SN VALUATION

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Bond Unwinding

If one takes a look at a typical fixed income portfolio, you will notice most of the bonds were purchased near par, or above it. I would say 90% of a bond was purchased at par or above. The long term implication is a devaluation of the portfolio as the bond approaches maturity. Also, with rates at historic lows and an improving economy, the FED may take a more hawkish stance in the next couple years and start increasing rates, thereby further devaluing the bonds, from the unprecedented historic highs seen today. So, if a bond has an average weighted nominal coupon rate of 6%, the total return on the portfolio will be south of the 6%. The reason why there was a flurry to the fixed income space was 1) safe haven, 2) more importantly, the bonds which were selling at depressed prices during the Great Recession at 20-40 range, appreciated like an equity and investors were reaping 15-25% annual returns during the past couple years. Now that fixed income prices have stabilized for the most part and interest rates globally have hit bottom, the only investment proposition provided by the fixed income portfolios is 1) safety haven. We can anticipate returns very near the average weighted coupon rate of the portfolio from now on.