
*Suitable for wholesale/sophisticated investors*

# Alternative diversifiers: do you still rely on bonds?

In a more uncertain macro environment characterised by high debt levels, demographic headwinds and sluggish productivity, traditional diversifying assets such as bonds may no longer help create resilient portfolios. Even historically, bonds may have hurt diversification more often than they helped, especially during rising inflation.

We believe investors should explore diversifying assets that can have a higher certainty of providing resilience on a forward-looking basis, including volatility strategies.

## Bonds often fail to deliver resilience when needed

Investors often rely on bonds to do the heavy lifting in diversifying a balanced portfolio. In return for this, investors accept lower expected returns than from growth assets.

In reality, bonds have often done a poor job providing diversification when it mattered. This was especially the case during inflationary shocks, such as the environment that may lie ahead.

To illustrate, Figure 1 shows rolling 1-year real returns for the S&P 500 index and ten-year US bonds since 1940.

The shaded areas indicate the 19 times that 1-year US real equity price returns were worse than -10%. US bond real returns were also negative in 14 of these 19 times (red shading), further harming portfolios. The fact that bonds generally helped during the large equity falls in the 2000s likely reflects the overall disinflationary environment at that time.

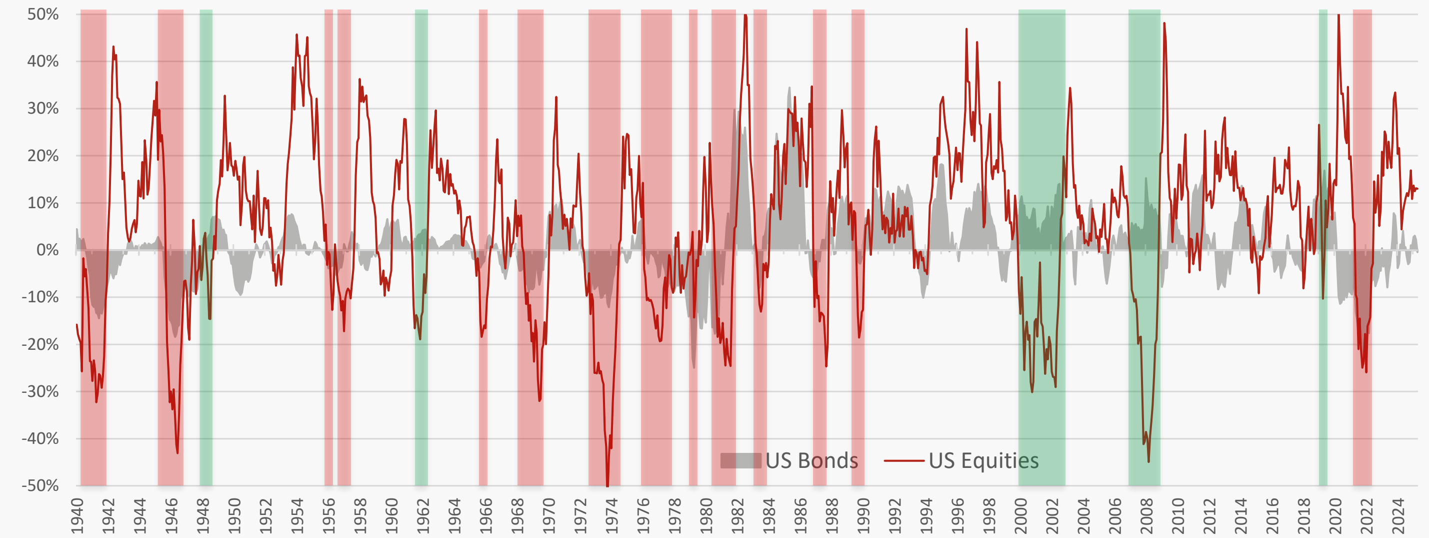
> *"bonds failed to provide strong diversification in 14 out of 19 large equity falls since 1940*

## Key to resilient portfolios

A macro-aware approach to building resilient portfolios includes understanding the nature and behavior of diversifying assets in different market environments.

For example, volatility strategies can deliver diversification based on the tendency of volatility to go up during equity falls. Meanwhile, trend following strategies can capture momentum across different assets during equity turbulence. Several other alternative diversifiers can similarly provide portfolio resilience in a different and potentially more reliable way to fixed income assets.

Figure 1: Rolling 1-year real returns for US equities and 10-year US bonds. Shading shows US equity price returns worse than -10%. Red shading indicates US bond returns were also negative at some point; green shading indicates US bond returns were positive.




*US equity returns are the S&P500 Index price return (SPX Index). Bond returns are the estimated performance of 10-year US Treasurys.*
*Source: SouthPeak, Bloomberg, Goldman Sachs, US Treasury*

# Alternative diversifiers: aim for more reliable resilience with better returns

Arguably, a more uncertain macro environment compared to the last decades has already started to emerge. With this in mind, it may be useful to look at the performance of bonds and some alternative diversifiers in the last four periods of equity turbulence; Feb-Mar 2020, Apr-Sep 2022, Mar-Apr 2025 and Mar 2026.

To keep the analysis simple, we will look at CTA strategies (using the SG CTA index), hedge funds (using the HFRX index with daily liquidity) and volatility (using SouthPeak's systematic long and short volatility strategies).

We have not included Illiquid assets such as private credit because we believe a lack of mark-to-market is often confused with genuine diversification for many of these assets.

As shown, bonds only helped in 2025 and performed poorly as a diversifier in both 2022 and 2026. Meanwhile, CTAs added positive returns in 2022 but underperformed in 2025 and went sideways the other two periods. Our hedge fund index did not impress during any of the turbulence. Conversely, the volatility strategies performed well in all four periods.

Given the macro uncertainty ahead, we think investors should explore an allocation to a variety of alternative diversifiers, including volatility strategies.

| Scorecard | Bonds | CTAs | HFs | **Vol** |
|---|---|---|---|---|
| Covid-19 | o | o | – | + |
| Mid-2022 | – | + | – | + |
| Tariffs | + | – | o | + |
| M-E War | – | o | – | + |

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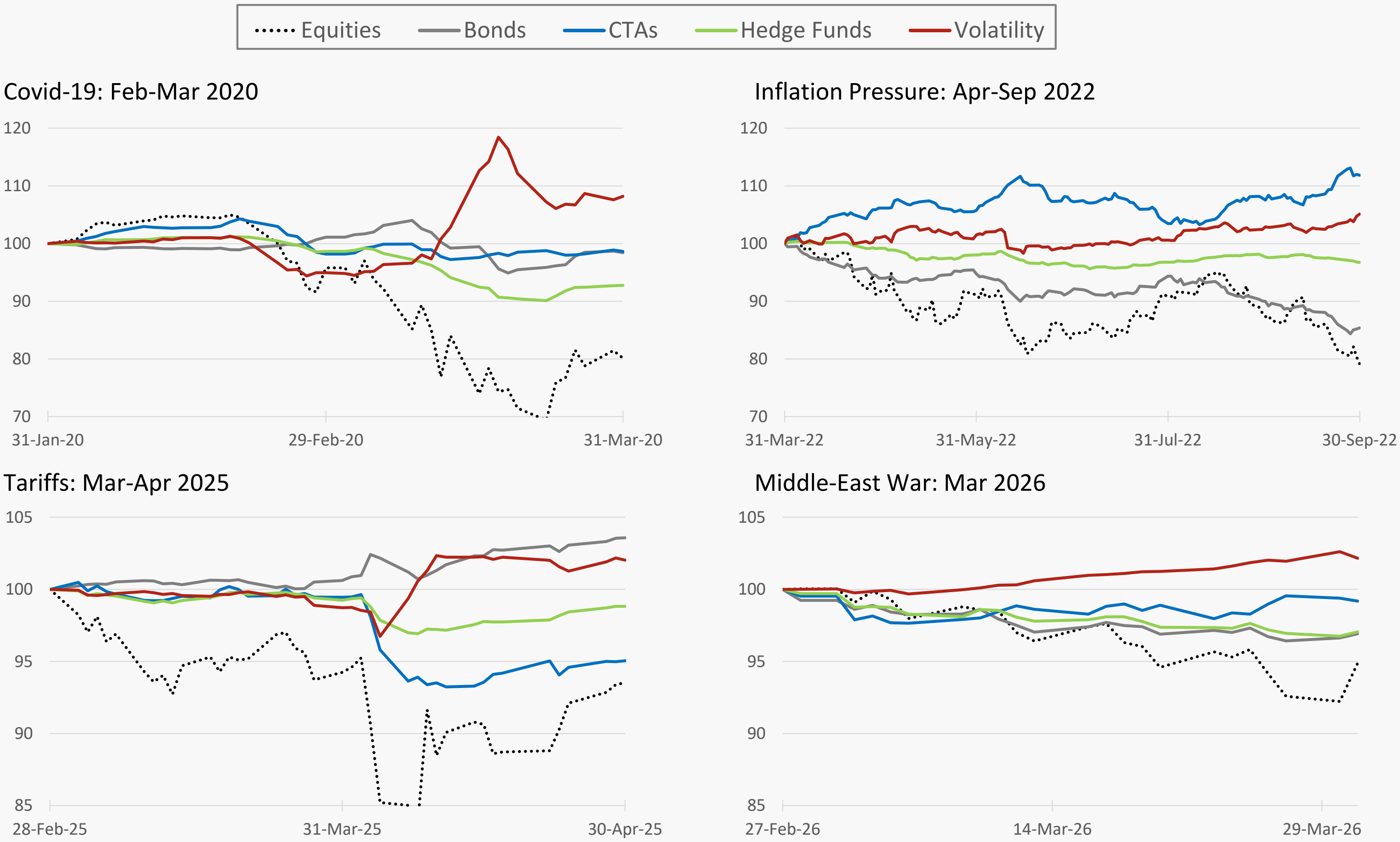
*investors should look to incorporate a range of alternative diversifiers, including volatility strategies*

Figure 2: performance of bonds and alternative diversifiers in four recent periods of equity turbulence




*Volatility returns are estimated from actual returns of the strategies in SouthPeak's real diversification funds, are in AUD, net of fees and expenses. Returns are estimated, unaudited and subject to adjustment. Other returns are in USD as per the following indices: Equity (SPX Index), Bonds (LEGATRUU Index)., CTA (NEIXCTA Index), Hedge Fund (HFRXGL Index). Past performance is not an indicator of future performance. Source: Bloomberg, SouthPeak.*

# Portfolio construction: including volatility strategies in diversifying assets

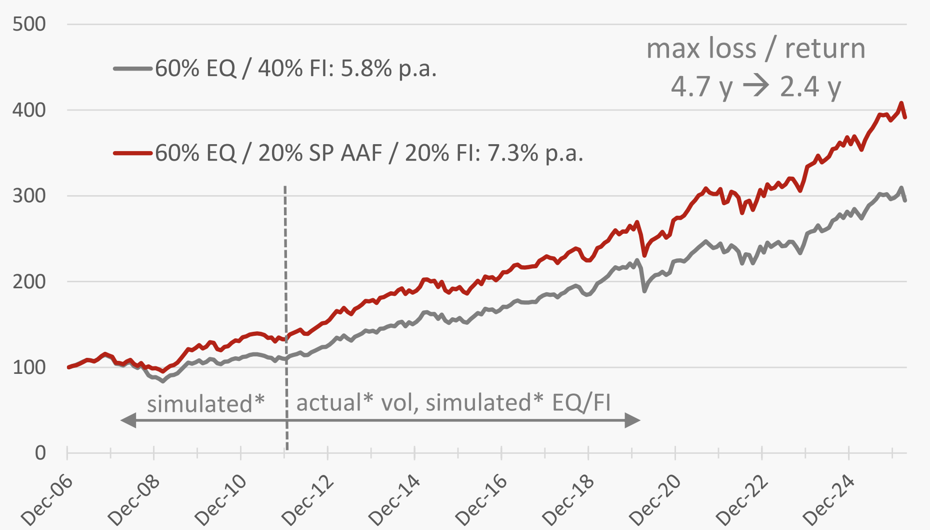
While the previous page explored the resilience of alternative diversifiers, it is also important to consider the expected return that a diversifying asset brings to a balanced portfolio.

Figure 3 compares a balanced portfolio of 60/40 Australian equities and bonds to the estimated performance of a portfolio that moves half of its diversifying assets from bonds to a volatility-based alternative diversifier; the SouthPeak Alternative Alpha Fund ('SP AAF').

Over the period examined, including volatility as an alternative diversifier would have improved portfolio returns by 1.5% p.a. while also reducing drawdowns. The worst drawdown would have lost 2.4 years of average returns, compared to 4.7 years for the 60/40 portfolio.

By potentially increasing returns and reducing losses, the inclusion of alternative diversifiers improves compounding and can help address sequencing risk. This makes them a valuable tool for all investors, but particularly for those approaching/in retirement.

Figure 3: Including volatility strategies in diversifying assets




** SouthPeak Alternative Alpha Fund returns for Feb 2012 – May 2025 are estimated from the actual returns of the fund's strategies in SouthPeak's real diversification funds together with AUD cash. Returns from June 2025 are from the SouthPeak Alternative Alpha Fund. Returns are estimated, unaudited and subject to adjustment. Returns prior to Feb 2012 are simulated. Simulations have been created using models with assumptions and may have the benefit of hindsight. No actual investments were made. There can be sharp differences between simulated and actual results for many reasons. Estimated returns are net of estimated transaction and management fees. Cash returns are RBA cash, RBACTRD Index. Equity returns are the S&P/ASX 200 Total Return Index, AS51T Index. FI returns are the Bloomberg AusBond Composite 0+ Yr Index, BACMO Index. Past performance is not an indicator of future performance. See important information on the last page. Source: Bloomberg, SouthPeak.*

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*replacing part of their diversifying assets with alternative diversifiers such as volatility can help investors improve the resilience of their portfolios while also targeting higher returns*

*Note: Including volatility strategies in growth assets is discussed in our paper 'Adding returns and resilience to Australian equities'.*

## Important information



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## About SouthPeak

SouthPeak is a specialist volatility manager providing alpha and protection.

We aim to deliver attractive outperformance with low correlation to bonds and equities.