

What's Going On with the Bond Market?

We had a number of questions and we obviously talked about it in the strategy report. What in the world is going on with the bond market? And the the one question that was submitted is it was almost like an AI prompt. Pretend I'm in the third grade when the world's going on with the bond market. Explain it that simply. If we look at what. Here we show some returns of our Money for the Rest of Us fixed income model portfolio as well as the Vanguard Total Bond Market ETF.

That's the orange bar. And that basically replicates the overall U.S. bond market as represented by the Bloomberg Aggregate Bond Index. So just in investment grade bonds, what we can see that that that bond market is down 2% year to date. And that's because bonds follow math. When interest rates go up, the price of bonds fall. And the reason why they fall is because the newly issued bonds are issued at the prevailing interest rates. So right now, the yield to maturity on the aggregate or BND is around 5.5%.

And if you're holding, let's say, a ten year treasury that's only yielding 3%, the coupon payment is 3%, and that price of that bond has to fall enough that the actual coupon payment divided by the new price equals the prevailing interest rates. In this case, let's say five, 5.5%. And so that's when interest rates fall, the value of bonds go up.

And when interest rates go up, the value of bonds fall. And that's what we've seen this year. The question is why. And will it continue. And we spent a lot of time in in this past strategy report and earlier ones explaining what's going on. And nobody knows exactly why bond markets, there's trillions of dollars traded every day. We have some pretty good educated guesses. We there's a a huge amount of issuance of corporate bonds coming out, much of it tied to AI.

And so that increased supply. And if the demand hasn't kept up, then interest rates are going to go up to just the way supply and demand works. That's one reason. The second reason is inflation has surprised to the upside, and that has led the Federal Reserve, which is seeking price stability. They haven't they're not they haven't got it yet. And with the inflation report came out yesterday is really inflation has accelerated.

So the Federal Reserve raised its policy rate and will probably do so again either in October or December, depending on what the data looks like. And when you invest in bonds, you can invest in a series of short term bonds and roll them over. So I'd say a six month maturity bond. It matures. You buy another six months. And so you can just keep rolling short term bonds for ten years. Or you can just go and buy a ten year bond.

And the, the, there's some linkage to the yield on the ten year bond. It's tied to short term interest rates and expectations for future short term interest rates. And so the expectation is that short term interest rates would go up because the Fed is raising the policy rate. That has put some upward pressure on yields. And then finally, there's the what makes up the yields of bonds is that expectation for short term interest rates, the expectation for inflation, which hasn't really changed that much.

A five year inflation expectations are still 2.5%. But then there's this additional term premium or incremental yield that investors demand to hold bonds for uncertainty. And that is, as we mentioned in the strategy report, gone up over 1%. And that is its highest level since 2010. And so that is what has led to a an increase in yield this year, half a percent or more, depending on the maturity. And so that's what's going on.

Should You Sell Your Bond Funds?

What do we do about it? And that's where some of the other questions were. Now we show the returns here over the past any time period, but let's say the past three years. The our model portfolio has returned 4.9% and it's outperformed. In fact, it's outperformed the Vanguard Total Bond Market ETF really every period since inception. The reason it does is we've structured a bond portfolio that is has a higher yield to maturity than than the overall bond market, but less interest rate sensitivity.

So lower duration. And those are the holdings in there. And so it's yielding 6%, but the duration is, is much less. And so as interest rates go up, the value falls not as much as the overall bond market. So the question is, well should we get rid of something like the State Street DoubleLine Total Return ETF? Or if you own a mutual fund version, it's the DoubleLine Total Return Bond Fund. Similar holdings. It's got a duration of almost six years and a I yield to maturity of 6%.

We haven't, because we're managing a bond portfolio made up of a number of ETFs. So we're not trying to we're trying to basically manage the risk and opportunities because we are earning 6% in total and over 7% in DMX and in DMX has a duration of three years. So it's taking more credit risk. So we're trying to, to weight the different risks because there is no guarantee that interest rates are going to go up. And so as a bond investor, I've always focused more on yield.

And if, if our holding period is 6 to 7 years. So these are long term portfolios. We're gonna that's basically what we're going to earn over the next 6 to 7 years, irrespective of what interest rates do. Because again, going back to kind of the third grade explanation that the best estimate of the return for a bond fund or ETF is its starting yield to maturity if your holding period is seven years, because if interest rates go up and the price falls, you're now reinvesting or the ETF manager is reinvesting at those higher yields.

So you're getting additional income that's offsetting those losses. And after about 6 or 7 years, then you're you're in very good shape.

What If Rates Rise Another 1%?

So this is our expected return model. And like I said, our best estimate of return for bonds is a starting yield to maturity. And what you can do is we can say, okay, well, what if interest rates go up 1%? And if that happens, the price falls by just about its duration. So 5.7 years, but now you're getting an additional 1% a year in interest. So. And which then as that compounds your ten year return is 5.9%. So pretty close to the starting of the maturity. Now it takes a while to recover.

So if we go out three years actually we go out two years after that. Well let's just do one year, right? The price fell, then we got 1%, and then we're here at 0.4% return. But after two years, we're starting to

recover those losses from the interest income after. And let's say after five years, we pretty much have close to recovered. And that's why I say if you hold seven, six, seven, eight years, you're going to regain that.

So just because interest rates going up, we're not in a period where inflation is rising. I mean it's rising, but inflation expectations haven't increased. And so no, I haven't sold the intermediate term bond funds in my portfolio because I have shorter term bonds that complement that. And I'm trying to kind of create an overall portfolio that yields more than the overall bond market, but has a lower duration. Now, that doesn't mean that we should never sell.

I mean, if your time horizon is shorter or let's say you're entering retirement, you want to lock in, you just don't want to, you want to lock in some yields. Then you can use a bullet or a ETF that matures on a certain date. You can lock in those yields. And so it's not like we never sell. But when we have models, we have all kinds of people that look at the models and we're, we're managing a, a model in an overall portfolio that is made up of individual ETFs.

And so hopefully that gives you an explanation that even with something, something like DoubleLine, if you hold it 5 to 7 years, you're going to earn it starting into maturity, which right now is very attractive at 6%.

Revisiting Past Sales

Another question I had from one of our Plus members was regarding whenever I make, I share my portfolio and my holdings and my trades. And when I make a trade, I say, well, here's why I did it.

If I sold or if I bought, here was the thesis and and if it was a sell, how did it work out? Well, we had an interesting question from members like, well, what about several years later. What if you go visit what you sold and see how it did? And that's fair. And I like to be transparent. So I went back from all the sales that I had that a, an ETF or fund actually exited my portfolio. So this doesn't include where I took profits and cap exposure.

So for example, I recently reduced some exposure in small cap. And last year I sold some gold and Bitcoin, but I continued to hold it. So these are actual holdings. And I thought it would be interesting to kind of go through very quickly what I did and what has happened since. And the the reasons to sell generally is you're wrong or whatever thesis you had to buy, it just didn't work out. That's one reason. The second reason is there's a better opportunity.

And so as you weigh potential opportunities, you see something that's more attractive. So you sell something you have to, to invest. Third reason is you need the cash. You need the money. And part of that could also be, here's an opportunity to sell, to realize a loss, to offset a gain so there could be some tax loss harvesting aspect to it.

Simplifying the Portfolio in 2022

But when you look at how to go through these really quick. So back in 2022, I in July, I saw I made a number of trades to simplify my portfolio. And one of them was the Global Renewable Energy ETF. This was I bought back in 2017, and I was investing in a relatively new asset class called yieldcos and yieldcos

were renewable energy, but they had very attractive yields. And and basically a lot of them just converted and they weren't there anymore.

And so then the ETF I was in, I think it was y ae changed its name, changed its ticker. And so I exited. And in that case, I exited in July. It hasn't done terribly well since then. -6.3% annualized, 8.5% while I held it. Next one was Vanguard. You know, a lot of these, the Vanguard FTSE Emerging Markets ETF I had existing exposure. And so I just again, this was part of simplification. I had bought it in 2017. I sold in 2022.

Emerging markets had had a tough stretch over that five years, but it's done well since then 12.3% annualized. But again, I already had the emerging markets or WisdomTree Emerging Markets High Dividend ETF, DEM, and that's actually outperformed VWO. Since I sold this holding, it's returned 17% annualized. I also exited the MSCI India ETF. And again, same reason I had an existing ETF that I have since added to the Wasatch Emerging India Fund, and that's actually outperformed the India since I exited that.

So that worked out fine. Tweedy Browne Global Value Fund that that was an experiment I did in 2020. I decided to add some classic value active manager funds and that didn't work out. I sold this one in 2022, and the other one I bought at that time, we talked about last month in our live stream Longleaf. How long would it take to figure out Longleaf was was skilled and it would take a thousand years. I sold that last month. This one I sold in 2022. It's done.

It did -0.7% annualized while I held it. It's done 10% annualized since then, but I also already had a non-U.S. value ETF, IVLU, and that massively outperformed Tweedy Browne. It did 29% annualized since 2022. I sold iShares United Kingdom Small-Cap ETF. I had, I was kind of going through my experiments holding some more individual country ETFs. And I find I'm just I don't enjoy doing that. I don't necessarily have an edge. I exited this, it didn't do well while I held it. You can see down 11% annualized. It has since returned 8% annualized, but I already had small cap exposure that did better. It's done better than than the UK, I would say.

Two Simplify ETFs I Sold Too Early

So the other one is Simplify Interest Rate Hedge ETF. So this was an ETF that was seeking to hedge rising interest rates.

I bought it in September 2021. Did very very well. I shouldn't have sold it. I sold too early. I earned 34% annualized over that period. But in all of 2022, I sold in July, it earned 92% that year. It was very volatile and that that volatility made me I just wasn't quite comfortable with that level of volatility and the interest. The rising interest rate pressure was less. So I exited after a gain, but I admittedly I sold that one too early. It's returned 13.5% annualized since I sold.

Another ETF that I. I would admit I sold too early it. Another Simplify Volatility Premium ETF, SVOL. This was a an ETF that was selling. It was selling. I was thinking was it puts. I think it was it was put to future exposures on on VIX. So the volatility risk premium baked into the S&P. So it was like selling insurance

and it was getting a really high premium for doing that. We just we discussed this type of strategy in Money for the Rest of Us episode 565.

And you know, so what's a reasonable expectation expectation for this? I'm in WTPI, which is selling puts on the S&P 500, but this was actually selling exposure to to VIX or volatility, which is actually a much more volatile approach. And you actually have to to to basically they were buying some longer term puts or puts that were out to protect against large losses that can occur with this kind of strategy.

And then not to get too technical here, but the, the yield curve or the VIX curve had switched to where the you weren't making money on this thing. And I just I, and I didn't I don't I don't think I understood the ETF as well as I would have liked. And it and part of it was just I when you are selling exposure like this, there is the potential for big drawdowns and I and that that worried me the way the yield curve or the VIX curve has had switched, but it's returned 13.2% annualized.

I lost 7%. Should I have held maybe I got this type of exposure through WTPI and it's returned 14.8% since October 2022. So it's done better. That one is just simply for me to understand. But you could say that was I should have continued to hold.

Taking Profits on AI and Closed-End Funds

All right. Just a few more. The Aberdeen Global Infrastructure Fund this originally I bought was a the Macquarie First Trust Infrastructure Fund MFD, and they it was merged there was a proxy battle I bought when it was. It was a closed end fund. It was at a 14% discount. It. It narrowed down to 4% and I decided to take profit. So it returned 11.4% while I held it. It's returned 9% annualized since. These next three funds I sold at the same time, and the first two Harbor and iShares Exponential Technologies ETF.

This was my. I was playing AI, so this was you'll recall that ChatGPT came out in November 2022. I bought these two ETFs in July 2023 and sold them after they did. Or at least Harbor did very well, 31% annualized. But the valuations got more expensive or very expensive. And I decided to reallocate the small cap equity. Both have done well since, but the the small cap funds that went in the VSS and AVDV have also done very, very well, if not better.

The I also sold Schwab Fundamental International Small Cap ETF, Small Cap Equity ETF, FNDC, at the same time, again to invest in VSS and AVDV. Barings Corporate Investors. This was a private credit closed end fund that I bought in 2022. I sold in February 2025 after it rose to a premium of 36%. A premium has now narrowed. It's like a 7% premium, but it's returned nine -9.1% annualized since I exited. Whereas I returned, I earned 29% annualized while I held it because I bought it at a discount, and then it went to a premium.

And finally the DoubleLine Income Income Solutions I sold for the same reason I bought at a discount. It traded at par and I earned 5.5% annualized. And it's negative since. So maybe that wasn't terribly helpful.

Or not it. A member asked about it. I sometimes after you sell it, it things you sell too early. And I gave some examples of that. Sometimes you sell. And it was good timing because the it fell. And a lot of times

I sold because it was a better opportunity or I wanted to take profits. And then that's what's going on with that.

Lending Money to Family

So a member asked about loaning money or borrowing money from a family member in this case, and this member is doing a remodel is a very good relationship with their parents, and the parents are willing to lend for this remodel. And the question of, well, how do you go about it? And this is something that I have done to family members. I have lent money. One of his questions is, well, what interest rate?

If you lend money to a friend or family member in the U.S., you have to charge a minimum interest rate, which is called the applicable federal rate. And here's where they are as of October. So for example, we have one small loan outstanding to a family member, a student loan and its variable rate, and I just. Every month we charge the this midterm rate, whatever it is. And this is pretty informal loan. So in this case, I just didn't really do any paperwork. It. It's fine.

Like if they if they don't pay, they don't pay, but a small amount, something like \$100,000 or we've, I've done a mortgage loan to family members that's documented so that there is a contract.

Everybody knows upfront what happens if there's non-performance. And so I think it just makes sense to document larger amounts just in case something happens. Somebody could pass away. And and so and I've done this with other loans I've done to friends like I trust them, but what if they die and their beneficiaries? There needs to be some documentation. So I think it's important to have a good relationship with whoever you're lending to that there's definitely agreement, but it can be a way for you can help out family members.

So we've typically given kind of low interest or below market rate loans on our family loans that we've done. But it's definitely if it's a bigger amount, it's documented and, but we can't go any lower than these applicable federal rates.

Time-Weighted vs. Money-Weighted Returns

All right. Another question we had was, and I'll obviously share these slides if you're if you're listening to it later. But there's a question on how do you what are the just kind of a review of the different ways to calculate investment returns. What we generally use on Money for the Rest of Us Asset Camp. If you look at the returns, for example, on Asset Camp, the ten year returns those are those are called time weighted returns. And we usually show a the annualized version.

And so by time weighted it ignores the impact of cash flows or the timing of cash flows. So it there's we include a formula there, but you can. The formula is pretty simple. You have you calculate it monthly. You have the ending. Or you can do it daily. But let's say monthly you have your ending value and you subtract out new money that went in and you add back money that was withdrawn. And you divide by the beginning value minus one, and that gets you a percent return for the month.

And then those are linked every every month, or it can be done daily. And this is what you see if you're on Morningstar, they'll they're using time weighted returns. And so whether a bunch of money flows in or out of that ETF, it doesn't make a difference because we adjust for that in the formula. And that's

that's the standard way you can show it on a cumulative basis. And so you just sort of link all of those monthly returns and that gets you a number.

Or you can annualize it and include the formula there. I am used to annualized returns. To me, that's just more intuitive. It's not the same as the average. So it's not every year, but it's sort of on average, if it's compounding what is kind of that annual return, if it's lack of a better word, annualized, the other way that is often done where the manager has some control of whether the money flows in or out.

And this would be, let's say, a private equity fund or a venture capital fund where they're doing capital calls and they're doing distribution there. We do what's known as a money weighted return or a dollar weighted return, and it is a discounted cash flow type thing. And so money that's received 15 years later and that's discounted to today, it's now worth as much. So it lowers the return. So the faster the money comes back, the higher this.

What's essentially an internal rate of return is what it's called. But it's also called a dollar weighted return. And so I, I've been in some private capital fund of funds. And I look at the, the internal rate of return over time. Now this gets a little messy if you're, let's say an a university endowment, because the top line, you're showing annualized return for your entire portfolio, but which means you're kind of showing time weighted return for your entire portfolio, even though you have elements that the correct measures an internal rate of return.

And so it can get a little complicated, but you can use this as a reference. And but those are the main ways to calculate it. We include some other there that I won't go into here. And then we hop in and see if what other questions we might have.

What Criteria Do You Use to Sell?

The first question is what criteria do you have to find and sell ETFs that meet your requirements?

Well, I look at valuations. And so most most of my portfolio I'm I like to think I don't trade very much. But it ends up being 3 or 4 trades a year like a lot of them I just own for a long time. But if there's let's say an example trades I did this year, right. I, I had bought WINN so the Harbor and, and the iShares that was focused on growth was focused on AI. And I was sort of, I knew this was going to be fairly short term.

And when valuations got too high, I decided to sell because I looked at Asset Camp and saw that the most attractive area was non-U.S. small cap value. And so in that case I invested in there. And so then last month as and we've talked about it in our live streams valuations of small non-U.S. small cap value. They're still below average but they're not as cheap as they were. And VSS, or not VSS, the AVDV had returned essentially almost 50% on a 50% annualized, but very, very high since December 2024. And I decided I would take some profits. And so. So I think valuation is probably the primary thing I look for when selling ETFs where.

And that's one reason we created Asset Camp or are we doing on Plus membership. We have the strategy report and we're always looking at is there something more attractive. It's kind of challenging

right now because nothing is terribly attractive because we've had very strong returns for 3 to 5 years. And so then you're sort of kind of weighing, well, do I reduce exposure? Do I take some profits? And that obviously depends on your circumstances. But yeah, I would say fundamental criteria.

I don't like to sell. I would prefer to just to hold them for a very long term. And many of them I have, but I'm also in a situation where I run an education site. And so I share my portfolio. And, and so that does lead me to take. Probably trade more than it would otherwise, just as I do. Experiments, some of which work out, some of which do not work out as I. And I went through some examples today, but certainly the fundamentals is probably the main thing. But then also, you know, if I need cash flow. So if I'm if I need the money, then I'll also sell. Hopefully that that helps.

When Do You Rebalance?

All right. Next question is when do you do rebalancing?

I don't rebalance because I don't necessarily have a target. So I don't have a strategic asset allocation, which I use what I call an asset garden approach. So just a wide variety of asset types. And so I'll kind of rebalance not on on a time schedule, but just when I see something like this gets too big. So the AVDV and it was upwards of 3% of my investable assets, which I mean, it's not that high, but I chose to, to sell and pull it back down to 2% because I, my, my portfolio, my, I believe my equity portfolio is still half, 50% small cap.

Now, my equity portfolio is only 18% of my investable assets, but half of it's in small cap. And so if I see something do well, I'll just rebalance by selling. But it isn't so much. I have a target and I'm going to rebalance to the target. When it comes to traditional rebalancing, typically you do a calendar basis. Once a year is what we would do with our institutional clients if they had a target and ranges. If something got out of the range, then they rebalance.

But personally, I'm, I don't have targets. I official targets, I can say that I have ranges that I'm kind of comfortable with in terms of generally 15 to 20% equity, 15% or so in bonds. I have, you know, 5% or so in kind of these managed futures or these option type strategies. I have mentioned that I keep cryptocurrency and gold under 20% of my portfolio. And so I have rebalanced there if it got up to 20%. And so I do rebalance.

I just don't rebalance the targets and rebalance just as I'm watching markets on a monthly basis. And, you know, one reason we do a strategy report is I do it for my own portfolio. I do it for everyone else, but I also want to it gives me an opportunity to see what happened. Where are we now? Where are we heading? And then make my own portfolio decisions based on that, as well as on our models, portfolios, etc.

Building a TIPS Ladder

The next question is what is your view on building a TIPS ladder with some of the total DMX holdings in a retirement account? If you plan to retire in the next 5 to 10 years.

That would be a good reason. So yeah, if someone is planning on retiring and so you. Which means you're going to use the cash flow. And so you do have some exposure to interest rates, then it, it can

make sense to, to do a TIPS ladder, in fact, a brand new tool that we just developed. We haven't really told anybody about it, but as long as you mentioned it, let me let me share this. So under Members Analysis Tools, there's a TIPS ladder tool.

So you click that and you can decide how much do I want in today's dollars each year you can do how many years you want your TIPS ladder for. And it calculates it. And then it, it basically says which TIPS to purchase and how much and the rough yield. And then it kind of gives a few targets, 50,000. That's about what you get. And, and then there's kind of the summary list of TIPS. So there's another tool is TIPSLadder.com. I find that website a little more complicated than I prefer. And so we recently built this one. And you can.

And so check that out again. That's under Members Analysis Tools. It's our TIPS ladder tool. So bottom line is that yes if you're retired having some type of cash flow in the first few years, TIPS are attractive right now. So just go back to the TIPS like the real yields are over 2% and that's before inflation. So you get 2.5% plus inflation. And so that if inflation is two and a half, 3%, that's four and a half to 5% return. Pair that to the DoubleLine funds.

One was yielding six, one was yielding seven. But this way you guarantee basically that yield plus inflation. Whereas with an ETF, you they they can fall further in price. If if interest rates keep going up.

We'll be sharing the video of this as well as if you're a Plus member, we edit the audio and publish that as it'll be Plus episode 566. So you can listen to the audio version. We'll create a slide deck, a PDF of the slides, so you can take a look at those. And no, we appreciate everyone being here today.