Insight: Opportunistic Fixed Income

By Tom Woolwine, President, June 2014

The Fixed Income Market has changed dramatically over the past ten years. Most institutional investors have a policy allocation to "core" bonds with a common benchmark of the Barclays Aggregate Index (BAGG). Did you know these facts about its characteristics?

- Treasury sector has grown from 22% to 36%.
- Duration has risen from 4.5 to 5.6 years.
- Yield has fallen from 4.2% to 2.5%.

The DMS Portfolio Management Team has felt for some time that the market has reached the end of a falling interest rate environment. Their focus now is to implement an opportunistic fixed income strategy where appropriate. The objectives are as follows:

- Reduce interest rate risk
- Increase yield
- Improve diversification
- Emphasize down market protection

Alternative fixed income sectors being considered/employed, and the associated benefits include:

- International Bonds: Diversification of global interest rate cycles
- High Yield: Protection against inflation due to higher yield
- Emerging Market Debt: Diversification of interest rate cycles and higher yield
- Bank loans: Floating rate coupon resets as interest rates increase
- Real Estate-Oriented Securities: Bond-like income stream

DMS believes that combining these non-core assets with a traditional BAGG portfolio and expanding the tactical range for duration management will improve the probability of meeting client objectives. Absent from the list above are Treasury Inflation Protection Securities (TIPS). TIPS are long duration securities, and it is the team's belief that the negative price impact of rising rates would far outweigh any benefit from the inflation component.

It is imperative that fixed income strategies shift to manage the changes coming.

If you would like to know more about opportunistic fixed income management, please contact Tom Woolwine, President, at (913) 981-1345 or email twoolwine@dms-demarche.com.