

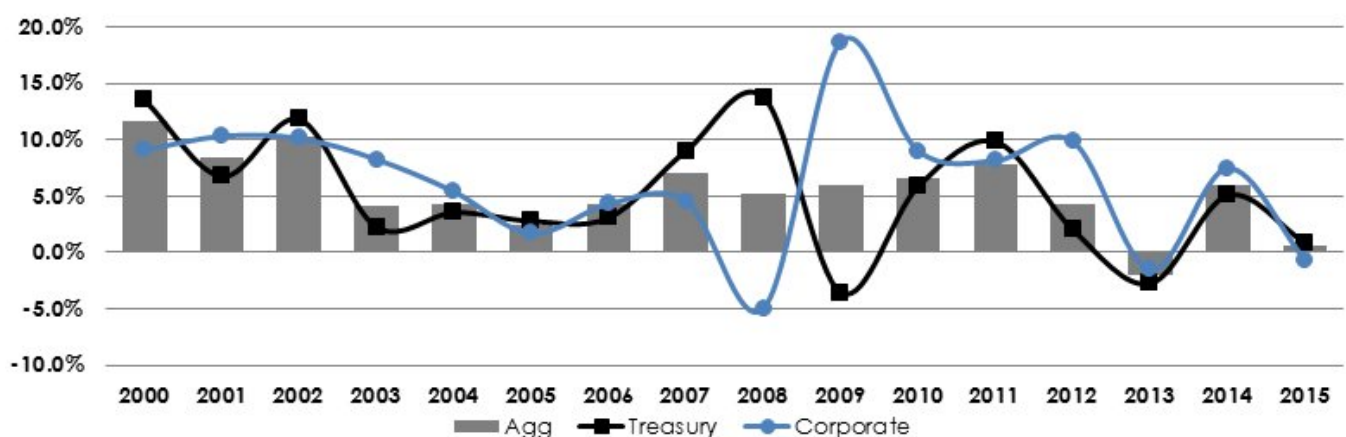
Corporates over Treasuries: Unlocking Value in the Barclays U.S. Aggregate Index

Published February 26, 2016

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Over the last several months, we have spent a great deal of time attempting to understand [what drives performance and volatility](#) of the Barclays U.S. Aggregate Index (Agg). While we remain convinced that simply owning the Agg as an investment strategy is suboptimal, we cannot ignore that it remains one of the most benchmarked indexes in the world. In response, WisdomTree sought to create an approach that started with the same investable universe but ultimately aimed to enhance the yield of the strategy. In the remainder of this discussion, we examine how over-weighting exposure to corporate debt, one common way investors can boost yield, ultimately fared relative to U.S. Treasuries and the broader U.S. aggregate. **Fixed Income 101** For fixed income investors, the single most important determinant of a bond's total return is its yield at the time of purchase. All else being equal, if investors can boost the yield of their portfolios, their hypothetical total returns also increase. The simple reason why higher-yielding securities don't always outperform U.S. Treasuries is because credit conditions evolve over time and there is at least some risk that you may not be paid back. In exchange for assuming this risk, investors receive greater income potential. In order to boost income potential, the Barclays U.S. Aggregate Enhanced Yield Index increases weight to the higher-yielding securities in the Agg, subject to a series of constraints. Generally speaking, this results in a portfolio that is under-weight U.S. Treasuries with increased exposure to investment-grade corporate debt. Below, we show calendar-year returns of the Agg compared to returns of Treasuries¹ and corporate² bonds since 2000. **Agg, Treasury & Corporate Bond Total Returns**



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

Key Takeaways While the Agg has enjoyed positive total returns for every year shown above (except 2013), returns will likely be constrained going forward unless interest rates continue to fall. While economic uncertainty has benefited Treasuries at the expense of corporates so far in 2016, we believe corporates will likely outperform once rates start to rise, given their higher starting yields. In fact, corporates have outperformed Treasuries in 9 out of 16 calendar years. Given the increasing concentration in U.S. Treasuries in the Agg over this period, corporates have also tended to outperform the Agg in 10 out of 16 calendar years, including 4 out of the last 6 since the global financial crisis. In the most recent rising-rate period of 2004–2006, corporates enjoyed a period of solid outperformance compared to Treasuries and the Agg. As shown above, Treasuries tend to outperform corporates during recessions or other periods of prolonged stress. Today, the market remains locked between two opposite forces: [concerns about a marked slowdown in global growth](#) vs. potential interest rate hikes by the Federal Reserve. In our current view, the probability of a global recession remains remote. In response, we believe a more intuitive approach to the Agg may be to over-weight the more attractive segments of the market (credit, securitized) and under-weight the most vulnerable, least appealing sector, such as U.S. Treasuries. With these principles in mind, WisdomTree helped develop the Barclays U.S. Aggregate Enhanced Yield Index, which seeks to enhance the yield of the Agg by over-weighting the higher-yielding segments of the market. [Read more about WisdomTree income strategies.](#) 1As represented by the Barclays U.S. Treasury Index. 2As represented by the Barclays U.S. Corporate Investment Grade Index.

Important Risks Related to this Article

Fixed income investments are subject to interest rate risk; their value will normally decline as interest rates rise. In addition, when interest rates fall, income may decline. 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.