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Seek diversified income

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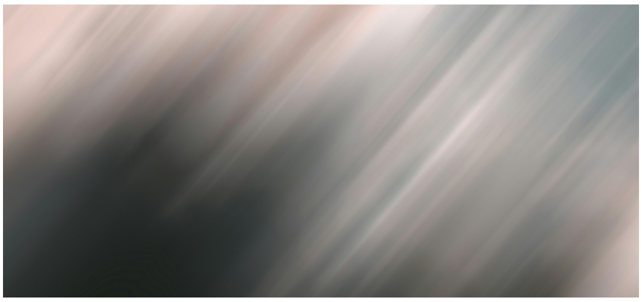
Author: Sagar Khandelwal, Strategist, UBS Switzerland AG

- **Why?** (1) Following recent sell-offs in government bonds on fears of higher-for-longer oil prices and more hawkish central banks, the case for quality bonds as a source of diversification and income have strengthened, especially those with short-to-medium maturities. (2) A diversified income portfolio should include a mix of strategies, including via equity income and yield-generating strategies. And (3) investors with well-diversified and appropriately sized allocations can also look to selective approaches to private credit and alternatives like private infrastructure as an additional source of yield and diversification.
- **Why now?** (1) Elevated levels of uncertainty strengthen the appeal of a diversified stream of income in a portfolio context. (2) Short- and medium-maturity quality bond yields in USD, EUR, and GBP have arguably overshot on higher oil prices, and could fall if even higher prices push down growth expectations. And (3) in the current environment, equity strategies and a careful allocation to private credit can help boost diversification and income generation.



Given tight credit spreads and concerns over government debt, we advocate for a diversified approach to generate yield. Source: Marcel Strauss_Unsplash

Video: [Seek diversified income]

Seek out quality

We believe the recent increase in benchmark government bond yields in USD, EUR, and GBP provides an opportunity for investors looking to lock in elevated yields and diversify portfolios. We do not expect central banks to change their rates hurriedly in response to the rise in energy prices, and even if energy prices stay higher for longer, yields could fall over the medium term if investors begin to price recession and central bank rate cuts. After many years of strong equity performance relative to bonds, investors may have an opportunity to rebalance toward bonds, to bring allocations back into line with long-term plans, and to help manage potential equity risks. We like looking for opportunities in quality government bonds with short-to-medium maturities, especially in the US, Eurozone, and the UK. While Swiss government debt yields remain low and inflation muted, we still think some allocation to government debt can make sense for adverse economic scenarios in which government debt tends to rally and yields fall in anticipation of monetary easing.

Build a resilient fixed income core

While we have an overall bias for quality, we do not exclude holding some exposure to higher-beta segments such as emerging markets, high yield, or subordinated debt. Amid elevated geopolitical and sector-specific risks, investors should avoid overexposure to any single segment of the credit market. However, in the context of a well-diversified fixed income portfolio, an allocation to riskier credit can help improve overall returns.

Be selective in private credit and alternatives

Private credit remains a source of yield, but rising defaults in the lower-middle market and liquidity mismatches highlight the need for a focus on quality—senior secured, sponsor-backed loans in non-cyclical sectors are preferred. We expect further differentiation within private markets as refinancing pressures build and cross-asset correlations evolve. Diversification across private credit, hedge funds, private infrastructure, and real estate can help stabilize income and reduce portfolio volatility, particularly as traditional correlations shift. In our view, selectivity and ongoing due diligence are critical in navigating the current landscape.

Global asset class preferences definitions
The asset class preferences provide high-level guidance to make investment decisions. The preferences reflect the collective judgement of the members of the House View meeting, primarily based on assessments of expected total returns on liquid and commonly known indices, House View scenarios, and analyst convictions over the next 12 months. Note that the tactical asset allocation (TAA) positioning of our different investment strategies may differ from these views due to factors including portfolio construction, concentration, and borrowing constraints.
Attractive: We consider this asset class to be attractive. Consider opportunities in this asset class.
Neutral: We do not expect outsized returns or losses. Hold longer-term exposure.
Unattractive: We consider this asset class to be unattractive. Consider alternative opportunities
Note: For equities, we have a five-tier rating system with two additional preferences
Most Attractive: We consider this asset class to be among the most attractive. Investors should seek opportunities to add exposure.
Least Attractive: We consider this asset class to be among the least attractive. Seek more favorable alternatives opportunities.
When equities are included with the other asset classes in the three-tier rating system, we collapse “Most Attractive” with “Attractive” and “Least Attractive” with “Unattractive.”

Appendix

Risk information
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