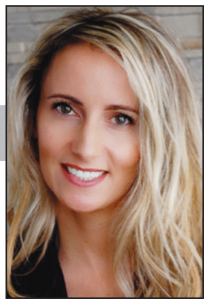
How portfolio innovation can protect your wealth

Managing Your Money



LYNN MacNEIL

It's no secret that institutional managers are the "smart money" investors that lead the trends in investment management. That's why retail investors (i.e. most people) should look to these institutional managers (money managers, pension funds, etc.) for investment guidance. The fact is, most retail investors have remained entrenched in portfolios consisting of only public market securities, while institutional investors have adapted to the changing economic and financial landscape over the past decade or two.

"Private and alternative markets now play a key role in institutional portfolios, yet retail investors aren't making the most of this trend."

In our wealth management practice, we follow a formula that was adapted from the institutional model. One of the key areas where we have implemented innovative trends from institutional management is in the private markets and alternative space. Private and alternative markets now play a key role in institutional portfolios, yet retail investors aren't making the most of this trend. Typically, they face hurdles such as limited accessibility, lack of available information and liquidity restraints, etc.

A prime example of this emerging trend is the Canada Pension Plan. Over the past 15 years, the CPP increased from just under 10% in privates and alternatives in 2006 to almost 50% today. Clearly, private and alternative investments are something institutional investors are actively adopting. Has your portfolio been adapted to embrace this innovation? Most likely not. The average retail investor is still stuck in a 60/40 portfolio (or somewhere thereabouts) – some balance between fixed income and equity. Most Canadians still have ZERO, or close to nothing in privates and alternatives.

2022 has been a crazy year in the markets. In the first 6 months, almost everything is down. I mean, everything – with few exceptions. And if you're thinking, "I'm in GICs or cash, I haven't lost anything!", don't forget: inflation is at 8%, eating away even at money that is parked "safely".

This is where the reasons to diversify into privates and alternatives become clear. They are meant to be uncorrelated to the market, reduce risk, increase return, hedge against inflation, and reduce volatility. They don't always work exactly as they are supposed to – few things do. But this first half of the year, they have provided excellent protection against the extreme volatility of the public stock and bond markets.

I'm not here to toot our own horns or to recommend any specific investment so I'll simply call them A, B, and C. These are investments that we have used successfully for years as part of our investment management formula. I'm using them only as an example of how, incorporated into an overall diversified portfolio, they have managed to preserve portfolio value during these challenging markets.

Investment A, a Canadian private equity investment, has returned 6% from January to June 2022, while the Canadian market is down -10%. It is known to have strong, uncorrelated risk-adjusted returns with a history of consistent profit distribution. In fact, it has not experienced a negative year since its inception in 2010.

Investment B is a private credit investment with performance built on a foundation of low-risk tolerance and a long history of consistent cash distributions. It's yielding 8% YTD with stable capital value while Canadian bonds are down -12%.

"Embracing innovation means refining strategies and overall portfolio construction to adapt to the changing financial landscape."

Investment C, a real asset investment which offers low correlation to equities, low volatility, and capital appreciation potential, has returned 5.6% from January to June.

Embracing innovation means refining strategies and overall portfolio construction to adapt to the changing financial landscape. Privates and alternatives are not for everyone but should be explored to evaluate if, and how, they fit into your investment strategies and overall portfolio construction. As these are more complicated investments, I encourage you to do your due diligence and read the fine print. My best advice is to work with professionals who are experienced in the area and know how to access and manage the risks.

Lynn MacNeil, F.P.L., CIM®, is an Associate Portfolio Manager and Financial Planner with Richardson Wealth Limited in Montreal, with over 27 years of experience working with retirees and pre-retirees. For a second opinion, private financial consultation, or more information on this topic or on any other investment or financial matter, please contact Lynn MacNeil at 514.981.5794 or Lynn.MacNeil@RichardsonWealth.com. Or visit our website at www.EphtimiosMacNeil.com.