Fixed-income securities represent a significant portion of all available financial assets and are included in most investor portfolios.

This study session begins by explaining the role played by fixed-income securities in portfolios and then introduces the two primary types of fixed-income mandates (liability-based and total return). A model for decomposing expected bond returns, which identifies the driving forces behind expected returns, is presented. The effects of illiquidity, leverage, and taxes on fixed-income portfolios are discussed. Next, liability-driven and index-based strategies are examined in greater detail. Coverage includes approaches, risks, and challenges associated with both immunization of single and multiple liabilities and the indexation and laddering of a fixed-income portfolio.

**READING ASSIGNMENTS**

**Reading 18**  
Overview of Fixed-Income Portfolio Management  
by Bernd Hanke, PhD, CFA, and Brian J. Henderson, PhD, CFA  

**Reading 19**  
Liability-Driven and Index-Based Strategies  
by James F. Adams, PhD, CFA, and Donald J. Smith, PhD

**LEARNING OUTCOMES**

**READING 18. OVERVIEW OF FIXED-INCOME PORTFOLIO MANAGEMENT**

The candidate should be able to:

- discuss roles of fixed-income securities in portfolios;
b describe how fixed-income mandates may be classified and compare features of the mandates;
c describe bond market liquidity, including the differences among market sub-sectors, and discuss the effect of liquidity on fixed-income portfolio management;
d describe and interpret a model for fixed-income returns;
e discuss the use of leverage, alternative methods for leveraging, and risks that leverage creates in fixed-income portfolios;
f discuss differences in managing fixed-income portfolios for taxable and tax-exempt investors.

READING 19. LIABILITY-DRIVEN AND INDEX-BASED STRATEGIES

The candidate should be able to:

a describe liability-driven investing;
b evaluate strategies for managing a single liability;
c compare strategies for a single liability and for multiple liabilities, including alternative means of implementation;
d evaluate liability-based strategies under various interest rate scenarios and select a strategy to achieve a portfolio’s objectives;
e explain risks associated with managing a portfolio against a liability structure;
f discuss bond indexes and the challenges of managing a fixed-income portfolio to mimic the characteristics of a bond index;
g compare alternative methods for establishing bond market exposure passively;
h discuss criteria for selecting a benchmark and justify the selection of a benchmark;
i describe construction, benefits, limitations, and risk–return characteristics of a laddered bond portfolio.