CORNERSTONE
FINANCIAL PLANNING

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I'm writing to let you know of changes in the way fixed income (bond) positions in your portfolio are being managed or may be shifted in the future. The idea for this communication both now and in the future came from your responses to my recent client survey. Several of you asked for clarification of trades made in your accounts, and this will now be integrated into my client service model!

The Federal Reserve continues striving to keep interest rates extremely low and many investors have taken positions with greater risk as a result. However, the Fed has signaled that it may begin to moderate its position as the economy continues to recover (especially the jobless rate), which would likely allow interest rates to climb.

The value (price) of many fixed income investments respond inversely to movements in interest rates. While not the best descriptor, "duration" is the financial term used to describe this relationship. A positive duration implies that the value of a bond will likely rise as interest rates fall, and drop as interest rates rise. For example, duration of 3 could mean that the value of a fixed income security might rise by 3% if interest rates fall by 1%, and vice versa. Duration is not the sole determinate of price fluctuations in fixed income securities, but it plays a significant role.

With interest rates remaining at near historic lows, strategists and money managers are beginning to consider how to protect portfolio value in the face of rising interest rates. Reducing duration is one of the methods being employed. In recent weeks, strategists and managers have begun to manage duration by shortening the average maturity of bonds in their portfolio, and by purchasing assets that have traditionally responded positively to rising interest rates. For example, a portfolio of bank loans whose interest rate adjusts to the prime interest rate have generally weathered a rising rate environment rather well. Shortening the maturity date of bonds or purchasing higher quality bonds can also limit sensitivity to interest rates.

(When applicable) Your position in the Sector Rotation/Country Rotation/Managed Bond, etc. reflects changes the strategist has made to reduce duration.

I expect to see other strategists and managers begin to follow suit and will notify you when such changes are occurring in your portfolio. As always, please contact me with your questions or concerns.

Best Regards,

Gary D. Case

Gary D. Case, CFP®

218 12th Avenue Road ♦ Nampa, Idaho 83686
(208) 466-1971 ♦ (208) 371-7368 ♦ Fax (888) 589-4667