Decomposing 60/40

COMMENTARY
September 2026

With interest rates on the rise from who-can-be-sure-of-what (we have our thoughts…), bond prices are generally on the downtrend. But bond income (from the now generally higher yields) is on the rise. We therefore have once again entered the "60/40 Portfolio is Dead!" phase of the interest rate cycle. These generally lazy takes often fail to provide sufficiently broad context either as to why investors might want to incorporate bonds in their portfolios or to the various ways one can choose to do so. So, we'd like to remind folks that neither all bonds nor all bond investing methodologies are created equal. As is always the case in investing, your results will depend greatly on **how you choose to invest in the asset class**.

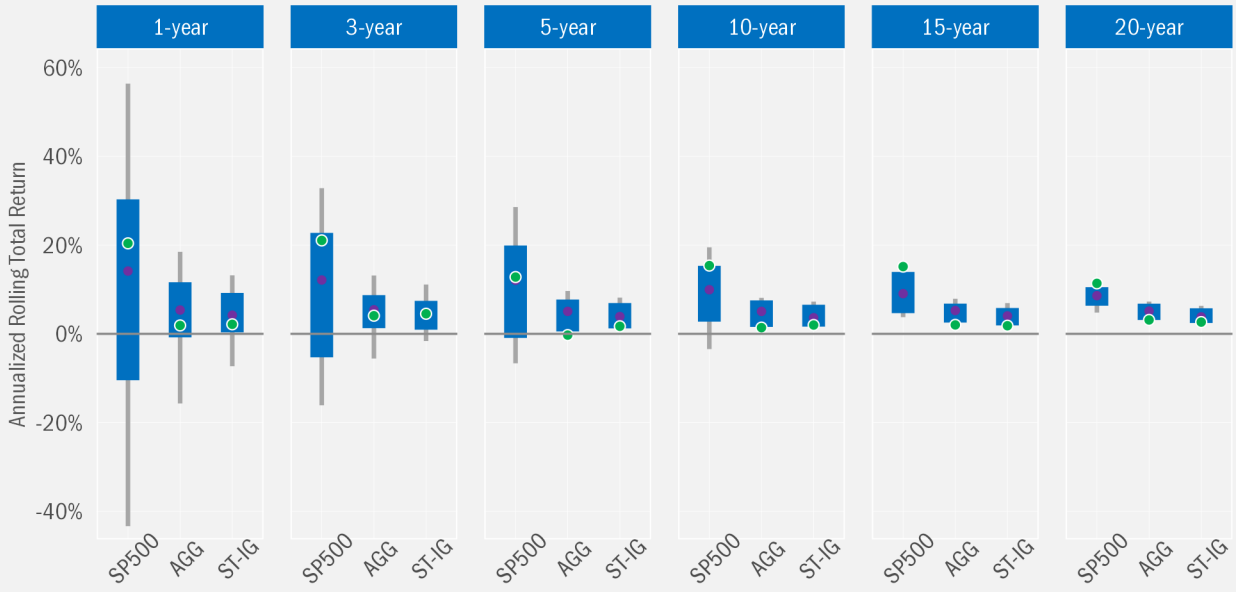
- Secular shifts in interest rates create variability across fixed income investment outcomes
- Over most any meaningful time frame, bond prices have proved rather reliably less volatile than stocks
- While it's true that directional changes in bond prices periodically align with those of stocks, such positive correlation is not a reliable characteristic (a statement of the opposite is generally more accurate)
- Just as one can invest in stocks in a manner well different than all stocks (i.e., the "market"), one can invest in bonds in a manner well different than the "bond market"

Bonds as Ballast

"60/40 is Dead!" memes come in various forms, often focusing on stock/bond correlations and flare up conversationally when that number turns meaningfully positive or when bond prices are falling by their lonesome, such as they may have been more recently as longer-term bond yields were reaching multi-decade highs. The notion implicit to many of these takes is that investors should look to other asset classes to fill portfolio role(s) for which bonds otherwise may have been utilized. Time and again, the notes fail to present such periods as occasionally expected behavior, while also generally failing to revisit the core reason many invest in bonds: their relative price stability, even when the direction of price changes is near-term negative and/or directionally aligned with stock price moves. In Figure 1 we present the historical range of three "markets": the U.S. stock market (SP500, represented by the S&P 500 Index), the U.S. Investment

Figure 1: Historical Range of Returns by Time Horizon

Blue bars show the middle 80% of rolling outcomes; purple marks the median and green marks the latest value



Monthly data from 09.29.89 to 08.31.26. Past performance is not indicative of future results. Investing in securities involves risk, including risk of losing some or all the invested capital. There is no guarantee that any investment or investment strategy will achieve its objective. Indexes are unmanaged. One cannot directly invest in an index. Index performance reflects the reinvestment of dividends, but does not reflect the expenses associated with the management of an actual portfolio. Please see additional important information regarding indexes at the end of this report. SOURCE: SRCM using data from Bloomberg

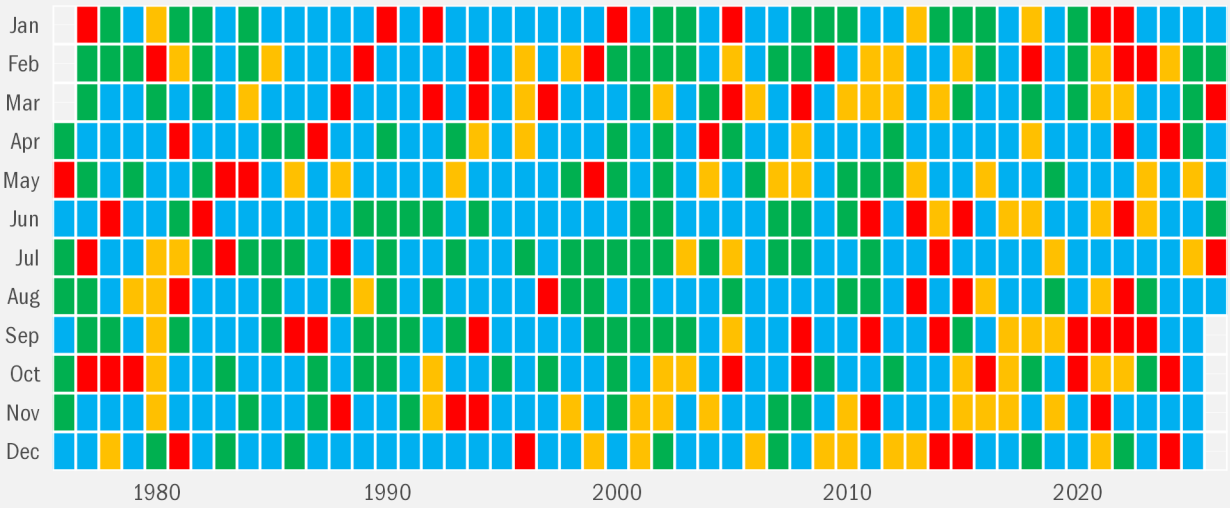
Grade bond market (AGG, represented by the Bloomberg U.S. Aggregate Bond Index, which tracks the U.S. investment grade taxable bond market), and our preferred bond benchmark (ST-IG), the Bloomberg 1-5 Yr Government/Credit Index, which comprises a short-duration subset of the Aggregate. Readily apparent from the data is the fact that stocks are more volatile (showing wider ranges with markedly higher highs and lower lows) than the broader bond market over each of the rolling periods reviewed, while the historical ranges of returns for the short-duration index are narrower still. This despite the fact that bond returns are not altogether reliably positive on a month-to-month basis (bonds carry investment risk too!!!) and that, fair to the core arguments of the T6040PID crowd, stocks and bonds rather often, actually, move down at the same time. See Figure 2 for more.

The data in Figure 1 support our preference for an approach that generally emphasizes shorter duration bonds in the portfolio. Bonds carry two primary risks: interest rate and credit. The former reflects a bond's sensitivity to changes in interest rates, with bonds that have a longer time until maturity tending to carry more interest rate risk. Credit risk is the potential for the issuer to default. While we have sought across the portfolios we manage to modulate exposure to interest rate risk over time, both higher and lower, we generally have maintained less-than-market sensitivity to changes in interest rates (measured by "duration"; duration tends to increase with time to maturity, though the math will depend on additional bond characteristics).

Investors generally seek additional compensation for that interest rate risk, such that interest rates tend to be increasingly higher for bonds of increasingly longer duration[1]. In normal times, therefore, it may seem attractive to add duration to a portfolio in order to pick up additional income. But as is the case with all investing, a higher expected return carries higher expected risk. These facts inform our twin preferences of 1) preferring equity exposure when seeking higher returns while 2) seeking to use bond holdings as a damper against stock market volatility. Since we

Figure 2: Monthly Relative Performance of Stocks and Bonds

The 303 blue squares represent months in which stocks and bonds both gained. The 141 green squares represent months in which stocks fell, but bonds gained. The 86 orange squares represent months in which stocks gained, but bonds fell. The 75 red squares represent months in which stocks and bonds both fell



From 03.31.76 to 08.31.26. Past performance is not indicative of future results. Investing in securities involves risk, including risk of losing some or all the invested capital. There is no guarantee that any investment or investment strategy will achieve its objective. Indexes are unmanaged. One cannot directly invest in an index. Index performance reflects the reinvestment of dividends, but does not reflect the expenses associated with the management of an actual portfolio. Please see additional important information regarding indexes at the end of this report. The equity index used for this presentation is the S&P 500 Index, which measures the performance of the large-cap segment of the U.S. equity market. The fixed income index used for this presentation is the Bloomberg U.S. 1-5 Year Government/Credit Bond Index, which includes investment grade, U.S. dollar-denominated, fixed-rate Treasuries, government-related and corporate securities with maturities between 1 and 5 years. SOURCE: SRCM using data from Bloomberg

[1] Readers may recall the yield curve "inversions" of the recent past when this normal characteristic of interest rates was not in place as longer-term yields were lower than short-term yields as the Federal Reserve set on a course of lifting its short-term rate target above the COVID-era lows.

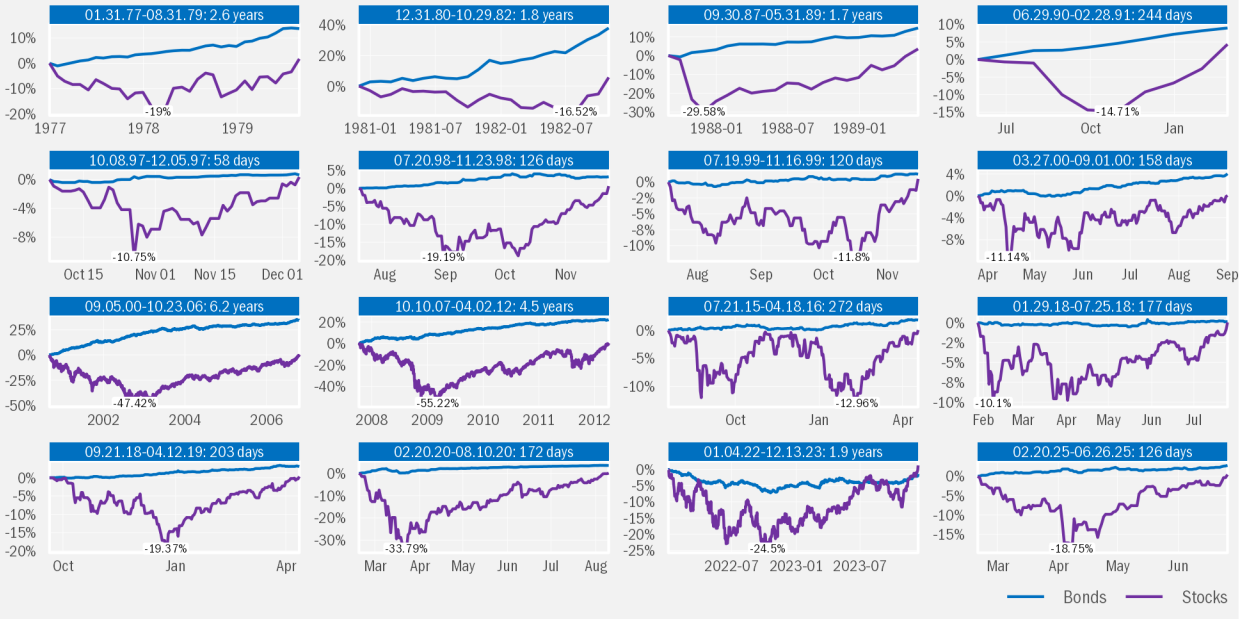
mostly seek to use bonds as a stock-risk offset, we tend toward the more cautious side of the spectrum when seeking incremental income through an extension in portfolio duration.

Softening the Blow

Our preference for seeking to add portfolio stability with fixed income is not merely a personal predilection. While the range-out-outcome view of Figure 1 helps to demonstrate the relative stability of bond returns, Figure 3 conveys a characteristic of bonds perhaps even more meaningful to client investment experience. Decades of work have shown us that clients have tended to appreciate the generally more stable performance of bonds during larger equity market meltdowns, even though bonds may have limited their absolute returns during more favorable equity market climes. That is, bonds can help limit the depth, duration and/or emotional tax of market declines. In this context, history is relatively less ambiguous. In Figure 3 we show twelve of the largest U.S. equity market drawdowns (decline from prior peak back to breakeven) along with the corresponding performance of our fixed income benchmark over the same timeframe. Due to a limitation of the bond data, we are using monthly data up to September 30, 1997. From then onward we show daily data. The monthly periodicity certainly flatters the stock drawdowns over that earlier period, in that we are missing intra-month market troughs, and may well flatter the bond performance for the same reason, but we cannot know this as the data are not available. That qualification noted, this relative stability during times of market duress is among the more defensible reasons, in our view, to maintain exposure to fixed income in portfolios that, for whatever reason, require some manner of potential damper against equity market risk (e.g., intention for the funds, owner tolerance for investment risk).

There are numerous ways to demonstrate this potential dampening effect, and we present another in Figure 4, which shows the relative drawdowns of the various benchmarks that we use to compare performance of the accounts that we manage. Because we tend to target equity exposure in 10% increments, we maintain benchmarks at eleven risk levels: 0% equity/100% fixed income, 10/90, 20/80 and so on through 100% equity. The implication of the chart is that portfolio drawdowns tend to be lighter in more or less direct proportion to the amount of fixed income owned relative

Figure 3: Relative Performance of Stock and Bonds During Stock Drawdowns



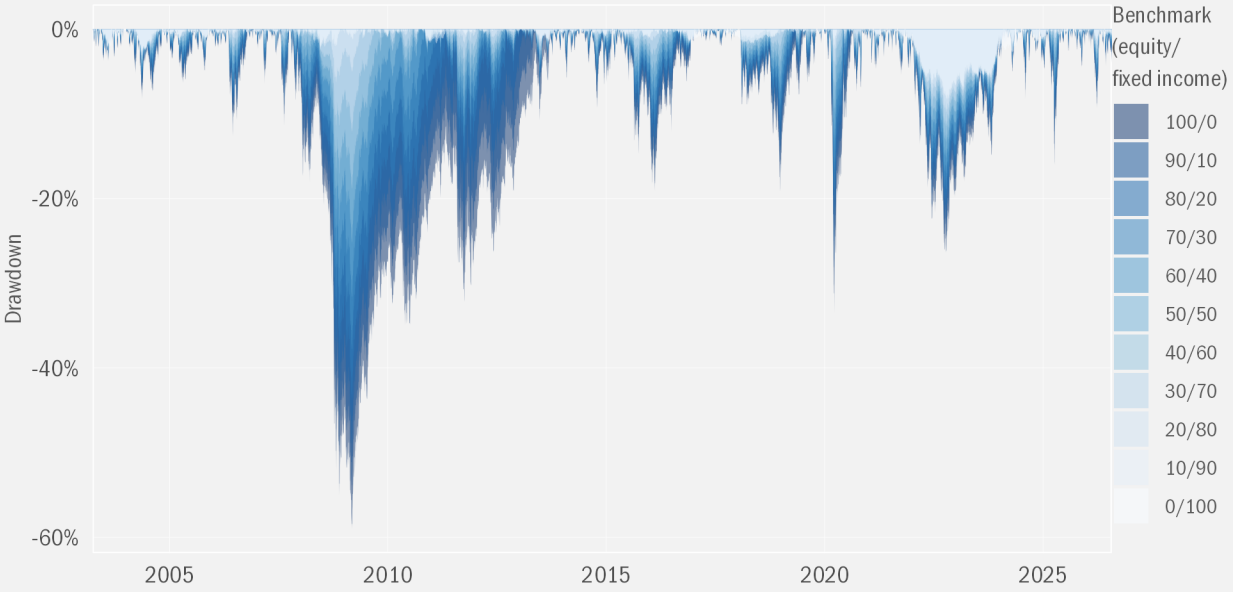
Monthy data from 03.31.76 to 09.30.97. Daily data onward to 08.31.26. Past performance is not indicative of future results. Investing in securities involves risk, including risk of losing some or all the invested capital. There is no guarantee that any investment or investment strategy will achieve its objective. Indexes are unmanaged. One cannot directly invest in an index. Index performance reflects the reinvestment of dividends, but does not reflect the expenses associated with the management of an actual portfolio. Please see additional important information regarding indexes at the end of this report. The equity index used for this presentation is the S&P 500 Index, which measures the performance of the large-cap segment of the U.S. equity market. The fixed income index used for this presentation is the Bloomberg U.S. 1-5 Year Government/Credit Bond Index, which includes investment grade, U.S. dollar-denominated, fixed-rate Treasuries, government-related and corporate securities with maturities between 1 and 5 years. SOURCE: SRCM using data from Bloomberg

to equity in the portfolio. Even so, the lighter expected drawdown that tends to come along with higher ratios of fixed income to equity in a portfolio may come at the cost of lower long-term returns. In Figure 5 we chart those same data we used to create Figure 4, only this time without resetting the value to zero at each new peak. Starkly outlined by the final values is the potential benefit that may come from assuming additional investment risk, in the case of this chart by taking on additional equity exposure.

There is No 60/40

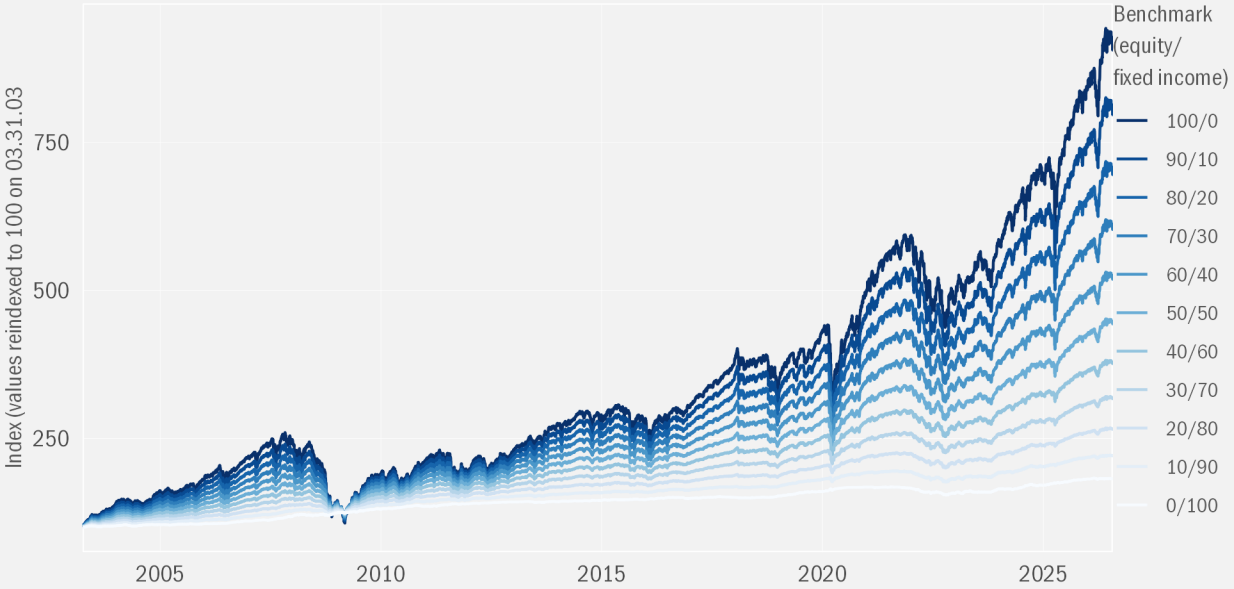
There really isn't any "one" 60/40, which means that "the" 60/40 can't be dead. Indeed, potential implementations of a 60/40 approach (or 20/80 split; 70/30 split, etc.) likely are as varied as there are managers who build them. We believe the construction of the 40% fixed income slice of the 60/40 portfolio can be every bit as impactful to long-term returns and client comfort on the way to realizing them as can be the composition of the 60% equity portion. As we have sought to show on these pages, for example, investor experiences likely differed widely during the Fed's 2022-23 hiking cycle depending on how their managers had positioned the fixed income side of the ledger vis-à-vis interest rate risk. Importantly, we look for our approach within fixed income to neatly align with our overarching belief that striking an appropriate balance of expected returns against tolerance for investment risk is central to success in the pursuit of long-term financial goals.

Figure 4: Relative Drawdowns of Benchmark Indexes



Daily data from 03.31.03 to 07.30.26. Past performance is not indicative of future results. Investing in securities involves risk, including risk of losing some or all the invested capital. There is no guarantee that any investment or investment strategy will achieve its objective. Benchmark names: the first (second) number is the weight of equity (fixed income). Benchmarks are rebalanced quarterly. The equity index used for this presentation is the Bloomberg World Large and Mid Cap Net Return Index, which is a float market-cap-weighted equity benchmark that covers 85% market cap of the global equity market. The fixed income index used for this presentation is the Bloomberg U.S. 1-5 Year Government/Credit Bond Index, which includes investment grade, U.S. dollar-denominated, fixed-rate Treasuries, government-related and corporate securities with maturities between 1 and 5 years. Indexes are unmanaged. One cannot directly invest in an index. Index performance reflects the reinvestment of dividends, but does not reflect the expenses associated with the management of an actual portfolio. Please see additional important information regarding indexes at the end of this report. SOURCE: SRCM using data from Bloomberg

Figure 5: Long-Term Total Return of Benchmark Indexes



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The S&P 500 Index measures the performance of the large-cap segment of the U.S. equity market.

The Bloomberg U.S. Aggregate Index is a broad-based flagship benchmark that measures the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, mortgage-backed securities (MSB; agency fixed-rate pass-throughs), asset-backed securities (ABS) and commercial mortgage-backed securities (CMBS; agency and non-agency).

The Bloomberg 1-5 Yr Government/Credit Index is a broad-based benchmark that measures the non-securitized component of the U.S. Aggregate Index. It includes investment grade, US dollar-denominated, fixed-rate Treasuries, government-related and corporate securities with 1 to 5 years to maturity.

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