Invesco Fixed Income Investment Insights

Q&A: The potential benefits of a multi-sector approach

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Rob Waldner
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"A multi-sector bond strategy tries to enhance returns by shifting between different sectors at appropriate times. Shifting allocations tactically among sectors is the essence of multi-sector investing"

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Joe Portera
CIO, High Yield and Multi-Sector Credit

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CIO, EMEA Fixed Income

Dawn Silvia
Senior Client Portfolio Manager

Invesco Fixed Income's multi-sector teams gathered for a roundtable discussion to share their thoughts on multi-sector investing approaches and the benefits to institutional investors - particularly in today's uncertain environment.

Q: What do you mean by "multi-sector investing"?
Rob: Multi-sector is short for "multiple sectors" meaning distinct types of bonds such as government, corporate credit, and structured securities. Multi-sector investing comes from placing different sectors side-by-side and allocating capital based on how well each should perform within the anticipated investment climate. There are times when markets reward investors for carrying credit risk and times when markets punish credit risk. A multi-sector bond strategy tries to enhance returns by shifting between different sectors at appropriate times. Shifting allocations tactically among sectors is the essence of multi-sector investing.

Q: Why should an investor think about using a multi-sector strategy?
Rob: We believe an investor should consider a multi-sector strategy for four reasons: performance, diversification, cost, and convenience. From a performance standpoint, there can be large differentials in asset class and sector performance from period to period. For example, the best assets to own in one period may be the worst in the next. Skilled "sector rotation" may potentially add tremendous performance when compared to static allocations. A multi-sector portfolio seeks to offer diversification by investing across a range of fixed income asset sectors. (Diversification does not guarantee a profit or eliminate the risk of loss.) On a cost basis, the investor may aggregate allocations across sectors into a multi-sector vehicle, economizing on fees and foregoing overhead and expenses required to shift asset allocation. Finally, the investor tends to benefit from the ease and convenience of paying a professional asset manager to do asset allocation and risk management.

In addition to potentially enhanced performance, a multi-sector strategy seeks to offer diversification from traditional or single-sector, fixed income strategies. It may also add stability to a multi-asset portfolio in times of rising interest rates.

Q: Why would investors benefit from a multi-sector approach in the current market environment?
Dawn: Investors may benefit from a multi-sector approach in any market environment, but it can be even more beneficial during times of market uncertainty, like our current market environment. One of the largest potential benefits of a multi-sector approach is the flexibility to move quickly between asset classes, which may help minimize downside risk. With many asset classes late in the market cycle, and a fair amount of geopolitical uncertainty unfolding, what you don't own will be just as important as what you do own. A multi-sector approach allows managers to continue to add attractive securities to the portfolio, but also the ability to move away from sectors that are experiencing adverse conditions.

Q: How do you approach it?
Gareth: We believe the fixed income markets can't be navigated in the same way they have been over the last 30 years. We think the long-term trend of declining interest rates is over. Going forward, generating attractive risk-adjusted returns may demand a more flexible approach. We divide our approach into two main strategies: opportunistic and unconstrained/absolute return. The main difference between the two is: the opportunistic approach centers on income and stability of net asset value, while the unconstrained/absolute return approach centers on positive total return and lower correlation with broader fixed income markets and equities.

Joe: No matter which strategy is adopted, Invesco offers two advantages: "depth" and "process." By depth we mean that performance is diversified among four sources: strategic beta (long-term average asset allocation), tactical beta (short-term alternation among sectors), alpha (bottom-up security selection), and risk management (constraining, budgeting, tracking, hedging to avoid adverse outcomes). (Diversification does not guarantee a profit or eliminate the risk of loss). In terms of process, we build views and allocations systematically from econometric models, market indicators, and valuations. Rigor and repetition help ensure results.

Q: What does Invesco do differently?
Dawn: Our multi-sector strategies are benchmark agnostic and unconstrained in nature. We do not have a bias toward specific fixed income sectors. Some strategies in the marketplace are biased toward high yield and credit, some toward global macro and currencies, and some toward structured products. We combine macro-related strategies and sector-related strategies to deliver diversified sources of return.

Q: What, if anything, should investors watch out for when considering a multi-sector approach?
Gareth: Investing involves legitimate risk. We believe that multi-sector investing may be more reliable than fixed, single-sector allocations. The breadth of multi-sector levers available and the attention to tactical asset allocation may increase the chances for success relative to single-sector approaches.

Joe: Investors should make sure that multi-sector managers work from a diversified platform with dedicated resources across sectors, in our view. Managers should have the ability to do active asset allocation and tactical positioning while drawing from a global opportunity set.

Investment risks

The value of investments and any income will fluctuate (this may partly be the result of exchange rate fluctuations) and investors may not get back the full amount invested. Past performance is not a guide to future returns.

Fixed-income investments are subject to credit risk of the issuer and the effects of changing interest rates. Interest rate risk refers to the risk that bond prices generally fall as interest rates rise and vice versa. An issuer may be unable to meet interest and/or principal payments, thereby causing its instruments to decrease in value and lowering the issuer's credit rating. The values of junk bonds fluctuate more than those of high quality bonds and can decline significantly over short time periods.

The risks of investing in securities of foreign issuers, including emerging market issuers, can include fluctuations in foreign currencies, political and economic instability, and foreign taxation issues.

The performance of an investment concentrated in issuers of a certain region or country is expected to be closely tied to conditions within that region and to be more volatile than more geographically diversified investments.

Mortgage- and asset-backed securities, which are subject to call (prepayment) risk, reinvestment risk and extension risk. These securities are also susceptible to an unexpectedly high rate of defaults on the mortgages held by a mortgage pool, which may adversely affect their value. The risk of such defaults depends on the quality of the mortgages underlying such security, the credit quality of its issuer or guarantor, and the nature and structure of its credit support.

Asset-backed securities are subject to prepayment or call risk, which is the risk that the borrower's payments may be received earlier or later than expected.

Commodities may subject an investor to greater volatility than traditional securities such as stocks and bonds and can fluctuate significantly based on weather, political, tax, and other regulatory and market developments.

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