

**EXECUTIVE BRIEF**

The Unowned Layer

The Advisory Gap in Most Complex Portfolios

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Executive Summary

Complex portfolios are surrounded by genuine expertise. And they still accumulate structural risk.

Legal counsel handles entity structure. Accountants manage tax and reporting. Investment advisers set allocation. Banks execute. Each does their job well. None of them is positioned to own the layer where portfolio mechanics are actually determined.

That layer includes how hedges are constructed, how overlays interact, how capital is consumed by collateral, and how the portfolio behaves under stress. It includes the question of whether the hedge framework still reflects the portfolio it was originally built to protect.

The expertise required to examine that layer sits inside banks, attached to product distribution and balance sheet incentives. What the market has not produced is that same expertise operating independently, with no products to sell and no transaction conflicts. The result is a gap that persists quietly, often for years, accumulating cost that is rarely measured and not always visible until something forces the question.

1. How the Gap Forms

The advisory circle around a complex portfolio assembles gradually, with advisers added as problems arise. Each addition is justified. Over time the circle becomes a trusted, stable ecosystem the principal relies on across a wide range of decisions.

The problem is not the advisers. The problem is the architecture. The circle was built to solve discrete problems. It was not designed to see across them. Each adviser stops at the boundary of their mandate.

Legal counsel: entity structure, documentation, governance. Not the economic content of the derivative programme inside those entities.

Accountants: tax, reporting, accounting treatment. Not whether the instruments chosen are the right ones.

Investment advisers: allocation, manager selection, portfolio construction. The overlay programme sitting above that allocation is typically outside their frame.

Banks: execution, financing, product access. Deep structuring expertise exists here, but it operates inside a product mandate. Recommendations are shaped by what the bank can sell, not solely by what the client needs.

Hedge programme design sits between all of these mandates. Who owns whether the instrument is appropriate, whether the hedge ratio is correct, whether the collateral arrangement is efficient? Nobody asks the question, because nobody owns it.

2. What Drift Looks Like

A composite example makes the mechanics concrete. A family office establishes a USD hedge programme in 2019 against offshore equity holdings. The overlay is calibrated when rates are near zero, the portfolio is heavily growth-oriented, and carry costs are negligible.

Over the following five years, the asset mix shifts as private assets grow. Rates reprice materially. Carry economics reverse. Liquidity reserves tighten. The hedge ratio set at inception is never revisited. The programme still functions operationally. Nothing is broken. Reports are clean. Governance has no reason to raise it.

But the hedge framework no longer reflects the portfolio it was designed to protect. The overlay is consuming capital and carry in a way that was never underwritten at current rates, with a cost that is visible in isolation but rarely attributed to programme design.

This is the normal condition of portfolios built incrementally. Not broken. Drifted. Drift does not generate audit findings. It accumulates until something forces the question, and by that point the cost of correction is material.

3. Why It Persists

The gap persists for three reasons, none of which involves negligence.

Advisers optimise within their mandate.

The gap is not in their performance. It is in the design of the circle itself.

Governance processes are not designed to surface it.

Investment committee reviews assess allocation, performance, and manager quality. The questions that expose drift require a different frame: is the programme still doing what it was designed to do? Are the overlays interacting constructively? What happens to liquidity pathways under stress? These do not arise naturally in a conventional governance review.

The expertise that could identify it is conflicted.

Banks have the skills. The mandate attached to those skills is not the clients.

4. What the Unowned Layer Contains

The gap covers three domains, each with material consequences for capital efficiency and portfolio resilience.

Efficiency

Is the collateral and margining architecture consuming more capital and liquidity than it needs to? Are the carry economics of maintaining the current programme still positive? Has the cost-benefit calculation been revisited since market conditions changed?

Interaction

Do the overlays interact constructively, or do they create concentration, friction, or offsetting exposures the aggregate risk picture obscures? Has the portfolio's convexity profile been examined deliberately, or is it an accident of inception?

Resilience

What happens to the portfolio's liquidity position if markets move sharply? If the hedges pay off in a dislocation, is there a monetisation doctrine that converts those gains into usable capital? Or do they sit unrealised until the moment passes?

5. A Diagnostic

Six questions. If you cannot answer all of them cleanly, the unowned layer is probably active.

1. When was the derivative programme last reviewed by someone with no commercial interest in its continuation?
2. If your hedges paid off materially in a dislocation, is there a monetisation doctrine that would convert those gains into usable capital? Who owns it?
3. Do you understand how the overlays interact with each other under stress? Has that been modelled?
4. Has the FX overlay, if you have one, been re-examined since the interest rate environment changed? Are the carry economics still positive?
5. Does your governance process include a review of hedge ratios and collateral efficiency, or only a performance review?
6. When your bank last recommended a change to your derivative programme, was there an independent assessment before it was implemented?

These are not crisis questions. They are maintenance questions. Most portfolios of genuine complexity cannot answer all of them cleanly.

About This Brief

This Executive Brief is a companion to the Para Bellum Advisors practitioner paper: The Unowned Layer. The full paper covers the market structure analysis, a composite case study, and the extended diagnostic framework.

Available at www.parabellumadvisors.com/insights/

About Para Bellum Advisors

Para Bellum Advisors is an independent advisory firm specialising in derivatives structuring, structured finance, and capital optimisation for institutional investors and corporate treasury teams.

We work with private credit managers, project finance and infrastructure investors, asset managers, family offices, and corporate treasury teams managing complex exposures where structural precision makes a material difference to outcomes.

Our work sits at the intersection of derivatives structuring, capital efficiency, and execution. Practitioner-led, with three decades of APAC experience. No products to sell. No transaction conflicts. We act as an extension of the investment team, providing senior-level structuring capability without adding permanent headcount.

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