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Diversifying beyond traditional assets as correlations rise.

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Much has been written recently about the diminished diversification benefit of bonds relative to equities in a portfolio context. We agree that bonds have provided less diversification over the past five years than they did during the prior two decades. However, we view this less as a structural break in the stock-bond relationship and more as a reversion toward the longer-term historical pattern, in which correlations have generally been flat to modestly positive rather than persistently negative.

Stock vs. bond correlations explained

Although the long-term correlation between stocks and bonds has been positive on average, the relationship is highly regime dependent. In periods characterized by low inflation and periodic growth shocks, the stock-bond correlation has typically been negative, allowing bonds to provide a meaningful source of portfolio diversification. By contrast, during periods of elevated inflation or inflation shocks, stocks and bonds have tended to move more closely together, reducing the diversification benefit of fixed income.

As shown in Exhibit 1, the correlation between stocks and bonds was negative for much of the 2000 to 2020 period. More recently it has reverted to positive territory.

Exhibit 1: Bonds are no longer dependable ballast due to rising correlations

Source: Bloomberg. As of 6/30/2026.

Why did this long-term relationship turn negative from 2000 to 2020?

The 2000 to 2020 period was characterized by low inflation, or even outright disinflation at times, alongside periodic growth shocks, such as the technology bubble, the Global Financial Crisis, and the COVID-19 pandemic. In this environment, concerns about weakening economic growth generally placed downward pressure on equity prices, while also contributing to lower interest rates and higher bond prices. This opposing response to growth shocks helped produce a negative correlation between stocks and bonds.

Several broader forces contributed to the low-inflation environment. Increasing globalization and an emphasis on free trade and market liberalization limited the use of trade barriers, such as tariffs, that can contribute to inflationary pressure. Furthermore, coordinated and accommodative central bank policies kept interest rates suppressed for extended periods.

Why did correlations revert to the long-term positive relationship?

Several economic and geopolitical dynamics have shifted since the low-inflation, low-rate environment that prevailed from 2000 to 2020. Inflation became less benign following the extraordinary fiscal and monetary measures introduced during the pandemic. Although much of that emergency stimulus has been spent, a range of factors continues to keep inflation above central bank targets. Elevated input costs, a shift to onshoring, tariffs, and resilient labor markets have placed a floor under goods and services prices, while large and rising fiscal deficits have contributed to upward pressure on term premiums.

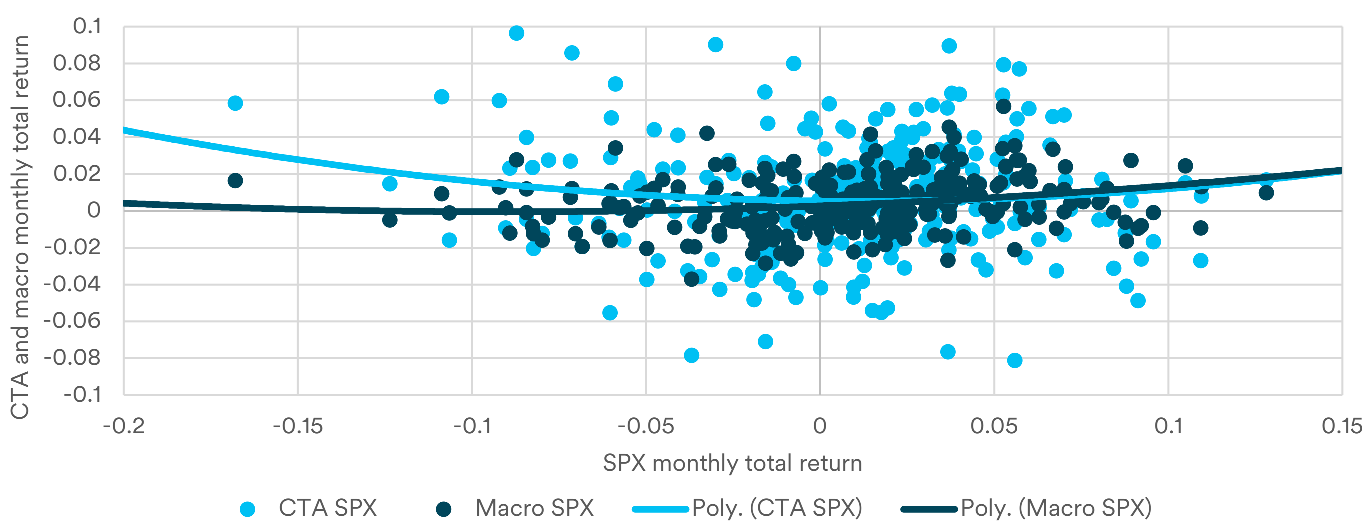
Summary

The unusually negative stock-bond correlation that prevailed for much of the 2000 to 2020 period reflected a specific macroeconomic backdrop of low inflation, suppressed interest rates, and recurring growth shocks. As inflationary pressures, higher policy rates, and larger fiscal deficits have reemerged, stock-bond correlations have reverted closer to their longer-term pattern of being flat to modestly positive, limiting the diversifying role of bonds.

This reinforces the importance of building diversification from multiple sources rather than relying on any single asset class or historical relationship. Allocating assets across equities, bonds, and real assets may help provide positive exposure to growth, disinflationary, and inflationary regimes, respectively. Complementing those core exposures with alternative diversifiers, such as trend and macro strategies, can help broaden a portfolio's opportunity set and improve resilience during periods when traditional stock and bond allocations move together.

These exposures can enhance portfolio balance, reduce reliance on any one source of diversification, and support more durable long-term risk-adjusted outcomes.

Exhibit 2: Trend-following and macro strategies give reason to smile (or smirk)



Source: Bloomberg. As of 6/30/2026.

GLOSSARY AND INDEX DEFINITIONS

For financial term and index definitions, please see: https://www.seic.com/ent/imu-communications-financial-glossary

IMPORTANT INFORMATION

