

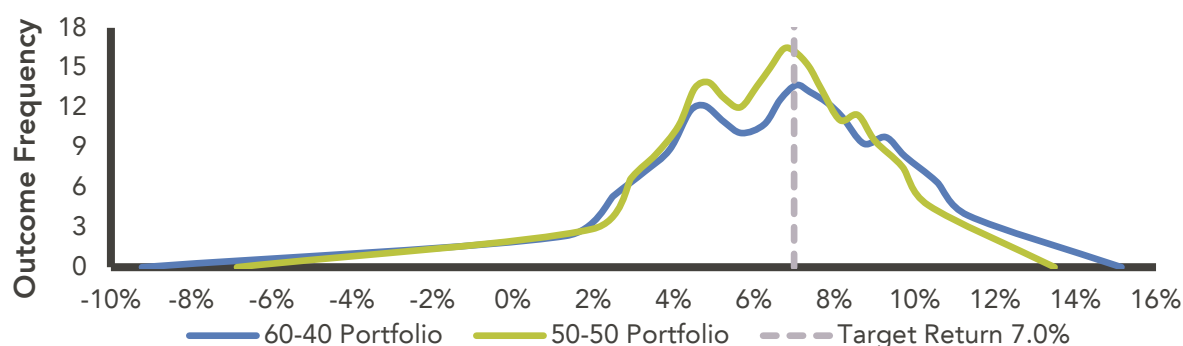
# Chart of the Week

March 1, 2023

## De-risking at a Lower Price

NIC SOLECKI, ASSOCIATE RESEARCH ANALYST

Expanding allocations to fixed income may provide some stability in the face of uncertainty and market risks



	60-40 Portfolio	50-50 Portfolio
Avg. Annualized 10 Yr. Return	6.47%	6.26%
Avg. Annualized 10 Yr. Volatility	9.93%	8.38%
Avg. Return/Avg. Volatility	0.65	0.75

Source: Marquette Associates Asset Allocation Software as of December 31, 2022; distribution in chart is result of Monte Carlo simulation of 1,000 trials. The 10-year return assumptions are simulated capital market returns. It is important to note that these values are present output from the software simulations, and not deterministic views of future capital market performance.

In 2023, managing uncertainty and risk is top of mind as markets continue to grapple with inflation, a potential recession, and ongoing geopolitical conflict. Increasing allocations to investment-grade fixed income may be one way investors can better position their portfolios to navigate the current environment.

The chart above illustrates return outcomes for two portfolios based on a Monte Carlo simulation of portfolio returns over a forward-looking ten-year investment horizon. As a baseline, the 60-40 portfolio consists of a 60% allocation to U.S. equities (the S&P 500) and a 40% allocation to investment-grade fixed income (the Bloomberg U.S. Aggregate). Alternatively, the 50-50 portfolio shifts an incremental 10% from equities to IG fixed income. Benefitting from today's elevated yields and lower volatility inherent to fixed income, the 50-50 portfolio projects a greater concentration of outcomes centered around the 7% target rate of return with less volatility than the 60-40 baseline portfolio. Although the expected return decreased slightly, portfolio risk decreased by roughly 1.5 percentage points, creating a more favorable risk-adjusted return. As described in Marquette's latest white paper, [The 60/40 Portfolio Revisited: Back from the Dead?](#), the rise in yields in 2022 has made fixed income a more attractive investment relative to prior years and reduced the expected return differential between stocks and bonds. For many investors, the 60/40 portfolio seems poised to meet their long-term risk and return goals, but for those looking to remove additional risk from their portfolios, the new yield environment makes further de-risking more of an option than it has been over the past decade. ■

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This document may contain hypothetical performance that is intended for institutional and/or those investors with access to the resources to independently analyze this information and who have the financial expertise to understand the risks and limitations of these types of presentations.

**Criteria Used and Assumptions Made in Calculating Hypothetical Performance: Asset Allocation Analysis**

The return and risk projections included in this document are based on a Monte Carlo simulation of macroeconomic factors, which are used to model monthly return outcomes of capital markets. The simulations are created by a powerful economic scenario generator that simulates the future performance of the capital markets and macro-economy and are updated quarterly; the underlying models are calibrated based on the long-term historical record, so that they will reproduce the kinds of volatility and stress scenarios that have been observed over the 20<sup>th</sup> and 21<sup>st</sup> centuries. The models are linked and correlated so that the behavior of different asset classes and economic variables is consistent within each random scenario.

Total portfolio returns are time weighted, using underlying asset class returns. This assumes that either passive or active management will match or exceed the returns of the indices. Returns are annualized returns based on the average 10-year returns generated in the 1,000 Monte Carlo simulations. The returns for the total portfolio are calculated by the following formula:

$$Ret_{t=i} = [(MV_{t=i} - MV_{t=i-1}) - NetCashFlow_{t=i} - Fee_{t=i}] / [MV_{t=i-1} + NetCashFlow_{t=i}]$$

**Risks and Limitations of Using Hypothetical Performance in Making Investment Decisions**

While the asset allocation model incorporates average correlations between asset classes, this can vary depending on what is happening in the market. This is especially true when financial markets are in flux. For example, while we expect international equities to decline in a similar manner to domestic equities, the possibility exists — though unlikely — for the next bear market to be concentrated in the U.S. Every market downturn has its own unique nuances, so while these scenarios demonstrate what might happen and how they could affect a portfolio, it is critical that the investor understands the unpredictable nature of financial markets and that any downturn will not exactly match the generic scenarios and investment decisions should not be made based on hypothetical scenarios. Models cannot capture every potential outcome across all economic scenarios. While re-balancing is incorporated in the construction of each portfolio, the model does not reflect transaction costs associated with re-balancing.

The sources of information used herein are believed to be reliable. Marquette Associates has not independently verified all of the data used herein and its accuracy cannot be guaranteed. Estimates and projections of financial market performance do not guarantee future performance. Since the model used to create this report relies on market data, results will vary depending on the date of the study. Past results do not guarantee future results and are subject to change as more data becomes available.

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## PREPARED BY MARQUETTE ASSOCIATES

180 North LaSalle St, Ste 3500, Chicago, Illinois 60601    PHONE 312-527-5500  
CHICAGO BALTIMORE MILWAUKEE PHILADELPHIA ST. LOUIS    WEB [marquetteassociates.com](http://marquetteassociates.com)

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