CIBC ASSET MANAGEMENT

# The evolved portfolio: Alternative investments enter the mainstream

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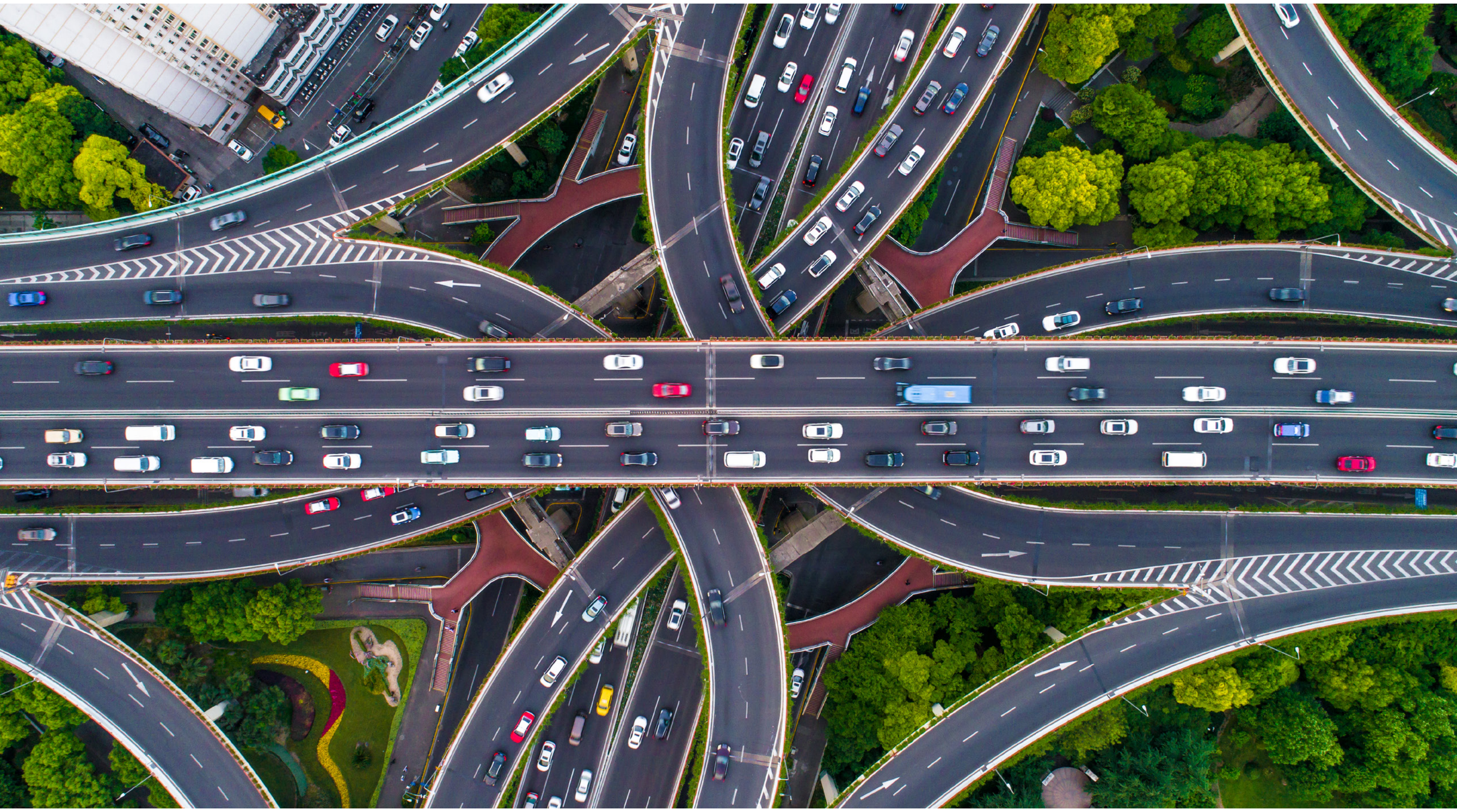

Professional asset allocators and advisors are navigating shifting asset correlations while balancing investor objectives and constructing robust portfolios. Traditional assets – publicly traded stocks and bonds – continue to form the foundation of portfolios. However, today investors require more tools to add uncorrelated returns, enhance income, or boost total returns. To meet these needs, there is a deepening availability of alternative investments, such as private credit, real assets, and hedge funds.

Previously only accessible to institutional investors, the world of alternatives remains murky to many investors. As access to alternative investments broadens, CIBC Asset Management is committed to partnering with advisors to deliver education, insights, and thought leadership.

The following Q&A features **Meric Koksal**, MD and Head of Product, and **David Wong**, CIO, MD and Head of Total Investment Solutions at CIBC Asset Management.

## How has the use of Alternative Investments evolved to where they are today?

**David:** Alternative investments can be broadly categorized into two groups: those where the underlying assets are liquid, such as hedge funds or commodities, and those where the underlying assets are illiquid, such as private equity, private credit, private real estate, and private infrastructure.

While alternative investments have existed since the 1940s, their widespread adoption began in the 1980s with the approach developed by David Swensen, who led the Yale endowment. Swensen's innovative strategy, now widely known as the Yale Model, helped the endowment achieve annualized returns of 13.7% from 1985 until his passing in 2021[1]. This was over 3% higher than the average for his endowment peer group and approximately 5% higher than the S&P 500. These results fundamentally transformed how institutions and high-net-worth individuals have invested over the past several decades.

However, for individual investors, alternative investments have historically played a minimal role in portfolios given the lack of availability (or high barriers to entry). The exciting development today is that these options are increasingly becoming accessible to individual investors through the creation of alternative funds designed specifically for wealth channels. These funds are built with features that make them more user-friendly, such as evergreen availability, lower minimum investment sizes, relatively frequent subscription and redemption periods, as well as timely and more transparent performance updates. They also eliminate barriers like capital calls over time and the J-curve effect, which have traditionally made alternatives impossible to implement for all but the largest institutions and family offices. From this perspective, we are living in an exciting era where a broader group of investors can now adopt these strategies.

## What are the options for alternative investments, and how do they work?

**Meric:** Alternative investments encompass a variety of strategies, each offering unique benefits to investors. Private equity involves investing in the ownership of private companies and spans different stages of a company's lifecycle. This includes venture capital for early-stage companies, growth equity for more established businesses, and buyouts where controlling stakes are acquired. Private equity can enhance returns for investors, as it typically includes a liquidity premium and provides opportunities to invest in companies at earlier stages of development which is more and more realized before they go public.

Private credit, also referred to as private debt, involves lending money directly to private companies. This form of non-bank lending can be an attractive option for the fixed-income portion of a portfolio, as it aims to deliver higher income, currently around 9-10% annualized, paid monthly.

Real assets, such as infrastructure, real estate, and natural resources, provide another compelling option. These investments involve physical assets and can take the form of either equity or debt. Real assets play a crucial role in creating a well-diversified portfolio by complementing the traditional equity and fixed-income mix. Additionally, they act as a hedge against inflation, as the value of physical assets and the income they generate – such as rents, tolls, or commodity prices – tend to rise with the cost of living.

Hedge funds, while sometimes considered separately, also fall under the broader umbrella of alternative assets. Hedge funds primarily invest in public securities and add value through not only investment selection, but also through sophisticated financial strategies.

Each of these options can benefit a client's portfolio in different ways. Focusing on those providing access to private companies, private equity can enhance returns, private credit can provide higher income, and real assets can provide a combination of growth and income while offering inflation protection. Importantly, all three categories – private equity, private credit, and real assets – offer returns that are not highly correlated to public markets, which helps reduce overall portfolio volatility and improve risk-adjusted returns.

## What are the performance characteristics of alternative investments?

**David:** It is challenging to generalize the performance of alternative investments because they encompass such a wide range of strategies, and returns can vary significantly depending on manager selection. Additionally, data availability for alternatives can be more delayed compared to traditional investments due to factors such as lags in appraisals for private assets.

That said, certain categories of alternatives provide timely performance data. For example, relative value market-neutral equity hedge funds often perform well during volatile periods. In the first quarter of 2025, when the S&P 500 declined by 4.3% in U.S. dollar terms, the median manager in this category delivered positive returns. Similarly, in 2022, when the S&P 500 fell by 18%, the median manager in this hedge fund universe achieved a gain of over 1%.[2]

Private assets, on the other hand, tend to exhibit lower volatility because they are not subject to daily market pricing. For instance, during the volatile April 2025 period, the S&P 500 experienced significant swings, creating discomfort for public market investors. In contrast, private equity investors did not receive immediate valuation updates, allowing them to maintain a long-term perspective. This approach can help investors avoid the emotional decision-making often triggered by short-term market fluctuations.

## How do alternative investments benefit investor portfolios?

**David:** Alternative investments can provide meaningful benefits to a traditional portfolio, particularly for investors with a long-term timeframe. These benefits include diversification, access to unique opportunities, and differentiated return patterns.

Diversification is a key advantage, as alternative investments offer exposure to businesses, properties, or loans that are not available in public markets. Private managers can actively shape companies to grow revenues or reduce expenses in ways that public market managers, who typically hold smaller stakes, cannot.

Additionally, the return patterns of alternatives often differ from those of traditional assets. For example, hedge funds can carefully reduce specific market exposures, while private equity valuations are based on expert appraisals conducted less frequently, smoothing out short-term volatility.

According to JP Morgan's analysis, a traditional portfolio consisting of 60% S&P 500 equities and 40% U.S. bonds delivered an average return of 8.8% with a volatility of 9.6% between 1990 and Q3 2024. This equates to approximately 0.92 units of return for every unit of risk. However, if an investor reallocated 10% from equities and 10% from bonds into a diversified mix of private equity, real estate, and hedge funds, the portfolio would have achieved a higher return of 9.2% with reduced volatility of 8.9% over the same period. This adjustment not only improved returns but also lowered risk, resulting in approximately 1.03 units of return for every unit of risk. This demonstrates that incorporating a 20% allocation to diversified alternatives can enhance both the performance and efficiency of a portfolio[3].

Before adding alternatives to a portfolio, it is essential for investors to understand what each investment brings to the table and how it aligns with their financial goals. For instance, a young investor with a 30-year time horizon may have the flexibility to adopt a different portfolio profile than someone who is newly retired and requires immediate income. By taking a thoughtful approach and focusing on long-term outcomes, investors can achieve greater portfolio efficiency and potentially higher returns.

## Before incorporating alternatives into a client portfolio, what should advisors consider?

**David:** As with any investment, alternative assets carry potential risks. These include lower liquidity compared to public markets, higher concentration in individual investments, and greater use of leverage, which can amplify losses if not managed carefully. Perhaps the biggest risk for individual investors is a lack of understanding about what they are buying.

Executing a successful alternative strategy, such as the Yale model, requires a long-term focus and guidance from knowledgeable advisors. Advisors should help clients evaluate their investment goals, time horizon, liquidity needs, and risk tolerance. For example, private investments are best suited for long-term holdings and may not be appropriate for clients with immediate cash flow needs.

Also, investors need to keep in mind that while liquidity features are increasingly present in the strategies that are available to wealth channel investors, they are not meant to be used as a way to be extremely tactical. It is especially important with alternatives to work with a network of experts and specialists in alternative assets that they can lean on to dig as deep as possible into the risks to increase the odds of success.

**Meric:** When considering if privates should be a part of the asset allocation, the questions are not that different from other investments. To provide a bit more detail to what David mentioned:

- **What are the Investment Goals?** Preserving capital, targeting growth, creating consistent income, or a combination of these? There are different private funds that fit with each one of these goals.
- **What is the time horizon and liquidity / cash flow needs?** This is especially important as privates do not offer the same liquidity profile as public markets. Public markets offer intraday or daily liquidity. While private investments have evolved with regards to their liquidity profiles, they still currently offer quarterly liquidity to a limit which varies by investment. It is important that these are considered as longer-term holdings.
- **What is the client's risk tolerance?** Given the liquidity profile we just talked about, private investments can be considered medium to high risk. This should be taken into account with regards to specific client profiles.
- **What are the fees involved?** Advisors should also consider fees, as private investments often involve additional costs beyond traditional management fees. It is crucial to ensure that clients fully understand the fee structure of any alternative investments of before incorporating them into their portfolios.

One question often taken for granted for public markets: How much does the client know about alternative investments? Education is a critical component when expanding advice services into the alternatives sphere.

## How can advisors introduce and discuss these strategies with clients who may be unfamiliar with alternative investments?

**Meric:** Advisors play a critical role in educating clients about alternative investments. They should start by conducting thorough research to determine whether alternatives are a good fit for their clients. Fortunately, there are many excellent educational resources available today that explain the benefits and risks of alternative investments.

Once advisors decide alternatives are a good fit for their clients, they can map out how these investments fit within a client's overall asset allocation and demonstrate how they can help achieve financial goals. Last but not least, regular reporting is essential once alternatives are introduced into a portfolio, as these investments typically have less liquidity than public markets. The good news is that private investments have evolved to offer more transparency and timely reporting, including monthly NAV updates.

At CIBC Asset Management, we are committed to supporting advisors by providing tools and insights to help them deliver the benefits of alternatives, such as enhanced returns, higher income potential, and improved risk-adjusted performance, to their clients. As advisors walk their clients through this educational journey, we intend to be the partner of choice for alternative strategies and thought leadership.

## About the authors

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## About CIBC Asset Management

At CIBC Asset Management, we believe that every customized investment solution begins with research and rigour. We specialize in a variety of investment solutions such as equities, fixed income, currency management, liability-driven investments, asset allocation, and responsible investments.

Across a spectrum of investment solutions, we commit to robust research. Dedicated sector and regional analysts focus on industry research and security-specific idea generation. Our investment professionals leverage deep and diverse expertise by sharing proprietary research across asset-class teams. By sharing insight across asset class teams, we maximize opportunities to add value to our client portfolios.

[1] Chronograph, "The Evolution of the Yale Model for Institutional Investing", February 2024.

[2] eVestment, May 2025

[3] JP Morgan, Guide to the Markets, May 2025