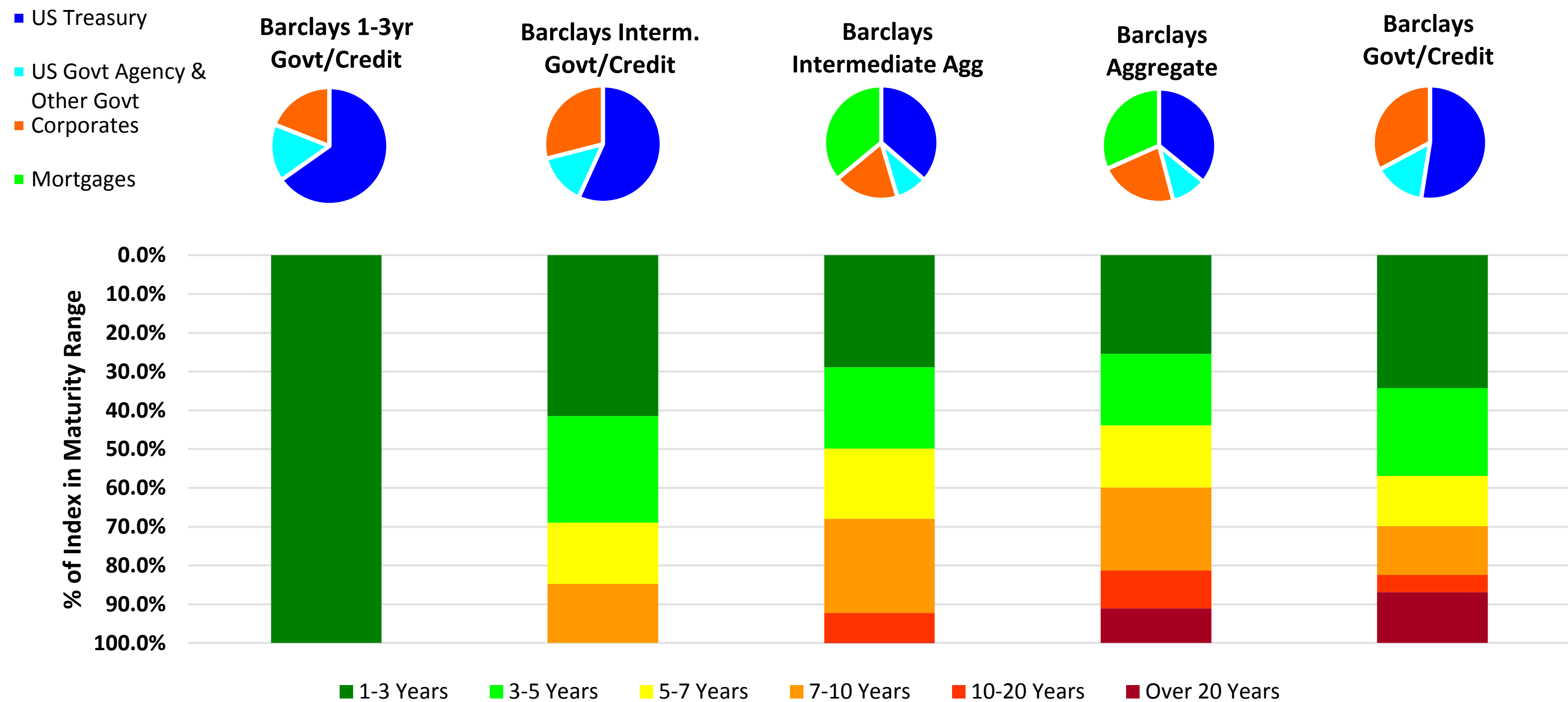
MARKET MICROSCOPE – Comparison of US Bond Indexes

The typical asset allocation for a balanced portfolio is 60% equities & 40% bonds. Many people like to talk about stock portfolios and fluctuations of the stock market, but you don't hear as much about the bond market. What is it made up of? What are the drivers of return/performance?

The pie charts below contain the breakdown of each index by bond sector. The primary difference between the indexes in terms of sector allocation is the inclusion of Mortgage-Backed Securities in Aggregate indexes.

The bar chart breaks down each index by bond maturity. The Intermediate Government Credit Index has only about 15% of the portfolio allocated to bonds with a maturity greater than 7 years (and none with a maturity greater than 10 years). That number rises to about 32% for the Intermediate Aggregate Index, and 40% for the Aggregate Index. This leads to a significantly higher Average Maturity and Average Portfolio Duration value for the Aggregate Index compared to the Intermediate Government Credit Index. Duration has the greatest impact on the return of a bond portfolio – changes in interest rates affect higher duration portfolios more strongly than lower duration portfolios. Other important risks to consider include credit/default risk, liquidity risk, inflation and reinvestment risk.



Average Maturity	1.97	4.15	5.36	7.58	7.63
Average Duration	1.91	3.84	4.42	5.55	5.60
Current Yield	1.90%	2.52%	2.95%	3.19%	2.94%

Barclays Index data as of 12/31/13