

WHEN TALKING ABOUT INCOME POTENTIAL, WHAT YIELD DO YOU MEAN?

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In perhaps one of the most confusing yet least talked about elements of the asset management industry, the concept of “yield” can be a particularly difficult conversation to have. Particularly in fixed income, where investors conceivably buy a bond fund for income, many advisors care about one number and one number only: “What is the yield?” Most of the time, these same advisors don’t like the response: “It depends what you mean by ‘yield.’” In an effort to promote transparency, we thought it might be a useful exercise to explain the yields quoted on our materials and provide an explanation as to not only the what, but also why we calculate them in the first place. For all these calculations, the data only represents a particular snapshot of the time when it was calculated.

Yield to Maturity: *The single discount rate that equates the present value of a bond’s cash flows to its market price. Also referred to as the internal rate of return of a bond.* This measure is perhaps the most basic to bond investors, but it does not take into account any fund-related expenses. However, it does provide investors with a glimpse into the income potential of the actual holdings of the portfolio.

Yield to Worst: *The rate of return generated assuming a bond is redeemed by the issuer on the least desirable date for the investor.* Similar to the yield to maturity, this measure may be more important with bonds that have embedded options where, in certain market scenarios, the bond may be called before its maturity. This measure is often a more conservative measure than yield to maturity and is the preferred yield measure on corporate bonds and portfolios.

Implied Yield: *The annualized rate of return generated by a fund’s investment in [forward currency contracts](#). The calculation is intended to show the yield of forward currency contracts, assuming that foreign exchange rates remain constant.* This measure is most relevant for currency strategy funds. At current levels, foreign interest rates are higher than those in the U.S. For this reason, a substantial portion of a forward currency contract’s return may be attributable to returns derived from exposure to foreign interest rates. These interest rates are “embedded” in the value of the forward currency contract and cannot be separated from the spot return component of the contract. For this reason, the currency strategy funds intend to distribute any capital gains on these contracts annually.

Embedded Income Yield: *Represents the annualized rate of return generated by a fund’s investments in both fixed income securities and derivatives exclusive of interest rate changes and movement in foreign exchange spot rates. The calculation is intended to capture the fund’s potential to earn income return over the next year given current holdings and market conditions. The embedded income yield will differ from the portfolio’s yield to maturity, due to the incorporation of derivatives in the embedded income yield.* This term is used to give investors an idea of what the income potential of the fund is by combining the yield to maturity of bonds and any impact on income potential from derivative positions (such as forward currency contracts). The term will also be relevant for the rising rate suite of products where the implied interest rate on the futures contracts is offset against the yield to maturity of the bond portion.

SEC 30-Day/Standardized Yield: *A standard yield calculation developed and required by the Securities and Exchange Commission (SEC). It is based on the most recent 30-day period covered by the fund’s filings with the SEC. The yield reflects the dividends and interest earned during the period, after the deduction of the fund’s expenses.* This measure is required by the SEC.

Distribution Yield/Indicated Yield: *Calculated by annualizing the most recent fund distribution and dividing by the fund’s current NAV. The yield represents a single distribution from the fund and does not represent the total returns of the fund.* Many income-focused investors may be sensitive to how much net yield is distributed to fund shareholders. This amount is perhaps the most difficult to forecast in an exchange-traded fund.

12-Month Yield: *The sum of the per-share dividends over the last 12 months, divided by the fund’s current net asset value (NAV).* In short, this is a 12-month trailing calculation of the distribution yield, mentioned above. In conclusion, while no single yield can give investors a completely transparent picture of a fund’s income potential, the values listed above may provide some guidance to help them make their decisions.

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DEFINITIONS

Forward currency contracts : A forward contract in the forex market that locks in the price at which an entity can buy or sell a currency on a future date.