










# The Impact of Valuations on Asset Class Performance

January 2025

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After analyzing the impact of the macroeconomic environment on the relative performance of alternative asset classes, we now turn to asset valuations and explore what they, too, can reveal.

**In this paper, we categorize valuation levels across various asset classes and seek to use historical performance to analyze the relationship between asset valuations and the timing of certain investments.**

## Valuations Across Time

Asset valuations are used to assess the value of material investments, such as a company, property, or security. While certain metrics can aid in comparing investment opportunities, they can also be measured in the aggregate, often by taking the mean valuation of a category of assets over a certain period. In this assessment, we will use the following valuation metrics in aggregate—each designed to measure the median price of an asset class:



**Public Equity**  
P/E Ratio



**Private Equity**  
EV/EBITDA Ratio



**Private Debt**  
Credit Spreads



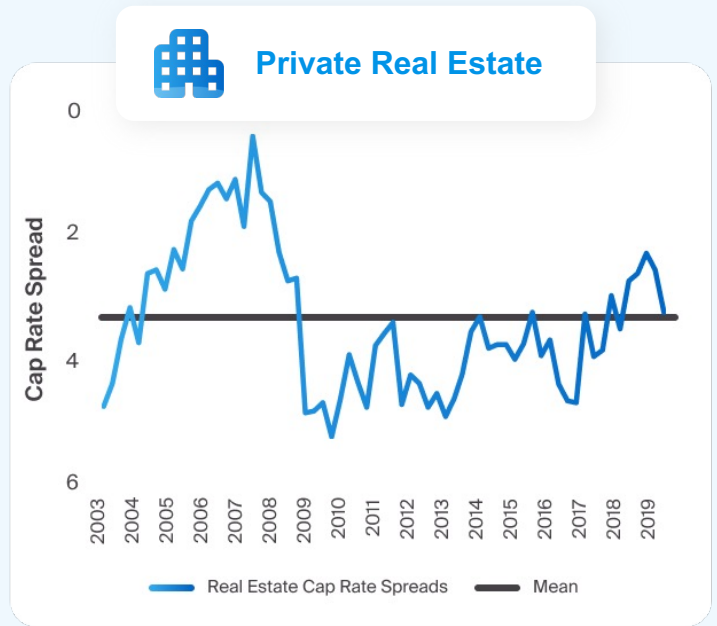
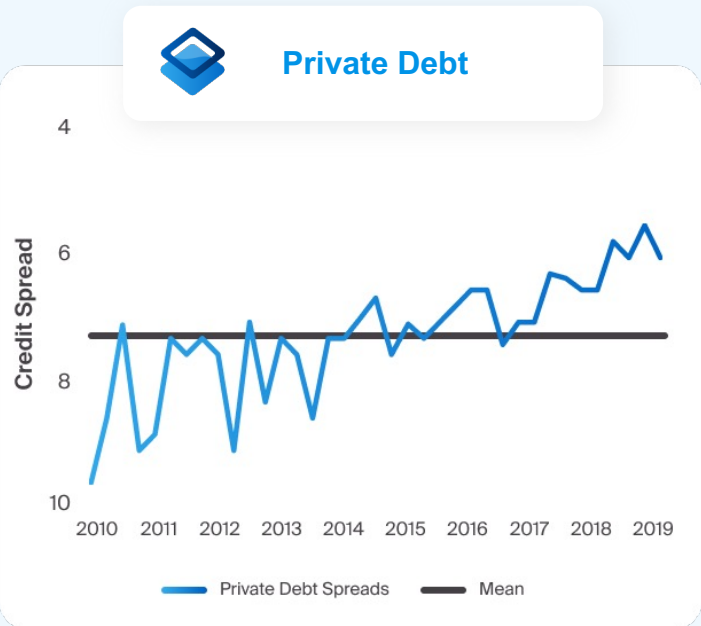
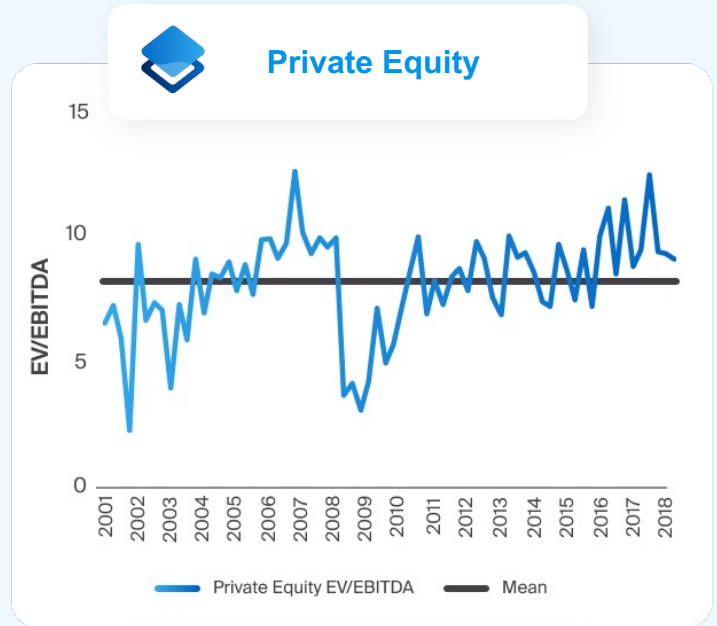
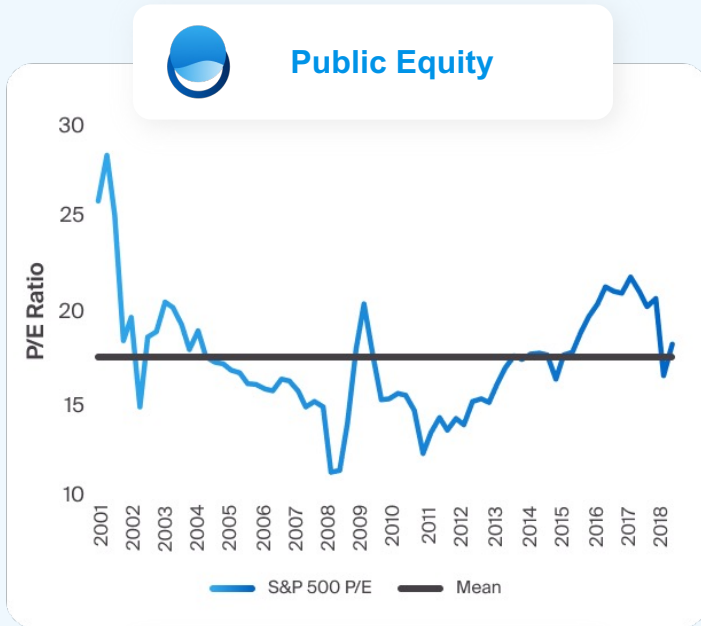
**Private Real Estate**  
Cap Rate Spreads

As we evaluate these valuation metrics, we will consider the reversion to the mean, a concept that suggests that asset prices and valuations tend to move back toward their historical averages.<sup>1</sup> Behind this principle is the idea that extreme highs or lows in valuations are often unsustainable, and, eventually, prices will "revert" to more typical levels, which we'll show are opportunistically rich for deployment into alternative asset classes. An assessment over the periods depicted in Exhibit 1 of valuation metrics generally appears to support that concept for asset classes like public equity, private equity, and private real estate, albeit with varying degrees of speed to mean reversion.

<sup>1</sup> [Corporate Finance Institute, Mean Reversion](#)



Exhibit 1: Observation Periods by Asset Class



Source: Bloomberg, public equity valuations represented by the P/E ratio of the S&P 500; Pitchbook, private equity valuations represented by the median buyout EV/EBITDA of global completed deals, private debt valuations represented by the median private debt spread/interest rate of global completed deals; NCREIF, private real estate cap rate spreads, represented by the spread between the median cap rate of real estate properties across all sectors, less the yield of the 10-year treasury, all valuations data ends in Q1 2019, to account for the five-year forward return length, updated as of Q3 2024.

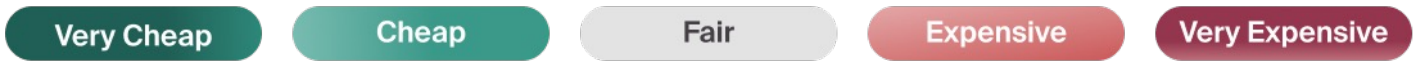
A period of cheaper valuation may provide a greater opportunity to generate returns, as asset valuations are generally recognized to revert to their long-term means—“buy low, sell high,” as the saying goes. Periods of relative “cheapness” may give rise to several benefits. For instance, cheaper valuations can provide a more attractive entry point, which may lead to higher return potential, and can also increase capital efficiency, potentially allowing an investor to pick up more assets at a lower cost. In addition, lower valuation environments may provide greater flexibility and leverage in negotiations, by securing potentially better terms like equity stakes, control positions, or covenants. Lastly, deploying capital into lower valuation environments may also mitigate the impact of macroeconomic regimes, as these periods may not only give rise to meaningful forward returns, as we intend to show, but may allow investors to benefit from coinciding recoveries and expansions that tend to follow strikes in valuation.



But of course, assets may be less expensive for other reasons. They may be out of favor or have lost intrinsic value and could continue to lose value. Thus, valuation is only one part of the broader picture.

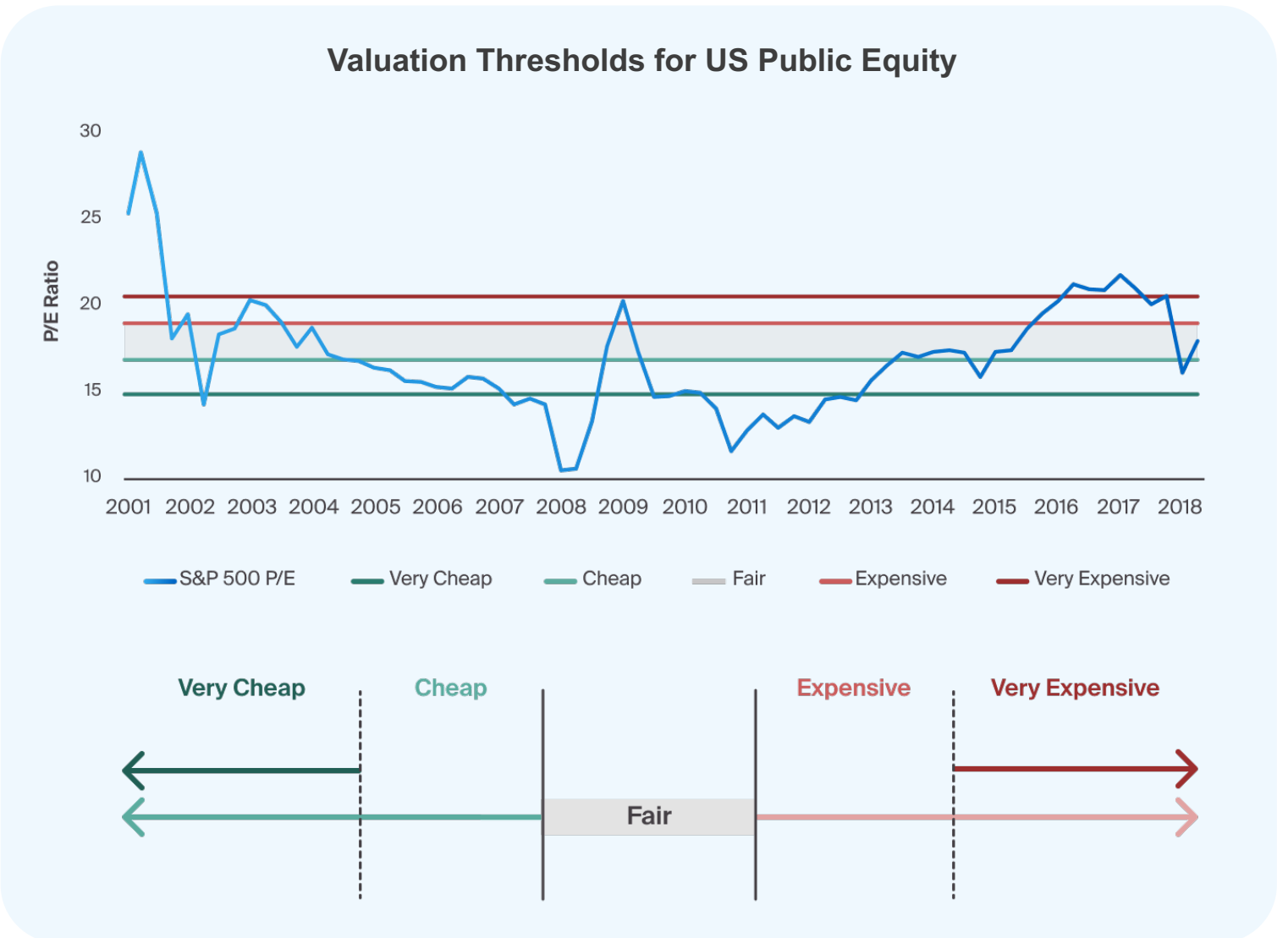
Still, assuming asset valuations are mean reverting by nature, do periods of cheaper valuations give rise to greater forward-looking returns and could they provide more opportunity for deployment into private markets?

To categorize valuation environments for public and private markets, we will use a framework of aggregating price levels into five baskets:



The valuation metric that defines each threshold will change depending on the asset class. We show this concept in Exhibit 2, using valuation for US public equities represented by the S&P 500.

**Exhibit 2:** Valuation Thresholds for US Public Equity



Source: Bloomberg, public equity valuations represented by the P/E Ratio of the S&P 500, all valuations data ends in Q1 2019, to account for the five-year forward return length, updated as of Q3 2024.





While the valuation data is non-normally distributed, meaning that valuation results are asymmetric about the mean, they are generally mean reverting. Over time, extreme values tend to revert to an equilibrium. As a result, we chose the price levels representing each basket based on both a review of the quantitative historical deciles of each series and a qualitative assessment of valuation level to account for Very Cheap and Very Expensive tail cases.

Using historical forward returns across various interval lengths (for a review of forward returns look at our [regime piece](#)), we can illustrate a hypothetical experience following deployment within these valuation environments. Below, we summarize the results of our assessment, to convey the forward performance that each asset class had achieved at different valuation levels.

**Exhibit 3:** Historical Heatmap of Three-Year and Five-Year Forward Returns

### Three-Year Forward Returns

Asset Class	Average	Valuation Level				
		Very Cheap	Cheap	Fair	Expensive	Very Expensive
Public Equity	10.6%	17.6%	10.3%	10.1%	11.6%	10.7%
Private Equity	14.5%	16.5%	16.6%	14.2%	9.7%	11.9%
Private Debt	8.6%	10.6%	10.5%	8.7%	7.5%	9.8%
Real Estate	9.9%	9.8%	11.4%	13.7%	4.7%	-5.1%

### Five-Year Forward Returns

Asset Class	Average	Valuation Level				
		Very Cheap	Cheap	Fair	Expensive	Very Expensive
Public Equity	10.4%	16.0%	11.2%	9.8%	9.8%	10.6%
Private Equity	14.0%	15.7%	15.4%	13.2%	12.6%	10.7%
Private Debt	8.5%	9.7%	9.7%	8.2%	8.2%	9.1%
Real Estate	7.7%	10.7%	11.5%	10.7%	0.4%	-4.8%

Source: Bloomberg, three- and five-year public equity returns represented by the S&P 500 Total Return Index; Preqin, three- and five-year forward return for private equity represented by the Preqin Private Equity Index, three- and five-year forward return for private debt represented by the Preqin Private Debt Index, three- and five-year forward return for private real estate represented by the Preqin Private Real Estate Index; Bloomberg, public equity valuations represented by the P/E ratio of the S&P 500; Pitchbook, private equity valuations represented by the median buyout EV/EBITDA of global completed deals, private debt valuations represented by the median private debt spread/interest rate of global completed deals; NCREIF, private real estate cap rate spreads, represented by the spread between the median cap rate of real estate properties across all sectors, less the yield of the 10-year treasury, all valuations data ends in Q1 2019, to account for the five-year forward return length, updated as of Q3 2024.

Using this framework may help advisors be better informed when and where deploying capital may be more attractive. Combined with an understanding of macroeconomic conditions, investment decisions can become more dynamic, as regimes and valuations may not always shift in unison.

By no means are historical results indicative of future returns. They demonstrate how asset class valuations influenced past performance.

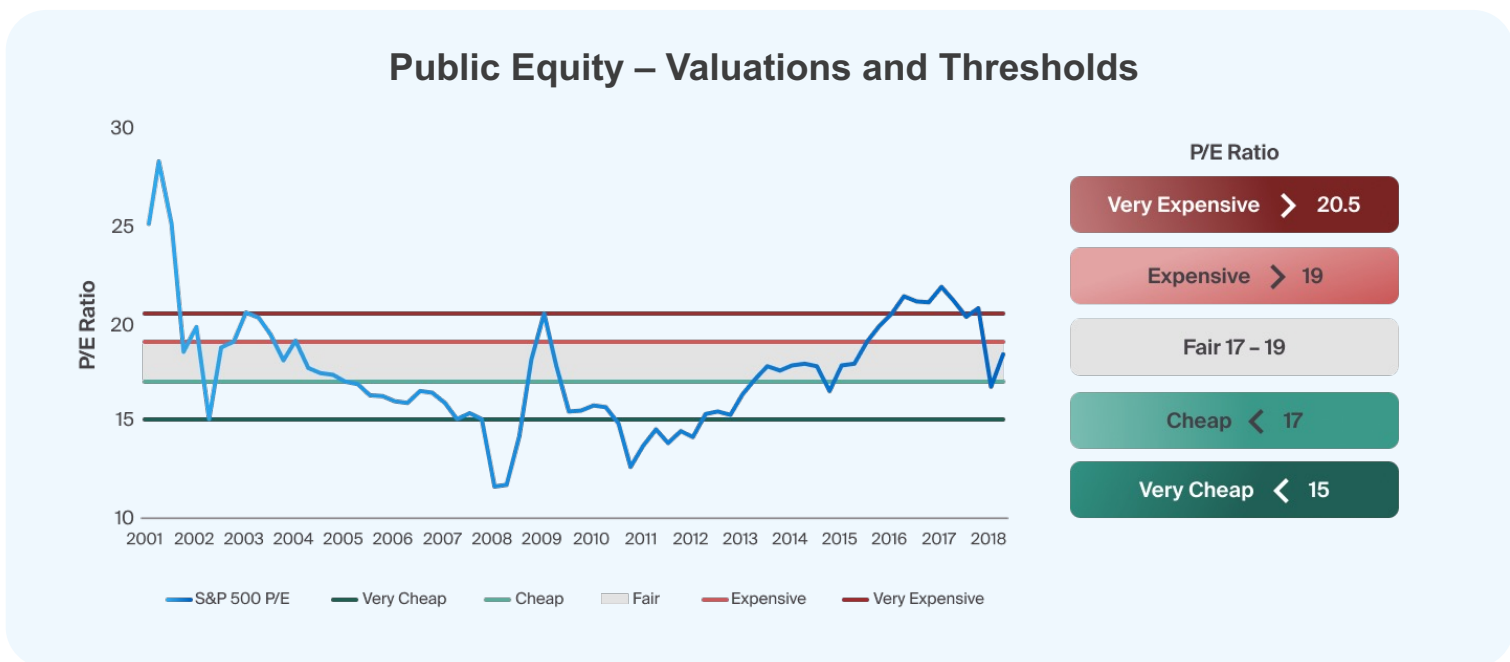


## Public Equity

The price-to-earnings multiple, or P/E ratio, is one of the simplest and most familiar valuation metrics, estimating the value of a company based on the relationship of its stock price to its earnings per share. It indicates how much the market is paying for each dollar of earnings and is calculated by dividing the stock price by the earnings per share.

A low P/E ratio can indicate undervaluation or company challenges, while a high P/E ratio may suggest overvaluation, expected growth or relatively high earnings growth. For our purposes, the S&P 500 P/E ratio reflects the valuation of the largest 500 publicly traded companies in the US, signaling shifts in investor confidence and broader economic conditions.

**Exhibit 4:** Historical P/E Ratio of the S&P 500 Paired With Valuation Thresholds



Source: Bloomberg, public equity valuations represented by the P/E ratio of the S&P 500, all valuations data ends in Q1 2019, to account for the five-year forward return length, updated as of Q3 2024.

The pricing levels above illustrate the pattern of mean reversion behavior across valuations levels over time.



## A Historical Perspective: The Global Financial Crisis

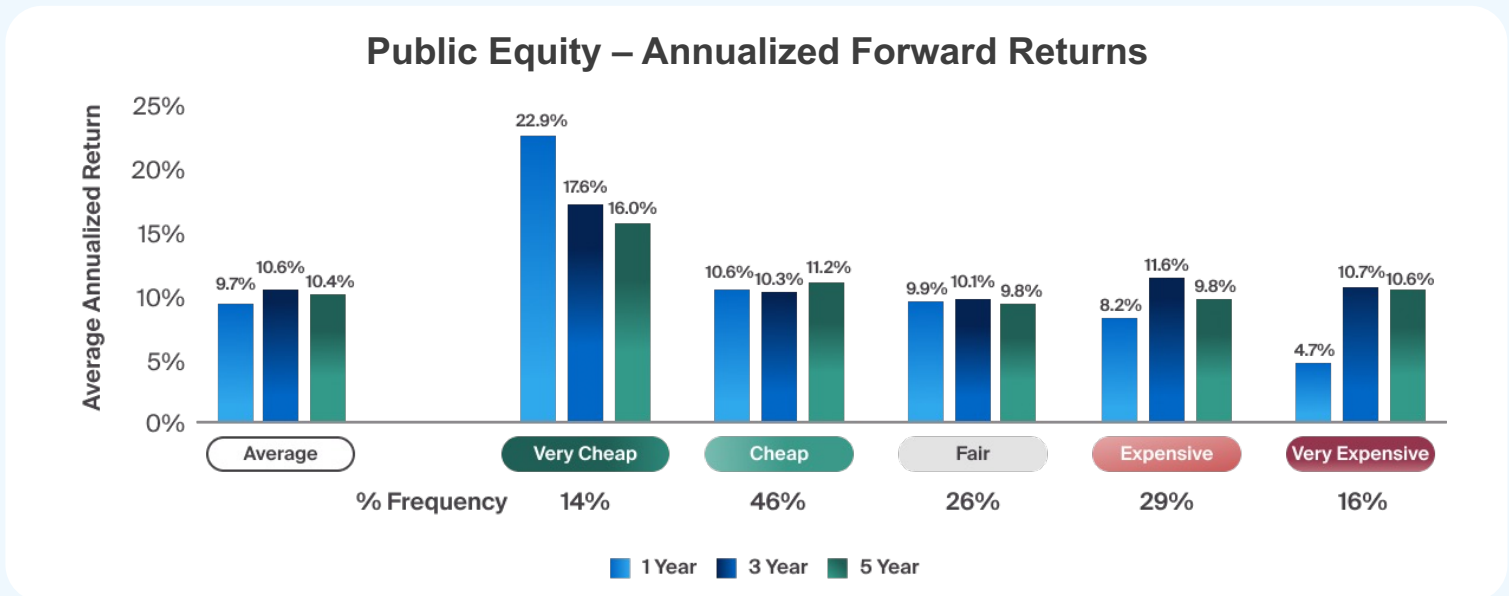
The Global Financial Crisis (GFC) triggered a dramatic and immediate decline in public equity valuations, with major stock indices plummeting by 50% or more from their pre-crisis peaks. Market volatility spiked, and credit markets froze, disrupting capital flows and impacting investor confidence. Corporate earnings fell due to a sharp economic slowdown, contributing to prolonged low valuations. The crisis also prompted increased financial regulation aimed at preventing instability, which impacted the financial sector and market dynamics. In this period, P/E ratios hit just under 12, a local low point. (Exhibit 4)



## Historical Returns

Our assumption would be that returns are highest when deployed into cheaper environments and lower in expensive ones. This aligns with our findings, as public equity forward returns outperformed their average and all other price levels when deployed in Very Cheap environments.

**Exhibit 5:** Public Equity Forward Returns Relative to Valuation Levels



Source: Bloomberg, public equity valuations represented by the P/E ratio of the S&P 500, three-year and five-year forward return for public equity represented by the S&P 500 Total Return Index, all valuations data ends in Q1 2019, to account for the five-year forward return length, updated as of Q3 2024.

We assess the one-year forward returns for public equity exclusively to highlight some features of the asset class's inherent liquidity, which we will discuss in greater depth in the conclusion. The one-year forward returns show the greatest dispersion of returns across valuation levels and outperformed in the shortest term (Exhibit 5).

In the more frequently occurring range of Cheap to Expensive valuations, forward-return differentiation was not as pronounced across price levels. What's more pronounced was the gradual decline in the one-year forward returns as price categories increase. This decline may reflect public equity's short-term sensitivity to valuation changes, which can happen following a period of valuation reversion.

Investing in public equities appears more time dependent in the short term, when investors may be rewarded if the market is timed correctly, but timing the market is a strategy that may result in miscues.

### Key Observations

- ➔ Deploying capital when public equity valuations are Very Cheap generated considerably higher forward returns compared to other valuation environments.
- ➔ One-year forward returns for public equity drastically underperformed following Very Expensive valuation periods.
- ➔ Forward returns exhibit much lower variability between price levels outside of Very Cheap.
- ➔ The negative relationship between one-year forward returns and valuation level is perhaps indicative of the asset class's sensitivity to short-term price fluctuation.





## Measuring Private Markets Performance and Valuations

Private markets are generally illiquid with much longer holding periods. To better reflect the nature of investing in these asset classes, we will focus on three- and five-year forward returns.



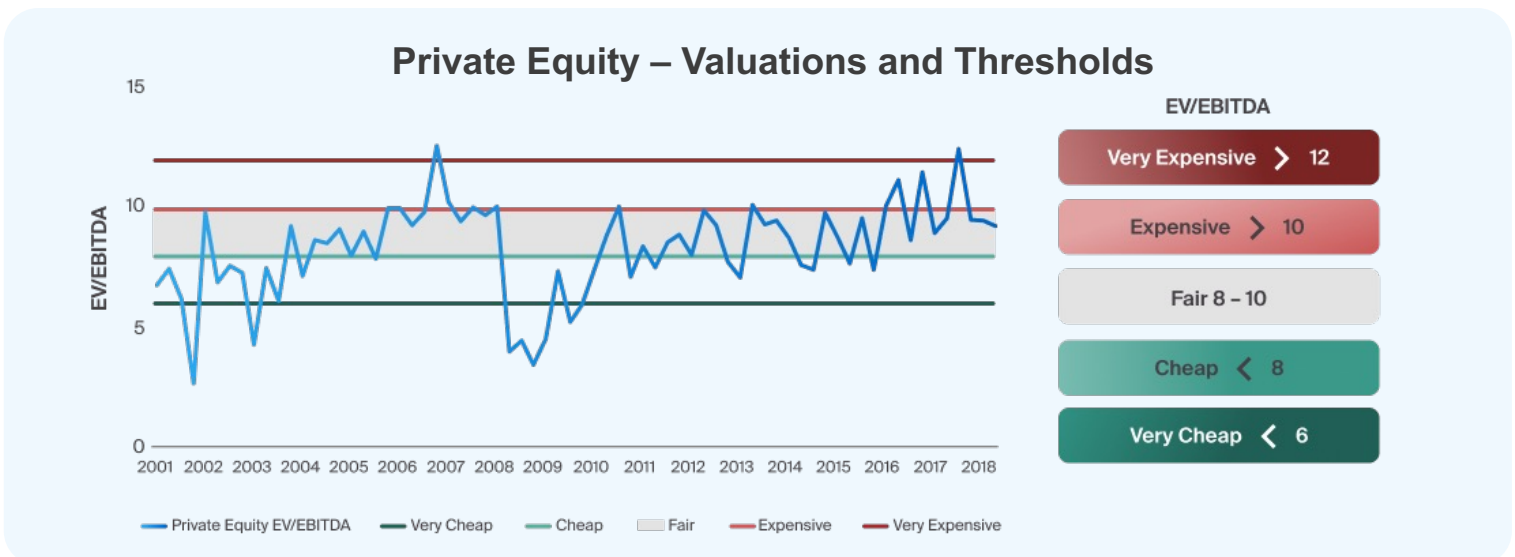
### Private Equity

In the same way that the P/E ratio expresses the relationship between the price of an investment and its earnings for public equity, EV/EBITDA, or the enterprise value over earnings before interest taxes depreciation and amortization, is used in private equity. EV/EBITDA is used to compare the relative value of businesses—regardless of their capital structures—to negotiate acquisitions of private companies and calculate target prices.

A high EV/EBITDA ratio suggests that investors are willing to pay a premium to acquire a company or invest in it, which may indicate either overvaluation or expectations of growth. Conversely, a low ratio may suggest concerns about a business's growth potential or persistent operational issues. However, the undervaluation may indicate that the business is priced attractively relative to its earnings. The EV/EBITDA ratio is considered a good measure of value because it isolates companies' operational performance from their capital structure and other non-operational factors. In aggregate, the ratio tracks an industry's temperature.

We tracked the EV/EBITDA of completed buyout transactions below (Exhibit 6). This private equity market aggregate assessment should not be compared to individual transactions.

**Exhibit 6:** Historical Private Equity EV/EBITDA Paired With Valuation Thresholds



Source: Pitchbook, private equity valuations represented by the median buyout EV/EBITDA of global completed deals, all valuations data ends in Q1 2019, to account for the five-year forward return length, updated as of Q3 2024.

## A Historical Perspective: The Global Financial Crisis

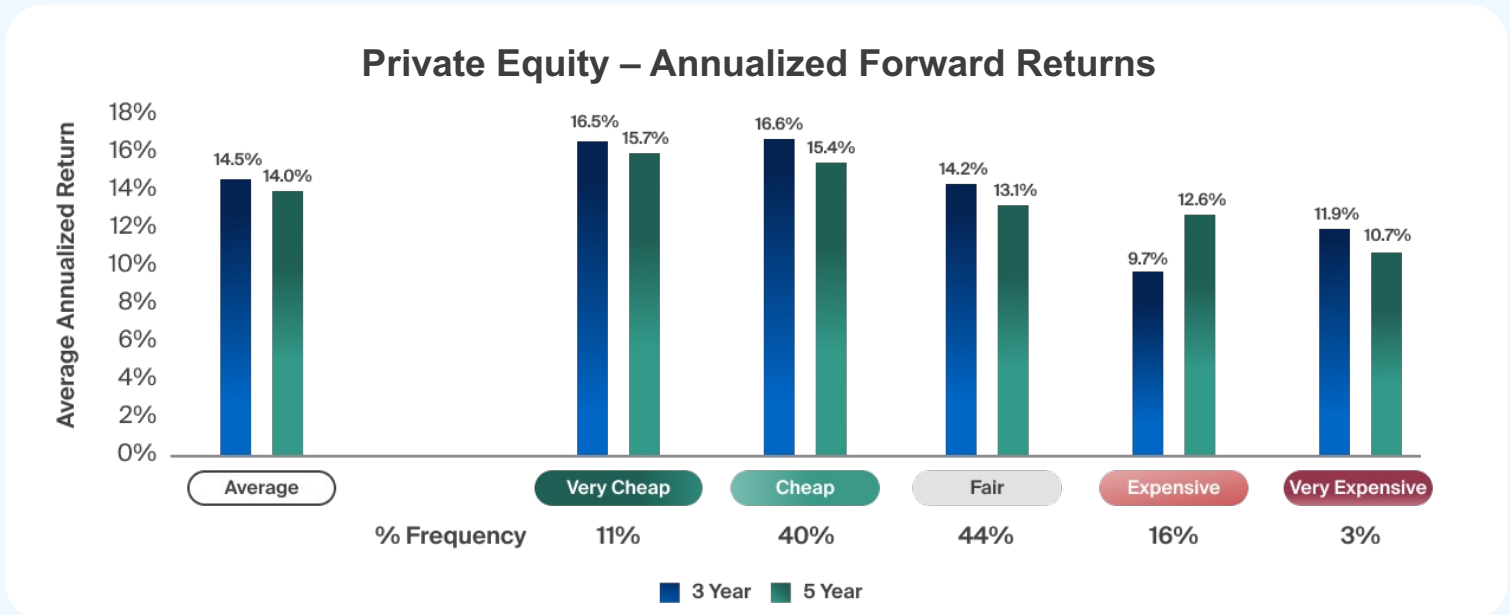
The GFC led to a significant drop in private equity valuations. The crisis limited access to capital and tightened credit conditions, making it difficult for private equity firms to finance new deals or exit investments, and to achieve expected returns. The market also saw a slowdown in deal activity and a heightened focus on improving operational efficiencies within portfolio companies. In this period, EV/EBITDA ratios fell below 3.5 (Exhibit 6).



## Historical Returns

Private equity historical returns resemble public equity ones, with higher returns achieved through deployment into cheaper environments, yet we can see a more consistent trend across valuation levels (Exhibit 6).

**Exhibit 7:** Private Equity Forward Returns Relative to Valuation Levels



Source: Pitchbook, private equity valuations represented by the median buyout EV/EBITDA of global completed deals; Preqin, three- and five-year forward return for private equity represented by the Preqin Private Equity Index, all valuations data ends in Q1 2019, to account for the five-year forward return length, updated as of Q3 2024.

Private equity returns appeared sensitive to changing price levels over time. Unlike public equity returns, private equity returns varied much less between Very Cheap and Very Expensive, with gradual declines in returns across categories between Cheap and Expensive (Exhibit 7). Therefore, while private equity forward returns appeared to be sensitive to asset valuation, the outcomes of deploying in different valuation environments were less variable than those of public equity, particularly over longer investment periods.

### Key Observations

- ➔ Deploying capital when private equity valuations were both Very Cheap and Cheap generated higher forward returns compared to Expensive and Very Expensive environments, especially on a three-year forward basis.
- ➔ Private equity forward returns did exhibit a negative relationship with the valuation environment, but dispersion was relatively low, particularly over a five-year holding period.
- ➔ While private equity returns did seem to be meaningfully impacted by the valuation environment at point of entry, the asset class offered more opportunities to outperform its long-term historical average compared to public equity based on the frequency of results and the lower deviation between Very Cheap periods and other price categories.



## Private Debt

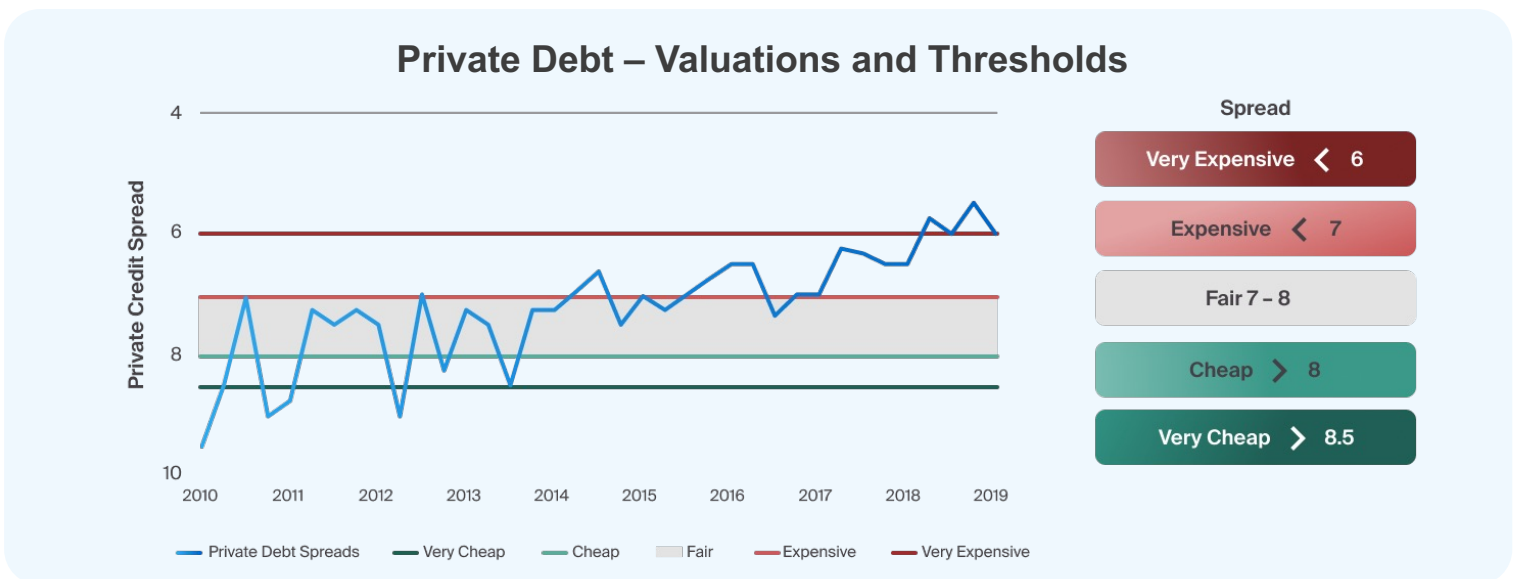
We will use a different metric from the price-dependent equity multiples to assess private debt valuations: credit spreads. When debt is issued, its perceived risk is often based on its spread to a base rate. Private debt valuation can be assessed similarly; credit spreads are expressed as the interest rate for an issued loan net of the base rate, conveying the loan's price level.

Credit spreads are the differences between the interest rates on private loans and a base rate, such as SOFR (Secured Overnight Financing Rate). The spread represents the additional yield an investor would receive on a riskier loan compared to the base rate or a risk-free benchmark, which can help investors determine the appropriate interest rate level for the risk embedded in loans.

A wide credit spread reflects more risk and uncertainty related to a borrower's low credit rating or economic instability. A narrow credit spread implies lower risk and a more stable investment environment. Credit spreads are considered a good value descriptor because they are anchored by a base rate that allows straightforward comparisons between the risk-return profile of credit investments. In aggregate, credit spreads act as a thermometer of risk premium across the private debt market and reflect investor sentiment.

Global private debt spreads for completed deals, calculated by taking the median interest rate of debts minus the base rate applied to the deal, are depicted below, with bands indicating the price levels from Cheap to Expensive. Note that the observation period for private debt is shortened compared to the other asset classes based on data availability and due to the regulatory shifts prior to 2010, which are discussed in the box below.

**Exhibit 8:** Historical Private Debt Spreads Paired With Valuation Thresholds



Source: Pitchbook, private debt valuations represented by the median private debt spread/interest rate of global completed deals, all valuations data ends in Q1 2019, to account for the five-year forward return length, updated as of Q3 2024.



## A Historical Perspective: The Global Financial Crisis

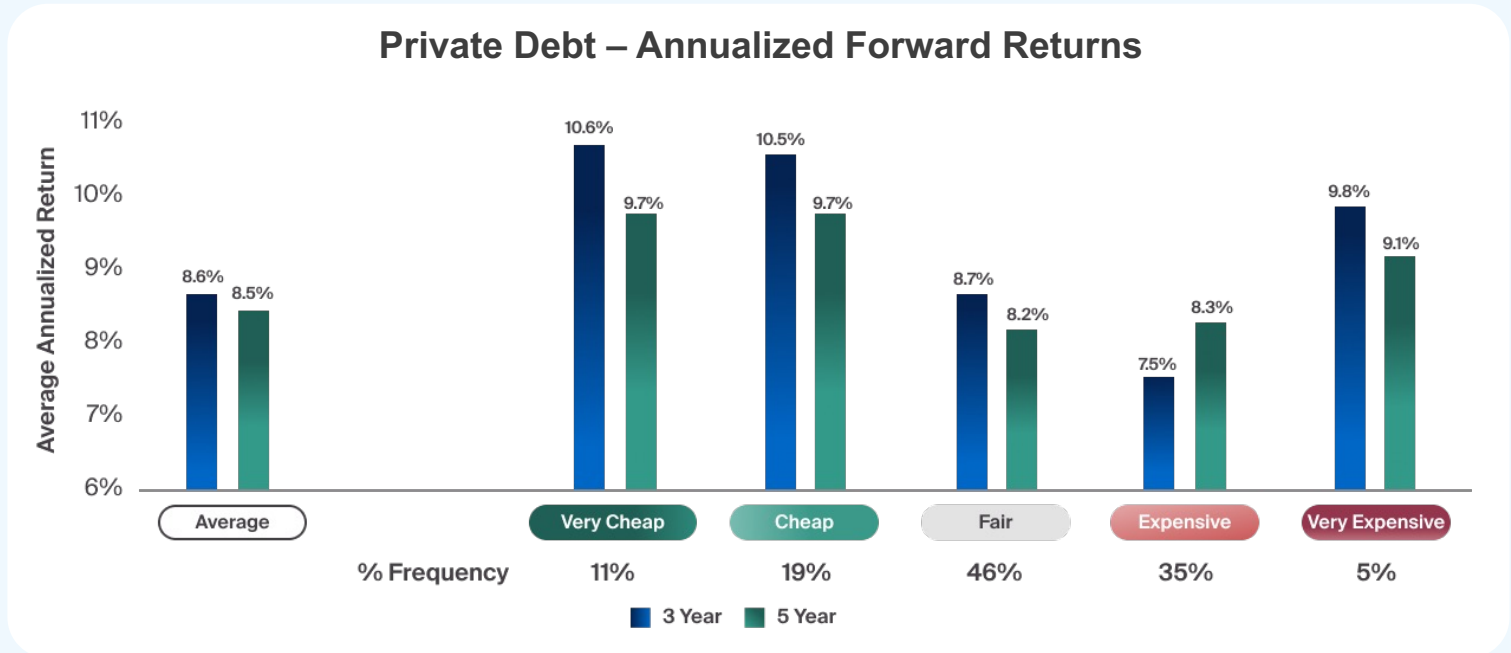
After the GFC, private debt markets saw increased regulation and stricter lending standards, leading to a shift towards higher-quality, senior-secured loans and greater emphasis on covenants and due diligence. Non-bank lenders, such as private equity and hedge funds, gained prominence as traditional banks faced tighter regulations. Investors demanded higher risk premiums and adopted more conservative investment strategies, including longer investment horizons and increased diversification. Since then, a new valuation floor was established within our observation period. During that period, which starts in 2010, the median credit spread landed at 7.05 (Exhibit 8).



## Historical Returns

Similar to the behavior of other asset classes we analyzed, private debt strategies generated greater forward returns at the lower end of the asset valuation spectrum (Exhibit 9).

**Exhibit 9:** Private Debt Forward Returns Relative to Valuation Levels



Source: Pitchbook, private debt valuations represented by the median private debt spread/interest rate of global completed deals; Preqin, three- and five-year forward return for private debt represented by the Preqin Private Debt Index, all valuations data ends in Q1 2019, to account for the five-year forward return length, updated as of Q3 2024.

In periods of Very Cheap and Cheap valuations, private debt sharply outperformed its long-term historical average for the three- and five-year periods (Exhibit 9). But as price categories get more expensive, returns appeared less compelling, aside from a jump in the Very Expensive territory, which is likely to be attributed to the non-normal nature of our dataset, which sees private debt spreads gradually rise. Following the GFC, spreads steadily increased due to regulation and stricter lending standards.

Investing in private debt is time dependent over the long term, yet compared to private equity, it achieved more compelling results during “cheaper” periods. But we must bear in mind the gradual maturation of the private lending landscape.

### Key Observations

- Deploying capital when private debt valuations are both Very Cheap and Cheap generated forward returns that exceeded long-term historical returns.
- As investing in tighter rate spread environments typically resulted in lower returns, private debt forward returns exhibited a negative relationship to price, aside from Very Expensive, which accounts for just 5% of our sample.



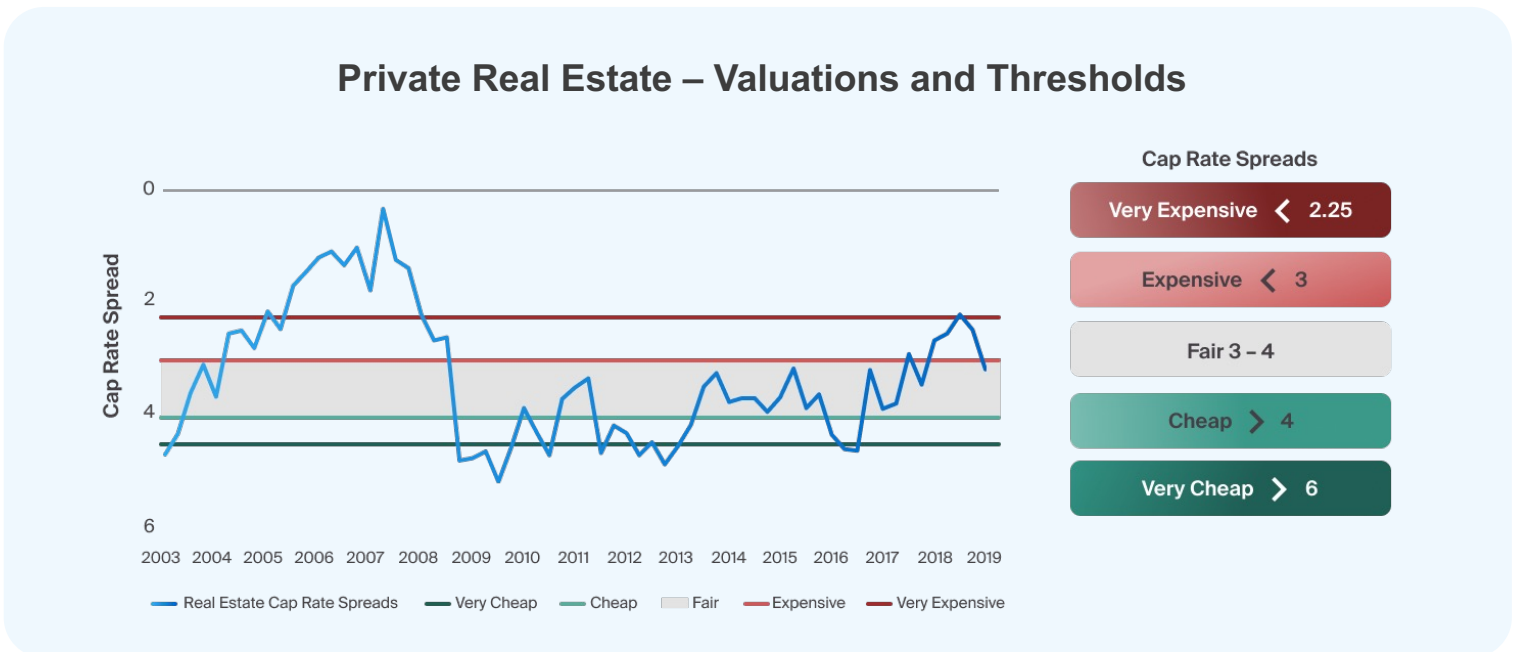


## Private Real Estate

The capitalization rate, or cap rate, is a key metric used to value real estate assets and gauge their return potential. Cap rates are calculated by dividing an asset’s net operating income by its value, which aims to reflect the price an investor is willing to pay. Investors can use the cap rate spread—the difference between the cap rate and a risk-free benchmark, such as government bond yields—to value private real estate, either at an asset level or, in our case, across all sectors in aggregate.

High cap rate spreads may indicate elevated risk and suggest that an asset’s net operating income is high relative to its market value, reflecting potential concerns about price. In practice, investors typically demand higher returns to compensate for additional risk, creating a mismatch between a property’s operating income and its price. Conversely, low cap rate spreads tend to reflect more stable real estate properties with lower risk, as prices better reflect achieved income and thus a potentially more expensive valuation environment. Due to their tie to this base rate, cap rate spreads may be good value descriptors and, in aggregate, a strong gauge of investor sentiment.

**Exhibit 10:** Historical Private Real Estate Cap Rates Paired With Valuation Thresholds



Source: NCREIF, private real estate cap rate spreads, represented by the spread between the median cap rate of real estate properties across all sectors, less the yield of the 10-year treasury, all valuations data ends in Q1 2019, to account for the five-year forward return length, updated as of Q3 2024.

## A Historical Perspective: The Global Financial Crisis

The GFC led to a widening of private real estate cap rate spreads as investors demanded higher returns for increased risk. The crisis caused a sharp decline in property values and increased uncertainty in the real estate market, leading to higher capitalization rates for properties. This was driven by tighter credit conditions, reduced liquidity, and a general aversion to risk. In this period, cap rate spreads hit just over five.

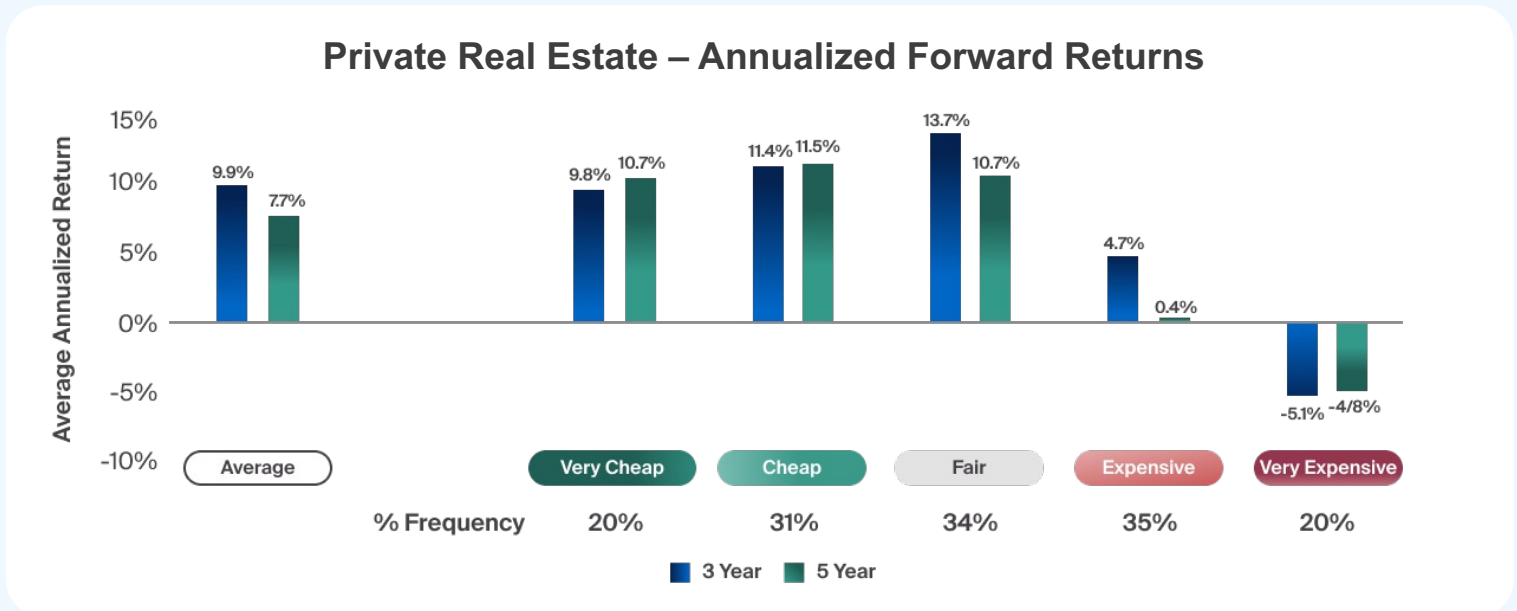




## Historical Returns

Real estate performance respective to valuations indicates a slight variation from prior asset classes, as greater forward returns were generated at the Cheap and Fair price levels (Exhibit 11).

Exhibit 11: Private Real Estate Forward Returns Relative to Valuation Levels



Source: NCREIF, private real estate cap rate spreads, represented by the spread between the median cap rate of real estate properties across all sectors, less the yield of the 10-year treasury; Preqin, three- and five-year forward return for private real estate represented by the Preqin Private Real Estate Index, all valuations data ends in Q1 2019, to account for the five-year forward return length, updated as of Q3 2024.

Periods of Very Cheap valuations generated lower returns than Cheap and Fair periods. The Very Expensive valuation periods generated the most dramatic performance as they significantly underperformed the historical average (Exhibit 11). While the impact of the GFC drawdown was largely reflected in the dataset, deploying capital in Expensive periods resulted in the lowest forward performance across all asset classes.

### Key Observations

- ➔ Private real estate returns historically exhibited high sensitivity to rich valuation environments compared to other private markets asset classes.
- ➔ Expensive real estate valuation environments led to significant underperformance compared to other private markets asset classes.
- ➔ Deploying capital in private real estate across Very Cheap, Cheap, and Fair valuation conditions produced relatively similar returns, all exceeding long-term averages.



## Risks and Considerations

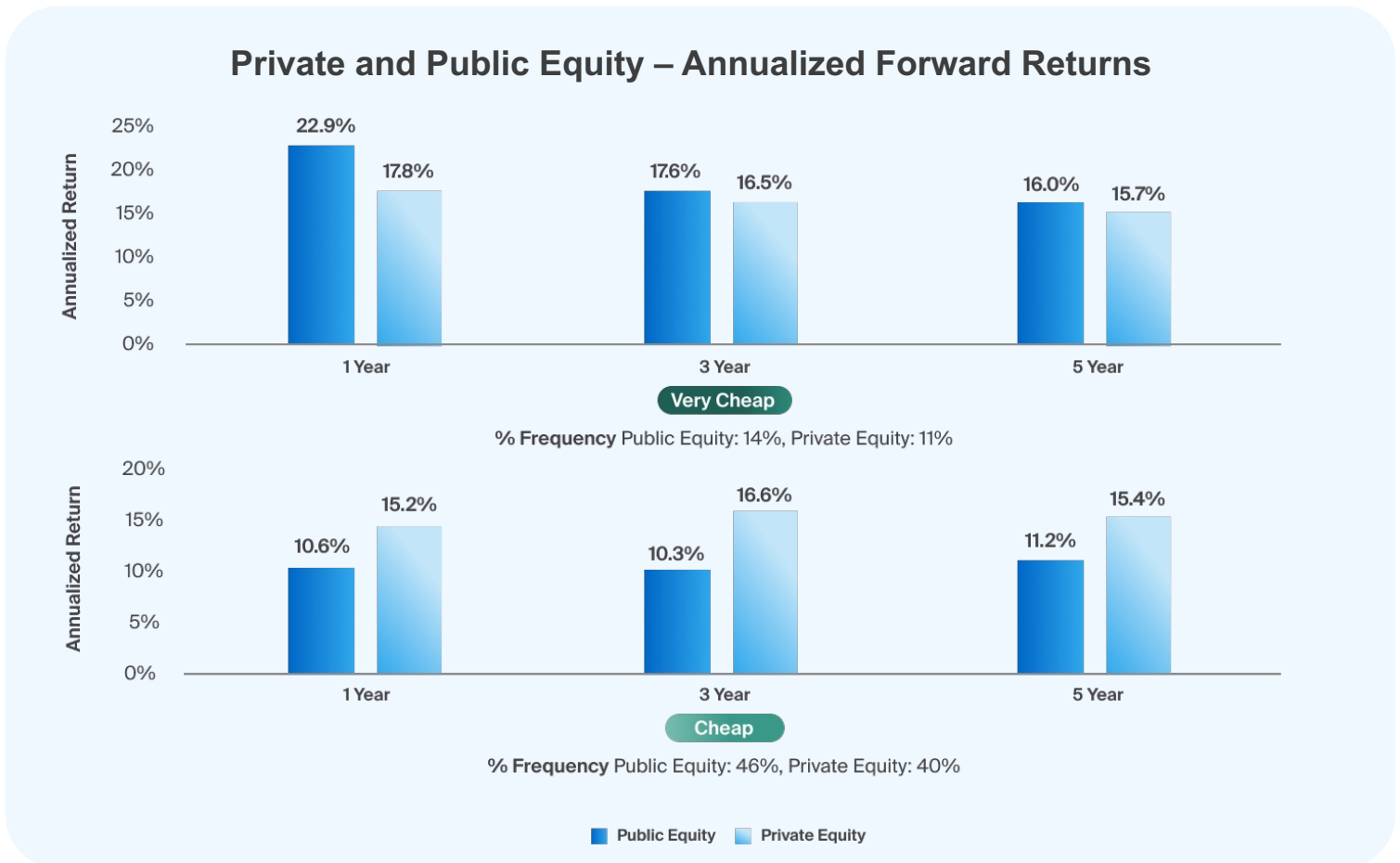
Advisors may be exposed to significant risks when allocating portions of their portfolios to alternative asset classes. Funds in these alternative asset classes may have limited liquidity at both the fund and asset level. Alternative fund managers may also employ tactics that are inherently riskier than those available to traditional fund managers, such as greater use of leverage or short selling.

It is also worth noting that it is not possible to invest in any of the broad asset class indices used in this analysis, and therefore, the experience of an advisor who invests in individual strategies may have been quite different from the results shown here.

## In Summary

Our hypothesis regarding the entry point impact at different valuation levels on forward-looking returns across asset classes generally held true during the time periods we analyzed. We observed that investing at lower valuation entry points historically resulted in higher returns across all the asset classes in focus. However, to readdress a prior idea, valuations in private markets appeared somewhat slower and more persistent compared to public markets. Forward returns across these asset classes tended to react to changes in valuations over different periods of time.

**Exhibit 12:** Return Differentials Between Public and Private Equity in Cheap Valuation Periods



Source: Bloomberg, public equity valuations represented by the P/E ratio of the S&P 500, public equity represented by the S&P 500 Total Return Index; Pitchbook, private equity valuations represented by the median buyout EV/EBITDA of global completed deals; Preqin, three- and five-year forward return for private equity represented by the Preqin Private Equity Index, all valuations data ends in Q1 2019, to account for the five-year forward return length, updated as of Q3 2024.



Public equity outperformed private equity across all three forward-return intervals following Very Cheap valuations, which speaks to public equities' reactivity and potential overdependence on price to generate outperformance. In addition, public equity underperformed as the time horizon extended. Following periods of Cheap valuations, private equity outperformed across all time horizons, highlighting two takeaways (Exhibit 12).

First, achieving the highest performance in public equity could have been dependent on finding Very Cheap valuations to deploy, which are rare and may result in miscues. Second, private equity, by nature, performed best over the longer term, which supports the idea that private asset classes are designed to create value and enhance operational efficiency to generate return. This is why we saw the forward returns for private equity remain stable as the time horizon increased while public equity declined.

These concepts in practice can be referred to as valuation expansion versus contraction.

Valuation expansion can be described as the situation in which valuations adjust over time to reflect the intrinsic value of an investment, aligning to the real demand of this asset. Valuation expansion typically occurs over extended periods of time, but it's during these periods of expansion that investments may result in higher, more consistent long-term returns, often characterized in private markets asset classes.

Contraction often is much quicker and more reactionary to changes in market dynamics like shifts in monetary policy, recessionary drawdowns, or other factors that may drive public market equity performance. In other words, public markets may be more sensitive to valuation contractions and fast reversions. Private markets indices tend to follow broader economic cycles of valuation expansion. Other private markets asset classes follow similar characteristics, but perhaps not as clearly as the distinction between public and private equity.

Valuation reversion, which suggests that an asset returns to its historical average valuation from a period of unusually high or low performance, is certainly related to these observations. Performance derived from this reversion, as the data may suggest above, may be more common in public markets than private, which reflects both the illiquidity and underlying valuation dynamics of private markets compared to public.

Overall, periods when valuations fell in line with their historical trend and even instances when they are more expensive may represent opportunities for outperformance.

## Methodology

We used a balance of both quantitative and qualitative approaches to select the price thresholds for valuations environments across the asset classes. Quantitatively, we assessed the historical valuation data by decile; however, as we were limited by the non-normal nature of our dataset, we enhanced our assessment with qualitative attention to high and low valuation points to inform where these thresholds made the most sense. The decision to divorce our assessment from a wholly systematic approach was made based on capturing the most meaningful dataset given our data availability, which led us to consider outliers, periods of mean reversion, and non-normal behavior.

Our valuation dataset is also trimmed to 2018, which is the most recent year when capital could have been deployed to generate five-year forward returns. In later iterations of this research, we plan to depict more recent valuation levels.



## Authors



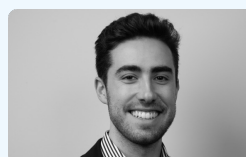
**Neil Blundell**  
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**Duy Nguyen**  
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**Linge Sun**  
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Investment Strategy



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