

P I M C O

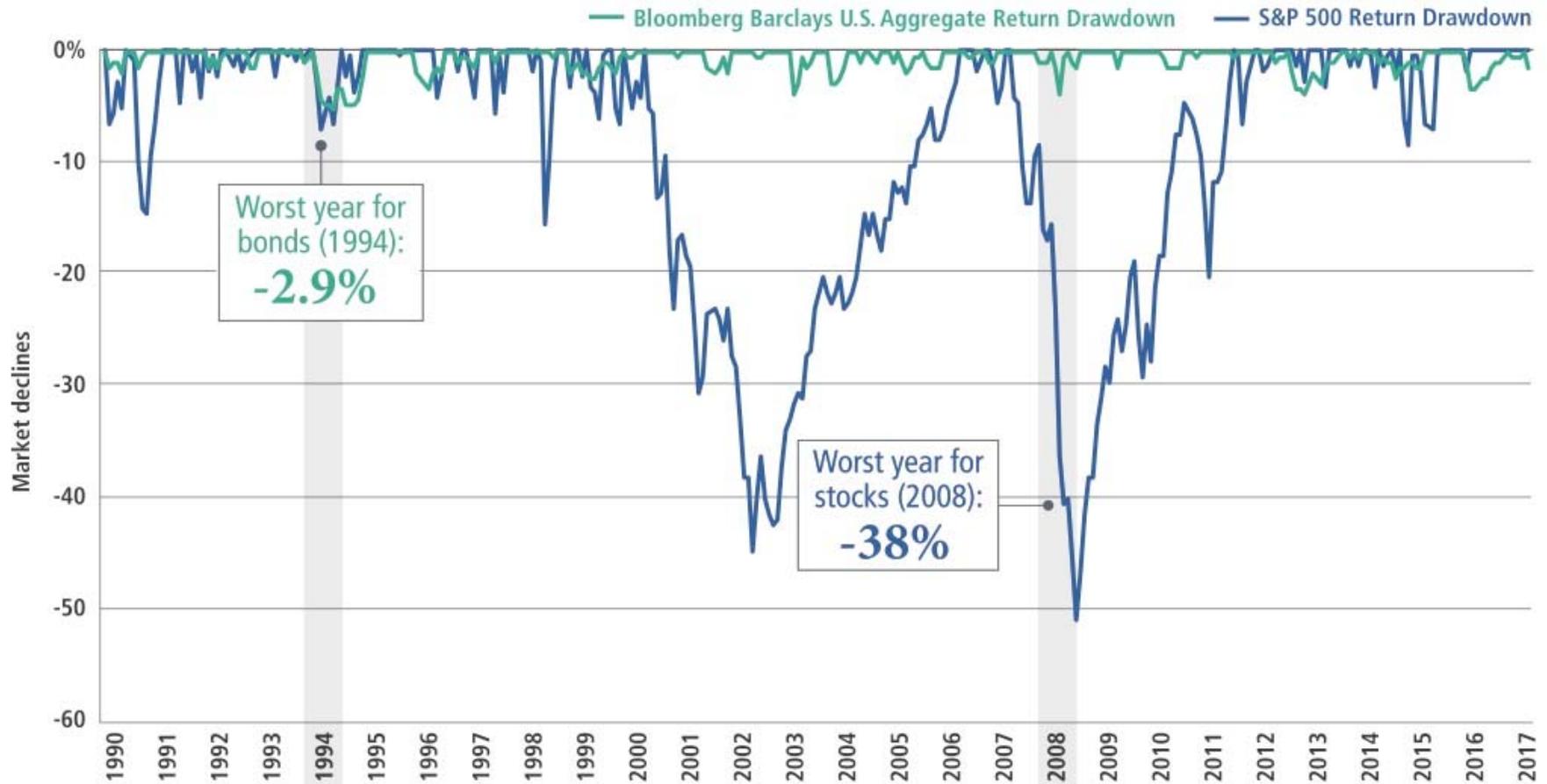
---

# Rates and Bonds



Most investors are familiar with the bond “seesaw” showing the inverse relationship between bond prices and interest rates – when one rises the other falls. But the reality is much more nuanced. Here we highlight the three important reasons why bonds may be a valuable part of a diversified portfolio across rate environments.

# Bond declines have tended to be modest and short-lived



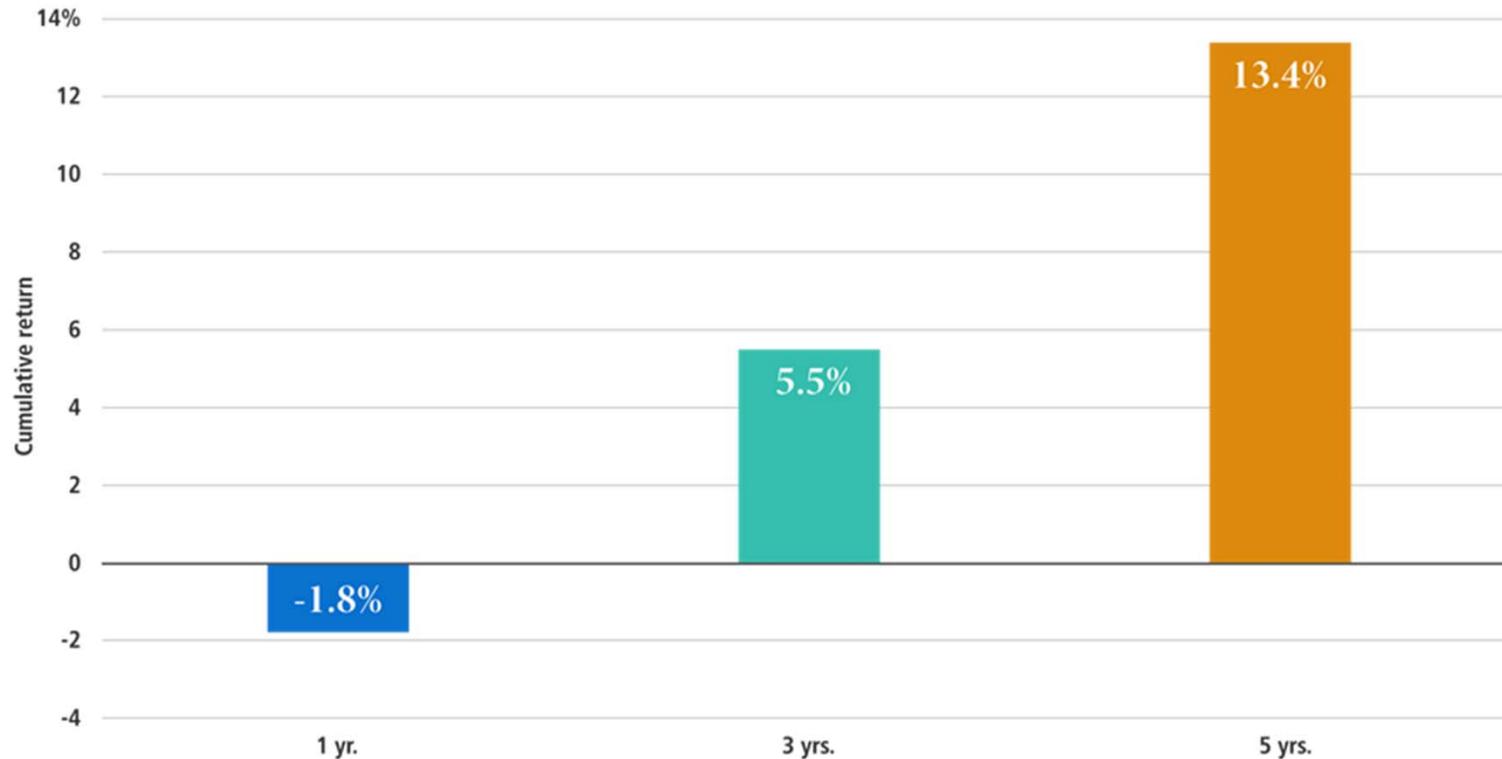
Performance quoted represents past performance. Past performance is not a guarantee or a reliable indicator of future results.

Source: Morningstar Direct. Chart shows U.S. stock and bond declines beginning December 1989 and ending December 2017.

Stocks are represented by the S&P 500 Index, bonds by the Bloomberg Barclays U.S. Aggregate Index. Worst years are calendar years.

Bonds have historically been used for capital preservation, income and growth, and diversification due to their low-to-negative correlations to stocks – essential goals for many investors. Bonds, particularly core bonds, have also been less volatile than stocks. In fact, bond declines have been dramatically less severe than stocks and usually short-lived.

# Rising rates build income



**Hypothetical example for illustrative purposes only.**

Source: PIMCO, as of 31 December 2017. The chart shows the estimated performance of the Bloomberg Barclays U.S. Aggregate Index assuming a parallel rate rise of 1%, and no further changes in rates thereafter. Credit spreads are assumed to remain constant. In the analysis contained herein, PIMCO has outlined hypothetical event scenarios which, in theory, would impact the index returns as illustrated in this analysis. No representation is being made that these scenarios are likely to occur or that any portfolio is likely to achieve profits, losses, or results similar to those shown. The scenarios do not represent all possible outcomes and the analysis does not take into account all aspects of risk. Total returns are estimated by re-pricing key rate duration replicating portfolios of par-coupon bonds.

Because interest income is the primary driver of bond returns, the ability to reinvest into a gradually rising rate environment has the potential to help build long-term growth. When rates rise, new bonds pay a higher coupon, increasing the income investors receive. By contrast, higher rates can be a headwind for equity investors, as increased borrowing costs weigh on corporate profits.

An increase in a bond portfolio's income also helps to offset the negative impact on its declining price. Over time, rising income may provide a return advantage for investors.

# Rising rates don't impact all bonds the same

Date range	Rate hike (basis points)	Performance during past periods of Fed tightening							
		U.S. Treasury	MBS	Investment grade credit	Munis	High yield	Non-U.S. developed	Emerging markets	Senior floating rate
29 March 1988 to 24 Feb 1989	325	3.92%	5.27%	5.21%	7.44%	n/a	4.83%	n/a	n/a
4 February 1994 to 1 Feb 1995	300	-2.69%	-0.49%	-3.93%	-3.56%	-1.74%	-3.55%	-21.70%	n/a
30 June 1999 to 16 May 2000	175	3.27%	2.27%	0.10%	-0.16%	-2.27%	5.07%	14.92%	n/a
30 June 2004 to 29 Jun 2006	425	5.41%	6.80%	5.85%	9.30%	14.88%	9.49%	25.44%	12.38%

Source: BofA Merrill Lynch U.S. Treasury Master Index; Bloomberg Barclays U.S. Agency Fixed Rate MBS Index; Bloomberg Barclays U.S. Credit Index; Bloomberg Barclays Municipal Index; Bloomberg Barclays U.S. High Yield 1% Issuer Cap Index; JP Morgan GBI Global Ex-U.S. USD Hedged Index; JP Morgan EMBI Global Index (measures external debt); Credit Suisse Institutional Leveraged Loan Index. The high yield, EM and senior floating rate indexes did not exist during periods marked n/a. Non-U.S. developed data is through the nearest month end.

News about the bond market typically focuses on U.S. Treasuries, which tend to be the most sensitive to changing rates. In reality, the bond market is exceedingly diverse and global, and each sector or asset class responds differently to economic and market trends. Some, such as floating rate and high yield bonds, actually have tended to do well in a rising rate environment.

Although a market event may temporarily depress prices across the board, skilled active bond fund managers can diversify a portfolio in an effort to defend against threats to capital while also seeking to capture a range of growth opportunities for their investors.

# Disclosure

---

**Past performance is not a guarantee or a reliable indicator of future results.**

**All investments** contain risk and may lose value. Investing in the **bond market** is subject to risks, including market, interest rate, issuer, credit, inflation risk, and liquidity risk. The value of most bonds and bond strategies are impacted by changes in interest rates. Bonds and bond strategies with longer durations tend to be more sensitive and volatile than those with shorter durations; bond prices generally fall as interest rates rise, and the current low interest rate environment increases this risk. Current reductions in bond counterparty capacity may contribute to decreased market liquidity and increased price volatility. Bond investments may be worth more or less than the original cost when redeemed. **Equities** may decline in value due to both real and perceived general market, economic and industry conditions. **Diversification** does not ensure against loss.

**Management risk** is the risk that the investment techniques and risk analyses applied by investment manager will not produce the desired results, and that certain policies or developments may affect the investment techniques available to the manager in connection with managing the strategy. There is no guarantee that these investment strategies will work under all market conditions or are suitable for all investors and each investor should evaluate their ability to invest long-term, especially during periods of downturn in the market. Investors should consult their investment professional prior to making an investment decision.

This material contains the opinions of the manager and such opinions are subject to change without notice. This material has been distributed for informational purposes only and should not be considered as investment advice or a recommendation of any particular security, strategy or investment product. It is not possible to invest directly in an unmanaged index. Information contained herein has been obtained from sources believed to be reliable, but not guaranteed.

PIMCO provides services only to qualified institutions and investors. This is not an offer to any person in any jurisdiction where unlawful or unauthorized. | **Pacific Investment Management Company LLC**, 650 Newport Center Drive, Newport Beach, CA 92660 is regulated by the United States Securities and Exchange Commission. | **PIMCO Europe Ltd** (Company No. 2604517) and PIMCO Europe Ltd - Italy (Company No. 07533910969) are authorised and regulated by the Financial Conduct Authority (12 Endeavour Square, London E20 1JN) in the UK. The Italy branch is additionally regulated by the Commissione Nazionale per le Società e la Borsa (CONSOB) in accordance with Article 27 of the Italian Consolidated Financial Act. PIMCO Europe Ltd services are available only to professional clients as defined in the Financial Conduct Authority's Handbook and are not available to individual investors, who should not rely on this communication. | **PIMCO Deutschland GmbH** (Company No. 192083, Seidlstr. 24-24a, 80335 Munich, Germany), PIMCO Deutschland GmbH Italian Branch (Company No. 10005170963) and PIMCO Deutschland GmbH Swedish Branch (SCRO Reg. No. 516410-9190) are authorised and regulated by the German Federal Financial Supervisory Authority (BaFin) (Marie- Curie-Str. 24-28, 60439 Frankfurt am Main) in Germany in accordance with Section 32 of the German Banking Act (KWG). The Italian Branch and Swedish Branch are additionally supervised by the Commissione Nazionale per le Società e la Borsa (CONSOB) in accordance with Article 27 of the Italian Consolidated Financial Act and the Swedish Financial Supervisory Authority (Finansinspektionen) in accordance with Chapter 25 Sections 12-14 of the Swedish Securities Markets Act, respectively. The services provided by PIMCO Deutschland GmbH are available only to professional clients as defined in Section 67 para. 2 German Securities Trading Act (WpHG). They are not available to individual investors, who should not rely on this communication. | **PIMCO (Schweiz) GmbH** (registered in Switzerland, Company No. CH-020.4.038.582-2), Brandschenkestrasse 41, 8002 Zurich, Switzerland, Tel: + 41 44 512 49 10. The services provided by PIMCO (Schweiz) GmbH are not available to individual investors, who should not rely on this communication but contact their financial adviser. | **PIMCO Asia Pte Ltd** (8 Marina View, #30-01, Asia Square Tower 1, Singapore 018960, Registration No. 199804652K) is regulated by the Monetary Authority of Singapore as a holder of a capital markets services licence and an exempt financial adviser. The asset management services and investment products are not available to persons where provision of such services and products is unauthorised. | **PIMCO Asia Limited** (Suite 2201, 22nd Floor, Two International Finance Centre, No. 8 Finance Street, Central, Hong Kong) is licensed by the Securities and Futures Commission for Types 1, 4 and 9 regulated activities under the Securities and Futures Ordinance. The asset management services and investment products are not available to persons where provision of such services and products is unauthorised. | PIMCO Australia Pty Ltd ABN 54 084 280 508, AFSL 246862 (**PIMCO Australia**). This publication has been prepared without taking into account the objectives, financial situation or needs of investors. Before making an investment decision, investors should obtain professional advice and consider whether the information contained herein is appropriate having regard to their objectives, financial situation and needs. | **PIMCO Japan Ltd** (Toranomon Towers Office 18F, 4-1-28, Toranomon, Minato-ku, Tokyo, Japan 105-0001) Financial Instruments Business Registration Number is Director of Kanto Local Finance Bureau (Financial Instruments Firm) No. 382. PIMCO Japan Ltd is a member of Japan Investment Advisers Association and The Investment Trusts Association, Japan. Investment management products and services offered by PIMCO Japan Ltd are offered only to persons within its respective jurisdiction, and are not available to persons where provision of such products or services is unauthorized. Valuations of assets will fluctuate based upon prices of securities and values of derivative transactions in the portfolio, market conditions, interest rates and credit risk, among others.

# Disclosure

---

Investments in foreign currency denominated assets will be affected by foreign exchange rates. There is no guarantee that the principal amount of the investment will be preserved, or that a certain return will be realized; the investment could suffer a loss. All profits and losses incur to the investor. The amounts, maximum amounts and calculation methodologies of each type of fee and expense and their total amounts will vary depending on the investment strategy, the status of investment performance, period of management and outstanding balance of assets and thus such fees and expenses cannot be set forth herein. | **PIMCO Taiwan Limited** is an independent management company (Business license number is (107) Jin Guan Tou Gu No.001), registered by Financial Supervisory Commission. 40F., No.68, Sec. 5, Zhongxiao E. Rd., Xinyi Dist., Taipei City 110, Taiwan (R.O.C.), Tel: +886 (02) 8729-5500. | **PIMCO Canada Corp.** (199 Bay Street, Suite 2050, Commerce Court Station, P.O. Box 363, Toronto, ON, M5L 1G2) services and products may only be available in certain provinces or territories of Canada and only through dealers authorized for that purpose. | **PIMCO Latin America** Edifício Internacional Rio Praia do Flamengo, 154 1o andar, Rio de Janeiro - RJ Brasil 22210-906. | No part of this publication may be reproduced in any form, or referred to in any other publication, without express written permission. PIMCO is a trademark of Allianz Asset Management of America L.P. in the United States and throughout the world. ©2018, PIMCO.