4 drivers of return in the bond market

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If you think about the construct of the bond market, there are really four things that drive return over time. There really is no strategy that works in every market. That's why it's important to be flexible.

So duration, credit, currency and inflation work very differently in different environments. So take **duration** first, that's a big one that we talk about and hear about in fixed income as a matter of concern. When the economy is slowing and inflation expectations are coming down, oftentimes the Federal Reserve is taking interest rates lower and that tends to be an environment where you want more duration or more interest rate risk in a portfolio. So as we think about getting towards the end of a business cycle and the Fed taking rates lower, it's a good time to have duration in a portfolio as a balance to other risks. For example, **credit** risk is one that you want to be reducing as you get towards the end of a credit cycle. And we want to be really careful in this environment, particularly in those companies, in those industries that are more highly levered to reduce our exposure there and balance it with duration.

As it relates to **currency** exposure. I would be very cautious there. The U.S. dollar is very expensive right now by historical standards, but there is no indication that it's going to be coming down anytime soon. So as we look at currency exposure, we don't want to take a lot of foreign currency exposure because what we see is that investors are still flocking towards the US for the relatively higher level of yield.

And lastly, from an **inflation** standpoint, that's a risk you want to take as you're coming out of an economic recession and you're increasing inflation expectations as demand is coming back. So I think that could be something we start to see perhaps the end of 2020 as inflation expectations move up.

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