

Liquid alternatives: The death of 60/40 and rebirth of hedge funds. Is this time truly different?

June 2025

The case for allocating to liquid alternatives is more compelling in today's environment amid persistent inflation, structurally higher interest rates, unstable equity-bond correlations, and heightened geopolitical risk.

This contrasts with the relatively benign investment environment of the post-GFC pre-COVID-19 era which was characterised by low inflation, declining interest rates, stable equity markets, and a low bond-equity correlations.

Isabella Milazzo, Consultant, Frontier Advisors, noted this was an “era where the 60:40 portfolio was effective and the potential benefits of liquid alternatives were muted”.

However, in today's environment, “we've seen the breakdown of the equity-bond correlation, which undermines one of the key pillars of traditional portfolio construction”.

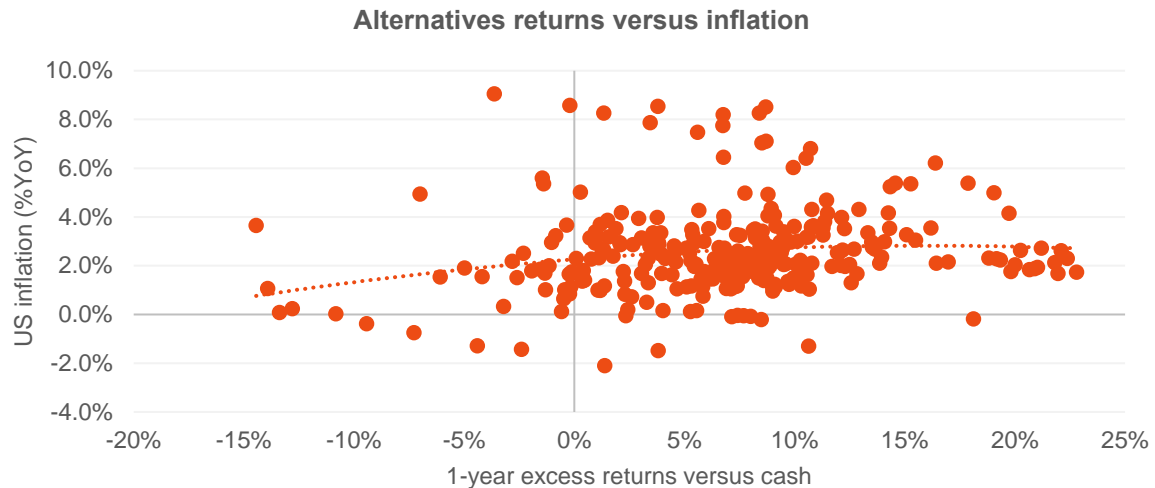
“Add to that the backdrop of rising geopolitical tensions and global fragmentation, and we're left with a market landscape that is defined by greater uncertainty, higher volatility, and greater dispersion both across and within asset classes”.

Despite these inherent challenges, Milazzo suggests that “these conditions create a broad and deep opportunity set for liquid alternative strategies to extract alpha”.

The three experienced panellists agreed the world has shifted to a structurally more challenging backdrop where the outcome of the traditional 60:40 portfolio is less certain, but there is opportunity for liquid alternatives to supplement bonds in providing diversification and defensiveness.

Chenelle de Rozario Harding, Consultant, NSW Treasury Corporation, spoke to the breakdown of the equity-bond correlation. Harding spoke to her experience in helping allocators construct an alternatives portfolio with a lot of breadth to emulate a bond portfolio, with the aim of providing consistent returns over a long period of time. Harding suggested this breadth works to ensure a consistent return stream that is both diversifying and attractive from a return-seeking perspective.

For Arthur Bengasino, Acting Head of Opportunities and Real Assets, TelstraSuper, the most important aspect of a liquid alternatives portfolio is understanding both the current environment, and the objectives of the allocation. Bengasino explained the “volatility of the equity-bond correlation is more important than the correlation itself”.



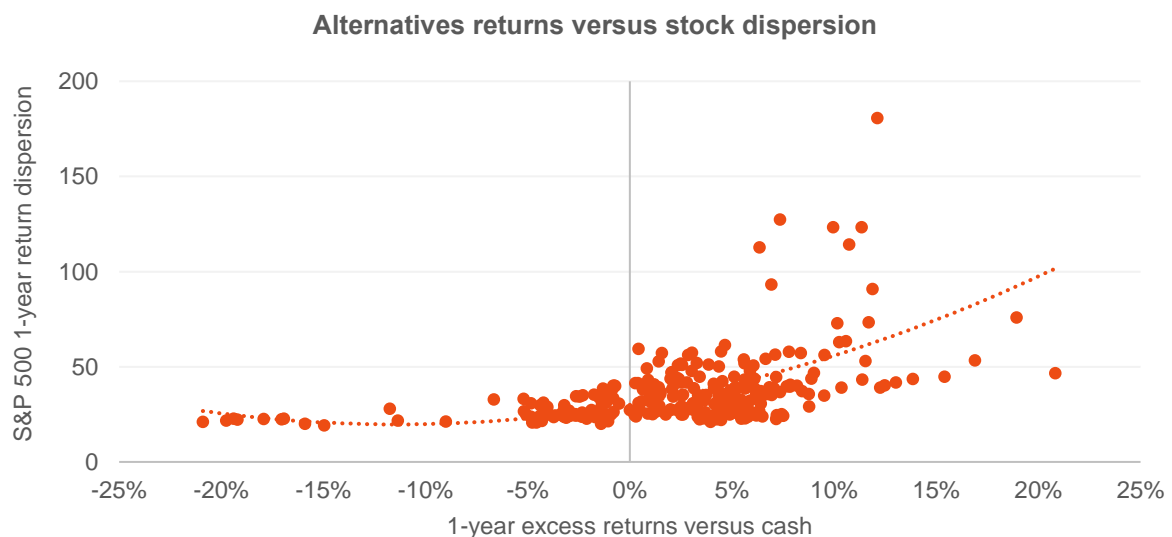
Source: Frontier Advisors, Datastream. Monthly data from 30 June 2000 to 31 May 2025. Alternatives returns are represented by the EurekaHedge Multi-Strategy Hedge Fund index.

A key element in today's environment is the expectation of structurally higher inflation. Milazzo highlighted the resiliency of liquid alternatives in varying inflationary environments.

Bengasino expects liquid alternative strategies to perform well in inflationary environments due the decoupling in the underlying data that occurs. He explained long-short macro-oriented strategies benefit most from this dynamic.

Iain McMahon, Frontier's Head of Defensives and Alternatives, concurred with Bengasino albeit noted he observes no strong relationship between inflation and the excess returns of liquid alternative strategies suggesting performance is resilient (as shown in the chart above).

The panel finished with a discussion on how the environment today leads to great security level dispersion, noting dispersion as a key driver of liquid alternative returns.



by

Source: Frontier Advisors, Datastream. Monthly data from 30 June 2000 to 31 May 2025. Alternatives returns are represented by the EurekaHedge Multi-Strategy Hedge Fund index.

Next steps

Frontier can assist clients in an designing a liquid alternatives allocation that appropriately balances diversification, defensiveness, and performance to help bolster total portfolio resiliency in today's uncertain market environment. Get in touch with Isabella Milazzo, Consultant in Frontier's Defensive and Alternatives Team at imilazzo@frontieradvisors.com.au for more information.