Goldman Sachs

"An unexpected asset could now be the best 60/40 portfolio hedge"

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Christian Mueller-Glissmann: An unexpected asset is now likely to be the best hedge for 60/40 portfolios.

Since the pandemic, the correlation between equities and bonds has risen substantially. That means holding a 60/40 portfolio has gotten more risky because bonds are less likely to buffer equities when they fall. The situation has improved a bit recently. But has stirred risk of stubbornly high inflation. This could cause the Fed to hold off on significant rate cuts. And that would be bad news for bonds, of course. But it could also weigh on economic growth and equity valuations eventually. That's not our base case. But it's definitely something multi-asset investors are worried about.

One good hedge in this situation could be the US dollar which would benefit from higher US rates for longer and in case of a risk of shift across assets. Our research tells us when the equity/bond correlation is positive, a 60/40 portfolio and the dollar tend to be negatively correlated. For nervous 60/40 investors, the dollar could be a good portfolio addition.