

Related GMO Investment Solutions

- [Alternative Allocation Strategy](#)
- [Benchmark-Free Allocation Strategy](#)

LIQUID ALTERNATIVES AT WORK

Preserving Capital and Reallocating Through Market Stress

Asset Allocation Team | October 2026

GMO's liquid alternatives are hedge fund strategies (e.g., equity long-short, global macro, event-driven) managed with an emphasis on risk control and liquidity. The GMO [Alternative Allocation](#) Strategy ("ALTA") is a liquid alternative solution combining several underlying strategies; ALTA is available in a mutual fund with daily liquidity.

Liquid alternatives are a **tool** for your portfolio. Maximum effectiveness can be realized by deploying them smartly to achieve specific objectives. While they provide diversifying returns, liquid alts also serve as a source of **dry powder in dynamic allocations** that meaningfully vary weights with the market environment. In this use case, **daily liquidity is not merely an operational detail—it is a strategic advantage** and can actually facilitate higher total portfolio returns. In 2022, GMO's outsized allocation to liquid alternatives¹ within our unconstrained [Benchmark-Free Allocation](#) Strategy² helped to protect capital during the drawdown and facilitated portfolio rotation by taking advantage of changes in valuations.

From Defensive Positioning to Opportunistic Reallocation

Entering 2022, GMO's multi-asset portfolios were defensively positioned as we believed stocks and bonds were extremely expensive.³ At the time, Benchmark-Free held no Treasuries, less than 30% in stocks, and allocated over 60% to liquid alts.

As stocks sold off,⁴ risky assets became cheaper. Benchmark-Free's liquid alts portfolio held up well, with positive returns and low volatility. We actively drew down our liquid alts allocation to fund the purchase of 23 percentage points of stock and credit over the course of the year, materially changing Benchmark-Free's exposure to risky assets.

1

GMO's Alternative Allocation Strategy was initially launched in 2019. Effective January 31, 2025, GMO materially revised the strategy and established a new composite to reflect increased total exposure, wider volatility bands, and more diversified sources of return.

2

GMO's Benchmark-Free Allocation Strategy is an absolute return, go-anywhere liquid dynamic allocation strategy.

3

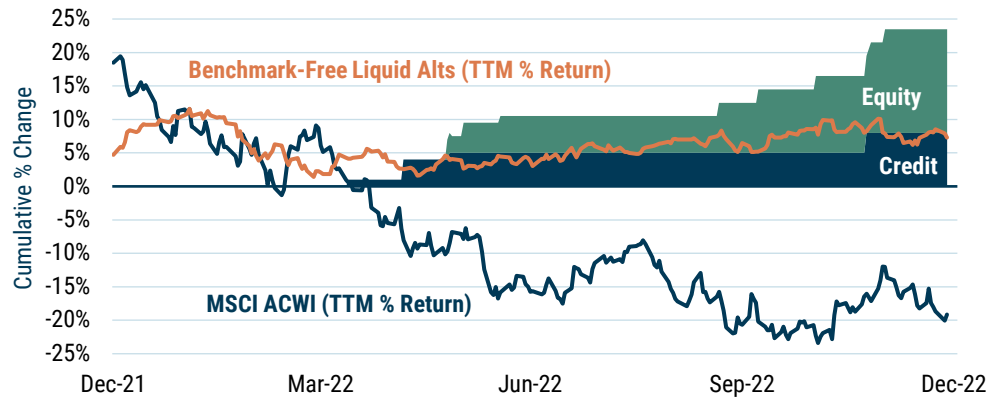
The yield on the 10-year U.S. Treasury hit an all-time low below 1% nominal, and stocks were swept up in a growth bubble in late 2021.

4

MSCI ACWI was down 18% and 10-year U.S. Treasury yields rose 236 bps in 2022.

LIQUID ALTS PROVIDED DRY POWDER TO REALLOCATE

GMO Benchmark-Free added 23% to risky assets sourced from liquid alts in 2022



As of 12/31/2022 | Source: GMO

MSCI data may not be reproduced or used for any other purpose. MSCI provides no warranties, has not prepared or approved this report, and has no liability hereunder. Please visit <https://www.gmo.com/americas/benchmark-disclaimers/> to review the composite benchmark disclaimer notice.

The features of our liquid alts allocation worked together to manifest this result:

- **Positive Return**—Tapping into multiple return drivers, our liquid alts portfolio was able to deliver a positive return when it was desperately needed.
- **Diversification**—Because liquid alts have virtually no equity beta or duration exposure, they were able to deliver when stocks and bonds both suffered double-digit drawdowns.
- **Liquidity**—Daily liquidity facilitated our seamless, incremental rotation out of alternatives, allowing us to purchase newly cheaper stocks and credit, and thus benefit from a strong equity rebound.

Preparing the Portfolio for Potential Risks

Liquid alternatives were critical for GMO's Benchmark-Free Strategy in 2022, a rare period where both stocks and bonds experienced major drawdowns. Could we face a similar drawdown in the future?

A number of scenarios could be particularly damaging for risk assets: selling pressure from a deluge of IPO shares coming off lockup; an AI boom that falls short of elevated growth and profit expectations; or some combination of either path with persistent inflation that drives real rates higher and pressures both stocks and bonds.

We believe today's wide range of plausible macro outcomes warrants the inclusion of diversifying assets in portfolios. While GMO's liquid alternatives are not designed to be

consistently negatively correlated to equities, several of our largest risk allocations within our Alternative Allocation Strategy⁵ could potentially benefit from an AI-driven unwind. Our Equity Dislocation and World Market Neutral strategies maintain short exposure to some of the market's most speculative AI-related areas and have historically performed well during periods when enthusiasm surrounding these themes has softened. Long-Short Quality shares many of these characteristics through its preference for higher-quality, more defensively positioned businesses, while our Global Macro strategies currently maintain a net short equity stance.

Together, these exposures could provide valuable diversification and a potential source of liquidity precisely when many traditional assets are under pressure, creating opportunities to rebalance into attractively priced risk assets following a market correction. **Liquid alternatives aren't insurance**, but they may be capable of generating positive returns through the cycle and performing independently from stocks and bonds, which could help in a macro tail event.

Conclusion

GMO's Asset Allocation team has used liquid diversifying strategies in portfolio construction for more than 25 years. That experience is reflected in Benchmark-Free, where liquid alts have been a critical component of the strategy's ability to deliver equity-like returns with roughly half the volatility since inception. By providing attractive returns, consistent diversification, and liquidity, we believe a liquid alternatives allocation can help investors preserve flexibility and capitalize on opportunities during periods of market stress.

AVERAGE ANNUAL TOTAL RETURN (NET, %) IN USD

		<i>Inception</i>	<i>1-Year</i>	<i>3-Year</i>	<i>5-Year</i>	<i>10-Year</i>	<i>Since Inception</i>
Alternative Allocation Composite	1/31/2025	15.91	N/A	N/A	N/A	N/A	13.98
FTSE 3-Mo. T-Bill		3.91	N/A	N/A	N/A	N/A	4.14
Benchmark-Free Allocation Composite*	7/31/2001	19.61	15.35	9.68	6.58	8.22	
CPI Index		3.01	2.81	4.04	3.32	2.55	

*Prior to January 1, 2012, the accounts in the Benchmark-Free Allocation Composite served as the principal component of a broader real return strategy. Beginning January 1, 2012, accounts in the composite have been managed as a standalone investment. Returns include a substantial, one-time litigation settlement recovery received on December 16, 2024. This event contributed 2.45% to 2024 annual performance, based on a representative account. Performance for other periods, including this date, was also positively impacted, sometimes materially. Without this recovery, performance would have been lower in both absolute terms and relative to the benchmark. Returns include a substantial, one-time proceed from the sale of certain Russian securities. The one-time sale of these securities contributed 0.93% (1-day performance impact), based on a representative account. Performance for other time periods was also positively impacted. Without these proceeds, performance would have been lower. Additional information is available upon request.

Performance data quoted represents past performance and is not indicative of future results.

Net returns are presented after the deduction of a model advisory fee and incentive fee if applicable. These returns include transaction costs, commissions and withholding taxes on foreign income and capital gains and include the reinvestment of dividends and other income, as applicable. Fees paid by accounts within the composite may be higher or lower than the model fees used. GMO LLC claims compliance with the Global Investment Performance Standards (GIPS®). A Global Investment Performance Standards (GIPS®) Composite Report is available on GMO.com by clicking the GIPS® Composite Report link in the documents section of the strategy page. GIPS® is a registered trademark owned by CFA Institute. CFA Institute does not endorse or promote this organization, nor does it warrant the accuracy or quality of the content contained herein. Actual fees are disclosed in Part 2 of GMO's Form ADV and are also available in each strategy's Composite Report.

Risks associated with investing in the GMO Alternative Allocation Strategy may include: (1) Management and Operational Risk: the risk that GMO's investment techniques will fail to produce desired results, including annualized returns and annualized volatility; (2) Leveraging Risk: the use of derivatives and securities lending creates leverage. Leverage increases the Fund's losses when the value of its investments (including derivatives) declines; and (3) Derivatives and Short Sales Risk: the use of derivatives involves the risk that their value may not change as expected relative to changes in the value of the underlying assets, pools of assets, rates, currencies, or indices. Derivatives also present other risks, including market risk, illiquidity risk, currency risk, credit risk, and counterparty risk. This is not a complete list of risks associated with investing in the strategy. Please contact GMO for more information.

Disclaimer

The views expressed are the views of the Asset Allocation team through the period ending October 2026, and are subject to change at any time based on market and other conditions. This is not an offer or solicitation for the purchase or sale of any security and should not be construed as such. References to specific securities and issuers are for illustrative purposes only and are not intended to be, and should not be interpreted as, recommendations to purchase or sell such securities.