



## Tracking the Agg? Why the bond index may not work for investors

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Your success. Our priority.

The Agg wasn't, shouldn't be, was never intended to be an investment.

The benchmark in the fixed income market is the Agg. You were never supposed to, though, invest in a benchmark. A benchmark is what you compare your investments to. The Agg, for some reason, has become an investment. There's an ETF that tracks the Agg. It's the biggest ETF there is. The problem here is why would you invest in a market cap-weighted index. What that means is, a market cap-weighted index in the stock markets like the S&P, it makes sense to a reasonable degree. Big companies, that's a measurement of success. But if you take a bond index that's representative of the market capitalization of bonds, you're buying the biggest borrowers. You don't want to own in proportion to who's issued the most debt. You want to invest in proportion to where there's the best opportunity.

The Agg right now is a very concentrated index. What does that mean? 37% Treasuries. Then you add mortgage-backed securities which are really a government-backed, and other government-backed securities. And you end up with an index that's 70% government. So, you don't get a lot of diversification. You're putting all your eggs in the proverbial same basket.

One of the things you probably want to do is look at parts of the bond market that maybe aren't in the Agg. You want things that zig when the Agg zags. What does that mean? It's called diversification. If you think about diversification, if you look at U.S. Treasuries versus high yield bonds, high yield bonds are very risky and Treasuries are very safe. But if I combine the two, they have what's called a negative correlation. When one goes one way, the other goes the other way? I can get a portfolio that has a little more risk than Treasuries but more yield, with less risk than just if I was in the high yield market.

What I'm saying is, you want to go beyond the bond benchmark. You want to go beyond the Agg. Let's include components of the bond market like high-yield, like investment-grade, like emerging markets, so we can benefit from diversification, lower correlations, create what's called a more efficient portfolio.

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"The Agg right now is a very concentrated index..." Source: Bloomberg, 8/31/17.

The Bloomberg Barclays US Aggregate Bond Index (U.S. Aggregate) is a broad-based benchmark that measures the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, MBS (agency fixed-rate and hybrid ARM pass-throughs), ABS and CMBS (agency and non-agency).

The Standard & Poor's (S&P) 500 Index tracks the performance of 500 widely held, large-capitalization U.S. stocks.

It is not possible to invest directly in an index.

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