

Does borrowing make sense in 2025?

UBS House View Briefcase

Vincent Heaney, Strategist, UBS AG London Branch; **Matthew Carter**, Strategist, UBS AG London Branch; **Jon Gordon**, Strategist, UBS AG Hong Kong Branch; **Thomas Lee Ruiz**, Strategist, UBS Switzerland AG; **Christopher Swann**, Strategist, UBS Switzerland AG; **Daisy Tseng**, Strategist, UBS AG Singapore Branch

Key message

The Fed has resumed its easing cycle, cutting rates by 25 basis points in September in response to a softening US jobs market. Elsewhere, the global rate-cutting cycle has continued in recent months. Falling borrowing costs may raise the appeal of borrowing strategies as a tool to manage liquidity, diversify, boost returns, and avert ill-timed asset sales. Borrowing can form part of a prudent financial plan, although the risks should be carefully considered.

House view

01 The global easing cycle from central banks has continued, raising the appeal of borrowing strategies.

- Weaker-than-expected US labor market data for August led the Federal Reserve to cut rates by 25bps in September, with projections for a further 50bps of rate cuts by the end of this year.
- The Swiss National Bank has already bought its policy rate down to zero and kept policy on hold at last week's meeting.
- The Bank of England cut its policy rate by 25 basis points to 4% in August.

02 Against this backdrop, prudent borrowing can play multiple roles that support financial goals.

- It may provide immediate funds without selling assets, avoiding taxable gains and transaction costs.
- Investors looking to fund new private market investments may find it more efficient to borrow against diversified bond portfolios rather than hold excess cash to meet capital calls.
- Borrowing to invest can yield higher long-term returns if expected returns exceed borrowing costs.

03 With the right risk management, borrowing strategies may grow in appeal this year.

- Borrowing comes with risks that investors must be willing and able to bear. Investors should compare loan interest rates with expected returns; if returns are lower, borrowing may not be viable.
- A borrowing strategy's robustness must be assessed against market risks and spending plans. Key factors in choosing a borrowing strategy include loan duration, refinancing potential, and interest rate expectations.

New this week

Federal Reserve Chair Jerome Powell emphasized last week that there is no "risk-free path" for US monetary policy, highlighting the challenge of balancing inflation with a softening labor market. Meanwhile, the Fed's preferred inflation gauge, the personal consumption expenditures (PCE) price index, for August remained above the central bank's 2% target.

One liner

Subject to careful planning and risk management, borrowing may help manage liquidity, improve portfolio diversification, help navigate currency swings, and boost return potential in the year ahead.

Did you know?

- Two of the 12 voting members of the Fed's policy-setting committee dissented in favor of a rate cut at July's meeting—the first time since 1993 the committee has seen multiple dissents.
- Historical analysis, while no guarantee of future performance, suggests borrowing to invest in diversified portfolios may bear fruit. CIO analysis of 24-month rolling returns for a 60/40 portfolio of US stocks (S&P 500) and US government bonds between 1998 and August 2024 finds such a portfolio would have generated returns ahead of US dollar borrowing costs on nearly 75% of occasions (and by an average 3.4% each year).

Investment view

We believe a falling-rate environment in 2025 may accommodate proactive borrowing approaches, with judicious use of debt as a tool for achieving financial goals. By leveraging debt wisely, investors have the potential to enhance portfolios, manage risks, and improve the likelihood of achieving long-term financial goals.

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