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Reimagining asset allocation: A balanced macro approach

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For decades, the 60/40 portfolio has been a cornerstone of long-term balanced investing. But in today's increasingly complex and dynamic macroeconomic landscape, investors are asking whether this traditional mix remains fit for purpose.

At FTSE Russell, we've been rethinking what a diversified, resilient asset allocation should look like in an era of shifting growth and inflation dynamics, policy uncertainty, societal polarity, geo-political tensions, globalisation reversal, and continued technological disruptions. The result is a framework we call Balanced Macro. It is an approach to strategic allocation that aims to harvest risk premia embedded in risky assets such as stocks, bonds, and commodities, while dampening the impact of macro-economic regimes.

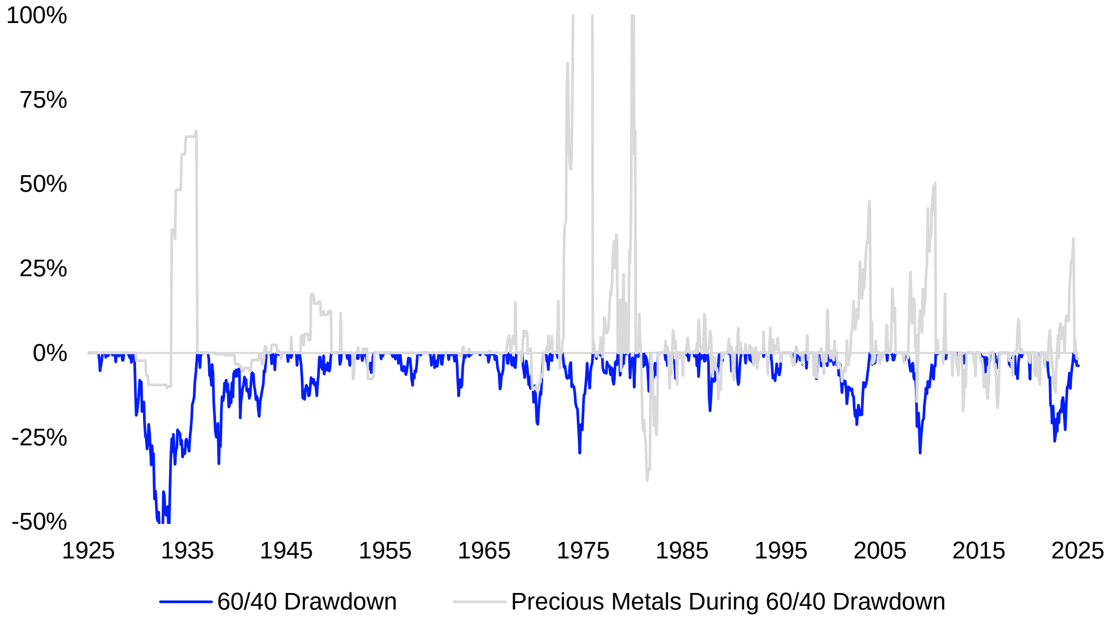
This paper provides a high-level summary of the key ideas behind Balanced Macro Allocations. Our goal is to spark deeper conversations with our clients who are re-evaluating how to future-proof their portfolios.

Moving beyond 60/40

The 60/40 portfolio gained mainstream popularity in the early 2000s due to a unique economic environment: where inflation was anchored at approximately 2% and the markets and central banks were focused mainly on the business cycle. For over 25 years, a key feature of this environment was the negative correlation between equities and nominal bonds. With a few rare exceptions, when stocks declined, bonds rallied, providing diversification and reducing drawdowns.

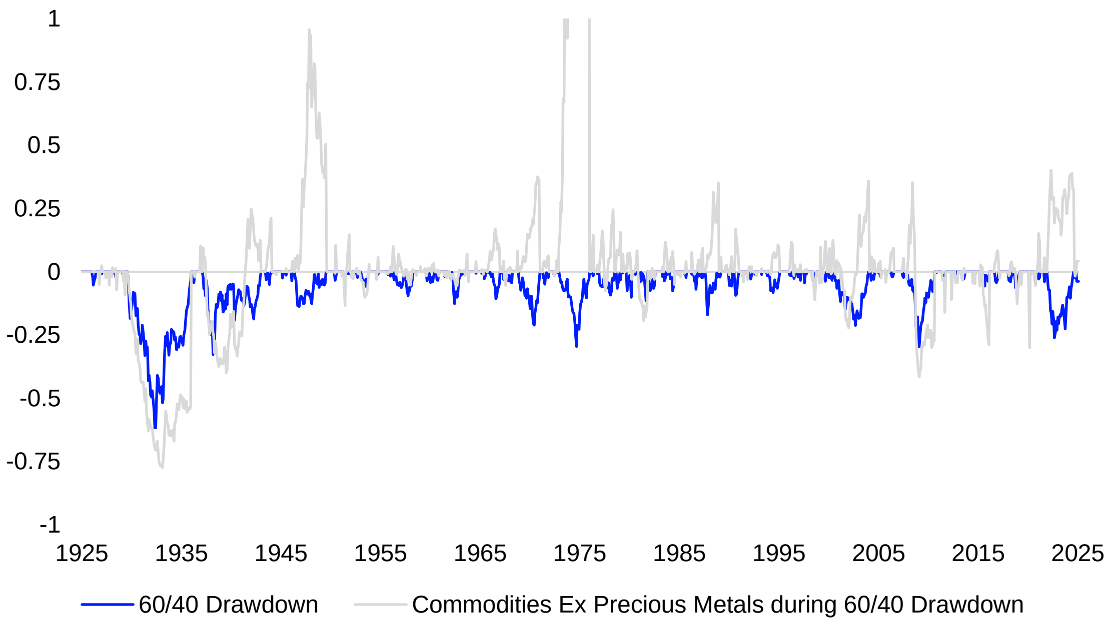
This pattern was heavily reliant on inflation remaining stable. In the 60/40 allocation, equities offer return potential, and bonds offer protection. But this is only true when inflation is stable. In regimes of dominant and unexpected inflation, bonds and equities can become positively correlated, and underperform in tandem, as seen in 2022 and more frequently in the last century. This correlation reversal renders the 60/40 ineffective just when diversification is needed most.

Figure 1: Performance of precious metals during 60/40 drawdowns



Source: SBBI®, Index Research and Design, FTSE Russell, June 2025.

Figure 2: Performance of Commodities during 60/40 drawdowns



Source: SBBI®, Index Research and Design, FTSE Russell, June 2025.

FTSE Russell's Balanced Macro approach directly addresses the imbalance of 60/40 in high inflation regimes. We propose an allocation that is balanced not only with respect to the business growth cycle but also with respect to inflation. Our approach expands the allocation to assets that provide a natural hedge to inflation, commodities and inflation-linked bonds.

Understanding macro regimes

To build balance into the portfolio, we analyse how asset classes respond to shifts in macro risk drivers, growth and inflation.

Figure 3: Growth vs. Inflation quadrant framework

	Falling Growth	**Rising Growth**
Rising Inflation	Precious Metals – Gold – Silver – TIPS – Inflation Linked – Convertibles	Commodities – Energy – Industrial Metals – Livestock – Agricultural
Falling Inflation	Nominal Bonds – US Bonds – Global Bonds – EM Gov-t Bonds – Corporate Bonds	Stocks – US Stocks – Global Stocks – Credit Spreads

Source: Index Research and Design, FTSE Russell, June 2025.

We classify macro regimes along these two dimensions. This creates four distinct quadrants. Each quadrant aligns with a unique asset behaviour profile:

- Equities thrive when growth surprises are positive, and inflation is stable or falling
- Nominal bonds underperform when either growth or inflation expectations rise
- Commodities, especially industrial metals and oil, perform well when both growth and inflation are rising
- Precious metals and inflation-linked bonds are effective hedges in stagflation (rising inflation, falling growth)

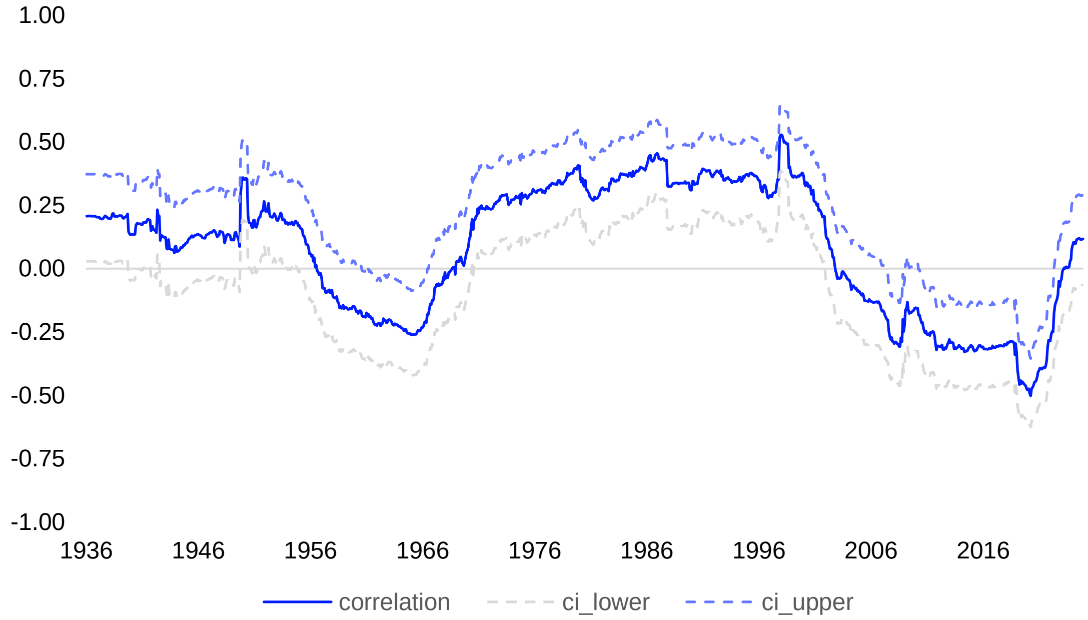
By assigning assets to macro quadrants based on these sensitivities, we build a macro-regime classification system. Within each quadrant, assets tend to move together consistently, driven by the same macro forces. However, across quadrants, assets are impacted differently by the macro factors; and as a result, their correlations will change.

Diversification across regimes

The above insight is a powerful one: correlations within macro regimes are stable, while correlations across regimes are not.

For instance, while equities and bonds exhibited strong negative correlation during much of the 2000s, this relationship reversed under the post-Covid inflationary stress in recent years. Correlations between macro quadrants can swing dramatically — from –40% to +40% — depending on whether growth or inflation dominates.

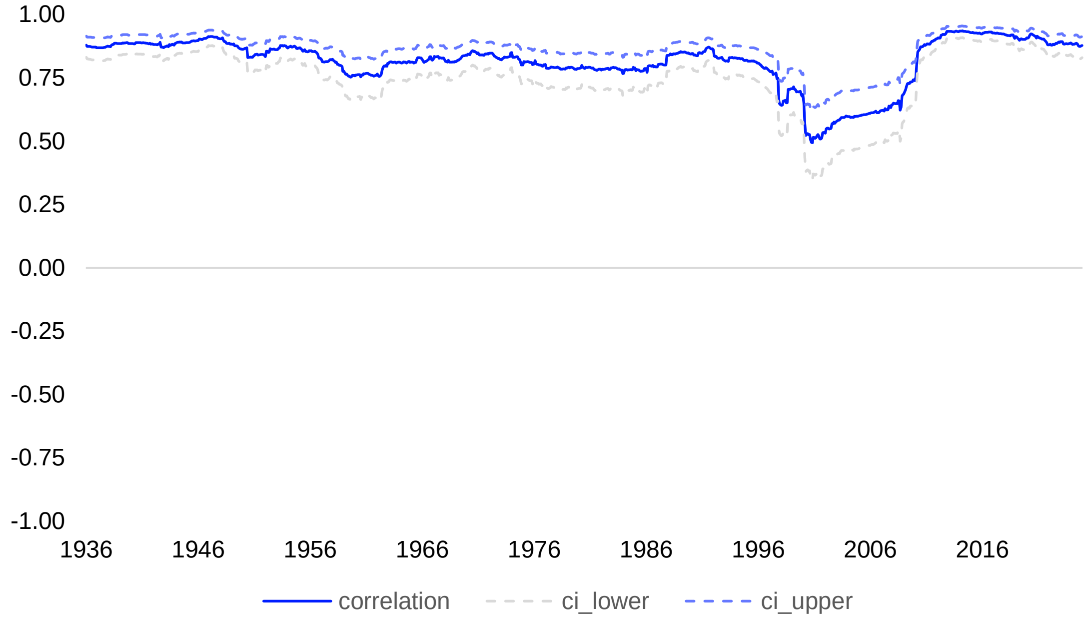
Figure 4: Historical stock-bond correlation



Source: SBBI®, Index Research and Design, FTSE Russell, June 2025.

On the contrary, the correlation between large stocks and small stocks, or stocks and credit, has been relatively stable.

Figure 5: Historical large cap – small cap correlation



Source: SBBI®, Index Research and Design, FTSE Russell, June 2025.

Our diversification approach respects this reality. Allocations within quadrants take correlations into account, because they are stable. But when allocating across regimes, we avoid using correlations, because cross-quadrant relationships are unpredictable and regime-sensitive.

A smarter approach to portfolio construction

Our allocation process operates in two layers:

– Within each macro quadrant, we build a risk-balanced portfolio using stable correlation structures and a risk-parity framework

– Across quadrants, we aggregate without relying on correlations, instead aiming for a balanced exposure to the growth and inflation dimensions of risk

This methodology acknowledges the macro forces that drive asset behaviour and reduces reliance on unstable assumptions. The result is a well-diversified, regime-resilient allocation.

Performance with purpose

The table below examines performance and risk/return characteristics since the end of Bretton Woods[1]. We start with 100% allocation to US Large Caps and gradually introduce more balance with 60/40 and finally with Balanced Macro. Returns step down as we introduce more balance because US Large Caps had a stellar performance and any diversification away from it lowers the return. But volatility declines more sharply, leading to improved Sharpe ratios from 0.45 and 0.51 to 0.58.

Table 1: Risk Return Statistics

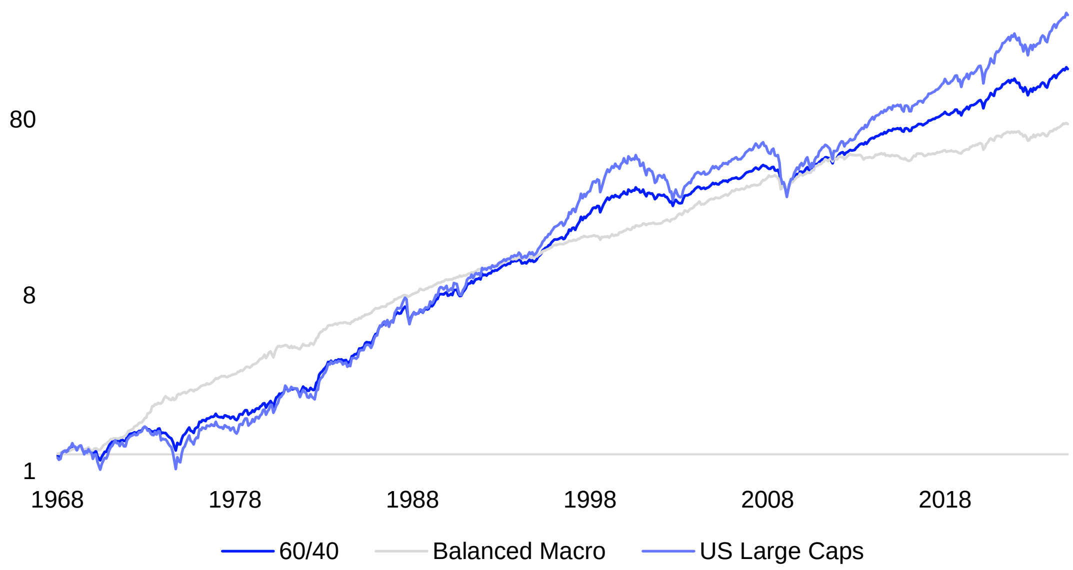
	Large Caps	60/40	Balanced Macro
Average Return	11.3%	9.3%	7.8%
Volatility	15.4%	9.7%	5.8%
Risk Adjusted Return	0.74	0.96	1.35
Sharpe	0.45	0.51	0.58
Max Drawdown	-51.1%	-29.8%	-16.7%
Days to MDD Recovery	1127	610	395
Return-to-MDD	0.22	0.31	0.47
Var 95	-23.1%	-13.6%	-6.1%
CVaR 95	-33.0%	-19.3%	-11.0%

Source: Index Research and Design, FTSE Russell, June 2025.

More importantly, the improvement in downside protection is even more pronounced. Return-to-Maximum-Drawdown ratio doubles. Further downside risk metrics, such as VaR, CvaR, show the same pattern: the more balance we introduce, the more resilient the portfolio becomes.

[1] The Bretton Woods system, established in 1944, created a framework of fixed exchange rates. Currencies were pegged to the U.S. dollar, which in turn was convertible to gold at $35 per ounce. It was designed to ensure global monetary stability after World War II. By the late 1960s, persistent U.S. trade deficits, inflation, and dwindling gold reserves eroded confidence in the dollar's convertibility. The system collapsed in 1971 when President Nixon suspended gold convertibility, leading to the adoption of floating exchange rates and effectively ending Bretton Woods.

Figure 6: Historical performance



Source: Index Research and Design, FTSE Russell, June 2025.

Let’s talk: Applications and extensions

Balanced Macro is more than a strategic allocation — it’s a flexible framework. It can be applied in a variety of ways.

– As a direct replacement for 60/40 or complementary overlay to 60/40 allocation,

– with and without leverage,

– as the core “balanced” building block in end-of-service and life-cycle strategies.

It can further be adapted for:

– Regional markets (e.g., Eurozone, China) in response to reversing globalisation.

– Sustainable and Shariah versions, using ESG-aligned equities and bonds, and environmentally considerate commodities.

– An expanded set of assets, incorporating emerging market equities and debt, convertibles, REITs, Infrastructure Investments, etc.

Balanced Macro offers a way to build more resilient portfolios for an uncertain macro future — without requiring forecasts, tilts, or market timing.

Let’s explore how it might fit into your allocation strategy.

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