Investing with UBS Wealth Management

Our CIO Investment Philosophy

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Contents

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Foreword

Investing is personal. It connects investors' aspirations, be it lifetime or legacy goals, with their ability to achieve those aims. And when markets move fast, behavioral biases can lead to mistakes and regrets. This is why at the Chief Investment Office (CIO), our investment philosophy and guiding principles are built to navigate the choppy seas of volatile markets with a steady hand.

For many clients, the aim is to grow and protect your wealth over generations, and everything we do is geared toward accomplishing this task. The starting point is understanding investors' goals, financial circumstances and total wealth, and preferences so that the right investment strategy is defined for their needs.

In the following pages, we share our views about how investors should think about investing and what they need to do to invest confidently. So that each investor—regardless of their experience—can better navigate the complex world of investing, this publication maps different investor circumstances and preferences with the relevant investment principles and parameters.

Together, we can define a wealth strategy that best fits an investor's needs and aspirations.

Mark Haefele
Chief Investment Officer
Global Wealth Management

CIO Wealth Journey

Discover

- Financial & non–financial goals
- Investment preferences & values
- Financial situation & total wealth

Define

- Investment framework
- Designing right portfolio for each investor
- Investment principles
  - SAA, TAA, instrument selection
  - Reference currency, investment universe, liquidity needs
  - Borrowing

Execute

- Superior solutions for the right investment strategy
- Reviewing and rebalancing

Our portfolio philosophy

Before we outline in detail how to design the optimal portfolios for different investors' needs, we first outline our key investment pillars. Successful investing requires a clear understanding of the basis on which portfolios are constructed and managed.

At the heart of our philosophy is the conviction that portfolios should be Personal, Long term, Active, and Diversified.

Personal
We develop portfolios to align with the goals, preferences, and financial situation of the individual investor.

Long term
We believe portfolios with long-term objectives are better placed to gain from value creation over time.

Active
We adjust portfolios to account for the short- and medium-term opportunities markets present and changes in investors' personal circumstances.

Diversified
Diversification has been described as "the only free lunch in investing" and this principle is reflected in our portfolio strategies. We believe globally diversified, multi-asset class portfolios deliver superior risk-adjusted rates of return over time.

Personal

Designing a portfolio for each investor
Investors' portfolios must suit their personal needs and circumstances. Investment advice and portfolios are constructed in the context of a financial plan. Portfolios are tailored to the different risk level required and reflect specific investment preferences and constraints. Portfolios that meet individual investors' goals, values, and constraints make those goals more achievable and make sticking with a plan more comfortable.

Long term

Benefiting from value creation and avoiding behavioral traps
We believe that a long-term approach to investing is important. This may refer to multiple years or even a multigenerational time horizon. While corporate profits experience cyclical ups and downs, they tend to grow over time. So long-term investors are compensated for taking market or credit risk. Successful investing is less about timing the market, but staying invested for the long term.

Active

Taking advantage of short to medium-term opportunities
While we maintain a long-term investment approach, markets often present short- and medium-term opportunities. Therefore, many of our portfolio strategies include a tactical asset allocation. We also analyze the short- to medium-term outlook for individual securities, sectors, styles, themes, and countries in each asset class, so your decisions can add to overall performance and suit your investing approach. Such tactical investment positions are assessed in the context of investors' portfolios.

Diversified

Managing risk
There is always a best- and worst-performing part of every portfolio, but consistently selecting the best part on a forward-looking basis is near impossible. So most of our portfolio strategies take on exposure to multiple asset classes, including equities, bonds, and alternatives such as hedgefunds. We also diversify by investing across securities and countries to limit exposure to idiosyncratic corporate risks, and, in some strategies, across different levels of liquidity. Historically, diverse portfolios have achieved a superior rate of risk-adjusted return than those that are more concentrated. We believe globally diversified portfolios deliver superior risk-adjusted rates of return over time.

Why invest?

Before getting into how to define the right strategy, let us start with why one should invest.

Wealth is a means to an end. The importance of wealth, its significance, can differ from person to person. Wealth can provide a sense of security or standing in the world. It can finance certain goals. And it can influence outcomes.

Growing or preserving wealth—often generated over generations—requires investing it. This is especially important because inflation, taxation, or consumption can erode one's wealth over time. Sustaining your lifestyle and that of your loved ones therefore requires an investment strategy.

Some may feel nervous about investing because they are afraid they will lose their wealth. But it's important to remember that over the long term, holding cash usually leads to wealth erosion while investing usually leads to wealth growth.

Inflation is a measure of the changing cost of goods and services across an economy. This means inflation erodes the spending power of your wealth. Over the years and across generations, that spending power can diminish dramatically.

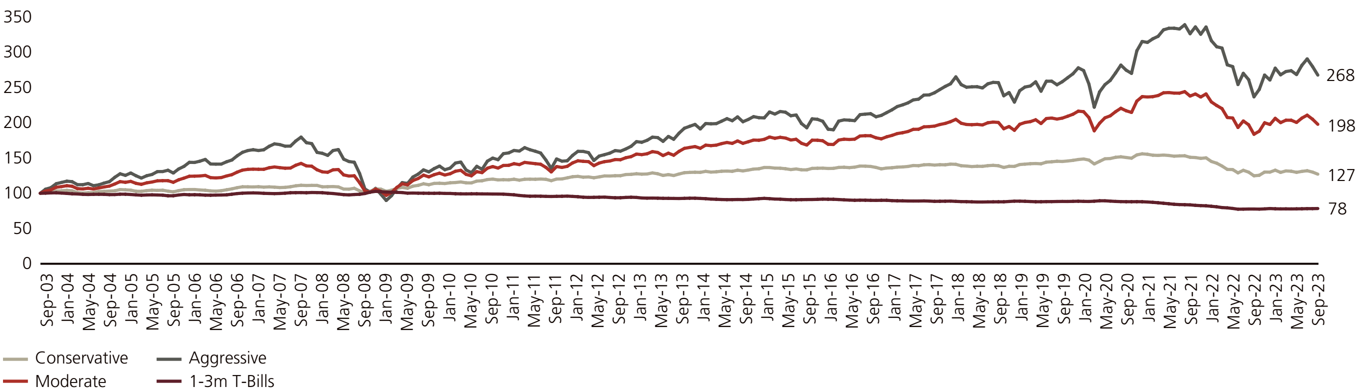
Inflation rates can be a helpful starting point for forecasting your future spending, but it is important to note that your personal spending composition will be different to the mix of goods and services used by inflation indexes. So, when working out how much money an investor will need, and factoring in assumptions on how an investor's personal inflation might rise, will provide a more realistic estimate of the returns an investor will need from his/her investments.

The power of compounding returns is one of the great forces of investing—small, incremental returns, accumulate over time. For example, the difference between a portfolio returning 5% versus 3% per year does not seem great at first look. However, as these portfolios grow over an investor's lifetime (compounding these annual returns), the difference in cumulative return also grows. Figure 1 shows an example of the opportunity cost of investing more conservatively. Over this 20-year period, and Aggressive investment portoflio would have averaged a 5% annual real return, versus 3.5% for a Moderate portfolio and 1.2% for a Conservative portfolio. We also see that leaving money in cash (e.g., 1-3 month Treasury bills) would have resulted in a loss of purchasing power due to inflation.

Figure 1

Cash loses purchasing power over time, while compounding returns allows for growth over time

Inflation adjusted "real" cumulative performance



Source: UBS AG, UBS QIS, US Federal Bank of St Louis for CPI inflation

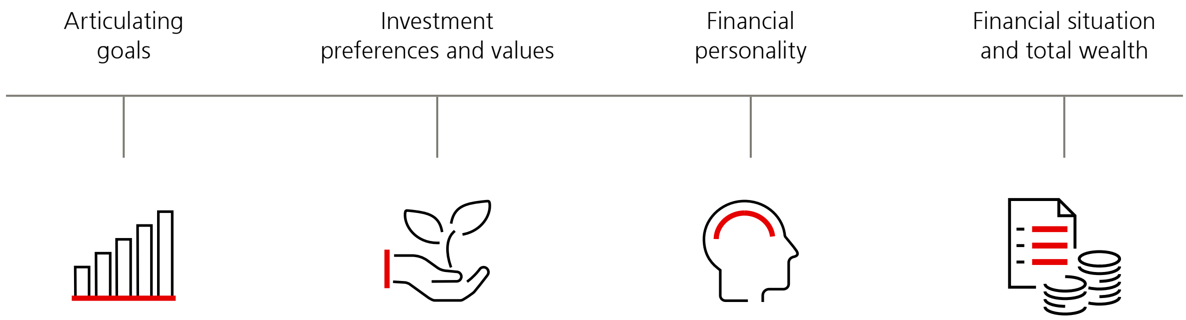
To achieve one's goals, it is important to consider the entire investment portfolio and total wealth—not just individual elements of it.

Part I

Understanding to Discover

Goals, investment preferences and values, and one's financial situation determine the right investment portfolio.

In this section we look at what information is important to know and why in order to design the right investment strategy. We look at the importance of defining goals, understanding one's investment preferences and values, understanding an investor's financial personality and finally the importance of incorporating a holistic total wealth view of one's wealth.



Articulating goals

Investing can help achieve one's ambitions in life. Goals often reflect one's values and build the foundation of how to make investment decisions: From the assets chosen, to the returns needed and the length of time one needs to invest. Once these goals are defined, a personalized investment plan can be established aimed at achieving these objectives.

In the process of articulating goals, a lot of questions should be considered and addressed. For example:

- How much readily available funds are needed in order to maintain one's lifestyle?
- How should future generations benefit from the family's wealth?
- Should investments be made in ways that help the world?
- Where does one wish to live in the near future and later in one's life?
- What does one wish their legacy to be?

In some circumstances, some of the goals defined might conflict with others. When this happens, it may be worth ranking goals in order of importance or being flexible in terms of their timeline.

The investment strategy needs to be aligned with an investor's goals.
At UBS, we look at financial goals along the following dimensions:

- Covering short-term expenses
- Meeting lifetime goals
- Meeting objectives across generations

To help investors stay on track of achieving their goals, we organize their plans into three distinct but connected strategies: Liquidity. Longevity. Legacy. We name this approach the UBS Wealth Way.

> Create a wealth plan and stay invested for the long term.

UBS Wealth Way is an approach incorporating Liquidity. Longevity. Legacy. strategies that UBS Financial Services Inc. and our Financial Advisors can use to assist clients in exploring and pursuing their wealth management needs and goals over different time frames. This approach is not a promise or guarantee that wealth, or any financial results, can or will be achieved. All investments involve the risk of loss, including the risk of loss of the entire investment.

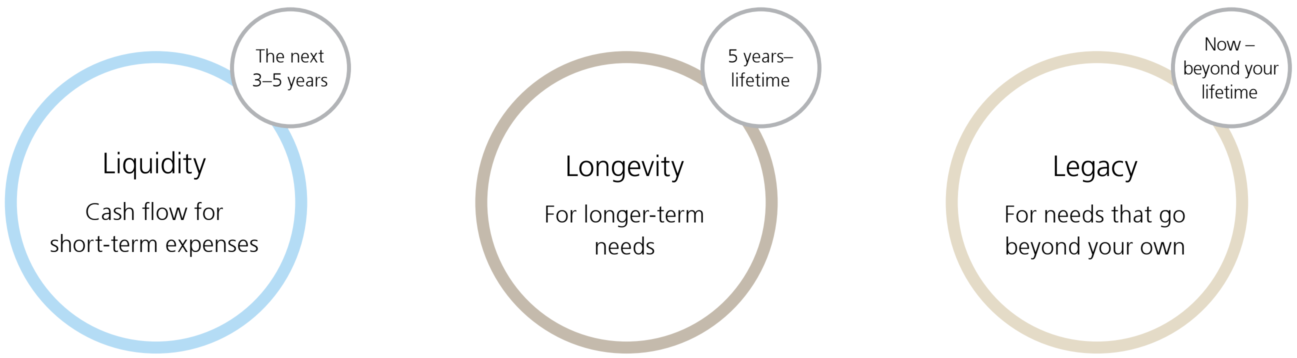
UBS Wealth Way

UBS Wealth Way considers every aspect of one's wealth, ensuring that each element of an investor's wealth context shares one razor-sharp focus: To help them and their family achieve their goals in the short term, long term, and for generations to come. This approach also provides peace of mind; even if one's Legacy strategy portfolio is highly volatile, investors can be confident and patient with the knowledge that the Liquidity strategy and Longevity strategy are sufficiently funded and prudently invested to help them meet their lifetime goals.

Liquidity
A strategy that focuses on helping investors meet the costs of short-term expenses and liabilities over the next three to five years. In this strategy, capital preservation is paramount.

Longevity
A strategy that ensures investors achieve their financial goals during their lifetime. The most appropriate portfolios for this strategy prioritize generating consistent growth and income through balance and diversification. The exact composition of the portfolio will depend on their financial situation, goals, investment preferences, and values.

Legacy
A strategy that looks after the assets that remain after one has achieved their lifetime goals and focuses on achieving goals beyond one's lifetime. For example, maximizing the wealth transferred to the next generation, or helping solve social and environmental problems. In this strategy, investors can seek to maximize after-tax growth potential without needing to worry about the sequence-of-returns risk of funding day-to-day expenses.



To help provide cash flow for short-term expenses

To help **maintain** your lifestyle
- Entertainment and travel
- Taxes
- Purchasing a home

For longer-term needs

To help **improve** your lifestyle
- Retirement
- Healthcare and long-term care expenses
- Second home

For needs that go beyond your own

To help **improve** the lives of others
- Giving to family
- Philanthropy
- Wealth transfer over generations

Time frames may vary. Strategies are subject to individual client goals, objectives and suitability. This approach is not a promise or guarantee that wealth, or any financial results, can or will be achieved.

Investment preferences and values

An important consideration when designing the optimal investment strategy is to identify an investor's investment preferences—for example, preference for sustainable investing or systematic investing (rule-based decision-making), preference for specific asset classes (e.g., no hedge funds), or home bias. We have developed a broad set of investment strategies to accommodate different styles and constraints as outlined on page 27.

Investing with purpose

Many investors want their investments to help the world. They do not see their business and investments as being separate from society. They see their wealth as an engine for doing good and put their skills and resources to work on solving the world's problems.

That is where sustainable investing comes in. Sustainable investing comprises two investment approaches: sustainability focused investing and impact investing. Both approaches enable families to do good while aiming to meet the families' financial goals. Sustainable investing provides access to nearly all types of assets, from equities and bonds to more non-traditional options like hedge funds and private markets.

Sustainability-focused investing – doing well by doing good

Sustainability-focused investing allows investors to invest in ways that reflect their values, without compromising the opportunity to achieve returns. Investors can implement a sustainable approach across their investment portfolio or focus on specific sustainability topics and goals. For example, investors might look for investments that reward sustainability leaders in their regions or sectors or they might invest in bonds that fund environmental or social projects.

Impact investing – driving measurable change

Impact investing gives families the opportunity to drive measurable and verifiable positive change while receiving a competitive financial return. Such investments aim to answer and measure one question: "Is my investment making an additional positive impact beyond what would have occurred anyway?" At UBS, we see this additional impact arising from the funds investors put into sustainable organizations—because those funds enable those organizations to grow and achieve more.

Impact investments usually focus on specific issues and geographies and aim for expected returns comparable to equivalent asset classes. For example, impact investments might focus on:

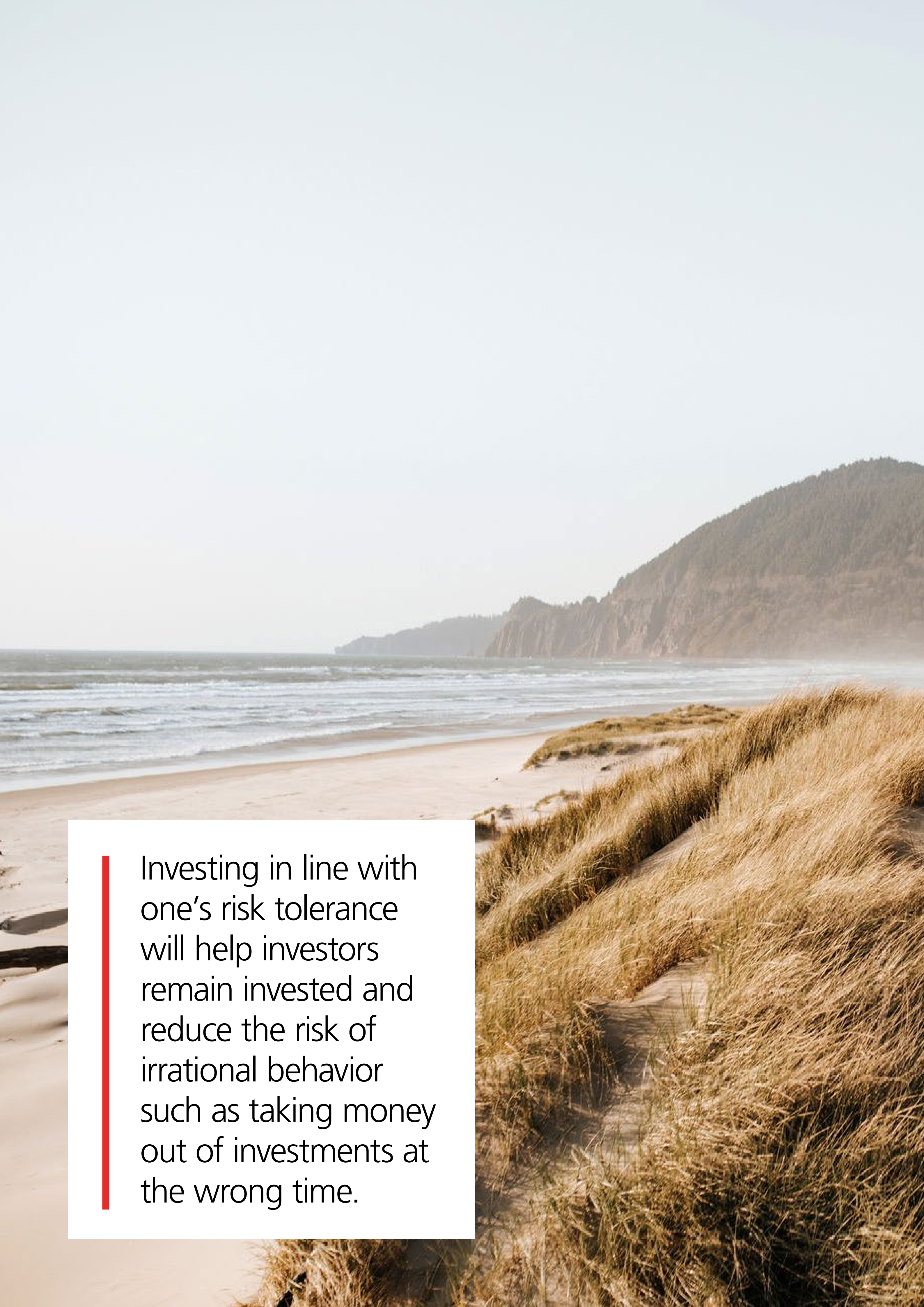
- investing in companies with products and services that aim to solve specific challenges;
- investing in multilateral development bank (MDB) bonds that support sustainable development.

Financial personality

Understanding one's attitude to risk is an important consideration that will impact the level of risk one wishes to take. Investors uncomfortable with how their portfolio performs in certain environments or reacts to unexpected events are less likely to stick with their financial plan. This is important because historically those who remain invested through bouts of short-term volatility benefit most from compounding returns over the long term. The financial personality is looked at an investor level so it relates to the aggregation of the different strategies of the UBS Wealth Way. We discuss in more detail on page 16 how risk tolerance is assessed and considered in the design of the optimal investment strategy.

Financial situation and total wealth

When making investment decisions, it is important to map out the totality of one's wealth. Assessing an investor's overall financial situation may affect the risk capacity that person has as well as the optimal allocation of assets—e.g., avoiding bulk risk / overconcentration. Investment advice needs to be holistic and take into consideration one's financial assets, real assets, collectibles, single stock concentrated positions, and charity aspirations. Managing each element as part of a big picture helps investors focus the total wealth on achieving their goals—and, in turn, improves their chances of reaching them.



Investing in line with one's risk tolerance will help investors remain invested and reduce the risk of irrational behavior such as taking money out of investments at the wrong time.

Part II

Define

Creating the optimal investment strategy for each investor

Defining the right strategy

In the following section, we explore how to design and construct the optimal portfolio for one's needs. One of the most frequent first questions investors ask is how much risk they should take.

How much risk and return?

Risk is a normal part of life. In the context of investing (where asset values can rise and fall), risk is about the chance of growing one's wealth while accepting potential fluctuations in the value of the wealth or even loss of wealth. And when investing, there is little reward without some risk.

Return and risk are intrinsically linked in investing. Generally, if one aims for higher returns, he/she will need to bear more risk. The objective of each long-term investor is twofold: 1) to find the risk/return mix that matches their needs and preferences, and, 2) to maximize the return for the risk taken.

Investors should neither assume risks beyond their comfort level nor miss out on potential returns. The aim is to incorporate an understanding of a suitable risk level. This is important because investors who remain invested through the long term, despite the downturns, benefit from the continuous effect of compounding—when investments generate earnings, which remain invested and generate their own earnings—in other words, generating earnings from previous earnings).

The appropriate risk level one needs to take depends on three parameters:

Risk tolerance	How comfortable you are with taking risks and experiencing the ups and downs of markets;
Risk capacity	Your ability to cope financially when markets fall;
Risk required	Your need to take risks to achieve your goals.

While we need to ensure that the right amount of risk is taken to protect your investment portfolio as best as possible. It is important to have a well-diversified and well-managed portfolio.

Risk tolerance

Understanding your financial personality
Each investor has a unique set of preferences and behavioral characteristics that leads to different comfort zones for their individual investment journeys. Correctly understanding one's comfort zone and subscribing to a disciplined investment approach help prevent irrational behavior and investment mistakes. It also helps strike the right balance between expected risks and returns, thereby neither assuming risks beyond your comfort zone nor missing out on potential returns.

Risk tolerance is affected by each person´s loss aversion, uncertainty aversion, and investment temperament.

Loss aversion
How willing and able is an investor to lose money in exchange for the chance of growing it? Someone with a high loss aversion would rather avoid investments that could lose modest amounts of money—even if they might deliver big returns. They may also avoid investments that can fluctuate wildly. At the other end of the spectrum are those with a low loss aversion. They're keen to receive big returns and don't mind if there are bumps in the road along the way.

Uncertainty aversion
Some investors prefer investing with certainty over uncertainty of outcome. For example, they might be willing to earn a smaller amount with a high degree of certainty than a higher payout with less certainty.

Investment temperament
Investment temperament measures the aversion to significant losses. Ask yourself: What level of losses would create a strong negative reaction? This amount varies by investor.

Risk capacity

Risk capacity is defined by one's financial situation (for example, its total assets, liabilities, income, and expenses) and how much risk they can afford to take. Is an investor in a position to cope with or afford to lose money if markets fall?

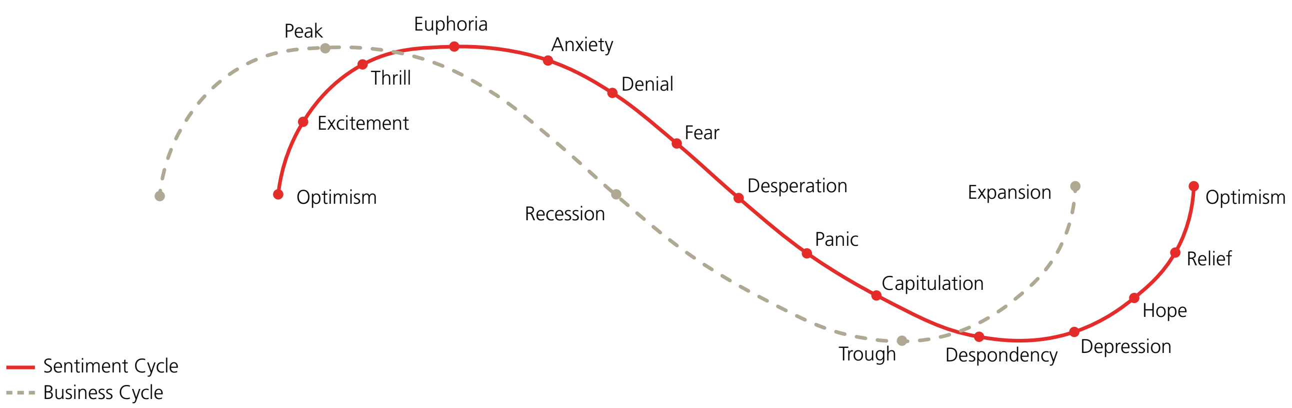
Risk required / Return target

Furthermore, one should also consider the returns required and therefore the risk required to meet one's goals with a high probability. This may mean taking more risk than one expects.

The Longevity strategy (as introduced with the UBS Wealth Way framework) is focused on helping investors meet their goals over their lifetimes. Its aim is to ensure they are invested in such a way that they have a high probability to meet those objectives. This means using *shortfall risk* as a measure of risk to identify the appropriate allocation. Next, we look at how to measure risk.

Figure 2

The path to higher returns can feel like a roller-coaster ride, allowing for emotions to affect investment decisions



Source: UBS AG

Strategies are subject to individual client goals, objectives and suitability.

Measuring risk and return

There are various ways to measure investment risk. Below, we introduce a few of the main ways that are important when establishing an investment strategy.

Volatility

Volatility is a measure of the variability of investment returns. Said differently, it measures how much investment returns fluctuate over a certain period of time. Investments with low volatility are considered less risky. It is a fundamental measure of risk for professional traders and risk managers. It is often applied in modern financial theory and used when constructing portfolios. However, the measure does not distinguish between rises and falls in investment values and typically underestimates extreme changes in markets.

To get a clearer picture of risks, it is a good idea to use volatility alongside other measurements. Historical measures of negative and extreme changes in investments can be useful, such as maximum drawdown or time to recovery. This is especially true for illiquid asset classes like private equity, debt, infrastructure, or real estate. Appraisal valuation and less frequent, potentially time-lagged reporting of these assets leads to relatively low reported volatility figures that do not necessarily capture all relevant risks.

Drawdown measure

A maximum drawdown is the biggest loss an investor would have experienced if they had invested when assets were at their most expensive—then sold them when their value hit rock bottom. So, the maximum drawdown measure indicates the maximum possible loss if you had bought at the highest point and sold at the lowest.

The measure often links in with time to recovery. This shows how long it previously took for the investment's value to climb from its earlier lows to its previous high. It is worth knowing that drawdowns happen in many assets, even high-quality ones. And drawdowns do not necessarily result in losing money. This will only happen if:

- one needs to sell the investment during the drawdown, for example, because they need more spending money;
- the investment does not recover its value, for example, because it simply was not a great investment in the first place (bad wine does not improve with age).

Shortfall risk measure

This refers to the risk that one fails to achieve their goals or fails to preserve their wealth because the returns from their investments are too low. The measure can help investors work out whether an investment is likely to reach their goals and gives an indication of the risk that wealth does not fall below a certain amount. A limitation of the measure is that it only focuses on the negative side of an investment. For example, two investments could have similar levels of shortfall risk, but one may have more potential to deliver bigger returns.

One should not forget that historical risk measures only show you what has happened to an investment in the past and cannot predict what might happen in the future.

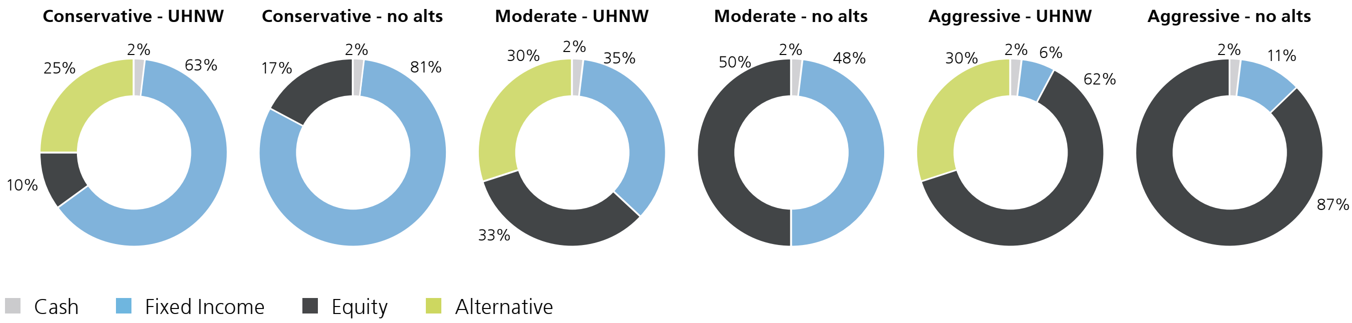
Return

Return is measured in several ways. It can be shown as an average return per year or as a total (cumulative) return. There are two main ways of calculating an average return per year; either as a simple (arithmetic) return or as a compound (geometric) return. The former one simply adds each individual annual return and divides that by the number of years—example: if year one is –50% and year two is +200% this gives a cumulative total return of 50% and a simple average return p.a. of 75%. The compound return, on the other hand, expresses how much the investment grew on average per year to get to its final value, if each year had the same return. Using the example above, the average compound return p.a. is 22%.

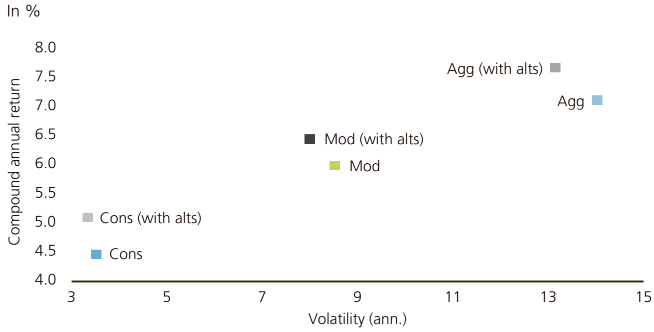
The compound return is always less than the simple return because of the effect of volatility. Said differently, an investment cannot compound/grow as much if, to take three steps forward, it takes two step back. The power of compounding comes from higher returns combined with lower volatility.

Figure 3

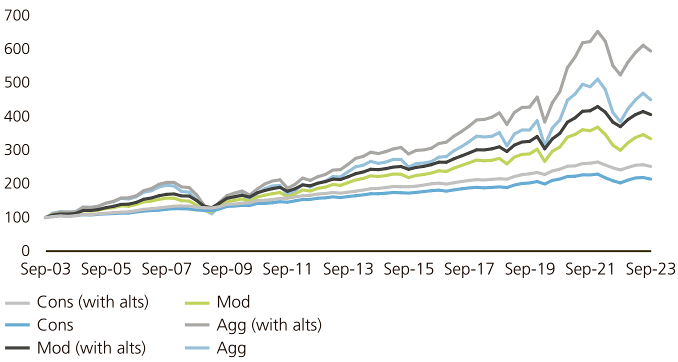
You can see how different asset allocations fare in terms of volatility, historical performance, maximum historical drawdown, and time to recovery.



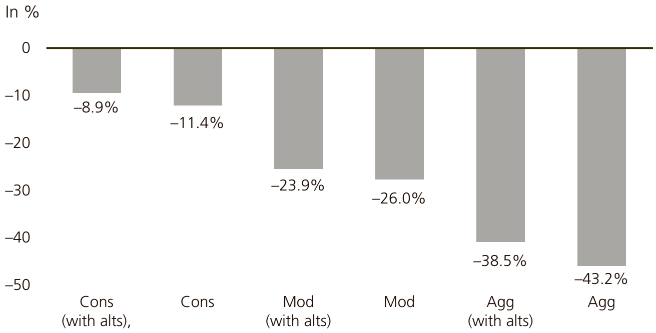
Estimated return & risk - strategic CMAs



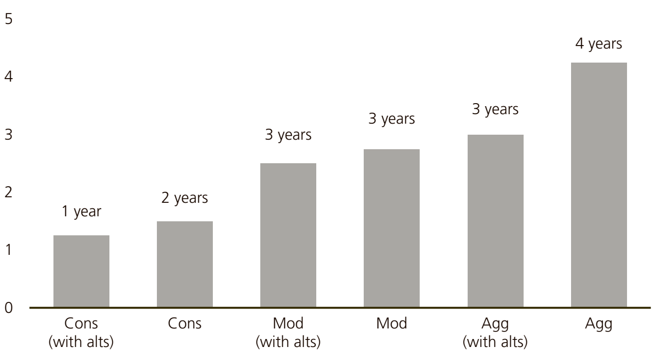
Simulated growth of $100



Maximum drawdown



Maximum time under water



Note: Quarterly data covers period from 01 Oct 2008 - 30 Sept 2023.
Source: Bloomberg, Cambridge Associates, UBS

Defining the reference currency

Many wealthy investors' finances, businesses and liabilities are often spread across different countries. The "reference currency" is the one used to manage, monitor, and measure the assets. It is important to determine the best reference currency for each asset.

What are the factors that can help an investor choose an overall reference currency for their entire investment portfolio?

- The currency in which most of their assets are denominated
- Their main place of residence
- The currency of their main income streams
- The currency of their expenses and liabilities
- The currency of possible future investments
- Diversification

Investors should also consider whether their reference currency choice might:

- Limit the choice of assets they can invest in. Difficulty in comparing performance and results across banking relationships
- Complicate their reporting tasks. Create artificial biases for or against foreign assets
- Concentrate risks in their portfolio. Accurately represent the portfolio situation for future planning.

Reducing currency risk

Currency hedging

Investing in foreign assets considerably broadens the investment universe and the opportunity for diversification. However, it comes with the risk of losses due to unfavorable changes in exchange rates—if investors are forced to convert underperforming currencies. This risk can be reduced by investing in "currency forwards" (a contractual agreement in which investors commit to buying a currency at a locked-in price at a future date). This strategy is known as "currency hedging."

Currency markets are typically volatile. Because this volatility is usually higher than that of fixed income investments, the impact of hedging currency risk can be sizable in a portfolio with a large share of fixed income assets. Currency hedging can also work well in investment portfolios mostly made up of equities, although the impact is less dramatic.

But what about boosting portfolio returns? Can currency hedging help? This depends on the price of hedging, which is closely linked to the differences in interest rates between the two currencies. If the price of hedging is lower than the expected swings in foreign currency, hedging is favorable from a returns perspective. As a result, whether an investor opts for currency hedging can depend on how confident they are in exchange-rate forecasts.

Reducing risk through currency hedging can free up investors to add riskier assets to their investment portfolios. Some currencies, referred to as risk-on currencies, tend to perform well when markets are rising, but poorly when markets fall. Hedging is typically more advantageous when investing in equity markets denominated in "risk-on" currencies like the Australian dollar, Canadian dollar, Swedish Krona that tend to exacerbate stock price declines. Currency hedging is less urgent for those who invest in "risky" currencies, like the Japanese yen and the Swiss franc. That's because "risky" currencies typically perform better when markets fall. So, they already hedge risk by being able to offset declines in other investments.

Defining liquidity needs

Investors often fail to consider how much liquidity (cash or assets readily available to be converted into cash) they might need—whether that is to pay for unexpected expenses (for example medical bills) or to cover planned purchases (such as buying a property or business). Often, investors tend to hold more liquidity than they need, which means they can miss out on the opportunity to grow that money by investing it.

Designing a Liquidity strategy

Investors can tackle their cash management needs with a Liquidity strategy (see "UBS Wealth Way" on page 10). A good Liquidity strategy consists of enough resources to cover around three to five years of net portfolio withdrawals (spending minus income from guaranteed sources such as pension or annuity income). By assessing the short-term cash flow and by setting aside resources dedicated to meeting these needs regardless of short-term market conditions, the goal is to create a buffer between cash needs and market returns—leading to peace of mind. It is important to remember that while cash may sound appealing and safe, it creates great opportunity cost and does not protect against wealth erosion from inflation.

To provide readily available money, the Liquidity strategy may include elements like cash, cash alternatives (short-term investments like certificates of deposit, money-market funds, and short-duration bonds), and borrowing.

In a nutshell, when designing a Liquidity strategy, it is important to:

- Work out how much liquidity investors may need to meet future expenses and financial commitments.
- Consider their investment preferences and different attitudes toward market risk, liquidity risk, and credit counterparty risk).
- Look at the current rates of return available for liquidity products.
- Diversify risk by choosing various liquidity products, for example strategies from different providers that run for different lengths of time.

> Keeping a significant amount of wealth in cash may sound like a safe option. However, in another way, it is riskier—because its purchasing power is being eroded by inflation.

Strategies are subject to individual client goals, objectives and suitability.

Illiquidity as a growth driver

The UBS Wealth Way's Liquidity strategy introduced earlier covers investors' cash flow needs over the next few years. That means any assets invested can be converted quickly into cash with little or no loss of value. When we talk about illiquid investments, however, we refer to investments that can only be sold with a significant time lag or with a large discount to current value. Investments in private equity (non-publicly traded companies) should not be relied upon for meeting short- or medium-term spending needs. Private equity assets usually commit an investor to providing funds for a business over multiple years. The investor typically does not invest everything upfront. Instead, the private equity fund manager can "call" cash at any time when the investment opportunity arrives (known as "capital calls"). Hence, investors will need to make sure they have enough liquidity to cover their commitments at any point in time. We do not recommend keeping capital commitments in Liquidity strategy investments, which prioritize capital preservation, because this would dilute the return on private market investments. Instead, we recommend investing any capital commitments into a liquid balanced portfolio in line with the strategy's risk level, which you can liquidate as needed to meet capital calls. Investors who are worried about the risk of locking in public market losses to meet capital calls should consider reserving some of their borrowing capacity for this purpose.

How much illiquidity is appropriate depends very much on the specific situation of an investor. The time horizon affects the level of risk an investor is prepared to take as well as liquidity requirements. In principle, longer-time horizons allow for more illiquidity and more risk, as investors have more time to recoup losses.

> A multigenerational time horizon allows for illiquid investments as a growth driver.

So, the amount of less liquid assets and the time horizon of the Longevity strategy depends on the investor's cash flows and goals. For example, if a significant outflow is expected in the shorter term, then the amount of illiquidity should be carefully evaluated. The Legacy strategy (read more on "UBS Wealth Way" on page 10), however, has a multigenerational time horizon, which allows for investments in illiquid assets as well as more risk as short-term volatility is less relevant to the overall health of the portfolio. At UBS, we find that a typical investors with low spending needs may allocate up to 30% of their Longevity strategy to private equity without suffering liquidity problems, and up to 40% for the Legacy strategy.

Borrowing liquidity

An additional source of liquidity would be borrowing money, for example using the investment portfolio (including illiquid assets, like property) as collateral. However, one should bear in mind that when times are tough and markets are down, there may be limits on the amounts one can borrow and the value of loans taken in the past may be reduced. (read more on page 27).

Strategies are subject to individual client goals, objectives and suitability.

> Diversification helps to reduce risk in an investment portfolio over time and is one of best strategies to help achieve long-term goals.

Defining your investment universe

The term "investment universe" simply refers to the range of assets an investor wishes to invest in, whether that is equities, bonds, private equity, real estate, and so on.

To define their investment universe, investors need to go through the following steps:

- Understand the nature of different asset classes (groups of investments with similar characteristics).
- Consider each asset class and the aspects that drive their performance (such as earnings, interest rates, inflation, and growth). Start with so-called "risk-free" assets (like cash), then work your way up to riskier, but potentially more rewarding assets, like equities.
- Look at the expected returns and risks of each asset—and compare how those assets might behave in different economic environments and relative to each other (this measure is called "correlation").

The choice of investment universe also depends on the investor's needs. For example, in case of a large need for stable and regular cash flows, the investor may need to devote more of the investment portfolio to assets that provide an income, such as fixed income products, dividend-paying equities, and debt-financing solutions.

Diversifying investments

"Diversification" is one of the sharpest tools in an investor's kit. It involves spreading money—and risks—across lots of different asset classes, rather than placing all one's hopes on one or a handful to achieve goals. Investing in one or a small amount asset classes—or even worse, individual assets—leaves portfolios vulnerable to significant losses if they drop in value. The most powerful argument in favor of diversifying is that historically no asset class consistently performs better than others. Since it is extremely difficult to identify what the best-performing assets will be, diversification enables investors to maximize the chance of returns by spreading their wealth across different assets. As Figure 4 indicates, there is no asset class that consistently outperforms all others.

Nobel Prize-winning economist Harry Markowitz demonstrated that a simple asset allocation between equities and bonds for example reduced behavioral risks and delivered superior returns. He concluded that "diversification is the only free lunch in investing." In the decades following his work, diversification has become one of the main investment strategies. Diversified portfolios are more efficient in terms of their risk-return characteristics (referred to as the "Sharpe Ratio").

So investors should consider:

- Putting their money in different asset classes – such as liquidity or cash, fixed income, equities, commodities, real estate, and alternative investments (see table on page 27).
- Investing in different countries – there's less risk if just one country's economy falls behind.
- Buying different assets within an asset class (a group of similar investments). For example, buying shares in various companies, and buying shares in companies from different industries.

Figure 4

Historical annual returns in order of best to worst. Historically, no asset class regularly outperforms all others

2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023 YTD	Key
78.5%	26.9%	21.3%	18.2%	38.8%	15.4%	10.3%	21.3%	37.3%	9.2%	36.4%	38.5%	35.4%	8.6%	25.0%	Cash
58.1%	25.5%	14.9%	17.5%	34.8%	15.3%	8.9%	17.5%	30.2%	8.1%	30.5%	28.4%	27.6%	6.3%	8.9%	US Govt FI - Int
40.5%	20.9%	13.2%	17.4%	33.5%	13.5%	8.3%	17.3%	25.0%	7.8%	26.5%	20.0%	25.4%	2.8%	7.1%	US Govt FI - Long
37.2%	18.9%	12.3%	17.3%	32.5%	13.4%	5.7%	13.8%	22.9%	7.3%	25.5%	18.3%	25.2%	1.5%	6.0%	US Muni FI - Short
31.8%	16.7%	9.7%	17.3%	22.8%	13.2%	5.5%	11.4%	19.9%	1.8%	22.0%	17.1%	22.6%	-3.6%	5.2%	US Muni FI - Int
29.8%	15.8%	9.2%	16.8%	20.7%	13.0%	4.5%	11.2%	18.5%	1.7%	18.4%	12.9%	14.8%	-4.1%	5.0%	US Muni FI - Long
27.2%	15.7%	8.4%	16.3%	14.8%	10.0%	3.8%	11.2%	15.2%	1.4%	17.5%	11.9%	13.9%	-6.0%	4.3%	US Corp FI - Inv Grade
23.4%	15.5%	7.3%	15.5%	12.7%	9.6%	1.8%	10.2%	14.6%	1.2%	15.0%	11.8%	12.8%	-6.6%	3.9%	US Corp FI - High Yield
22.0%	15.1%	7.0%	15.3%	9.1%	8.7%	1.5%	9.9%	14.6%	0.3%	14.4%	9.4%	11.3%	-7.5%	3.8%	EM FI - Hedged
20.0%	15.1%	4.8%	14.5%	9.1%	7.5%	1.2%	9.6%	13.7%	-0.1%	13.8%	9.1%	10.2%	-11.2%	3.7%	EM FI - Local
19.7%	12.2%	4.4%	14.0%	7.4%	7.4%	1.2%	7.1%	10.3%	-1.5%	13.5%	7.8%	5.3%	-11.7%	2.5%	US Large-Cap Growth
17.2%	10.6%	4.2%	11.3%	1.0%	6.4%	0.0%	6.9%	8.6%	-2.1%	11.1%	6.2%	3.2%	-12.6%	1.8%	US Large-Cap Value
16.0%	10.2%	2.6%	10.1%	0.0%	6.2%	-0.8%	5.6%	8.6%	-2.3%	10.4%	6.1%	1.0%	-14.5%	1.8%	US Mid-Cap
13.2%	9.7%	0.4%	10.1%	-2.0%	4.9%	-0.8%	5.4%	8.2%	-4.3%	10.3%	5.6%	0.4%	-15.3%	1.8%	US Small-Cap
9.9%	8.7%	0.1%	9.4%	-2.2%	3.0%	-1.1%	1.4%	7.5%	-4.7%	10.3%	5.5%	0.0%	-15.6%	0.0%	Int'l Dev Equity
5.8%	8.5%	-1.5%	6.4%	-2.6%	2.5%	-2.4%	1.2%	6.2%	-6.2%	9.3%	5.3%	-1.1%	-17.3%	-0.1%	EM Equity
1.2%	7.8%	-1.8%	5.7%	-4.7%	1.8%	-3.8%	1.0%	5.8%	-8.3%	9.0%	3.1%	-1.8%	-17.8%	-1.6%	Hedge Funds
0.1%	4.0%	-4.2%	4.6%	-5.3%	0.0%	-4.4%	0.9%	4.8%	-9.1%	7.7%	2.8%	-2.5%	-20.1%	-1.8%	Private Equity
-4.8%	2.2%	-5.3%	3.6%	-6.0%	-2.2%	-4.6%	0.3%	2.2%	-11.0%	7.5%	2.7%	-3.0%	-20.4%	-2.0%	Private Credit
-7.4%	1.1%	-12.1%	2.0%	-8.6%	-4.9%	-14.9%	0.0%	1.9%	-13.8%	4.0%	1.8%	-4.7%	-25.0%	-2.4%	Private Real Estate
-22.9%	0.1%	-18.4%	0.1%	-9.0%	-5.7%	-14.9%	-0.1%	0.8%	-14.6%	2.2%	0.5%	-8.7%	-29.1%	-7.1%	Private Infrastructure

Source: Bloomberg, Cambridge Associates, UBS. Data as of 30 Sept 2023.

Constructing your investment portfolio

The right investment portfolio will be a combination of the strategic asset allocation (SAA), tactical asset allocation (TAA), and instrument selection.

These are the three core decisions in investing and can be thought of as the investment process that needs constant monitoring. At each step multiple evaluations and decisions are needed to have an overall successful portfolio. Most private investors will delegate all or part of this work to experts to build a best-in-class portfolio. As we've outlined above the essential input from the investor is to provide the right guidelines for this process to deliver results that match one's investment needs and preferences.

Strategic asset allocation (often abbreviated to "SAA")

This involves setting target allocations for the assets in an investment portfolio, and will reflect investors' financial situation, tolerance to and capacity for risk, values, and goals. The investment manager may need to rebalance the allocations periodically, should they move away from the original targets. The strategic asset allocation usually has the biggest impact on a portfolio's overall performance. Figure 5 provides an example of a strategic asset allocation as selected by other wealthy families.

At UBS, we typically follow these steps when creating SAAs for investors:

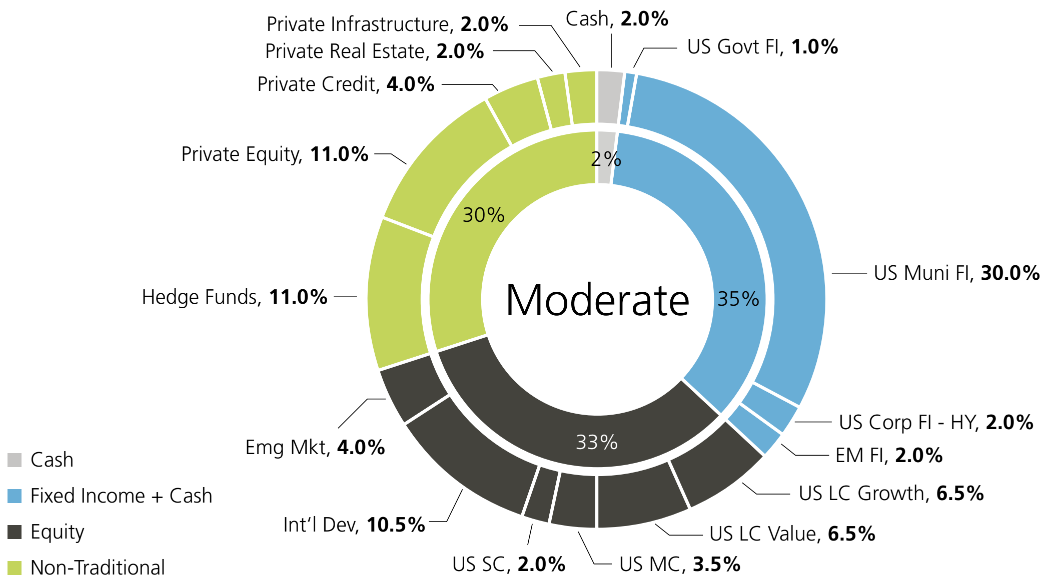
- Define a group of asset classes (investment universe) that reflects a wide range of risk and return characteristics. We only include asset classes that offer a "risk premium" (a return that acts as a form of compensation for investors who have taken the extra risk) or offer opportunities to hedge risk (reducing risk by owning assets that aim for opposing outcomes).
- Analyze and forecast the long-term risk and return outlook for each asset class.
- Understand all the factors about the family that are pertinent to its investment choices. For example, do hedge funds and illiquid assets fit with the family's needs, goals, and risk tolerance? What is the investor's tax bracket and corresponding asset location (i.e. nontaxable trust, taxable account, etc.).
- Construct the right investment portfolio for the family: One that is diverse and has a favorable (after-tax) expected return for a certain level of risk.

When constructing investment portfolios, we recommend investors:

- **Do not hold more cash over the long run than necessary for reaching your goals,** so that more of the wealth can go to work in return-generating investments.
- **Consider investing in a wide range of asset classes,** to reduce the portfolio's exposure to risks and benefit from diversification.
- **Consider adding quality longer-term fixed income products to portfolios** that mainly comprise equities.
- **Invest globally,** considering such factors as "market capitalization" (the total value of a company's shares of stock) and "capital asset pricing model" (often abbreviated to CAPM).
- **Regularly rebalance** to remain in the appropriate risk/return portfolio.
- **Consider hedging the portfolio's exposure to foreign currency risks,** if there is not a strong case for a major currency misvaluation. This avoids a source of risk that is not systematically rewarded.
- **Consider the tax efficiency of each investment and the optimal asset location** in order to maximize after-tax wealth relative to financial goals and risk tolerance.

Figure 5

Example of Strategic Asset Allocation: UBS Moderate SAA



Source: UBS AG

Tactical asset allocation (often abbreviated to "TAA")

This involves the investment manager temporarily deviating from the strategic asset allocation to take advantage of certain situations and opportunities in markets. Once the investment manager has achieved their goal, they then switch back to the original strategic asset allocation. An example of a tactical position could be to go underweight equities vs. bonds.

Our TAA investment process involves four key stages:

- Establishing our macroeconomic views across our base case, and upside and downside scenarios, including considering what our quantitative models and proprietary networks are telling us.
- Identifying opportunities within and across asset classes (equities, government bonds, credit, foreign exchange, commodities), and within regions as well as finding potential portfolio hedges.
- Translating ideas into proposed portfolio adjustments across our various portfolio strategies.
- Having our views challenged by a panel of external experts.

Instrument selection

Selecting instruments represents the implementation phase of portfolio construction. These instruments will need to match an investor's SAA and TAA strategies. Investment instruments come in many forms such as stocks, bonds, real estate or derivatives and are often pooled into funds.

Funds can offer efficient diversification into a particular asset class via "passive" index funds which invest across a particular market—for example an S&P 500 fund will invest in most companies of the S&P 500 index capturing a broad US equities exposure. Funds can also be managed by "active" managers who aim to beat the market by selecting the right securities at the right time—these can be classic mutual funds or ones with more sophisticated strategies such as Hedge Funds or Private Equity funds. Other funds may be focused on direct indexing in order to harvest losses against gains to create additional after-tax returns, something known as tax-loss harvesting to produce tax alpha.

Selecting the right securities or the right fund manager out of thousands of options available requires time and skill for due diligence and monitoring, a task often delegated to experts. These decisions will fit within the investment process requiring review and adjustments as markets and one's circumstances change.

Choosing the right strategy for you

Beyond our traditional core investment strategies, we have developed different strategies to meet different investor preferences. Our endowment/institutional-style strategies endeavor to preserve the real value of assets across generations, our income-oriented strategies seek additional returns through term and credit premiums, dividends, and options, and our systematic allocation strategy dynamically adjusts portfolio equity allocations based on a quantitative assessment of the risk environment. We have also created a sustainable investing strategy, which aims to deliver a commensurate risk-return profile to traditional strategies, but with a focus on assets that fulfill sustainability objectives. The different investment frameworks can be combined to meet investor's needs and preferences.

Choosing the right investment strategy to fit your goals.

Global strategic asset allocation
Our classic approach, aiming to offer an attractive risk / return trade-off through diversification

Endowment/institutional style
A higher allocation to alternatives, locking up capital in exchange for higher risk-adjusted returns

Systematic allocation
A dynamic, quantitative, strategy aiming to achieve performance and reduced drawdowns

Global credit opportunities
A fixed income focused strategy utilizing an expanded fixed income universe to enhance yield

Regional focus
Portfolio strategies with a higher allocation to local assets

Sustainable investing
A strategy focused on assets which align with key sustainability metrics and goals

Modular investing
Portfolio construction with different thematic building blocks

For illustrative purposes only. Past performance is not an indication of future return.

Borrowing to meet your goals

Borrowing is not always prudent, but it can be a valuable resource that can be part of a long-term strategy. Borrowing is an especially attractive alternative to holding excessive cash or selling assets with long-term growth potential. After all, cash is increasingly eroded by inflation, and a diversified portfolio with a healthy allocation stocks and other growth assets is the most reliable way to protect the real value of savings in a higher-inflation environment.

We look at debt primarily as a tool to help meet three main objectives:

To provide a "bridge loan" or secure liquidity

When choosing how to fund the Liquidity strategy, investors may consider setting aside some of their safe borrowing capacity as a complement to cash and fixed income. Borrowing to finance spending may seem irresponsible, but it can make sense for an investor where the alternative is selling assets with a high expected return, or holding excessive cash reserves. A securities-backed loan or line of credit, which can give investors access to cash at short notice, can be a relatively low-cost way of funding spending needs without sacrificing longer-term returns. The proceeds can be used for any purpose, from real estate purchases anywhere in the world to university tuition.

To increase diversification

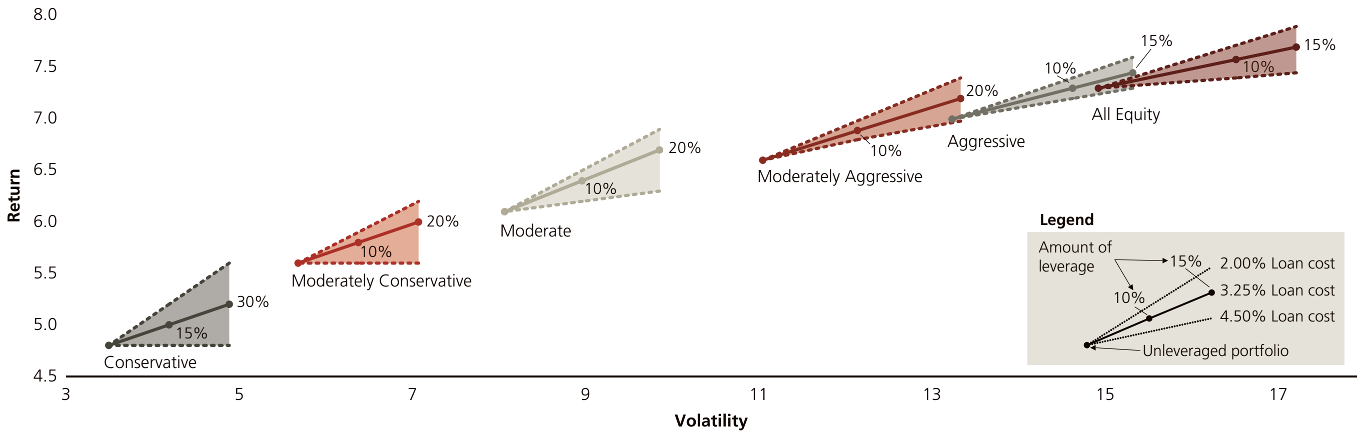
This applies if one's net worth is overly concentrated—perhaps even in a single asset. This is often the case for entrepreneurs or high-level executives, whose wealth can be highly focused prior to selling a business or tied up in restricted company stock.

In such a situation, investors may want to consider borrowing against their concentrated illiquid assets to fund a diversified portfolio in their Longevity and Legacy strategies. By adding investments that are less correlated to the bulk of your net worth—or select "hedging" strategies to help protect against risks to the portfolio—the careful use of leverage can help improve the risk-adjusted return on one's net worth, and add assets that can succeed even if the concentrated investments struggle.

Figure 6

Prudent leverage may improve returns more than adding to risk assets

Expected risk & returns after various borrowing costs and amounts of leverage, in %



Source: UBS. For illustration purposes only.

Strategies are subject to individual client goals, objectives and suitability.

To increase return potential

"Leveraging" involves obtaining a loan against an investment portfolio. Investors then invest the borrowed money to boost returns or diversify to reduce risk in the portfolio. But while leveraging can boost returns, it can also raise risks significantly, particularly when rates go up or the value of the assets that serve as collateral goes down. And if markets fall, you might lose the money you invested in your portfolio. So it is important to:

- Understand the reasons for taking a loan
- Consider how the loan might affect the risk/return expectations
- Work out the right level of leverage in one's portfolio, in terms of an appropriate amount to borrow and the potential benefits for your portfolio.

Regularly rebalance one's portfolio

Reviewing and rebalancing

Typically, the performance relative to defined goals is measured, where the goals are expressed through a performance target or financial indexes. Furthermore, checks should be in place to make sure all investment guidelines have been followed as defined in the investment policy statement—such as the minimum/maximum weightings for asset classes, sustainability guidelines, or risk-taking. It is important that portfolios are rebalanced on a regular basis to maintain the desired risk/return level. Rebalancing can also pose an opportunity to tax-loss harvest for more efficient after-tax return. Finally, costs should be monitored to make sure they are in line with the outcome received.

Once these checks have been made, they need to be documented and the findings reported to the decision makers Feedback should be relevant and timely, and should support further decision making.

Closing remarks

We hope our publication has provided a clearer picture about investing and our key investment principles. Investors should remember investing is a journey, one that is more successful with careful planning, clear direction, and good stewardship.

Having established and implemented an investment strategy, investors will have to also continuously monitor the performance and rebalancing of their portfolios to stay on track. Every so often, it is helpful to take a step back and reconfirm that the overall investment strategy still holds in light of new aspirations. An investor's portfolio strategy should evolve along with their changing goals and circumstances.

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