What to do with your bond portfolio before rates rise

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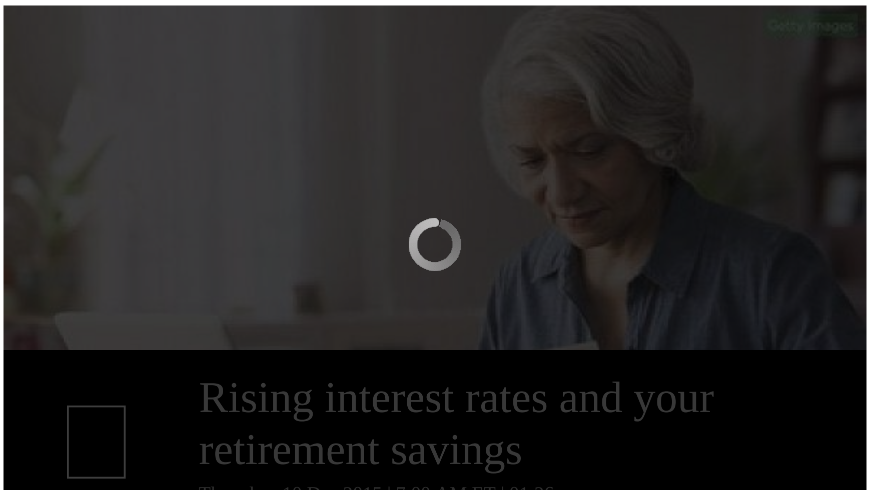

The Federal Reserve is expected to raise interest rates after Tuesday's two-day meeting and that will affect your bond holdings.

Though an anticipated 0.25 percent rate increase from the Fed will not drastically change your returns, a prolonged campaign of rate hikes may be a drag on your fixed income portfolio as rising rates mean lower bond prices.

"The biggest misconception investors have about fixed income is that prices do not fluctuate or that your fixed income investment won't go down in value," said Marc Henn, a certified financial planner and president of Harvest Financial Advisors in West Chester, Ohio.

If you haven't reviewed at your bond portfolio in awhile, here's what you should do:

Stay diversified

It's tempting to look at how stocks have performed in the Trump rally and want to ditch bonds completely.

"Clients sometimes question why have bonds at all," said Mark Rylance, a

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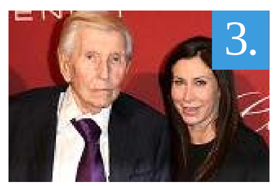
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CFP with RS Crum in Newport Beach, California. "We then walk them through their diversification effects — bonds go up when stocks go down."

For investors with long-term goals, such as saving for retirement or a child's education, price declines in bonds because of rising rates will eventually be offset by more income from debt issued at higher rates, said Matthew Tucker, head of fixed income iShares strategy at BlackRock.

"For most investors, the message is 'don't panic and don't make adjustments to your asset allocation,'" Tucker said. "Bonds are doing what they're supposed to be doing."

Rebalance if needed

Disciplined investors may want to take their recent gains from the stock market and invest them in fixed income to maintain their target asset allocation. It is a process known as rebalancing.

Shon Anderson, a CFP and chief wealth strategist at Anderson Financial Strategies in Dayton, Ohio, is using the volatility in the bond market to rebalance his clients' portfolios, selling stocks and buying bonds.

"We're telling clients that fixed income is oversold at this point," Anderson said.

Check your duration

If you are concerned about rising rates, look at your bond portfolio's duration.

Duration is the measure of interest rate sensitivity, expressed in years. For example, Vanguard Total Bond Market Index, the largest U.S. bond fund by assets, has an average duration of 5.79 years. That means if rates were to rise by 1 percentage point, this fund could lose as much as 5.79 percent.

If you are comfortable with your bond allocation and its duration, stick with it.

"Rate hikes are likely already baked into the prices," said Kashif Ahmed, a CFP and president of American Private Wealth in Woburn, Mass. "The day after a hike, the bond market will still be there and people will still need a properly allocated portfolio."

Tom Anderson
Personal Finance Writer

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