

Beyond a Crystal Ball: What is Investment Skill?

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THE TRADITIONAL VIEW

Investment Skill
=
Forecasting Skill
=
Predicting
Market/Securities
Movement

THE EXPANDED VIEW

Investment Skill
=
Forecasting Skill
+
Structuring Skill

This article challenges the conventional understanding of investment skill, arguing it extends far beyond market forecasting. Rather than reducing skill to whether a manager has a crystal ball, this piece introduces structuring skill as a comprehensive framework encompassing four distinct competencies.

Four Components of Structuring Skill

Engineering: Designing strategies that isolate intended market views while minimizing trade baggage—unintended risk exposures that inflate tracking error and reduce information ratios.

Market-making: Generating returns through liquidity provision, applicable to both institutional dealers and asset managers who harvest liquidity premiums during market dislocations.

Operational: Managing the organizational infrastructure required to execute complex strategies, including technology systems, legal expertise, and cross-asset trading capabilities.

Access: Leveraging established networks and market presence to secure superior opportunities in private equity, new issues, and broker relationships.

Robust Alpha Characteristics

The article identifies four markers of persistent alpha: repeatable processes that generate consistent opportunities, frequent opportunities meaningful to portfolio performance, replication barriers rooted in operational complexity rather than solely proprietary insight, and genuine alpha rather than systematic exposures mistaken for skill.

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