. Until the regulatory framework is clarified, uncertainty may persist—and so may the trading opportunities for those paying attention.

RYAN

Long Volatility and the Cost of Protection

"The negative bleed is just too much." We hear this often when clients talk about long volatility. Yes, these strategies carry cost—but in crises, they tend to shine. They're generally focused on conditional return, rebalance power, and protecting against what's not priced in.

ZACK

The first three and half months of the year proved to be quite an eventful period for financial markets. Heightened uncertainty, rapidly developing narratives, and large dispersion between asset classes and strategies can understandably raise questions. It is our role to monitor developments, assess their impacts on the strategies and markets we cover, and remain focused on our long-term perspective.

We remain committed to helping clients understand how alternative public assets can help serve as effective tools in institutional portfolios—supporting financial goals while enhancing resilience through market turbulence. As always, we welcome the opportunity to discuss these topics further and to serve as a resource in navigating what lies ahead.

5 Source: Goldman Sachs, April 2025.

6 Source: eVestment, April 2025.

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