Episode 177: Winning the Loser's Game: A Look at Alternative Investments

Tue, May 06, 2025 3:51PM • 52:50

SUMMARY KEYWORDS
Alternative investments, retirement planning, financial personality, market volatility, private equity, hedge funds, real assets, liquidity, regulatory oversight, inflation hedge, accredited investor, fee compression, systematic strategies, portfolio diversification, investment knowledge.

SPEAKERS
Wade Pfau, Briana Corbin, Alex Murguia

Briana Corbin 00:00
The purpose of retirement style is to help you discover the retirement income plan that is right for you. The first step is to discover your retirement income personality. Start by going to risaprofile.com/style, and sign up to take the industry's first financial personality tool for retirement planning. You investing isn't about beating the market. It's about not losing to it. This week, Wade and Alex talk alternative investments, the losers game, and why your retirement plan might benefit from thinking a little differently.

Wade Pfau 00:53
Hey, everyone, welcome to retire with style. I'm Wade. I'm here with Dr Alex Murguia, and we're going to begin an arc on alternative investments.

Alex Murguia 01:03
Thank you, Dr Pfau, but

Wade Pfau 01:06
before we do get to that, I finally have played my first game of pickleball against Alex or with Alex. Actually, we're on the same team for much of it, and I didn't realize how good Alex was. But yeah, I'm no longer a neophyte when it comes to pickleball, I play it a lot like I play ping pong, which is more defensive, try to just consistently return things and wait for the other person to try to slam it and make a mistake, which can work against lower level players, but it's not gonna get me too far up the rankings I think.

Alex Murguia 01:37
Well, actually, Wade, you're saying something interesting, and not the fact that I'm a far superior player. Now you're saying something interesting, and that's, I don't know if you're familiar. You familiar with Charles Ellis, famous like investment writer,

Wade Pfau 01:51
yeah, the madness of crowds or something? No, no. He wrote winning

Alex Murguia 01:55
the losers game. Okay? And in it what he's, what I think the wisdom of the crowd is, I want to say it's James walkie. I'm going to mispronounce his name, but something like that. But Charles Ellis, he wrote winning the losers games, and he was a big time tennis guy, just to throw this in there. And so I believe the preface of his book, he's talking about how tennis and investing are similar in the sense of, in tennis, you can either go for winners, their style of folks go for winners, or some people are pushers, where you just get the ball back, get the ball back, get the ball back. And he was pointing out that, other than the high high levels, just getting the ball back is actually a fairly effective winning strategy for 99 point percent of the folks out there. Maybe it's not 99 maybe it's 97.3 but you know, that kind of thing. And I think in there, there's, and he's drawing parallels to investing, from the standpoint of, you don't have to go for the Home Run Ball, just, you know, slow and steady wins the race. And he's so he's comparing tennis to investing in the sense of just tennis, just make sure you get it over. Make sure you get it over, because most likely, the folks you're playing against, unless you're on the ATP tour, you don't have to worry about anything else, just get it over. Don't be the hero. I You see how that there's parallels to that with investing.

Wade Pfau 03:18
Yeah, a lot of people go for those home runs, and they consistently just missed the court. So yeah, and they turn it and

Alex Murguia 03:25
frankly, yeah, you just mentioned pickleball to make small talk. But really it's a great transition, because the reality is that, you know, alternative investments we're going to talk about, we're going to do a whole arc on alternative investments, right? And the reality is, you have to first ask yourself, Is this needed to, quote, unquote, win the losers game, winning the losers game. And, you know, I go back to your research, in the sense of people get too caught up with things. And the reality is, you know, the sustainable draw rates are usually just based on a standard 6040, s, p, risk free rate type of portfolio, and it kind of gets the job done. And by no means am I trying to lead the witness by saying, just do that and call it a day, or go to alternatives and call it a day kind of thing. I just want to kind of point out it's interesting how there's many ways to get this right.

Wade Pfau 04:22
And part of that would just be right. Do you even want to consider alternative investments? But yeah, even bigger first step is, can you tell us a little bit about what alternative investments actually are? Yeah, no,

Alex Murguia 04:35
we'll get to that before then, since you did talk about pickleball, and I was kind of leading to start the podcast. But not so fast. We're creating our retirement style pickleball paddles, and part of this is just, you know, in retirement, what are you gonna do? Right play pickleball hell, not even in retirement, but we wanted to, you know, kind of engage our community so you. Know, I got my kids to actually set up an entire entity to be create pickleball paddles, so we can kind of begin to promote them for us, and they'll do it for like, high schools and things like that, like branded pickleball paddles, but they're doing some for us, and we've created them. And so if you don't mind, in the show notes, we're going to have a link of two paddles that we've created,

and vote on them. And every episode, we'll do is we'll see who voted on them, you know, we'll have a time stamp for, you know, per episodes, and we'll give one away, right? But vote on which one do you prefer? And this will help us with our production quantities, if you will. So if you don't mind in the show notes, just click on the link. We'll have a picture of the paddles, you know, where you can pick which one you prefer, and we'll take it from there, and there'll be one lucky winner for a paddle. And these are legit paddle. I've gone down that rabbit hole. And so for me, these are easily based on the quant, the quality of construction, the specs and things along those lines. 180 $225 paddles and so, yeah, we won't. We're gonna use them as promotional items, frankly, but you know, pick which one you like, and we'll have a winner. And with each episode, based on the poll and paddle will be yours.

Wade Pfau 06:24
And those with good memories may recall Alex actually showed them on the previous episode with the YouTube version of the podcast. He has since lost the paddles.

Alex Murguia 06:34
Well, come on. What happened is we had a last two days ago, Wade came to DC. We had a company event for like the McLean retirement researcher and RISA. We got everyone together and flew everyone in, and we had a big company event at Tyson's pickleball paddle club. And it was awesome. It was great. We brought out the paddles there, and Wade, I know I have them because afterwards we were, I was driving Wade at the to the airport, and we stopped at a park to get some more reps in, and we had the paddles there, so they're around. I suspect my wife sort of probably saw them in the house somewhere, thrown around, and said, What is this mess? And it's, it's hidden away in some closet or something. So I did not lose them. They're they're in here

Wade Pfau 07:24
somewhere, and I think they're still in the car. You just didn't bring them in the house. No, no. I checked before the podcast.

Alex Murguia 07:29
Remember, I said, let me go see if I can find them. I didn't see them in the car, all right? And incidentally, do not leave pickleball titles in the car, especially during the summer. They'll delaminate the core, the carbon layer will most likely become unglued to the core at extreme temperature,

Wade Pfau 07:49
so turn into diamond.

Alex Murguia 07:53
Wow, yes, I got that way. Thank you. No, no, it'll turn into mush. It's inside. It's usually a probably propylene core, which is plastic, and it'll it'll just like get warped. But our paddles won't, because they're foam. They're all foam inside. So it's cutting edge wave at 121 20 density. So like I said, I went all in on this sort of pickleball paddle rabbit hole. But that's not what we're about, right? This is alternative investments.

Wade Pfau 08:28

Okay, so alternative investments, and you've really been boning up on this topic as an investments person and doing workshops with the retirement researcher Academy, so it's a great chance to also share that knowledge with a broader audience. Yeah,

Alex Murguia 08:47
that's a great point. And just to give people wait, what do you mean? We've been voting up on retirement research, or that's our membership site, where we really get into specific topics, and it's geared for a lot of do it yourself investors. That obviously, while we have McLean Asset Management as our traditional wealth management firm, we realize a lot of folks like to do it themselves and learn, and many of them are listening to the podcast. And what we've done is we've tried to create Retirement Research, or to be kind of a master class for all things retirement income planning. And in that vein, we we've been doing a series of workshops on alternative investments and it, and based on the popularity of it and the feedback we got, and Wade and I figured, you know what we should, we should do an arc on the podcast on this, because if those folks are interested in it, it stands to reason that our listeners are as well. And so what we'll do is we'll take snippets of that and present it in the podcast over the next let's say three to four episodes, if you will.

Wade Pfau 09:50
Yeah, and anything, especially at this time of market volatility, finding assets that aren't necessarily correlated with assets exposed to significant downturn. And broader diversification. What are alternatives? Yeah, justification they are, and whatever getting into here,

Alex Murguia 10:07
yeah, I'll get to that. And now with just as a caveat, warning here, if you will, by no means are we espousing, Hey, everyone, invest in alternative investments. Or hey, don't invest in alternative investments. The job that we're going to take on here is just to help you become informed consumers. At the end of day, this is not an endorsement. This is not the opposite of endorsement. It's just as best as we can lay down the facts and and for you to make informed decisions of obviously you have any questions, feel free to give us a holler, contact us, etc. But for the most part, we're just laying the groundwork here as part of, hey, this is what it's about. And Wade alternatives. It goes back to what we were talking about the beginning of the podcast, winning the losers game. And there are many ways to kind of get this right, and I've used this before, but think about when you're bringing in asset classes to a portfolio, you have certain primary colors, and at the end of the day, you're shooting for a color, you know, a combined color, and you make that with primary colors like yellow and blue, make green, that kind of thing. And so whatever the green is for you, it's, it's preference, it's whatever style you like. That being the case, alternatives can be one of the could potentially be one of the primary colors. You may not need it to get to the color you need at the end of the day. So by no means, just because we're presenting this is that, hey, let's get this, because there's so many things to invest in, right? And if you decide to invest in everything because they're quote, unquote investable, you may end up with a portfolio that's just muddy at the end of the day. So the caveat is, this is just from an informed standpoint, because we have a lot of we come across a lot of prospects that come to us, and when we look at their statements, they have alternatives, and a lot of them don't know what role that they play in the portfolio, what it even is and the like, because it's this broad statement of alternatives. And that's, that's where things get tricky, in the sense of, there's a broad statement of mutual funds. There's many types of mutual funds. Some are conservative, some are aggressive. Broad statement of ETFs, right? And so to some extent,

alternatives, I view them in those lights, especially when you hear the word hedge funds or private equity and things like that. What is that? What's the underlying subcategories of those? And that's what we'll be getting into in this series. But the beginning with alternatives, Wade is really an alternative to stocks and bonds is what they're getting at. And so, as you can imagine, that's a pretty broad universe to do. And so the definition of alternative is meant to be more of an anti definition of what it's not right now. And so alternatives are considered what aren't stocks or bonds. It's kind of the way that it's being used right now, in the in the nomenclature. But, wow, Wade, that's amazing. That must be really loud because, yeah, picked up on the microphone. When, when, when, when you say you're having yard work done and stuff like that. You don't even notice. So, yeah, that's amazing. Be careful. Effectively. You know, over the last 20 years or so, there's been a huge sort of interest in this, in this. And you know, it all starts with institutions, endowments, and then it begins to trickle down and trickle down. And we're at that point that it's really starting to trickle down to, let's say, the most common denominator investors, not there yet. There's certain vehicles that sort of present the opportunity to do that, which we'll get into. But you know, alternatives is what's not it's considered right now, the definite, the quick and dirty definition, is really anything that's not a stock or bond that you can quote, unquote, invest in right now, it's a broad brush, because that can include private equity. And under private equity, there's, you know, a subcategory of what those are, private credit underlying that, there's subcategories of what those are, hedge funds under that, subcategories of what those are, and real assets under that subcategory of what those are. And so, for the

Wade Pfau 14:24
clarify too, this is usually a term used more in the accumulation world. So in retirement income, you might think of annuities as alternative investments, but that's not really what we're Yeah.

Alex Murguia 14:35
That's a great point here where, yeah, because an annuity is ultimately a private contract, right? And so and it behaves differently in stocks and bonds, from, uh, from a return standpoint, well, it's not even a stock or bond from return, it's really an insurance product, but it behaves differently. So yes, Wade, you're right, but that's not how we're we're using it, right? Whole

Wade Pfau 14:56
separate hearts on Yeah, we've had many arcs on that one, right? Part of today's alternative investments conversation. Thank

Alex Murguia 15:03
you. And yeah, historically, they've only been accessible to institutions because there haven't been interlocutors to sort of provide access. And the reality is, someone with 50 grand wanted, wanting to put it to work in private equity 20 years ago, you know, those calls wouldn't be returned, whereas an institution with 50 million looking to put to work, those calls will be returned and they'll have a dinner and etc. But the reality is, new structures are allowing more and more individual investors to participate.

Briana Corbin 15:35
Let's take a moment to let the audience know that this show is sponsored by retirement researcher. You can learn more about retirement researcher at retirement researcher.com and subscribe to our newsletter, where You'll receive weekly actionable information for your

retirement planning benefit. Retirement researcher is an online community devoted to helping you create the retirement income plan geared towards your goals.

Wade Pfau 15:59
And why might they want to do that?

Alex Murguia 16:02
Well, it's very cool thing to say at parties, to be able to say, I have alternatives. You know, when someone's talking about the S, p5, 100 index and how they just leave it there and forget about it, to be able to say, I also have private equity. That's a flex move. No, they do it simply because, I mean, the I'm going to discuss why they do it. I'm not going to say that that's a correct assumption, and that's not a correct assumption, etc, but the answers that you will see, and frankly, if you have an advisor, they're going to pitch you on this, this is, these are the buzzwords that you'll hear, and that there's a potential for higher returns. There's enhanced diversification benefits. It has the ability to potentially hedge against inflation and market volatility. You know, they at the end of the day, alternatives provide this opportunity to enhance returns while reducing the overall portfolio risk through diversification. That's kind of a nice way of putting all those bullet points together into one sentence. Whether it does or not, it's subject to the person doing the analysis, if you will. But that is the thesis of, why would you seek alternative investments now? Why does it reduce the overall portfolio risk, etc? And these are things we'll get into throughout the arc, but you'll get statements like they have a lower correlation to the public markets, meaning they may perform well. You know, when traditional stocks and bonds are struggling, like, you know, perhaps this past month, if you will. Now there's many counters to that, such as, they're not priced every day, and so you there's a lag, etc, etc. But that's not right now, this is more the setup of what you're hearing. Everything that I say that will be counters to that we'll go over, but I'm giving you the thought process behind it. The other piece on the inflation side, they'll say, you know, many alternatives, like real assets. What they do? Real Assets being commodities, real estate, infrastructure, and by real estate, it could be residential, but it could also be like forestry. Things along those lines, they'll say they provide a hedge against inflation. And in today's economy, that's kind of a relevant pitch. So think about it. What's happening right now? Markets are extremely volatile. If someone is presenting you, hey, you know what? There's nothing I can do about stocks going down when they're going down at this level, or even up, because we've just as of this recording, I think the the markets have been up eight days in a row, something like that, something that hasn't happened since, like the year 2020, something crazy like that, right? But they'll say you need something that doesn't correlate, that acts independent of whatever the stocks or bonds are doing. Right? You can check that box of a story being told right now. You can also check the box that, hey, you need an inflation hedge. Look at Gold going gangbusters right now, right? That's an inflation hedge. That's a hard commodity, but you can see someone saying that with real estate as well, and so that's, that's the storyline, why folks would seek alternatives, frankly, higher returns, diversification benefits and the hedge against inflation. And I know I said it earlier kiddingly, but there is some truth to be able to say, Hey, I'm behind a velvet robe, and I have access to this, and you can't, it's just almost a human nature thing where, I mean, Daniel Crosby said it, and I was making fun of him about the hedonic treadmill, you know, keeping up with the Joneses, where you kind of always want that. And in, although we may not admit it, you know, outright, in your heart of hearts. I think many people just like the fact that, hey, I get something that you don't. So look at me. I'm more sophisticated than you. As stupid as that sounds, Wade, I think there's, there's, there's an echo of truth in that. Am I off on that?

Wade Pfau 19:52
Yeah, the whole idea of conspicuous consumption, the hedonic treadmill, may not apply. That's more once you. To improve your lifestyle, it's hard to go backwards again. So then

Alex Murguia 20:03
I got it wrong. I thought that was like keeping up with the Joneses kind of thing. Like, always need to more. Always need more. You know,

Wade Pfau 20:11
once you get an uptick in lifestyle, then you have to keep getting more upticks, because the great opportunity you had with this higher lifestyle, it quickly dissipates, so you gotta keep getting then

Alex Murguia 20:25
thank you. Wave, always adding value, consumption and so I mentioned it earlier. The core categories are things like private equity, private credit, hedge funds, real assets now under private equity, and these are things that we will really drill down on.

Wade Pfau 20:47
Before you mention that you have not mentioned cryptocurrencies, is that not part? Oh

Alex Murguia 20:52
yeah, there is. But I that's new, and I think we'll give it its own treatment, frankly, at a certain point, because it's just so hot right now, but, yeah, I would say cryptocurrency could be considered that, especially with regards to Bitcoin, which is seen as an alternative to, like, let's say gold, or, you know, safety, but you know, when you talk about Ethereum, and let's say ripple and things like that, I It's almost like technology plays, with regards to new innovations, where, like, ripples trying to take over Swift, right, the Swift way of wiring money, you know, things like that. I think it's a little different in the sense of, yes, it's not like a stock or bond, but is it quasi like us, like it's every coin, like its own little ecosystem of a stock, you know, kind of thing, and so I want to give that its own treatment later on. But yeah, I mean, the main ones are, like I said, private equity, private credit, hedge funds, real assets. You're right. Crypto is one, but I don't want to bunch it into right here, because it's almost its own beast right now, in and of itself. And like under private equity, you're talking there venture capital, growth equity buyouts under private credit, there you could be talking about direct lending, mezzanine finance, distressed debt. Under hedge funds, you have a lot of types of hedge funds that could be long, short, hedge funds, global macro, hedge funds, event driven, hedge funds, market neutral hedge funds, managed futures, hedge funds, which could be a cousin of real assets, except managed futures, hedge funds, are largely trend following strategies. It's just commodities have so much volatility that it's kind of a nice play to use them real assets that, to me, is actual real estate. Real estate is commercial real estate, residential real estate, etc. Infrastructure plays, if you like, data centers, you know, prisons, you know, things like that. Commodities, there you have the standard hard metals and the like. But I you know, expand, amplify what that could be when you're talking about farmland, when you're talking about timber, when you're talking about things along those lines and so. So all of those, to me, are nice, sort of ultra a nice alternative bucket, if you will. Okay,

Wade Pfau 23:14
could you talk a little about the history in terms of how we're seeing this trend increasingly, where household investors may have opportunities in this space that historically may not really have existed.

Alex Murguia 23:27
Yeah. I mean, I think this is the way things go naturally. It's like that phrase, The future's here. It's just not evenly distributed, if you will. And dating back to, let's say, 20 plus years. This was, you know, endowment started really in, you know, before then. But let's just say, for argument's sake, endowments really started getting all in on it. I would say the person that really brought this to the forefront, to the No, you know, to the everyday investors, in the sense of what, what's going on here? What are they doing? How are they doing it? Why are they doing it? Would be David Swensen. He passed away a few years ago, but he was an innovator in terms of just managing endowments, and he did it for Yale, and he was sort of the Warren Buffett, if you will, of endowment investing. And they structured their endowment to be heavily, heavily weighted to private equity hedge funds, real assets leading to far superior returns than the standard 6040, portfolio. Now you have to understand that's an endowment that's multiple billion dollars. They go directly to the venture capital firms in Palo Alto. They go directly to private equity funds. You know they don't, you know they don't, kind of have an intermediary to, you know, to have access to these things. That's something that you and I wouldn't be privy to. So but it started like that, if you will, with the institutional money, really putting their, their ass, their their their their money to work, if you will. You. And had had great success. And, you know, genius deals, right? And so folks started saying, hey, how do we get in on that? How do we get in that? And then, whenever there's a market for something, whenever there's a demand for something, people figure out a way to facilitate those, you know, the participation in those. And so that's really how it starts. Years go by. It ebbs and flows, and we are where we are now, with regards to, you know, from top down, the institutional folks, the ultra high net worth, family office folks, the high net worth folks and the like. Now it's still a high net worth thing, but with technology, there's many, there's many ways to facilitate the ability to invest in many of these vehicles, just through standard interval funds or ETFs and things like that, that we'll get into as we progress.

Wade Pfau 25:55
And maybe while we're on the same topic, there's this idea of being an accredited investor, to have access to these types of opportunities. Could you talk a little bit about that? And yeah,

Alex Murguia 26:07
no, no, that's a good point. Who qualifies for certain alternatives? Because this is the other piece. Like, you can't just pick up the phone and say, Okay, I'm in, or go log into your Charles Schwab account and say, Hey, you're in, right? And so from that standpoint, an accredited investor. You know who qualifies for alternatives institutional investors. Obviously, these includes pension funds, insurance companies, banks, university endowments, sovereign wealth funds, you know, if you're not one of those, you know, I wouldn't call yourself an institutional investor, a credit investor, high net worth individuals who meet certain criterias of net worth and annual income requirements. I'll go over that in a second. And you know, in addition to that, you can be an accredited investor if you have qualifying investment knowledge based on your profession. So let's say I don't meet any of the quote, unquote criteria to be an accredited investor from a income standpoint, from a net worth standpoint, or whatever, being that I'm in the business and we're running McLean asset management and the like, I would consider

myself to be, you know, a qualifying to have qualifying investment knowledge based On that, based on my profession, and so would somebody you know that's looking for an investment. The other one are qualified purchasers. Or these are defined as individuals that you know that have 5 million or more in investments, or entities with 25 million or more. Those are the sort of hurdles. Now, what's an accredited investor, if you will? Again, this is important, and to me, an accredited investor, someone you qualify if you meet the following wealth and investment criteria, knowledge wealth, you need to have a liquid net worth. I mean just a net worth of a million dollars or more that exclude the value of your primary residence, you know, individual, individually or jointly with your spouse, right? So you need a million or more in assets, not counting your house income. Individuals with an income of 200,000 or more for the past two years with the expectation that that's something that's going to continue going forward, if you have a spouse, the watermark is 300,000

Wade Pfau 28:23
right? And this is an either or. You don't need both income.

Alex Murguia 28:29
Investment knowledge. If you listen to this podcast, you're in good shape. Just kidding. Just kidding. Wade, that was a late reaction. No investment knowledge. These are investment professionals. If you don't meet the above, could you still be accredited? Well, if you're an investment professional, you can, but you have to show that you have something that says that you have knowledge. And so that would include some sort of licensing that you have, such as the series seven, series 65 I believe the next one is series 82 something like that, or persons affiliated with the fund, including employees, directors, officers or general partners. So if you're there, you're in good shape. But again, why? You know, I want to stress enough, why would you even do this? Again, it's because low correlation to public markets potential for higher risk adjusted return, and understanding that the risk return, piece of it has to do with liquidity, trade offs that you're making, and that goes back to, you know, the why they want to accredit investors, because you don't want to buy, you don't want to purchase something or participate in something. Then three months later, say, oh, I need the money because I don't know my roof caved in and I don't have any other assets to pay from it. You may be stuck in a lock up period, and then you'll say, Oh, I didn't know that. And so it becomes one of these things that, were you savvy enough to know what you were doing before you got in it? And that's how they assess you being a credit investor. There. And that also avoids you can imagine, there's good and bad in everything, and you have enough of a sample size, you have a normal distribution on morality. And the reality is that some people will take advantage of others simply because they don't know what they're doing under the auspices of, ooh, they want alternative investments. Let's sell them this. You know, they'll be happy to buy it, you know, that kind of thing. And so in its wisdom, the SEC feels that a credit investor status is the way to kind of, you know, have some sort of level of checks and balances.

Wade Pfau 30:36
So does that just generally mean these aren't available in brokerage accounts, like if I log into whichever big brokerage I may be using, there's no you can.

Alex Murguia 30:45
There's certain types in everyone, like, like Schwab, for instance, even though I said that the minimalist here for credit investors is a million dollars, I want to say Schwab is significantly

higher than that. Like, if you just log into your Schwab institutional account or whatever. And you look for alternative investments. First, you have applications that you have to sign, like similar like, if you wanted an options, if you wanted to do options, or a margin account, things like that, there's an extra step that you would need to have access to it. And I believe their watermark is much higher than a million dollars. I would put it in the three to $4 million range, I think, but I'm doing that from memory. It's higher on an order of magnitude, more than just the basic million dollars of net worth. But you can, you could potentially do it, not probably every type of alternative that's out there. You know, I'm not so sure everyone's doing crypto right now, but you can do that. I'm sure hedge fund strategies are available. I'm sure certain private equity strategies are available that you can get direct through schwa. But again, there are higher minimums, if you will, than what's considered accredited investors. Why do they do that? It's a hassle, logistically and administratively to process all of that, and for them, they're like, you know, someone in there, in all their wisdom, decided it's probably not worth the compliance risk to make these very readily available to everyone. That would be like my no frills answer.

Wade Pfau 32:13
So then on that sort of theme, like, what sort of myths or misconceptions are there about alternatives? Well,

Alex Murguia 32:21
I think people, I think it's about risk adjusted returns, and people throw out, and this is my hat on that there is value to consider this, and there is value to look into it and do due diligence. It's not like baseball cards and you're like, Ah, forget that. You know? I mean, I mean, a lot of people just say alternatives are too risky. Alternatives is such a broad term as I said, it's everything that's not stock or bonds, and there's many alternatives that are actually quite more tame than investing in stocks, maybe not all types of bonds, because, you know, three month t bill is hard to beat from a risk standpoint, but when you consider risk adjusted return, which is how you should be looking at it, then things change, right? So just a broad brush strokes alternative to risky. I think that's mentally lazy. I think you really have to look at it from a wider frame, and that wider frame is risk adjusted returns. Because I think alternatives run the gamut of being quite risky to some being very conservative. The other one is, oh, it's only for institutional investors. Yeah, I think that was practically the case even up to five years ago. But the reality is, is that there's, you know, with technologies. Technology is a great thing because it really begins to democratize accessibility to certain items, right? The information asymmetry becomes less or less. That becomes less and less markets. You know, demand develops for certain types of things. If demand is there, people all of a sudden get creative and innovative and how they can facilitate that matchmaking process of matching a buyer to a seller, if you will. And so that process is ongoing right now, and you're seeing that, you know, through the increase in retail access. I mean, there's a couple of there's a couple of behind the scenes firms that are worth billions of dollars right now, like C, I c, a, I S and the like, in which they're actually making for advisors, these platforms so that they could offer to their clients, you know, alternative investments. And you know, they're white labeled by large brokerage houses doing that. But even registered investment advisors like myself, like ourselves, can do that. Just because you can do it doesn't mean you should. I'm just sort of providing the misconceptions, such as they're too risky, that's a not so fast kind of statement, only for institutional investors. That's becoming significantly less and less, not more and more and high fees. Is another misconception, not misconception. I would just call it conception, because I would say that's probably was an accurate concept. Perception few years ago, where hedge funds are charging 2% and 20% of

the profits in addition for what you know kind of thing. And so you're seeing again, markets work. When there's increased demand, there's actually more players trying to provide that service. When there's more players trying to provide that service, there's there's fee compression, if you will. Now you can make the case that there's another trend happening, where people are identifying, especially with hedge funds, that it's not really this manager skill. What they're what they're doing is, is really finding premiums in the market that are available for the taking, and if you can develop systematic strategies, systematic being, that's code for kind of indexing, if you can develop indexing, robotic trading strategies to what this manager was doing, and capture systematically that quote, unquote premium, then why you we don't need to charge that much, and we can replicate it. So you're seeing that a lot, and a lot of players coming in, which I think that's a good thing, replicating strategies. And alpha becomes, quote, unquote beta, if you will. And that's that's the trend that you're seeing. And with that, you're naturally going to see fee compression in the same way that actively managed mutual funds, you know, are anchoring down simply because a mutual, an active, managed, future mutual fund, charging you 1.5 is not going to compare with an ETF that's charging you five seven bibs, you know, and that's point oh, five, you know, point five of a percent, as opposed to 1.5 so you're Seeing this huge, this huge trend in a manner that's creating a nice sort of on ramp for individuals. And again, just because there's an on ramp form doesn't mean they should do it. I'm just saying that the time is getting there where all these sort of conceptions that you had previously, such as they're too risky, they're only for institutional investors, or that the fees are just egregious. I think it's time to reconsider those assumptions in a major way.

Briana Corbin 37:10
Are you getting close to or are you in retirement? Well, investing during retirement is a little bit different than during your working years. Your investments are there to help you pay for retirement, and now is when they need to earn their keep to make sure you're on the right track. Download retirement researchers, eight tips to becoming a retirement income investor by heading over to retirement. Researcher.com/eight tips again. Get your copy of retirement researchers, eight tips to becoming a retirement income investor by going to retirement researcher.com/eight tips. That's the number eight tips.

Wade Pfau 37:50
So now and then, as part of that, like there are now mutual funds and ETFs that replicate some of these strategies that traditionally might have only been available through hedge funds. So that's also making it more widely available, but you do still need to meet that accredited investor definition absolutely

Alex Murguia 38:08
now, now, but some ETFs, you know, begin to there's some funds that are out there that you can just pick up as an ETF, but they wouldn't be, you know, that's a different game. There wouldn't no longer be these, like, I'm a partner with, you know, within some sort of private equity Apollo fund, number three, you know, kind of thing, it would be more you're going to have access to an interval fund, an ETF and stuff like that, that begins to replicate these. Then the accredited stuff is more relaxed, but there's still structural considerations you need to consider and what you really want to look at, and I think this is actually one of the most important ones. It's just liquidity versus illiquidity of what you're getting. Because these are private funds. Again, they're no longer they're no longer like daily liquid sort of ETF mutual funds, although there are some alternatives that are getting there that we'll go over, but for the most part, you want to

consider liquidity versus illiquidity. I'll give you an example I had. We picked up a client a few months ago, high high net worth, and the percent that came from one of those large brokerage companies and the percent that this person had in, like, a private equity participation was de minimis. I mean, like, not even 1% of his portfolio, right? And he transferred that's assets over to us. And he couldn't transfer the alternative piece because of the way it was set up, and he couldn't, like liquidate it either, because of the way it was set up and the like, he has to wait three more years, right? And so the reality is, is this is an insignificant part of the portfolio will not, will not really move the needle in any way, shape or form, and it's 80% of the nuisance of the portfolio. It, you know, it's like the 8020 rule the other way around, of what you don't want, right? The how you spell Pareto backwards, you know, how you need, like, a, is it a palindrome? No, no. Whatever it is, you know, it's what Palindrome is when the same is, like radar or something like that, words and backwards, yeah. And so it's just one of those weird things that it's a headache. And so you really want to look at liquidity versus illiquidity, simply because sometimes it's just not worth the aggravation, right? And And with that, liquidity comes like, are you locked in for future? You know, do you have to give more commitments? You know, over time? What happens if you don't do that? And this goes back to your initial point. Are you in the accumulation or distribution? Right? If you're in the distribution phase, I would give significantly more weighting towards liquidity than illiquidity. If you're in the accumulation phase, you can be a little more relaxed on that. But still, it's one of those things, regulatory oversight. This is important because some folks, you know anyone, is that, you know, if you're going to invest in this, most likely there's some sort of subscription document and the like, and there's, you know, quasi oversight, but the reality is not really, and so do you want, you want to make sure that there's some regulatory oversight around this. I mean, some of these funds aren't audited, you know, some of these funds aren't, aren't priced on a daily basis, and so you want to make sure that there's oversight in them, simply because you don't need the aggravation. I'm going under the assumption that you know the main crux of your portfolio are going to be stocks and bonds, and this is sort of complementary pieces. And so if it's going to be a complimentary piece, you want to make damn sure that there's that there's oversight to this, because if not, it's just not even worth the aggravation at all. At that point, access and minimums is another structural consideration when you're trying to create a portfolio, and you want to know what, how much of the allocation to put in this and that, what are their minimums? Because you may identify this great alternative, but at the minimum is $5 million as a commitment, and your entire portfolio is $6 million well, I think you have your answer in terms of where you're going with that. And so you want to give those structural considerations a strong play in that. And the only piece here is many people will say liquidity, and liquidity is very important, because not only is it a basic structural consideration, but it's potentially one of the sources of returns. And what I mean by that is there could be a liquidity premium. You know, if you're locking your money up for five years in this special interest fund, one of the reasons that you should be expecting a higher return is because you're committing capital for five years, you're not pulling that out in any particular time. And that could have a competitive advantage for that fund over others with regards to what they're investing in, how they're investing in, the way the fund is vintage doubt, etc.

Wade Pfau 42:59
Okay, so as we wrap up today's episode, why now? Why are alternative investments really something that, if you've never thought about before, you might want to at least pay more attention to at the present?

Alex Murguia 43:14
Yeah, look, I mean, you do this when you're doing your expectations for withdrawal rates. What's the market premium expected to be? You know, it's most likely. What you hear is it should be less, not more, over the next like economic cycles in plural. And so, you know, as investors, you know you're always looking for, where are their rates of return that I'm not accessing, frankly, that's what, that's what we ask ourselves all the time. That doesn't mean we do everything. In fact, we don't, but doesn't mean that you don't always ask yourself that and assess the landscape and the light, right? And so, you know, the market dynamic, you know, is the risk? Is the market risk premium going to be the same or the next 30 years? And it was over the last past 30 years, probably not. And so you want to make sure that you're positioned to be able to capture, you know, returns where they are. I mean, you don't see this internationally, but domestically, there hasn't been much of a small cap premium at all, you know, over the last investment cycle or so. Some people attribute that to private equity. You know companies don't need to go public as quickly. And because of private equity, you have act, you know they can provide funding for these smaller companies for a significantly longer period of time that can have them stall going public, right? And so maybe private equity is a way to have access to this premium. You know that you did, that you could have gotten in a regular markets previously. Again, I'm just speaking in generalities right now, because someone can come back to me and say, well, the size premium has existed. It has existed internationally just fine over the last few years. But maybe that structure there, from a private equity standpoint, is different from the structure here, etc. The larger point being that there's, you know. If there's lower expected returns in the public markets, then it's at least our job as an investment firm to scour the universe right. No matter what inflationary concerns, we're still even though inflation has been trending downward since COVID, we're still at a higher high than we were before, and so it behooves us to look into alternatives from an inflation hedging standpoint. Now it's not just simply gold. In fact, I'm not a gold bug by any means, but real estate, residential real estate, timber. There's other areas that maybe provide a better hedge, if you will. And frankly, technological innovations are making things much easier to do. Like I said, if you can begin to turn alpha into beta by systematizing trading strategies and, you know, providing then liquid access to investors, then it becomes very interesting, you know, from that vantage point, because you know what I invest in, every single alternative that's out there. No but are there some that actually capture my attention? As, hey, this is interesting. We should really look at this in a serious manner Absolutely. Now that would be a mute point if there was no way for our underlying investors to access that in a manner that we deem meets the criteria of liquidity and illiquidity, because I think that's that's quite important, that in a manner that meets the criteria for regulatory oversight. That's quite important. But the moment you create ETFs and liquid assets, guess what those things are under FINRA or the SEC, you know, I mean, they're under regulatory bodies. And so from that standpoint, that gives me great, you know, relief from that standpoint. And then the minimums are just, you know, going down from that standpoint, because of the corollary that, you know, they're they're making them tradable. They're making them more liquid. They're making them XYZ. When you do that, it just stands to reason that pricing does go down. And so to me, those are, those are, those are very interesting reasons of quote, unquote, why now you seen this growth of alternative investments?

Wade Pfau 47:10
Okay, so that's the introduction to the arc. We'll be going into more depth on the different private equity and and so forth. And upcoming episodes, before we wrap up today. We do have a listener question. Try to keep the habit of continuing with that. And so Alex Vicki writes in, I do

not have 40 credits needed to be eligible for Social Security, but my husband does. I just want to make sure that I understand correctly that the spousal benefit entitles me to receive 50% of his social security benefits. If I file before he does, we're the same age, born one month apart, and yes, from the basic level of you do not need the 40 credits to qualify for a spousal benefit. So yes, generally speaking, you are entitled to 50%

Alex Murguia 47:57
just for the interest. Because people are listening. Can you define 40 credits?

Wade Pfau 48:03
You the credits are that that's for a quarter. You, during each of the four quarters of a year, you earn enough, which it's like, in the range of a couple $1,000 per quarter to qualify for credits. And so you basically need to have 10 years of Social Security covered earnings above a fairly minimal type level of a few $1,000 a year to achieve 40 credits to be eligible for your own worker benefit. So you do need the 40 credits to be eligible for a worker benefit, but if your spouse qualifies, you can receive spousal and survivor benefits without necessarily being eligible for your own worker benefit.

Alex Murguia 48:44
So I obviously knew that Wade. I didn't ask for me. I asked for our listening audience, not for me. I knew that Wade. Just to reiterate, okay, I just want to reiterate. I knew that one

Wade Pfau 48:57
well. The point is, though there are some, so generally speaking, you're eligible to 50% of your spouse's benefit. But there could be exceptions to that. A couple things is just based on claiming ages. Now with in this case, they're both about the same age, that makes things a bit simpler. But if you're claiming before your full retirement age, there's reduction factors based on the full the full retirement age primary insurance amount of your husband in this case, so And also, if your husband claimed early, he would have a reduction. And so when you and the reduction factors are different for spousal and worker benefit. So it might not line up to be precisely 50% in that scenario. And the other direction, if your husband delays past full retirement age, he'll get a higher benefit, but the spousal benefit is 50% of the primary insurance amount, so it does not get delay credits. You don't get any delay credits for waiting past your full retirement age, and you don't get any kind of quasi delay. Credits from your spouse waiting past full retirement age. Now that the benefit of that spouse delaying, though, would be the survivor benefit would be higher, potentially someday, it's just a spousal benefit is not is linked to the full retirement age benefit. So that could be another possible reason why your spousal benefit isn't quite 50% of the husband's benefit. And again, that's because if he delayed pass full retirement age, and the other thing is just their family maximums. So if your husband has other claimants on or other dependents on their benefit, maybe you still have minor children, maybe you're caring for parents who are eligible for dependent benefits, then you could hit that family maximum, and that could then reduce everyone's benefit to keep everyone under the family maximum. And so that could be another possible reason you're receiving less than 50% and then if you're working, there's the earnings test before full retirement age that could lead you to not receive after the earnings test, 50% of the benefit. But all that aside, yes, the general answer is, you do not need 40 credits to receive a spousal benefit. And yes, at a very general level, spousal benefits are 50% of the workers benefit. So Thanks for writing in, Vicky.

Alex Murguia 51:20
Thank you, Vicki, don't forget to check out the link. Vote on the panel.

Wade Pfau 51:26
Yeah, check out that pickleball paddel link, and thanks everyone for listening, and we'll catch you next time on retire with style. Bye. Now.

Briana Corbin 51:35
Wade and Alex are both principals of McLean Asset Management and retirement researcher. Both are SEC registered investment advisors located in Tysons, Virginia. The opinions expressed in this program are for general, informational and educational purposes only, and are not intended to provide specific advice or recommendations for any individual or on any specific securities to determine which investments may be appropriate for you. Consult your financial advisor, all investing comes with the risk, including Risk of loss past performance does not guarantee future results. You