Wellesley Asset Management
Convertible Bond Specialists

Lessons From “The Lost Decade” | 2018

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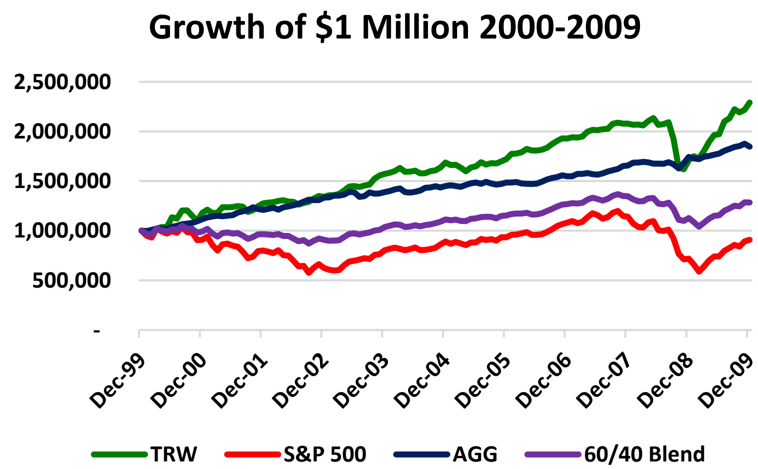
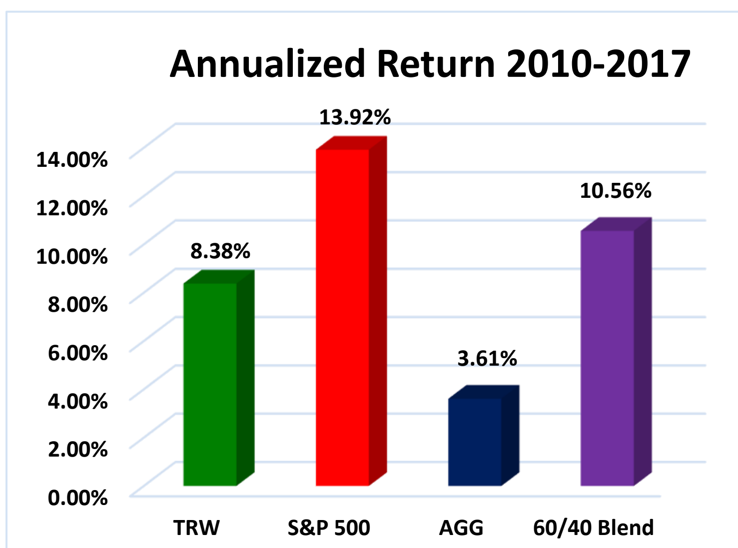
2018 marked the 9th year of this impressive bull market. Over that period, we’ve seen US stock market indexes reach new all-time highs. Alongside the stock market, interest rates have started to marginally move up. The Fed has hinted at up to 3 more rate increases this year alone. Since July, 2016 the US 10-year treasury has increased over 100 bps. Will this tread continue and if so how will stock and bond markets react?

It can sometimes be helpful to reflect on other time periods when setting future expectations. Specifically, what can be learned from “The Lost Decade” period from 2000-2009, when US stock markets had two painful corrections: the dot.com burst and the real estate crisis. Those events left many investors adverse to risk and derailed from their financial goals.



The S&P 500 actually was down 9.1% from 2000-2009. Investors in US equities not only suffered disappointing returns, <u>but lost 10 years of earning power.</u> Even those in a blended portfolio enjoyed only moderate gains. In contrast, the TRW, a convertible bond index, was up 8.64% annualized over that same period. Investing in principal protected convertible bonds with a balanced & disciplined approach -- like those found in TRW -- helped investors earn positive impactful returns. Convertibles, while not immune to volatility, have favorable characteristics that helped in “The Lost Decade”.

This leads back to where markets sit today. The first 8 years since “The Lost Decade” have been more than kind to stock investors, and as expected, equities have outperformed convertible bonds. The TRW Index has still returned 8.38% annualized over this time period. If there’s a lesson to be learned, it’s that time will once again decide the fate of this current bull market.



At Wellesley Asset Management, we believe that convertible bonds, and specifically those in the TRW, can participate in up markets. More importantly, we believe convertibles may produce meaningful returns in markets that are less favorable.

Disclosures:

Past performance does not guarantee future results.

The following indices have been used as benchmark data. Indices do not reflect the costs of trading, management fees or other expenses. It is not possible to invest directly in an index. WAM accounts differ from an index in that they are actively managed and may include substantially fewer and different securities than those comprising an index. Exposure to an asset class represented by an index is available through investable instruments based on the index. All numbers are approximate. A direct investment in an index is not possible.

TRW is the Thomson Reuters Wellesley Absolute Convertible Bond index ("TRW"). The Index is a joint venture between Thomson Reuters and Wellesley Investment Advisors that was created in January 2013. Index performance for the period from February 2002 to the creation date is calculated based upon a model portfolio maintained by WIA. Index performance from inception to February 2002 is backtested performance based upon historical trading for certain accounts. TRW is intended to represent a strategy with the goals of absolute returns and outperforming both equities and fixed income over complete market cycles deploying convertible bonds. WIA has discretion over the selection of index constituents and their weighting in the index.

The S&P 500 Total Return Index is a free-float capitalization-weighted index published since 1957 of the prices of 500 large-cap common stocks actively traded in the United States. The stocks included in the S&P 500 are those of large publicly held companies that trade on either of the two largest American stock market exchanges; the New York Stock Exchange and the NASDAQ. The S&P 500 Total Return Index calculates the performance of a group of stocks assuming that all dividends and distributions are reinvested.

The Bloomberg Barclays US Aggregate Bond Total Return covers the USD-denominated, investment-grade, fixed-rate, taxable bond market of SEC-registered securities. The index includes bonds from the Treasury, Government-Related, Corporate, MBS (agency fixed-rate and hybrid ARM pass-throughs), ABS, and CMBS sectors. The U.S. Aggregate Index is a component of the U.S. Universal Index in its entirety. Unmanaged index returns do not reflect any fees, expenses or sales charges.

Blend 60/40 is a mix portfolio of 60% the S&P 500 Total Return Index & of 40% the Bloomberg Barclays US Aggregate Bond Total Return. These weightings are assigned on day one of each period and not rebalanced in any way. Exact weightings will vary over time periods. The periods in question are 1/1/2000-12/31/2009 & 1/1/2010-12/31/2017. Source Morningstar Workstation.

An investment in convertible securities involves a risk of loss. The value of an investment in convertible securities may decrease as well as increase.

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