HOW TO PROFIT WHEN RATES RISE: NEGATIVE DURATION BOND STRATEGIES

Bradley Krom — U.S. Head of Research
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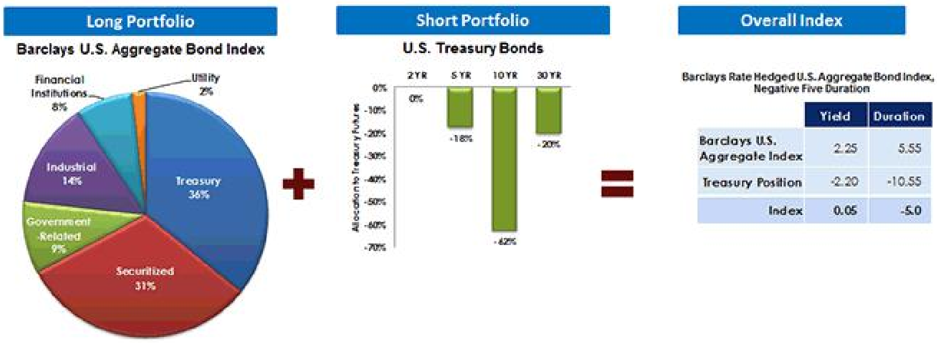
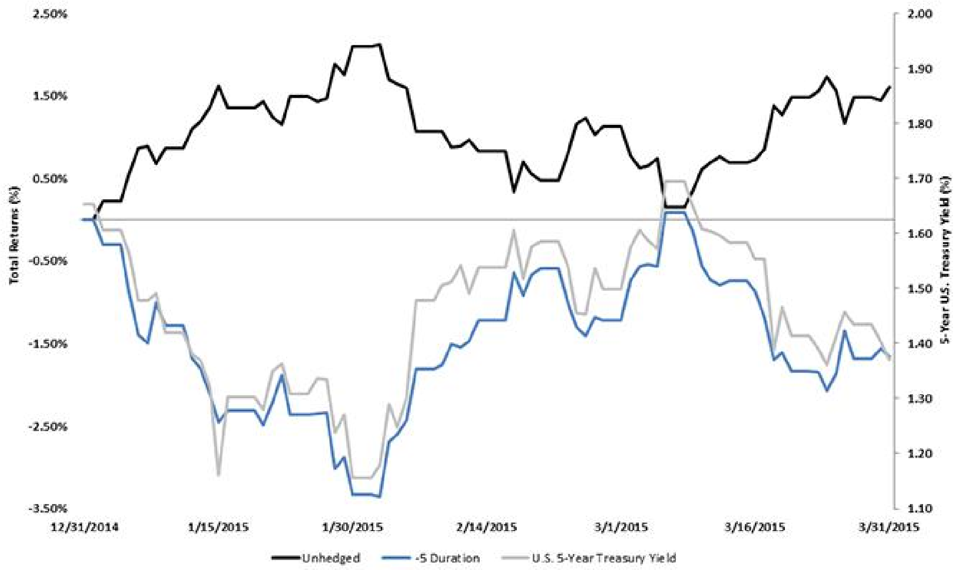
As the debate rages surrounding the timing of the first Federal Reserve (Fed) rate hike, we continue to discuss the potential tradeoffs surrounding this inevitable shift in policy. While some investors may be content to ride out the waning bull market in bonds, others may seek to position more tactically. We continue to believe that asymmetric risks remain in the bond market. As a result, investors should consider hedging interest rate risk. Historically, investors have quantified the amount of interest rate risk in their portfolios via duration. For every 1% move higher in interest rates, a five-year duration bond's price is expected to fall by approximately 5%. For those interested in expressing a view on rising U.S. rates, a negative duration bond strategy could provide investors a way to profit from rising rates (and lower bond prices). As in most markets, there is no free lunch. One of the hurdles associated with a "short" bond position is the costs of maintaining that position. What we mean by costs is that if a long position in a bond pays the holder interest, then a short position in that same security will require the short to pay the interest. A long bond position is akin to lending; a short position is akin to borrowing. For investors that believe higher interest rates are coming, timing is a crucial factor: time is literally money due to the cost of being short. Unless interest rates rise (and bond prices fall), the short position will experience negative total returns due to the impact of negative carry. One option to help defray the costs of the short position is to invest in a portfolio of bonds (positive carry) and then "overhedge" the portfolio by selling longer maturity securities to achieve a negative duration target. Through our collaboration with Barclays and Bank of America Merrill Lynch, WisdomTree has established strategies that are constructed on this simple premise. **Negative Duration Mechanics** As investors have become more comfortable with currency-hedged equity strategies that isolate equity risk from currency risk, interest-rate-hedged bond strategies operate on a similar principle. In creating our suite of rising-rate strategies, we sought to focus on traditional bond indexes that investors already have exposure to today. The only difference in our approach is that a second adjustment factor is applied via the interest rate overlay. As figure 1 shows, the negative duration variant of the Barclays U.S. Aggregate Bond Index (Agg)[1] can be thought of as a combination of two portfolios: a portfolio of bonds and a portfolio of short Treasury positions. The bond portfolio provides income that helps defray the cost of the short positions. In a rising-rate environment, the profits from the short positions help offset losses from the long bond position, thus generating positive total returns. **Figure 1: Under the Hood of Negative**



Sources: Barclays, WisdomTree, as of 12/31/15.
Past performance is not indicative of future results. You cannot invest directly in an index.

Duration In our view, the best way to understand these strategies is to examine the net effect of a rise in rates. On January 30, interest rates across the U.S. yield curve made fresh year-to-date lows. Over the next several weeks, interest rates rose, resulting in losses for unhedged positions in the Agg. As figure 2 shows, an unhedged portfolio fell by approximately 1.45%, whereas the negative duration strategy rose by 2.86%.[2] Over the same period, the five-year U.S. Treasury bond yield rose by nearly 54 basis points, implying a price loss of approximately 2.58%.[3] As we have mentioned previously, U.S. Treasury bonds continue to trade like growth stocks: total returns are almost exclusively being driven by price returns. **Figure 2: Unhedged vs. Negative Duration Returns as Yields Rise & Fall Barclays U.S. Aggregate Index Total Returns:**



Sources: Barclays, Bloomberg, as of 3/31/15.
Past performance is not indicative of future results. You cannot invest directly in an index. Performance, especially for very short time periods, should not be the sole factor in making your investment decision.

Unhedged vs. -5 Duration

While investors should view a negative duration strategy as an implicit bet against U.S. interest rates, they must also understand that total returns from plain-vanilla fixed income are primarily being driven by changes in bond prices, as opposed to income. As a result of potential changes in Fed policy coming this year, we believe that interest rates may be poised to rise in the coming months. In today's market environment, investors should consider tactical positions in negative duration fixed income strategies to benefit from rising U.S. interest rates. [1]Barclays Rate Hedged U.S. Aggregate Bond Index, Negative Five Duration. [2]Source: Barclays, as of 3/9/15. [3]Calculated: 54 basis points x 4.78 years = -2.58% price change.

Important Risks Related to this Article

There are risks associated with investing, including possible loss of principal. High-yield or "junk" bonds have lower credit ratings and involve a greater risk to principal. Fixed income investments are subject to interest rate risk; their value will normally decline as interest rates rise. The Fund seeks to mitigate interest rate risk by taking short positions in U.S. Treasuries, but there is no guarantee this will be achieved. Derivative investments can be volatile, and these investments may be less liquid than other securities and more sensitive to the effects of varied economic conditions. Fixed income investments are also subject to credit risk, the risk that the issuer of a bond will fail to pay interest and principal in a timely manner or that negative perceptions of the issuer's ability to make such payments will cause the price of that bond to decline. The Fund may engage in "short sale" transactions of U.S. Treasuries, where losses may be exaggerated, potentially losing more money than the actual cost of the investment, and the third party to the short sale may fail to honor its contract terms, causing a loss to the Fund. While the Fund attempts to limit credit and counterparty exposure, the value of an investment in the Fund may change quickly and without warning in response to issuer or counterparty defaults and changes in the credit ratings of the Fund's portfolio investments. Investing in mortgage- and asset-backed securities involves interest rate, credit, valuation, extension and liquidity risks and the risk that payments on the underlying assets are delayed, prepaid, subordinated or defaulted on. Due to the investment strategy of certain Funds, they may make higher capital gain distributions than other ETFs. Please read the Funds' prospectus for specific details regarding the Funds' risk profile. Barclays Capital Inc. and its affiliates ("Barclays") is not the issuer or producer of the Funds, and Barclays has no responsibilities, obligations or duties to investors in the Funds. These Barclays Indexes are a trademark owned by Barclays Bank PLC and licensed for use by WisdomTree with respect to the WisdomTree trust as the

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DEFINITIONS

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

Bullish : a position that benefits when asset prices rise.

Hedge : Making an investment to reduce the risk of adverse price movements in an asset. Normally, a hedge consists of taking an offsetting position in a related security, such as a futures contract.

Interest rate risk : The risk that an investment's value will decline due to an increase in interest rates.

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.

Negative duration strategies : Refer to WisdomTree's Interest Rate Strategies that target a negative overall duration; namely, the WisdomTree Barclays U.S. Aggregate Bond Negative Duration Fund and the WisdomTree BofA Merrill Lynch High Yield Bond Negative Duration Fund. .

Short (or Short Position) : The sale of a borrowed security, commodity or currency with the expectation that the asset will fall in value, the opposite of Long (or Long Position).

Long (or Long Position) : The buying of a security such as a stock, commodity or currency, with the expectation that the asset will rise in value, the opposite of Short (or Short Position).

Currency hedging : Strategies designed to mitigate the impact of currency performance on investment returns.

Overlay strategy : overlaying debt instruments on top of an existing portfolio.

Barclays U.S. Aggregate Bond Index, 1-3 Year : This index is the 1-3 Yr component of the U.S. Aggregate index.

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.

U.S. Treasury Bond : a debt security issued by the United States government.

Barclays Rate Hedged U.S. Aggregate Bond Index, Negative Five Duration : Combines long positions in the Barclays U.S. Aggregate Bond Index with short positions in U.S. Treasury Bonds to provide a duration exposure of -5 years. Market values of long and short positions are rebalanced at month-end.