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TINA, or is there?

Recently, financial media outlets have been cautiously highlighting elevated asset prices, while ultimately resorting back to the familiar adage, TINA. The acronym for "There Is No Alternative" [to stocks] has increasingly become a colloquialism at the proverbial water cooler as investors continue to pile into equity markets. Bank of America recently published statistics showing the allocation of its private client base is at all-time highs of 65%. If you are worried about stock valuations, do you turn to bonds?

But an allocation shift to what has historically been a less volatile asset class like bonds may demand a second thought. Yields on government and corporate bonds are near record lows, the return on the Bloomberg US Corporate Bond Index has turned negative YTD, while the prospects for cash vehicles are deeply concerning from a real return perspective.

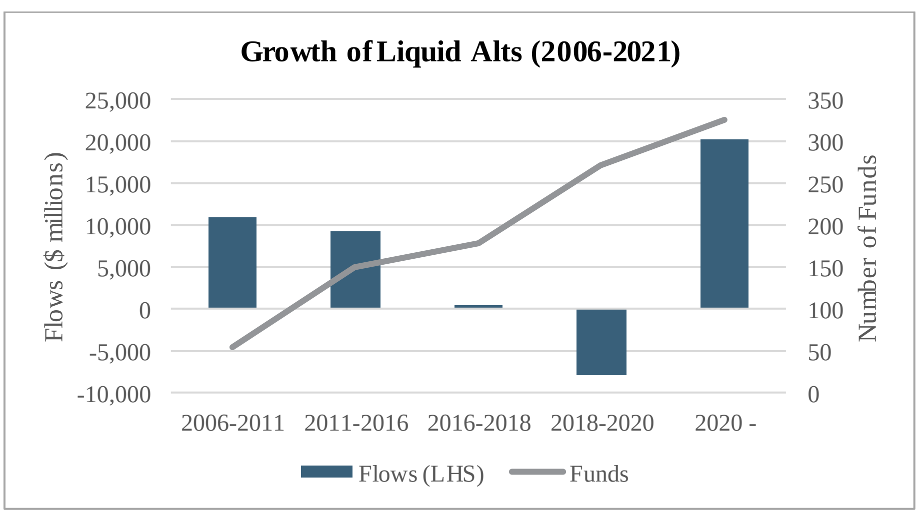
So how do you think about asset allocation in a TINA world? What might help diversify the traditional "60/40" portfolio? With an effort to avoid sounding glib, *alternatives* may be a key part of the solution. The assets have the potential to offer investors an uncorrelated return stream across market environments.

What is meant by "alternatives"?

To frame the discussion, let's demystify what has been a somewhat opaque corner of the market. Broadly, the asset class is a catch-all for investments that do not fit into narrowly defined buckets such as public equity (stocks), bonds, or cash. Everything from private equity, hedge funds, commodities, real estate, and even fine wine have called the alternatives space home. Each of these subsectors could then be divided another dozen times over.

Crucially, there is no common economic factor or cash flow stream, within alternatives, that governs the risk/return profiles of these assets collectively. Rather the unifying element is they are definitively not public equity, bonds, or cash. This renders a broad allocation to "alternatives" ambiguous in the context of achieving a specific set of portfolio goals. A deeper dive into individual assets within the category, and even subcategory, is essential.

More often than not, they have traditionally come in the form of illiquid, private vehicles, yet the last 15 years has seen dramatic growth in alternative offerings in mutual fund and ETF form. According to Morningstar the liquid alts category is approaching $150 billion in AUM with over **$20 billion in net new flows in the last year alone.**



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When does an allocation to alternatives make sense?

Should you have an allocation to hedge funds? Does that mean a macro hedge fund? Activist? Long/short? Quants? Should you hold positions in both coffee futures as well as iron ore if you seek commodity exposure? Mortgage REIT or office REIT? **It depends on your goals and how the alternative asset returns are expected to move with the rest of the portfolio.**

Alternative assets should provide a risk/return profile that cannot be replicated by long positions in stocks, bonds, or cash. They ought to behave differently than standard asset classes. In slightly more technical terms, alternatives should act as a diversifier and provide positive alpha to a portfolio – the portion of returns not attributable to broad market exposure.

This could potentially mean higher return targets relative to the S&P 500 in exchange for higher risk, as may be the case for venture capital or levered investments. On the other hand, it may encompass a return stream that is ***uncorrelated*** with stock market beta or interest rate risk associated with bonds. An uncorrelated asset should not be confused with a *negatively* correlated asset. Ideally, the former should move independently, striving for positive returns across a range of different equity environments, while the latter should generally outperform when stocks fall and underperform otherwise. Alternatives can offer each of these outcomes and almost everything in between.

Investing in the space then requires a clear and consistent approach with respect to long-term portfolio goals. It entails an understanding of where the risks are in achieving those goals and what investment **specifically** can protect against potential shortfalls. Referencing the earlier discussion, coffee and iron ore futures have maintained a low correlation to one another over the prior 5 years. How would each potentially impact your portfolio(s) differently?

Many alternatives are still highly correlated with equity markets

A common misconception is that all alternatives behave as diversifiers. Taking a look at correlations of key indices over the previous five years suggests many alternatives move closely with equity markets.

Sep 2016 – Sep 2021

	S&P 500	Bloomberg Commodity	CS Hedge Fund	S&P Private Equity	Dow Jones Real Estate	Bbg Bond Aggregate
S&P 500	1.00					
Bloomberg Commodity	**0.65**	1.00				
CS Hedge Fund	**0.83**	0.76	1.00			
S&P Private Equity	**0.90**	0.66	0.88	1.00		
Dow Jones Real Estate	**0.76**	0.57	0.72	0.82	1.00	
Bbg Bond Aggregate	0.01	-0.16	0.11	0.09	0.31	1.00

Jan 2008 – Dec 2009

	S&P 500	Bloomberg Commodity	CS Hedge Fund	S&P Private Equity	Dow Jones Real Estate	Bbg Bond Aggregate
S&P 500	1.00					
Bloomberg Commodity	**0.54**	1.00				
CS Hedge Fund	**0.70**	0.82	1.00			
S&P Private Equity	**0.91**	0.55	0.65	1.00		
Dow Jones Real Estate	**0.87**	0.37	0.52	0.85	1.00	
Bbg Bond Aggregate	0.44	0.23	0.26	0.22	0.34	1.00

This also holds true during sustained periods of economic downturn as seen in the second table encompassing the global financial crisis of ‘08-‘09. The data suggest that blanket exposure to alternative assets will likely not provide diversification, lending credence to investing carefully and intentionally in the space.

We do not believe in TINA as an answer to solving for portfolio allocation concerns. With the vast number of investment vehicles and asset classes available there is always an alternative. Rather, current market dynamics demand a deep dive into the portfolio and understanding which sector, or even subsector can aid in achieving long-term risk/return targets.

Reach out to our team to find out more at sales@corealt.com

Disclosures:

Indexes are unmanaged and one cannot invest directly in an index. Investing involves risk, including the possible loss of principal. Diversification may not protect against market loss.

Barclays Capital US Aggregate Bond Index: The Barclays Capital US Aggregate Bond Index, also known as "the BarCap Aggregate," is a broad bond index covering most U.S. traded bonds and some foreign bonds traded in the U.S. The BarCap Aggregate was once known as the Lehman Brothers Aggregate Bond Index.

S&P 500 Index: The Standard & Poor's 500, often abbreviated as the S&P 500, or just the S&P, is an American stock market index based on the market capitalizations of 500 large companies having common stock listed on the NYSE or NASDAQ. The S&P 500 index components and their weightings are determined by S&P Dow Jones Indices.

Credit Suisse Hedge Fund: The Credit Suisse Hedge Fund Index is compiled by Credit Suisse Hedge Index LLC. It is an asset-weighted hedge fund index and includes only funds, as opposed to separate accounts. The index uses the Credit Suisse Hedge Fund Database, which tracks approximately 9,000 funds and consists only of funds with a minimum of US$50 million under management, a 12-month track record, and audited financial statements. The index is calculated and rebalanced on a monthly basis, and reflects performance net of all hedge fund component performance fees and expenses.

The S&P Listed Private Equity Index comprises the leading listed private equity companies that meet specific size, liquidity, exposure, and activity requirements. The index is designed to provide tradable exposure to the leading publicly-listed companies that are active in the private equity space.

The Bloomberg Commodity Indices (BCOM) are a family of financial benchmarks designed to provide liquid and diversified exposure to physical commodities via futures contracts. The principal potential benefits of including commodities in a diversified financial portfolio include positive returns over time and low correlation with equities and fixed income. BCOM provides broad-based exposure to commodities, and no single commodity or commodity sector dominates the Index. Rather than being driven by micro-economic events affecting one commodity market or sector, the diversified commodity exposure of BCOM potentially reduces volatility in comparison with non-diversified commodity investments.

The Dow Jones Real Estate index is designed to track the performance of real estate investment trusts (REIT) and other companies that invest directly or indirectly in real estate through development, management, or ownership, including property agencies.

Correlation: a statistical measure of how two securities move in relation to one another.