Five Common Mistakes When Investing in Fixed Income

POTENTIAL BENEFITS OF ACTIVE MANAGEMENT

THE "RISK" IN RISK-TO-REWARD IS OFTEN MISUNDERSTOOD

When investors talk about risk, they normally mean loss of principal. Traditional rule of thumb is "the greater the risk, the greater the potential reward." In the fixed income markets, there are many kinds of risks including credit risk, duration risk, interest rate risk and default risk to name a few. In today's low rate environment, many novice investors may have (knowingly or not) increased their risk profile in an effort to enhance the income earned from their investments. **Many of these risks can potentially be mitigated by professional, active management focused on uncovering any hidden vulnerabilities in a portfolio.**

THE SET-IT-AND-FORGET-IT MENTALITY

Passive investors usually think long and hard about their initial investments, but once completed, they often walk away. This set-it-and-forget-it mentality may lead to sub-optimal allocations and missed opportunities over time. **Active management across multiple cycles has the potential to increase risk-adjusted returns since an experienced portfolio management team takes the time to adjust allocations in response to the ever-changing market environment.**

FOCUSING SOLELY ON CREDIT RATINGS

A credit rating is a quantified assessment of the creditworthiness of a borrower. AAA, AA, A, and BBB ratings are considered to be investment grade, while BB, B, CCC/CC/C and D are below-investment grade ratings, which present a greater risk of loss to principal and interest than higher-rated securities. US Government and Agency securities are generally considered to be of the highest quality.

Astute active managers have found that these assigned ratings are often lagging indicators of actual credit quality. In fact, the health of a specific company or even an entire industry can deteriorate quickly and drastically. **Active managers normally monitor both industrywide and credit-specific fundamentals, which we believe is critical to the early detection and potential avoidance of possible landmines.**

BENCHMARK INDEXES MAY BE RISKIER THAN THOUGHT

The Bloomberg Barclays US Aggregate Bond Index is the most widely used core, investment grade, fixed income benchmark, representing over $1 trillion in assets as of 5/31/2020. However, passive investors likely don't realize that this index is comprised of over 70% US government-related securities, which tend to be lower yielding and more interest rate sensitive than other areas of the fixed income markets. In contrast, **active managers have the potential to expand the investable universe and provide access to asset classes not found in many of the more traditional benchmarks,** such as short duration high yield and floating rate securities.

MISSED OPPORTUNITIES FROM INEFFICIENT MARKETS

Unlike equities where the price is quoted on an exchange, the pricing mechanism used for bonds reflects a number of factors including the bond's coupon rate, time to maturity, supply/demand dynamics and credit rating, to name a few. Bond pricing is therefore not nearly as intuitive or efficient, so price discovery and information dissemination, while improving, are still at a premium. **Active management can help bridge the information gap many retail investors face when considering individual bonds.**

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DIFFERENTIATE YOURSELF

AAM partners with institutional and boutique managers that we believe have distinct and proven investment processes. Because these managers primarily serve institutional clients, they are typically not otherwise available to individual investors.

Contact a financial professional to learn more about how actively managed fixed income mutual funds can add value to a diversified portfolio.

All investing involves risk; loss of principal is possible.

You should carefully consider the investment objectives, potential risks, management fees, and charges and expenses of each fund before investing. Each fund's prospectus and summary prospectus contains this and other information about the fund, and should be read carefully before investing. You may obtain a current copy of each fund's prospectus and summary prospectus by calling 888.966.9661.

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Fixed income securities are subject to certain risks including, but not limited to: interest rate risk, credit risk, prepayment risk, inflation risk, default risk and reinvestment risk. The value of most bonds and bond strategies are impacted by changes in interest rates; fixed income securities decrease in value if interest rates rise. Bonds and bond strategies with longer durations tend to be more sensitive and volatile than those with shorter durations. Credit risk is the risk due to changes in the financial condition of the issuer, borrower, counterparty, or underlying collateral. Prepayment risk is the possibility that debt issuers may repay or refinance their loans or obligations earlier than anticipated. Reinvestment risk means a bond or future cash flows will need to be reinvested in a security with a lower yield. Callable bonds have provisions that allow the bond issuer to purchase the bond back and retire the issue when interest rates fall. Default risk occurs when the issuer can't pay the interest or principal in a timely manner or at all. Inflation risk occurs when the rate of price increases in the economy deteriorates the returns associated with the bond. Foreign securities are more volatile, harder to price and less liquid than US securities and are subject to different accounting and regulatory standards, and political and economic risks. These risks are enhanced in emerging markets countries. Bond investments may be worth more or less than the original cost when redeemed. Diversification does not ensure against loss.

Active investing has higher management fees because of the manager's increased level of involvement while passive investing has lower management and operating fees. Investing in both actively and passively managed mutual funds involves risk and principal loss is possible. Both actively and passively managed mutual funds generally have daily liquidity. There are no guarantees regarding the performance of actively and passively managed mutual funds. Actively managed mutual funds may have higher portfolio turnover than passively managed funds. Excessive turnover can limit returns and can incur capital gains.

The Bloomberg Barclays US Aggregate Bond Index is an unmanaged, broad based index composed of US dollar denominated, investment grade, fixed-rate taxable bonds with at least $250 million par amount outstanding and at least one year to final maturity. It is not possible to invest in an index.

Duration is a measure of the sensitivity of the price of a fixed-income investment to a change in interest rates expressed as a number of years. A bond's term to maturity is the length of time during which the owner will receive interest payments on the investment. When the bond reaches maturity the principal is repaid.

A bond rating is a grade typically given by a private independent rating service that indicates a security's credit quality, which is intended to evaluate a bond issuer's financial strength, or its ability to pay a bond's principal and interest in a timely fashion. High-yield bonds are debt obligations with a bond rating of Baa or lower according to Moody's, or BB or lower on the Standard & Poor's scale. Below investment grade (commonly known as "high yield" or "junk") securities are considered speculative and may be subject to greater market and credit risks. Accordingly, the risk of default may be higher than investment grade securities. In addition, these securities may be more sensitive to interest rate changes and may be more likely to make early returns of principal. In limited situations when the rating agency has not issued a formal rating, the rating agency will classify the security as not-rated.

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MUTUAL FUNDS