ARKTOS
WEALTH MANAGEMENT

On The Mark

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Bonds Still Work. Just Not for Everything.

Key Takeaways

- **Expect some bumps**. Heavy borrowing and interest rate uncertainty may keep bond volatility elevated.
- **Starting yields matter.** Higher yields mean more income and a better starting point for future returns.
- **Diversify your diversifiers.** Bonds don't hedge every shock, particularly when inflation is the risk.

Every summer, we take a long road trip. And no matter the route, we inevitably hit a few rough patches along the way. The bumps get your attention, but they don't necessarily mean you're headed in the wrong direction.

Bond investors may recognize that feeling today. Long-term Treasury yields have moved sharply, and bond-market volatility has picked up.

So what should investors expect from bonds from here?

Why Did Bond Volatility Rise?

Part of the answer is simple: there are more bonds looking for buyers.

The federal government continues to borrow heavily, while companies are issuing more debt to fund the buildout of AI infrastructure. With more bonds competing for buyers, investors can demand higher yields to own them. Uncertainty around economic growth and Federal Reserve policy has added to the swings.

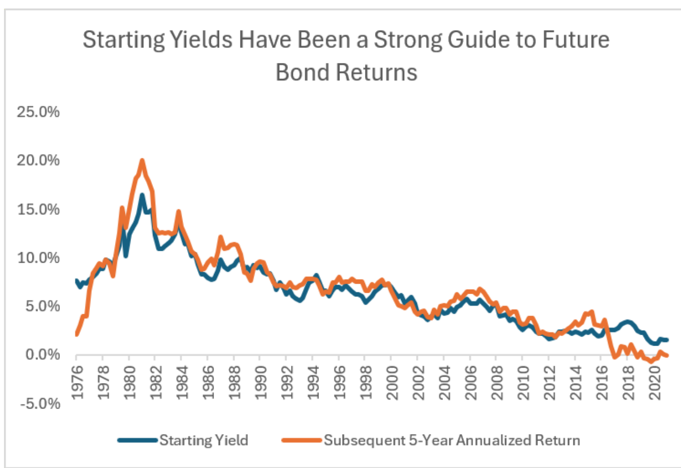
What's notable is that markets aren't signaling runaway inflation. We can see this by comparing regular Treasury bonds with inflation-protected Treasuries (TIPS). The difference gives us an estimate of what investors expect inflation to average over time—and those expectations have remained relatively stable.

But stable doesn't mean settled. Inflation remains above the Federal Reserve's target, and markets remain uncertain about how quickly—or smoothly—it returns to 2%. That uncertainty, combined with more debt for investors to absorb, has led to higher bond yields.

Look Beyond the Bumps

All of this can make for an uncomfortable ride in the short term. But for bond investors, short-term price swings are only part of the return story. Over longer periods, the income investors earn at the starting point has historically mattered a great deal.

History illustrates this remarkably well. Since 1976, the starting yield on the Bloomberg U.S. Aggregate Bond Index has had a 95% correlation with the Index's annualized return over the following five years.



Source: Bloomberg U.S. Aggregate Bond Index. Forward return uses the index level 20 quarters (5 years) after each starting date. Historical index duration and composition have changed over time.

At its simplest: Bond Return = Income + Price Change.

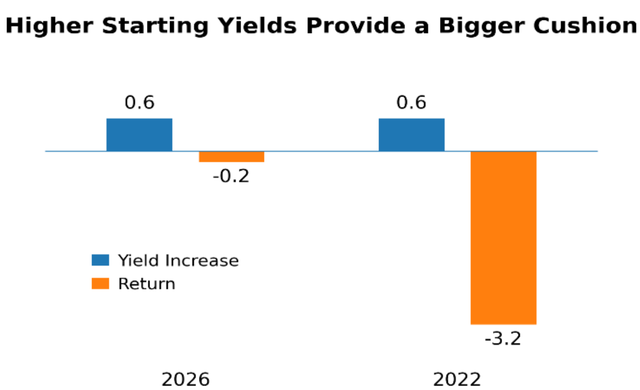
When interest rates rise, existing bond prices generally fall. But those higher rates also mean investors earn more income. And the longer the holding period, the more that starting income matters.

That doesn't mean today's yield guarantees what investors will earn over the next five years. Over shorter periods, changes in interest rates can still push bond returns meaningfully higher or lower. But it does give investors a useful way to set expectations.

A Different Starting Point

That perspective is particularly important after 2022. Investors entered that year with historically low bond yields. When inflation surged and the Federal Reserve rapidly raised rates, bond prices fell sharply, with very little income available to cushion the decline.

Bond yields have risen roughly 60 basis points since the start of 2026. The chart below shows why today's starting point matters: a similar rise in yields would have had a much larger impact on bond returns in 2022 than it does today.



Source: Bloomberg, AssetMark. Estimated returns based on a 60 basis point increase in Bloomberg Aggregate Index yield. Data as of 8/20/26.

Today, higher yields provide investors with more income to help offset price declines when rates rise. That doesn't eliminate volatility, but it does provide a much larger cushion than investors had entering 2022.

The lesson from 2022 isn't that bonds no longer work. It's that the starting point matters.

What Should Investors Do?

Our view is that economic growth remains resilient, but inflation is likely to remain uneven. That backdrop doesn't call for abandoning bonds—but it does argue for being thoughtful about where we take risk.

We continue to favor somewhat shorter-duration bonds relative to the Bloomberg U.S. Aggregate Bond Index. This allows investors to benefit from today's higher income while reducing sensitivity to swings in long-term interest rates.

But bonds shouldn't be asked to protect a portfolio from every possible risk.

Bonds have historically been valuable diversifiers when economic growth slows. Inflation can be different. As investors experienced in 2022, inflation can put pressure on stocks and bonds at the same time.

That's why we believe investors should diversify their diversifiers, complementing traditional bonds with investments such as real assets and gold that may respond differently when inflation is the shock.
Bonds still have an important role to play. But no single investment can protect against every risk. With higher starting yields and broader diversification, investors are better equipped for the road ahead.

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