

Translating fixed income in a new era

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EXECUTIVE SUMMARY

- Today's bond market is fundamentally different from 20 years ago. It is larger, more sensitive to interest rate changes, and more diverse, meaning a traditional core bond allocation may no longer provide the same level of portfolio protection.
- Higher interest rates are good news for income, but they also mean bond prices can be more volatile than investors are used to. The "safe and boring" reputation of bonds has been tested, and managing the price sensitivity to rate changes is an important consideration in building a bond portfolio.
- High yield fundamentals are stronger than perceived, while investment grade may carry underappreciated risk, making it critical to assess underlying credit quality rather than rely on broad labels.
- Bonds are once again delivering meaningful income, but with greater supply, complexity, and risk, making it more important to understand both the sources of yield and the risks involved.



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After more than a decade of near-zero interest rates following the 2008 Global Financial Crisis (GFC), and further compounded by COVID-era fiscal stimulus, the fixed income landscape has changed meaningfully. Today's bond market is larger, more interest rate-sensitive, and more complex than it was in the past. As a result, investors can no longer rely on the same assumptions or benchmarks that guided bond investing in the post-2008 era. The rules of the game have shifted, requiring a more thoughtful and flexible approach.

One key shift has been the changing relationship between stocks and bonds. While bonds historically helped cushion equity market declines, that dynamic has proven less reliable, particularly in inflation-driven environments like 2022, when both asset classes fell simultaneously. Not all bonds behave the same way, and differences across sectors have widened in recent years. Corporate, securitized (including mortgages and asset-backed securities), government, and emerging market bonds are now diverging more meaningfully, with returns increasingly driven by factors such as credit quality, interest rate sensitivity, and liquidity.

Translation for investors: The bond market of 20 years ago is not the bond market of today. It is bigger, more sensitive to interest rate changes, and more varied across different types of bonds. Simply owning a core bond fund and expecting it to protect portfolios the way it once did may no longer be enough.

A regime shift for the bond market

The most defining shift in recent years has been the move away from near-zero percent interest rates and increased debt issuance. As central banks aggressively raised rates to combat inflation in 2022 and 2023, yields climbed well above pre-2020 levels and have largely stayed there. The low-rate era is likely behind us, and portfolio strategies need to reflect that reality.

Bonds were once seen as the steady, predictable part of a portfolio. That perception has changed. Volatility has been higher than long-term historical averages and may remain elevated due to rapid policy shifts, inflation surprises, and geopolitical uncertainty. Yield swings have been larger and more frequent, and duration risk—a measure of how sensitive a bond's price is to interest rate changes—has moved to the forefront of investor concerns.

Translation for investors: Higher interest rates are good news for income, but they also mean bond prices can be more volatile than investors are used to. The “safe and boring” reputation of bonds has been tested, and managing the price sensitivity to rate changes is an important consideration in building a bond portfolio.

Public and private bond markets have converged

Over the past decade, the boundaries between public and private bond markets have grown increasingly blurred. Traditionally, most investors accessed bonds through public markets, which provide access to broadly traded securities like corporate bonds, U.S. Treasuries, and mortgage-backed securities (MBS). Private markets, by contrast, involve loans made directly to companies, and are negotiated privately rather than issued and traded on a public exchange.

The post-2008 regulatory environment imposed stricter capital requirements on banks, creating a lending void that private credit¹ managers were well-positioned to fill. More capital has since shifted from public bond markets into privately negotiated loans. Today, large private credit firms can finance deals that once relied entirely on public bond issuance. This evolution has made the distinction between public and private fixed income less clear than it once was.

Furthering the convergence has been strong demand, as some public market retail investors have increasingly sought the yield premium and diversification that private credit tends to offer, prompting asset managers to develop hybrid vehicles that blend characteristics of both markets.² The result is a fixed income landscape where the line between public and private is less a wall and more a spectrum, with capital flowing more freely across it than at any prior point in modern financial history. Understanding where capital flows, and why, is an increasingly essential context for fixed income investing as the convergence trend is expected to accelerate going forward.

Translation for investors: There is a growing market for loans made outside the traditional public bond market. These private credit securities can offer attractive income, but they come with real strings attached. They are harder to sell, less transparent in their pricing, and not always the right fit for every investor. Understanding what investors own and why matters more than ever in this part of the market.

The Agg isn't what it used to be

The Bloomberg Aggregate Bond Index (commonly called “the Agg”) has long served as the default benchmark for fixed income investing. However, it may no longer serve the same purpose it once did. Over time, the Agg has become longer in duration³ and more concentrated in government debt. In 2008, the index had an effective duration of approximately 4.3 years. Today it sits at roughly 5.8 years, an increase of about 35% (Figure 1). Sector weights have also shifted, and credit exposure has declined, all during a period when credit sectors performed exceptionally well.

FIGURE 1

Since 2008, the duration of the Agg has significantly increased and stabilized at higher levels.



Source: Bloomberg, TIAA Wealth CIO. As of March 31, 2026.

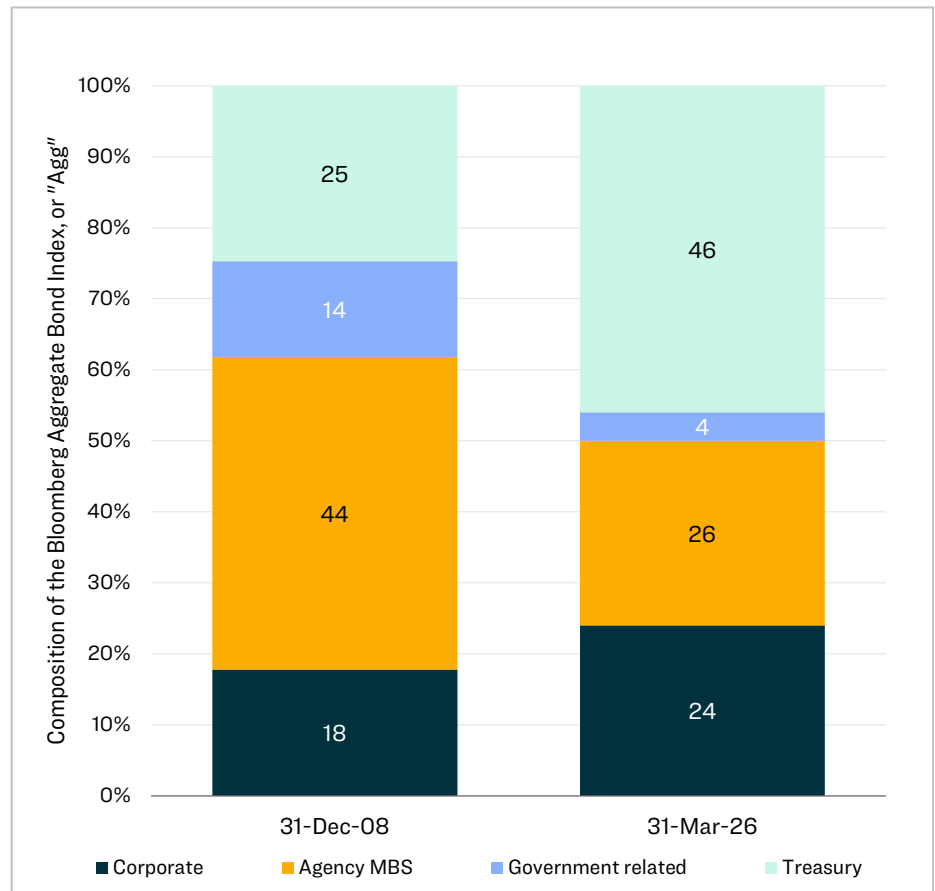
The practical result for investors is that the Agg index is now more exposed to interest rate movements and less exposed to the credit sectors that have historically provided better returns. Greater rate-driven volatility has come at precisely the time when interest rate moves have been most impactful.

Beyond its changing composition, the Agg also excludes significant and growing portions of the fixed income market (Figure 2). Notable omissions include securitized credit (which is different than agency MBS that comprises a large component of the Agg), inflation-linked bonds, floating rate securities, and below-investment-grade

bonds. Each of these sectors behaves differently across market cycles and offers diversification, income, or risk management properties that the core index does not provide. Investors relying solely on Agg-based strategies may be missing meaningful yield and diversification opportunities, not because of a deliberate choice, but simply because those sectors were never in the index to begin with.

FIGURE 2

Since the GFC, the composition of the Agg index has shifted meaningfully, with Government debt now accounting for half of the index.



Source: Bloomberg, TIAA Wealth CIO. As of March 31, 2026.

It is worth noting that U.S. Treasuries have not lost their relevance. They remain the ultimate flight-to-safety asset and a critical source of stability when markets come under severe stress. The concern is not Treasuries themselves, but the growing concentration of Treasuries within the Agg index.

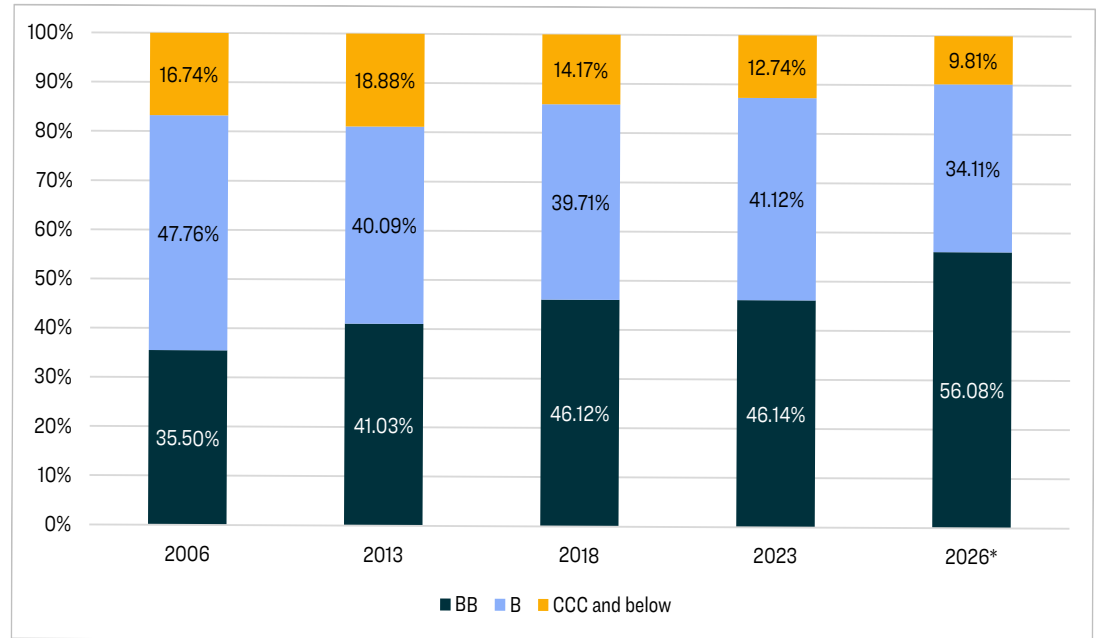
Translation for investors: The most widely used bond index has quietly become more concentrated and more sensitive to interest rate changes over time. If a bond allocation simply tracks this index alone, investors may be taking on more rate risk than realizing while missing out on other parts of the bond market that could provide value.

Credit quality: Two markets moving in opposite directions

The high yield corporate bond market has improved meaningfully in credit quality since the mid-2000s. BB-rated bonds (as defined by S&P Global ratings), the highest quality tier within high yield, now represent approximately 56% of the Bloomberg U.S. Corporate High Yield Index, up from 35 to 40% two decades ago. CCC-rated bonds, the riskiest tier, have shrunk to roughly 9% of the index, down from 15 to 16% historically. Riskier borrowers have increasingly migrated to private credit markets, corporate fundamentals have strengthened, and the market has shifted toward larger, more resilient issuers (Figure 3).

FIGURE 3

There's been a noticeable shift of credit quality in the Bloomberg U.S. Corporate High Yield Index over the past 20 years.



Source: Bloomberg, S&P Global, TIAA Wealth CIO. *Data as of May 31, 2026.

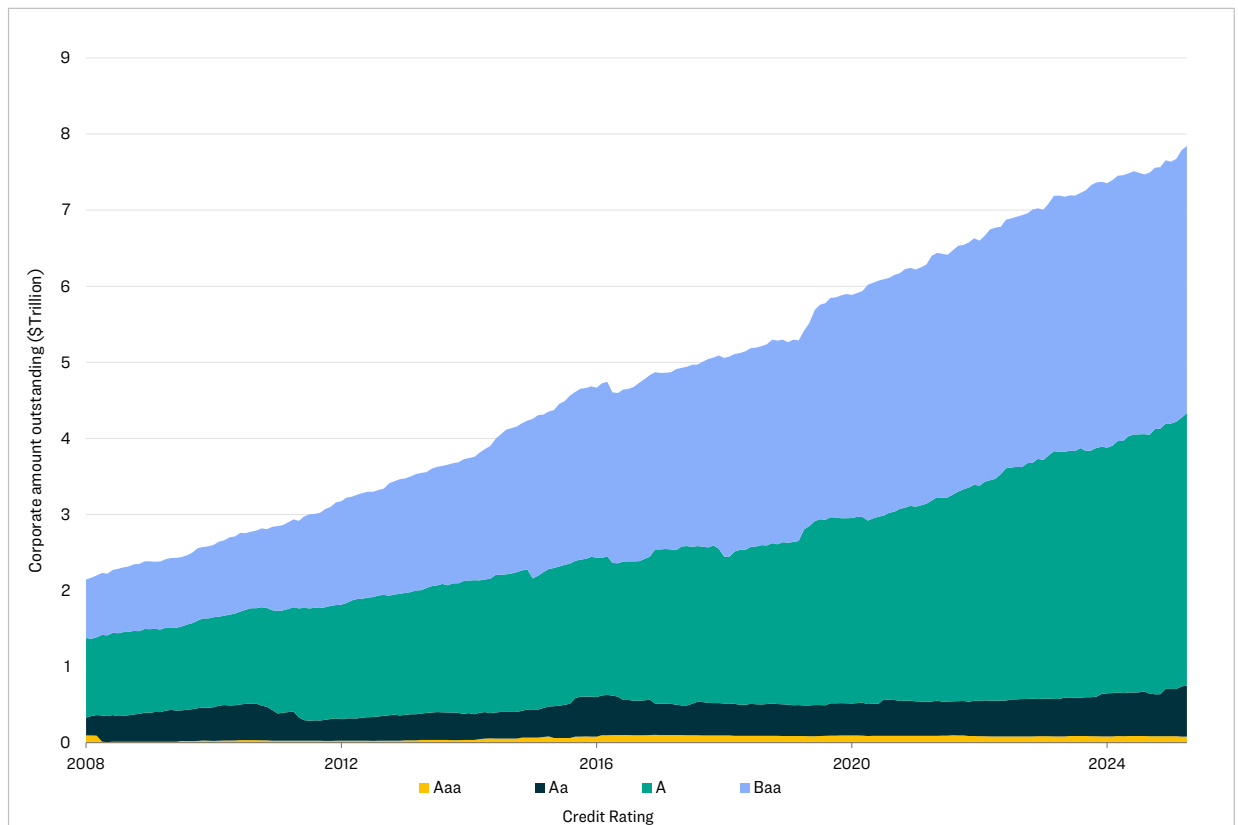
For investors, this quality improvement has meaningful implications. Default rates are likely to remain below long-term historical averages for the foreseeable future, and spreads (the extra yield high yield bonds offer over less risky bonds) can reasonably be expected to stay tighter than historical norms. That said, at current levels there is limited room for further improvement and meaningful room for spreads to widen if economic conditions deteriorate.

The investment grade corporate bond market tells a contrasting story as credit quality has actually declined since the GFC (Figure 4). Baa-rated bonds (as rated by Moody's rating agency), the lowest investment grade tier, now represent nearly half of the index, driven by a surge in issuance from companies that increased their borrowing during the low-rate era. This means a large portion of the investment grade index is only one or two ratings notches away from falling into high yield territory.

Translation for investors: Not all bond markets are created equal. The high yield market is in better fundamental shape than its reputation might suggest, while the investment grade market carries more hidden risk than many investors assume. Understanding the quality composition of what investors own, rather than simply relying on broad category labels, is increasingly important.

FIGURE 4

With surging issuance of bonds over the years, IG quality has deteriorated.



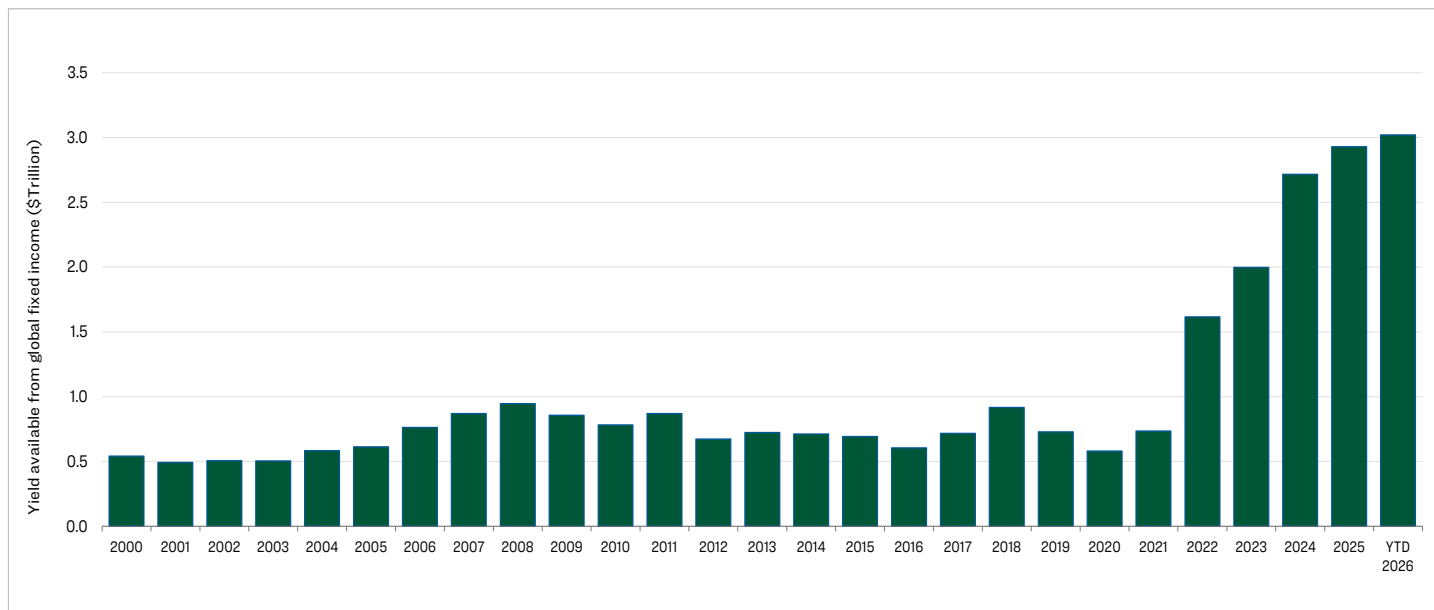
Source: Bloomberg, Moody's, TIAA Wealth CIO. As of March 31, 2026.

What to watch going forward

- **Rates are likely to stay higher than recent history.** Even with marginal policy easing from central banks, structural forces including persistent fiscal deficits, deglobalization pressures, and demographic trends suggest rates are unlikely to return to the lows of the 2010s. Positioning portfolios with this baseline in mind remains prudent.
- **Bond supply is rising across markets.** U.S. Treasury issuance continues to grow as the government finances deficits projected to exceed \$2 trillion in fiscal year 2026. On the corporate side, investment grade issuance is on pace to exceed \$2 trillion gross in 2026, nearly 50% above recent years. Major technology companies are a notable driver, with Amazon, Oracle, and Google alone accounting for over \$100 billion in new bond deals year to date. Strong investor demand has absorbed this supply so far, but the key question is at what point appetite begins to shift.
- **Income is back, but it comes with tradeoffs.** Higher yields have made bonds a genuinely compelling source of income again, producing more return potential than at almost any point in the past 25 years (Figure 5). The global fixed income market has also grown and diversified, offering investors more ways to access those potential benefits, including through international bonds where diverging monetary policies create additional opportunities. However, higher yields also accompany more credit risk, refinancing pressures, and thinner liquidity during market stress. Capturing income on a risk-adjusted basis requires discipline and a clear-eyed view of what risks investors are accepting in exchange for that yield.

FIGURE 5

Liquid bond markets are generating more income today than at any point in the past 25 years.



Source: The above data represents the Bloomberg Multiverse Index, which provides a broad based measure of the global fixed income bond market, TIAA Wealth CIO. As of 3/31/2026.

Translation for investors: The good news is that bonds are genuinely paying investors again after years of lower yields. The caveat is that higher income does not come for free. More supply, more complexity, and more moving parts means that knowing where income is coming from and what risks accompany it matters more than it did in simpler times.

Rethinking how to build a bond portfolio

Rather than treating fixed income as a single, monolithic allocation, investors benefit from thinking clearly about what different parts of their bond portfolio are designed to do. Some bonds generate income. Others preserve capital. Others provide ballast during equity market stress or capture opportunities in specific sectors or regions. Each objective may call for different types of bonds, different levels of interest rate sensitivity, and different sector or geographic exposures.

The 2022 bond market selloff served as a wake-up call. One of the worst years on record for bond returns forced many investors to confront what they actually owned and ask whether their benchmark reflected their investment goals or simply mirrored who had issued the most debt. Fixed income indices are, by construction, shaped by who borrows the most. Heavy borrowing is not a signal of financial health, yet market-cap weighted bond indices reward the largest borrowers with the largest weights. Investors who defaulted to the index found themselves overweight in government bonds and underweight in other bond sectors that would have served them better.

A more deliberate approach addresses this directly. Investors who are attuned to interest rate sensitivity, willing to look across the full fixed income universe—including international bonds, securitized credit, and select leveraged finance—and are able to adapt as market conditions evolve will be better positioned to meet their goals. Asset managers have developed new strategies and products built for today's environment, and access to these tools is broader than ever for individual investors.

Translation for investors: Think of a bond portfolio less like a single ingredient and more like a recipe with distinct components, each serving a different purpose. The old approach of buying one core bond fund and holding it long term may leave investors with more risk and less opportunity than they realize. A more intentional, diversified approach to fixed income is not just an institutional luxury. It is both increasingly accessible and increasingly necessary.

Conclusion

Fixed income has become a more complex and, in many ways, more rewarding asset class. Higher yields have restored bonds as a genuine source of income and return potential after years of meager payouts. At the same time, the risks demand more active engagement. Shifts in bond issuance have changed the composition of major indices in ways that create unintended concentrations and sector gaps. The line between public and private markets continues to blur. Credit quality is moving in different directions across different parts of the market.

Investors who embrace broader diversification, manage interest rate sensitivity thoughtfully, and look beyond conventional indices will be well positioned to make the most of this new era in fixed income.

Endnotes:

1 Private credit refers to loans that are directly negotiated between a borrower and a non-bank lender, instead of being issued through public bond markets or traditional banks.

2 Private credit comes with important tradeoffs. These investments tend to be less transparent than publicly traded bonds, with limited pricing visibility and fewer standardized disclosures. They are also generally less liquid, often requiring investors to commit capital for longer periods with restrictions on withdrawals.

3 Duration is a measure of how sensitive a bond's price is to interest rate changes.



CIO: FOCUSPOINT

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