Strategic: Diversify with alternatives

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Why? 1) We see low stock correlation and high return dispersion as continued drivers of hedge fund returns and should support performance in 2026. 2) Private equity should also be supported by increased distributions and exits as central banks continue easing and fiscal policy remains pro-growth. 3) While selectivity is required, we believe direct lending still offers attractive income and diversification for underallocated investors.

Source: Pexels

Video: Diversify with alternatives

Hedge funds

The environment of low stock correlation and high return dispersion—drivers of strong hedge fund returns since 2010—remains in place and should support performance in 2026. We believe that equity market neutral strategies can enhance portfolios due to their ability to generate returns in both rising and falling markets, while limiting directional exposure. We also see appeal in global macro and multi-strategy funds, given their flexibility to benefit from economic trends and risks like persistent inflation, trade tensions, or debt sustainability concerns. Meanwhile, the resurgence in M&A activity is creating fresh opportunities for merger arbitrage strategies.

Private equity

With central banks easing and fiscal policy remaining pro-growth, we expect increased distributions and exits, supporting private equity returns. In a world of lower rates and high public market valuations, we focus on middle-market, value-based buyouts, complex carveouts, and secondary funds, with a preference for regional diversification in Europe and Asia to mitigate local risks. The supportive macro backdrop and favorable liquidity conditions should help private equity managers navigate elevated valuations and concentrated market leadership.

Select direct lending

Private credit headlines highlight the need for quality and selectivity. While tighter spreads and Fed rate cuts have moderated returns, we believe direct lending still offers attractive income and diversification for underallocated investors. Risks are mainly contained to lower-middle-market borrowers; senior, sponsor-backed loans to larger, less cyclical companies remain resilient, in our view. Careful sizing and manager selection are essential, and those with outsized allocations should consider diversifying into other alternative investments.

Private real estate and infrastructure

Reliable, inflation-linked cash flows and exposure to structural trends make these appealing portfolio assets in our view. We favor digital infrastructure, renewables, logistics, living sectors, and data centers, with a preference for core and core-plus assets that derive a greater share of returns from income rather than capital appreciation.

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.

Appendix

Risk information
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