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# Finding the Right Fixed-Income Recipe

Fixed income comes in many flavors and can serve a variety of roles in a portfolio.

As kids, we dream about eating an ice-cream-only diet forever. But as we mature, we understand the importance of a balanced diet. Flavor matters, but we learn to focus on the benefits food can provide to help enhance our overall health.

This benefit-focused mindset is also helpful for investors: Is my portfolio using the right ingredients to support my financial health?

If we think of a portfolio as a balanced meal, stocks (aka equities) generally act as the protein helping to grow your portfolio. But what about fats, which can help regulate your body, and carbohydrates, which provide energy? That's where bonds (aka fixed income) can fill many important roles.

## What Sets Fixed-Income Types Apart

While all fixed-income investments share some basic traits, they're an investment type with many different flavors from which to choose. With so much variety, specific characteristics and roles can vary widely.

As we see it, there are two broad ways fixed income can serve investors. These include the potential to either reduce portfolio volatility (think fats) or generate income (think carbohydrates).

### Key Points

- Fixed income is a large umbrella, covering many different types of investments with varying characteristics.
- Broadly speaking, fixed income can serve two main roles in a portfolio: potentially reducing volatility or generating income.
- A financial professional can be an important resource to help you develop the right mix for your portfolio.

## Potential Volatility Reducers (aka Fats)

Though dietary fats have gotten a bad rap, they're necessary to support cell growth, help protect your organs, regulate your body temperature, and even absorb some nutrients.

In investing, you may need a cushion from equity-driven volatility. That's a role that can be filled by high-quality bonds such as US Treasuries, municipal bonds, mortgage-backed securities, and global-government bonds.

These types of fixed income tend to behave differently than equities, which is why they can potentially offset volatility and add diversification to your portfolio. However, these types of fixed income have historically offered lower yields than equities.

## Income Generators (aka Carbohydrates)

When your body needs energy, it looks to carbohydrates. In your portfolio, rather than energy, think about where you source your income. This is where corporate bonds, global high-yield bonds, and emerging-market debt can help.

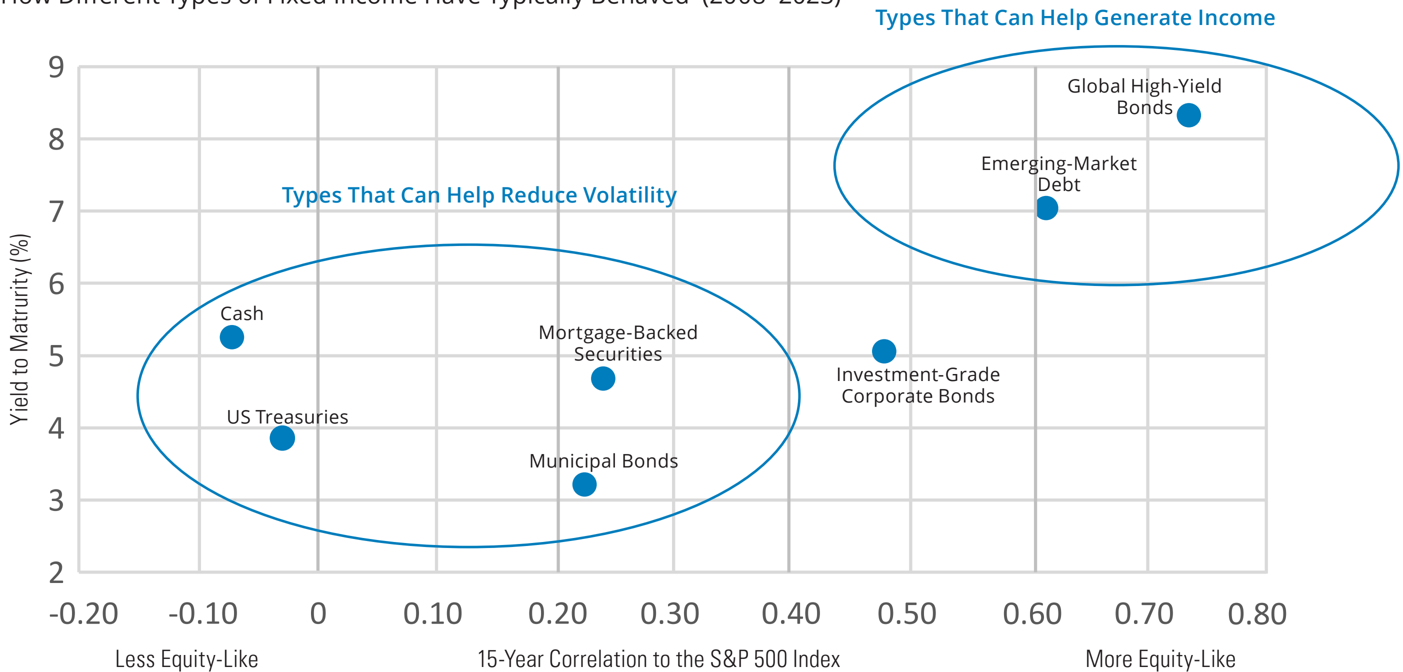
These bonds carry more risk because they tend to behave more like equities than say, a US Treasury bond. To compensate for added risk, these types of fixed income have tended to provide higher yields and a higher source of income.

**FIGURE 1** compares how different types of fixed income have historically behaved in relation to equities (correlation) and their return (yield). Fixed income that's less correlated to equities can offer diversification and help reduce overall portfolio volatility (bottom left circle), while fixed income that's more correlated to equities has generally offered higher returns and can be a source of income (upper right circle).

FIGURE 1

**Understanding the Roles of Fixed Income**

How Different Types of Fixed Income Have Typically Behaved (2008–2023)




As of 12/31/23. **Past performance does not guarantee future results.** Indices are unmanaged and not available for direct investment. **Correlation** is a statistical measure of how two investments move in relation to each other; a correlation of 1.0 indicates the investments have historically moved in the same direction; a correlation of -1.0 means the investments have historically moved in opposite directions; and a correlation of 0 indicates no historical relationship in the movement of the investments) to equities. **Yield to maturity** (i.e., the expected total return if a bond is held until maturity) for all indices except Municipals, which is Yield to Worst (i.e., the lowest possible yield on a bond without it defaulting). For illustrative purposes only. Please see representative index definitions on page 3. Diversification does not ensure a profit or protect against a loss in a declining market. Data Sources: Bloomberg, S&P Dow Jones, and Morningstar, 2/24.

## Don't Settle for Something Bland

Though they may have different purposes, there is some common ground between all types of fixed income, including risks.

For example, an issuer can default and fail to repay its debt to borrowers (credit risk), and prices can also fluctuate with the market: when interest rates rise, bond prices typically fall (interest-rate risk). That's why it's important to manage risk in your bond portfolio just as carefully as you do in your equity portfolio.

To sum it up, proper nutrition can be a complex equation, but your portfolio's recipe doesn't have to be. Talk to your financial professional today to make sure you're invested in the right types of fixed income to help you reach your goals.

**Talk to your financial professional about the roles fixed income should play in your portfolio.**

**Cash** is represented by the Bloomberg US Treasury Bill 1-3 Month Index, which is designed to measure the performance of public obligations of the US Treasury that have a remaining maturity of greater than or equal to 1 month and less than 3 months. **Emerging Market Debt** is represented by the Bloomberg Emerging Markets Aggregate Bond Index, a hard-currency emerging-markets debt benchmark that includes USD-denominated debt from sovereign, quasi-sovereign, and corporate EM issuers. **Global High-Yield Bonds** are represented by the Bloomberg Global High Yield Index, a multi-currency measure of the global high yield debt market. **Investment-Grade Corporate Bonds** are represented by the Bloomberg US Corporate Index, which measures the investment grade, fixed-rate, taxable corporate bond market. **Mortgage-Backed Securities** are represented by the Bloomberg US MBS Index, which tracks fixed-rate agency mortgage-backed passthrough securities guaranteed by Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC). investment-grade corporate fixed-rate debt issues with maturities of one year or more. **Municipal bonds** are represented by the Bloomberg Municipal Bond Index, an unmanaged index that is considered representative of the broad market for investment grade, tax-exempt bonds with a maturity of at least one year. **US Treasuries** are represented by the Bloomberg US 7-10 Year Treasury Bond Index, which measures the performance of the US Government bond market and includes public obligations of the US Treasury with a maturity of between seven and up to (but not including) 10 years.

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