(UBS)

Building a solid financial core with the right asset class mix is essential

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Stocks drifted lower and the US dollar hovered at the lowest level in two months as investors await the releases of key US economic data this week that would shape expectations for the Federal Reserve's next moves.

Our view remains that the Fed is likely to cut interest rates by another 25 basis points in the first quarter of next year, providing a favorable backdrop for risk assets. But with volatility likely to pick up as markets assess fresh data, we think investors should revisit some of the foundational principles in constructing a resilient portfolio.

Build a strong core portfolio with a suitable asset mix, and rebalance regularly. Just like building a strong core at the gym is key to balance and strength, building a solid financial core with the right asset class mix is essential, in our view. For most investors, equities should form the core of a growth-oriented portfolio, typically comprising 30-70% of total assets, while a 15-50% allocation to fixed income is a common benchmark. Investors looking to diversify even further can consider an allocation to alternative assets such as hedge funds, private markets, and infrastructure, based on individual risk tolerance, time horizon, income needs, and liquidity requirements. Additionally, regular and disciplined rebalancing back toward a long-term allocation target is critical in keeping the core strong over the long term.

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Include an allocation to gold as a hedge against market and geopolitical risks. While gold does not generate income and its protective behavior is not guaranteed in every downturn, we still believe a modest allocation—of up to a mid-single-digit percentage of total assets—can enhance diversification and buffer against systemic and geopolitical risks. With elevated debt and political uncertainty, we think the current strong demand from central banks and global investors is likely to continue in the coming year.

Consider structured investments to manage volatility and enhance yield. Investors can consider substituting some direct equity exposure with capital preservation strategies, which are designed to help capture most of the potential gains in an asset while limiting potential losses. While returns on such strategies may be capped in strong markets, they can also reduce drawdowns. The flexibility of capital preservation strategies may allow investors to tailor the degree of capital preservation and participation in market gains. Yield-generating structured investments may also become more attractive as interest rates drop.

So, while we retain a positive outlook for markets into 2026, we believe investors should build a strong portfolio to navigate potential volatility with greater confidence.

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