Bonds Are a Bit of a Mess—Now What?

Rethinking Portfolio Defense and Income Generation

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"Treasury bonds define everything from how the stock market ends up performing to the cost of a mortgage, a car loan, a credit card. There is almost nothing financial they do not touch."

—Ezra Klein
New York Times columnist

The bond market poses two distinct yet interconnected challenges. At 3EDGE Asset Management, we believe our investment solutions are designed to address these challenges.

Bonds have historically played an important role in client portfolios by providing income, stability, and potential downside protection. But the bond market has changed. Rising interest rates, inflation uncertainty, bond market volatility, and higher stock-bond correlations have made traditional bonds less reliable as the primary allocation for hedging equity exposure and generating income.

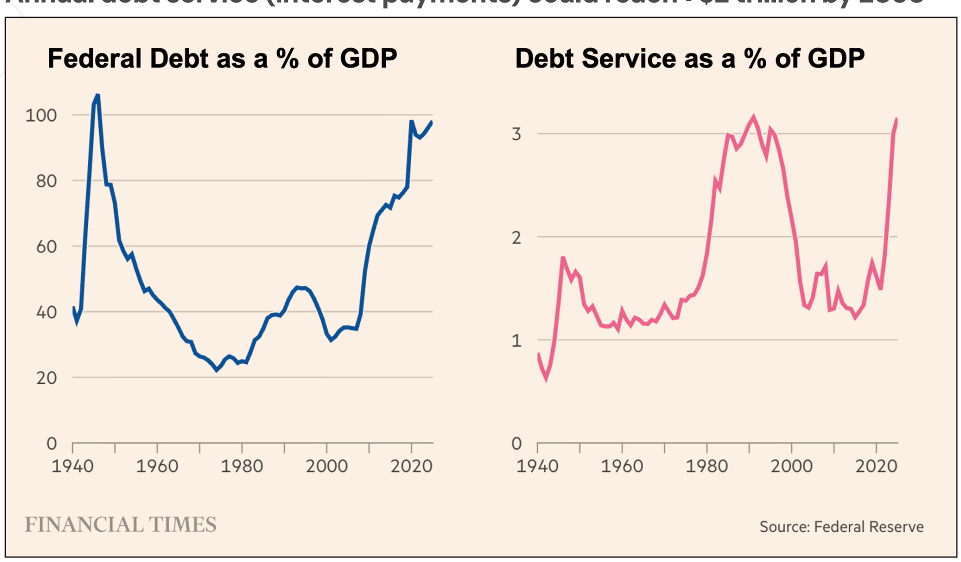
The first challenge facing investors is whether traditional bonds can continue to play the same defensive role within a 60/40 stock/bond portfolio. In the years ahead, investors may need more than a traditional bond-only allocation to represent the 40% of the 60/40 stock bond allocation in providing the diversification, downside-risk management, and income they historically expected. A broader, multi-asset approach may be better suited to address this challenge.

The second challenge is investors' ongoing need for yield and current income. The need for yield and current income has become more pressing. Higher costs of living, longer retirements, and the desire for more predictable cash flows have increased the importance of income generation within client portfolios. However, chasing yield too aggressively can expose clients to a multitude of risks, including interest-rate risk, credit risk, and liquidity risk. Additionally, the ETF market has recently seen dramatic growth in income-generating investment vehicles that may carry hidden risks investors may not be aware of. To succeed, clients seeking current income could benefit from a multi-asset portfolio with a risk-management focus.

Figure 1:

Federal Debt and Debt Service Near All-Time Highs
Source: Financial Times
Data as of 5/31/2026

Annual debt service (interest payments) could reach >$2 trillion by 2030



Challenge #1: R.I.P. the Traditional 60/40 Portfolio

For over four decades, from the 1980s up to 2020, a 60/40 portfolio of stocks and bonds was generally sufficient for long-term investing success. Equities were held for capital appreciation, while bonds served as a portfolio diversifier and hedge against equity exposure (risk), while also providing current income. Unfortunately, the bond portion of a traditional 60/40 portfolio may no longer be sufficient on its own to provide the diversification and downside protection investors have historically expected.

Rising Interest Rates and Bond Yields

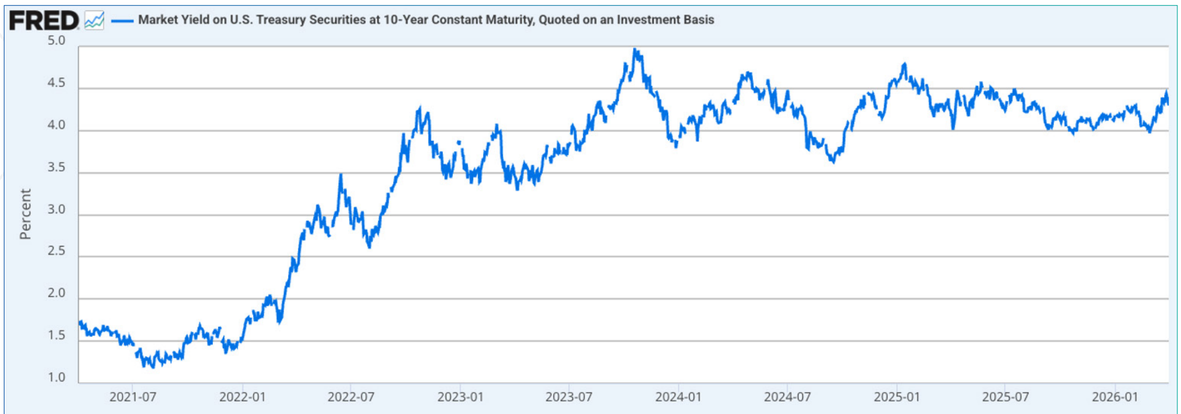
Beginning in August 2020, after more than four decades of low and falling interest rates and one of the greatest bond bull markets in history, the 10-year U.S. Treasury yield bottomed at around one-half of one percent, and from there bond yields began to rise precipitously, driven by inflation and tightening monetary policy.

As yields rose sharply from historic lows, bond prices declined, creating one of the worst bond bear markets in modern history. The bond market and interest rate environment have materially changed, and bond yields are unlikely to return to their pandemic-era lows any time soon (Figure 2).

Figure 2:

Market Yield on U.S. 10-Year Treasuries Since 2021

Source: Board of Governors of the Federal Reserve System via FRED®
Data as of 6/30/2026



When will interest rates return to normal?

In my travels, I often hear investors ask, “When are interest rates going to go back to normal?” In many cases, what they really mean is, “When will the 10-year U.S. Treasury yield return to the near-zero levels seen during the pandemic?” Unfortunately, that scenario is unlikely to be the base case anytime soon.

Stock-Bond Correlations

From 2008 through 2020, investors grew accustomed to a favorable stock-bond relationship: when stocks declined, bond prices often rose and yields fell. That relationship was supported by a generally disinflationary environment. However, the correlation between stocks and bonds has now risen to resemble the more inflationary economic regimes of the 1970s and early 1980s.

Going forward, an investor’s bond and equity holdings may decline together during an equity market downturn. That’s because in periods of rising yields or widening credit concerns, bonds may no longer reliably hedge stock market declines or provide the diversification and downside protection investors have historically expected.

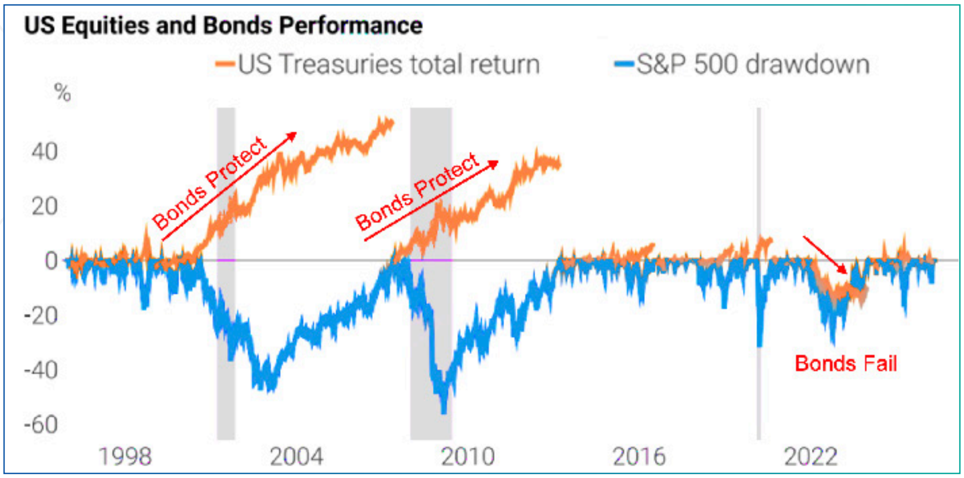
The problem is not “bonds are bad.” The problem is that clients still need income and protection in a market where the traditional bond playbook is less reliable.

Taken together, higher-for-longer rates and rising stock-bond correlations (Figure 3) call into question whether the "40" in a 60/40 portfolio can continue to serve as a reliable diversifier and equity market hedge. The bottom line is that going forward investors may need to think differently about the role of their bond holdings and the bond market in general.

Figure 3:

The Rising Correlation Between U.S. Equity and Bond Performance

Source: Macrobond, Bloomberg, GlobalData TS Lombard.
Data as of 3/31/2026



Our Answer: 3EDGE Conservative

The **3EDGE Conservative strategy** seeks to serve as a complement to, or potential replacement for, traditional core bond exposure. The strategy is dynamically managed, globally diversified, and multi-asset, investing across stocks, bonds, hard assets, and cash. The dynamic nature of the portfolio means that the investment committee makes regular adjustments, guided by the 3EDGE Global Capital Markets model, as the outlook for the global markets changes over time. 3EDGE Conservative is more than simply a bond substitute; it is designed to play a broader role than bonds alone. It seeks to provide capital preservation, downside-risk management, and diversification through a portfolio that can allocate across multiple asset classes and geographies and can adjust as market conditions change.

The question is not whether bonds still belong in investors' portfolios, because they do. The question is whether, in the years to come, traditional core bonds alone can provide sufficient asset-class diversification and protection from equity market declines. Since inception (1/1/2016), 3EDGE Conservative has produced higher returns, lower drawdowns, and stronger risk-adjusted outcomes than the S&P U.S. Aggregate Bond Index[2], while also offering daily liquidity. Additionally, 3EDGE Conservative has maintained relatively low correlations to equities, including the S&P 500 index, helping serve as a potential hedge against investors' equity holdings.[1]

The 3EDGE Conservative Strategy is more than simply a bond substitute; it is designed to play a broader role than bonds alone

Challenge #2: Investors' Search for Yield and Current Income

The need for yield and current income has become even more pressing, as higher costs of living and longer retirements have increased the importance of income generation within client portfolios. However, not all yield is created equal and reaching too aggressively for yield can expose clients to a variety of risks, including credit risk, interest-rate risk and liquidity risk.

A large number of income-focused investment vehicles, including ETFs, have recently come to market, particularly defined outcome strategies and structured investment notes. However, these products are often quite complex and may carry hidden risks that are not necessarily well understood. Reaching for yield by over-allocating to high-yield bonds, long-duration fixed income, private credit or defined outcome vehicles such as structured notes can introduce risks that may not be obvious until market conditions deteriorate.

We believe clients should not simply reach for the highest available yield, but instead consider incorporating sustainable income-generating investments within a diversified, multi-asset and risk-managed portfolio. The challenge is not simply finding more current income; it is making sure that income endures, especially in a market environment with numerous potential risks, including inflation that could remain higher for longer, monetary and fiscal policy uncertainty, higher interest rates and more volatile long-term U.S. Treasury bond yields, among others.

Caveat Emptor — A Warning About Structured Investment Notes & Defined Outcome Solutions

In the current uncertain investment environment, recently created investment vehicles such as structured investment notes and other defined outcome strategies may appear attractive because they package a defined payoff with partial downside protection into a single security.

However, these products can involve added complexity, limited liquidity, opaque pricing, conditional protection, and reduced flexibility. By contrast, the 3EDGE Income Plus approach is not built around a one-time contractual payoff formula. It is built around ongoing portfolio management.

Our Answer: 3EDGE Income Plus

3EDGE Income Plus seeks to provide attractive yields and current income without relying on a single narrow source of yield. Current income matters, but so does how that income is generated. The strategy uses a flexible, globally diversified, multi-asset approach that can dynamically combine traditional fixed income, equity income, and non-traditional income sources. It is designed to provide not only current income, but also asset-class diversification, portfolio flexibility, risk management, and daily liquidity in what may remain a challenging environment for investors.

3EDGE Income Plus Strategy Target Asset Class Ranges

Target Asset Class Ranges*	Traditional Equity Income Sources	Traditional Fixed Income Sources	Non-Traditional Income Sources
3EDGE Income Plus	**0% – 40%** *e.g. Dividend paying stocks, Equities with covered calls, etc.*	**55% – 95%** *e.g. U.S. Treasuries, Collateralized Loan Obligations, etc.*	**5% – 25%** *e.g. Covered Call Gold ETFs, Closed-End Funds, etc.*

*See disclosures for additional details.

Conclusion:

Navigating the bond market may be more challenging in the years ahead. The traditional assumptions that shaped bond portfolio construction from 2008 through 2020 may no longer apply. Inflation has proven more persistent, interest rates are no longer anchored near zero, bond prices have become more volatile, and geopolitical tensions and central bank policy uncertainty may continue to affect bond holdings.

The issue is not that all bonds are bad, but rather that investors may need a more robust toolkit than traditional bonds alone to hedge equity market exposure and generate adequate current income.

The good news is that investors do not need to rely solely on complex, illiquid, or opaque solutions to address these bond market challenges. 3EDGE Conservative and 3EDGE Income Plus seek to offer transparent, liquid, multi-asset approaches designed to help investors navigate the changing bond market landscape.

For more information about 3EDGE Asset Management and our investment offerings, please visit our website at 3edgeam.com or email us at info@3edgeam.com

Footnotes:
1:Refer to the 3EDGE Conservative Strategy fact sheet available on https://3edgeam.com/sma-fact-sheets/
2:The S&P U.S. Aggregate Bond Index is designed to measure the performance of publicly issued U.S. dollar denominated investment-grade debt.

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The target asset class ranges shown for the 3EDGE Income Plus Strategy are strategic allocation guidelines established by 3EDGE Asset Management and are intended to illustrate the portfolio's investment framework. Traditional Equity Income Sources may include U.S. equities, international equities, emerging market equities, ex-U.S. equities, and global equities. Traditional Fixed Income Sources may include U.S. Treasuries, investment-grade bonds, short-term fixed income and cash, collateralized loan obligations (CLOs), and other similar fixed income investments. Non-Traditional Income Sources may include hard assets, commodities, covered-call strategies, closed-end funds, and other investments that cannot be reasonably classified under the previous two categories. The Strategy may from time to time be outside of the percentage ranges shown when deemed appropriate by 3EDGE Asset Management. 3EDGE may change the target allocation ranges at any time in its sole discretion. Ref:0926.