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# A Unified Measure of Risk/Reward for Alternative Investments

Accounting for all the new risks of alternative investments

## Problem

Existing risk/reward measures are not adequate for alternative investments because they do not account for significant new risks that have not been present in traditional investments.

This has caused many to invest in alternative investments that appeared “safe” by traditional measures only to be surprised when the latent risks were exposed over time. These surprises have caused many to view alternative investments as too risky for prudent investors.

The problem is not that alternative investments are necessarily “too risky” but that traditional risk/reward measures do not properly account for all the risks present in these new types of investments. These new risks which have not been present in traditional investments require new measures.

Many such measures have been proposed and some including the Sharpe Ratio, the Calmar Ratio, the Sterling Ratio, etc. have come into common usage. Each of these measures attempts to address components of the total risk of an alternative investment. None of them is sufficient as a single measure because they all leave out significant risks.

This forces investors to decide which ratio is more important when faced with conflicting results. If fund A has a better Sharpe Ratio but a worse Calmar Ratio than those of fund B the investor must decide between the measures in order to decide which is the better investment?

## The Need for a Comprehensive Measure

What is needed is a comprehensive risk/reward measure that incorporates the important benefits of the Sharpe Ratio and other risk/reward measures and that takes into account each of the significant risks that may be present in any investment, whether traditional or alternative, one that allows direct comparison between very different types of investment types and managers. The measure should also allow the direct comparison of risk/reward between funds or managers with extensive track records and funds or managers with limited track records.

This paper proposes such a new measure of risk/reward, the Galt Ratio, that unifies each of the individual components of risk present in any investment to allow direct comparison between all types of alternative and traditional investments even when one or more of the fund managers have limited track records.

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