



Rethinking Duration Management

Moving Beyond Traditional Bonds

Fixed Income Solutions Team

Over the past several years, we have engaged with institutional investors seeking to extend their fixed income asset duration to take advantage of higher long-term yields while protecting their asset-liability position. These efforts have generally focused on reallocating from universe bonds to long bonds or to strategies somewhere in between.

A common starting point for investors seeking long duration bond exposure is a mandate designed to deliver benchmark-like performance relative to the Canadian bond market or a custom subset. This typically includes the following approaches:

- ▶ **Long bonds** (e.g. efficient exposure to FTSE Long-Term Bond Index)
- ▶ **Custom long bonds** (e.g. blend of long-term provincial and long-term corporate bonds)
- ▶ **Custom liability-matching portfolio** (e.g. 50% provincial and 50% corporate bond mix with a term structure matching the liability profile)

While some of these mandates may not be strictly “passive” (e.g., they may employ active security selection or pursue sector/issuer diversification), their objective is not to generate outperformance.

In the longer-end, investors are often satisfied with benchmark-like returns for a few reasons:

- ▶ It is more challenging for asset managers to outperform long-bond indices as the investment opportunity set is small and frictional trading costs are higher, particularly those with allocation to long corporate bonds.
- ▶ Long end investors tend to pursue liability-hedging motives and may prefer to limit active positioning for philosophical standpoint reasons.

Investors seeking higher yields or broader diversification may allocate to U.S. long-term corporate bonds or long-term high-quality fixed-rate private debt. While these approaches can help address some limitations of the Canadian public bond market, they also tend to narrow the overall opportunity set.



The Term Structure of Credit Spreads and Compensation for Risk

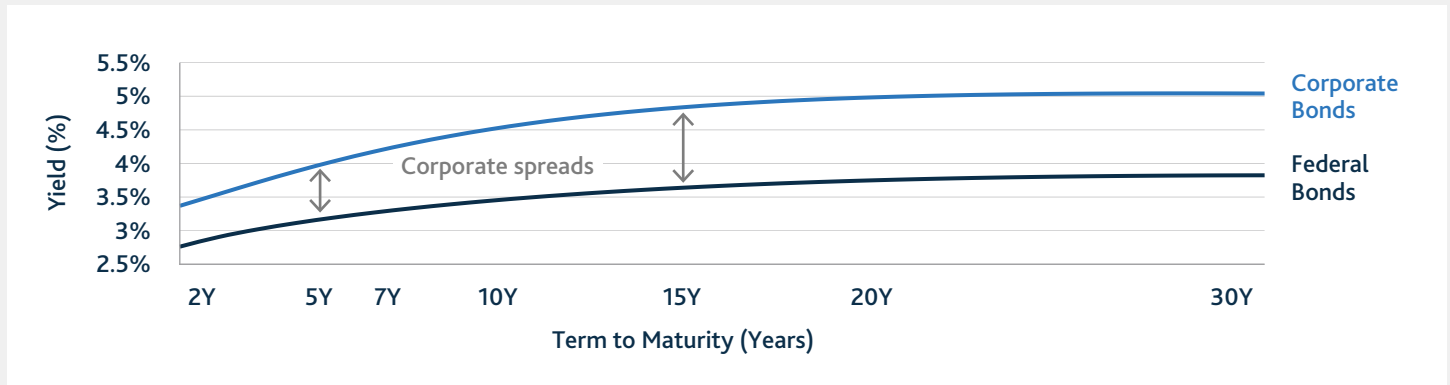
It is well known that corporate spreads generally increase with term-to-maturity ([Chart 1](#)).

A less appreciated feature of the credit market is that the compensation for credit spread risk declines with terms-to-maturity. In other words, shorter-dated corporate bonds tend to offer higher credit-spread returns per unit of credit-spread volatility risk¹ ([Chart 2](#)).

As a result, investors limiting their allocation to long duration bonds not only face fewer investment options and possibly more sector and issuer concentration, but they also deploy capital where compensation for spread-risk is generally less attractive.

Chart 1

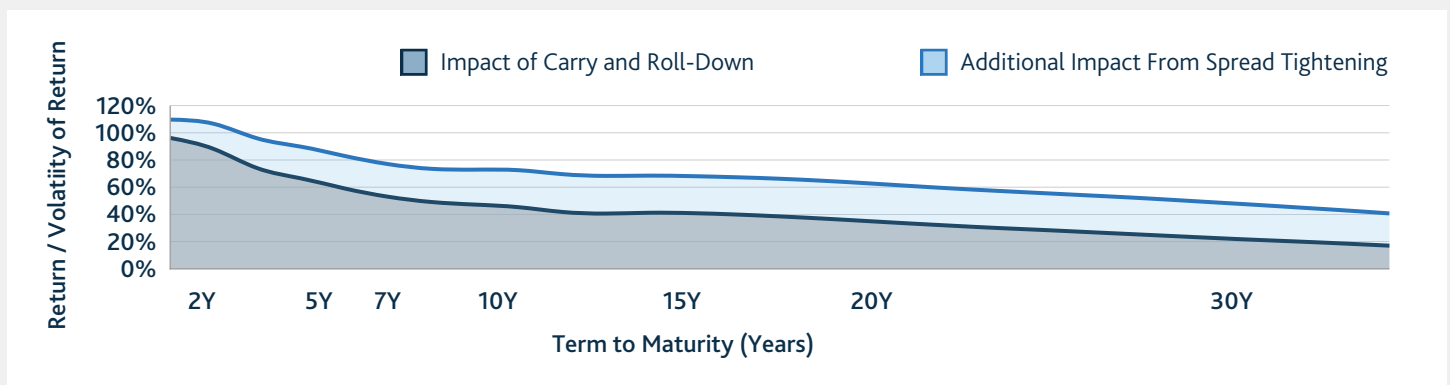
The term structure of corporate spreads (as of May 31, 2026)



Notes: Corporate curve based on a blend of 60% Corporate A and 40% Corporate BBB. Sources: Fiera Capital, FTSE.

Chart 2

Historical corporate spread returns per unit of spread return volatility (2016-2025)



Notes: Assuming 60% Corporate A and 40% Corporate BBB. Sources: Fiera Capital, FTSE.

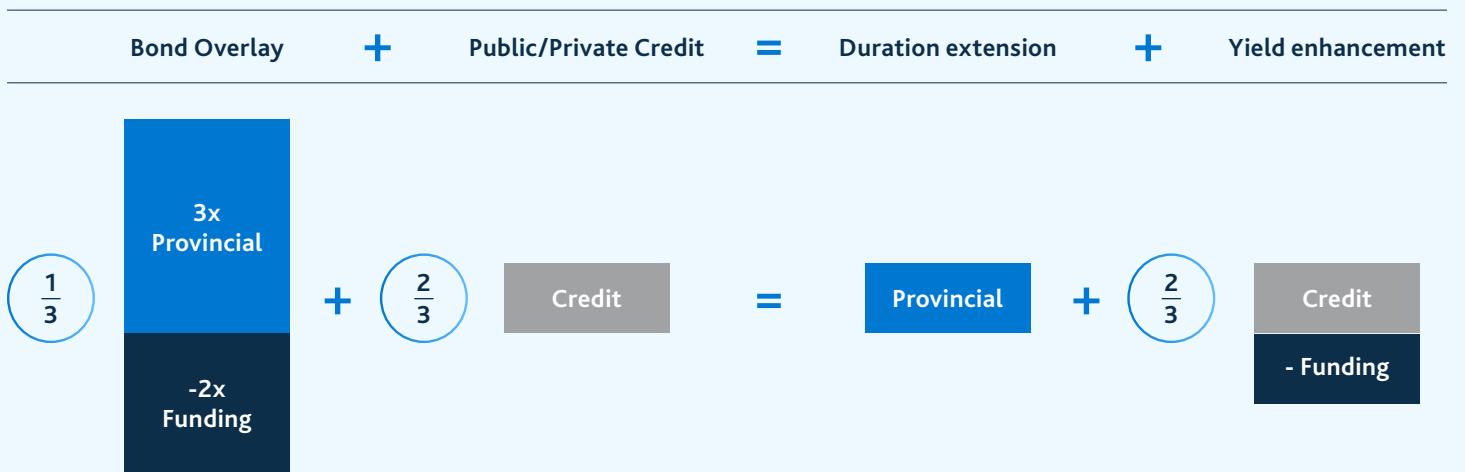
Decoupling the Duration and Credit Decision

Fortunately, investors do not need exposure to long-term corporate spreads to gain long-term interest-rate exposure. Bond overlay strategies, which have been used for many years by pension plans to manage interest-rate risk while freeing up capital for return-seeking assets, can also be used to separate the **duration** and **credit** decisions (Chart 3).

Chart 3

Using bond overlays to support yield enhancement

The use of bond overlays helps broaden the opportunity set considerably through decoupling the interest rate and credit decisions.



- ▶ Free up capital to enhance the yield through public/private credit, enabling diversification, greater return per unit of credit risk and scope for value added
- ▶ Take advantage of low funding costs using high quality and liquid collateral

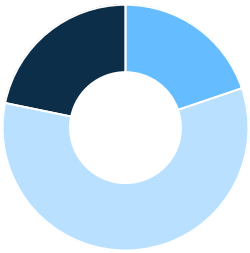
Simplified for illustrative purposes only.
Sources: Fiera Capital.

Illustration: Comparing Alternatives that Achieve Long Bond Duration

For illustrative purposes (Table 1,2 and Chart 4), we compare the historical risk and return profile of three alternative strategies designed to outperform passive long bonds while maintaining duration broadly in line with long bonds over time.

Table 1

Asset Mix – Year End 2025²



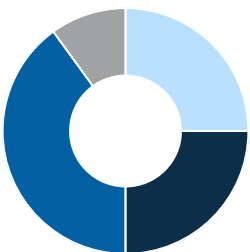
Passive Long Bonds

- Federal Bonds **20%**
- Provincial and Municipal Bonds **59%**
- Corporate Bonds **22%**



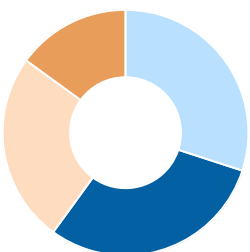
Long Bonds with Strategic Tilt

- Provincial Bonds / Strips **25%**
- Long Corporate Bonds **75%**



Overlay with Public Credit

- Provincial Bond Overlay **25%**
- Long Corporate Bonds **25%**
- Universe Corporate Bonds **40%**
- Global Bonds **10%**



Overlay with Public & Private Credit

- Provincial Bond Overlay **30%**
- Universe Corporate Bonds **30%**
- Commercial Mortgages **25%**
- Direct Lending **15%**

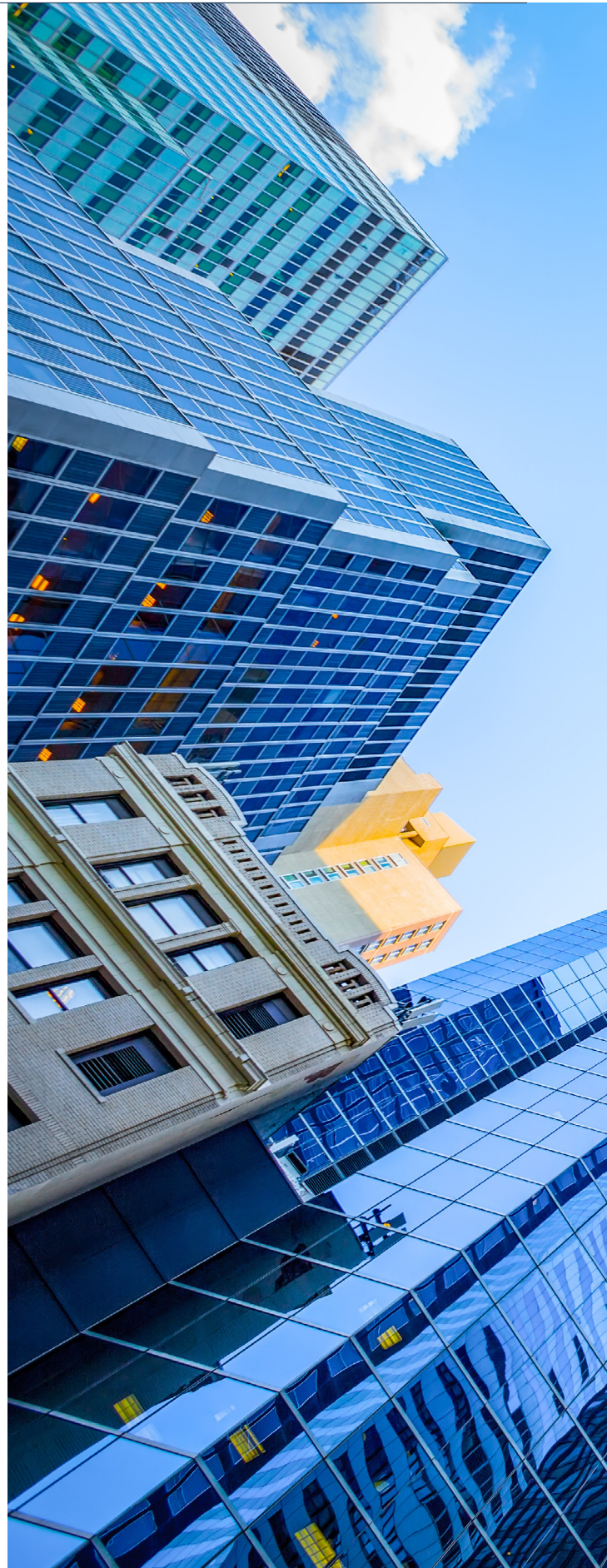


Table 2

Summary Results – Last 10 Years (2016-2025)²

Key Characteristics (as of Year-End 2025)

Asset Mix	Passive Long Bonds	Long Bonds w/ Strategic Tilt	Overlay w/ Public Credit	Overlay w/ Public & Private Credit
Yield	4.55%	4.91%	5.42%	6.46%
Duration	14.5	14.5	14.5	14.5
Corporate Spread Duration	12.3	12.3	7.9	4.2
Exposure Leverage	1.0	1.0	1.3	1.6
Investment Grade %	100%	100%	96%	84%

Key Performance Statistics

Asset Mix	Passive Long Bonds	Long Bonds w/ Strategic Tilt	Overlay w/ Public Credit	Overlay w/ Public & Private Credit
Return p.a.	1.23%	2.48%	2.40%	2.67%
Volatility	11.1%	11.6%	11.6%	11.3%
Maximum Drawdown	-30.5%	-28.1%	-29.2%	-27.2%
Correlation with Equities	0.43	0.54	0.54	0.50

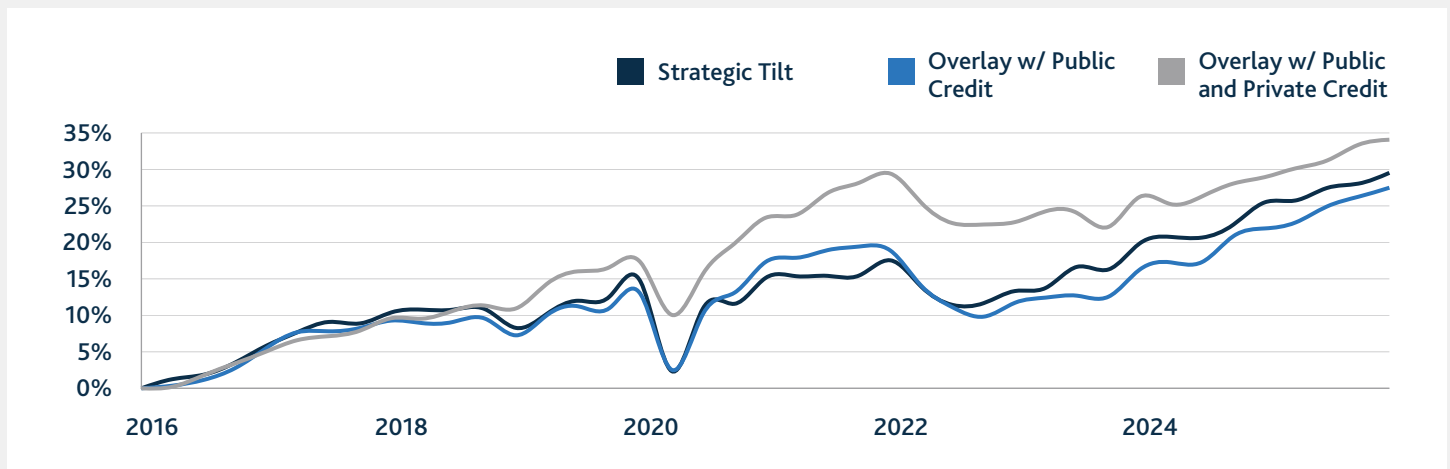
Risk-Adjusted Performance (vs. Passive Long Bonds)

Asset Mix	Passive Long Bonds	Long Bonds w/ Strategic Tilt	Overlay w/ Public Credit	Overlay w/ Public & Private Credit
Value Added p.a.	-	1.25%	1.17%	1.43%
Tracking Error	-	2.1%	2.1%	1.3%
Information Ratio	n/a	0.59	0.58	1.07

Notes on metrics: Yield is shown on an annualized basis using weighted IRR adjusted for FX hedging costs for direct lending. Duration is indicative of the sensitivity to rates and corresponds to modified duration and deemed 0 for floating rate assets. Corporate spread duration is the spread duration for the portion invested in corporate bonds (including Emerging market debt for global bonds) and is based on the average term to maturities for commercial mortgages and direct lending. Leverage is defined as exposure divided by capital invested. Return and value added based on annualized geometric returns and net of indicative management fees assuming \$200M portfolio. Volatility, correlation and tracking error based on quarterly net returns. Source: Fiera Capital

Chart 4

Cumulative gains versus passive long bonds on \$200M initial investment (2016-2025)²



Several key observations emerge from these results:

- > **A strategic tilt toward long corporate bonds represents the most direct improvement.** Overweighting corporate bonds and underweighting government bonds has added roughly 1.3% per year relative to passive long bonds. This reflects both the yield advantage of credit and credit-spread compression during that period. Given current market conditions, the historical magnitude of these gains is unlikely to be fully replicated over the next decade.
- > **Combining provincial bond overlay with shorter corporate bonds delivers a similar outcome through a more resilient structure.** By holding shorter, actively managed credit and synthesizing long duration through a government bond overlay, the strategy separates rate and credit decisions. This enables a higher and more efficient running yield without extending spread-duration, leaving the portfolio better positioned in the current environment, as reflected in its higher yield.
- > **Layering private credit onto the overlay structure produces the most attractive overall profile.** Improved risk-adjusted returns can be achieved by incorporating an allocation to private credit and moderately increasing the leverage. The result is lower drawdowns, lower tracking error and a meaningfully higher information ratio. The key trade-off, however, is a reduced liquidity profile.

In a positively sloped yield curve environment with tight credit spreads, investors seeking to achieve specific yield and duration targets face a challenging trade-off. Allowing for some leverage can help broaden the range of options available and tailor the portfolio to meet a wider set of objectives and considerations. This case is particularly compelling today, with public credit spreads near multi-decade tights, leaving little room for further compression and limited cushion against widening.

Selecting the Appropriate Strategy

The “right” approach for a given investor depends on several factors



Duration objectives and return requirements

Longer duration and return requirements make overlay-based strategies more compelling, given the more limited public and private credit opportunity set at the long end.



Diversification and liquidity requirements

Greater needs for liquidity and redemption flexibility favor strategies with higher liquidity and or stronger near-term cash flow generation (e.g. within private strategies, those with shorter loan repayment periods that can distribute coupons as income).



Risk tolerance and philosophy

The degree of comfort and preference with certain types of risks, along with the tolerance for volatility, will influence both the choice of strategy and the targeted sources of value added (e.g. tactical vs. strategic).



Governance needs and requirements

The strategies considered, the number of managers involved and the choice of investment vehicles will depend on the governance framework in place and capacity for manager oversight.



Why Discuss This with Fiera Capital?

Fiera Capital offers a broad range of fixed income capabilities across public and private markets, from core long duration government and corporate strategies to active long bond mandates, bond overlays and specialized private credit solutions. We are well positioned to deliver highly integrated solutions that allow institutional investors to tailor their fixed income portfolios to their governance, liquidity and risk objectives within an integrated, outcome-focused framework.

Endnotes

- 1 This feature is consistent with Duration Times Spread risk measure in the bond market and akin to the low volatility anomaly in equity markets. See *Systematic Investing in Credit* (2020) by Arik Ben Dor, Albert Desclee, and Lev Dynkin for more details.
- 2 Strategies assume monthly rebalancing and are net of indicative management fees assuming \$200M portfolio. Long bonds, long provincial bonds and long corporate bonds based on FTSE Long Bond Index, FTSE Long Provincial Bond Index and FTSE Long Corporate Bond Index, respectively. Universe corporate bonds based on Fiera Credit Fund. Global bonds based on Fiera Global Multi-Sector Income (GMSI) Fund. Commercial mortgages based on ACM Commercial Mortgage Fund. Direct lending based on Fiera Comox Private Credit Strategy since inception April 2020 and Cliffwater Direct Lending Index (CDLI) prior that, assuming currency hedging back to CAD. Provincial bond overlay based on levered exposure to FTSE Long Provincial Bond Index to achieve duration objective, with funding deemed to occur at 3M Overnight Index Swap (OIS) rates plus 20 basis points. Equities based on MSCI World (\$CAD). Sources: Fiera Capital, FTSE, Cliffwater, Bloomberg, MSCI.

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