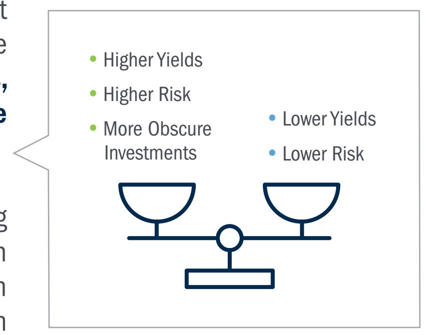
The Challenge of Fixed Income Investing in the 2020s

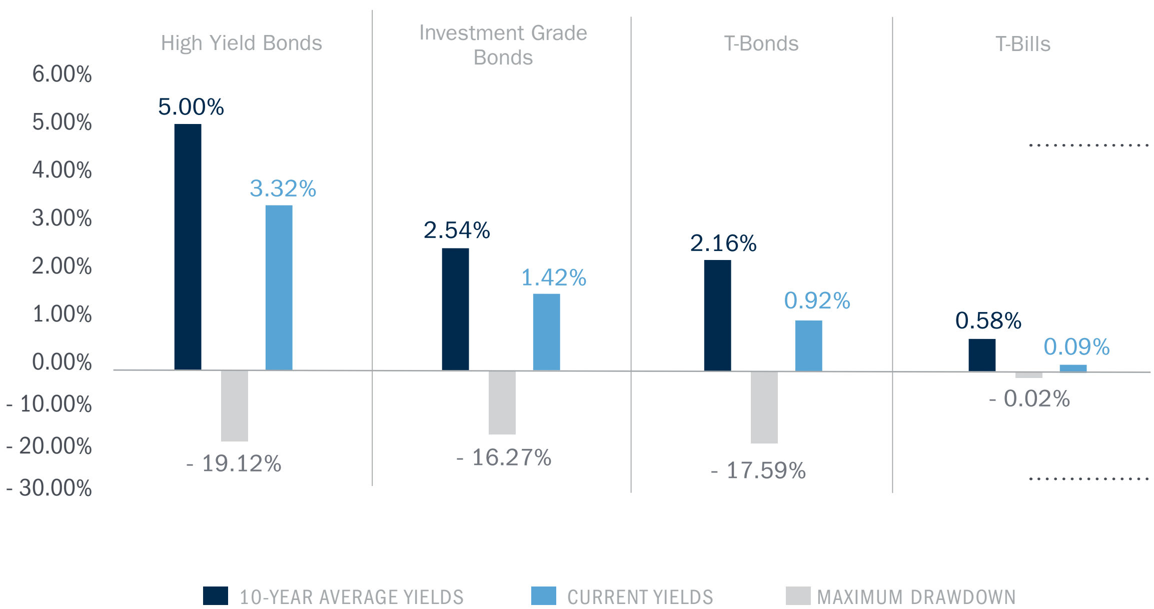
Fixed income investing has fundamentally changed in the last decade. Increasingly low interest rates, unprecedented central bank monetary policy, and aging demographics have altered the way investors think about generating income in their portfolios. **Forced to weigh low yields, higher risk, and more structured fixed income investments, income-focused investors face difficult trade-offs regarding asset allocation.**



The trend of lower yields accelerated and became more entrenched in the 2010s prompting investors to chase higher yields in unconventional ways. However, most high yields come with the trade-off of higher risk in the form of higher volatility and higher principal drawdown. In fact, many leading fixed income indexes reflect this reality even with current yields lower than average trailing 10-year yields.

Select Indexes Current and 10-Year Average Yields and Maximum Drawdowns

1.1.2011 - 12.31.2020



As yields rise, so do historical drawdowns.

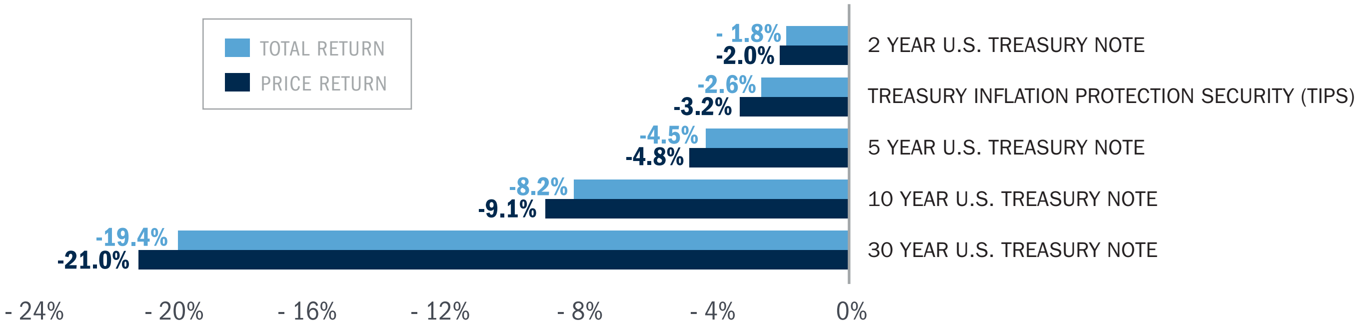
Maximum drawdown is the maximum decline a security experiences prior to reaching its previous peak.

High Yield Bonds: ICE BofA BB Yield Bond Index; Investment Grade Bonds: ICE BofA AAA Bond Index; T-Bonds: 10 year U.S. Treasury Rates; T-Bills: 90 day U.S. Treasury Bills
Sources: Morningstar Direct, Federal Reserve Economic Data

Rising Interest Rates Hurt More When Yields are Low

Fixed income securities have historically been viewed as an investment that not only generates income, but generally preserves capital, at least far more than equity investments. However, with so little yield generated today, relatively small increases in interest rates can impair total returns. This is true even for the highest quality fixed income investments: U.S. Treasury Securities. A mere 1% rise in rates from current levels would drop the market value of a 30 year U.S. Treasury Bond by over 20%. Impacts could be even worse for lower quality fixed income investments.

Impact of a 1% Rise in Interest Rates | Assumes a parallel shift in the yield curve and steady spreads

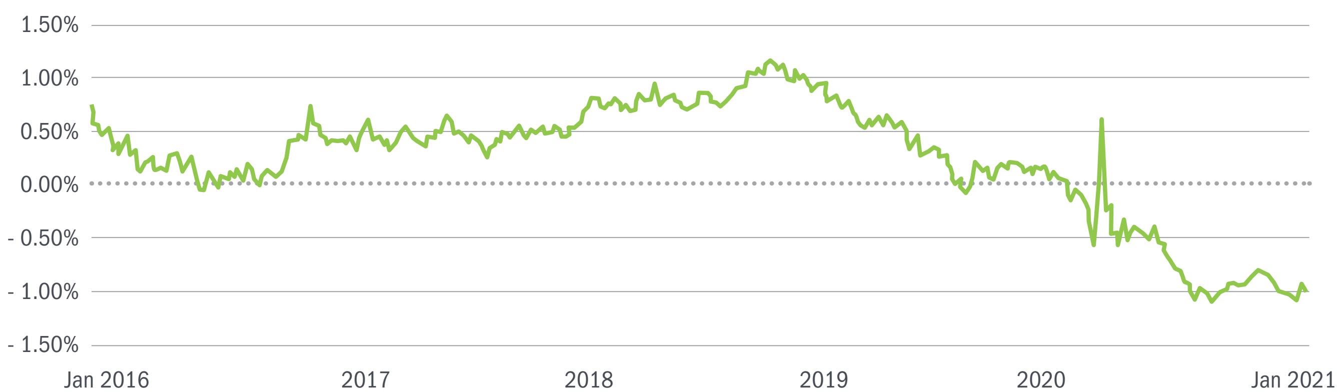


Source: J.P. Morgan Guide to the Markets, Q1 2021

Negative Yields? They Are Already Here in Real Terms

Record low nominal U.S. Treasury yields have pushed real rates, the inflation adjusted yield, into negative territory. While market observers may fret over potential negative yields, in essence, the U.S. is already there.

Inflation Adjusted Real 10 Year Treasury Yields | 2016 - January 2021



Source: Federal Reserve Economic Data, U.S. Treasury Inflation Adjusted 10 year Note.

Alternatives: A More Palatable Trade-Off?

Current market conditions reveal a simple and challenging reality: with traditional investment options, investors can generate higher income with higher potential drawdowns or they can settle for lower yields and lower drawdowns. However, another option is available with the world of alternative investments. Alternative investment paradigms offer new possibilities which seek to challenge pre-conceived notions about performance trade-offs creating a nuanced advantage in the world of income investing. **By giving up intraday liquidity, investors are presented with a host of new investment options that can potentially generate higher yields with lower volatility and drawdown.**

Liquidity, while a benefit, **can also be a curse of sorts as daily liquid investments tend to draw very large amounts of capital in a short amount of time leading to pricing distortions**. These distortions can then lead to the very volatility and drawdown that investors sought to avoid. Less liquid investments tend to avoid these distortions while still generating above market yields broadening their appeal to institutional investors.

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