

Barbells — giving you financial flexibility



Wealth
Management

Introduction

Investing in fixed income securities can help meet the financial needs of many investors. The key is designing an investment strategy to take advantage of changing interest rates while still providing income, safety and possible growth.

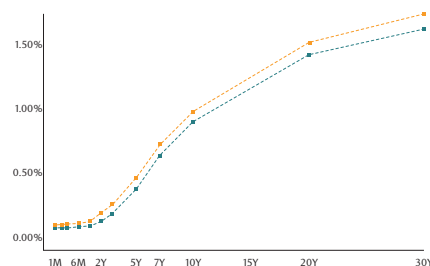
Predicting the direction of interest rates, however, is an exercise that confounds even the savviest investors. If interest rates go up, you want to have investable cash to take advantage of the higher rates; but if rates move lower, you want to have some money invested at the higher rates.

One way to lock in those attractive longer-term rates and still retain the flexibility to reinvest if interest rates move upward is to employ a portfolio strategy called a barbell.

What is a barbell?

A barbell strategy involves the simultaneous purchase of securities from both the short and long end of the yield curve. The yield curve is a graph depicting the yields for the spectrum of U.S. Treasury securities starting with 3-month Treasury bills and ranging all the way up to 30-year Treasury bonds. The yield curve is continually moving to reflect changing market expectations for future economic conditions.

Hypothetical Treasury yield curve



Generally, similar amounts of money are invested in both short- and long-term maturities with nothing invested in the middle. The visual effect of this type of investment strategy, with assets deployed at both ends of the maturity spectrum, resembles a barbell similar to the graph shown.

Just as stock investors avoid placing all their money in a single stock, bond investors using a barbell strategy avoid placing all of their money in a single maturity. A barbell strategy allows more attractive long-term rates to be captured by one end of the barbell, with the other end providing the flexibility that comes with shorter-term investments.

Depending on the exact shape of the yield curve, different barbell strategies can be designed. The most popular barbell involves investments in short- and long-term maturities. This structure takes advantage of a normal yield curve. If an investor does not believe that current long-term rates are attractive, a barbell utilizing a combination of short- and intermediate-term maturities can be designed.

An investor would also want to use short and intermediate maturities in a flat-yield curve environment where it is difficult to obtain higher yields by extending maturities. In this market, a barbell strategy can be especially important since it becomes even more difficult to design a prudent investment strategy.

Benefits

Fixed income investors employing a barbell strategy enjoy the following benefits:

- **Higher yields** — A portion of their portfolio is invested in longer-term bonds which typically earn higher yields than would be available from strictly short-term investments. This part of the barbell acts to boost the overall yield of the investment portfolio and lock in these yields if rates go lower.
- **Flexibility and opportunity** — The short-term investments provide the financial flexibility to shift funds into other sectors of the fixed-income market as opportunities present themselves.

Doing the heavy lifting

If you are uncertain as to the future direction of interest rates and how to best allocate your funds, then a barbell portfolio of fixed income securities is a simple way to maintain short-term flexibility while achieving longer-term financial goals.

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