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### The Need For An Institutional Approach To Alternatives

According to most investor surveys, institutional investors typically have large allocations to alternatives (e.g., 20%, 30%, 40%), while their retail counterparts continue to dip their toes in the water with low, single digit exposures. Why is this? Time horizon, access, and familiarity all play a part to be sure. But perhaps of equal, if not greater importance is that institutions have clearly defined goals, coupled with a realistic understanding of the market environment, both of which put risk management front and center.

Pension plans manage to an actuarial rate of return—an assumed interest rate used to estimate plan liabilities, and with that, funding status.

Endowments and foundations often have specific spending policies that determine how much will flow to the operating budget of an entity. In short, they know exactly what they are trying to accomplish.

In addition, most institutions are forced to acknowledge the reality of a market environment in which the bellwether asset, that is the 10-year Treasury, yields 1.78% (as of 3/31/2016). And, they recognize the limiting effect that such low yields portend

for total portfolio returns.

In contrast, most individual investors have been conditioned to think in terms of risk tolerance, separate and distinct from need. In other words, they don't know their actuarial rate of return to meet stated goals. And given that individuals have a much shorter time frame over which to invest, the sequence of returns earned is all the more important, and as such, risk management in conjunction with a clear return goal is paramount.

Rear view mirror investing is dangerous. Historical averages mean nothing as the tailwinds of the last few decades diminish. Individual investors should follow the lead of institutions and use the full 'investment' tool box at their disposal if they are going to meet goals, especially given today's challenging investment environment. Financial advisors can help spearhead this change.

The bottom line: enhanced returns and better risk management could be the rewards of more meaningful allocations to alternatives (e.g., 20%, 30%, 40%). Dipping that toe in the water will have no effect.

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