CIO's views on bond yields, equities, and balanced portfolios. (Shutterstock)

# Ask CIO: Bond yields, equities, and balanced portfolios

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**Bond yields have fallen and equity markets have rallied in recent weeks as softer US economic data reignited hopes for Federal Reserve policy easing later this year. What should investors expect from here? Read on for the CIO view on this and other key questions.**

**Is it time to lock in bond yields?**

Bond yields have come off from their year-to-date highs as softer US economic data reignited hopes of Federal Reserve policy easing this year. The 10-year US Treasury yield has fallen to around 4.4% at the time of writing, from 4.7% in late April. We think yields can fall further this year as inflation slows, the US economy cools, and the Federal Reserve cuts rates. In our base case, we see the US 10-year yield declining to 3.85% by the end of the year.

We therefore recommend that investors lock in yields on quality bonds and recommend diversification against equity market risks. Investors can benefit from current attractive yields and potential capital gains if yields fall (as we expect). Beyond individual bonds, active and diversified fixed income exposure can provide investors with a convenient way to realize the full return potential of the asset class while managing global interest rate, credit, and concentration risks.

**What's next for US equity markets?**

The S&P 500 has recovered its April losses, helped by solid first-quarter earnings and lower bond yields. While a range of economic and geopolitical risks remain, we think solid economic and earnings growth, the likelihood that interest rates will still fall, and rising investment in AI should create a supportive backdrop for equities for the rest of this year. In our base case, we see the S&P 500 ending the year around 5,200, but think the index could rally toward our upside scenario target of 5,500 if we continue to get good news around inflation and AI spending.

We continue to favor quality stocks, and rate the US technology, health care, and industrials sectors as most preferred. We also see value in small- and mid-cap stocks.

**Why invest in a balanced portfolio now?**
Market sentiment has improved amid a positive first-quarter earnings season, but inflation, monetary policy, and geopolitical uncertainties remain. We continue to believe that holding a balanced portfolio—including equities, bonds, and alternatives—is the most effective way for investors to preserve and grow wealth over time.

We expect balanced portfolios to deliver positive returns this year, with potentially smoother returns thanks to diversification. A balanced and diversified approach can also help navigate fast-changing market narratives. We still see reinvestment risks to holding excess cash given our view that the Fed will likely ease policy by 50 basis points this year, with additional rate cuts likely in 2025.

Balanced portfolios can potentially lower swings in wealth. A portfolio with a 60/40 split between stocks and bonds has historically been less volatile than one composed solely of stocks. Indeed, a 60/40 portfolio has only delivered a negative return over a five-year horizon on 5% of occasions, and never over a 10-year horizon (compared with 12% and 5% of the time for equity-only portfolios).

Including alternative investments in balanced portfolios ensures investors tap more sources of return than just stocks and bonds. Investors considering alternative assets like hedge funds and private market investments should be aware of additional risks including illiquidity and longer lock-up periods.

For more, please see the UBS House View Briefcases.

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## Non-Traditional Assets

**Non-traditional asset classes are alternative investments that include hedge funds, private equity, real estate, and managed futures (collectively, alternative investments).** Interests of alternative investment funds are sold only to qualified investors, and only by means of offering documents that include information about the risks, performance and expenses of alternative investment funds, and which clients are urged to read carefully before subscribing and retain. An investment in an alternative investment fund is speculative and involves significant risks. Specifically, these investments (1) are not mutual funds and are not subject to the same regulatory requirements as mutual funds; (2) may have performance that is volatile, and investors may lose all or a substantial amount of their investment; (3) may engage in leverage and other speculative investment practices that may increase the risk of investment loss; (4) are long-term, illiquid investments, there is generally no secondary market for the interests of a fund, and none is expected to develop; (5) interests of alternative investment funds typically will be illiquid and subject to restrictions on transfer; (6) may not be required to provide periodic pricing or valuation information to investors; (7) generally involve complex tax strategies and there may be delays in distributing tax information to investors; (8) are subject to high fees, including management fees and other fees and expenses, all of which will reduce profits.

Interests in alternative investment funds are not deposits or obligations of, or guaranteed or endorsed by, any bank or other insured depository institution, and are not federally insured by the Federal Deposit Insurance Corporation, the Federal Reserve Board, or any other governmental agency. Prospective investors should understand these risks and have the financial ability and willingness to accept them for an extended period of time before making an investment in an alternative investment fund and should consider an alternative investment fund as a supplement to an overall investment program.

In addition to the risks that apply to alternative investments generally, the following are additional risks related to an investment in these strategies:

- Hedge Fund Risk: There are risks specifically associated with investing in hedge funds, which may include risks associated with investing in short sales, options, small-cap stocks, “junk bonds,” derivatives, distressed securities, non-U.S. securities and illiquid investments.
- Managed Futures: There are risks specifically associated with investing in managed futures programs. For example, not all managers focus on all strategies at all times, and managed futures strategies may have material directional elements.
- Real Estate: There are risks specifically associated with investing in real estate products and real estate investment trusts. They involve risks associated with debt, adverse changes in general economic or local market conditions, changes in governmental, tax, real estate and zoning laws or regulations, risks associated with capital calls and, for some real estate products, the risks associated with the ability to qualify for favorable treatment under the federal tax laws.
- Private Equity: There are risks specifically associated with investing in private equity. Capital calls can be made on short notice, and the failure to meet capital calls can result in significant adverse consequences including, but not limited to, a total loss of investment.
- Foreign Exchange/Currency Risk: Investors in securities of issuers located outside of the United States should be aware that even for securities denominated in U.S. dollars, changes in the exchange rate between the U.S. dollar and the issuer’s “home” currency can have unexpected effects on the market value and liquidity of those securities. Those securities may also be affected by other risks (such as political, economic or regulatory changes) that may not be readily known to a U.S. investor.