What's The Endowment Model And Why Does It Matter To You?

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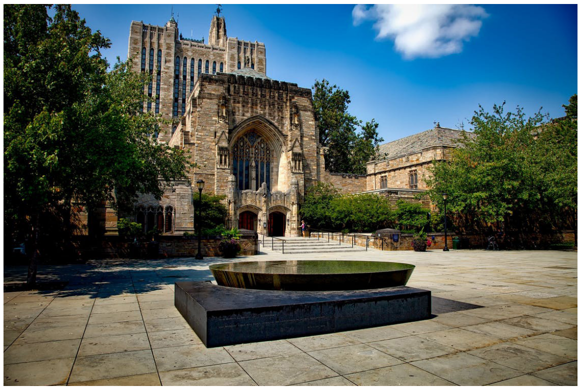

Throughout the history of the markets, large institutional investors have had a significant advantage over the little guy. This advantage has allowed some large investors to outperform by a substantial margin:

> *"For the 20-year period ending June 30, Yale's endowment earned a 12.1 percent annualized return, beating its benchmark Wilshire 5000 stock index, which gained 7.5 percent. A passive portfolio with a 60 percent stock allocation and 40 percent in bonds, meanwhile, had a 20-year return of 6.9 percent."*
> *-Institutional Investor: "We Crush Stock Indexes, Yale Claims"*

A few decades back, Yale, led by Chief Investment Officer David Swensen, created what would become known as the endowment model.

The Financial Times defines the endowment model as "allocat[ing] a significant portion of assets to non-traditional asset classes such as absolute return, private equity and real estate".

This model, with its heavy use of alternative investments such as hedge funds and private equity, has been replicated heavily throughout the institutional investment community, all with the goal of increasing investment returns while mitigating risk.

> *"Yale is not alone in producing extraordinary, market-beating results. Consider the endowment world's top ten 20-year performers. Each institution surpassed by a comfortable margin the returns of stocks, a stock/bond mix, and bonds. The high-return portfolios share a common commitment to diversification, equity orientation, and active management, employing a heavy dose of alternative assets."*
> -*2017 Yale Endowment report*

The problem with the endowment model is that, historically, alternative investments have only been available to institutions and wealthy families who commonly have over $1 million in financial assets.

Fortunately, on January 3rd, 2019, the Canadian securities regulators amended the regulations to make alternative mutual funds (and alternative ETFs), which can include hedge fund and private equity strategies, available to all investors. Some in the industry dub these strategies "liquid alternatives".

The advent of liquid alternatives had the effect of leveling the playing field between the large institutions and the average investor.

This means that much of the endowment model, long praised by leading multi-billion dollar institutional investors, will now be accessible to all investors, accredited or not, in the near future.

We can look forward to a dynamic and rapidly growing liquid alternatives market in Canada, which will ultimately result in better investment outcomes for investors.

-Julian