Common Fixed Income Strategies for Inflationary Times

Series I Savings Bonds and TIPs

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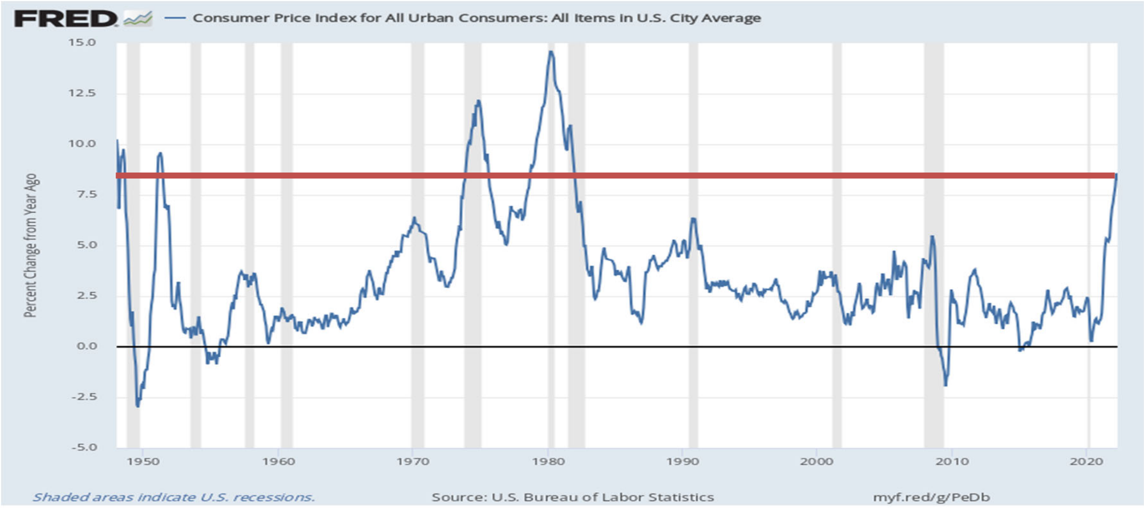
Executive Summary:

- Inflation seems to be on everybody's mind and I-bonds have emerged as a (seemingly) competitive offering;
- Series I savings bonds are government backed treasury securities which can be purchased through October 2022 at a 9.62% rate; the rate will reset to the 6-month inflation rate plus a real rate of zero. However, they have four limits that make them difficult to utilize in an advisory account:
    - You can only purchase $10,000 year calendar year.
    - You cannot custody them at Schwab, Fidelity or other custodians.
    - There are rules on redemption that that limit ability to rebalance and may cause forfeiture of interest on sale.
    - They are not income generating. They must be redeemed to access the income.
- I-Bonds are modeled after TIPS, in an analogous way that Series-EE bonds are modeled after Treasuries. Both Series-I and Series-EE are intended for small savings, gifts to children, etc.
- TIPS have the same inflation protection as I-Bonds, but with price risk associated with changing real yields.
    - 10-year TIPS are currently trading with a 0.2% real yield versus 0.0% for I-Bonds
    - There is no limit on TIPS purchases or redemptions,
    - TIPS can be used effectively during the rebalancing of an advisory portfolio.

Why the Interest in Inflation Protected Securities?

With consumer inflation running hot at 8.3% year-over-year (the highest levels we have seen since the early 1980s) and broad-based stock and bond markets down more than 15% from their peaks, clients are naturally looking for investment solutions which can provide a real return that keeps up with inflation. As such, a government security promising to pay the rate of inflation plus a real yield seems quite attractive.



In general, the bond market is volatile, and fixed income securities carry interest rate risk. (As interest rates rise, bond prices usually fall, and vice versa. This effect is usually more pronounced for longer-term securities.) Fixed income securities also carry inflation risk, liquidity risk, call risk, and credit and default risks for both issuers and counterparties.

While I-Bonds can be a good tool for small amounts of inflation-protected savings, gifts to children, and educational purposes, TIPS provide the same inflation protection that can be used effectively in client portfolios.

Wealthcare offers access to TIPS through several of our portfolio strategies:

- All Dynamic strategies currently. This can change when the relative value of TIPS diminishes.
- Pure Gamma Core-Plus
- All other Core-Plus strategies

In addition, our Core-Plus and Resilient models offer additional real return strategies through the use commodities, precious metals, and real estate/REITS.

About Series I Savings Bonds:

Savings bonds were introduced in the 1930s and 1940s as a way to encourage savings and broad participation by Americans in financing government activity (e.g. World War II). In 1998, the treasury department began to issue Series I savings bonds thus providing Americans the ability to save and earn a real return. Interest on an I-bond is earned every month and compounds semiannually. Interest is earned for 30 years unless cashed out. Funds are locked for 1 year. If cashed out prior to 5 years, a saver loses the previous 3 months of interest. The interest rate is a combination of two rates:

a) A fixed rate of return which is the same throughout the life of the I-Bond (currently at 0%);
b) A variable rate calculated two times a year which is based upon changes in the Consumer Price Index for all items.

To purchase, Series I Savings Bonds, a client would need to go online to www.treasurydirect.gov and open an account. A client can purchase up to $10,000 in I-Bonds each year.

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