



Liquidity

Private Credit, Alternatives, and Liquidity Trade-off

Beyond public stocks and bonds, more investment activity is taking place in less familiar areas of the market, including private credit and other alternative investments. Private credit broadly refers to lending outside the traditional banking system, often by asset managers and institutional investors to middle-market companies, real estate projects, or specialized borrowers.

This market has grown as regulatory changes, bank balance sheet constraints, and investor demand for yield have pushed more lending into private markets. For individual investors, private credit and alternatives may offer income and diversification, but involves risks including illiquidity, fees, and valuation uncertainty.

But they also involve meaningful trade-offs, including limited liquidity, less transparency, higher fees, and added complexity.

Private credit strategies generally seek to earn a premium over traditional bonds in exchange for less liquid and sometimes more complex loans. Because these loans are not traded on public exchanges, they are usually valued less often. Their prices also do not move daily the way public bond prices do. This can make private credit appear steadier on paper, even when the underlying risks remain real. Those risks may include weaker borrower credit quality, default, valuation uncertainty, and changing economic conditions.

The illiquidity investors accept can help borrowers obtain more customized financing and may give lenders additional yield.

But it also means investors may not be able to access their money quickly if their circumstances change.

For financial advisors, the private credit conversation should begin with suitability. These strategies may be appropriate only for investors who can tolerate limited liquidity, understand the risks, and have a long enough time horizon. Many offerings restrict when and how often investors can redeem shares. Some also include minimum holding periods, redemption limits, or gates that may restrict withdrawals during periods of market stress.

Advisors should help clients determine whether they can commit capital for several years without needing access to it. They should also assess whether the potential added yield is worth the trade-off compared with higher-quality public bonds, cash, or other liquid investments.

Risk assessment is also essential. Private credit portfolios may include loans to borrowers with higher leverage, smaller scale, or more specialized business models than those found in traditional bond indexes. These features can create opportunities for skilled managers, but they can also increase losses if credit conditions weaken. In an economic slowdown or credit downturn, default rates may rise, and recovery values may be uncertain. Because private loans do not trade often, recognizing and pricing these changes can be slower and more subjective than in public markets.

Transparency is often more limited in private strategies than in public funds. Investors may receive less frequent or less detailed information about

specific holdings. Valuations may also rely on manager estimates that are reviewed periodically rather than tested continuously in the market.

This does not necessarily mean the assets are mispriced or that the manager has acted improperly. But it does require greater trust in the manager's process, controls, and alignment with investors.

Due diligence matters. Advisors should review the manager's track record, underwriting standards, borrower and sector diversification, valuation process, fee structure, use of leverage, and performance during prior periods of stress.

The broader category of alternative investments includes private equity, real assets, hedge funds, and other nontraditional strategies. These investments may provide different sources of return and, in some cases, lower correlation to traditional stock and bond markets. They may also offer exposure to inflation-sensitive assets, specialized strategies, or opportunities that are not available in public markets.

Still, alternatives often involve higher fees, complex structures, limited liquidity, and unique tax or reporting considerations. Understanding how each strategy fits within a broader portfolio is more important than chasing a recent vintage, headline return, or popular market theme.

Investors considering private credit or alternatives should take a structured approach. First, define the role the investment is expected to play, such as income, diversification, inflation sensitivity, or opportunistic growth. Second, decide how much of the overall portfolio can reasonably be committed to less liquid strategies, recognizing that emergencies, life changes, and market shocks can occur without warning.

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Third, work with an advisor to evaluate specific options, with attention to manager quality, strategy design, risk controls, liquidity terms, valuation practices, and fees. In many cases, alternatives may be better suited as a modest satellite allocation around a core portfolio of liquid, transparent holdings.

Investors should also consider the psychological side of illiquid investments. Because private credit and other alternatives do not trade daily, they may reduce the temptation to react to short-term price swings. That can be helpful. But the absence of daily pricing can also create a false sense of stability. Risk does not disappear simply because it is not marked to market every day.

Clear communication about expected return patterns, liquidity limits, valuation practices, and access to capital can help reduce surprises if a strategy experiences stress or restricts withdrawals.

Private credit and alternatives can be useful tools when they are used thoughtfully and in the right proportion. They should not replace a well-diversified portfolio of traditional assets. Instead, they may serve as complements for investors who understand and can accept the trade-offs. By evaluating these investments through the lens of overall financial planning, investors can better decide whether private strategies support their long-term goals.