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Diversify with alternative investments (by Daniel Kalt)

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To optimally diversify an investment portfolio to weather possible stock market fluctuations and in view of the meager yields on Swiss franc bonds, hedge funds can be a good option, offering an attractive risk/return profile, in our view.

It is still early days for 2025, but we can already see where the journey could take us this year—with the challenges for Swiss investors clearly apparent. We believe that the markets will trend upwards this year, but we do not assume that the increase in equities will be linear. Quite the opposite: In view of the turbulent geopolitical landscape, we must be prepared for the fact that there will be swings that could be quite severe and strain the nerves of many investors. We believe the most effective medicine that can help is to optimize the diversification of your portfolio across asset classes, regions, and sectors.

Traditionally, high-quality Swiss franc bonds have taken on the role of diversifier in a balanced portfolio—i.e., divided roughly 50/50 across equities and bonds. However, a quick look at the franc yield curve is enough to see why CHF bonds are currently ill-equipped for the job. With a yield-to-maturity of 0.4% on the 10-year Swiss government bond and around 0.25% on the 5-year one, these fixed income investments are very likely to rack up losses when accounting for currency devaluation through inflation. Diversification is therefore likely to have a rather expensive price tag.

As a possible way out and replacement for the less attractive bonds, investors could therefore consider alternative asset classes to diversify a portfolio. These include private market investments such as private equity or private debt, as well as broadly diversified investments in infrastructure, which tend to yield highly stable and positive returns in real terms. Specific hedge fund instruments seem even more suitable to us. Carefully selected hedge fund strategies have risk/return characteristics that make them a suitable addition or even a substitute for Swiss franc bonds, in our view. Hedge funds are

usually able to generate steady, positive value gains over long investment periods, and they are also interesting from an income tax perspective. At the same time, they usually have price setbacks that are significantly smaller than for equities, and their portfolio function is often closer to bonds than to equities. This feature makes hedge funds a valuable building block in an optimally diversified strategic asset allocation, in our view. In our asset management strategy, we allocate 12% to hedge funds in a portfolio with a balanced risk profile, alongside 50% for equities, 5% for liquidity, and 33% for bonds.

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