NO HEAVY LIFTING REQUIRED

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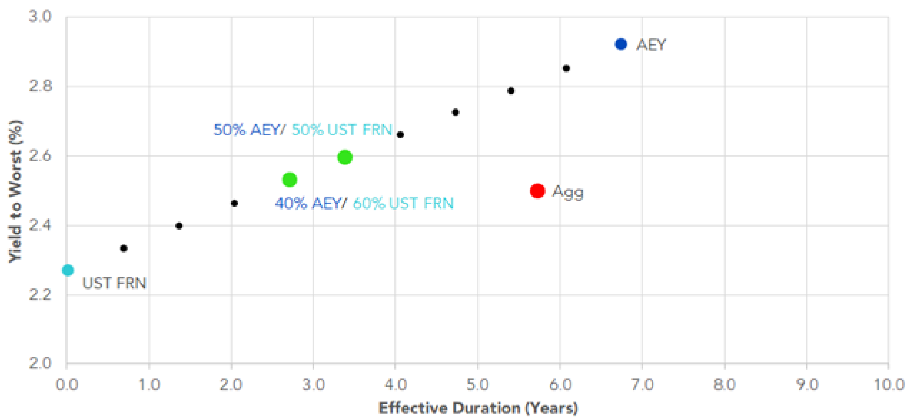
07/03/2019

When looking at the money and bond markets these days, they almost seem to be saying to the Federal Reserve (Fed), "Would you please cut rates already?" Even though the economic data doesn't warrant an urgent rate cut, the policy makers have put themselves in a very difficult situation by having to make a move. In other words, the bond market is the tail wagging the Fed dog. Against this backdrop, I continue to advocate a solution for fixed income investors in which no heavy lifting is required: the barbell strategy.

As the reader may recall, we began writing about this approach last summer. We utilize Yield Enhanced (AEY) and U.S. Treasury floating rate (UST FRN) strategies and comparing the results to the widely followed Bloomberg Barclays U.S. Aggregate Index (Agg) benchmark. At first, the combination centered around a 70% AEY and 30% UST FRN blend, but during 2019, this ratio has continued to be adjusted due to the decline in intermediate yields and the resulting flattening of the yield curve.

Yield to Worst and Effective Duration Comparison Enhanced Yield/UST FRN vs. Aggregate



Source: Bloomberg, 6/27/19. Past performance is not indicative of future results. You cannot invest directly in an index. Index performance does not represent actual fund or portfolio performance. A fund or portfolio may differ significantly from the securities included in the index. Index performance assumes reinvestment of dividends but does not reflect any management fees, transaction costs or other expenses that would be incurred by a portfolio or fund, or brokerage commissions on transactions in fund shares. Such fees, expenses and commissions could reduce returns. WisdomTree, its affiliates and their independent providers are not liable for any informational errors, incompleteness or delays or for any actions taken in reliance on information contained herein.

The accompanying graph now illustrates the combination of either 50% AEY/50% UST FRN or 40% AEY/60% UST FRN as the newest pairings. Here are the respective results compared to the Agg:

50% AEY/50% UST FRN: +9 basis points (bps) in yield; -2.34 years in duration
40% AEY/60% UST FRN: +3 bps in yield; -3.01 years in duration

Conclusion

The WisdomTree Yield Enhanced U.S. Aggregate Bond Fund (AGGY), which seeks to track the Bloomberg Barclays U.S. Aggregate Enhanced Yield Index, and the WisdomTree Floating Rate Treasury Fund (USFR), which seeks to track the Bloomberg U.S. Treasury Floating Rate Bond Index, can be utilized as the two ends of the barbell. The strategy laid out in this blog post offers a strategic solution designed to help fixed income investors navigate the waters that loom ahead without making a high conviction bet on where rates are headed in the seemingly ever-changing interest rate landscape.

Unless otherwise stated, data source is Bloomberg, as of June 27, 2019.

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You cannot invest directly in an index.

DEFINITIONS

Federal Reserve : The Federal Reserve System is the central banking system of the United States.

Bloomberg Barclays U.S. Aggregate Enhanced Yield Index : a constrained, rules-based approach that reweights the sector, maturity, and credit quality of the Barclays U.S. Aggregate Index across various sub-components in order to enhance yield.

Floating Rate Treasury Note : a debt instrument issued by the U.S. government whose coupon payments are linked to the 13-week Treasury bill auction rate.

Bloomberg U.S. Aggregate Bond Index : Represents the investment-grade, U.S. dollar-denominated, fixed-rate taxable bond market, including Treasuries, government-related and corporate securities, as well as mortgage and asset backed securities.

Yield : The income return on an investment. Refers to the interest or dividends received from a security that is typically expressed annually as a percentage of the market or face value.

Yield curve : Graphical Depiction of interest rates on government bonds, with the current yield on the vertical axis and the years to maturity on the horizontal axis.

Basis point : 1/100th of 1 percent.

Duration : A measure of a bond’s sensitivity to changes in interest rates. The weighted average accounts for the various durations of the bonds purchased as well as the proportion of the total government bond portfolio that they make up.